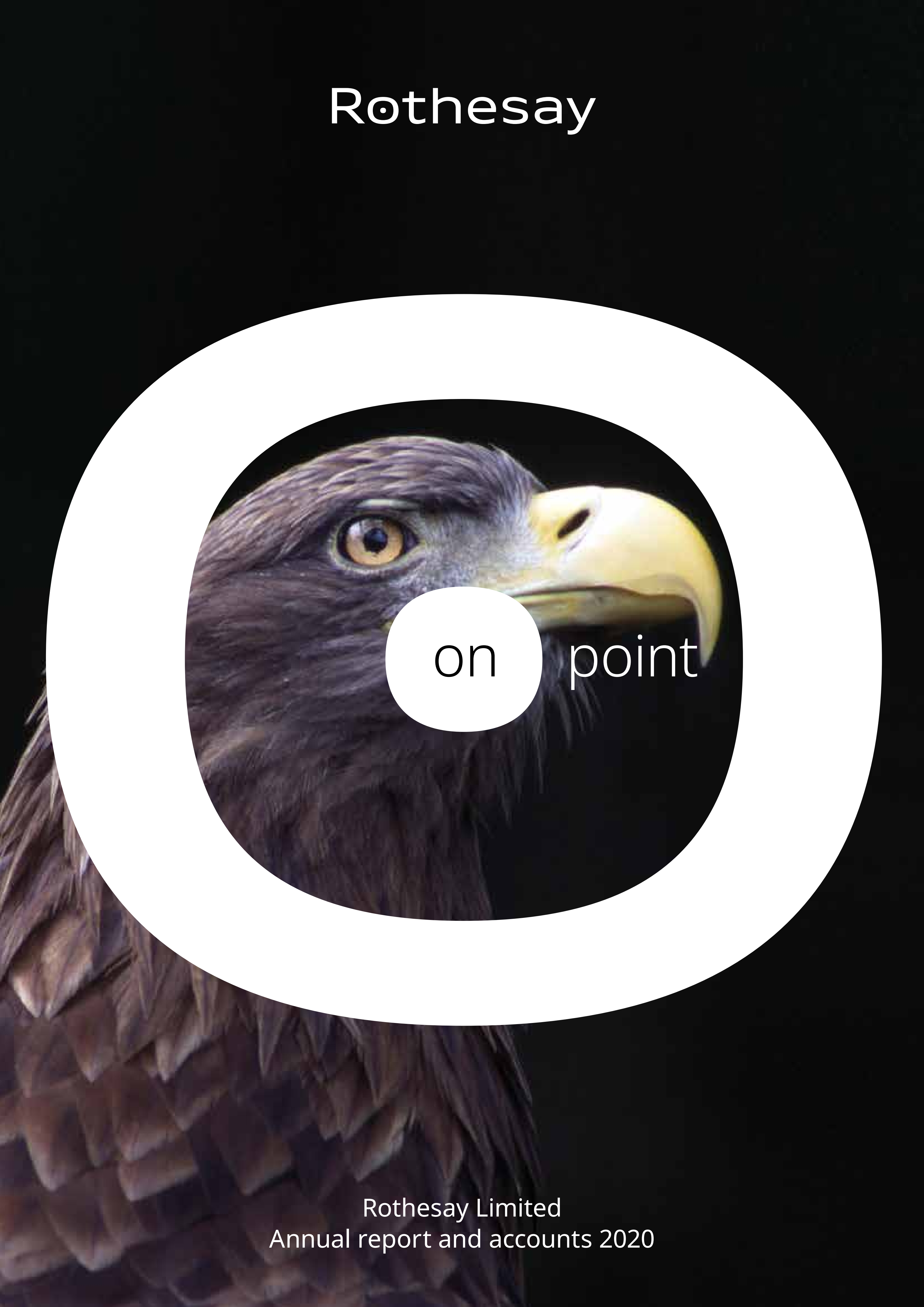


# Rothesay

on point

Rothesay Limited

Annual report and accounts 2020

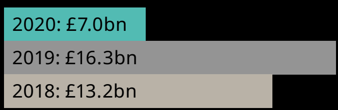
Our purpose

# We are dedicated to securing the future for every one of our policyholders.

Rothesay refers to Rothesay Limited (formerly Rothesay Holdco UK Limited) and its subsidiaries, together the Group.

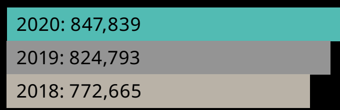
# Performance at a glance

## New business premium APM[1]




£7.0bn

## Number of policies




847,839

## Paid to policyholders in the year


£2.8bn

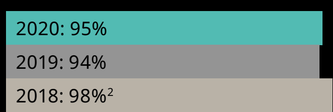
## Percent reinsured APM


87%

## Group SCR coverage APM


201%

## Customer satisfaction APM




95%

1 APM – Alternative Performance Measure, please see page 30 for further details.
2 Since 2019 Rothesay no longer issues satisfaction surveys in relation to bulk annuity exercises and hence the 2018 result is not comparable.

IFRS profit before tax

2020: £1,469m
2019: £640m
2018: £102m

# £1,469m

Market consistent embedded value APM

2020: £7.0bn
2019: £6.0bn
2018: £3.4bn

# £7.0bn

Assets under management APM

2020: £62.0bn
2019: £53.7bn
2018: £36.3bn

# £62.0bn

## Who we are

# Purpose-built to protect pension schemes and their members' pensions

Rothesay is the UK's largest pensions insurance specialist, purpose-built to protect pension schemes and their members' pensions. Our singular focus is to secure pension annuities for the future, providing certainty as well as genuine service excellence for every policyholder we look after.

Our conservative investment strategy and prudent underwriting mean we are trusted by some of the UK's best known companies to provide pension solutions, including Allied Domecq, Asda, British Airways, Cadbury's, the Civil Aviation Authority, National Grid, the Post Office, Prudential and telent.

Underpinned by sophisticated risk management, our expert team never stops developing new ways to drive predictable, dependable returns that minimise risk and create real security.

Today, we manage over £60 billion in assets, secure the pensions of over 800,000 people, and pay out, on average, over £200 million in pension payments each month. We are securing the future for every one of our clients and policyholders, and improving how pensions are delivered as we do it.

## What we deliver

**Real financial security**
We are obsessed about effectively managing risk – we measure every asset and liability every day, so we can react in the moment as the world changes.

+

**Genuine service excellence**
We are focused on every detail, to provide genuine service excellence for every one of our policyholders and trustees.

**1st**
insurance company to be PASA Accredited for customer experience[1]

**95%**
of policyholders surveyed rate our service 'good' or 'excellent'

**201%**
regulatory capital coverage

**AA**
average asset rating

**A+**
Fitch Ratings credit rating

**A3**
Moody's credit rating

1 In 2020 our Accreditation was renewed by the Pensions Administration Standards Association (PASA), an independent body dedicated to improving standards in pensions administration.

# Section 2

# Strategic report

Every decision that we make is informed by our conservative investment philosophy, cautious approach to risk management and sophisticated technology platform. We challenge ourselves every single day to think creatively so that our business model is best placed to meet our clients' needs.

# "Financial strength and stability in the face of challenging conditions."

**Naguib Kheraj**
Chairman

# Chairman's statement

**Our Chairman reflects on 2020**

## 2020 proved to be another year of substantial progress for Rothesay, despite the impact of the COVID-19 pandemic.

In common with many businesses, we had to cope with significant disruption and adapted quickly to operate with our staff and our key operational business partners working from home for most of the year. Thanks to the dedication of our people and the teams supporting our business at our third party administrators, we were able to maintain both uninterrupted service to policyholders and tight control over operational, credit and market risk during a period of exceptional volatility in markets. Our technology worked seamlessly and reliably throughout.

We focused on ensuring that the experience of our policyholders remained at industry-leading standards and on the wellbeing of our staff and those working at our service providers.

After a record level of new business in 2019, Rothesay continued to win a significant share of the pension risk transfer market in the UK, taking on a further £7bn of new liabilities. We were also active in investing almost £10bn of assets into our target allocation at attractive yields relative to the assumptions made at the time of original underwriting. Despite this level of activity on both sides of the balance sheet we ended the year with SCR coverage of 201% and very substantial capital above our normal target range.

As part of our continuing focus on environmental, social and governance issues, we committed to ambitious targets to achieve carbon neutrality and became a signatory to the UN Principles for Responsible Investing and a supporter of the Task Force on Climate-Related Financial Disclosures. We also allocated capital to start the Rothesay Foundation as a means to channel a portion of our earnings to support important and relevant charitable and community endeavours.

We welcomed the ruling in December from the Court of Appeal to overturn the original decision by the High Court in relation to the proposed Part VII transfer of business from the Prudential Assurance Company to Rothesay. The judgement means that we can now seek approval for the transfer of the business to Rothesay as envisaged originally.

In a transaction which implied an equity value for Rothesay of £5.75bn, our two existing institutional shareholders – GIC and MassMutual – acquired the 35% shareholding in the Company held by Blackstone, thereby increasing their respective shareholdings to 49% each. This represents a substantial positive vote of confidence in Rothesay and enables the business to benefit from a renewed long-term commitment from shareholders to continue supporting our growth strategy. We benefited greatly from Blackstone's engagement with the Company over the past seven years.

The change in shareholdings will have a knock-on impact on governance. Qasim Abbas, who ably represented Blackstone's interest on our Board stepped down on closing of the deal. We thank Qasim for his contributions over the years. GIC and MassMutual now have an entitlement to each nominate a second Director to the Board; in order to ensure that we maintain an independent majority on the Board, we have appointed two new independent Non Executive Directors – Jane Hanson and Ed Giera. Simon Morris has informed us of his decision to step down from our Board on 13 February 2021 and we expect to appoint Heather Jackson as a further new independent Non Executive Director shortly thereafter. The new Directors bring extensive and relevant experience as well as complementary skills to the Board and will improve our gender balance.

Whilst markets remain volatile and the path to reopen sectors of the economy is not yet clear, the progress on vaccines to protect the population against COVID-19 provides some basis for optimism for a return to more human interaction and mobility in 2021. We look forward to being able to conduct our business in person again in the near future.

**Naguib Kheraj,**
Chairman
11 February 2021

> This year, more than ever, we have seen the value of the purpose-built risk management infrastructure that we have developed to protect policyholders' pensions.

**Addy Loudiadis**
Chief Executive Officer

# Chief Executive's statement

## The rapid spread of COVID-19 has impacted all of our lives in ways we could not have imagined at the beginning of 2020.

The human cost of the pandemic has been both shocking and saddening and I would like to take this opportunity to extend my sympathies to all those who have been affected by the disease and the economic crisis it has created.

Rothesay responded quickly to ensure that any impact on our business and our stakeholders was minimised. Our immediate priorities were the health and welfare of our people and ensuring our policyholders continued to receive their pensions as normal. We transitioned to remote working in early March, even before the UK lockdown measures were implemented. This enabled us to fully test our remote IT systems and operational infrastructure to ensure we were able to provide a seamless continuation of all business functions and the same level of market-leading customer service to our policyholders. Credit and thanks are due to our employees and third party administrators for going above and beyond to ensure that Rothesay remained fully operational.

Our purpose-built risk management systems proved invaluable in supporting us to protect the balance sheet in the adverse and volatile market conditions experienced in the immediate aftermath of lockdown. Regular stress testing and live monitoring of the financial and solvency position of Rothesay has allowed us to respond dynamically as market conditions have evolved throughout the year, ensuring that we ended 2020 with a robust SCR coverage ratio of 201% (2019: 202%).

### Group performance

Although much of our focus in 2020 has been on protecting the balance sheet, we have successfully completed the investment of premiums received in 2019 according to our long-term investment strategy. During 2020, we have invested almost £10bn of assets and this has helped generate record IFRS pre-tax profit of £1,469m (2019: £640m) despite volatile market conditions.

Our investment portfolio has an average rating of AA and is focused on assets with high-quality collateral.

New business volumes during 2020 have held up well, with Rothesay's new business in 2020 being the third highest in our history even though many transactions were executed entirely remotely. This shows the strong sense of cooperation and collaboration between trustees, consultants, legal advisers and insurers working together in the interests of pension scheme members. With the help of our counterparties, we have continued to apply rigorous underwriting and due diligence despite remote working and have assisted 12 pension schemes to de-risk during 2020, generating £7.0bn of new business premiums (2019: £16.3bn). Assets under management increased to £62.0bn from £53.7bn at the end of 2019.

As a result of this new business, Rothesay's market consistent embedded value has increased by £1.0bn to £7.0bn (2019: £6.0bn). More details can be found on our financial performance in the financial review on page 33.

### Risk and capital management

The macroeconomic environment worldwide has been extremely challenging during 2020, with significant volatility in interest rates and credit markets. Low real interest rates will remain a challenge for all pension providers and the macroeconomic environment remains volatile given the long-term impact of the actions taken by governments in response to COVID-19 and continuing geopolitical tensions.

New business premium (APM):

**£7.0bn**

2019: £16.3bn

Rothesay SCR coverage (APM):

**201%**

2019: 202%

# Chief Executive's statement
**continued**

In the midst of this market volatility, having detailed real-time information is critical for the successful and efficient operation of any insurance business. Our market-leading risk management systems provide us with a strong advantage and allow us to be proactive and to navigate even the most difficult markets. Continued investment in the systems and people to manage the risks we assume on behalf of our policyholders is a key part of our strategy.

Our balance sheet remains strong with Own Funds of £7.3bn (2019: £6.1bn) and an SCR coverage ratio of 201% (2019: 202%), well above our target operating range and giving us significant surplus capital to write new business. This has been achieved without the need for new capital and is after allowing for the capital strain from writing £7.0bn of new business. Rothesay's liquidity has also remained robust throughout the market turmoil and we continue to hold large liquidity buffers.

We continue to hedge market and longevity risk exposures, using robust collateral provisions to mitigate counterparty risk. We entered into six new reinsurance agreements in 2020, leading to reinsurance of 87% of our longevity exposure (2019: 78%). As well as reinsuring the larger new business transactions written in 2020, we also reinsured longevity risk on some of our existing liabilities.

## Our policyholders

Providing over 800,000 policyholders with a safe and secure pension is at the heart of what we do. We pride ourselves on the quality of the service we provide. This year we were reaccredited by the Pensions Administration Standards Association (PASA), an independent body dedicated to improving standards in pensions administration. We are also members of the Institute of Customer Service, an independent, professional body for customer service.

This year, more than ever, we have been focused on ensuring that our policyholders received excellent service and I am pleased to say that thanks to the outstanding effort of our administration partners this has been achieved, with service levels being met consistently (including in response to telephone calls) despite the challenges of working remotely.

During 2020 we have also updated our brand, introducing a new look and feel for the Company which we believe is a better reflection of who we are.

As part of Rothesay's preparations for Brexit, we concluded that it was necessary to transfer approximately 400 Irish annuity policies to an EU-regulated insurance company. This transfer took place in September and was required to ensure that payments under the affected policies can continue to be lawfully paid following the end of the Brexit implementation period.

In December the Court of Appeal found in favour of Rothesay and Prudential regarding the proposed transfer of a portfolio of annuities business from Prudential, providing clarity for us and the sector as a whole about the operation of Part VII transfers. In 2021, we plan to seek approval for the transfer of the Prudential annuity business to Rothesay as envisaged in the original transaction and will focus on ensuring that any transition is as smooth as possible for policyholders.

## Our shareholders

In December, GIC and MassMutual acquired the shares held by Blackstone in a transaction that valued the Group at £5.75bn. This was a strong expression of confidence in the Company and provides the business with exceptional support from two of the world's leading institutional investors and a long-term platform for growth in the future.

I would like to take this opportunity to thank the Blackstone team for their invaluable partnership over the last seven years, which has been instrumental in helping us develop and grow the business into a market leader.

## Our people

Our people are a key strength of Rothesay. The team has delivered a great set of results despite the challenges of home-schooling, remote working and lockdown. Close coordination between all the areas of the firm and our relentless attention to detail ensured that all of the business written in 2020 was meticulously executed and I am proud of the way in which our people responded to the COVID-19 pandemic. It is a testament to the team that even though almost all of our employees have been working from home since March, the business has continued to operate normally.

We received an outstanding response to our 2020 employee engagement survey, with 95% of employees participating (2019: 81%) and with 92% of employees saying that they were proud to work at Rothesay (2019: 87%).

During 2020 we have continued to recruit, particularly to strengthen our control functions and to support development of our IT platform. We have honoured all of our pre-COVID-19 job offer commitments and onboarded many new employees remotely. At the end of 2020, Rothesay had 305 employees, including seven in Rothesay Asset Management US, an increase of 21% from 2019.

This year we have seen increased public debate on the subjects of race and inclusivity. Racism and other forms of discrimination have no place at Rothesay. Rothesay is committed to promoting equality and diversity, and a culture that actively values difference. We have a clear equal opportunity policy and we recognise that people from different backgrounds and experiences can bring valuable insights to the workplace and enhance the way we work. We will continue to engage with our people, and the businesses we partner with, to promote working environments where everyone feels valued.

## Corporate Social Responsibility

Our Corporate Social Responsibility policy describes the way in which we aim to engage positively with all of our stakeholders. The policy also describes the way in which we take financially material environmental, social and governance factors, including climate change, into account in our investment process.

Rothesay is determined to play its part in combating climate change and global warming. We are in the process of aligning our investment portfolio with the goal of the Paris Accord to limit global warming to 1.5ºC above preindustrial levels and are committed to supporting a low carbon economy in which the UK achieves carbon neutrality by 2050. We are also a signatory to the UN Principles for Responsible Investing, a supporter of the Task Force on Climate-Related Financial Disclosures and an early adopter of the Sustainability Reporting Standard for Social Housing. See page 59 for further information.

In 2019 we established the Rothesay Foundation with the aim of supporting charities that seek to improve the quality of life for older people, helping them to live their lives in a happy, safe and fulfilling way. The Foundation has now started to support these charities, many of whom had financial difficulties due to the COVID-19 crisis.

During 2020, we have contributed over £4.1m to charitable causes. This includes making a significant contribution to the COVID-19 Support Fund, the UK insurance industry's initiative to help some of the people hardest hit by the COVID-19 crisis. We also encouraged our employees to donate towards charitable causes through various matching incentive programmes which were widely utilised.

## Looking forward

Our market opportunity remains strong and attractive. Total market volumes for 2020 have exceeded £30bn, despite the impact of COVID-19, making 2020 the second highest volume year for pension risk transfers in history. This follows on from the £40bn of transactions that were executed during 2019, providing clear evidence of the depth and resilience of the sector. Market forecasts estimate annual market volumes under normal conditions of £40bn+ p.a. and 2021 is shaping up to be another busy year. Our strong capital position and supportive shareholders ensure we are well positioned to pursue strategic opportunities as well as pension risk transfer business. As always, we will remain disciplined and selective when underwriting new business.

Rothesay is designed to protect pensions even through the most difficult times. It is a matter of great pride to us, and comfort to our stakeholders, that every pension we provide is as secure now as it was before the start of the COVID-19 pandemic. As we emerge from the challenges of COVID-19, I am confident in Rothesay's financial and operational resilience and I look forward to 2021 with optimism and excitement about what the future holds for Rothesay, our customers and our other stakeholders.

Finally, I would like to take this opportunity to give huge thanks to our people and our administration partners for their truly outstanding efforts through the year.

**Addy Loudiadis**
Chief Executive Officer
11 February 2021

# Our markets

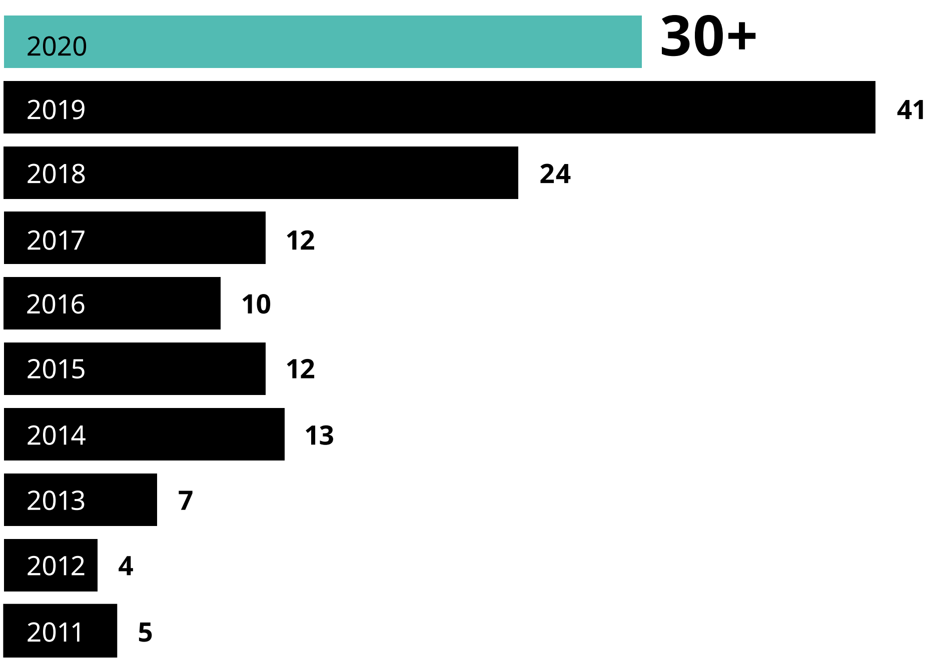
# 1. Pension risk transfer

### Rothesay's core market is growing strongly

Rothesay's core market is in pension risk transfer. Market volume has grown considerably in the last few years, but total market penetration is still only 8% of the £2.1 trillion UK market.

Almost 90% of UK defined benefit pension schemes are now closed and such benefits are no longer offered to new employees. This means companies and trustees want to de-risk their pension scheme liabilities. This is where we step in, either with a buy-in or full buy-out.

### Growing pension risk transfer market (£bn)




Showing UK pension risk transfers completed per year. 2020 and 2019 data sourced from Aon.
Prior year data sourced from LCP and Hymans Robertson market reports.

**Securing UK pension schemes**

For many of our clients, pension scheme protection is a two-step process, starting with bespoke insurance, leading to a complete transfer of members into our care.

## Buy-in

Bespoke insurance to bring immediate financial security to your pension scheme.

In a buy-in, the scheme purchases a bulk annuity insurance policy which is held as an asset of the scheme.

This makes Rothesay responsible for all the risks relating to the insured benefits e.g. longevity risk, market risk, interest rate and inflation.

The scheme is still responsible for paying pensions to its members – Rothesay has no direct relationship with the scheme members.

## Buy-out

Full transition of your scheme and members into Rothesay's care, for total protection.

In a buy-out, Rothesay takes full responsibility for the pension scheme and the employer's obligations to its members.

The pension scheme is wound up and the assets move over to Rothesay. The scheme members become Rothesay policyholders and receive new individual policies.

# Our markets
**continued**

# 2. Wholesale annuity

Our second source of business in acquiring back-books of annuities from insurance companies, either through acquisition of companies or blocks of business.

The opportunity to acquire back-books looks positive; many companies are wishing to leave the individual annuity market and we are able to help with our extensive experience in the sector.

### Acquisition of companies
Traditional company acquisition, where we take on all of the company's assets, liabilities and obligations, including the economic exposure and administration of their annuities.

### Acquisition of blocks of business
1. Reinsurance transaction between Rothesay and the insurer selling the block. During this step, the insurer is responsible for administration but Rothesay has full economic exposure.
2. Approximately 18 months later, the goal is a Court-sanctioned transfer of the business to Rothesay. Now, we take over the administration as well as the economic exposure.

## Wholesale annuity transaction timeline

| | 2011 | 2014 |
|---|---|---|
| **Transaction** | Acquisition of Paternoster | Acquisition of MetLife Assurance Limited |
| **Size of transaction** | £3bn | £3bn |
| **Number of policies (000s)** | 42 | 24 |
| **Type of business** | Bulk annuities | Bulk annuities |

| 2015 | 2016 | 2018 |
|---|---|---|
| Purchase of annuity portfolio from Zurich UK Life (reinsurance followed by Court-approved transfer), with three follow-on transactions | Purchase of annuity portfolio from Aegon UK (reinsurance followed by Court-approved transfer) | Purchase of annuity portfolio from Prudential (reinsurance followed by proposed transfer) |
| **£1bn** | **£6bn** | **£12bn** |
| **28** | **187** | **400** |
| Individual and bulk annuities | Individual and bulk annuities | Individual and bulk annuities |

# Our business model: Security for the long term

## Underwrite the liabilities

**We achieve maximum pre-deal certainty about the profile of the liabilities we are taking on through our meticulous underwriting and due diligence.**

We model the benefits of every single policyholder and project them to maturity. This means we can accurately estimate the cost of providing the insured benefits and holding the risk capital.

We scrutinise all new business to ensure we minimise risk and will be able to achieve our return threshold.

## Hedge the risks

**We assess the risk impact of transactions before completion so we can lock in the economics. This gives certainty to clients and protects our balance sheet. You can see our full risk breakdown on page 37.**

We reinsure the majority of our exposure to longevity risk. This process also gives independent third party price verification.

Collateral management is an integral part of the Group's activities. We closely monitor collateral so that our security is not compromised by market shifts.

# Invest the assets

**We seek assets which match our liability cash flows and provide an appropriate risk-adjusted return.**

Our portfolio is rated on average as AA and is made up of three diverse categories:

1. Cash and government bonds.
2. Infrastructure and other corporate bonds.
3. Secure, illiquid assets.

# Deliver the pension benefits

**We have strategic partnerships with well established pension administrators – Willis Towers Watson, Mercer and Capita Employee solutions.**

Working with these partners gives us scale and contingency capabilities. High levels of automation and sophisticated technology enable our partners to interact with our risk management systems to eliminate discrepancies and optimise policyholder service.

# Our investments

## Good progress has been made with investing the assets received as premiums in 2019 despite the COVID-19 pandemic.

We have remained disciplined and cautious about making investments during 2020 and have been very selective in the investment decisions made. A systematic review of our investment portfolio led to the identification of sectors most likely to be adversely impacted by COVID-19 and of assets most at risk of downgrading to sub-investment grade. Where possible, we have proactively switched assets accordingly.

Our in-house team is responsible for the management of Rothesay's £62bn asset portfolio. Assets are sought which match our liability cash flows and which provide an appropriate risk-adjusted return. Rothesay operates a cautious investment strategy which seeks to diversify exposure and actively manages risk. We are constantly looking for new ways to reduce risk and achieve the dependable returns that create real security for people's pensions in the future.

At the end of 2019, Rothesay had substantial cash and gilts to deploy into longer-term assets due to the record amount of new business written in that year. Much of 2020 has been focused on investing those assets according to Rothesay's long-term investment strategy. We have succeeded in investing almost £10bn of assets more quickly than envisaged when the business was originally underwritten and at better risk-adjusted returns.

The in-house team considers financially material environmental, social and governance (ESG) factors as part of the investment process and these factors are formally documented in all committee approval papers for new investments in order to ensure that appropriate account is taken of them. We are aligning our investment portfolio with the goal of the Paris Accord to limit global warming to 1.5°C above pre-industrial levels and are committed to supporting a low carbon economy in which the UK achieves carbon neutrality by 2050. For more information on responsible investment see page 59.

The average rating of Rothesay's investment portfolio is AA and the portfolio can be divided into three broad categories:

- **Cash and government bonds** – This part of the portfolio is available for future investment and to meet collateral calls and cash requirements and also backs some of our very long-dated cash flows.
- **Corporate bonds and infrastructure** – Given the scale of Rothesay's balance sheet, we also invest in a diversified portfolio of corporate bonds, including regulated infrastructure such as water, energy and transportation.
- **Secure, illiquid assets** – These assets include loans secured against property, equity release mortgages (ERMs) and loans secured against other collateral. They are attractive because investors are rewarded for illiquidity rather than credit risk. Structural features such as collateral, covenants and other security features mean that recoveries in the event of default are maximised and credit risk minimised.

The charts on the next page provide a breakdown of our investment portfolio at 31 December 2020 by sector and geography.

### Corporate bonds and infrastructure
Given recent market conditions, there have been fewer opportunities to invest in more illiquid assets in 2020, so many of the new investments have been in more liquid, highly rated corporate bonds, including US universities and healthcare providers, as well as in loans issued by conservatively managed and leveraged real estate investment trusts (REITs), particularly those focused on industrials. These include a number of private placements. Over time, we may look to switch out of the more liquid positions into other assets.

The table below provides a summary by sector of our corporate bond and infrastructure holding:

| Sector | Percentage |
|---|---|
| Infrastructure | 27 |
| Real estate | 14 |
| Banking & insurance | 14 |
| Education | 9 |
| Consumer goods & services | 7 |
| Communications & media | 7 |
| Technology & electronics | 5 |
| Healthcare | 5 |
| Industrial & energy | 5 |
| Automotive & transportation | 3 |
| Retail | 2 |
| Other | 2 |

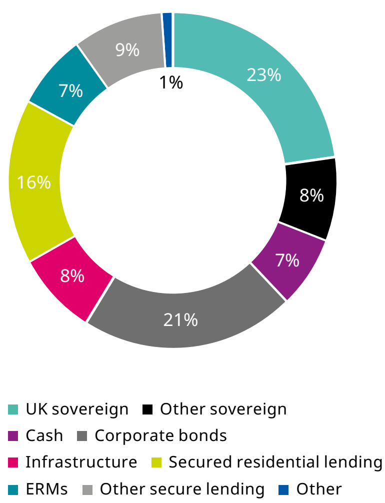
Of our £19bn holding of corporate bonds and infrastructure, around 30% (or 9% of total assets) is rated BBB and of those only £0.2bn is rated BBB-. Rothesay holds no sub-investment grade bonds.

A breakdown of the investment portfolio by rating can be found in note F.2.1.

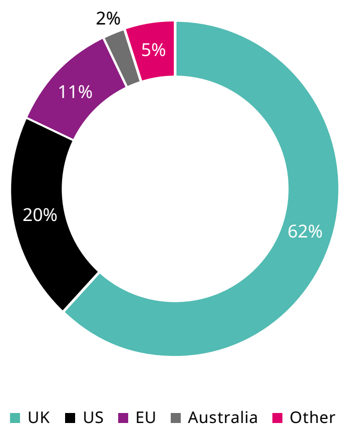
### Mortgages
We took the decision to slow down origination of ERMs and Dutch mortgages given the practical difficulties associated with property underwriting in the second quarter of 2020 and gradually re-started origination as COVID-19 restrictions were lifted and as market practise has evolved.

By the end of 2020, our total ERM portfolio had increased to £4.2bn (2019: £2.7bn) or 7% of assets under management (2019: 5%).

### Our investments




### International diversification



# Why we are successful

**Rothesay is a purpose-built specialist business, with a unique culture and set of capabilities that continue to drive our growth and leadership.**

## Purpose-built

We were founded with a single purpose: to secure UK pensions at scale, exceptionally well and within a robust regulatory environment.

We are designed from the ground up with modern systems, structures and capabilities to protect and deliver pensions more securely and effectively.

## Financial strength

We have an extremely strong capital position with an absolute focus on maintaining solvency. Our safety-first approach to writing business means we rigorously analyse every risk and would rather invest in no business than risky business.

## Unique integration

Our governance is robust yet agile, and our team think diversely but operate as one, blending actuarial rigour with investment expertise.

Every decision is a product of our multi-disciplinary management team who are experts across investments, underwriting and risk management.

## Sophisticated technology

Our industry-leading, purpose-built technology platform underpins the whole business, so that we are always informed and can adapt in real time to market changes.

Our engineers drive its evolution so that our platform grows with the industry.

## Original thinking

We continuously bring creative and innovative ways of delivering for our clients, and develop bespoke solutions for every pension scheme.

Our original thinking has led to several pioneering firsts, including our rapid response times and our dynamic technology-focused approach.

## Service excellence

We support clients through every step of the process and don’t leave a stone unturned from pitch to buy-in to buy-out. And once policies are issued, we provide excellent customer service. Our straightforward and straight-talking approach helps us build clarity and trust in every interaction.

# Our strategy and KPIs: Measuring success

# Financial security

| | 2019 | 2020 |
|---|---|---|
| **RLP SCR coverage** Indicates capital strength through comparing how RLP is capitalised relative to the regulatory requirement (APM) | 201% | **203%** |
| **Assets under management** Measures business size to indicate resilience (APM) | £53.7bn | **£62.0bn** |
| **External ratings** Impartial indicators of our financial strength | **A3** Moody's Investors Service | **A+** Fitch Ratings |

**2020 progress:**

- Maintained a robust solvency position against a volatile economic backdrop.
- Raised £100m Tier 3 debt in order to repay £100m of hybrid capital.
- Reinsured £7.4bn of liabilities giving effective reinsurance coverage of 87%, including reinsurance with two new counterparties.
- Made good progress in the development of the full internal model (FIM).
- MassMutual and GIC acquired Blackstone's stake in the business, ensuring Rothesay has two long-term, sophisticated strategic investors.

**Opportunities in 2021 and beyond:**

- Continue to maintain a robust solvency position.
- Expand our risk function to better identify and manage emerging risks including climate change.
- Invest in capital models, extending the partial internal model (PIM) to a FIM covering all risks.
- Continue to optimise our capital structure through appropriate levels of equity and debt.

# Steady growth

| | 2019 | 2020 |
|---|---|---|
| **New business premiums** Signals the Group's growth (APM) | £16.3bn | **£7.0bn** |
| **MCEV new business profit** Indicates the value generated by new business (APM) | £1,612m | **£576m** |

**2020 progress:**

- De-risked the liabilities of 12 pension schemes, which generated £7.0bn of new business.
- Grew the Rothesay team by 53 talented individuals across the whole Group.

**Opportunities in 2021 and beyond:**

- Continue to seek appropriate new business opportunities, with a view to growing our market share.
- Focus on recruitment in asset origination to continue diversifying our investment portfolio.
- Continue to strengthen our in-house IT capabilities to continue developing our IT platform.
- Strengthen Rothesay's profile as an investor overseas, particularly in the US, to allow us to continue to diversify investments.

# Our strategy and KPIs: Measuring success continued

# Service excellence

| KPI | 2019 | 2020 |
|---|---|---|
| **Service quality** Measures the number of policyholders who rate our service ‘good’ or ‘excellent’ (APM) | 94% | **95%** |
| **Complaints** Measures satisfaction through number of complaints upheld per 1,000 customers (APM) | 0.36 | **0.42** |

**2020 progress:**

- Performance throughout the year above our stringent benchmarks across all TPAs.
- Maintained low complaint rates and high satisfaction despite the challenges of COVID-19.
- By leveraging our TPAs’ existing functionality we are now able to offer an online service to our policyholders.

**Opportunities in 2021 and beyond:**

- Continue to excel in customer service.
- Prepare for a potential transfer of the Prudential portfolio should our application for approval be successful.

# Reliable performance

| | 2019 | 2020 |
|---|---|---|
| **IFRS profit before tax** Measures profitability, by capturing all recurring and non-recurring items | £640m | **£1,469m** |
| **MCEV** Indicates the risk-adjusted value of the business (APM) | £6.0bn | **£7.0bn** |
| **Employee engagement** Measures the number of employees who say they are proud to work at Rothesay | 87% | **92%** |

**2020 progress:**

- Invested all assets received from 2019 new business more quickly and at better yields than planned, contributing to an increased IFRS profit.
- Maintained high levels of employee engagement despite COVID-19.
- Committed to ambitious environmental targets to ensure a sustainable business model.

**Opportunities in 2021 and beyond:**

- Increase our market penetration – the total market volume has grown considerably in the last few years, but penetration is still only 8% of the £2.1 trillion UK market.
- Maintain employee engagement despite ongoing restrictions from COVID-19.
- Make progress towards our ambitious environmental targets.

> "Record IFRS profits driven by investment of the assets received as premiums in 2019."

**Andrew Stoker**
Chief Financial Officer

# Financial review

## The financial review describes the financial performance of Rothesay Limited and its subsidiaries.

### IFRS financial performance

Rothesay made a profit before tax of £1,469m (2019: £640m). The increase in profits was largely as a result of investing the assets received from the £16.3bn of new business executed throughout 2019 and as such is unlikely to be repeated in 2021.

The financial performance analysis shown in the table on the next page provides an explanation of the way in which profits have been generated. Further explanation of the line items can be found in the notes on Alternative Performance Measures on page 156.

New business profits (APM) in the analysis are calculated assuming full investment of premiums and the short-term impact of any under-investment is reported separately in the table. New business profit (APM) for the year was £449m (2019: £958m) (APM). The analysis has been prepared assuming that once fully invested, the risk-adjusted yield on the assets held increases by 7bps compared to the 1.32% yield being achieved at 31 December 2020 (2019: an increase of 12bps).

As most of the new business written in 2020 was written in the second half of the year, there is a temporary reduction in profits from of the delay in investing assets received as new business premiums of £547m (2019: a reduction of £909m) (APM). We anticipate that this will reverse as assets are invested according to our long-term strategy. Profits for the year include profits of £909m generated on investment of the assets received as premiums last year (2019: £273m) (APM).

Profits generated on the in-force book were £476m (2019: £299m) (APM). These profits mainly arose from increased longevity reinsurance and the release of prudent margins as the business runs off and as members exercise their options.

The impact of the change to non-economic assumptions, a gain of £284m (2019: a gain of £46m) (APM) was largely as a result of the £296m impact of a change in estimating approach to marking assets and liabilities which increase with limited price indexation (LPI). In previous years, we have projected LPI using future assumed rates derived from the LPI swap market. However, over time this market has become highly illiquid and all but a very small number of banks have withdrawn from the market, leading to rates which are out of line with the LPI rates actually realised. For 2020, in valuing our liabilities, we have therefore projected rates using LPI models based on realised LPI and other market inputs. The impact of the change to non-economic assumptions also includes an increase in expense provisions for 2020 that was largely offset by demographic assumption changes (see note E.2).

Rothesay made economic profits of £212m (2019: £244m) (APM). Economic profits (APM) represent the change in value of assets from changes in economic conditions less the change in value of liabilities from those changes. Economic profits in 2020 include gains from credit spread tightening and other market movements.

IFRS profit before tax:

£1,469m

2019: £640m | **+130%**

MCEV (APM):

£7.0bn

2019: £6.0bn | **+17%**

# Financial review
**continued**

| Financial performance (Alternative analysis of profit generation) (APM) | 2020 £m | 2019 £m |
|---|---|---|
| New business profit (assuming assets fully invested) | **449** | 958 |
| Impact of temporary investment delay | **(547)** | (909) |
| Investment profit from prior year | **909** | 273 |
| Performance of in-force book | **476** | 299 |
| Non-economic assumption changes and model refinement | **284** | 46 |
| Acquisition and Group costs | **(119)** | (112) |
| Administration expenses | **(53)** | (48) |
| **Operating profit before tax** | **1,399** | 507 |
| Borrowing costs | **(108)** | (87) |
| Project and other one-off expenses | **(34)** | (24) |
| Economic profits | **212** | 244 |
| **IFRS profit before tax** | **1,469** | 640 |

## COVID-19
The continued economic disruption as a result of COVID-19 has impacted the fair value of our financial investments. Where possible, we have continued to use observable market prices but where assets have been valued using techniques where inputs are unobservable, we have considered whether adjustments need to be made. For example, in valuing loans secured on commercial real estate, we have adjusted underlying property values on a property-by-property basis and, in calculating the impact of the no negative equity guarantee of ERMs on the valuation rate of interest, house prices are assumed to have fallen by 5% with no offsetting change in assumed future house price growth.

It is unclear as to whether COVID-19 will materially impact future mortality. In valuing our insurance and reinsurance assets and liabilities, we have allowed for reported deaths but we have not made any changes to our mortality assumptions to allow for the impact of COVID-19 as we believe it is still too early to know what this might be and scenario analysis suggests a wide range of possible outcomes.

## Alternative Performance Measures
Rothesay's strategy is focused on protecting the security of policyholder benefits, growth through writing value driven new business and, ultimately, delivering sustainable shareholder value.

In the opinion of the Directors, the prescribed IFRS results and disclosures do not capture long-term value creation or changes to capital requirements and therefore do not fully reflect the performance of Rothesay.

Rothesay therefore uses a number of Alternative Performance Measures (APMs) which focus on value generation and capital strength. Further information on Rothesay's APMs can be found on page 156 including definitions, why the measure is used and, if applicable, how the APM can be reconciled to the nearest GAAP measure. Rothesay uses the symbol APM to highlight APMs throughout the financial statements.

## IFRS income statement highlights

The key line items in the consolidated statement of comprehensive income for Rothesay are summarised in the table below:

| Income statement highlights | **2020 £m** | 2019 £m | Commentary |
|---|---|---|---|
| Gross premiums written | **7,281** | 16,606 | Gross written premiums are made up of new business of £7.0bn (2019: £16.3bn) and regular premiums of £0.3bn (2019: £0.3bn) generated on the inwards longevity reinsurance business written in prior years. |
| Net premiums written | **5,869** | 15,361 | Net premiums written represent the gross premiums written less the £1,412m (2019: £1,245m) of regular premiums ceded to reinsurers. |
| Investment return | **4,648** | 2,295 | Large positive investment returns arose from the growth in the value of assets due to falling interest rates and rising bond prices in the second half of the year. |
| **Total revenue** | **10,517** | 17,656 | |
| Net claims paid | **(1,491)** | (1,396) | Claims paid represent the total payments due to policyholders during the year of £2.8bn (2019: £2.4bn) less the reinsurers' share of such claims £1.3bn (2019: £1.0bn). |
| Change in net insurance liabilities | **(7,232)** | (15,327) | The change in insurance liabilities in 2020 was largely as a result of new business and changes in market conditions (predominantly the reduction in interest rates) partly offset by the run off of liabilities. |
| Operating expenses | **(206)** | (184) | Operating expenses consist of £53m (2019: £48m) of administration expenses, £119m (2019: £112m) of acquisition expenses and £34m (2019: £24m) of non-recurring and project expenditure. |
| Finance costs | **(119)** | (109) | Finance costs mainly represent interest payable on borrowings and have increased as the Group's borrowings have increased. |
| **Total claims and expenses** | **(9,048)** | (17,016) | |
| **Profit before tax** | **1,469** | 640 | |
| **Income tax** | **(276)** | (124) | The Group's effective tax rate is 18.8% (2019: 19.3%). |
| **Profit after tax** | **1,193** | 516 | |

# Financial review
**continued**

## IFRS balance sheet highlights
The key line items in the consolidated statement of financial position for Rothesay are summarised in the table below:

| Balance sheet highlights | **2020 £m** | 2019 £m |
|---|---|---|
| Financial investments | **93,712** | 73,742 |
| Reinsurance assets | **616** | 388 |
| Other assets | **1,932** | 1,971 |
| **Total assets** | **96,260** | 76,101 |
| Share capital and share premium | **1,471** | 1,518 |
| Tier 1 notes | **347** | 347 |
| Capital contribution reserve | **(46)** | 17 |
| Other reserves | **3,103** | 1,894 |
| **Total equity** | **4,875** | 3,776 |
| Insurance contract liabilities | **55,247** | 47,932 |
| Reinsurance liabilities | **993** | 848 |
| Payables and financial liabilities | **33,607** | 21,999 |
| Borrowings | **1,426** | 1,427 |
| Other | **112** | 119 |
| **Total liabilities** | **91,385** | 72,325 |
| **Total equity and liabilities** | **96,260** | 76,101 |

## Assets under management
Total assets increased from £76.1bn as at 31 December 2019 to £96.3bn as at 31 December 2020 primarily as a result of new business and the change in market conditions. Assets under management (APM) increased from £53.7bn as at 31 December 2019 to £62.0bn as at 31 December 2020. Assets under management can be derived by adjusting total assets for reinsurance, payables, derivatives and collateralised financing as shown in the table below.

Payables and financial liabilities increased from £22.0bn at 31 December 2019 to £33.6bn at 31 December 2020 largely as a result of the changes in economic conditions. Payables are dominated by derivative financial instruments and collateralised financing agreements. Derivatives are used to manage market and credit risk. The derivative liability as at 31 December 2020 of £30.4bn (2019: £19.7bn) is largely offset by derivative assets of £30.7bn (2019: £19.5bn).

| Assets under management (APM) | **2020 £m** | 2019 £m |
|---|---|---|
| Total assets | **96,260** | 76,101 |
| Less reinsurance assets | **(616)** | (388) |
| Less payables and financial liabilities | **(33,607)** | (21,999) |
| **Assets under management** | **62,037** | 53,714 |

## Reinsurance
Reinsurance assets fell by €140m as a result of the Part VII transfer of the Irish portfolio to Monument Life. At the same time, insurance liabilities fell by a similar amount.

During 2020 we entered into six new reinsurance contracts covering around £7.4bn of longevity risk in relation to both new and existing business. Some of Rothesay's reinsurance is an asset on an IFRS basis because projected claims exceed the regular premiums due on some longevity reinsurance contracts but overall the reinsurance represents a net liability of £377m (2019: net liability of £460m).

## Total equity
The increase in total equity (an increase of £1,099m from £3,776m at 31 December 2019 to £4,875m at 31 December 2020) was driven by the increase in retained earnings during 2020.

## Insurance liabilities
Insurance contract liabilities increased from £47.9bn as at 31 December 2019 to £55.2bn as at 31 December 2020 largely as a result of the new business written in 2020 and falling interest rates (see note E.2).

## Borrowings
On 22 May 2020, RLP issued a further £100m of Tier 3 bonds. The proceeds of the Tier 3 issuance were used to repay £100m of loans from participating interests leaving overall borrowings unchanged.

As part of our LIBOR transition programme, with effect from 19 December 2020 the subordinated loan from participating interests was converted from a floating rate loan to a fixed rate loan. The fair value of the loan was unchanged as a result of the conversion.

## Changes to accounting standards
The International Accounting Standards Board has announced that the implementation of IFRS 17, the accounting standard for insurance contracts, will be further delayed until 1 January 2023. The standard will have a big impact on the way Rothesay's results are reported because the standard rebuilds performance measurement from the ground up in areas ranging from a new definition of insurance revenue to the elimination of upfront profits and spreading of profit across the lifetime of the contract. As a result, IFRS profits that have been declared in the past (and up to 31 December 2022) will be re-calculated and the opening balance sheet adjusted accordingly. We do not envisage that the change in accounting will have a material impact on the way in which Rothesay is run.

During 2020 the IFRS 17 project team has continued to make progress. An initial assessment has now been completed on the potential impact of IFRS 17 and work will continue during 2021 on detailed implementation. The IFRS 17 project is being overseen by the Audit Committee.

Rothesay has taken the deferral option in relation to IFRS 9 and will adopt the standard on the effective date of the new insurance contract standard. However, IFRS 9 is expected to have relatively little impact on Rothesay as assets are already fair valued.

## Market consistent embedded value (APM)
Rothesay prepares supplementary information on an MCEV basis because we consider that embedded value reporting provides investors with a useful measure of the future profit streams of Rothesay's in-force long-term business. MCEV has increased from £6,032m at 31 December 2019 to £7,035m as at 31 December 2020, largely as a result of new business, the change in the approach to projecting LPI and falling interest rates. MCEV is summarised in the table below. Adjustments allow for Group borrowings and other Group adjustments.

| Market consistent embedded value (APM) | **2020 £m** | 2019 £m |
|---|---|---|
| Net worth of RLP | **6,374** | 5,181 |
| Value of in-force business | **2,745** | 2,757 |
| Less: debt and Group adjustments | **(2,084)** | (1,906) |
| **MCEV** | **7,035** | 6,032 |

The shareholders' equity on an MCEV basis is consistent with the sum of the shareholders' equity on an IFRS basis, the value of in-force business (APM) as shown above and debt valuation differences of £581m as at 31 December 2020 (2019: £499m). Most of this difference arises from the treatment of the Restricted Tier 1 notes as debt under MCEV. The debt valuation is £2,007m (2019: £1,926m) on an MCEV basis.

The value on an MCEV basis of new business written in 2020 was £576m (2019: £1,612m).

# Capital management

## The Group's capital position has remained robust throughout 2020.

Rothesay's capital management framework is designed to meet the following objectives:

- to maintain financial strength in adverse conditions;
- to give customers long-term confidence in Rothesay;
- to satisfy our regulatory obligations;
- to match the profile of our assets and liabilities, taking account of the risk inherent in the business;
- to allocate capital efficiently to support new business growth;
- to retain financial flexibility by maintaining strong liquidity; and
- to provide an appropriate return to shareholders.

Rothesay aims to maintain solvency coverage in the range of 130% to 150% of the regulatory minimum solvency capital requirement (SCR), so our capital position provides significant surplus capital for new business and potential future dividends. We operate a dynamic capital management framework which uses interest rate and other hedging to target stability of the IFRS balance sheet under normal conditions and seeks to manage both the IFRS and solvency balance sheets as conditions deteriorate. This is facilitated by our access to real-time solvency information.

Rothesay's solvency position has remained robust throughout the period despite considerable market volatility and falling interest rates. We started the year with capital surplus well above our target operating range. As at 31 December 2020, Rothesay had an SCR coverage ratio (APM) of 201% (2019: 202%), giving us significant excess capital to write new business. The solvency positions of the Group and RLP are summarised in the following table.

| | Group | | RLP | |
|---|---|---|---|---|
| Solvency position of the Group and RLP | **2020 £m** | 2019 £m | **2020 £m** | 2019 £m |
| Tier 1 capital | **5,781** | 4,677 | **5,857** | 4,658 |
| Tier 2 capital | **984** | 1,059 | **984** | 1,059 |
| Tier 3 capital | **512** | 396 | **512** | 396 |
| Own Funds (APM) available to meet SCR | **7,277** | 6,132 | **7,353** | 6,113 |
| SCR | **3,623** | 3,038 | **3,623** | 3,038 |
| **Surplus above SCR** | **3,654** | 3,094 | **3,730** | 3,075 |
| **SCR coverage (APM)** | **201%** | 202% | **203%** | 201% |
| **SCR coverage without transitional solvency relief** | **152%** | 153% | **154%** | 152% |

Assets in excess of those required to meet the technical provisions are known as Own Funds.

As part of the transitional arrangements in relation to the introduction of Solvency II, the Group is permitted to take credit for transitional solvency relief which amortises linearly to zero, falling by 1/16th on 1 January 2017 and again each year thereafter. Given the large fall in interest rates over 2020, the value of transitional solvency relief was recalculated as at 31 December 2020. The impact of recalculation was to increase the transitional to £1,298m net of the associated impact of tax on Own Funds and allowing for amortisation of 4/16ths (2019: £1,138m allowing for amortisation of 3/16ths). Transitional solvency relief now covers 57% of the risk margin (2019: 52%).

Rothesay's SCR is calculated using a partial internal model (PIM). The PIM means that Rothesay's bespoke models are used for calculation of credit and counterparty risk capital and ensures that the allocation of capital to investment is consistent with the risk inherent in the types of highly secured and collateralised investments which are core to Rothesay's investment strategy. The PIM was originally approved for use from 31 December 2018 and updated during 2019 to reflect feedback received from the Prudential Regulation Authority (PRA) and to cover investments in Dutch mortgages. Work continues on a Full Internal Model (FIM), extending the PIM to cover other risk components but for now the standard formula is used to calculate the SCR for all other risk components and for aggregation across risk components.

The table below provides a breakdown of the SCR post-diversification benefit between modules. Insurance risk relates mainly to longevity risk. Market risk is dominated by spread risk, i.e. the risk that credit spreads widen. The proportion of insurance risk capital has decreased during the period due to additional reinsurance transacted. The market risk proportion has increased from 54% of the SCR at the end of 2019 to 64% of the SCR, due to changes in economic conditions, investment of assets in 2020 and the reduction in insurance risk.

| | **2020 %** | 2019 % |
|---|---|---|
| Market risk | **64** | 54 |
| Insurance risk | **24** | 33 |
| Operational risk | **6** | 7 |
| Counterparty risk | **6** | 6 |

An analysis of the change in Own Funds (APM) and SCR is shown in the table below. Own Funds (APM) have increased from £6,132m to £7,277m after allowing for amortisation of 1/16th of transitional solvency relief on 1 January 2020. The biggest drivers of this change were changes in economic conditions (particularly falling interest rates and inflation), increased longevity reinsurance and the impact of investing assets according to our longer-term investment strategy. The increase in SCR from this new investment was less than envisaged when the new business was originally underwritten, i.e. investment has been more capital efficient than assumed. The SCR (APM) increased from £3,038m to £3,623m, largely as a result of falling interest rates and the impact of investing assets. The increase was partially offset by a realignment of hedges between funds. All numbers are shown net of tax impacts and allow, where relevant, for changes in transitional solvency relief.

In the table below, we have amended the 2019 movement analysis (compared to that provided in the 2019 annual report and accounts) to remove the impact of writing new business on the financial resources requirement limit when re-calculating transitional solvency relief as we believe that this impact distorts the analysis. This has led to a £606m reduction in the impact of writing new business (on a fully invested basis) and a corresponding reduction in the short-term impact of delayed deployment compared to that shown in the 2019 annual report and accounts. Differences between IFRS accounting standards and Solvency II mean that management actions and changes in economic conditions can have very different impacts on the two bases.

| | **2020** | | 2019 | |
|---|---|---|---|---|
| Change in Own Funds and SCR (APM) | **Change in Own Funds £m** | **Change in SCR £m** | Change in Own Funds £m | Change in SCR £m |
| Opening position | **6,132** | **3,038** | 3,918 | 2,163 |
| Amortisation of 1/16th of transitional on 1 January | **(88)** | **18** | (43) | — |
| New business (on a fully invested basis) | **5** | **455** | 732 | 1,170 |
| Short-term impact of delayed investment | **(218)** | **(294)** | (606) | (420) |
| Investment impact from prior year | **606** | **304** | 271 | 41 |
| Performance of in-force book | **541** | **(298)** | 124 | (265) |
| Non-economic assumption changes | **192** | **(54)** | 35 | (4) |
| Acquisition costs and administration expenses | **(172)** | **—** | (160) | — |
| Borrowing costs | **(108)** | **—** | (86) | — |
| Non-recurring and project expenditure | **(34)** | **—** | (24) | — |
| Economic conditions | **421** | **454** | 446 | 307 |
| New capital issuance | **—** | **—** | 1,479 | — |
| Changes to internal model | **—** | **—** | 46 | 46 |
| **Closing position** | **7,277** | **3,623** | 6,132 | 3,038 |

> A year like 2020 demonstrates the importance of having a robust risk management framework.

**Peter Shepherd**
Chief Risk Officer

# Risk management

## The management of risk is central to the success of the business. Every employee knows that they are responsible for the identification and management of risk.

Rothesay's risk management principles are driven by the key objectives of the business:

- To ensure that our liabilities to policyholders can be met in a full and timely manner.
- To maintain our financial strength and capitalisation.
- To produce stable earnings from our in-force business.
- To protect and increase the value of our shareholders' investment.
- To safeguard Rothesay's reputation.

The risk management framework is intended to ensure that we identify and understand all of the risks inherent in the business. Where appropriate, longevity reinsurance, asset liability matching and hedging strategies are used to manage that risk and to optimise use of capital. We also look to mitigate credit risk through investing in assets that benefit from collateral and structural protections.

Throughout 2020 Rothesay continued to invest in the risk function, increasing headcount across the function including in relation to compliance, to meet the needs of Rothesay and to be able to respond robustly to the changing nature of the uncertainties facing Rothesay.

### Risk management framework

Rothesay has an embedded risk management framework (RMF) which ensures that every employee knows how they contribute to the effective management of all types of risks.

Further detail on the components of our RMF is provided on the next page. The RMF informs and is directed by Rothesay's business strategy. Risk management considerations are integral to setting business strategy, as we seek to optimise our risk-adjusted returns and create shareholder value whilst also meeting the expectations of our customers and other stakeholders. The RMF ensures both clear ownership and strong oversight of all of Rothesay's risks, both quantifiable and non-quantifiable.

### Board risk appetite and culture

Rothesay's risk appetite expresses the types of risk that Rothesay is willing to be exposed to in pursuing strategic objectives. The Board's risk appetite sets the tone for the culture of risk management throughout the organisation.

Our strategic approach is to de-risk our business in order to achieve attractive risk-adjusted returns. We aim to protect regulatory surplus and minimise balance sheet volatility by hedging longevity risk and adopting a cautious approach to investment.

Risk taking is therefore limited to circumstances where we believe that we fully understand the inherent and residual risks, where we are able to manage them within prudent, observable levels and where incurring the risks provides sufficient value to our stakeholders.

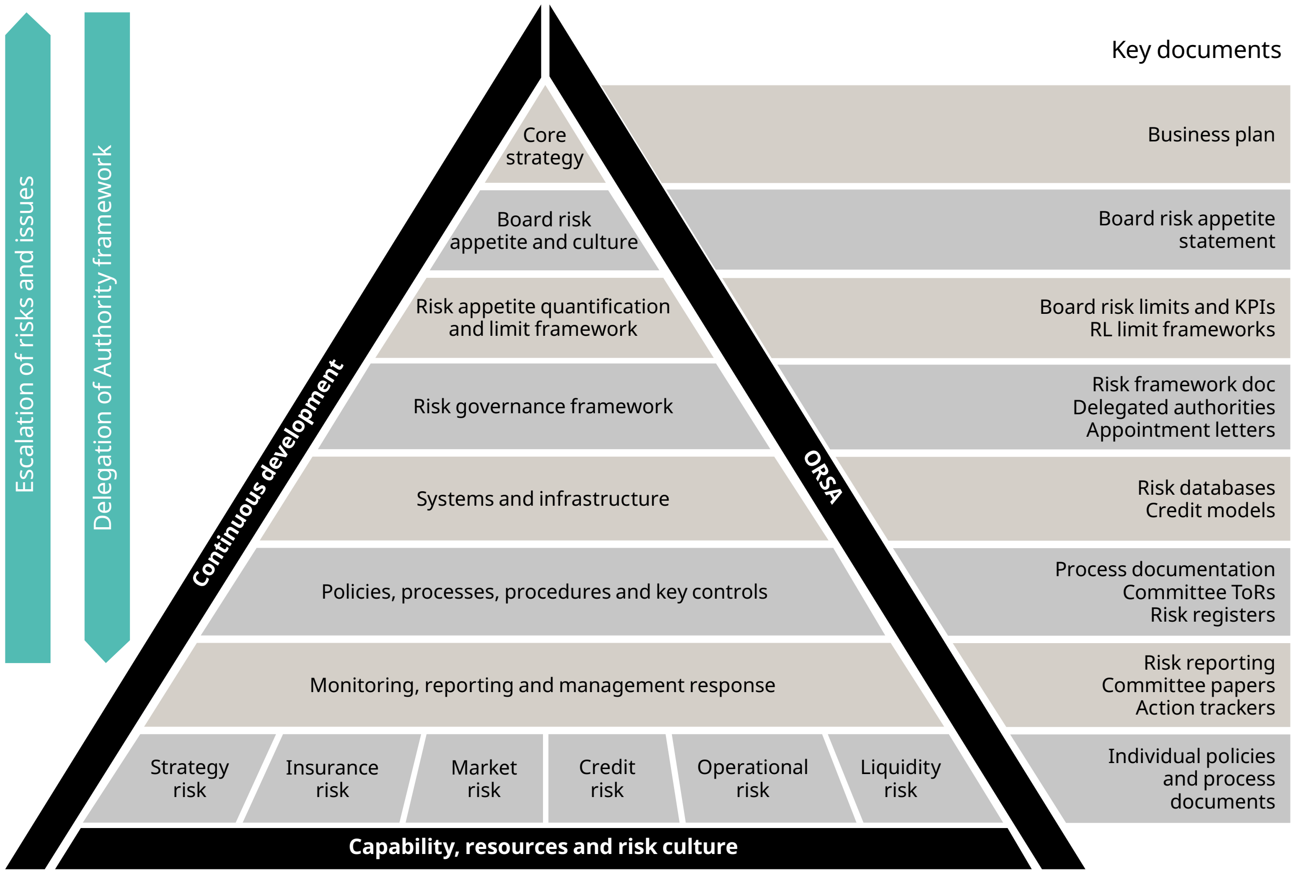
We aim to substantially mitigate the financial risks in our portfolio in order to protect policyholders, lock in value and to safeguard capital surplus such that excess capital may be invested into attractive risk-adjusted new business opportunities where Rothesay believes it has a comparative advantage.

Our risk appetite statement sets out the types of risk that we are willing to be exposed to in order to meet our strategic objectives. They are categorised as:

- Desired – risks that are core to the business model;
- Tolerated – risks that we incur as a result of the business model but try to mitigate or manage in some way; or
- Undesired – risks that we will seek to avoid or fully eliminate where possible.

All possible risks are considered as part of defining the overall risk universe for Rothesay, with each risk categorised as above and assigned an executive risk owner.

# Risk management
**continued**




## Risk appetite quantification and limit framework

The risk limit framework is intended to ensure the stability of earnings and solvency position of the business. Risk appetite is translated into quantifiable limits and early warning triggers that prompt management action to avoid our risk exposures breaching the Board's risk appetite. Limits exist in relation to market, credit, counterparty, liquidity, demographic and longevity risks and are sized with reference to our overall risk appetite and capital position. Limits are constantly reviewed and regularly reported against.

## Risk governance framework

Rothesay's risk governance arrangements strengthen the risk-taking and risk management of the business by adding challenge, oversight and independent assurance.

This framework is part of our commitment to compliance with the Senior Managers and Certification Regime (SMCR).

Rothesay adopts the principles of a 'three lines of defence' model for effective risk management that provides a consistent, transparent and clearly documented allocation of accountability and segregation of functional responsibilities.

- **First line**: Day-to-day risk management is delegated from the Board to the Chief Executive Officer (CEO) and, through a system of delegated authorities, to business managers. Rothesay also makes the distinction between:
  - the risk-taking functions, including investment and new business origination; and
  - the control functions, whose responsibility it is to ensure the integrity of Rothesay's operations and reporting. These include operations, finance and legal.

- **Second line**: Risk oversight is provided by the Chief Risk Officer (CRO), his team and risk management committees. The executive-level Working Level Risk Committee (WLRC) is chaired by the CRO and consists of relevant senior managers working within a delegated risk management framework. This committee, and its sub-committees, review all material new investment, hedging or liability transactions, and is supported by a number of other committees which focus on risks arising from new activities, methodology and assumptions underlying our financial modelling and the management of third party suppliers.
- **Third line**: Internal Audit provides the Board and Executive with comprehensive, independent, objective assurance over governance, risk management and internal control.

| | | Risk Preference | | |
|---|---|---|---|---|
| **Risk type** | **Definition** | **Undesired** | **Tolerated** | **Desired** |
| **Strategy Risk** | The risk of loss in future earnings and capital arising from changes in the competitive, economic, legal or political environment, changing customer behaviour, or a failure to select appropriate strategic or long-term business plans. | | | • |
| **Insurance Risk** | The risk of loss or of adverse change in the value of insurance liabilities, due to inadequate pricing and provisioning assumptions, or changes in longevity or other expectations. | | | • |
| **Market Risk** | The risk of loss or of adverse change resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. | | • | |
| **Credit Risk** | The risk of loss or of adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors. | | | • |
| **Liquidity Risk** | The risk of being unable to realise investments and other assets in order to settle financial obligations when they fall due. | • | | |
| **Operational Risk** | The risk arising from inadequate or failed internal processes, personnel or systems, or from external events. This includes conduct risk and IT security risk. | • | | |

The Board has overall responsibility for the management of the exposure to risks and is supported by the Board Risk Committee (BRC) whose membership consists entirely of Non-Executive Directors and looks to ensure that the management of the business is conducted within the delegated risk framework from the main Board.

### Systems and infrastructure
Rothesay operates an integrated system infrastructure which captures all assets and liabilities centrally and provides us with the capability to report and monitor risk daily at both the portfolio and the individual transaction level. Close coordination of underwriting, reinsurance, investment and risk hedging functions ensures risk management is central to all aspects of the business, and that new business pricing reflects latest market conditions, hedging costs and investment opportunities as well as comprehensive liability analysis.

### Policies, processes, procedures and key controls
Our risks are grouped into one of six categories: strategy, insurance, market, credit, operational and liquidity risk. Rothesay has developed appropriate processes and documented procedures, appropriate controls and other risk mitigation techniques in order to manage them effectively. The policy framework ensures that an appropriate suite of risk management policies is maintained which set out the principles and standards for risk identification, measurement, mitigation, control and monitoring.

# Risk management
**continued**

### Monitoring, reporting and management response
We monitor our risk exposures against risk appetite as well as management actions on a continuous basis to confirm that our risk mitigations are effective. We then report our monitoring to oversight committees and individuals with responsibility for risk management in order to inform business decisions. Monitoring considers both those risks to which Rothesay is currently exposed, in addition to emerging risks that may impact Rothesay in the future.

### Capability, resources and risk culture
Rothesay seeks to attract and retain the highest quality talent in the industry. The effectiveness of our risk management depends upon the high quality of our people and the strong risk culture and risk management practices.

We are committed to maintaining the highest standards of integrity, transparency and accountability. Good conduct is fundamental to our purpose, strategy and how we operate and is also good business practice. A good culture is one where people do the right thing, feel empowered to speak up if something doesn't look right and know they can rely on support from management. Training is conducted so that everyone understands Rothesay's culture and the part they play in maintaining standards and in managing risk effectively.

Risk management and conduct are an integral part of Rothesay's performance review process.

### Own Risk and Solvency Assessment (ORSA)
The ORSA is undertaken at least annually and involves an assessment of the risks to which the business is exposed as well as solvency forecasting in a range of scenarios, including consideration of the stresses that could jeopardise Rothesay's business plans. The ORSA is an important input to Rothesay's strategic planning cycle.

Rothesay also runs a number of stress tests on a daily and weekly basis. The stresses have been developed so as to provide coverage over the key risks implicit within the portfolio at the time. Examples of stresses currently applied to the portfolio include issuer default stresses, property stresses, credit spread widening, credit downgrades and market risk stresses on liquidity outflows.

### Continuous development
The way we think of and manage risk is constantly evolving. The CRO is responsible for developing the RMF to ensure that risk management remains effective.

### Changes in Rothesay's risk profile and emerging risks
2020 was dominated by the impact of COVID-19 on our business operations and on financial markets.

Our market-leading risk management systems have allowed us to protect our balance sheet during adverse and volatile market conditions. By the end of 2020, market conditions had improved, with credit markets being close to the levels seen at the end of 2019, although we believe that there is heightened risk of corporate downgrades in 2021 as the impact of COVID-19 restrictions continue to be felt.

As noted earlier, the transition to home working was seamless and our third party administrators also responded well. As a result, there has been no obvious impact on our operations, with productivity remaining at a good level and risk controls continuing to work effectively. Despite COVID-19, Rothesay continued to grow in 2020, writing £7bn of new business. Rothesay now manages assets of over £62bn and insures the pensions of over 800,000 individuals.

We entered into six new reinsurance contracts in 2020 covering both new and existing business and taking our reinsurance coverage up to 87% (2019: 78%). Longevity reinsurance reduces the capital intensity of new business and allows the release of capital held against existing business.

Rothesay has continued its strategy of investment in a diverse range of assets, but given market conditions in 2020, there have been fewer opportunities to invest in more illiquid assets so many of the new investments have been in more liquid, highly rated corporate bonds, including US universities and healthcare providers, as well as in loans issued by conservatively managed and leveraged real estate investment trusts, particularly those focused on industrials. A systematic review of our investment portfolio led to the identification of sectors most likely to be adversely impacted by COVID-19 and of assets most at risk of downgrading to sub-investment grade. Where possible, we have proactively switched assets accordingly. This analysis is also used in stress and scenario testing.

The long-term impact of COVID-19 is still unclear. The long-term effectiveness of vaccination programmes is uncertain and governments continue to advise that it may be some time before life returns to normal. Rothesay's evolving investment strategy, together with the backdrop of market volatility and uncertainty over the future impact of COVID-19, has meant that

Rothesay's proactive approach to risk management has continued to be crucial in delivering Rothesay's strategic objectives and ensuring continued financial security for our policyholders.

Rothesay has continued to strengthen its control functions and the risk function, bringing in additional experts in credit risk. We have also strengthened our in-house internal audit capabilities.

There continue to be changes in accounting regulation, asset trading markets, pensions and tax, the effects of which are highly uncertain. The government's proposed reform of the leasehold market could have an adverse impact on Rothesay's loans secured on ground rents. In addition, the Treasury is consulting on changes to prudential regulation now that the UK is outside the EU which could impact Rothesay's regulatory balance sheet. Potential changes include a reduction in the risk margin and a relaxation of matching adjustment rules.

## Transition from LIBOR

The interest rate London Interbank Offer Rate (LIBOR) benchmark is expected to cease after the end of 2021. During 2020 the risk function has been overseeing the project which aims to ensure that Rothesay is ready to transition to alternative rates.

Rothesay closely monitors its exposure to the basis between LIBOR and Sterling Overnight Index Average (SONIA) swaps and has taken action to mitigate this risk. Most new trades are SONIA-based and during 2020 we have been converting existing contracts to be SONIA based. In addition, we have converted our own floating rate bond to a fixed rate (on a fair value neutral basis).

We are now using SONIA as the basis for setting the risk free rate under IFRS and MCEV. The PRA is now consulting on the changes required under Solvency II (Consultation paper CP1/21 - "Solvency II: Deep, liquid and transparent assessments, and GBP transition to SONIA"). Scenario analysis shows that whatever the change required, the impact on our solvency position is likely to be small.

## RPI reform

In November, it was announced that the UK's Retail Price Index (RPI) inflation measure will be aligned with the Consumer Price Index including housing costs (CPIH) from 2030, with no compensation for holders of index-linked gilts. Rothesay closely hedges its inflation exposure and does not use RPI-linked assets to hedge CPI-linked liabilities, so the change in the value of index-linked gilts and RPI-linked derivatives as a result of RPI reform was largely matched by a change in the value of liabilities.

## Brexit

As a UK insurer serving the domestic market, Rothesay's business model is largely unaffected by the UK's withdrawal from the EU.

The successful Part VII transfer of our small portfolio of Irish annuities to Monument Life Insurance DAC (formerly Laguna Life) in September 2020 means that none of the remaining business was written under passporting. We do have a number of ex-pat policyholders based outside the UK. In the unlikely event that we are prevented from making payments to such policyholders we will look to take alternative steps to ensure continuity of pension payments. We have asked all who may be affected to contact their banks for clarification on the measures they plan to take.

Rothesay has reviewed its investment portfolio, suppliers and counterparties and taken action to ensure contract continuity. We have also taken steps to ensure that our EU employees continue to have the right to work in the UK.

## Longer term

Rothesay has identified a number of emerging risks that could impact the business over the medium to long term. Geopolitical risk continues to be high across Europe and Asia, driven by changes in government, evolving global relationships and unexpected fallout from Brexit.

Over the longer term there are risks relating to climate change and how this could impact Rothesay's investments, as well as emerging or changing drivers of population mortality, including antimicrobial resistance, new screening technologies, dementia management and scope for pharmacological breakthroughs. Rothesay's investment policy requires consideration of the potential impact of climate change on new investments. See page 59 for further details of our commitment.

Rothesay continues to manage its affairs prudently such that we are not over-exposed to one particular risk and so that we only accept risks which we understand and where we are adequately rewarded for accepting them.

# Risk management
**continued**

## Principal risks and uncertainties facing Rothesay

Rothesay's principal risks are credit, insurance, liquidity and market related. An overview of these and other risks associated with the business, including an outline of how each is mitigated and how the risk has changed from last year, is provided in the table below. Our risk exposures generally increase with the size of the balance sheet; in the table below we have only shown an increasing trend where the increase has been out of line with this.

In the table, strategic priorities 1 to 4 refer to:
**1.** Financial security **2.** Steady growth **3.** Service excellence **4.** Reliable performance

More details can be found in sections E and F of the financial statements.

| Risk | Mitigation | Strategic priority | Change from last year |
|---|---|---|---|
| **Credit risk**<br>The risk that an investment counterparty's creditworthiness deteriorates or that the counterparty defaults. Our financial and/or capital position could be adversely impacted by downgrades, credit spread widening or defaults. | Rothesay carefully selects the investments it makes in order to generate an adequate risk-adjusted return, has a preference for investments with structured protection such as collateral, and may purchase external credit protection to mitigate the impact of any defaults.<br><br>Rothesay maintains a highly experienced market-facing team as well as a second-line internal credit risk team who regularly monitor and assess the credit risk associated with its investments. | 1,4 | This risk has increased as a result of the impact of COVID-19 restrictions and as the balance sheet has grown. |
| **Counterparty default risk**<br>The risk that a financial counterparty's creditworthiness deteriorates or that a counterparty defaults. Our financial and/or capital position could be adversely impacted by downgrades, credit spread widening or defaults. | Rothesay prefers to work with highly rated and stable counterparties, and to diversify counterparty exposures where appropriate.<br><br>Derivative and reinsurance contracts are subject to margining requirements to ensure exposures are appropriately collateralised.<br><br>Rothesay actively monitors counterparties for downgrade risk, and may also purchase credit protection to mitigate specific exposures. | 1,4 | This risk has increased as a result of the impact of COVID-19 on our counterparties. |
| **Insurance risk**<br>The risk that demographic experience is different from expected. As the pensions insured by Rothesay are guaranteed, our financial and/or capital position could be adversely impacted if, for example, policyholders live longer than expected. | Rothesay invests in both people and modelling capabilities to understand its longevity experience and to help assess what could happen in the future.<br><br>Rothesay aims to reinsure a majority of its longevity exposure. As at 31 December 2020, Rothesay had reinsured 87% of its longevity risk (2019: 78%) (APM). | 1,4 | Although we are now more reinsured, the balance sheet has also grown.<br><br>The impact of COVID-19 on future longevity remains uncertain. |

| Risk | Mitigation | Strategic priority | Change from last year |
|---|---|---|---|
| **Market risk**<br>The risk of adverse movements in interest rates, inflation or currency. Rothesay's financial and/or capital position could be adversely impacted by market movements to the extent that assets and liabilities are mismatched. | Rothesay monitors interest rate risk and foreign exchange risk closely, and uses derivatives to hedge the risks. We also undertake regular scenario testing, for example in relation to a UK downgrade, to understand the impact of potential combinations of stresses.<br><br>Assets and liabilities are matched as closely as possible, including using inflation-linked assets to meet inflation-linked liabilities. | 1,4 | Volatile market conditions have increased in 2020. |
| **Property risk**<br>The risk of a fall in the value of property. Through its investments secured on property, Rothesay's financial and/ or capital position could be adversely impacted by falls in the value of property. | Residential property risk is reduced through strict underwriting criteria, covering, for example, the quality of the underlying property, flood risk and loan-to-value limits by age of borrower. We have also established prudent reserves covering the potential cost of the no negative equity guarantee on equity release mortgages.<br><br>Exposure to commercial real estate is reduced by ensuring that loans have a low loan-to-value ratio, that there are appropriate covenants and that properties have strong tenants. | 1,4 | The long-term impact of COVID-19 restrictions on property prices remains unclear, heightening this risk. |
| **Liquidity risk**<br>The risk of being unable to realise investments and other assets in order to settle financial obligations when they fall due. Given our holding of illiquid assets, there is a risk that we are unable to meet payments or collateral calls as they fall due in adverse circumstances. | Rothesay has a comprehensive liquidity management framework that ensures sufficient liquidity is held to meet collateral outflows as well as projected expenses and other outflows, in extreme market conditions. | 1,4 | Market movements in 2020 led to large collateral calls. However Rothesay's liquidity position has remained robust throughout. |
| **Climate change**<br>Rothesay's assets are exposed to the potential impact of climate change. Such risks include:<br>• physical risks such as increasing frequency and severity of flooding; and<br>• transition risks which can arise from the process of adjustment towards a low-carbon economy. | Rothesay has established a Climate Change Working Group to focus on improving the way in which we manage this risk.<br><br>Our in-house investment team is responsible for the selection and management of all of Rothesay's assets. The team considers climate-related risk as part of the investment process.<br><br>In addition, Rothesay considers flood risk as part of its lending policies. | 1,4 | Rothesay has committed to supporting the UK in achieving carbon neutrality by 2050 and to aligning our investment with the aims of the Paris Accord.<br><br>See page 59 for further information. |

# Risk management
**continued**

| Risk | Mitigation | Strategic priority | Change from last year |
|---|---|---|---|
| **Operational risk**<br>The risk of operational failure, including conduct failures. Rothesay is exposed to the risk of operational failure as a result of failure of a strategic business partner or of its own systems and processes. This could lead to reputational damage and increased costs. | Rothesay has no appetite for material operational risk losses, and has a strong control environment to limit these risks as far as possible.<br><br>The Customer and Conduct Committee is responsible for ensuring that stakeholders are treated fairly by Rothesay and its strategic business partners.<br><br>Scenario analysis covering a variety of potential operational risk events is regularly carried out. Rothesay seeks to mitigate cyber risk through robust processes and controls including data protection, penetration testing and staff training, and maintains ISO 27001 and ISO 22301 accreditation.<br><br>Where Rothesay outsources some of its responsibilities, we undertake thorough due diligence in advance of appointment and then have a strong programme of oversight. | 3,4 | Through the COVID-19 pandemic, Rothesay and our business partners have demonstrated operational resilience.<br><br>Cyber and financial crime risk continue to be heightened. |
| **Strategic, political and regulatory risk**<br>The risk of adverse changes to the regulatory or political environment. Rothesay's strategy, financial or capital position could be adversely affected by the impact of regulatory or political change. | Rothesay continues to actively monitor the political landscape. Where appropriate, Rothesay carries out lobbying activities or responds to consultations which may directly impact it. Strategic decisions take into account the overall political landscape.<br><br>Rothesay's potential exposure to leasehold reform is mitigated by structural protections in the loans advanced.<br><br>Rothesay seeks to have a regular dialogue with regulators in order to ensure compliance, as well as the ability to react quickly to any unanticipated developments. Rothesay seeks to have an open and transparent relationship with regulators at all times.<br><br>Rothesay is a member of the Confederation of British Industry and the Association of British Insurers and we participate in consultations to ensure that our interests are protected for the benefit of our stakeholders. | 1,2,4 | There are continued political risks globally.<br><br>The government's planned reform of the leasehold market could have an adverse impact on Rothesay's loans secured on ground rents.<br><br>The emergence of defined benefit consolidator schemes could prove a threat to the pension de-risking market if consolidator schemes become a viable alternative means of de-risking pension liabilities for well-funded pension schemes or companies. |

# Viability statement

## Rothesay viability statement

Rothesay's strategy and business model, which are detailed in the strategic report, both centre around long term pension security for our policyholders. This focus leads both management and the Board to consider the viability of Rothesay on an ongoing basis. The viability of Rothesay is linked to our ability to generate profits and maintain solvency and liquidity over a period of time.

## Why we assess viability

The Board's assessment of viability is a central process within our risk management and strategic planning framework. Rothesay has been purpose-built to protect pensions and ensuring the Group remains viable is critical to protecting our policyholder's pensions.

## The period we assess

Making a viability assessment requires the principal risks (pages 42 to 44) of the Group to be thoroughly understood and regularly updated for changes.

Rothesay's own views of risk and associated capital requirements have been investigated through the ORSA, including consideration of the way in which future changes to Rothesay's risk profile and also external influences may impact on the Group's solvency needs and ability to execute the business plan. The ORSA, approved by the Board in December 2020, considers risks across a five-year time horizon and therefore it is felt appropriate for the viability assessment to be considered across the same time horizon. Rothesay recognises that the Group has policyholder liabilities which extend beyond the five-year horizon but considers that year by year projections beyond the five-year period are likely to be unreliable given everything that might happen in that time. However, given the projected financial position of the company in five years' time on a range of scenarios, the Board do not consider there to be any going concern or viability issues beyond this time frame.

## How we assess viability

The ORSA includes a number of forward-looking scenarios intended to test the impact of stresses and scenarios that may impact Rothesay's ability to execute the business plan. Scenarios considered include shocks to new business (up and down), liquidity, financial markets (including the global financial crisis) and longevity. More details can be found in notes E and F of the financial statements. The results demonstrate the robustness of Rothesay's solvency and provide insight into the way in which the business plan would need to be adapted to respond to adverse conditions. Management and the Board believes Rothesay is well capitalised on both a regulatory and economic capital basis.

Given the dynamic nature of the market, the strategic business plan is based on a shorter period of three years and is prepared on a rolling basis and reviewed and approved annually by the Board. The last business plan was reviewed and approved in July 2020 and has not been impacted by the change in ownership of Rothesay, and remains appropriate. The business plan is refreshed if there are material changes to the business model or market environment. The business plan is centred around Rothesay's projected new business targets, with assumptions about pricing, reinsurance, investment strategy, revenue generation, expenses and leverage based on Rothesay's existing business and target operating model. In certain scenarios where there is very material new business growth, the plan also assumes that new equity would be provided by our shareholders. IFRS pre-tax profits are driven by two key sources: new business profitability and profit emergence on the Rothesay back-book.

## COVID-19

Scenario analysis has helped inform the Board's assessment of the future potential impact of COVID-19 on Rothesay's financial position. The results of this analysis combined with Rothesay's continuing operational and financial resilience throughout 2020 mean that the Board is confident that COVID-19 will not impact Rothesay's long term viability.

## Our assessment of viability and going concern

Based on the results of this analysis, the Board has a reasonable expectation that Rothesay will be able to continue in operation and meet its liabilities and obligations as they fall due over the five-year period of the assessment.

The same analysis also informs the Board's assessment of Rothesay's ability to continue to adopt the going concern basis of accounting.

# Section

# 3

# Stakeholder engagement

## Providing long-term pension security is at the heart of what we do.

As well as policyholders, Rothesay has responsibility to a number of other stakeholders, including our suppliers, our people, our community, the regulators, the environment and our investors.

### Section 172 (1) statement

At each Board meeting, the Board considers the impact on stakeholders and the requirements of s.172 of the Companies Act 2006 when making decisions. The Company Secretary sets out the text of s.172 on every Board agenda.

Given the long-term nature of our business, the Board is very focused on the likely long-term consequences of decisions and believes that it has acted in a way that promotes the success of Rothesay. Our Corporate Social Responsibility policy describes the way in which Rothesay aims to engage positively with all our stakeholders – a key concern of the Board.

Stakeholder engagement and the way in which their interests have been taken into account by the Board in its decision making is described in the table in the following pages.

# Stakeholder engagement
**continued**

| Overview | Engagement | Outcomes |
| --- | --- | --- |
| **Our customers**<br>Providing long-term pension security to our 847,839 policyholders is at the heart of what we do.<br>Read more **on page 50** | • The Customer and Conduct Committee receives regular reports on customer service levels and complaints and oversees customer interaction.<br>• The Board discusses customer service issues and in 2020 was focussed on ensuring that customers continued to receive excellent service despite the impact of COVID-19.<br>• Directors and management have ad hoc meetings with pension scheme trustees throughout the year. | • Customers continued to receive excellent customer service despite the impact of COVID-19.<br>• 95% of policyholders rate our service 'good' or 'excellent'.<br>• We were able to help 12 pension schemes to de-risk their liabilities in 2020. |
| **Our people**<br>The commitment and quality of our people are integral to Rothesay's success.<br>Read more **on page 56** | • Senior management and the Chairman have frequent, informal interaction with our people.<br>• The Board reviewed the results of our employee engagement surveys and the actions taken in response.<br>• The Board oversaw the way in which we supported our people through the COVID-19 pandemic. | • Rothesay's people have very high levels of engagement with 92% saying that they are proud to work at Rothesay.<br>• Almost all results of the 2020 employee survey were improved compared to 2019.<br>• Staff turnover has been very low. |
| **Our community**<br>We invest over £30.9bn in the UK economy and make a significant tax contribution in the UK. We have also established the Rothesay Foundation and support a range of charities.<br>Read more **on page 62** | • The Board has reviewed Rothesay's Corporate Social Responsibility policy.<br>• The Board approved the establishment of the Rothesay Foundation and the contribution to the COVID-19 Support Fund.<br>• The Chief Financial Officer (CFO) was a member of the COVID-19 Support Fund Committee which oversaw the distribution of funds. | • Through the Rothesay Foundation and other charities, we have made donations of over £4.1m. |
| **Our environment**<br>Rothesay is committed to reducing the carbon intensity of both our investments and our own operations.<br>Read more **on page 59** | • The Board receives updates on the work of the Climate Change Working Group and has debated and approved the various commitments made by the Group.<br>• The Board Risk Committee oversees the activities of Rothesay's Climate Change Working Group and receives regular reports on progress. | • We have become a supporter of the Task Force on Climate-related Financial Disclosures (TCFD), a signatory to the UN Principles for Responsible Investing, and an early adopter of the Sustainability Reporting Standard for Social Housing.<br>• We have made ambitious climate-related commitments.<br>• Our energy consumption reduced between 2019 and 2020. |

| Overview | Engagement | Outcomes |
| --- | --- | --- |
| **Our business partners**<br>Our strategic outsourcing partners are critical to us delivering service excellence to our customers.<br>Read more **on page 64** | • The Board receives regular updates on the performance of our strategic outsourcing partners, who are monitored against defined KPIs.<br>• The Audit Committee received the results of an internal audit into the way in which we oversee third parties. | • Our partners have continued to deliver excellent service to Rothesay and our customers Rothesay and our customers despite the impact of COVID-19 on their operations. |
| **Our regulators**<br>Having a transparent, open and proactive relationship with our regulators is important to the performance of the business. | • The Chairman and Executive Directors have regular meetings with the PRA.<br>• The PRA attends the Board as part of the Periodic Summary Meeting cycle.<br>• The Board receives regular updates on regulatory compliance from the CRO and Chief Compliance Officer. | • Our regulators have been fully engaged with the change of control process and with the development of the full internal model. |
| **Our reinsurers**<br>Our reinsurers help us to manage our balance sheet by allowing us to hedge longevity risk.<br>Read more **on page 64** | • Members of senior management have met with a number of the reinsurers during 2020.<br>• The BRC oversees reinsurance counterparty risk management and approves all material reinsurance transactions.<br>• The Audit Committee receives a report from the Chief Actuary on Rothesay's reinsurance arrangements and strategy. | • Our reinsurers have provided a further £7.4bn of longevity reinsurance protection.<br>• The reinsurers have also responded quickly in support of us underwriting new business. |
| **Our shareholders**<br>Rothesay benefits from the support and commitment provided by its two long-term institutional shareholders.<br>Read more **on page 65** | • Each of the shareholders is represented on the Board by a Non-Executive Director.<br>• The shareholders receive regular management information. | • GIC and MassMutual increased their investment in Rothesay by acquiring Blackstone's shareholding.<br>• The shareholders support Rothesay in other ways, for example assisting in the sourcing of investments and providing longevity reinsurance. |
| **Our bondholders**<br>Rothesay appreciates the support of our bondholders.<br>Read more **on page 65** | • Senior management meets with debt investors on a regular basis and makes presentations to groups of investors and analysts. | • We are pleased with the support provided by our bondholders through debt changes made in the year. |

## Our customers

# Securing the future for 847,839 people

There's one thing Rothesay must always do, regardless of everything else – and that's pay the benefits of our 847,839 policyholders. However they come to us – buy-in or buy-out, or from another insurer – it's this obligation that we prioritise above all others.

We also know it's not enough to simply pay benefits. It's also vitally important to be there for our policyholders, especially in huge life-event moments like retirement. That's why we are proud to deliver demonstrably excellent customer service, focused on real care in every detail.

This combination of secure and certain income alongside genuine service excellence means our customers can be reassured that their future is in safe hands.

# Genuine service excellence

## 30 seconds

80% of calls to our call centres are answered in 30 seconds or less

## 95% positive

Policyholders rating our service ‘good’ or ‘excellent’

## UK team

Every one of our call centres is based in the UK

**COVID-19**

Our priority throughout the COVID-19 crisis has been ensuring that we continue to provide our policyholders with the service they expect.

Our third party administration partners quickly moved to home working for most staff and they have responded well to the crisis. The Operations team spent time with all our administrators to understand the impact of home working and other COVID-19-related constraints on their operations. By prioritising work appropriately, service levels have been met consistently throughout the crisis. Even with most staff working remotely, 80% of calls have been answered in 30 seconds or less.

**Our Irish policyholders**

As a result of Rothesay’s acquisition of MetLife Assurance Limited in 2014, we acquired a small portfolio of Irish annuities. In order to ensure continuity of pension payments post-Brexit, we took the decision to sell the portfolio to the Monument Life Group. The transaction was initially structured as a reinsurance contract with Monument Re Limited but we received Court approval to transfer the policies to Monument Life Insurance DAC with an effective date of 7 September 2020.

Extensive preparations meant that the transfer was seamless with our Irish policyholders continuing to receive their pension payments as expected.

**Prudential transaction**

In December 2020, the Court of Appeal ruled in favour of Rothesay and Prudential, providing clarity for us and the sector as a whole about the operation of Part VII transfers. We plan to seek approval to transfer the Prudential portfolio to Rothesay during 2021 as originally envisaged by us and Prudential when the reinsurance agreement was first entered into.

We will work hard to ensure an effective transfer of this business should we be granted approval. Until then the policyholders remain Prudential’s customers and will continue to be serviced by them.

# Our customers
**continued**

## Supporting vulnerable customers
The COVID-19 crisis has meant that supporting vulnerable customers has never been more important. We are proud of the fact that all of our policyholders are treated as individuals and we have strong governance in place to help ensure we follow best practice in this area. We are actively engaged with the Association of British Insurers (ABI) and are a member of their Vulnerable Customers Working Group.

Rothesay has also joined the Death Notification Service. This is a free customer-facing service that is intended to make the death notification process easier during a difficult time.

## Enabling flexibility with small pots
In 2018, we initiated a "small pots" initiative under which pensioners with relatively small annuities (benefit value of less than £10,000) were offered a one-off opportunity to take a lump sum payment and this initiative continued throughout 2019 and into early 2020. Unfortunately, as a result of COVID-19, we decided to suspend the initiative during 2020, with a view to re-starting when conditions normalise.

We are actively engaging with the FCA on this initiative, which is overseen by our Customer and Conduct Committee to ensure fair treatment of our customers.

## Branding
During 2020 we updated our brand, introducing a new look and feel for the Company which we believe better reflects our size along with our founding principles of meticulous attention to detail and passionate care for the pensions we protect. We also shortened our name to simply 'Rothesay' as this is how our policyholders and partners refer to us and is consistent with our heritage as a company which was purpose-built to protect pensions rather than to provide other forms of life insurance.

## Robust service delivery
Not only do we ensure that all of our processes follow the 'Treating Customers Fairly' principles, we also seek to exceed the standards and guidelines set out by the Financial Conduct Authority, the Pensions Regulator and the Association of British Insurers.

As noted earlier, we operate an outsourcing model for pension administration and payroll services. Each of our three pension administrators – Capita Employee Solutions, Willis Towers Watson, and Mercer – have dedicated teams who support Rothesay, with all calls and policyholder interaction carried out in the UK.

A high degree of automation and technology means that our outsourced administration platforms interact with our risk management systems to minimise discrepancies and ensure that we pay policyholders and fund our clients accurately and on time.

In the last year we have continued to invest in automation and efficiency projects to ensure we have a robust control environment to manage existing and future business without compromising our high service levels and our continued commitment to our policyholders. We assign new third party contracts in a way which is intended to deliver a high quality customer service and takes into account factors such as transaction timing, scheme complexity, membership size, potential business pipeline, ongoing projects and cost.

We continue to manage the administrators through a series of proven, robust governance processes, including service level agreements which are amongst the most challenging in the industry. This ensures we maintain excellent customer service levels across case work and call handling (with 95% of targets being met). Our complaint levels continue to be low with just 0.98 complaints received per 1,000 policyholders (APM) of which only 0.42 complaints per 1,000 policyholders were upheld (APM).

Our administrators escalate all complaints to the in-house Operations team immediately for review and sign-off of the response. Where policyholders express dissatisfaction or make complaints, then we undertake a full root cause analysis.

The Board receives regular updates on customer service levels and satisfaction and all complaints are reported to our Customer and Conduct Committee, which is chaired by Terry Miller, an independent Non-Executive Director.

## Pension trustees

# Rothesay provides pension de-risking solutions to the trustees of over 190 pension schemes.

As noted earlier, during 2020, Rothesay assisted 12 pension schemes to de-risk their liabilities, resulting in new business premiums (APM) of £7bn. Most of this business was completed with all parties working remotely. We were particularly pleased that £0.8bn of the business written was with existing pension scheme clients – a strong endorsement of Rothesay.

Rothesay is a Technical Partner of PensionChair, a leading industry network for pension scheme Trustee Chairs. In this role, we provide expert insight to the PensionChair membership. We are also a premier sponsor of the Association of Member Nominated Trustees – a body that provides training and support to member-nominated trustees.

There are a number of phases to a bulk annuity transaction. Through a well-managed and collaborative implementation, data cleanse and transition process, the optimal member outcome can be achieved. We aim to deliver certainty to trustees and members whatever the operating environment by:

- Ensuring that Rothesay is strongly capitalised to give confidence in our ability to provide long-term pension security for our policyholders;
- Performing detailed due diligence up front so that all parties are clear as to the risks that are being insured or bought out;
- Working with the trustees and their administrators to make the data cleaning process and conversion from buy-in to buy-out as seamless as possible; and
- Ensuring operational resilience in order to provide excellent customer service into the future.

Rothesay undertakes a regular survey of trustees. Individual trustees are asked a series of questions by an independent facilitator who then produces a report summarising the results. This report and Rothesay 's planned actions in response to the feedback are discussed at the Board.

In addition, Directors and management of Rothesay have ad hoc meetings with pension scheme trustees throughout the year.

"Rothesay came in armed with all the answers to our questions. It was clear that they knew all about administration. This was a huge comfort to us as we prioritise admin and member experience alongside benefit security."

**A pension trustee**

"I would have no hesitation in recommending Rothesay to anyone. They are thoroughly professional and keen to deliver, a good combination."

**A pension trustee**

# Our people

## Our people are the defining factor in our success.

Average employee turnover:

**4.3%**

(2019: 7.4%)

# Our immediate priority in response to COVID-19 was the health and safety of our people and their families.

**COVID-19**
Almost all of our employees transitioned to remote working early, giving time to ensure that everyone was well equipped for working from home.

As well as providing technology and equipment for home working, we have been very focused on the welfare of our people. Managers are checking in regularly with their teams and staff are being surveyed twice a week to identify if individuals are unwell or need additional support from the business. To encourage our people to take holiday during lockdown, we gave people an extra day's holiday for each day of holiday taken (up to a maximum of five).

We are being cautious in terms of the timing and transition back to the office. When the office did re-open for some staff, we put in place measures such as one-way systems, increased frequency of cleaning, touch-free automated doors, and two metre distancing to minimise the risk of COVID-19 transmission in the office. We have also been offering COVID-19 testing facilities to all employees both at home and in the office and encourage their regular use.

We will continue to monitor and follow government advice regarding the transition back to the office and our primary focus will continue to be the health and welfare of our people.

### Building the team that builds our business
To meet the demands of a growing business, we have continued to recruit despite the impact of COVID-19, with headcount increasing from 252 at the end of 2019 to 305 at the end of 2020. Hiring in 2020 has been focused on the following areas:

- **Investment** – to help us to deliver Rothesay's long-term investment strategy. This includes further growth of our New York office.
- **Finance** – to develop and maintain our internal model for capital management and to maintain robust controls as the balance sheet grows.
- **Technology** – to ensure Rothesay is at the leading edge of automation.
- **Risk, Compliance and Internal Audit** – to ensure robust second and third lines of defence.

Year-on-year increases in graduate numbers have also strengthened our capability pipeline for the future. We wanted to do the right thing by our new graduates so we took the decision not to delay their start dates despite the challenges of remote on-boarding. We have then worked hard to ensure that they have received appropriate training and support.

As we grow we are determined to maintain and build on the values and culture that got us here. We are committed to maintaining the highest standards of integrity, transparency and accountability. That commitment is reflected in our Compliance Manual and training. But in practice it is brought to life in our culture, our behaviours and our everyday decisions and interactions.

### Investing in our people
In 2020 we delivered a comprehensive learning and development agenda, designed to support an environment where our employees can thrive and fulfil their career ambitions. Our people are encouraged to own their career development and select their learning activities from the programmes which have been tailored to Rothesay's requirements.

We continue to invest in partnerships with suppliers to deliver training and learning platforms that augment the technical skills and soft skills of our people. Much of this training has been delivered remotely during 2020 as a result of COVID-19.

All employees have access to Mind Tools, providing digital, on-demand career and management learning solutions. We are also a member of Cityparents, an award-winning network providing quality content aimed at all City professionals.

Rothesay supports employees in gaining a range of professional qualifications and we also sponsor a number of apprentices. We continue to invest in the health and wellbeing of our employees and their families. In the 2020 employee engagement survey, 92% of our employees agreed or strongly agreed with the statement "Rothesay actively looks after the wellbeing of its employees". Health benefits include private healthcare for employees and their families, subsidised gym memberships, subsidised health assessments, free flu jabs and comprehensive online resources.

## Engaging our employees

In 2020, we continued to focus on strengthening our internal communications capability and have completely redeveloped our Company intranet. This has assisted in helping new hires become part of the team despite the impact of home working. We have ensured that there is regular communication from all parts of the business.

Our offices at The Post Building mean that under normal working conditions all our UK-based employees are working together on one floor. This facilitates the absence of functional silos – an integral part of the Rothesay culture. The Chairman and other members of the Board have frequent, informal interaction with Rothesay's employees.

In 2020 we repeated the employee engagement survey using an external consultancy in order that we can use benchmarking data to better interpret the results. We received an outstanding response rate of 95% (2019: 81%) with 92% of employees saying that they were proud to work at Rothesay (2019: 87%) and the results leading to an engagement score of 81% (2019: 69%).

The survey design was reviewed by the Chairman and senior management and the results were discussed at the Board. The Board has then assisted in determining people-related priorities for 2021.

## Gender pay gap

The table below provides a summary of our gender pay gap data:

| | 2020 Mean | 2020 Median |
|---|---|---|
| Hourly pay | **29%** | **32%** |
| Bonus | **50%** | **56%** |

In common with many other organisations, our gender pay gap arises as a result of having a higher number of men in senior roles than women. For a more detailed discussion of this topic and information on the actions we are taking to address it, please see our separate Gender Pay Gap Report when it is published.

## Diversity and inclusion

During 2020, we have seen increased public debate in the US and UK on the subjects of race and inclusivity. We recognise that prejudice and discrimination are still present in society today and that they have a real, damaging impact on the lives of many of our employees and customers. Racism and other forms of discrimination have no place at Rothesay.

Rothesay is committed to promoting equality and diversity, and a culture that actively values difference. Our policies are designed to ensure that our people are not to be disadvantaged in any way as a result of their age, race, gender, disability, religion or belief, sexual orientation, gender re-assignment, marriage and civil partnership or pregnancy and maternity. We recognise that people from different backgrounds and experiences can bring valuable insights to the workplace and enhance the way we work.

In the 2020 employee engagement survey, 86% of our employees agreed or strongly agreed with the statement "My co-workers respect my thoughts and feelings" with only 4% disagreeing.

During 2020 all our people received training on what it means to be an inclusive company. We continue to look at ways of identifying a more diverse range of talent for the long term and during 2020 we participated in #100BlackInterns and have partnered with SEO London, an organisation which prepares talented students from ethnic minority or low socioeconomic backgrounds for career success.

We offer training and support to new parents and their managers and have recently started an initiative in which all employees taking extended parental leave are offered one-to-one coaching to support their return to work.

## Our environment

# We fully support the Paris Climate Accord and the path towards carbon-neutrality.

Rothesay exists to safeguard the future of hundreds of thousands of policyholders, providing them with real financial security over the long-term. Fundamental to this is the management of a wide range of uncertain risks over a time horizon measured in decades. We therefore believe that acting to manage and mitigate potential financial and non-financial risks resulting from climate change is critical – not only to protect our policyholders, but also to protect societies and economies at large across the globe.

We fully support the Paris climate Accord and the path towards carbon-neutrality. As a significant investor in the UK and other developed economies, we believe it is our responsibility to be an advocate for climate change management with our counterparties, by encouraging them to define and deliver on tangible emissions targets. We are also committed to providing increasingly clear and complete reporting on the climate change risks within our portfolio, to provide transparency for our investors and policyholders.

The table on the next page summarises our current work on climate change risk management, aligned with the TCFD recommendations on climate-related disclosures. In 2021 we plan to publish Rothesay's inaugural ESG report, which will set out the initiatives and actions discussed on the next page in further detail.

# Our environment
**continued**

| Governance | Strategy | Risk management | Metrics and targets |
|---|---|---|---|
| Climate-related risks are incorporated in Rothesay's risk management framework, which is overseen by the BRC. Climate change and ESG risk is a standing agenda item at each BRC meeting, and ESG risk is also discussed at the Board.<br><br>Rothesay is in the process of developing its 'Responsible Investing' policy, to formalise and embed the investment and risk management practices with respect to ESG, and expects to implement this in the first half of 2021.<br><br>Rothesay's in-house team is responsible for the selection and management of all of the Group's assets. The team considers climate-related risk and metrics as part of the investment process and is required to document this as part of committee approval papers for new investments.<br><br>The CRO and Head of Asset and Liability Management are jointly responsible for the management of climate-related financial risks. | Given Rothesay's focus on annuity business, we believe that climate-related risks and opportunities mainly impact our investment strategy and that our business model is compatible with proactive sustainable investing.<br><br>The long-term nature of the Group's investments means that Rothesay is exposed to financial risks from climate change, and these are examined as part of the investment process to ensure that climate change will not impact the long-term pension security of our policyholders.<br><br>Rothesay's dynamic investment strategy means that we are well placed to take advantage of any climate-related investment opportunities.<br><br>Our climate change management strategy is underpinned by overall targets, defined in line with the science based targets initiative (see 'Metrics and targets'). Rothesay aspires to be a strong advocate for climate change management via its business and investment activities. We are a supporter of TCFD, a signatory to the UN Principles for Responsible Investing, and an early adopter of the Sustainability Reporting Standard for Social Housing. | Climate-related risks are incorporated in Rothesay's risk management framework (as described in the risk management section), including the annual ORSA process. The in-house investment team assess climate-related risk (physical and transitional) as part of the transaction approval process and this assessment is reviewed and challenged by the second line risk function.<br><br>We have assessed our investment portfolio to identify the sectors and asset types with the greatest exposure to climate risk, and are in the process of conducting counterparty-level reviews for the highest priority sectors. These reviews are used to feed into decisions around investment/divestment, counterparty engagement, and risk limit calibration.<br><br>In addition, for our property-backed assets we have conducted studies focusing on assessing vulnerability to specific climate change linked natural disasters, for example flood risk for our UK and Dutch mortgage portfolios.<br><br>Building on the work conducted for the 2019 PRA insurance stress testing exercise climate change scenarios, Rothesay is developing its own climate change stress testing capabilities, engaging with a range of third party providers. | Climate-related financial risks are summarised in the principal risks and uncertainties facing the Group (see page 43). Rothesay has defined two key business and portfolio-wide ambitions relating to climate change management:<br>• Rothesay is committed to supporting a low carbon economy in which the UK achieves carbon neutrality by 2050.<br>• Rothesay will construct its investment portfolio with the aim of aligning with the Paris Climate Accord of 2015 whose objective is limiting warming beyond preindustrial levels to 1.5 degrees Celsius.<br><br>In line with the Streamlined Energy and Carbon Reporting (SECR) requirement, the Group has disclosed its Scope 1 and 2 emissions for 2020 and has also summarised the various energy efficiency initiatives that have been undertaken throughout 2020 on the next page.<br><br>Rothesay is in the process of producing its inaugural ESG report, which will provide further detail on the different metrics Rothesay uses to assess climate risk and monitor progress against targets, including portfolio emissions, counterparty level deep-dives within different sectors, and portfolio temperature alignment.<br><br>As of December 2020, Rothesay is a signatory to the UN Principles for Responsible Investing (UN PRI), and as such will provide full disclosure of mandatory requirements under this framework over time. |

## Streamlined Energy and Carbon Reporting

The table below summarises the Group's energy consumption, $CO_2$ emissions, and emissions intensity metrics for 2020. The scope of this reporting covers all of Rothesay's UK entities, reflecting Scope 1 and 2 emissions, as well as selected elements of Scope 3. Rothesay is in the process of developing and refining its approach to assessing its Scope 3 emissions to include emissions produced by counterparties in which Rothesay holds investments. Further details can be found in Rothesay's separate ESG report for 2020 when available later in the year.

This reporting has been compiled in line with the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard (Revised 2014), utilising the emission factors from the UK Government's GHG conversion factors for Company Reporting in 2020. Rothesay has performed the underlying calculations internally, and Jones Lang Lasalle was engaged by Rothesay to provide an external and independent high-level data check and methodology review.

As noted above, the reporting below does not include Rothesay's US entity, Rothesay Asset Management US. However, Rothesay currently has only seven employees in the US and we consider the reporting below to materially capture the total energy consumption and emissions of the Group.

### Rothesay UK greenhouse gas emissions and energy use data for 2020

| | 2020 |
|---|---|
| **Energy consumption (kWh)** | **1,197,093** |
| **Total $CO_2$e emissions (in tonnes)** | **263.4** |
| Scope 1 $CO_2$e emissions (tonnes)[1] | **58.6** |
| Scope 2 $CO_2$e emissions (tonnes)[2] | **203.4** |
| Scope 3 $CO_2$e emissions (tonnes)[3] | **1.4** |
| **Carbon dioxide emissions intensity** | |
| **Emissions intensity (Total $CO_2$e tonnes per FTE)** | **0.86** |

1 Scope 1 covers $CO_2$ emissions occurring from sources owned or controlled by Rothesay. For 2020, these emissions were estimated using the Area Method, as detailed by The Climate Registry's General Reporting Protocol v3.0.
2 Scope 2 covers $CO_2$ emissions from the generation of electricity purchased by Rothesay. These are primarily calculated using meter readings, with the Area Method used to estimate Rothesay's contribution for communal office areas.
3 Scope 3 covers $CO_2$ emissions occurring from business travel in rental or employee-owned vehicles where Rothesay are responsible for purchasing the fuel. These are estimated from total mileage by using the 'Average car' and 'Petrol' conversion factor from the UK Government's GHG conversion factors for Company Reporting in 2020.

It should be noted that Rothesay's emissions in 2020 will have been impacted by COVID-19 and the associated restrictions on employees working from the office and business travel. However, regardless, Rothesay expects that emission intensity would have reduced in 2020 as a result of the relocation of all UK-based staff to a newly redeveloped site, The Post Building. The Post Building has been developed to high standards with respect to energy efficiency – it has a B EPC rating and was provided with a Gold rating from LEED early in 2020.

Rothesay remains committed to continuing to take steps to minimise our emissions intensity, and supporting our employees to do the same. Initiatives Rothesay has introduced this year to reduce Scope 1 and 2 emissions of the Company include implementing secure printing, which has contributed to a reduction in the number of pages printed in 2020.

Rothesay has also taken steps in 2020 to support employees in reducing their own emissions – for example, at the new UK office over 400 secure cycling spaces are available. Rothesay supports the cycle-to-work scheme and, in November 2020, Rothesay launched a new employee benefit offering zero-emission electric car leasing by way of a salary sacrifice scheme (in line with the UK Government's scheme for Ultra Low Emission Vehicles).

## Our community

# Investing in projects that benefit the UK

£30.9bn
Invested in the UK economy

2019: £30.5bn **+1%**

### Investment in the UK economy
Rothesay has invested £30.9bn (2019: £30.5bn) in helping fund projects that benefit the UK, such as transport, infrastructure, education and social housing.

In addition, by providing funding to back equity release mortgages, Rothesay is helping older people access the equity in their houses, without the need for them to move. Mortgages are written with a no negative equity guarantee which means that borrowers don't have to worry about the liability growing above the value of the house.

Rothesay did not furlough any of our employees or take advantage of any other COVID-19 government support.

### Taxation
Rothesay's tax strategy is designed to ensure compliance with the tax laws of those countries in which Rothesay operates (primarily the UK). Any tax planning undertaken has commercial and economic substance and has regard to Rothesay's corporate responsibilities and brand and the potential impact on shareholders, policyholders and other stakeholders. We do not undertake planning that is contrived or artificial. Rothesay has zero tolerance for tax evasion of any kind.

Rothesay makes a significant tax contribution in the UK, with £458m remitted to UK tax authorities in 2020 (2019: £223m). Rothesay has an effective corporation tax rate of 18.8% during 2020 (2019: 19.3%). Other taxes include property taxes, employer payroll taxes and irrecoverable indirect taxes.

| Taxes paid | **2020 £m** | 2019 £m |
|---|---|---|
| Corporation tax | **294** | 59 |
| Other taxes | **13** | 12 |
| Taxes collected | **151** | 152 |
| **Total remitted** | **458** | 223 |

## Giving back

In 2020 we contributed over £4.1m to charitable causes.

During 2019 Rothesay established the Rothesay Foundation (previously known as the Rothesay Life Foundation), to support charities that seek to improve the quality of life for older people, helping them to live their lives in a happy, safe and fulfilling way. In 2020 Rothesay has provided £2.5m to the Foundation and grants have been provided to a number of charities, including:

- **Goodgym** – a community of runners that combine getting fit with doing good. They stop off on their runs to do physical tasks for community organisations and to support isolated older people with social visits and one-off tasks they can't do on their own.
- **SafeLives** – a charity dedicated to ending domestic abuse.
- **Food Train** – a charity dedicated to making daily life easier for older people, providing vital services to those who are no longer able to manage independently, through age, ill health, frailty or disability. Food Train makes hundreds of grocery deliveries every week, ensuring those most in need have access to fresh groceries.

In 2020 we also made a significant contribution to the COVID-19 Support Fund, the UK insurance industry's initiative to help some of the people hardest hit by the COVID-19 crisis. The fund has the aim of providing immediate relief to charities affected by COVID-19, as well as a longer-term programme of support for people, communities and issues where there is the greatest need. Rothesay's CFO was a member of the COVID-19 Support Fund Committee which oversaw distribution of the funds raised to:

- Community-based charities that were under unprecedented strain from the impact of COVID-19;
- Charities supporting the most vulnerable – in particular, families and children living in poverty and older people in isolation; and
- Initiatives to promote wellbeing and mental health across society.

We continue to partner with Age UK, the UK's largest charity dedicated to helping everyone make the most of later life. The charity helps more than six million people every year, providing companionship, advice and support for older people who need it most. We sponsor Age UK's Avoiding Scams booklet which provides useful information on how to protect people from scams and we also continue to sponsor and issue their Bereavement Guide.

Rothesay supports Tax Help for Older People, a charity service providing free, independent and expert help and advice for older people on lower incomes who cannot afford to pay for professional tax advice.

On an annual basis we choose an employee-nominated charity of the year. In 2020 our charity of the year was MIND, an organisation dedicated to ensuring that everyone experiencing a mental health problem gets support and respect.

We are a corporate partner of the British Museum and support a number of other charities. We encourage our employees to support charities personal to them through our matched giving policy, which gives everyone an annual matched allowance of £1,000. In response to COVID-19, we introduced an additional 3-for-1 matching for donations of up to £300. We are proud that so many people have engaged in fundraising and social events designed to give back to the community.

# Our strategic business partners

## Outsourcing model
As noted previously, we follow a strategic outsourcing model for the provision of administration services and middle office functions. Key to delivery of excellent customer service is our close working relationship with our third party administrators, Willis Towers Watson, Mercer and Capita Employee Solutions.

COVID-19 meant that we have been in close dialogue with each of our administration partners about the operational challenges posed by working from home and their capacity and appetite for taking on new business.

We also work closely with each of the equity release mortgage servicers.

The Board receives regular reporting on the performance of all of Rothesay's outsourcing partners.

## Other suppliers
### *Oversight*
The Third Party Oversight Committee, a sub-committee of the Working Level Risk Committee, is responsible for the oversight of third party relationships. Its objective is to ensure that the legal, regulatory, information security, reputational, commercial, operational and financial risks associated with third party relationships are appropriately managed.

### *Prompt Payment Code*
Rothesay is a member of the Prompt Payment Code. Rothesay's finance team aims to pay suppliers promptly, with the average time taken to pay invoices in 2020 being 14 days (2019: 13 days) and 93% being paid within 30 days (2019: 95%).

Prompt Payment Code

### *Modern slavery*
As required by the Modern Slavery Act 2015, on 25 September 2020 a statement was published on Rothesay's website describing the steps taken by Rothesay to ensure that slavery and human trafficking is not taking place in any part of our business or in any of our supply chains.

The statement also notes that we expect our suppliers to ensure fair employment practices. For example, we require our cleaning suppliers to pay their personnel, who work at our premises, a salary which is equivalent to (at least) the London Living Wage.

## Reinsurers
As previously noted, we have reinsured the largest new business written in 2020, as well as reinsuring some of our existing liabilities. This has led to us entering into two reinsurance contracts with existing counterparties and four contracts with a new reinsurance counterparty. We now have reinsurance coverage (APM) of 87% (2019: 78%).

The long-term nature of these reinsurance agreements means that developing a strong working relationship with our reinsurance counterparts is important and we look to provide our reinsurance counterparties with the same quick and efficient execution that we target for client transactions. During 2020 we have continued to develop a new internal reinsurance administration system which will facilitate this.

# Our investors

## Shareholders

In November, two of our existing shareholders, GIC and MassMutual, substantially increased their investment in Rothesay by acquiring Blackstone's 35% shareholding. This is a strong expression of confidence in Rothesay and provides the business with exceptional long-term support from two of the world's leading institutional investors and a stable platform for growth in the future.

Following the transaction, GIC and MassMutual each hold 49% of Rothesay Limited with the remainder being held by the Employee Benefit Trust, Directors, management and staff. The implications of the change of ownership on governance, on Rothesay's long-term strategy and on our people was considered by the Board and is discussed in the Governance report.

Each of the shareholders has the right to appoint two Non-Executive Directors, with each having appointed one to date. The shareholder Directors attend Board and other Board Committee meetings, providing an important contribution to the effectiveness of the Board and to the overall performance of Rothesay. The shareholders receive regular management information and their teams also interact directly with management. Going forward, it is also anticipated that members of the teams will attend relevant parts of Board and other Board Committee meetings as observers.

The shareholders support Rothesay in other ways, for example assisting in the sourcing and evaluation of investments, providing debt financing and providing longevity reinsurance. Prior to Blackstone's sale of its shareholding in Rothesay, Blackstone also provided Rothesay with opportunities to invest in debt financing of some of Blackstone's other ventures.

For further information on related parties transactions see note I.3.

## Bondholders

On 22 May 2020, we issued a further £100m of Tier 3 bonds with the same maturity and coupon date as the Tier 3 bonds issued in 2019. The proceeds were used to repay the floating rate Tier 2 loan issued on 21 December 2012.

Senior management meet with debt investors on a regular basis and make presentations to groups of investors and analysts, albeit that the restrictions of COVID-19 meant that in 2020 there was less face-to-face interaction than normal.

Rothesay also has a regular dialogue with it's relationship banks.

## Credit rating agencies

Rothesay's life company has credit ratings from Moody's Investors Service and Fitch Ratings and Rothesay's outstanding public bonds have all been rated by Fitch Ratings. Rothesay meets with the ratings agencies at least once per year and updates them on material events.

Rating of RLP:

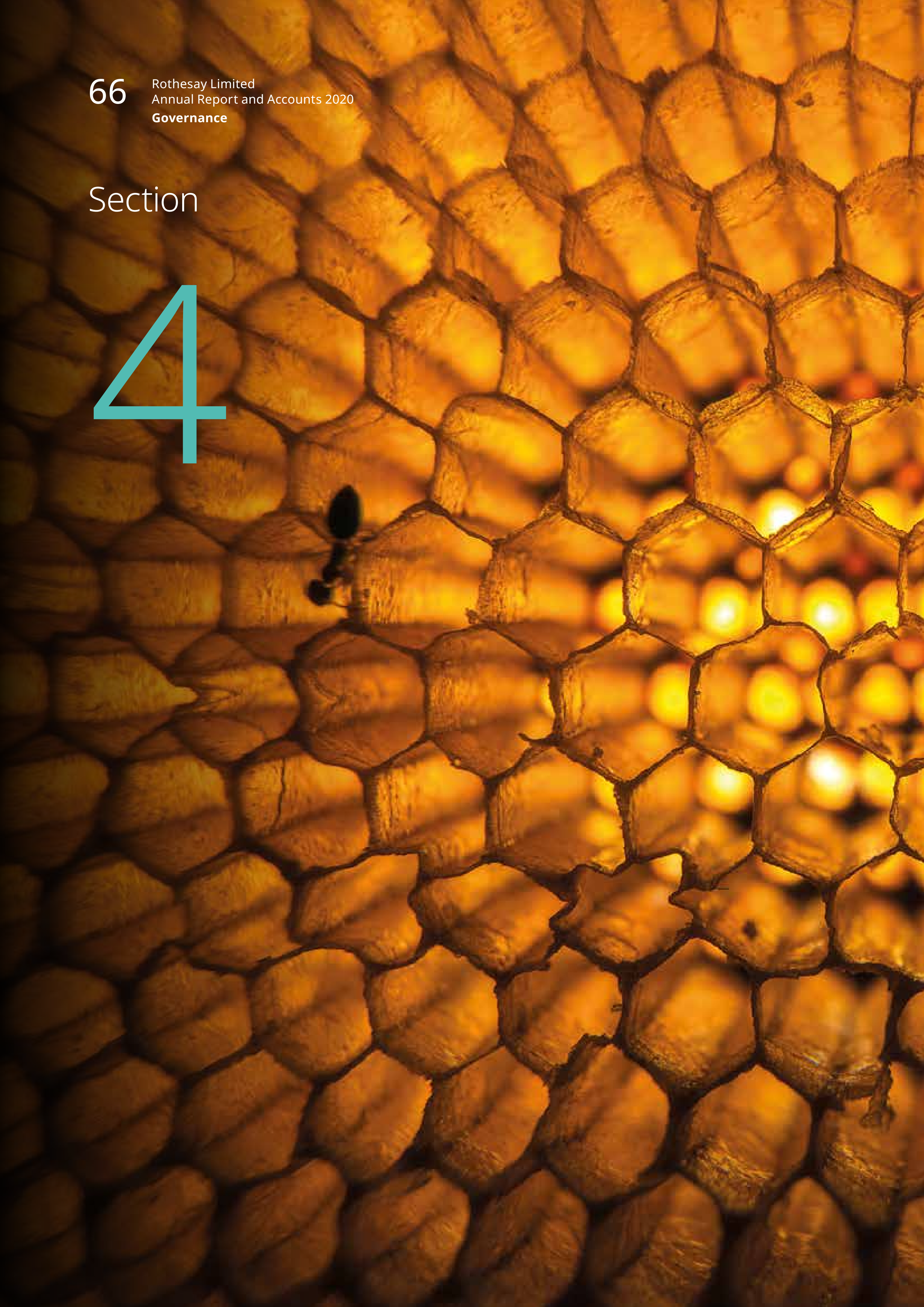
A3

Moody's Investor service

A+

by Fitch Ratings

# Section 4



# Governance

The Board, together with management, is responsible for ensuring the security of our policyholders' pensions as well as generating and delivering sustainable shareholder value through the management of Rothesay's business.

# Chairman’s introduction

**Naguib Kheraj**
Non-Executive Chairman

## Robust corporate governance

Rothesay’s governance structure means that decisions can be made quickly and efficiently whilst ensuring that there is robust oversight.

### The Board

A strong Board with an effective committee structure facilitates the governance framework of Rothesay. Our Board remains highly engaged; the continuing development of the full internal model, the COVID-19 crisis, the volume of new business and the change in ownership of Rothesay necessitated a number of additional Board meetings during the year and the level of attendance and contributions was very high. In addition, many issues were dealt with via email correspondence enabling matters to be progressed efficiently. Following the start of the Covid pandemic, meetings switched to take place principally by video-conference.

### Shareholders

In November 2020, GIC and MassMutual acquired Blackstone’s 35% shareholding in Rothesay Limited. This represents a strong expression of confidence in Rothesay and provides the business with exceptional long-term support from two of the world’s leading institutional investors and a stable platform for growth in the future.

Following the transaction, GIC and MassMutual each hold 49% of Rothesay Limited with the remainder being held by the Employee Benefit Trust, management and staff.

Each of the shareholders has the right to appoint two Non-Executive Directors with each having appointed one to date. The shareholder Directors provide an important contribution to the Board and the overall performance of Rothesay.

The Shareholder Agreement sets out a number of reserved matters, including:

- Changes to the rights of shareholders.
- Issuance of new equity or debt.
- Material changes to the business strategy of Rothesay.
- Material acquisitions or disposals.

### Board composition

Following the change of ownership of Rothesay, on 1 December 2020, Qasim Abbas stepped down from the Board. Simon Morris has also announced his intention to stand down from the Board with effect from 13 February 2021.

In order to ensure that the Board will continue to have a majority of independent Non-Executive Directors when GIC and MassMutual appoint their second shareholder Directors, new independent

Non-Executive Directors have been appointed. These appointments broaden the knowledge and experience of the Board and improve its gender balance. Jane Hanson was appointed to the Board on 1 January 2021, Ed Giera on 25 January 2021 and Heather Jackson is expected to be appointed to the Board in March.

During 2020 the Board renewed the appointments of Ray King, Terry Miller, Stan Beckers and, after satisfying itself that he remains appropriately independent, Charles Pickup to the Board. The Committee also approved the re-appointment of Naguib Kheraj as Rothesay's Chairman.

### How the Board operates

The Board is led by the Chairman, Naguib Kheraj. Naguib was appointed to the Board on 1 October 2014 and became Chairman on 18 December 2017.

Day-to-day management of Rothesay is led by Addy Loudiadis, the Chief Executive Officer, and Tom Pearce, the Managing Director.

The Board has responsibilities to shareholders, policyholders, the regulators, employees and other stakeholders for the overall performance of Rothesay. More information on stakeholder engagement can be found on page 48. The Board's role is to provide oversight and direction to the senior management team and to ensure that there is an appropriate risk and control framework for Rothesay.

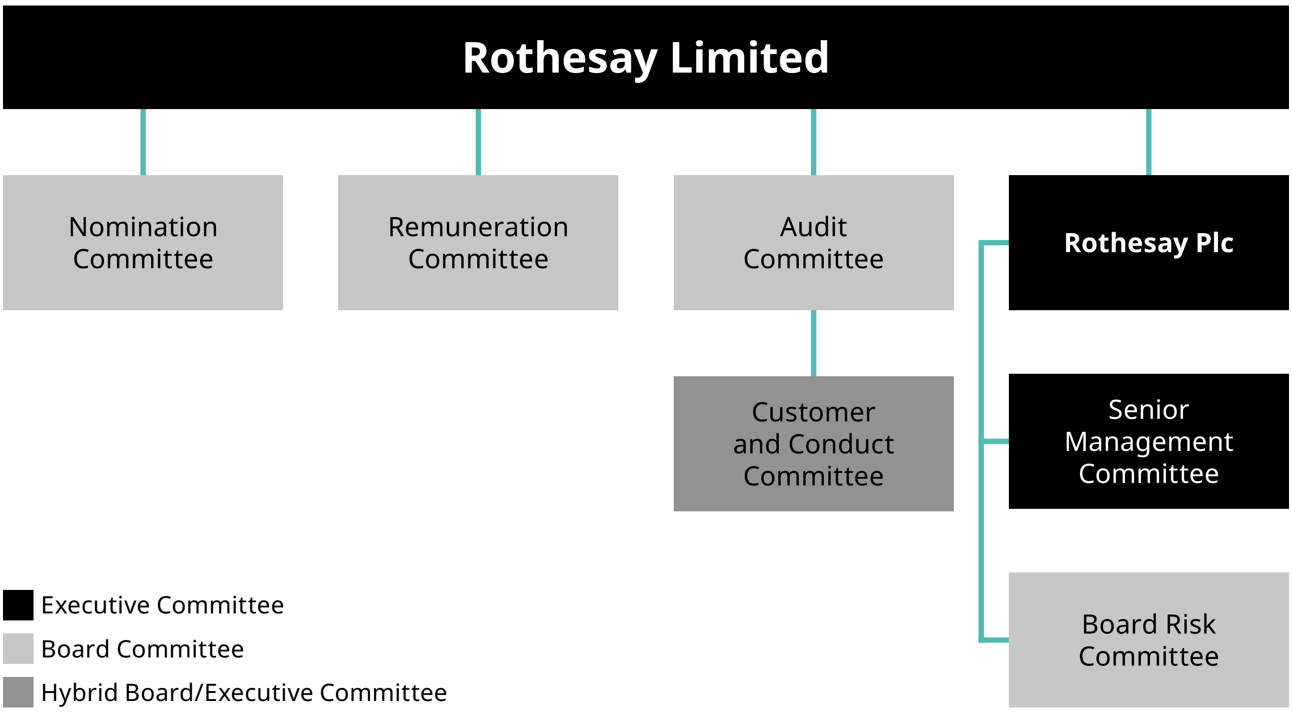
The Board has a schedule of matters reserved for its consideration and approval, including:

- Strategy and business plans.
- Material new investments and new insurance transactions.
- Acquisitions and disposals.
- The constitution of Board Committees.
- Capital management policy including dividend policy.
- Other key Rothesay policies.

The Board is supported by the Audit Committee, the Board Risk Committee, the Remuneration Committee and the Nomination Committee. Terms of reference for these Committees can be found at www.rothesay.com. In the following sections of the governance report, the chairs of these Committees provide a report on activity in the year. The report from the chair of the Audit Committee also includes commentary on the activity of the Customer and Conduct Committee.

### How the Board spent its time in 2020

The Board met formally seven times during 2020, in addition to meeting on a number of other occasions on an ad hoc basis and dealing with a number of matters via email correspondence.



# Chairman’s introduction
**continued**

In the first half of the year, a lot of time was spent discussing the impact of COVID-19, the steps being taken to ensure the welfare of Rothesay’s people and to ensure that excellent customer service was maintained. The Board also discussed the impact of COVID-19 on Rothesay’s investment portfolio and the actions being taken to protect Rothesay’s capital and liquidity position.

The Board agenda is set by the Chairman and generally includes:

- An update from the CEO on business performance.
- Reports from Committee chairs.
- An update on Rothesay’s financial performance.
- Updates from the risk and compliance functions.
- Discussion on material new investments and liability transactions.
- Discussion of key initiatives such as development of the internal model, climate change work, and the development of Rothesay’s IT platform.
- Board legal and governance update.

The Board is focussed on ensuring that the growth of the business is appropriately controlled and received updates through the year on the steps being taken to strengthen control and oversight functions.

The COVID-19 crisis meant that the Board was unable to hold a strategy off-site event during the year so strategic business planning was covered in an extended meeting as part of the formal Board meeting schedule.

The Board spent time in formal meetings as well as separate sessions discussing the development of Rothesay’s full internal model. The Board also spent time reviewing progress and future plans in relation to the development of Rothesay’s IT platform.

The Board spent time reviewing both internal and external perceptions of Rothesay as part of a branding refresh initiative.

The Board reviewed the results of the 2020 employee engagement survey and discussed management’s proposed response as well as the progress made by management in response to the 2019 survey.

The Board increased its focus on risks and initiatives in relation to climate change. This resulted in a commitment to aligning our investment portfolio with the goal of the Paris Accord to limit global warming to 1.5°C above pre-industrial levels and to supporting a low carbon economy in which the UK achieves carbon neutrality by 2050. The Board also approved Rothesay becoming both a signatory to the UN Principles for Responsible Investing and a supporter of the Task Force on Climate-Related Financial Disclosures.

Towards the end of the year, a considerable amount of time was spent considering the implications of the sale by Blackstone of its stake in Rothesay. As noted above, the change provides the business with an exceptional long-term stable platform for growth but the change also impacted governance and remuneration arrangements (see the Remuneration and Nomination Committee reports below).

### Board performance and effectiveness

The Board recognises that the continuous development of Directors is important to the Board’s performance and effectiveness.

During the year, the following development activities took place:

- One-to-one briefing sessions for independent Non-Executive Directors on the annual report and accounts.
- Training sessions on Rothesay’s approach to managing cyber risk, the Senior Managers & Certification Regime, the Compliance Manual and IFRS 17.

The Board also considered the fitness and propriety of senior management and Directors.

Rather than undertaking a formal, externally facilitated review of Board effectiveness during 2020, the Chairman led an internal review of effectiveness. This involved a questionnaire being completed by all Directors, the results of which were then shared and discussed with the Board. The Chairman also held one to one sessions with Directors to solicit their views and provide them with feedback.

These reviews led to a small number of recommendations which will be addressed over 2021.

### Corporate governance highlights

- Review and approval of the changes required as a result of the acquisition of Blackstone’s shares by GIC and MassMutual.
- Review and approval of the Group’s commitments in relation to climate change.
- Approval of the larger new bulk annuity and longevity reinsurance contracts.
- Approval of the issuance of Tier 3 bonds by RLP and of the repayment of the £100m floating rate bond.
- Review and approval of the new Rothesay branding.
- Approval of charitable donations to the Rothesay Foundation and the COVID-19 Support Fund.
- Review of the results of the 2020 employee engagement survey and discussion of management’s planned response.

# The Wates Corporate Governance Principles

The Board has decided to apply the Wates Corporate Governance Principles for Large Private Companies (the Wates Principles). Information can be found on our approach to compliance in the strategic report and in this governance report.

| Principle | Where further information can be found |
|---|---|
| **1: Purpose and Leadership** – An effective board develops and promotes the purpose of a company and ensures that its values, strategy and culture align with that purpose. | Rothesay's purpose is to provide pension security for our policyholders and value to our shareholders over the long term.<br><br>Rothesay's strategic objectives are discussed on page 24.<br><br>More information can be found on Rothesay's culture on page 57. |
| **2: Board Composition** – Effective board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual directors having sufficient capacity to make a valuable contribution. The size of a board should be guided by the scale and complexity of the company. | Board effectiveness is described above under "Board performance and effectiveness".<br><br>Board composition is described on page 68.<br><br>The Nomination Committee is responsible for ensuring that Rothesay's Board and management team have the appropriate mix of expertise and experience. See page 84. |
| **3: Board Responsibilities** – The board and individual Directors should have a clear understanding of their accountability and responsibilities. The board's policies and procedures should support effective decision-making and independent challenge. | Board governance is described on page 68.<br><br>The Audit Committee is responsible for overseeing the systems and controls that ensure the reliability of information provided to the Board. See page 74. |
| **4: Opportunity and Risk** – A board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value and establishing oversight for the identification and mitigation of risks. | The Board has overall responsibility for identifying opportunities to create and preserve value and this is discussed above under "How the Board spent its time in 2020".<br><br>The BRC is responsible for the operation of Rothesay's risk management framework. The framework is described on page 37 and more can be found on the BRC on page 79.<br><br>Risks and opportunities are also highlighted as part of the description of strategic objectives on page 24. |
| **5: Remuneration** – A board should promote executive remuneration structures aligned to the long-term sustainable success of a company, taking into account pay and conditions elsewhere in the company. | The Remuneration Committee is responsible for ensuring that Rothesay's remuneration policy appropriately rewards and incentivises our people. See page 81. |
| **6: Stakeholder Relationships and Engagement** – Directors should foster effective stakeholder relationships aligned to the company's purpose. The board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions. | Rothesay's purpose is to provide pension security for our policyholders and value to our shareholders over the long term. Rothesay has responsibility to a number of other stakeholders, including our suppliers, our people, our community, the environment and our bondholders. Further information on stakeholder engagement and examples of how we take their interests into account can be found on pages 46 to 65. |

# Board of Directors

### NAGUIB KHERAJ

INDEPENDENT NON-EXECUTIVE DIRECTOR AND CHAIRMAN

Naguib Kheraj is a Senior Advisor to the Aga Khan Development Network and serves on various boards within that Network. Naguib is also Deputy Chairman of Standard Chartered and a member of the Finance Committee of the University of Cambridge. He previously served on the Investment Committee of Wellcome Trust, the Finance Committee of Oxford University Press and the Board of NHS England. In his executive career, Naguib held various leadership positions at Barclays including serving as Group Finance Director and was also CEO of JP Morgan Cazenove

### ANTIGONE (ADDY) LOUDIADIS

CHIEF EXECUTIVE OFFICER

Addy Loudiadis is Rothesay's founder and Chief Executive Officer. Addy established Rothesay in 2007 as a business purpose-built to protect pensions. Addy was previously a partner of Goldman Sachs and served as the co-head of the Investment Banking Division in Europe. Before moving to investment banking, she was head of European Fixed Income Sales at Goldman Sachs. Addy sits on the Board of the Association of British Insurers.

### THOMAS (TOM) PEARCE

MANAGING DIRECTOR

Tom Pearce is Managing Director and a co-founder of Rothesay, responsible for strategy and business development. Prior to the establishment of the Company in 2007, Tom was previously in the European Financing Group at Goldman Sachs, responsible for UK life insurance. Tom joined Goldman Sachs in 2000 in European Fixed Income.

### ANDREW STOKER

CHIEF FINANCIAL OFFICER

Andrew Stoker is the Chief Financial Officer of Rothesay following his appointment in 2014. At Rothesay, Andrew has responsibility for the finance, actuarial and HR functions. Andrew was previously a partner in EY's risk and actuarial practice and prior to that was Chief Actuary at Lucida plc.

Andrew has also held roles at PwC, Tillinghast (now Willis Towers Watson) and Legal & General. Andrew is an Associate Trustee of the Great Ormond Street Hospital Children's Charity.

### CONSTANT (STAN) BECKERS

INDEPENDENT NON-EXECUTIVE DIRECTOR

Stan Beckers retired from his role as Chief Executive Officer of NN Investment Partners B.V. in 2017, having previously been Co-Head of BlackRock Solutions at BlackRock Advisors (UK) Limited and, prior to that, had spent six years with Barclays Global Investors Ltd, most recently as Chief Investment Officer of Scientific Active Equity Europe. Stan started his career at BARRA (now MSCI BARRA) where, over a 20-year period, he established and managed its non-US operations. Stan is currently Chair of Nomura Asset Management UK. Stan was previously a non-executive director of Robeco N.V. and a non-executive director of Kas Bank N.V.

### EDWARD (ED) GIERA

INDEPENDENT NON-EXECUTIVE DIRECTOR

Ed Giera is a Non-Executive Director of Santander UK and the Renshaw Bay Real Estate Finance Fund. Ed is an experienced Non-Executive Director, having held a number of Board roles following his career with JP Morgan Securities. He provided corporate finance advisory and fiduciary services as Principal of EJ Giera LLC and was formerly a Non-Executive Director for NovaTech LLC, and the Life and Longevity Markets Association. Ed was also a director of Pension Corporation Group Ltd from 2012 to 2015, and Pension Insurance Corporation Holdings Ltd from 2008 to 2012.

### JANE HANSON

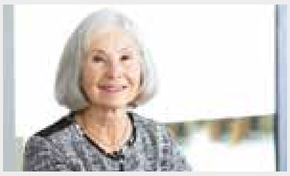
INDEPENDENT NON-EXECUTIVE DIRECTOR

Jane spent her early career at KPMG, latterly leading the Risk, Governance and Internal Audit advisory practice in the North of England. Jane held a number of Executive roles, including Director of Audit and Risk & Governance Director at Aviva plc. She is a Fellow of the Institute of Chartered Accountants in England and Wales and a magistrate. Jane is currently Chairman of The Reclaim Fund Ltd and Non-Executive Director of Direct Line Group plc, William Hill plc and Welsh Water. She is the Honorary Treasurer at the Disasters Emergency Committee and has previously held a number of other Non-Executive roles.

## RAYMOND (RAY) KING

INDEPENDENT NON-EXECUTIVE DIRECTOR

Ray King is a Non-Executive Director of Rothesay, having stepped down as Chairman in December 2017. Ray ended his executive career as Group CEO of Bupa, having previously been Finance Director. Earlier in his career he held senior management roles at Diageo/Guinness plc, Southern Water plc and ICI plc.



## THERESE (TERRY) MILLER

INDEPENDENT NON-EXECUTIVE DIRECTOR

Terry Miller is a non-executive director and the Senior Independent Director of Galliford Try Plc, a non-executive director of Goldman Sachs International Bank and Goldman Sachs International, and has been a director and trustee of the Invictus Games Foundation. She was previously General Counsel of the London Organising Committee of the Olympic and Paralympic Games (LOCOG) and a non-executive director of the British Olympic Association. Prior to her LOCOG appointment, she was a partner of Goldman Sachs, most recently as International General Counsel.

## SIMON MORRIS

INDEPENDENT NON-EXECUTIVE DIRECTOR

Simon Morris is the CEO of Boltons Place Capital Management, a private investment fund, and a non-executive director of Goldman Sachs Bank USA. He was previously a partner at Goldman Sachs, where he was Head of International Credit Trading and European Mortgage Trading. Simon served on the Securities Division Executive Committee, Firmwide Risk Committee and was co-head of Goldman Sachs International Risk Committee. Simon retired from Goldman Sachs in 2017 after 17 years. Prior to Goldman Sachs, Simon was at JP Morgan in Credit Trading.

## CHARLES PICKUP

INDEPENDENT NON-EXECUTIVE DIRECTOR

Charles Pickup was previously a partner in the Risk Consulting and Software division of Towers Watson (formerly Tillinghast) and acted as Actuarial Function Holder for Lucida plc, Countrywide and BlackRock. Prior to this, Charles worked at Commercial Union and Prudential Bache Securities specialising in UK life insurance.

## WILLIAM (BILL) ROBERTSON

INDEPENDENT NON-EXECUTIVE DIRECTOR

Bill Robertson was previously the Global Life Chief Risk Officer and Global Life Chief Actuary for Zurich Financial Services and also held various senior positions at Aegon. Prior to this, Bill was a partner at Hymans Robertson and Head of Actuarial at Scottish Amicable.

## M. TIMOTHY (TIM) CORBETT

NON-EXECUTIVE DIRECTOR

Tim Corbett is Chief Investment Officer of Massachusetts Mutual Life Insurance Company. Tim is responsible for MassMutual's overall investment strategy and has oversight of the company's General Investment Account. Prior to joining MassMutual in May 2011, Tim had been Chief Investment Officer and Head of Pension Fund Management with the State of Connecticut Treasurer's Officer since 2009.

## ROBIN JARRATT

NON-EXECUTIVE DIRECTOR

Robin Jarratt is Head of the Global Private Credit group at GIC. Robin has responsibility for all private credit investment by the firm in the US, Europe and Asia. Robin is a member of GIC Private Equity's Management and Investment Committees.

# Audit Committee report

**Bill Robertson**
Chairman of the Audit Committee

The Audit Committee plays a key role in monitoring the robustness of Rothesay's systems and controls.

| Committee membership |
|---|
| Bill Robertson (Chair) |
| Ed Giera |
| Jane Hanson |
| Ray King |
| Terry Miller |
| Charles Pickup |

**I am pleased to present the Audit Committee's report for the year ended 31 December 2020.**

The Committee is responsible for assisting the Board in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control, the internal and external audit processes and Rothesay's process for monitoring compliance with laws and regulations and the business principles. The Committee also receives reports from the Customer and Conduct Committee.

The Committee has unrestricted access to management and external advisers to help discharge its duties. It is satisfied that in 2020 it received adequate, reliable and timely information to perform its responsibilities effectively.

## Committee membership and attendance

The Committee is composed of only independent Non-Executive Directors with an appropriate mix of expertise and experience. Following approval of the change of control, Robin Jarratt stepped down from the Committee.

The Committee met on seven occasions in 2020 at appropriate times in the financial and regulatory reporting audit cycle. The Chairman of the Board, CEO, Managing Director, CFO, CRO, Chief Actuary, Chief Auditor, Chief Compliance Officer and representatives of PwC regularly attended Committee meetings. Other members of senior management were also invited to attend as appropriate to present reports. During the year the Committee held regular private sessions with the Chief Auditor, Chief Compliance Officer and PwC without management present.

A number of Committee members are also members of, or regular attendees at, the Board Risk Committee. This ensures effective coordination across the two committees.

As Chairman of the Committee, I report on matters dealt with at each Committee meeting to the subsequent scheduled Board meeting.

## Committee activities during 2020

The work of the Committee during 2020 fell under four main areas: financial statements and accounting policies, regulatory compliance, internal control (including oversight of the Internal Audit function) and oversight of the external audit. In addition, the Committee received reports from the Customer and Conduct Committee.

## Financial statements and accounting policies

The Committee reviewed the Rothesay's financial announcements, the annual report and accounts, the half-year results and the going concern assumptions in relation to the annual report and accounts.

During 2020 the Committee received regular reports on the progress of Rothesay's preparations for IFRS 17.

An important focus of the Committee is assisting the Board in ensuring that the annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess Rothesay's position and performance, business model and strategy. The Committee has also considered compliance with the Companies (Miscellaneous Reporting) Regulations 2018 and that there is appropriate disclosure on compliance with the Wates Corporate Governance Principles. The Committee has also reviewed the climate reporting disclosures.

The Committee reviewed the relevant Solvency II disclosures including the Solvency and Financial Condition Report (SFCR) and the Regular Supervisory Reports (RSRs). This included oversight of Rothesay's use of transitional solvency relief during the year, including consideration as to its continuing appropriateness.

The Committee reviewed the key assumptions used in calculating both the long-term insurance liabilities and the MCEV. Key assumptions included the annuity mortality assumptions, the credit default allowance on the investment portfolio and the prudence requirements around the IFRS assumptions. For MCEV, the illiquidity premium is also a key assumption. A lot of time was spent considering the impact of COVID-19 on both asset and liability valuation and the Committee reviewed the disclosures to ensure that uncertainty was appropriately captured. The following table provides more detail on significant accounting issues considered by the Committee.

The Committee reviewed Rothesay's tax policy, strategy statement and reporting on payment practices and performance under regulations made under Section 3 of the Small Business, Enterprise and Employment Act 2015.

The Committee receives reports from the Chief Actuary on areas including the reliability and adequacy of technical provisions, the quality of data, underwriting policy and reinsurance arrangements.

# Audit Committee report
**continued**

## Significant IFRS accounting issues considered by the Committee

| Issue | Committee's response |
|---|---|
| **Longevity, LPI and credit default assumptions used to determine the valuation of insurance liabilities**<br>The inherent uncertainty involved in setting the assumptions used to determine the insurance liabilities for Rothesay, particularly in relation to longevity, LPI and credit defaults, represents the most significant area of judgement due to the potential impact these assumptions have on the financial statements. | The Committee focused on the impact of COVID-19 on the valuation of liabilities and on management's proposed changes to reserving assumptions, particularly in relation to longevity, LPI and credit default.<br><br>**Longevity assumptions:** The Committee reviewed available data illustrating recent trends in longevity experience in the UK population, the longevity experience on different blocks of business, industry benchmarking data and reinsurer pricing. As 87% of the longevity risk is reinsured, Rothesay has visibility over pricing for the majority of its liabilities. Given the uncertainty in relation to future longevity trends, the Committee concluded that it was appropriate not to factor COVID-19 into future longevity assumptions for the 2020 year end.<br><br>**LPI assumptions:** The Committee reviewed the proposed change in approach to projecting rates of LPI using models rather than marking-to market. In doing so, the Committee considered industry benchmarking data.<br><br>**Credit default assumptions:** The Committee reviewed the methodology used to determine credit default assumptions and considered available industry benchmarking data. The Committee also considered whether allowance should be made for potential falls in the value of house prices when determining the cost of the no negative equity guarantee on ERMs.<br><br>The Committee concluded that the assumptions used are appropriate for the determination of the insurance liabilities. |
| **Valuation of investments classified as Level 3 under IFRS 13**<br>The valuation of Level 3 assets is based on either inputs into a valuation model or observable prices for proxy positions. This is inherently complex and requires the use of significant management judgement. Furthermore, the balances are material to the financial statements. | The Committee has reviewed and approved the Group's valuation policy. The Committee also receives and reviews a report from the finance function setting out the way in which all Level 3 assets have been valued and the range of plausible valuations. The Committee considered the impact of COVID-19 on the assets, particularly on underlying property valuations. The Committee has also reviewed the way in which LPI linked derivatives are being valued.<br><br>The Committee concluded that there are appropriate controls surrounding the valuation of Level 3 assets and that they are valued appropriately for inclusion in the financial statements. |

### Regulatory compliance

The Committee received regular compliance updates, including:

- from the Compliance function on whistleblowing and the way in which Rothesay ensures compliance with relevant laws and regulations, including anti-money laundering and anti-bribery;
- on compliance with the General Data Protection Regulation (GDPR) including data subject access requests;
- updates on Solvency II compliance including the operation of the matching adjustment fund and calculation of transitional capital relief; and
- the results of the reviews undertaken by the Compliance function.

The Committee also reviewed the new Compliance Manual and the work being undertaken to strengthen the robustness of the compliance control framework.

### The Customer and Conduct Committee

The Customer and Conduct Committee is responsible for ensuring that customers, clients and counterparties are treated fairly by Rothesay and its strategic business partners. The Committee also oversees Rothesay's approach to regulatory conduct. The Committee is chaired by an independent Non-Executive Director, Terry Miller. Two independent Non-Executive Directors, Charles Pickup and Jane Hanson, are members of the Committee and the Chairman of the Board also regularly attends.

The Customer and Conduct Committee generally considers the following regular items:

- a report from the Compliance function on regulatory conduct;
- a report from the Operations team on customer satisfaction, complaints and the performance of Rothesay's third party administrators, particularly in light of the impact of COVID-19 on their operations; and
- a report from the ERM team on complaints and on progress being made on long-outstanding cases.

The Customer and Conduct Committee also considered:

- the actions to be taken in response to the COVID-19 crisis, in particular suspension of the "small pots" initiative and changes to the origination approach for equity release mortgages;
- the migration of the servicing of the equity release mortgage portfolio acquired from UK Asset Resolution Limited to Pure Retirement;
- the Part VII transfer of our Irish business to Monument Life;
- examples of policyholder documentation using the new branding; and
- non-standard member options.

### Internal control and Internal Audit

Alongside the Board Risk Committee, the Committee seeks to ensure that Rothesay operates within a framework of prudent and effective controls and that the Board and its committees receive reliable information.

During 2020 the Committee reviewed the robustness of the controls over Rothesay's technology infrastructure. The Committee also oversaw work undertaken to improve Rothesay's operational resilience.

The Committee is supported in its oversight of the control framework by regular reports from the Internal Audit function. The Internal Audit Charter sets out the objectives, scope and responsibilities of the Internal Audit function and how it maintains independence from the first and second line management of Rothesay. The Committee reviews, and approves, the Internal Audit Charter annually.

The Chief Auditor reports directly to the Chairman of the Committee and her remuneration is approved by the Remuneration Committee. Rothesay is supported in delivery of internal audits by use of external advisers to supplement the in-house Internal Audit team. During 2016, Rothesay re-tendered these services with the result that EY was appointed.

During 2020 the Committee has overseen the strengthening of the Internal Audit function as the Chief Auditor has continued to build the in-house team.

The internal audit plan for 2020 was reviewed and approved by the Committee, with internal audits being planned and prioritised following a risk-based assessment of the business. In response to employees working from home, a number of shorter, more focused audits were undertaken designed to specifically target the risks associated with working from home by all staff. These included audit of the controls relating to payment processing, asset and liability operations and balance sheet management as well as oversight of the actions taken by the COVID-19 response team, including in relation to staff welfare.

# Audit Committee report

**continued**

The internal audit plan was then revised in line with the challenges faced as a result of remote auditing. The full reviews undertaken in 2020 included audits of:

- the oversight of Dutch mortgage origination;
- longevity risk management;
- the transition of business from Rothesay to Monument Life Insurance DAC;
- compliance with the Senior Managers & Certification Regime;
- the oversight of third parties; and
- the oversight of outsourcing arrangements with Northern Trust.

Internal Audit also closely monitored the project to develop Rothesay's IT platform.

The Committee received regular reports from Internal Audit on the audits that have been carried out, management's response to findings and progress in addressing identified issues. Internal Audit also provided its annual report on Rothesay's risk management and internal control systems to the Audit Committee, concluding that governance, risk and control systems are satisfactory.

During the year, the Committee assessed whether the Internal Audit function was effective and concluded it was. This included the Committee satisfying itself that the Internal Audit function has access to appropriate resources.

## External audit

The Committee ran a competitive tender process during 2016 and reappointed PwC as its auditors from the 2017 year end. The external audit contract is required to be put out for tender again no later than for the 2027 year end, at which time Rothesay will not be permitted to reappoint PwC.

Sue Morling became Rothesay's external audit partner from the 2020 year end as Lee Clarke had to rotate off the audit after the 2019 year end.

The Committee has approved an External Auditor Policy (which was reviewed during the year) which aims to:

- preserve the independence and objectivity of the external auditors in performing the statutory audits;
- ensure the effectiveness of the external auditors; and
- avoid any conflict of interest by outlining both the types of services that the external auditors can and cannot undertake and the considerations that should be applied in assessing potential conflicts of interest.

During 2020 the Committee performed its annual review of the independence, effectiveness and objectivity of the auditor by evaluating the auditor against a range of criteria. The review concluded that PwC remains independent and effective.

The Financial Reporting Council's Audit Quality Review Team (AQRT) carried out a review of PwC's audit of Rothesay's year end 2019 accounts as part of its routine process. As Chair of the Committee, I held discussions with the AQRT prior to the review commencing. The AQRT's final report was circulated to the Committee and an update on the process and review of the outcome was given by PwC. I am pleased to report that there were no significant recommendations made by the AQRT but certain limited improvements were suggested to the external audit process, which have already been implemented.

The fees paid to PwC for the year ended 31 December 2020 are summarised in the table below:

| | **2020 £000s** | 2019 £000s |
|---|---|---|
| Audit of the financial statements of Rothesay and its subsidiaries | **1,511** | 1,163 |
| **Total audit** | **1,511** | 1,163 |
| Required by regulation | **145** | 126 |
| Audit-related assurance services | **198** | 158 |
| Other assurance services | **222** | 167 |
| Non-audit services | **40** | 75 |
| **Total fees** | **2,116** | 1,689 |

Other assurance services provided in 2020 include work in relation to the issuance of the Tier 3 bonds and in relation to Rothesay's financial controls. These services are all in compliance with applicable independence rules and Rothesay felt that the external auditor was best placed to provide these services because of their understanding of Rothesay.

## Committee performance and effectiveness

Members and regular attendees of the Audit Committee completed a committee effectiveness questionnaire and the results were collated by the Finance department. The results were discussed at an Audit Committee meeting with the result that a number of minor changes will be introduced for 2021.

The Chairman's review of Board effectiveness also considered the effectiveness of both the Audit Committee and the Customer and Conduct Committee and resulted in a number of minor changes for 2021.

# Board Risk Committee report

**Stan Beckers**
Chairman of the Board Risk Committee

The Board Risk Committee is responsible for the operation of Rothesay's risk management framework.

| Committee membership |
|---|
| Stan Beckers (Chair) |
| Ed Giera |
| Naguib Kheraj |
| Ray King |
| Simon Morris |
| Charles Pickup |
| Bill Robertson |

**I am pleased to present the Board Risk Committee's report for the year ended 31 December 2020.**

The Committee's primary responsibilities are the ongoing monitoring and control of all risks associated with the activities of Rothesay, within the parameters set by the Board and as set out in the risk and investment policies of Rothesay.

The Committee is also responsible for the oversight of the executive-level Working Level Risk Committee (WLRC), and its sub-committees, which are responsible for the ongoing monitoring and control of all financial risks, insurance risks and operational risks associated with the activities of Rothesay. The WLRC membership consists of 15 members and is chaired by the CRO.

## Committee membership and attendance

The Committee has only independent Non-Executive Directors with an appropriate mix of expertise and experience. Following approval of the change of control, Qasim Abbas stepped down from the Board and Board Committees.

The Committee met for six scheduled meetings during 2020 in addition to reviewing risk limit changes via email.

Given the volatility of markets in the first part of the year, a number of Committee meetings were attended by the full Board. The CEO, Managing Director, CRO, CFO, Head of Asset and Liability Management, General Counsel, Chief Actuary and other Non-Executive Directors regularly attended Committee meetings. Other members of senior management were also invited to attend as appropriate to present reports.

## Committee activities during 2020

### *Risk appetite monitoring*

The Committee received regular, detailed reports on key risk exposures and the drivers of risk throughout Rothesay.

The Committee monitored Rothesay's exposure against Rothesay's overall risk appetite.

# Board Risk Committee report
**continued**

### *Risk management and governance*
During the year, the Committee was focussed on the impact of COVID-19, both realised and potential. The Committee oversaw the actions taken by Rothesay to mitigate the potential solvency and liquidity impact such as proactively trading out of sectors and investments with potential COVID-19 exposure, entering into derivative arrangements that allow the posting of corporate bonds as collateral and refinements to market risk hedging strategy. The Committee also considered the results of COVID-19 scenario testing, including a reduction in long-term interest rates to zero and large stresses to asset valuation and credit ratings. The Committee was reassured that Rothesay's financial and liquidity position would be resilient to such shocks.

The Committee received regular reports from the WLRC and the CRO. This allowed the Committee to monitor the way in which risk was being managed by Rothesay. Regular reporting includes:
- planned investment activity;
- compliance with risk limits, including in relation to liquidity;
- changes to credit ratings;
- climate change and ESG risk;
- changes in the risk register;
- stress testing and potential impact of emerging risks;
- market risk exposures;
- operational risk events;
- assessment and monitoring of cyber risk;
- economic capital coverage; and
- the results of the regular risk and control self-assessment.

The Committee received ad hoc reports on specific sectors in which Rothesay invests, such as social housing, utilities and US public finance (particularly universities and not-for-profit healthcare). The Committee considered in detail the potential impact of COVID-19 on Rothesay's commercial real estate loans and other property-related investments.

The Committee received progress updates on Rothesay's climate change-related initiatives, including the work supporting management's recommendations in relation to climate change commitments, namely the commitment to aligning our investment portfolio with the goal of the Paris Accord to limit global warming to 1.5°C above pre-industrial levels and to supporting a low carbon economy in which the UK achieves carbon neutrality by 2050.

During 2020, the Committee reviewed Rothesay's risk appetite statement, a number of risk-related policies, Rothesay's risk management framework and Rothesay's ORSA.

The Committee continued to monitor the potential impact of the UK leaving the EU and associated contingency planning. It also considered the potential impact of the planned reform of leasehold on Rothesay's loans secured on ground rents.

The Committee reviewed Rothesay's preparations for mandatory clearing of derivatives and in response to LIBOR reform.

The Committee reviewed the work being done by Rothesay to improve operational resilience and considered Rothesay's approach to cyber risk management.

### *New transactions*
The Committee reviewed the underwriting assumptions made in relation to the large bulk annuity transactions undertaken and proposed. This included consideration of any associated reinsurance and the asset investment approach. The Committee also reviewed and approved the other material reinsurance transactions entered into during 2020.

The Committee reviewed a number of risk limits including in relation to corporate bonds, US public finance and Real Estate Investment Trust (REIT) lending.

### *Internal model*
The Committee also oversaw the operation of the partial internal model, including review of minor model changes and of ongoing validation work. The work being undertaken to construct Rothesay's full internal model is being overseen by the Board.

## Committee performance and effectiveness
The Chairman's review of Board effectiveness also considered the effectiveness of the Board Risk Committee and resulted in a number of minor changes for 2021.

# Remuneration Committee report

**Naguib Kheraj**
Chairman of the Remuneration Committee

## Setting remuneration policy

The Remuneration Committee is responsible for ensuring that Rothesay's remuneration policy appropriately rewards and incentivises our people.

| Committee membership |
|---|
| Naguib Kheraj (Chair) |
| Stan Beckers |
| Tim Corbett |
| Robin Jarratt |
| Terry Miller |

**I am pleased to present the Remuneration Committee's report for the year ended 31 December 2020.**

### Committee membership and attendance

The Committee is composed solely of Non-Executive Directors with an appropriate mix of expertise and experience. Membership includes representation from Rothesay's shareholders facilitating the alignment of long term interests. The independent Non-Executive Directors form a majority given the Chairman's casting vote.

Following the change of shareholdings, Qasim Abbas stepped down from the Board and Board Committees.

The Committee met formally on three occasions in 2020 in addition to reviewing remuneration issues via email and ad hoc telephone calls. The CEO, Managing Director and the CFO also regularly attended part of Committee meetings as appropriate and relevant. The Committee has also retained an independent expert adviser from FIT Remuneration Consultants LLP to provide benchmarking, independent input and industry insights and he generally attends meetings.

### Committee responsibilities

The Committee is responsible for reviewing and making recommendations to the Board regarding the remuneration policy of Rothesay and for reviewing compliance with the policy in so far as it relates to senior managers and other employees. Within the context of the policy the Committee is specifically responsible for making recommendations for the remuneration packages of the independent Non-Executive Directors, Executive Directors and other senior managers of Rothesay. The Committee is further responsible for monitoring the overall level and structure of remuneration for the wider population.

Rothesay's remuneration policy is intended to:
- promote sound and effective risk management;
- align individuals' incentives with multi-year performance;
- discourage excessive or concentrated risk-taking;
- allow Rothesay to attract and retain proven talent; and
- align aggregate remuneration with the performance of Rothesay as a whole and encourage teamwork.

# Remuneration Committee report
**continued**

This is achieved by ensuring that variable remuneration is linked to performance across a range of financial and non-financial metrics. The CRO provides input to the annual appraisal process and financial metrics are ignored when evaluating the performance of second and third-line staff. Considerable attention is paid to non financial matters in assessing performance, including policyholder experience, operational risk management, compliance, conduct and teamwork. Remuneration packages combine a base salary, cash bonuses, a deferred equity award plan and a long-term share appreciation rights plan (the SARs plan).

A summary of the components of remuneration of Executive Directors and senior management can be found in the table on the next page.

## Committee activities during 2020

The Committee reviewed the Group's Remuneration Policy with a particular focus on ensuring that the importance of non-financial KPIs is reflected in variable pay.

The Committee reviewed and approved recommendations for the remuneration packages of senior managers of Rothesay and also reviewed the recommendations of management in relation to the compensation for employees of the wider Group and in relation to leavers.

The Committee again approved the award of shares to all employees under the Schedule 2 Share Incentive Plan in order that all employees benefit from the success of Rothesay.

The Committee reviewed the composition of the material risk-taker population regularly this year and their individual performance was discussed at year end.

Towards the end of the year, the Committee spent a lot of time considering the proposals associated with the acquisition by MassMutual and GIC of Blackstone's shareholding in Rothesay. This included the conclusion of a prior long term incentive plan and the sale by management and staff of the H shares and a proportion of vested new B ordinary shares with a substantial proportion of the consideration being deferred over a number of years. A new long-term incentive plan, the SARs plan, was put in place which is better aligned with the Company's plans as it does not depend on a corporate event such as an IPO or sale and provides for a more regular opportunity for employees to be able to realise the value of shares granted as part of deferred remuneration. In reviewing these arrangements, extensive consultations took place with shareholders as well as amongst the independent Non-Executive Directors and input was sought from the Committee's expert adviser.

The Committee also considered and recommended changes to the fees of the independent Non Executive Directors and the Chairman (with the relevant parties recused) in view of the growth in scale and complexity of the business, the demands on time of the Board and Committee participation and external benchmarking. The Committee took input from the Committee's expert adviser on these matters.

## Committee performance and effectiveness

The Chairman's review of Board effectiveness also considered the effectiveness of the Remuneration Committee and resulted in a number of minor changes for 2021.

## Components of remuneration

| Component | Rationale |
|---|---|
| **Salary** | Salaries are set at a level which is intended to reflect the individual's responsibility, skill, competence and contribution to Rothesay's objectives, whilst at the same time taking note of the external value placed on the job in the market generally. |
| **Bonus** | The annual bonus rewards the achievement of strategic objectives and is linked to Rothesay's KPIs, adjusted for current and future risks. Part of the cash bonus may be deferred. Bonuses are intended to both reward achievement and improve staff retention. |
| **Long-term share-based incentives** | Part of the annual bonus may be awarded as equity (through the deferred equity award plan) or stock appreciation rights (the SARs plan). The deferred equity award plan ensures that stock vests and is delivered over several years. The new SARs plan pays out at the end of three years, assuming performance triggers are met. Both plans ensure that the interests of shareholders and senior management are aligned.<br><br>In 2019, the creation of a new Schedule 2 Share Incentive Plan meant that all UK employees were offered shares in March 2020 which will not vest for at least three years. Further shares will be issued under this plan in 2021. |
| **Benefits** | Executive Directors and senior management are entitled to benefits in line with those provided to all employees. |
| **Pension** | Rothesay operates a defined contribution scheme. Executive Directors and senior management are entitled to membership of the scheme and receive contributions in line with those paid for all employees. |
| **Equity** | Executive Directors and senior management hold equity as a result of historic awards and annual vestings. |
| **Shareholding guidelines** | As the Company is not quoted, Executive Directors and senior management are unable to sell shares except as approved by the Remuneration Committee. |
| **Malus and clawback** | Any bonus that has been deferred is capable of a downwards adjustment or forfeiture and the rules of the deferred equity award plan ensure that equity can be clawed back even after vesting. |

# Nomination Committee report

**Naguib Kheraj**
Chairman of the Nomination Committee

## Appointing new talent

The Nomination Committee is responsible for ensuring that Rothesay's Board and management team have the appropriate mix of expertise and experience.

| Committee membership |
| --- |
| Naguib Kheraj (Chair) |
| Tim Corbett |
| Robin Jarratt |
| Ray King |
| Terry Miller |
| Charles Pickup |

**I am pleased to present the Nomination Committee's report for the year ended 31 December 2020.**

The Nomination Committee is responsible for monitoring the balance of skills, knowledge, experience, independence and diversity on the Board, identifying and recommending Board, Board committee and senior management appointments to the Boards of the various Group entities, as appropriate, and monitoring succession plans for the Executive Directors and the development plans of senior management within Rothesay.

The responsibilities of the Committee include reviewing the structure, size and composition of the Board of Directors, identifying and nominating candidates to fill Board vacancies as and when they arise and approving senior management appointments.

A summary of the Board's mix of experience is provided in the table on the next page.

### Committee membership and attendance

The Committee is composed of Non-Executive Directors with an appropriate mix of expertise and experience and a majority of independent Non Executive Directors. The CEO, Managing Director and General Counsel also regularly attended Committee meetings.

The Committee met three times during 2020.

### Committee activities during 2020

During 2020, the Committee was particularly focussed on developing succession candidates for key Board committee roles, addressing skills gaps on the Board and improving gender balance. In particular, the Committee sought to add more experience of IT and businesses dealing with large numbers of retail customers to the Board. The Committee was actively involved in the search process to identify suitable candidates which considered a wide pool of individuals and the short listed candidates were the subject of extensive interviews.

The change in ownership resulted in Qasim Abbas stepping down from the Board and has also resulted in our two shareholders each having the right to appoint a further Director. Simon Morris has resigned and will be leaving the Board on 13 February 2021.

The Committee recommended to the Board which approved the appointment of three new independent Non-Executive Directors: Ed Giera, Jane Hanson and Heather Jackson. Ed and Jane's appointments took effect in January 2021 and Heather is expected to take up her role in March. The Committee also recommended and the Board approved the appointment of Ed Giera to the Audit and Board Risk Committees and Jane Hanson to the Audit and Customer and Conduct Committees.

The Committee also recommended the re-appointment of Ray King, Terry Miller, Stan Beckers and Charles Pickup to the Board and the continuation of their Committee memberships. As Charles has served on the Board of Rothesay Life Plc for more than nine years, the Committee and the Board reviewed his independence carefully. The Committee and the Board as a whole concluded on the basis of the evidence of Charles' contributions to constructive challenge and debate in formal meetings and other interactions that he remains independent notwithstanding his tenure on the Board. The Committee also recommended the renewal of Naguib Kheraj as Rothesay's Chairman.

## Committee performance and effectiveness

The Chairman's review of Board effectiveness also considered the effectiveness of the Nomination Committee and resulted in a number of minor changes for 2021.

| | Naguib Kheraj | Addy Loudiadis | Tom Pearce | Andrew Stoker | Stan Beckers | Ed Giera | Jane Hanson | Ray King | Terry Miller | Simon Morris | Charles Pickup | Bill Robertson | Tim Corbett | Robin Jarratt |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| General management | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Insurance industry | | ✓ | ✓ | ✓ | | ✓ | ✓ | ✓ | | | ✓ | ✓ | ✓ | |
| Investment | ✓ | ✓ | ✓ | | ✓ | ✓ | | | | ✓ | | ✓ | ✓ | ✓ |
| Technology/ operations | | | | ✓ | ✓ | | ✓ | | | | | | | |
| Financial industry | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Accounting/ actuarial | ✓ | | | ✓ | | | ✓ | ✓ | | | ✓ | ✓ | ✓ | |
| Risk management | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| International business | ✓ | ✓ | | | ✓ | ✓ | | ✓ | ✓ | ✓ | | ✓ | ✓ | ✓ |
| Strategy development | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | ✓ | | ✓ | ✓ | ✓ |
| Mergers & acquisitions | ✓ | ✓ | ✓ | ✓ | | ✓ | ✓ | ✓ | | | ✓ | ✓ | ✓ | ✓ |
| Retail customers | ✓ | | | | | | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | | |
| Legal/regulatory | | | | ✓ | | | ✓ | | ✓ | ✓ | ✓ | | | ✓ |
| Corporate governance | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ |
| Human resources | ✓ | ✓ | ✓ | ✓ | ✓ | | ✓ | ✓ | ✓ | ✓ | | | | |

# Section

# 5

# Financial statements

The financial statements set out the consolidated results for Rothesay Limited and its subsidiaries for the year ended 31 December 2020.

# Report of the Directors

The Directors present their annual report and the audited consolidated financial statements for Rothesay Limited (formerly known as Rothesay Holdco UK Limited), registered number 08668809, (the Company) for the year ended 31 December 2020. Comparative information has been presented for the year ended 31 December 2019.

## 1. General information

Rothesay Limited is the ultimate holding company of the Rothesay group of companies. Rothesay Limited is a registered limited company incorporated and domiciled in the United Kingdom.

All accounting policies, where relevant, have been included within the specific note disclosures.

## 2. Results

The consolidated results for Rothesay and its subsidiaries (the Group or Rothesay) for the year are set out in the consolidated statement of comprehensive income on page 102.

## 3. Registered office

Details of the Company and its subsidiaries, including registered offices, can be found in note H.2.

Copies of the annual accounts of subsidiary undertakings are publicly available on the Companies House website or can be obtained from the Company Secretary, The Post Building, 100 Museum Street, London WC1A 1PB.

## 4. Directors

The membership of the Board of Directors of the Company is given within the corporate governance report on pages 72 to 73, which is incorporated by reference in this report.

During 2020 and up to the date of this report, the following changes to the Board took place:

- With the change of ownership of Rothesay, on 1 December 2020, Qasim Abbas stepped down from the Board.
- Jane Hanson was appointed to the Board as an independent Non-Executive Director on 1 January 2021 and Ed Giera was appointed on 25 January 2021.

## 5. Qualifying third party indemnities

The Articles of Association of the Company provide for the Directors and Officers of the Company to be indemnified in respect of liabilities incurred as a result of their office. The Company also provides certain protections for Group Directors and senior management against personal financial exposure that they may have incurred in their capacity as such. These include qualifying third party indemnity provisions (as defined under Section 234 of the Companies Act 2006) in force for the benefit of the Directors of the Group during the year and at the date of approval of the financial statements.

## 6. Disclosure of information to auditors

In the case of each Director in office at the date the Directors' report is approved:

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

## 7. Auditors

PricewaterhouseCoopers LLP will continue in office as auditors of the Company pursuant to Section 487(2) of the Companies Act. Resolutions to reappoint PricewaterhouseCoopers LLP as auditors to the Group and to authorise the Directors to determine their remuneration are proposed.

## 8. Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation. Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group and Company financial statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006. Under company law, Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Company and of the profit or loss of the Group for that period. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable 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;
- make judgements and estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are also responsible for safeguarding the assets of the Group and Company and hence for taking reasonable steps the prevention and detection of fraud and other irregularities.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Company and enable them to ensure that the financial statements comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS regulation.

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

### 9. Internal control and risk management systems

Rothesay has established internal control and risk management systems in relation to the process for preparing consolidated financial statements. The key features of these internal control and risk management systems include:

- management ensures that processes are appropriately followed, documented and controlled;
- the Risk function and management conduct checks on internal controls at least half yearly;
- the Internal Audit function reviews and assesses controls on an ongoing basis;
- management regularly monitors and considers developments in accounting regulations and best practice in financial reporting and, where appropriate, reflects developments in the consolidated financial statements. The Audit Committee is kept appraised of such developments;
- the Group's results are subject to various levels of review by management; and the Audit Committee and the Board review the draft consolidated financial statements, strategic report and report of the Directors. The Remuneration Committee reviews the remuneration disclosures. The Audit Committee receives reports from management and the external auditors on significant judgements, changes in accounting policies, changes in accounting estimates and other pertinent matters relating to the consolidated financial statements.

### 10. Date of authorisation of issue

The financial statements were authorised for issue by the Board of Directors on 11 February 2021.

ON BEHALF OF THE BOARD

**Addy Loudiadis**
Chief Executive Officer
11 February 2021

# Independent auditor's report to the members of Rothesay Limited

## Report on the audit of the financial statements

### Opinion

In our opinion, Rothesay Limited's Group financial statements and Company financial statements (the "financial statements"):

- give a true and fair view of the state of the Group's and of the Company's affairs as at 31 December 2020 and of the Group's profit, and Company's loss and the Group's and Company's cash flows for the year then ended;
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual report and accounts 2020 (the "Annual Report"), which comprise: the Consolidated and Company statement of financial position as at 31 December 2020; the Consolidated statement of comprehensive income, the Consolidated and Company cash flow statement, and the Consolidated and Company statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

### Separate opinion in relation to international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union

As explained in note A.1 to the financial statements, the Group, in addition to applying international accounting standards in conformity with the requirements of the Companies Act 2006, has also applied international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

In our opinion, the Group financial statements have been properly prepared in accordance with international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union.

### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Independence

We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group.

Other than those disclosed in note B.7 to the financial statements, we have provided no non-audit services to the Group in the period under audit.

## Our audit approach

### Overview

Audit scope
- Our audit scope has been determined to provide coverage of all material consolidated Group and Company financial statement line items.
- We have performed audit procedures that have assessed the extent of the impact of COVID-19, in particular on the valuation of insurance contract liabilities, ability to continue meeting regulatory solvency capital requirements, and financial performance, as well the ability of the Group to continue as a going concern.
- In December 2020 GIC and MassMutual purchased Blackstone's shares in Rothesay Limited. The Directors have asserted that no change to Rothesay's strategy are envisaged as a result of the change in shareholding and this has not significantly changed the scope of our audit work.

Key audit matters
- Valuation of insurance contract liabilities – Longevity Methodology and Assumptions (Group)
- Valuation of insurance contract liabilities – Credit Default Risk Methodology and Assumptions (Group)
- Valuation of insurance contract liabilities – Methodology and Assumptions to derive the Limited Price Indexation (LPI) (Group)
- Valuation of investments classified as Level 3 under IFRS 13 (Group)
- Impact of COVID-19 (Group)

Materiality
- Overall Group materiality: £52,800,000 (2019: £52,800,000) based on a materiality value that is an equivalent of 1.1% Total Equity.
- Overall Company materiality: £25,476,000 (2019: £25,100,000) based on 1.0% of Total Assets.
- Performance materiality: £39,600,000 (Group) and £19,107,000 (Company).

### The scope of our audit
As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements.

### Capability of the audit in 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 in the Auditors' responsibilities for the audit of the financial statements section, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the Group and industry, we identified that the principal risks of non-compliance with laws and regulations related to breaches of UK regulatory principles, such as those governed by the Prudential Regulation Authority, the Financial Conduct Authority, and UK tax legislation, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries, such as increasing revenue or the capital position of the Group and Company, management bias in accounting estimates and judgemental areas of the financial statements such as the valuation of life insurance contract liabilities and the valuation of investments classified as Level 3 under IFRS 13. The Group engagement team and component team are the same and share this risk assessment in setting up the appropriate audit procedures in response to such risks in their work. Audit procedures performed by the engagement team included:

# Independent auditor's report to the members of Rothesay Limited

**continued**

- Discussions with the Board, management, Internal Audit, senior management involved in the Risk and Compliance functions and the Group's and Company's legal function, including consideration of known or suspected instance of non-compliance with laws and regulation and fraud.
- Assessment of any matters reported on the Group's and Company's whistleblowing register and the results of management's investigation of such matters.
- Reading key correspondence with the Prudential Regulation Authority and the Financial Conduct Authority in relation to compliance with laws and regulations.
- Reviewing relevant meeting minutes including those of the Risk Committee and attending all Audit Committees.
- Reviewing data regarding policyholder complaints, the Group's and Company's register of litigation and claims, Internal Audit reports, and Compliance reports in so far as they related to non-compliance with laws and regulations and fraud.
- Procedures relating to the valuation of life insurance contract liabilities, in particular longevity, credit default risk assumptions and Limited Price Indexation 'LPI', and the valuation of investments classified as Level 3 under IFRS 13 described in the related key audit matters below. In addition we consider whether there are indications of management bias.
- Identifying risk criteria relating to the posting of journals that is susceptible to fraud and analysing the entire population of journals to assess those that meet this criteria.
- Designing audit procedures that incorporated unpredictability around the nature, timing or extent of our testing to material and immaterial financial statement line items, as well as validating the accuracy of member data from outsourced service providers to underlying evidence.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, 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.

## Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

This is not a complete list of all risks identified by our audit.

The "Impact of COVID-19" and "Valuation of insurance contract liabilities – Methodology and Assumptions to derive the Limited Price Indexation (LPI)" are new key audit matters this year. The key audit matter titled "Insurance contract liabilities", which was a key audit matter last year, is no longer included because of its constituent components being split out into the "Valuation of insurance contract liabilities - Longevity Methodology and Assumptions", and "Valuation of insurance contract liabilities - Credit Default Risk Methodology and Assumptions" key audit matters. Otherwise, the key audit matters below are consistent with last year.

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| ***Valuation of insurance contract liabilities – Longevity Methodology and Assumptions (Group)*** | |
| As disclosed in notes A.1 Basis of preparation and E.2 Insurance contract liabilities. | The procedures to assess the appropriateness of the longevity assumptions used in the valuation of insurance contract liabilities includes the following: |
| Annuitant mortality and specifically longevity improvement is inherently uncertain and continues to be an area of judgement. The potential impact of the ongoing COVID-19 pandemic on longevity also involves significant expert judgement. | • Understood and tested the governance process in place to determine the longevity assumptions; |
| Management utilises the Group's own historic experience and available market data in the calculation of the appropriate assumptions. For the rate of mortality improvement, this includes the latest model and datasets from the Continuous Mortality Investigation (CMI) bureau, CMI 2019. | • Assessed the appropriateness of expert judgements used in the development of the mortality assumptions. For example, the derivation of the mortality assumptions, the selection and parameterisation of the CMI model including the calibration of parameters (e.g. smoothing parameter, long-term rate) and prudential margin; |
| Whilst the Group manages the extent of its exposure to longevity risk through reinsurance, we consider the longevity assumptions underpinning insurance contract liabilities to be a key audit matter, especially given the mono-line nature of the Group's insurance business. | • Compared the longevity assumptions selected by the Group against those used by their peers; and<br>• Assessed the disclosure of the longevity assumptions and the associated financial impact on the liabilities arising from changes in these assumptions over 2020. Based on the audit procedures performed and evidence obtained, we consider the longevity assumptions used in the valuation of Insurance contract liabilities to be appropriate. |
| ***Valuation of insurance contract liabilities – Credit Default Risk Methodology and Assumptions (Group)*** | |
| As disclosed in notes A.1 Basis of preparation and E.2 Insurance contract liabilities. | The procedures to assess the appropriateness of the credit default assumptions used in the valuation of insurance contract liabilities included the following: |
| The Group has significant holdings in complex and illiquid investments. The deduction from the valuation rate of interest for credit default risk for these assets is judgemental and is generally lower than the corresponding credit default risk deduction on a typical unsecured credit portfolio. | • Assessed the methodologies used to derive the assumptions (including prudential margin) with reference to relevant rules and actuarial guidance; and by applying our industry knowledge and experience; |

# Independent auditor's report to the members of Rothesay Limited

**continued**

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| This reflects the Group's view of the security held against the asset class which in itself is an area of judgement. The challenging economic environment caused by the COVID-19 pandemic has increased the uncertainty in relation to the credit default assumptions made. | • Tested controls performed by management over the approval and implementation of credit default assumptions (to the extent available);<br>• Validated significant assumptions used by management against market observable data (to the extent available and relevant) and our experience of market practices;<br>• Compared the assumptions selected against those adopted by peers using our annual survey of the market (to the extent available);<br>• Tested the analysis of the movement in credit default risk assumption prepared by management for each asset class based on current market data and developments in the asset portfolio; and<br>• Assessed the disclosure of the credit default risk assumptions and the associated financial impact on the liabilities from changes in these assumptions over 2020.<br>Based on the audit procedures performed and evidence obtained we consider the methodology and assumptions for Credit Default used in the valuation of Insurance contract liabilities to be appropriate. |
| ***Valuation of insurance contract liabilities – Methodology and Assumptions to derive the Limited Price Indexation (LPI) (Group)*** | |
| As disclosed in notes A.1 Basis of preparation and E.2 Insurance contract liabilities. | The procedures to assess the appropriateness of the LPI methodology and assumptions used for the valuation of Insurance contract liabilities include the following: |
| Due to the nature of the Group's insurance business, there are significant insurance contract liabilities which relate to bulk pension annuities that are valued with reference to IFRS 4. | • Considered the liquidity of the LPI market in relation to assessing the relevance of the market quotes that are available and the rationale to moving to an internally developed model; |
| A significant proportion of these liabilities are contractually inflated over time by LPI. This exposure has also increased materially in recent years (particularly 2019) following large transactions. Therefore, the assumptions as to how LPI will behave in the future are significant inputs to the valuation of these liabilities. | • Assessed the appropriateness of the timing of this methodology change, with regards to the evolution of Rothesay's LPI exposure over time and in light of new information received over 2020; |

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| Management have adopted a new approach to the determination of this assumption as at 31 December 2020, calculating it using an internally developed model, where previously this was based on quotes obtained from the market. | • Assessed the methodologies used to derive the LPI assumptions (including the LPI spread, LPI volatility and prudential margin) with reference to relevant IFRS 4 accounting standards and academic literature; and by applying our industry knowledge and experience;<br>• Tested controls performed by management over the approval and implementation of LPI assumptions (to the extent available);<br>• Assessed the appropriateness of expert judgements used in the development of the LPI model. For example, the selection and parameterisation of the LPI model including the calibration of parameters and prudential margin. We have reviewed relevant academic literature and historic market data to support these judgements;<br>• Assessed the appropriateness of the output of the LPI model against the related liquid interest rate market and historic LPI data;<br>• Compared the assumptions determined against those adopted by peers using our independent benchmarking survey of the pensions market; and<br>• Assessed the disclosure of the LPI assumptions and the commentary to support the profit arising from changes in these assumptions over 2020.<br>Based on the procedures performed and evidence obtained, we consider the methodology and assumptions used to derive the LPI for the valuation of Insurance contract liabilities to be appropriate. |
| ***Valuation of investments classified as Level 3 under IFRS 13 (Group)*** | |
| As disclosed in notes A.1 Basis of preparation, D.1 Financial Investments, D.2 Derivatives, and D.3 Payables and Financial Liabilities. | The procedures to assess the appropriateness of the valuation of investments classified as Level 3 included the following: |
| The investments classified as Level 3 under the IFRS 13 fair value hierarchy is a material balance and comprise investments in commercial mortgage loans, ground rents, Dutch residential mortgages (DRM), equity release mortgages (ERM) and LPI derivatives. | • Understood and validated the design adequacy and operating effectiveness of management’s controls, including the monthly price verification process and controls over the accuracy of significant data inputs; |
| The ERM portfolio has increased significantly in the current year following the acquisition of a new ERM backbook portfolio as well as continued new originations. | • Reviewed management’s methodology and assumptions, including yield curves, discounted cash flows, property growth rates, longevity assumptions and liquidity premiums relevant to each asset class; |

# Independent auditor's report to the members of Rothesay Limited
**continued**

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| In addition, the Group holds a material portfolio of derivatives used to hedge LPI exposure within the insurance contract liabilities. These financial investments have been transferred from IFRS 13 fair value hierarchy Level 2 into Level 3 as at 31 December 2020 due to the use of significant unobservable inputs in the valuation techniques. | • Understood the valuation models used by management and obtained evidence to support the model's operation is in line with methodology; |
| The valuations of Level 3 investments are typically based on either inputs into a valuation model or observable prices for proxy positions. This is inherently complex and requires the use of significant management judgement. | • Engaged our relevant experts to assess the appropriateness of management's methodology;<br>• Independently revalued a sample of investments, including revaluation of the ERM portfolio during the year using an independent model;<br>• Tested significant inputs into the valuation of Level 3 financial investments to external sources, where possible;<br>• Considered the appropriateness of the spreads that represent the unobservable input to the valuation of the LPI derivative portfolio;<br>• With consideration of the impacts of the pandemic, identified sectors at higher risk and obtained evidence of management's credit risk assessments for relevant illiquid assets, including corroboration to external evidence; and<br>• Assessed the adequacy of disclosures in the financial statements.<br>Based on the procedures performed and evidence obtained, we consider the valuation of Level 3 financial investments to be appropriate. |
| ***Impact of COVID-19 (Group)*** | |
| As disclosed in the Strategic report and notes A.1 Basis of preparation, D.1 Financial Investments, E.1 Reinsurance assets/liabilities, E.2 Insurance contract liabilities. | In assessing management's consideration of the impact of COVID-19 on the Rothesay Group and its subsidiaries we have performed the following procedures: |
| The impacts of the global pandemic due to the Coronavirus COVID-19 continue to cause significant social and economic disruption up to the date of reporting. In our audit we have identified the following key impacts of COVID-19: | |
| Ability of the entity to continue as a going concern | |
| There are a number of potential matters in relation to COVID-19 which could impact on the going concern status of the Group and Company. Using downside scenarios driven by the required Own Risk and Solvency Assessment (ORSA) process, the Directors have considered the ability of the Group and Company to remain solvent with sufficient liquidity to meet future obligations. The Directors have also considered its requirements in respect of regulatory capital under Solvency II and the potential operational impacts on the business arising from remote working. | • Obtained management's updated going concern assessment and challenged the rationale for the downside scenarios adopted and material assumptions made using our knowledge of Rothesay's business performance, review of regulatory correspondence and obtaining further corroborating evidence; |

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| The Directors' have concluded that the Group and Company are a going concern. | • Considered information obtained during the course of the audit and publicly available market information to identify any evidence that would contradict management's assessment of the impact of COVID-19; and<br>• Inquired and understood the actions taken by management to mitigate the impacts of COVID-19, including review of Board Risk Committee minutes and attendance of all Audit Committees.<br>We agree with the Directors' conclusions in respect of going concern. |
| Impact on Estimation Uncertainty in the Financial Statements | |
| The pandemic has increased the level of estimation uncertainty in the financial statements. The Directors have therefore considered how COVID-19 has impacted the key estimates that determine the valuation of material balances, particularly the Insurance Contract Liabilities and Level 3 Financial Investments. | • Considered whether there has been any impacts from remote working on the design and operating effectiveness of key controls impacting the preparation of financial statement information;<br>• Challenged the judgements applied by management to derive the longevity and credit default assumptions, used to determine the insurance contract liabilities, in light of the emerging COVID-19 experience and by comparing these relative to the Group and Company's industry peers; and<br>• With consideration of the impacts of the pandemic, identified sectors at higher risk and obtained evidence of management's credit risk assessments for relevant illiquid assets, including corroboration to external evidence.<br>We have audited the balances impacted by estimation uncertainty and believe the values presented in the Financial Statements to be reasonable. |
| Qualitative Disclosures in the Annual Report and Financial Statements | |
| In addition, the Directors have considered the qualitative disclosures included in the Annual Report and Accounts in respect of COVID-19 and the impact that the pandemic has had, and continues to have, on the Group and Company. | • Reviewed the appropriateness of disclosures within the Annual report and accounts with respect to COVID-19 and, where relevant, considered the material consistency of this other information to the audited financial statements and the information obtained in the audit.<br>Based on the procedures performed and evidence obtained, we consider the disclosure of COVID-19 in the financial statements to be appropriate. |

## How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the Company, the accounting processes and controls, and the industry in which they operate.

# Independent auditor’s report to the members of Rothesay Limited

**continued**

The Group consists of 11 subsidiary companies and the parent Company; Rothesay Limited (formerly Rothesay Holdco UK Limited). Of the 11 subsidiary companies in the Group, the most significant component is Rothesay Life Plc, which conducts all insurance business on behalf of the Group. We determined the remaining entities to be immaterial to the Rothesay Group financial statements. For the audit of the Group, Rothesay Limited company and Rothesay Life Plc are considered full scope components and results in 95% coverage of total assets and 99% of consolidated profit before tax.

We tailored the scope of the Company audit considering the material financial statement line items and significant transactions that occurred during the year, such as the change in share ownership and equity events. We determined that the Company follows the same accounting processes and controls as other subsidiaries in the Group.

## Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

| | Financial statements – group | Financial statements – company |
|---|---|---|
| **Overall materiality** | £52,800,000 (2019: £52,800,000). | £25,476,000 (2019: £25,100,000). |
| **How we determined it** | a materiality value that is an equivalent of 1.1% Total Equity | 1.0% of Total Assets |
| **Rationale for benchmark applied** | We determine a materiality value that reflects the context of business performance and benchmarks which represent the key performance indicators considered important to the users of the financial statements. Based on the benchmarks used in the financial statements, we consider total equity to be the most appropriate benchmark as it represents the residual interest that can be ascribed to shareholders after policyholder assets and corresponding liabilities have been accounted for and the financial strength of the Group for the holders of listed debt issued. We have presented the materiality value as a percentage of Total Equity, but have also compared the materiality value against other relevant benchmarks, such as total assets, total revenue and profit before tax, to ensure the materiality selected was appropriate for our audit. | We consider that total assets is the primary measure used by the shareholders in assessing the performance of the entity and is a generally accepted auditing benchmark for the purpose of the Company financial statements. |

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £25,476,000 and £50,000,000. Certain components were audited to a local statutory audit materiality that was also less than our overall Group materiality.

We use performance materiality to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds overall materiality. Specifically, we use performance materiality in determining the scope of our audit and the nature and extent of our testing of account balances, classes of transactions and disclosures, for example in determining sample sizes. Our performance materiality was 75% of overall materiality, amounting to £39,600,000 for the Group financial statements and £19,107,000 for the Company financial statements.

In determining the performance materiality, we considered a number of factors – the history of misstatements, risk assessment and aggregation risk and the effectiveness of controls – and concluded that an amount at the upper end of our normal range was appropriate.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £2,600,000 (Group audit) (2019: £2,600,000) and £1,273,800 (Company audit) (2019: £1,267,950) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

### Conclusions relating to going concern

Our evaluation of the Directors' assessment of the Group's and the Company's ability to continue to adopt the going concern basis of accounting included:

- Obtained management's updated going concern assessment and challenged the rationale for the downside scenarios adopted and material assumptions made using our knowledge of Rothesay's business performance, review of regulatory correspondence and obtaining further corroborating evidence;
- Considered management's assessment of the regulatory Solvency coverage and liquidity position in the forward looking scenarios considered which have been driven from Rothesay's ORSA;
- Considered information obtained during the course of the audit and publicly available market information to identify any evidence that would contradict management's assessment of going concern (including the impacts of COVID-19); and
- Inquired and understood the actions taken by management to mitigate the impacts of COVID-19, including review of Board Risk Committee minutes and attendance of all Audit Committees.

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's and the Company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

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.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the Group's and the Company's ability to continue as a going concern.

Our responsibilities and the responsibilities of the Directors with respect to going concern are described in the relevant sections of this report.

# Independent auditor's report to the members of Rothesay Limited
**continued**

### Reporting on other information
The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The Directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, 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 audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic report and Report of the Directors, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

### Strategic Report and Report of the Directors
In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic report and Report of the Directors for the year ended 31 December 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the Group and Company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic report and Report of the Directors.

## Responsibilities for the financial statements and the audit
### Responsibilities of the Directors for the financial statements
As explained more fully in the Statement of Directors' responsibilities, the Directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Directors are also responsible for such internal control as they 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 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 Company or to cease operations, or have no realistic alternative but to do so.

### Auditors' 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 auditors' 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.

Our audit testing might include testing complete populations of certain transactions and balances, possibly using data auditing techniques. However, it typically involves selecting a limited number of items for testing, rather than testing complete populations. We will often seek to target particular items for testing based on their size or risk characteristics. In other cases, we will use audit sampling to enable us to draw a conclusion about the population from which the sample is selected.

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

### Use of this report

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

## Other required reporting

### Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not obtained all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- the Company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

### Appointment

We were appointed by the members on 26 February 2007 to audit the financial statements for the year ended 30 November 2007 and subsequent financial periods. The period of total uninterrupted engagement is 14 years, covering the years ended 30 November 2007 to 31 December 2020.

**Sue Morling (Senior Statutory Auditor)**
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Bristol
11 February 2021

# Consolidated statement of comprehensive income

**FOR THE YEAR ENDED 31 DECEMBER 2020**

| | Note | **2020 £m** | 2019 £m |
|---|---|---|---|
| **Income** | | | |
| Gross premiums written | B.1 | **7,281** | 16,606 |
| Premiums ceded to reinsurers | | **(1,412)** | (1,245) |
| **Net premiums written** | | **5,869** | 15,361 |
| Investment return | B.2 | **4,648** | 2,295 |
| **Total revenue** | | **10,517** | 17,656 |
| **Expenses** | | | |
| Policyholder claims | | **(2,798)** | (2,442) |
| Less: reinsurance recoveries | | **1,307** | 1,046 |
| Change in insurance contract liabilities | E.2 | **(7,315)** | (15,373) |
| Change in the reinsurers' share of insurance contract liabilities | E.1 | **83** | 46 |
| **Net claims and change in insurance liabilities** | | **(8,723)** | (16,723) |
| Acquisition and administration expenses | B.3 | **(206)** | (184) |
| Finance costs | B.4 | **(119)** | (109) |
| **Total expenses** | | **(9,048)** | (17,016) |
| **Profit before tax** | | **1,469** | 640 |
| Income tax expense | B.8 | **(276)** | (124) |
| **Profit for the year** | | **1,193** | 516 |

All income and expenses are related to continuing operations.

The consolidated statement of comprehensive income includes all income and expenses for the year. Rothesay has no items required to be reported in other comprehensive income, therefore a separate comprehensive income statement has not been presented.

Notes A–I form an integral part of these financial statements.

# Consolidated statement of financial position

**AS AT 31 DECEMBER 2020**

| | Note | **2020 £m** | 2019 £m |
|---|---|---|---|
| **Assets** | | | |
| Property, plant and equipment | | **8** | 9 |
| Lease – right of use asset | I.5 | **34** | 37 |
| Financial investments | D.1 | **93,712** | 73,742 |
| Deferred tax asset | G.1 | **5** | 2 |
| Reinsurance assets | E.1 | **616** | 388 |
| Accrued interest and prepayments | D.3 | **663** | 755 |
| Receivables | D.4 | **929** | 905 |
| Cash and cash equivalents | D.5 | **293** | 263 |
| **Total assets** | | **96,260** | 76,101 |
| **Equity and liabilities** | | | |
| **Equity** | | | |
| Share capital | C.1 | **3** | 3 |
| Tier 1 notes | C.2 | **347** | 347 |
| Employee benefit trust | C.1 | **(77)** | (30) |
| Share premium | C.3 | **1,545** | 1,545 |
| Capital contribution reserve | C.3 | **(46)** | 17 |
| Other reserves | C.3 | **3,103** | 1,894 |
| **Total equity** | | **4,875** | 3,776 |
| **Liabilities** | | | |
| Reinsurance liabilities | E.1 | **993** | 848 |
| Insurance contract liabilities | E.2 | **55,247** | 47,932 |
| Payables and financial liabilities | D.6 | **33,607** | 21,999 |
| Leasehold liabilities | I.5 | **40** | 39 |
| Borrowings | D.7 | **1,426** | 1,427 |
| Accruals and deferred income | | **72** | 80 |
| **Total liabilities** | | **91,385** | 72,325 |
| **Total equity and liabilities** | | **96,260** | 76,101 |

Notes A–I form an integral part of these financial statements.

The financial statements were approved by the Board of Directors on 11 February 2021 and signed on its behalf by:

**Addy Loudiadis**
Chief Executive Officer
11 February 2021

Company number 08668809

# Consolidated statement of changes in equity

**FOR THE YEAR ENDED 31 DECEMBER 2020**

| | Share capital £m | Share premium £m | Tier 1 notes £m | Capital contri-bution reserve £m | Profit and loss reserve £m | Reorgan-isation reserve £m | Employee scheme treasury shares £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|
| As at 1 January 2020 | **3** | **1,545** | **347** | **17** | **1,762** | **132** | **(30)** | **3,776** |
| Profit for the period | **—** | **—** | **—** | **—** | **1,193** | **—** | **—** | **1,193** |
| Employee benefit trust | **—** | **—** | **—** | **(16)** | **16** | **—** | **(47)** | **(47)** |
| Capital contribution | **—** | **—** | **—** | **(47)** | **—** | **—** | **—** | **(47)** |
| **As at 31 December 2020** | **3** | **1,545** | **347** | **(46)** | **2,971** | **132** | **(77)** | **4,875** |

**FOR THE YEAR ENDED 31 DECEMBER 2019**

| | Share capital £m | Share premium £m | Tier 1 notes £m | Capital contribu-tion reserve £m | Profit and loss reserve £m | Reorgan-isation reserve £m | Employee scheme treasury shares £m | Total equity £m |
|---|---|---|---|---|---|---|---|---|
| As at 1 January 2019 | 3 | 845 | 347 | 10 | 1,253 | 132 | (19) | 2,571 |
| Profit for the financial year | — | — | — | — | 516 | — | — | 516 |
| Retrospective restatement due to change in accounting treatment | — | — | — | — | (7) | — | — | (7) |
| Share issuance | — | 700 | — | — | — | — | — | 700 |
| Employee benefit trust | — | — | — | — | — | — | (11) | (11) |
| Capital contribution | — | — | — | 7 | — | — | — | 7 |
| As at 31 December 2019 | 3 | 1,545 | 347 | 17 | 1,762 | 132 | (30) | 3,776 |

# Consolidated cash flow statement

**FOR THE YEAR ENDED 31 DECEMBER 2020**

| | Note | 2020 £m | 2019 £m |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Profit for the financial year | | **1,193** | 516 |
| **Adjustments for non-cash movements in net profit for the financial year** | | | |
| Retrospective restatement due to change in accounting treatment | | **—** | (7) |
| Fixed asset write-off | | **—** | 1 |
| Depreciation | | **2** | 1 |
| Amortisation of debt costs | B.4 | **3** | 1 |
| Leasehold depreciation | I.5 | **3** | 2 |
| Financing charge on leasehold | I.5 | **1** | 1 |
| Share-based payments and vesting | | **(28)** | (3) |
| Interest income | B.2 | **(1,400)** | (1,125) |
| Interest expense | B.4 | **116** | 105 |
| Income tax expense | B.8 | **279** | 125 |
| **Net (increase)/decrease in operational assets** | | | |
| Financial investments | D.1 | **(19,970)** | (24,568) |
| Deferred tax | G.1 | **(5)** | (1) |
| Reinsurance asset | E.1 | **(228)** | (344) |
| Receivables | D.4 | **(24)** | (552) |
| Prepayment | D.3 | **125** | (205) |
| **Net increase/(decrease) in operational liabilities** | | | |
| Insurance contract liabilities | E.2 | **7,315** | 15,373 |
| Reinsurance liabilities | E.1 | **145** | 299 |
| Financial liabilities | D.6 | **10,632** | 8,051 |
| Other payables | D.6 | **949** | 33 |
| Accruals and deferred income | | **(7)** | 1 |
| **Cash flows used in operating activities** | | **(899)** | (2,296) |
| Interest paid | | **(116)** | (84) |
| Interest received | | **1,367** | 1,071 |
| Tax paid | | **(294)** | (59) |
| **Net cash flows generated from/(used in) operating activities** | | **58** | (1,368) |
| **Cash flows (used in)/generated from financing activities** | | | |
| Repayment of borrowings | D.7 | **(100)** | — |
| Employee share buy back | C.1 | **(23)** | — |
| Proceeds from issuance of debt (net of issuance costs) | D.7 | **96** | 778 |
| Proceeds from issuance of ordinary share capital (including share premium) | C.1 | **—** | 700 |
| **Net cash flows (used in)/generated from financing activities** | | **(27)** | 1,478 |
| **Net cash outflows used in investing activities** | | | |
| Acquisition of property, plant and equipment | | **(1)** | (9) |
| Cash flow on leasehold | | **—** | (1) |
| **Net cash outflows used in investing activities** | | **(1)** | (10) |
| Net increase in cash and cash equivalents | | **30** | 100 |
| Cash and cash equivalents at 1 January | | **263** | 163 |
| **Cash and cash equivalents at 31 December** | D.5 | **293** | 263 |

# Company statement of financial position

**AS AT 31 DECEMBER 2020**

| | Note | **2020 £m** | 2019 £m |
|---|---|---|---|
| **Assets** | | | |
| Investment in subsidiaries | H.2 | **2,480** | 2,491 |
| Financial investments | | **—** | 1 |
| Receivables | | **67** | 44 |
| **Total assets** | | **2,547** | 2,536 |
| **Equity and liabilities** | | | |
| Share capital | C.1 | **3** | 3 |
| Share premium | C.3 | **1,545** | 1,545 |
| Capital contribution reserve | | **(31)** | 22 |
| Retained earnings | | **934** | 941 |
| **Total equity** | | **2,451** | 2,511 |
| **Liabilities** | | | |
| Other payables | | **96** | 25 |
| **Total liabilities** | | **96** | 25 |
| **Total equity and liabilities** | | **2,547** | 2,536 |

Notes A–I form an integral part of these financial statements.

The loss for the financial year of the Company was £7m (2019: loss of £7m). As permitted by Section 408 of the Companies Act 2006, the Company's statement of comprehensive income has not been included in these financial statements.

The financial statements were approved by the Board of Directors on 11 February 2021 and signed on its behalf by:

**Addy Loudiadis**
Chief Executive Officer
11 February 2021

Company number 08668809

# Company statement of changes in equity

**FOR THE YEAR ENDED 31 DECEMBER 2020**

| | Share capital £m | Share premium £m | Capital contribution reserve £m | Profit and loss reserve £m | Total equity £m |
|---|---|---|---|---|---|
| As at 1 January 2020 | **3** | **1,545** | **22** | **941** | **2,511** |
| Loss for the financial year | **—** | **—** | **—** | **(7)** | **(7)** |
| Capital contribution | **—** | **—** | **(53)** | **—** | **(53)** |
| Share issuance | **—** | **—** | **—** | **—** | **—** |
| **As at 31 December 2020** | **3** | **1,545** | **(31)** | **934** | **2,451** |

**FOR THE YEAR ENDED 31 DECEMBER 2019**

| | Share capital £m | Share premium £m | Capital contribution reserve £m | Profit and loss reserve £m | Total equity £m |
|---|---|---|---|---|---|
| As at 1 January 2019 | 3 | 845 | 11 | 948 | 1,807 |
| Loss for the financial year | — | — | — | (7) | (7) |
| Capital contribution | — | — | 11 | — | 11 |
| Share issuance | — | 700 | — | — | 700 |
| As at 31 December 2019 | 3 | 1,545 | 22 | 941 | 2,511 |

# Company cash flow statement

**FOR THE YEAR ENDED 31 DECEMBER 2020**

| | Note | 2020 £m | 2019 £m |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Loss for the year | I.1 | **(7)** | (7) |
| **Adjustments for non-cash movements in net loss for the year** | | | |
| Amortisation of debt cost | | **—** | 1 |
| Interest expense | | **1** | 2 |
| **Net decrease/(increase) in operational assets** | | | |
| Financial investments | | **1** | 10 |
| Receivables | | **(23)** | (14) |
| **Net increase/(decrease) in operational liabilities** | | | |
| Other payables | | **29** | 10 |
| **Net cash flows generated from operating activities** | | **1** | 2 |
| Interest paid | | **(1)** | (2) |
| **Cash flows generated from operating activities** | | **—** | — |
| **Cash flows generated from financing activities** | | | |
| Repayment of borrowings | D.7 | **—** | — |
| Proceeds from borrowings | D.7 | **—** | — |
| Proceeds from issuance of ordinary share capital | C.1 | **—** | 700 |
| **Net cash flows generated from financing activities** | | **—** | 700 |
| **Cash flows used in investing activities** | | | |
| Investment in subsidiaries | H.2 | **—** | (700) |
| **Net cash flows used in investing activities** | | **—** | (700) |
| Net decrease in cash and cash equivalents | | **—** | — |
| Cash and cash equivalents at 1 January | | **—** | — |
| **Cash and cash equivalents at 31 December** | | **—** | — |

# Notes to the financial statements

## Note A — Significant accounting policies

### *A.1 Basis of preparation and consolidation*

The consolidated financial statements of Rothesay and those of the Company have been prepared and approved by the Directors in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. The accounting policies have been applied consistently. The financial statements have been prepared on a going concern basis.

The consolidated and separate financial statements of the Company are presented in sterling (£) rounded to the nearest million (£m) except where otherwise stated. The separate Company statement of financial position is presented on page 106.

Rothesay presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement more than 12 months after the year end is presented in the notes.

Assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expenses are not offset in the income statement unless required or permitted by IFRS.

The consolidated financial statements comprise the financial statements of the Group as at 31 December each year.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which Rothesay obtains control, and continue to be consolidated until the date when such control ceases. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the statement of comprehensive income from the date Rothesay gains control until the date Rothesay ceases to control the subsidiary. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies. The notes to the financial statements reflect the Rothesay Group position unless otherwise stated.

All intra-group balances, transactions, income and expenses, and profits and losses resulting from intra-group transactions and dividends, are eliminated in full.

Control is achieved when Rothesay is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, Rothesay controls an investee if and only if Rothesay has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns.

Rothesay re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control.

During the preparation of the consolidated financial statements Rothesay selects accounting policies and makes estimates and assumptions that impact on the items reported and their presentation. The Audit Committee reviews the reasonableness of these judgements and assumptions as well as the appropriateness of the accounting policies applied.

# Notes to the financial statements
**continued**

## Note A — Significant accounting policies (continued)
### *A.1 Basis of preparation and consolidation (continued)*
Judgements are decisions which management has made in the process of applying Rothesay's accounting policies. Matters of significant judgement are considered to be:
- The assessment of whether Rothesay controls underlying entities and investments (see note H.1).
- Assessment of the significance of insurance risk transferred to Rothesay in determining whether a contract should be accounted for as an insurance or investment contract (see note A.2).

Estimates are based on evidence available at the accounting date and opinions provided by subject matter experts. Actual results may vary from the estimates provided. As new facts become available estimates will be updated. Items considered particularly susceptible to changes in estimates are noted below:
- Fair value of financial investments where quoted market prices are not available (see note D.1).
- Measurement of net insurance contract liabilities (see notes E.1 and E.2).

During 2020, we have changed our approach to setting the rate of limited price indexation (LPI). Over time the LPI market has become highly illiquid and all but a very small number of banks have withdrawn from the market, leading to rates which are out of line with the LPI rates actually realised. In calculating the insurance liabilities, for 2020, we have therefore projected rates using LPI models based on realised LPI and other market inputs. This change has led to a reduction in insurance liabilities of £456m which was partly offset by a reduction in the estimated value of LPI linked derivatives of £160m. As this is a change in accounting estimate we have not restated prior year comparatives.

In accordance with IAS 1 and published FRC guidance, within each of the relevant notes Rothesay has included the following information:
- the assumptions made and the uncertainties around these;
- how sensitive the assets and liabilities are to these assumptions;
- expected resolution of the uncertainty and the range of possible outcomes for the financial year ending 31 December 2021; and
- explanation of any changes made to past assumptions if the uncertainty is unresolved.

### *A.2 Contract classification*
Rothesay has classified all of its policyholder contracts as insurance contracts in accordance with IFRS 4 Insurance contracts. Insurance contracts are contracts which transfer significant insurance risk to the insurer at the inception of the contract.

As permitted by IFRS 4 Insurance contracts, the liabilities of Rothesay's insurance contracts are accounted for using generally accepted accounting principles within the UK industry. Rothesay applies the modified historic statutory solvency basis (MSSB) of reporting as set out in the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers (ABI) in November 2005 (amended in December 2006). The SORP was withdrawn with effect for accounting periods beginning on or after 1 January 2015 but Rothesay continues to apply the principles.

### *A.3 Foreign currencies*
Transactions denominated in foreign currencies are translated into sterling at rates of exchange ruling on the date the transaction occurred. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at rates of exchange ruling at the financial statement date. Gains and losses on exchange are recognised in operating expenses.

## Note A — Significant accounting policies (continued)

### *A.4 Adoption of new or amended standards*

Rothesay has considered the following new standards and changes to existing standards which are relevant to Rothesay's operations, and became effective for financial years beginning on or after 1 January 2020. These amendments have all been endorsed by the EU.

#### Amendments to IFRS 9 — Financial instruments, IAS 39 — Financial instruments, and IFRS 7 — Financial instruments: disclosures — Interest rate benchmark reform:

Following the financial crisis, the replacement of benchmark interest rates such as LIBOR and other interbank offered rates (IBORS) has become a priority for global regulators. Many uncertainties remain but the route to replacement is becoming clearer. Given the pervasive nature of IBOR-based contracts among both financial institutions and corporates, there are significant potential impacts of these changes on financial reporting under IFRS.

The phase 1 amendments provide temporary relief from applying specific hedge accounting requirements to hedging relationships directly affected by IBOR reform. Rothesay does not apply hedge accounting and therefore has not been impacted by the amendments.

#### Amendments to IAS 1 — Presentation of financial statements and IAS 8 — Accounting policies, changes in accounting estimates and errors — Definition of material:

The amendments to IAS 1 and IAS 8 and consequential amendments to other IFRS i) use a consistent definition of materiality throughout IFRS and the Conceptual Framework for Financial Reporting; ii) clarify the explanation of the definition of material; and iii) incorporate some of the guidance in IAS about immaterial information.

The amended definition is 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity'.

The amendment clarifies that the reference to obscure information addresses situations in which the effect is similar to omitting or misstating that information. It also states that an entity assesses materiality in the context of the financial statements as a whole. The amendments clarify the definition of material but have not impacted on the preparation of Rothesay's financial statements.

#### Amendments to the Conceptual framework:

The IASB has revised its Conceptual Framework. This will not result in any immediate change to IFRS, but the Board and Interpretations Committee will use the revised Framework in setting future standards. The revised Framework has not impacted Rothesay's financial statements but will be used to understand the concepts in the Framework and the potential ways in which future guidance might be impacted.

#### Amendments to IFRS 3 Business combinations — Definition of a business:

This amendment has not been adopted by the EU but early adoption is permitted. To be considered a business, an acquisition would have to include an input and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present. To be a business without outputs, there will now need to be an organised workforce. The changes to the definition of a business will not impact Rothesay in the current year.

#### Amendments to IAS 1 Presentation of financial statements, on classification of liabilities

The amendment is expected to be effective for periods beginning on or after 1 January 2022. The IASB issued a narrow-scope amendment to IAS 1 to clarify that liabilities are classified as either current or non-current, depending on the rights that exist at the end of the reporting period. All entities should reconsider their existing classification in the light of the amendment and determine whether any changes are required. The changes are not expected to impact the classification of Rothesay's liabilities.

# Notes to the financial statements
**continued**

## Note A — Significant accounting policies (continued)
### *A.4 Adoption of new or amended standards (continued)*
### Amendment to IFRS 16, Leases — COVID-19 related rent concessions
As a result of the coronavirus pandemic, rent concessions have been granted to lessees. Such concessions might take a variety of forms, including payment holidays and deferral of lease payments. On 28 May 2020, the IASB published an amendment to IFRS 16 that provides an optional practical expedient for lessees from assessing whether a rent concession related to COVID-19 is a lease modification. Lessees can elect to account for such rent concessions in the same way as they would if they were not lease modifications. Rothesay has not received any concessions and therefore this amendment is not relevant to the Group.

### IFRS 17 Insurance contracts
The International Accounting Standards Board has announced that the implementation of IFRS 17, the accounting standard for insurance contracts, will be further delayed until 1 January 2023. The standard will have a big impact on the way Rothesay's results are reported because the standard rebuilds performance measurement from the ground up in areas ranging from a new definition of insurance revenue to the elimination of upfront profits and spreading of profit across the lifetime of the contract. As a result, IFRS profits that have been declared in the past (and up to 31 December 2022) will be recalculated and the opening balance sheet adjusted accordingly.

During 2020 the IFRS 17 project team has continued to make progress. An initial assessment has now been completed on the potential impact of IFRS 17 and work will continue during 2021 on detailed implementation. The IFRS 17 project is being overseen by the Audit Committee.

Rothesay has taken the deferral option in relation to IFRS 9 and will adopt the standard on the effective date of the new insurance contract standard. However IFRS 9 is expected to have relatively little impact on Rothesay as assets are already fair valued.

The following standards have not yet been endorsed and are effective for annual periods on or after 1 January 2022:

### Amendment to IFRS 3 'Business combinations'
The amendments update a reference in IFRS 3 to the Conceptual Framework for Financial Reporting without changing the accounting requirements for business combinations.

### Amendments to IAS 16 Property, plant and equipment
The amendment prohibits a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the Group is preparing the asset for its intended use. Instead, a Group will recognise such sales proceeds and related costs in profit or loss. This is not expected to apply to Rothesay.

### Amendments to IAS 37, Provisions, contingent liabilities and contingent assets
The amendments specify which costs a company includes when assessing whether a contract will be loss-making. This is not expected to apply to Rothesay.

### Annual improvements
Annual improvements make minor amendments to IFRS 1, First-time Adoption of IFRS, IFRS 9, Financial instruments, IAS 41, Agriculture and the illustrative Examples accompanying IFRS 16, Leases. None of the amendments are expected to impact Rothesay.

## Note B — Income statement notes
### *B.1 Segmental analysis*

*Segmental information is presented on the same basis as internal financial information used by Rothesay to evaluate operating performance. An operating segment is a component of Rothesay that engages in business activities from which it earns revenues and incurs expenses. Minor operating segments are combined to derive Rothesay reportable segments in accordance with the requirements of IFRS 8.*

*Rothesay writes both single and regular premium business. Single (single payment of premium which covers the life of the policy) and regular premiums (payments of premium made regularly over the duration of the policy) are recognised when they fall due.*

All of Rothesay's business risks and returns are within one business segment (i.e. long-term insurance business). This includes the premiums generated on inwards reinsurance contracts. Rothesay's insurance operations are within the United Kingdom. The split between regular premiums and single premiums is shown below:

| | Regular premiums | | Single premiums | |
|---|---|---|---|---|
| | **2020 £m** | 2019 £m | **2020 £m** | 2019 £m |
| Pension bulk annuities | **260** | 263 | **7,021** | 16,343 |
| **Total gross premiums written** | **260** | 263 | **7,021** | 16,343 |

Regular premiums are paid over the term of the longevity-only insurance policies written by Rothesay. Single premiums are one-off payments relating to bulk annuity contracts and inwards reinsurance.

Rothesay conducts a relatively small number of individual transactions each year. These transactions are one-off in nature and Rothesay's business plans do not anticipate conducting a large amount of repeat business.

### *B.2 Investment return*

*Investment return comprises all interest income on financial investments at fair value through profit and loss, realised investment gains and losses and movements in unrealised gains and losses, as well as expenses directly related to investments executed during the year.*

*Dividends on money market securities held in collective investment schemes are included as investment income on the date the units are created. Interest is accounted for on an accruals basis.*

*Realised gains and losses on investments carried at fair value are calculated as the difference between net sales proceeds and purchase price. Movements in unrealised gains and losses on investments represent the difference between the fair value of investments held at the statement of financial position date of each financial year and their purchase price or previous financial date.*

*Investment return includes fair value gains and losses. Interest is included on an accrual basis.*

| | **2020 £m** | 2019 £m |
|---|---|---|
| Interest income on financial investments at fair value through profit and loss | **1,400** | 1,125 |
| Unrealised gains on financial investments | **2,745** | 900 |
| Realised gains on financial investments | **561** | 316 |
| Investment management expenses | **(58)** | (46) |
| **Total investment return** | **4,648** | 2,295 |

Interest income has increased due to the growth in assets under management. The gains on financial investments were largely driven by the reduction in interest rates over the year.

The increase in investment management expenses reflects the growth in Rothesay’s investment activity.

# Notes to the financial statements

**continued**

## Note B — Income statement notes (continued)

### *B.3 Acquisition and administration expenses*

*The costs of acquiring new business are expensed during the financial year in which the premium is written and the costs incurred.*

Acquisition and administration expenses can be broken down as follows:

| | 2020 £m | 2019 £m |
|---|---|---|
| Acquisition and Group costs | **119** | 112 |
| Administration expenses – recurring | **53** | 48 |
| Administration expenses – project and other one-off expenses | **34** | 24 |
| Total operating expenses | **206** | 184 |

The following items have been included in operating expenses:

| | 2020 £m | 2019 £m |
|---|---|---|
| Depreciation | **2** | 1 |
| Operating lease rental expense for office premises | **4** | – |
| | **6** | 1 |

Project and other one off expenses include reinsurance fees and charitable contributions. Projects include the development of the full internal model, the development of our IT platform and development activity by our third party administrators.

### *B.4 Finance costs*

*Finance costs consist of finance costs and interest payable on financial liabilities. Finance costs are accounted for on an accruals basis.*

| | 2020 £m | 2019 £m |
|---|---|---|
| Interest payable on collateral | **3** | 9 |
| Interest payable on collateralised agreements and financing | **8** | 13 |
| **Total interest payable on collateral and collateralised agreements** | **11** | 22 |
| Interest payable on borrowings from participating interest | **21** | 26 |
| Interest payable on third party borrowings | **86** | 60 |
| Financing charge on leasehold asset | **1** | 1 |
| **Total borrowing costs** | **108** | 87 |
| **Net finance costs** | **119** | 109 |

Debt issuance expenses associated with the issue of subordinated loans are recognised over the term of the loan within interest payable.

Interest expense on the Tier 1 note is included in interest payable on third party borrowings.

## Note B — Income statement notes (continued)

### *B.5 Employee information*

| | 2020 No. | 2019 No. |
|---|---|---|
| Average number of staff employed during the year | **279** | 231 |
| **Employees by department at year end** | | |
| Management | **25** | 19 |
| New business origination | **17** | 17 |
| Investments | **46** | 40 |
| Technology | **57** | 44 |
| Finance, legal and HR | **58** | 53 |
| Operations and project management | **65** | 47 |
| Risk and Internal Audit | **37** | 32 |
| | **305** | 252 |

Rothesay staff costs during the financial year (including Directors' salaries and other pension costs) are as follows:

| | 2020 £m | 2019 £m |
|---|---|---|
| Wages and salaries | **85** | 77 |
| Social security costs | **13** | 11 |
| Other pension costs | **3** | 2 |
| **Total employee benefits expense** | **101** | 90 |

The key management personnel who have the authority and responsibility for planning, directing and controlling the activities of Rothesay include its Directors. Further details of key management personnel transactions are included in note I.3.

Directors' emoluments in respect of qualifying services to Rothesay were as follows:

| | 2020 £m | 2019 £m |
|---|---|---|
| **Directors' remuneration** | | |
| Aggregate emoluments | **8** | 9 |
| Company pension contributions to money purchase schemes | **—** | — |
| **Total Directors' remuneration** | **8** | 9 |
| **Highest paid Director** | | |
| Total amount of emoluments | **3** | 4 |
| Company pension contributions to money purchase schemes | **—** | — |
| **Total highest paid Director** | **3** | 4 |

In accordance with the Companies Act 2006, Directors' emoluments above represent the proportion of total emoluments paid or payable in respect of qualifying services. This total does not include the value of equity awards in accordance with the provisions of Schedule 5 of SI 2008/410.

During 2020 Directors received no emoluments for non-qualifying services which are required to be disclosed. Four Directors have been granted shares in Rothesay Limited in respect of long-term incentive schemes. No Directors have exercised options during the year.

### *B.6 Pension contributions*

*Rothesay operates a defined contribution pension scheme, sponsored by Rothesay Pensions Management Limited and contributions to the scheme are charged to the consolidated statement of comprehensive income as they accrue.*

The amount charged for the financial year was £3m (2019: £2m). There were no outstanding contributions as at 31 December 2020 (2019: £nil).

# Notes to the financial statements
**continued**

## Note B — Income statement notes (continued)
### *B.7 Auditors' remuneration*
Fees paid and payable to Rothesay's auditors are as follows:

| | **2020 £000s** | 2019 £000s |
|---|---|---|
| Remuneration receivable by the Company's auditors for the audit of the consolidated and Company financial statements | **34** | 29 |
| Remuneration receivable by the Company's auditors for the audit of the financial statements of the Company's subsidiaries | **1,477** | 1,134 |
| **Total audit** | **1,511** | 1,163 |
| Required by regulation | **145** | 126 |
| Audit-related assurance services | **198** | 158 |
| Other assurance services | **222** | 167 |
| Non-audit services | **40** | 75 |
| **Total fees** | **2,116** | 1,689 |

Other assurance services provided in 2020 include work in relation to the issuance of Tier 3 bonds and in relation to Rothesay's financial controls. These and the other non-audit services are all in compliance with applicable independence rules and Rothesay considered that the external auditor was best placed to provide these services because of their expertise and their understanding of Rothesay.

### *B.8 Income tax expense*

*Income tax assets and liabilities for the current year and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and laws used to compute the amount are those that are enacted or substantively enacted by the financial statement date. Management uses previous experience and the advice of professional firms when assessing tax risks.*

The major components of income tax expense for the years ended 31 December 2020 and 31 December 2019 are:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Current income tax: | | |
| UK corporation tax | **279** | 120 |
| Adjustment in respect of prior period | **—** | 5 |
| **Total current income tax** | **279** | 125 |
| Deferred tax: | | |
| Origination and reversal of temporary differences | **(3)** | (1) |
| **Total deferred tax** | **(3)** | (1) |
| **Total tax expense in the consolidated statement of comprehensive income** | **276** | 124 |

The tax expense in the consolidated statement of comprehensive income for the year and the standard rate of corporation tax in the UK of 19% (2019: 19%) is reconciled below:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Profit on ordinary activities before taxation | **1,469** | 640 |
| Tax calculated at UK standard rate of corporation tax of 19% (2019: 19%) | **279** | 122 |
| Difference in accounting and tax valuation basis | **—** | (4) |
| Adjustment in respect of prior period | **—** | 5 |
| Temporary differences | **(3)** | 1 |
| **Total tax expense reported in the consolidated statement of comprehensive income** | **276** | 124 |

## Note C — Equity

### *C.1 Share capital*

At 31 December 2020 and 31 December 2019 the share capital of Rothesay Limited comprised:

| | 2020 | | 2019 | |
|---|---|---|---|---|
| | No. | £m | No. | £m |
| Ordinary share capital of £0.002 each | **1,547,867,965** | **3.1** | 1,547,867,964 | 3.1 |
| Ordinary share capital of £0.001 each | **1** | **—** | — | — |
| Restricted shares of £0.001 each | **—** | **—** | 90,000,000 | 0.1 |
| **Authorised and issued share capital** | **1,547,867,966** | **3.1** | 1,637,867,964 | 3.2 |

On 12 March 2020, Rothesay issued 6,000,000 restricted H shares to three employees for total cash consideration of £0.01m. This took the total number of restricted shares to 96,000,000. The restricted shares were not entitled to participate in dividends but were entitled to receive a proportion of shareholder returns in excess of agreed hurdles in the event of a material change of control.

Immediately prior to completion of the acquisition of Blackstone's shareholding by MassMutual and GIC on 1 December 2020, Rothesay issued one class D share of £0.001. The D share has fixed 1% voting rights with economic returns limited to return of nominal capital. The 'new' ordinary shares were re-designated as ordinary shares.

Immediately following the approval of the change of control, the following changes occurred:

- 9,965,142 B ordinary shares were re-designated as A ordinary shares.
- Rothesay issued one A ordinary share of £0.002 for cash consideration of £3.71.
- 291,769,224 C ordinary shares were re-designated as A ordinary shares.
- The 96,000,000 restricted shares were re-classified as deferred shares and then subsequently cancelled.

The ordinary shares issued are analysed into the following categories:

| | 2020 | | 2019 | |
|---|---|---|---|---|
| | No. | £m | No. | £m |
| A £0.002 ordinary | **1,513,673,632** | **3.0** | 1,211,939,265 | 2.4 |
| B £0.002 ordinary | **34,194,333** | **0.1** | 44,159,475 | 0.1 |
| C £0.002 ordinary | **—** | **—** | 291,769,224 | 0.6 |
| D £0.001 | **1** | **—** | — | — |
| **Total** | **1,547,867,966** | **3.1** | 1,547,867,964 | 3.1 |

The A and B shares entitle the holder to participate in dividends. All ordinary shares entitle the holder to share in the proceeds of the winding up of the Company in proportion to the number of, and amounts paid, on the shares held. Only the A and D shares have full voting rights. The B ordinary shares have limited voting rights. All classes of shares have been fully paid. The table below provides an analysis of the movement in the number of shares:

| Number of shares | 2020 No. | 2019 No. |
|---|---|---|
| **At 1 January** | **1,637,867,964** | 2,499,655,342 |
| Ordinary share issuance | **2** | 333,040,293 |
| Preference share collapse into new ordinary shares | **—** | (1,214,827,671) |
| Restricted share issuance | **6,000,000** | 20,000,000 |
| Restricted share cancellation | **(96,000,000)** | — |
| **At 31 December** | **1,547,867,966** | 1,637,867,964 |

# Notes to the financial statements
**continued**

## Note C — Equity (continued)
### *C.1 Share capital (continued)*

During the prior year, with effect from 3 April 2019, the previous 943,519,813 A stapled shares (comprising one A ordinary share of £0.001 and the related preference share of £0.001), 44,159,475 B stapled shares (comprising one B ordinary share of £0.001 and the related preference share of £0.001) and 227,148,383 C stapled shares (comprising one C ordinary share of £0.001 and the related preference share of £0.001) were consolidated and reclassified respectively into 943,519,813 new A ordinary shares (of £0.002 each), 44,159,475 new B ordinary shares (of £0.002 each) and 227,148,383 new C ordinary shares (of £0.002 each).

On 20 June 2019, Rothesay issued 20,000,000 restricted H shares to the employee benefit trust for total cash consideration of £0.02m.

During September 2019, in order to ensure that Rothesay would remain appropriately capitalised given the new business pipeline, Rothesay allocated shares to existing institutional shareholders:

- On 11 September 2019 for total cash consideration of £500m, reflecting share premium of £499m Rothesay allotted 191,728,179 new A ordinary shares of £0.002 each and 46,157,744 new C ordinary shares of £0.002 each; and
- On 26 September 2019 for total cash consideration of £200m, reflecting share premium of £199m Rothesay allotted 76,691,273 new A ordinary shares of £0.002 each and 18,463,097 new C ordinary shares of £0.002 each.

### Employee benefit trusts

On 6 January 2016, the Company established an employee benefit trust, the Rothesay Employee Share Trust (the Trust). The Trust was established to purchase and hold shares of the Company for delivery of employee share schemes. Shares owned by the Trust are included at cost in the consolidated statement of financial position and are shown as a deduction from shareholders' equity. They are disclosed as employee scheme shares until they vest. The table below provides an analysis of the movement in the number of new B ordinary shares held by the Trust.

| Number of shares | 2020 No. | 2019 No. |
|---|---|---|
| **At 1 January** | **13,419,796** | 11,733,106 |
| Shares acquired from employees | **12,877,545** | 4,101,242 |
| Shares transferred to the ESIP Trust | **(226,800)** | — |
| Shares issued to employees as RSUs vest | **(2,761,025)** | (2,414,552) |
| **At 31 December** | **23,309,516** | 13,419,796 |

On 19 March 2020, the Trust purchased 2,428,491 new B ordinary shares for consideration of £9.5m. On 1 December 2020, the Trust purchased 10,443,161 new B ordinary shares for consideration of £38.8m. A further 5,893 new B ordinary shares were acquired by the Trust during the period from employees leaving employment.

On 4 April 2019, the Trust purchased 3,116,366 new B ordinary shares for consideration of £8.8m. A further 984,876 B shares (stapled pre-consolidation, new post-consolidation) were acquired by the Trust during the year from employees leaving employment.

On 20 June 2019, Rothesay issued and allotted to the Trust 20,000,000 H shares and the beneficial interest was sold to eight employees of Rothesay immediately thereafter.

## Note C — Equity (continued)

### *C.1 Share capital (continued)*

On 3 March 2020, the Company established a new employee share plan for all UK employees called the Rothesay Life UK Employee Share Incentive Plan (ESIP). The plan has been structured to operate within specific rules set by HM Revenue & Customs. A new employee benefit trust was established to support the ESIP (the ESIP Trust). The Trust transferred 226,800 shares to the ESIP Trust on 24 March 2020. These shares are held on trust for participating employees in accordance with the ESIP rules. Shares owned by the ESIP Trust are included at cost in the consolidated statement of financial position and are shown as a deduction from shareholders' equity. They are disclosed as employee scheme shares until they are withdrawn. The table below provides an analysis of the movement in the number of B ordinary shares held by the ESIP Trust.

| Number of shares | 2020 No. | 2019 No. |
|---|---|---|
| **At 1 January** | **—** | — |
| Shares transferred from the Trust | **226,800** | — |
| **At 31 December** | **226,800** | — |

### *C.2 Restricted Tier 1 notes*

*Under IFRS the Restricted Tier 1 notes (RT1) meet the definition of equity and are therefore recognised as such. Following a change to the legislation of regulatory capital instruments from 1 January 2019, the coupon payments are recognised as interest payable on third party borrowings.*

| | 2020 £m | 2019 £m |
|---|---|---|
| **Loan notes issued through public debt markets** | **347** | 347 |

On 5 September 2018, Rothesay issued £350m of Restricted Tier 1 notes with a fixed 6.875% coupon payable semi-annually in arrears. The notes were issued through the public debt markets. The notes were initially recognised at the fair value of the consideration received less transaction costs directly attributable to the issuance.

The notes are callable on or after 5 September 2028. If the notes are not repaid on that date, a fixed rate of interest per annum will be reset. The notes are direct, unsecured and subordinated obligations of the issuer.

Rothesay has the option to cancel the coupon payment which becomes mandatory upon breach or non-compliance with RLP's SCR, a breach of the minimum capital requirement (MCR) or where Rothesay has insufficient distributable reserves.

The full principal amount of each note is irrevocably and automatically reduced to zero on a permanent basis if RLP determines at any time that:
(i) eligible Own Fund items are less than or equal to 75% of the SCR;
(ii) eligible Own Fund items are less than or equal to 100% of the MCR; or
(iii) a breach of the SCR has occurred and has not been remedied within three months.

# Notes to the financial statements
**continued**

## Note C — Equity (continued)
### *C.3 Share premium account and reserve*

| | Share premium £m | Capital contribution reserve £m | Employee scheme treasury shares £m | Profit and loss reserve £m | Reorganisation reserve £m |
|---|---|---|---|---|---|
| **1 January 2020** | **1,545** | **17** | **(30)** | **1,762** | **132** |
| Profit for the financial period | **—** | **—** | **—** | **1,193** | **—** |
| Currency translation | **—** | **—** | **—** | **—** | **—** |
| Employee benefit trust | **—** | **(16)** | **(47)** | **16** | **—** |
| Capital contribution | **—** | **(47)** | **—** | **—** | **—** |
| **31 December 2020** | **1,545** | **(46)** | **(77)** | **2,971** | **132** |

| | Share premium £m | Capital contribution reserve £m | Employee scheme treasury shares £m | Profit and loss reserve £m | Reorganisation reserve £m |
|---|---|---|---|---|---|
| 1 January 2019 | 845 | 10 | (19) | 1,253 | 132 |
| Profit for the financial year | — | — | — | 516 | — |
| Retrospective restatement due to change in accounting treatment | — | — | — | (7) | — |
| Share issuance | 700 | — | — | — | — |
| Employee benefit trust | — | — | (11) | — | — |
| Capital contribution | — | 7 | — | — | — |
| 31 December 2019 | 1,545 | 17 | (30) | 1,762 | 132 |

### *C.4 Dividends on ordinary shares*
The Directors have recommended no payment of interim dividends during the year ended 31 December 2020 (2019: £nil). The Directors have recommended no final ordinary dividend in respect of the year ended 31 December 2020 (2019: £nil).

## Note D — Financial assets and liabilities

### *D.1 Financial investments*

*Financial investments are classified, at initial recognition, as financial investments at fair value through profit or loss, with the exception of receivables, cash and accrued interest, which are carried at amortised cost. Fair value is considered consistent with the risk management of the portfolio.*

*Financial investments at fair value through profit or loss are both financial investments held for trading and financial investments designated upon initial recognition at fair value. Such investments are carried in the consolidated statement of financial position at fair value with net changes in fair value presented in investment income. Transaction costs, which are incremental costs that are directly attributable to the acquisition of a financial asset, are expensed. Financial investments include collective investment schemes, government, sub sovereign and agency obligations, derivative assets, corporate bonds and other corporate debt, certificates of deposit, loans secured on property, equity release mortgages and collateralised agreements and financing.*

*The fair value of a financial instrument is the amount that would be received on the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. the exit price. Financial investments are marked to bid prices and financial liabilities are marked to offer prices. Fair value gains or losses are included in investment income.*

*The best evidence of fair value is a quoted price in an active market. If listed prices or quotations are not available, fair value is determined by reference to prices for similar instruments, quoted prices or recent transactions in less active markets, or internally developed models that primarily use, as inputs, market-based or independently sourced parameters, including but not limited to interest rates, volatilities, equity or debt prices, foreign exchange rates, credit curves and funding rates. The fair value of certain financial investments and financial liabilities require valuation adjustments for counterparty credit quality, funding risk, transfer restrictions, illiquidity, property prices and bid/offer inputs based on market evidence.*

*Financial instruments such as corporate debt securities, covered bonds, government, sub sovereign and agency obligations, certificate of deposits and certain money market instruments are valued by verifying to quoted prices, recent trading activity for identical or similar instruments, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations (e.g. indicative or firm) and the relationship of recent market activity to the prices provided from alternative pricing sources. Valuation adjustments are typically made (i) if the cash instrument is subject to regulatory or contractual transfer restrictions; and/or (ii) for other premiums and discounts that a market participant would require to arrive at fair value.*

*Certain financial instruments, including collateralised agreements and financing, loans secured on property and equity release mortgages, have one or more significant valuation inputs that are not observable. Absent evidence to the contrary, these instruments are initially valued at transaction price, which is considered to be the best initial estimate of fair value. When a pricing model is used, the model is adjusted so that the model value of the cash instrument at inception equals the transaction price. Subsequently, Rothesay uses other methodologies to determine fair value, which vary based on the type of instrument. Valuation inputs and assumptions are changed when corroborated by substantive observable evidence, including values realised on sales.*

*Rothesay uses derivative contracts for the purposes of efficient portfolio management and to mitigate the risk of adverse market movements. Rothesay's derivative contracts consist primarily of over the counter (OTC) derivatives. Rothesay measures the derivative assets and liabilities on the basis of our net exposure to the relevant risk and the fair value is the price paid to transfer the net long or short position at the balance sheet date. OTC derivatives are generally valued using market transactions and other market evidence, including market-based inputs to models, calibration to market clearing transactions, broker or dealer quotations or other alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations and the relationship of recent market activity to the prices provided from alternative pricing sources.*

# Notes to the financial statements
**continued**

## Note D — Financial assets and liabilities (continued)
### *D.1 Financial investments (continued)*

*Where models are used, the selection of a particular model to value an OTC derivative depends on the contractual terms of, and specific risks inherent in, the instrument, as well as the availability of pricing information in the market. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates, loss severity rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, model selection does not involve significant management judgement because outputs of models can be calibrated to market clearing levels. In circumstances where Rothesay cannot verify the model value by reference to market transactions, it is possible that a different valuation model could produce a materially different estimate of fair value.*

### *Derecognition*
*A financial investment (or, where applicable, a part of a financial investment or part of a group of similar financial investments) is primarily derecognised (i.e. removed from Rothesay's statement of financial position) when i) the rights to receive cash flows from the investment have expired; or ii) Rothesay has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) Rothesay has transferred substantially all the risks and rewards of the asset, or (b) Rothesay has transferred control of the investment.*

*When Rothesay has transferred its rights to receive cash flows from an investment or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risks and rewards of ownership. When it has neither transferred all of the risks and rewards of the investment nor transferred control of the investment, Rothesay continues to recognise the transferred investment to the extent of Rothesay's continuing involvement. In that case, Rothesay also recognises an associated liability. The transferred investment and the associated liability are measured on a basis that reflects the rights and obligations that Rothesay has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that Rothesay could be required to repay.*

### *Collateralised agreements and financing*
*Collateralised agreements (securities purchased under agreements to re-sell and deposits placed as collateral for stock borrowed) and collateralised financing (securities sold under agreements to repurchase and deposits received as collateral for stock loans) are treated as collateralised financing transactions and are carried at fair value through profit and loss under the fair value option, as the securities are managed on a fair value basis. The collateral can be in the form of cash or securities.*

*Cash collateral is recognised/derecognised when received/paid. Collateral posted by Rothesay in the form of securities is not derecognised from the consolidated statement of financial position, whilst collateral received in the form of securities is not recognised on the consolidated statement of financial position. If collateral received is subsequently sold, the obligation to return the collateral and the cash received are recognised in the consolidated statement of financial position.*

Rothesay's financial investments are grouped in a single category:

| | **2020 £m** | 2019 £m |
|---|---|---|
| **Financial investments carried at fair value through profit and loss, designated at initial recognition** | **93,712** | 73,742 |

## Note D — Financial assets and liabilities (continued)

### *D.1 Financial investments (continued)*

### Determination of fair value and fair value hierarchy

Rothesay uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: inputs are unadjusted quoted prices in active markets to which Rothesay had access at the measurement date for identical unrestricted assets and liabilities;
- Level 2: inputs to valuation techniques are observable either directly or indirectly; and
- Level 3: one or more inputs to valuation techniques are significant and unobservable.

The fair value of certain debt securities classified as Level 3 instruments is determined using inputs that are not based on observable market data. One of the most significant inputs is liquidity premiums. The valuation model discounts future cash flows using interest rate swap curves in addition to a spread to reflect the associated credit risk and liquidity premiums.

### COVID-19

The continued economic disruption a result of COVID-19 has impacted the fair value of our financial investments. Where possible, we have continued to use observable market prices. Where assets have been valued using techniques with unobservable inputs, we have considered whether adjustments need to be made. For example, in valuing loans secured on commercial real estate, we have adjusted underlying property values on a property-by-property basis. Sensitivities to the value of the inputs can be found at the end of this note.

The following tables show an analysis of financial investments recorded at fair value by level of the fair value hierarchy for 2020 and 2019 (please refer to note D.6 for financial liabilities):

| **31 December 2020** | **Level 1 £m** | **Level 2 £m** | **Level 3 £m** | **Total £m** |
|---|---|---|---|---|
| Collective investment schemes | **4,286** | **—** | **—** | **4,286** |
| Government sub sovereign and agency obligations | **8,900** | **9,971** | **—** | **18,871** |
| Corporate bonds and other corporate debt | **—** | **25,986** | **1,186** | **27,172** |
| Derivative assets (see note D.2) | **—** | **27,145** | **3,555** | **30,700** |
| Collateralised agreements and financing | **—** | **1,727** | **—** | **1,727** |
| Loans secured on property | **—** | **—** | **6,523** | **6,523** |
| Equity release mortgages | **—** | **—** | **4,222** | **4,222** |
| Certificate of deposits | **—** | **211** | **—** | **211** |
| **Total financial investments at fair value** | **13,186** | **65,040** | **15,486** | **93,712** |

| 31 December 2019 | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
|---|---|---|---|---|
| Collective investment schemes | 5,330 | — | — | 5,330 |
| Government sub sovereign and agency obligations | 7,951 | 10,005 | — | 17,956 |
| Corporate bonds and other corporate debt | — | 19,073 | 1,088 | 20,161 |
| Derivative assets (see note D.2) | — | 19,508 | — | 19,508 |
| Collateralised agreements and financing | — | 1,875 | — | 1,875 |
| Loans secured on property | — | — | 6,063 | 6,063 |
| Equity release mortgages | — | — | 2,669 | 2,669 |
| Certificate of deposits | — | 180 | — | 180 |
| Total financial investments at fair value | 13,281 | 50,641 | 9,820 | 73,742 |

Collective investment schemes represent money market funds with same-day liquidity.

# Notes to the financial statements
**continued**

## Note D — Financial assets and liabilities (continued)
### *D.1 Financial investments (continued)*
Approximately 17% (2019: 13%) of the total financial assets recorded at fair value are valued based on estimates and recorded as Level 3 investments.

The following table shows a reconciliation of the opening and closing recorded amounts in relation to the Level 3 financial instruments recorded at fair value (excluding equity release mortgages which are discussed in the equity release mortgages section of note D.1 below):

| | Government sub sovereign and agency obligations £m | Corporate debt £m | Loans secured on property £m | Derivative assets £m | Total £m |
|---|---|---|---|---|---|
| **At 1 January 2020** | **—** | **1,088** | **6,063** | **—** | **7,151** |
| Total gains in the statement of comprehensive income: | | | | | |
| Unrealised gains/(losses) | **—** | **33** | **(93)** | **—** | **(60)** |
| Realised gains | **—** | **—** | **12** | **—** | **12** |
| Transfer into Level 3 | **—** | **90** | **—** | **3,555** | **3,645** |
| Transfer out of Level 3 | **—** | **(47)** | **—** | **—** | **(47)** |
| Net purchases/additions | **—** | **22** | **541** | **—** | **563** |
| **At 31 December 2020** | **—** | **1,186** | **6,523** | **3,555** | **11,264** |
| At 1 January 2019 | 364 | 1,091 | 3,376 | 1 | 4,832 |
| Total gains in the statement of comprehensive income: | | | | | |
| Unrealised gains | 6 | 60 | 156 | 13 | 235 |
| Transfer out of Level 3 | (412) | (395) | — | (21) | (828) |
| Net purchases/additions | 42 | 332 | 2,531 | 7 | 2,912 |
| At 31 December 2019 | — | 1,088 | 6,063 | — | 7,151 |

Please see note D.6 for details of Level 3 derivative liabilities.

Rothesay's policy is to determine the relevant categorisation of financial assets and liabilities at least annually and, where availability of inputs has changed, transfers will be made between levels. The recorded amount of the total financial assets and investments transferred from Level 3 to Level 2 is £47m (2019: £828m). The increase in Level 3 derivative assets was driven by the transfer of LPI linked derivatives from Level 2 to Level 3 as a result of the assessment that the market for LPI swaps is illiquid. There were £90m of corporate debts transferred from Level 2 to Level 3 due to the lack of market pricing colour.

### Equity release mortgages
Equity release mortgages allow the borrowers to take equity from their homes either as a lump sum or in smaller, regular amounts. The total amount, capital plus interest, is repaid when the borrower dies or moves into long-term care. All equity release mortgage loans provide a 'no negative equity guarantee' (NNEG), which means that the mortgage repayment amounts (loan principal plus interest on redemption) are subject to a maximum of the sale proceeds of the property on which the loan is secured.

Equity release mortgages are valued using a discounted cash flow model by projecting future net cash flows on a closed form basis allowing for demographic assumptions, consistent with those used for insurance contracts adjusted for transfer to long-term care, prepayment rates, future expenses and potential cost of providing the NNEG. Cash flows are then discounted at a risk-free rate plus liquidity premium inferred from market-observed levels.

The NNEG can be thought of as a series of options written by Rothesay which allow the equity release mortgage holders to extinguish their loan by selling their property back to Rothesay at the current market value and at the point at which the mortgage must be redeemed (typically on death or transfer to long-term care), even when property values are lower than the outstanding loan balance.

## Note D — Financial assets and liabilities (continued)
### *D.1 Financial investments (continued)*
Underlying house prices have been updated in line with the latest available data. Sensitivities to interest rates and house prices are shown later in this note as these are the most material assumptions given the way in which the potential cost of the no negative equity guarantee is derived.

Given the various assumptions used in valuing the equity release mortgages, the instruments are recorded as Level 3 assets. The table below provides an analysis of the movement in the value of equity release mortgages. New business includes both the acquisition of back-books of equity release mortgages and new origination through our strategic partners. The change in economic assumptions includes the impact of changes in interest rates and property prices. The change in demographic assumptions includes the impact of changes in pre-payment rates and assumed mortality.

| | **2020 £m** | 2019 £m |
|---|---|---|
| **Carrying amount at 1 January** | **2,669** | 1,897 |
| Increase in respect of new business | **1,444** | 694 |
| Redemptions/repayments | **(145)** | (142) |
| Accrued interest for the year | **126** | 109 |
| Change in economic assumptions | **128** | 111 |
| Change in demographic assumptions | **–** | – |
| **Closing balance at 31 December** | **4,222** | 2,669 |

The table below provides a summary of the cash flows arising from the equity release mortgage portfolio based on the above assumptions:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Less than one year | **249** | 176 |
| One to five years | **913** | 624 |
| Over five years | **3,060** | 1,869 |
| | **4,222** | 2,669 |

## Collateralised agreements
Assets are transferred under repurchase and securities lending agreements with other financial institutions. The nature and carrying amounts of the assets (all carried at fair value) subject to repurchase and securities lending agreements, as well as their related liabilities, are as follows:

| | **2020** | | 2019 restated[1] | |
|---|---|---|---|---|
| | **Asset £m** | **Related liability £m** | Asset £m | Related liability £m |
| Government and agency obligations | **1,102** | **894** | 1,020 | 879 |
| Total collateralised agreements | **1,102** | **894** | 1,020 | 879 |

1 As at 31 December 2019 we have reclassified a financial liability of £203m from derivative financial instruments to collateralised financing agreements following a review of the classification of derivative contracts.

The asset collateral continues to be recognised in full and the related liability reflecting Rothesay's obligations to repurchase the transferred assets at a future date is recognised in other liabilities. Rothesay remains exposed to interest rate risk and credit risk on these pledged instruments. The counterparties' recourse is not limited to the transferred assets.

The net exposure to certain OTC derivatives is collateralised through cash. As at 31 December 2020, the total cash collateral received was £2,063m (2019: £1,193m). Other OTC contracts are collateralised with fixed income securities which are not recognised on the balance sheet of Rothesay.

# Notes to the financial statements
**continued**

## Note D — Financial assets and liabilities (continued)
### *D.1 Financial investments (continued)*
### Sensitivity of Level 3 financial investments measured at fair value to changes in key assumptions
The following table shows the impact on the fair value (FV) of Level 3 instruments of using reasonably possible alternative assumptions by class of instrument. Changes are made in isolation so, for example, no change is made to property price inflation in the property price sensitivities. Since part of any spread movement is likely to be included in the derivation of the valuation rate of interest, changes in fair value of assets also impact liabilities. The table below also shows the potential impact on profit before tax (PBT) of the same alternative assumptions, assuming that all other pricing inputs remain constant.

| | | | 2020 | | |
|---|---|---|---|---|---|
| **Impact on financial assets and PBT** | **Main assumptions** | **Changes in assumptions** | **Current FV £m** | **(Decrease)/ Increase in FV £m** | **(Decrease)/ Increase in PBT £m** |
| **Financial assets** | | | | | |
| Corporate bonds and other | Discount rate | +25bps yield to maturity | **1,186** | **(21)** | **(3)** |
| corporate debt | | -25bps yield to maturity | **1,186** | **22** | **4** |
| Loans secured on property | Liquidity | +25bps yield to maturity | **6,523** | **(258)** | **—** |
| | premium | -25bps yield to maturity | **6,523** | **280** | **—** |
| Loans secured on property | Property | +10% change in property prices | **6,523** | **19** | **41** |
| | prices | -10% change in property prices | **6,523** | **(28)** | **(76)** |
| Equity release mortgages | Liquidity | +25bps yield to maturity | **4,222** | **(125)** | **—** |
| | premium | -25bps yield to maturity | **4,222** | **131** | **—** |
| Equity release mortgages | House prices | +10% change in house prices | **4,222** | **80** | **81** |
| | | -10% change in house prices | **4,222** | **(101)** | **(103)** |
| Derivative assets | LPI bid-mid | +15bps LPI bid-mid spread | **3,555** | **(39)** | **(39)** |
| | spread | -15bps LPI bid-mid spread | **3,555** | **39** | **39** |
| **Financial liabilities** | | | | | |
| Derivative liabilities | LPI bid-mid | +15bps LPI bid-mid spread | **4,518** | **217** | **217** |
| | spread | -15bps LPI bid-mid spread | **4,518** | **(217)** | **(217)** |
| Collateralised financing | Liquidity | +25bps yield to maturity | **219** | **14** | **14** |
| agreements | Premium | -25bps yield to maturity | **219** | **(14)** | **(14)** |

| | | | 2019 | | |
|---|---|---|---|---|---|
| Impact on financial assets and PBT | Main assumptions | Changes in assumptions | Current FV £m | (Decrease)/ Increase in FV £m | (Decrease)/ Increase in PBT £m |
| **Financial assets** | | | | | |
| Corporate bonds and other | Discount rate | +50bps yield to maturity | 1,088 | (38) | (4) |
| corporate debt | | -50bps yield to maturity | 1,088 | 41 | 4 |
| Loans secured on property | Liquidity | +25bps yield to maturity | 6,063 | (250) | — |
| | premium | -25bps yield to maturity | 6,063 | 271 | — |
| Loans secured on property | Property | +10% change in property prices | 6,063 | 10 | 17 |
| | prices | -10% change in property prices | 6,063 | (16) | (42) |
| Equity release mortgages | Liquidity | +50bps yield to maturity | 2,669 | (144) | — |
| | premium | -50bps yield to maturity | 2,669 | 157 | — |
| Equity release mortgages | House prices | +10% change in house prices | 2,669 | 49 | 56 |
| | | -10% change in house prices | 2,669 | (62) | (71) |
| Derivative assets | Expected | +50bps credit default spread | — | — | — |
| | defaults | -50bps credit default spread | — | — | — |

No comparatives are shown for financial liabilities because Level 3 financial liabilities were immaterial in 2019.

## Note D — Financial assets and liabilities (continued)

### *D.2 Derivatives*

Rothesay uses derivative financial instruments as part of its risk management strategy and to hedge its solvency position. Objectives include managing exposure to market, foreign currency, inflation and interest rate risks on assets and liabilities (see also note F.2.2). The total net fair value of Rothesay's derivative assets and liabilities as at 31 December 2020 is an asset of £341m (2019: a liability of £233m).

The following table shows the fair value of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts.

| | **2020** | | | 2019 restated[1] | | |
|---|---|---|---|---|---|---|
| | **Assets £m** | **Liabilities £m** | **Notional amount £m** | Assets £m | Liabilities £m | Notional amount £m |
| **Derivatives held for risk management** | | | | | | |
| Interest rate swap | **21,769** | **(21,288)** | **393,911** | 14,463 | (14,527) | 332,733 |
| Inflation swap | **5,546** | **(6,042)** | **56,801** | 3,816 | (3,981) | 49,029 |
| Currency swap | **3,081** | **(2,741)** | **91,372** | 861 | 864 | 64,363 |
| Credit derivative | **143** | **(271)** | **18,939** | 286 | (332) | 15,024 |
| Forwards | **161** | **(17)** | **3,374** | 82 | (37) | 4,345 |
| **Total** | **30,700** | **(30,359)** | **564,397** | 19,508 | (19,741) | 465,494 |

1 Following a review of derivative contracts, Rothesay has reclassified a number of swaps from interest rate swaps to currency swaps. The impact of the restatement is a reclassification of £380m fair value derivative assets, £437m fair value derivative liabilities and £17bn in notional value. In addition, we have reclassified a derivative liability of £203m fair value and £145m notional from interest rate swaps to collateralised financing agreements.

Derivatives are used solely for efficient portfolio and risk management purposes, allowing market risks to be hedged in line with our risk appetite. The notional amount shown reflects the gross notional amount of derivative contracts. Under IFRS certain restrictions apply in relation to the offset of assets and liabilities. Rothesay does not consider that it meets these restrictions and therefore presentation is gross. Hence, multiple derivative contracts which generate offsetting risk positions inflate the size of the notional amount reported, but do not increase our risk exposure. As such, the notional amount should not be considered as an indicator of the market risk exposure generated by the derivative portfolio. Derivatives where the fair value is positive are recognised as an asset and where the fair value is negative they are recognised as a liability.

Rothesay's exposure under derivative contracts is closely monitored as part of the management of Rothesay's market risk (see also note F.2.2).

### *D.3 Accrued interest and prepayments*

| | **2020 £m** | 2019 £m |
|---|---|---|
| Accrued interest | **433** | 399 |
| Prepaid expenses | **230** | 356 |
| **Total accrued interest and prepayments** | **663** | 755 |

### *D.4 Receivables*

| | **2020 £m** | 2019 £m |
|---|---|---|
| Deposits pledged as collateral to third parties | **891** | 688 |
| Other receivables | **38** | 217 |
| **Total receivables** | **929** | 905 |

All receivables are due within one year. The fair value of receivables is £929m (2019: £905m).

The net exposure to certain OTC derivatives is collateralised through cash posted, as per the terms of the OTC contracts. At 31 December 2020, the total cash collateral posted was £891m (2019: £688m). Further details of the full extent of collateral usage can be found in the credit risk disclosure in note F.2.1.

# Notes to the financial statements
**continued**

## Note D — Financial assets and liabilities (continued)
### *D.5 Cash and cash equivalents*
The cash at bank and in hand of Rothesay at the year end is as follows:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Cash at bank and in hand | **293** | 263 |
| **Total cash and cash equivalents** | **293** | 263 |

### *D.6 Payables and financial liabilities*

| | **2020 £m** | 2019 restated[1] £m |
|---|---|---|
| Derivative financial instruments | **30,359** | 19,741 |
| Collateralised financing agreements | **894** | 879 |
| **Total financial liabilities** | **31,253** | 20,620 |
| Deposits received as collateral from third parties | **2,063** | 1,193 |
| Current tax payable | **65** | 82 |
| Employee payables | **43** | — |
| Other taxes and social security costs | **10** | 9 |
| Other payables | **173** | 95 |
| **Total payables** | **2,354** | 1,379 |
| **Total payables and financial liabilities** | **33,607** | 21,999 |

1 As at 31 December 2019 we have reclassified a financial liability of £203m from derivative financial instruments to collateralised financing agreements following a review of the classification of derivative contracts.

Financial liabilities are recorded at fair value (see note D.1 for accounting policy), of which £4,737m are valued using Level 3 techniques (2019: £1m). The remainder are valued using Level 2 techniques. The impact on the fair value of Level 3 financial liabilities of using reasonably possible alternative assumptions is included in Note D.1.

£4,731m (2019: £nil) of Level 3 derivative and other liabilities were transferred into Level 3 from Level 2 predominantly as a result of the decrease in observability of market inputs for LPI linked derivatives. The remaining movement of Level 3 financial liabilities were due to changes in economic conditions.

Payables and financial liabilities of £3,249m (2019: £1,660m) are all due within one year.

The net exposures to certain OTC derivatives are collateralised through cash. As at 31 December 2020, the total cash collateral received was £2,063mm (2019: £1,193m). Other OTC contracts are collateralised with fixed income securities which are not recognised on the consolidated statement of financial position for Rothesay.

Employee payables include deferred cash and the fair value of share-based payments awarded to employees.

## Note D — Financial assets and liabilities (continued)
### *D.7 Borrowings*

*Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the 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 method. Transaction costs are amortised over the period of the borrowings.*

Rothesay's borrowings are as follows:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Subordinated loans from participating interests | **298** | 398 |
| Subordinated loan notes | **1,128** | 1,029 |
| **Total borrowed** | **1,426** | 1,427 |

On 22 May 2020 RLP issued a further £100m of Tier 3 bonds with maturity on 12 July 2026 and a fixed 3.375% coupon payable annually in arrears. On 27 May 2020 RLP used the proceeds from the Tier 3 issuance to repay £100m of subordinated loans from participating interests.

As part of our LIBOR transition programme, with effect from 19 December 2020, the subordinated loan from participating interests was converted from a floating rate loan to a fixed rate loan with the coupon fixed at 6.05%. The fair value of the loan was unchanged as a result of the conversion.

On 12 July 2019 RLP issued £300m of Tier 3 bonds with maturity on 12 July 2026 and a fixed 3.375% coupon payable annually in arrears. On 19 November 2019 RLP issued a further £100m of the Tier 3 bonds with the same maturity and coupon as the original issuance. On 17 September 2019 RLP issued £400m of Tier 2 bonds with maturity on 17 September 2029 and a fixed 5.5% coupon payable annual in arrears. The Tier 2 bonds are callable on 17 September 2024.

The £300m revolving credit facility entered into in March 2017 was renegotiated in July 2019 and increased to £420m. The facility has subsequently been extended to August 2025 and remains effective but undrawn.

The carrying amounts, fair values and features of Rothesay's borrowings are summarised in the table below:

| | | | | | Carrying amount | | Fair value | |
|---|---|---|---|---|---|---|---|---|
| **Notional amount** | **Issue date** | **Redemption date** | **Callable at par at the option of the Group from** | **Coupon** | **2020 £m** | 2019 £m | **2020 £m** | 2019 £m |
| **Subordinated loans from participating interests** | | | | | | | | |
| £100m | 21 December 2012 | Lender has option to convert to equity from 21 December 2022 | 21 December 2017 and every six months thereafter | 6m LIBOR plus 4.25% | **—** | 100 | **—** | 97 |
| £300m | 19 September 2017 | 19 September 2028 | 19 September 2023 and annually thereafter | 6.05% | **298** | 298 | **317** | 302 |
| **Subordinated loans** | | | | | | | | |
| £250m | 22 October 2015 | 22 October 2025 | No call option | 8% | **249** | 249 | **317** | 306 |
| £500m | 12 July 2019 | 12 July 2026 | No call option | 3.375% | **485** | 386 | **533** | 403 |
| £400m | 17 September 2019 | 17 September 2029 | 17 September 2024 | 5.5% | **394** | 394 | **447** | 434 |

Prior to 19 December 2020, the subordinated loan from participating interests had a coupon of 3m LIBOR plus 5.95%.

# Notes to the financial statements
**continued**

## Note D — Financial assets and liabilities (continued)
### *D.7 Borrowings (continued)*
For the year ended 31 December 2020, an interest expense of £83m (2019: £62m) was recognised in the consolidated statement of comprehensive income in respect of these borrowings.

### Reconciliation of borrowings
The table below provides a reconciliation between opening and closing balances in the consolidated statement of financial position for liabilities arising from financing activity:

| | **1 January 2020 £m** | **Cash flows £m** | **Non-cash flows £m** | **31 December 2020 £m** |
|---|---|---|---|---|
| Subordinated loans from participating interests | **398** | **(100)** | **—** | **298** |
| Subordinated loan notes | **1,029** | **96** | **3** | **1,128** |
| **Total borrowings** | **1,427** | **(4)** | **3** | **1,426** |

| | 1 January 2019 £m | Cash flows £m | Non-cash flows £m | 31 December 2019 £m |
|---|---|---|---|---|
| Subordinated loans from participating interests | 398 | — | — | 398 |
| Subordinated loan notes | 249 | 778 | 2 | 1,029 |
| Total borrowings | 647 | 778 | 2 | 1,427 |

## Note E — Insurance contracts and reinsurance

### *E.1 Reinsurance assets/liabilities*

*Long-term business is ceded to reinsurers under contracts to transfer part of the insurance risk associated with the underlying insurance contracts. Such contracts are accounted for as insurance contracts provided the risk transfer is significant. Reinsurance inwards (i.e. where Rothesay is the reinsurer) is included in insurance contract liabilities.*

*The amounts that will be recoverable from reinsurers are estimated based upon the gross provisions, having due regard to collectability. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of the reinsurance company. The reinsurers' share of claims incurred in the profit and loss account reflects the amounts received or receivable from reinsurers in respect of claims paid or incurred during the year. Reinsurance assets/liabilities represent the discounted value of the premiums payable under the reinsurance contracts less the discounted value of the reinsurance claims payable. Premiums are recognised in the consolidated statement of comprehensive income as 'Premiums ceded to reinsurers' when due.*

*Reinsurance assets are reviewed for impairment at each reporting date, or more frequently when an indication of impairment arises during the financial reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that Rothesay may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that Rothesay will receive from the reinsurer. Any impairment loss is recorded in the consolidated statement of comprehensive income.*

| | **2020 £m** | 2019 £m |
|---|---|---|
| Insurance contract liabilities | **55,247** | 47,932 |
| Reinsurance assets | **(616)** | (388) |
| Reinsurance liabilities | **993** | 848 |
| **Insurance contract liabilities, net of reinsurance** | **55,624** | 48,392 |

Reinsurance assets in 2019 included the reinsurance of our €140m portfolio of Irish annuities. This transaction was structured initially as a reinsurance contract with Monument Re Limited and covered around 400 policyholders who remained RLP's customers until 7 September 2020, when the liabilities transferred to Monument Life Insurance DAC (formerly Laguna Life DAC and part of the Monument Re Group). Reinsurance assets (and insurance liabilities) reduced by £126m as a result of the transfer.

As noted previously, it is unclear as to whether COVID-19 will materially impact our mortality assumptions. In valuing the reinsurance assets and liabilities (and consistent with the valuation of insurance contract liabilities), we have allowed for reported deaths but we have not made any changes to our mortality assumptions as it is still too early to know what the long-term impact of COVID-19 might be on mortality.

Under the outward reinsurance contracts, Rothesay has committed to pay fixed cash flows to the reinsurer for each policy covered. In exchange, the reinsurers will pay cash flows that are linked to the actual longevity of the underlying policies. The contracts are generally collateralised for changes in longevity expectations and movements in market rates. Where a contract is collateralised no additional reserves are held, as part of the insurance contract liabilities, as the expected loss on default would be expected to be covered by the collateral. For the contracts where no collateral is held, an additional counterparty default allowance is held as part of the insurance contract liabilities to reflect the risk of loss on default. The calculation of the allowance considers the probability of default of the counterparty along with the expected level of collateral available to be reclaimed in the event of default. Longevity reinsurance contracts are valued as the net position comparing the discounted value of the fixed leg payable with the floating leg received from the reinsurer.

The value of the reinsurance liability has increased due to changes in economic conditions. Additional reinsurance has been transacted over the period covering both new business and business held at 31 December 2019. The additional reinsurance has increased the reinsurance asset.

At 31 December 2020 and 31 December 2019, Rothesay conducted an impairment review of the reinsurance assets and found no impairment necessary.

# Notes to the financial statements
**continued**

## Note E — Insurance contracts and reinsurance
### *E.2 Insurance contract liabilities*

*Insurance contract liabilities are determined by Rothesay's actuaries using methods and assumptions recommended by the actuarial function of RLP and approved by the Board. They are calculated using the historic statutory solvency basis required to comply with the reporting requirements under the Financial Services and Markets Act 2000 and in accordance with the SORP on Accounting for Insurance Business issued by the ABI in December 2005 and revised in December 2006. The SORP has been withdrawn with effect for accounting periods beginning on or after 1 January 2015 but Rothesay continues to apply the principles. Rothesay seeks to make prudent assumptions relating to expected future experience based on current market conditions and recent experience. The assumptions used incorporate prudent margins to reflect the inherent uncertainty that actual experience may be less favourable than our best estimate.*

*Insurance contract liabilities have been determined using the gross premium method of valuation. They are calculated as the discounted value of projected future claim payments (as determined by reference to the contractual arrangements with policyholders at an individual member level) adjusted for future administration costs and investment management expenses determined using prudent assumptions less the present value of future premiums (a schedule of agreed, guaranteed payments) under the longevity swap arrangements. Projected future claim payments allow for the effects of mortality. The administration costs are reflective of recent costs and expenses budgeted for the future.*

*In accordance with the previous solvency basis, where applicable Rothesay recognises negative mathematical reserves on its regular premium longevity risk transfer arrangements.*

*Note that insurance contract liabilities include reinsurance inwards, i.e. where Rothesay has reinsured a third party insurer. Where such contracts benefit from third party reinsurance, the insurance contract liabilities are shown net of those reinsurance arrangements.*

### Key valuation assumptions
This note details the assumptions with the greatest impact on Rothesay's insurance contract liability valuations.

#### *a. Mortality assumptions*
In what follows, we have changed the presentation of the mortality assumptions compared with prior years to improve clarity of disclosure.

Best estimate mortality assumptions have been determined separately for each insurance contract. The resulting assumptions are equivalent to using the base mortality assumptions set out in the table below:

| | **2020** | | 2019 | |
|---|---|---|---|---|
| | **Pensions originated** | **Insurance originated** | Pensions originated | Insurance originated |
| Males | **100.5% S2PMA** | **95.6% S2PMA** | 97.9% S2PMA | 92.9% S2PMA |
| Females | **100.5% S2PFA** | **95.6% S2PFA** | 97.9% S2PFA | 92.9% S2PFA |

For pension scheme originated business, ultimate mortality has been used in all cases. For insurance originated business, the stated base mortality basis incorporates the effect of selection adjustments for relevant policies. Past mortality improvements are applied assuming the base mortality rates are as at 2007.

## Note E — Insurance contracts and reinsurance (continued)

### *E.2 Insurance contract liabilities (continued)*

Recent mortality experience is analysed annually for each pension scheme and for insurance originated business. The last review was carried out during 2020 and no adjustments have been made to reflect the potential impact of COVID-19 given the ongoing uncertainty. The best estimate base mortality assumptions used in the valuation are based on this actual mortality experience. Mortality assumptions are generally set with reference to a Rothesay-specific suite of mortality tables. These have been expressed for reporting purposes as a single adjustment equivalent to the CMI S2 series of mortality tables drawn up by the Continuous Mortality Investigation (CMI) of the Institute and Faculty of Actuaries. The S2 tables are based on industry-wide experience.

The changes to the single equivalent rates over 2020 reflect the inclusion of new business, differences from expected mortality in recent years, updates to reflect the view of reinsurers (via reinsurance quotations) and the impact of updating the mortality improvements used to roll the base tables forward to the current date.

Allowance is made for future improvements in annuitant mortality with reference to statistical analysis of historical rates of mortality improvements, expert judgement of future changes in mortality improvements, industry benchmarking and reinsurance pricing. For 2020, mortality improvement assumptions were updated to reflect recent mortality improvements including adoption of the CMI 2019 improvement model. No allowance has been made for the potential impact of COVID-19 given the uncertainty of its long term impact. For both 2020 and 2019 an advanced calibration of the model has been used. The chosen long-term improvement rate assumption varies by age using a bespoke calibration that tapers non-linearly from age 70 to 0% at age 120. The long-term rates in the table below are expressed as core CMI model long term rates and are equivalent on a present value basis to the actual long-term rate adopted. The best estimate long-term rates have remained unchanged through 2019 and 2020. We have increased the assumed initial rates of improvements for full year 2020. The new initial adjustment parameter introduced in the CMI 2018 model has not been adopted, with adjustment to the initial rate of mortality improvements continuing to be made through the Sk parameter. As part of the adoption of the CMI 2019 model the calibration ages have been amended to improve the shape of initial improvement rates by age.

Best estimate improvements are equivalent to those shown in the table below:

| | Future mortality improvements (excluding margins) | |
|---|---|---|
| | **2020** | 2019 |
| Males | **CMI_2019*_M[1.7%; Sκ=7.5]** | CMI_2018_M[1.7%; Sκ=7.3] |
| Females | **CMI_2019*_F[1.7%; Sκ=7.5]** | CMI_2018_F[1.7%; Sκ=7.3] |

*Calibration ages 20-90

Prudent margins are then applied to both the base mortality assumptions and improvements to reflect the fact that future experience may differ from that assumed. The impact of the margins applied leads to an increase in assumed life expectancy for a 65 year old of 1.6 years (2019: 1.6 years). No changes have been made to prudent margins during 2020.

### *(b) Economic assumptions including valuation rate of interest*

The valuation rate of interest used to discount the cash flows for the purpose of valuing insurance contract liabilities is based on the risk adjusted yield obtainable on the basket of assets matching the applicable insurance contract liabilities at 31 December 2020. For the purposes of this calculation, any assets held by LTMF, RMA1 and RMA3 are treated as if they were held directly and inter-company arrangements ignored. Where assets are assumed to be re-invested, we now assume that they achieve a yield of SONIA (2019: a yield of LIBOR less 12.5bps).

# Notes to the financial statements
**continued**

## Note E — Insurance contracts and reinsurance (continued)
***E.2 Insurance contract liabilities (continued)***
### Key valuation assumptions (continued)
***(b) Economic assumptions including valuation rate of interest (continued)***

A 2.5% prudential margin is then applied to the risk-adjusted internal rate of return obtained on the basket of matching assets and an allowance made for investment management expenses of 3bps p.a. (2019: 3bps p.a.).

The result is equivalent to using the valuation rate of interest set out in the table below:

| | **2020** | 2019 |
|---|---|---|
| Equivalent rate of interest | **1.32% p.a.** | 1.78% p.a. |

In determining the risk adjusted yield on assets a deduction is made to reflect credit default risk, where applicable adjusted for the prudent expected recoveries in the event of default and, for some asset classes, the cost of rebalancing the portfolio following a downgrade. This deduction in yield is determined separately for each individual asset, reflecting the risk to the return being achieved on the asset.

The table below shows the average yield deduction by asset class before the application of the 2.5% prudential margin at 31 December 2020, and 31 December 2019.

| | Average yield deduction | |
|---|---|---|
| **Asset class** | **2020** | 2019 |
| UK government approved securities | **0 bps** | 0 bps |
| Secured lending | **35 bps** | 24 bps |
| Supranational/other sovereign | **27 bps** | 17 bps |
| Secured residential lending | **27 bps** | 28 bps |
| Corporate bonds (without covering credit default swaps) | **60 bps** | 56 bps |
| Infrastructure | **67 bps** | 63 bps |
| Equity release mortgages | **112 bps** | 125 bps |
| Other | **43 bps** | 36 bps |
| **Overall yield reduction** | **35 bps** | 31 bps |

Since the end of 2019, the average yield deduction has increased in aggregate. The change in default allowance is mainly due to the change in asset mix during the period. Our approach to deriving credit default assumptions was modified at the start of 2020 to better reflect the relative riskiness of individual assets.

Allowance is made for the risks associated with equity release mortgages through the valuation of the NNEG and this is included in the overall yield deduction above. The calculation of the NNEG is described in note D.1 and for the valuation rate of interest is calculated on a prudent basis allowing for future property price growth at a rate equivalent to 0.97% net of dilapidation costs and cost of sale (2019: 1.14%) and house price volatility equivalent to 13% (2019: 13%). Given the potential short term distortion in the housing market from the stamp duty holiday, in calculating the value of the NNEG allowed for in the yield deduction above, house prices are assumed to have fallen by 5% with no offsetting change in assumed future house price growth. The decrease in the yield deduction for equity release mortgages over the period has been driven by origination of lower-risk mortgages partially offset by the assumed fall in house prices and the reduction in assumed property price growth rate over the period.

An important actuarial assumption relates to the future rate of escalation of certain annuity benefits. Where possible such rates are derived from inflation swap markets. Whilst that is still the case for more liquid inflation rates, in 2020 we have changed our approach to setting the rate of limited price indexation (LPI). Over time the LPI market has become highly illiquid and all but a very small number of banks have withdrawn from the market, leading to rates which are out of line with the LPI rates actually realised. For 2020, we have therefore projected rates using LPI models based on realised LPI and other market inputs. This change has led to a reduction in insurance liabilities of £456m which was partly offset by a reduction in the estimated value of LPI linked assets of £160m.

**Note E — Insurance contracts and reinsurance (continued)**
***E.2 Insurance contract liabilities (continued)***
## Key valuation assumptions (continued)
***(c) Expense assumption***
The allowance made for future overhead maintenance expenses has been updated following an investigation into the total costs incurred by Rothesay during 2020 and the projected 2021 expenses. As part of this investigation, these costs have been split between acquisition and maintenance expenses. The long-term business provisions include an allowance to provide for the expenses payable under the third party administration agreements together with the long-term business overhead expenses expressed as an amount per policy. The average per policy allowance is £40 per policy per annum (2019: £36 per policy per annum). Additional allowances are then made for short-term project costs and investment management expenses.

Within these expense provisions, an allowance for future expense inflation has been made to cover the impact of both salary and price inflation. The future rate of expense inflation is assumed to be RPI (as implied by the RPI swap curve) plus an addition at each duration of 0.25% p.a. for all expenses (2019: 0.25% p.a.).

***(d) Member option and dependants assumptions***
A number of other, less financially significant, actuarial assumptions are made in determining the provisions. These assumptions include, inter alia, the proportion of deferred and immediate annuitants assumed to have a dependant eligible for contingent benefits, the dependant's age difference and the proportion of deferred annuitants opting to take a proportion or all of their benefit as a lump sum.

The modelling of member options allows for the probability that deferred annuitants choose to transfer their benefits each year. The cash flow profile resulting from the assumed take-up of member options impacts the composition of the basket of assets used to derive the valuation rate of interest (see E.2(b) on the previous page).

When deferred annuitants have passed the scheme normal retirement date and have been subject to an in-depth tracing exercise and yet remain untraced, a prudent allowance has been made for the probability of them taking their benefits in the future. All other individuals who have passed the scheme normal retirement date are assumed to start receiving pension payments immediately.

***(e) Movement in insurance contract liabilities, net of reinsurance***
The table below shows the change in insurance contract liabilities, net of reinsurance, over the year. The release of liabilities line reflects claims paid, release of prudent margins and unwind of discounting over the year.

| | **2020 £m** | 2019 £m |
|---|---|---|
| Carrying amount at 1 January | **48,392** | 33,065 |
| Increase in respect of new business | **7,142** | 16,362 |
| Release of liabilities | **(2,498)** | (2,028) |
| Effect of assumption changes | **2,579** | 985 |
| Other | **9** | 8 |
| **Closing balance at 31 December** | **55,624** | 48,392 |

# Notes to the financial statements
**continued**

## Note E — Insurance contracts and reinsurance (continued)
### *E.2 Insurance contract liabilities (continued)*
### Key valuation assumptions (continued)
#### *(e) Movement in insurance contract liabilities, net of reinsurance (continued)*
The following table shows the impact on the insurance contract liabilities, net of reinsurance, of changes in the assumptions used:

| Net increase/(decrease) in liabilities | 2020 £m | 2019 £m |
|---|---|---|
| **Change in assumptions used** | | |
| Valuation rate of interest | **3,435** | 1,747 |
| Inflation | **(412)** | (716) |
| **Effect of economic assumption changes** | **3,023** | 1,031 |
| Demographics | **(46)** | (212) |
| Member options | **(12)** | (10) |
| Expenses | **70** | 176 |
| LPI model refinement | **(456)** | – |
| **Effect of non-economic assumption changes and model refinement** | **(444)** | (46) |
| **Total effect of assumption changes** | **2,579** | 985 |

As shown previously, the valuation rate of interest decreased by 46bps over the year, which led to the £3.4bn increase in the net liability shown. This was partially offset by the impact of the fall in future rate of inflation.

Updates were made to the non-economic assumptions and modelling refinement during the period as described in section E.2 (a) for demographic assumptions, E.2 (b) for LPI model refinement and E.2. (c) for expenses. Note that the reduction in liabilities as a result of the change in approach to modelling LPI was partly offset by a reduction in the estimated value of LPI linked assets of £160m.

#### *(f) Sensitivity analysis*
The schedule below provides an analysis of the reasonably possible movements in key assumptions that would have a material impact on liabilities (net of reinsurance), profit before tax (PBT) and equity. The analysis is based on a change in a single assumption whilst holding all other assumptions constant. The analysis assumes an instantaneous shock to the assumptions other than for the interest rate and inflation sensitivities where the impact of dynamic hedging is allowed for as market conditions change. The sensitivity of liabilities to interest rates and inflation increased during 2020 as a result of the growth in net insurance liabilities. The change in the impact of interest rate moves on PBT and equity is partly due to us being more focussed on hedging the solvency balance sheet than at the end of 2019. When stressing credit default assumptions, the total spread on corporate bonds is assumed to move by approximately 30bps.

| 2020 | Change in assumptions | (Decrease)/ increase in net liabilities £m | Increase/ (decrease) in PBT £m | Impact on equity £m |
|---|---|---|---|---|
| Annuitant mortality | **+5% qx** | **(154)** | **149** | **120** |
| Annuitant mortality | **-5% qx** | **159** | **(154)** | **(125)** |
| Interest rate | **+100bps** | **(7,120)** | **(169)** | **(137)** |
| Interest rate | **-100bps** | **8,852** | **549** | **445** |
| Inflation | **+100bps** | **3,507** | **(48)** | **(39)** |
| Inflation | **-100bps** | **(3,111)** | **173** | **140** |
| Credit default assumption | **+10bps** | **(713)** | **(447)** | **(362)** |
| Credit default assumption | **-10bps** | **735** | **460** | **372** |
| Change in property prices | **+10%** | **(22)** | **121** | **98** |
| Change in property prices | **-10%** | **50** | **(179)** | **(145)** |
| Expenses | **+10%** | **142** | **(142)** | **(115)** |

## Note E — Insurance contracts and reinsurance (continued)
### *E.2 Insurance contract liabilities (continued)*
### Key valuation assumptions (continued)
#### *(f) Sensitivity analysis (continued)*

| 2019 | Change in assumptions | (Decrease)/ increase in net liabilities £m | Increase/ (decrease) in PBT £m | Impact on equity £m |
|---|---|---|---|---|
| Annuitant mortality | +5% qx | (228) | 225 | 182 |
| Annuitant mortality | -5% qx | 240 | (237) | (192) |
| Interest rate | +100bps | (6,149) | 241 | 195 |
| Interest rate | -100bps | 7,719 | (85) | (69) |
| Inflation | +100bps | 3,234 | (242) | (196) |
| Inflation | -100bps | (2,968) | 382 | 309 |
| Credit default assumption | +10bps | (508) | (310) | (251) |
| Credit default assumption | -10bps | 523 | 319 | 259 |
| Change in property prices | +10% | (14) | 72 | 59 |
| Change in property prices | -10% | 35 | (113) | (91) |
| Expenses | +10% | 134 | (134) | (108) |

The sensitivities shown capture non-linearity effects, which may be significant following large market movements. The risk management strategy adopted can result in Rothesay being immunised to market movements in either direction.

Given current interest rates, the -100bps interest rate sensitivity means that interest rates are assumed to fall below zero at all durations (2019: fall below zero for eight years).

The impact of reinsurance on the sensitivity to mortality risk is a reduction of 87% (2019: 78%). The impact of reinsurance has changed due to additional reinsurance transacted through the period.

The annuitant mortality sensitivity is defined in terms of a qx stress where qx represents the probability of a life dying during the year. As such, in the annuitant mortality stress it is assumed that in each year 5% more or fewer people survive to the end of each year than had previously been assumed.

#### *(g) Timing of cash flows*
The table below shows the discounted value of insurance liability cash flows, net of reinsurance, which are expected to arise during each year:

| | **2020** | | | |
|---|---|---|---|---|
| | **Less than 1 year £m** | **1 to 5 years £m** | **Over 5 years £m** | **Total £m** |
| **Insurance contract cash flows net of reinsurance** | **2,726** | **10,235** | **42,663** | **55,624** |

| | 2019 | | | |
|---|---|---|---|---|
| | Less than 1 year £m | 1 to 5 years £m | Over 5 years £m | Total £m |
| Insurance contract cash flows net of reinsurance | 2,440 | 9,057 | 36,895 | 48,392 |

# Notes to the financial statements
**continued**

## Note F — Risk and capital management
### *F.1 Capital management*
Rothesay's capital resources are of critical importance. Rothesay's capital management framework is designed to meet the following objectives:
- to maintain financial strength in adverse conditions;
- to give customers long-term confidence in Rothesay;
- to satisfy our regulatory obligations;
- to match the profile of our assets and liabilities, taking account of the risk inherent in the business;
- to allocate capital efficiently to support new business growth;
- to retain financial flexibility by maintaining strong liquidity; and
- to provide an appropriate return to shareholders.

From 1 January 2016, Rothesay was required to operate under the new Solvency II regime. Rothesay had sufficient capital available to meet its regulatory capital requirements at all times during the period ended 31 December 2020.

Under the Solvency II regime, Rothesay is required to hold sufficient assets to meet:
- Rothesay's technical provisions, being:
  - the liabilities of Rothesay calculated on a best estimate basis (the BEL); plus
  - the risk margin; less
  - available transitional solvency relief.
- The capital required to meet a 1-in-200-year stress (known as the solvency capital requirement or SCR).

Transitional solvency relief was last re-calculated as at 31 December 2020 and amortises by 1/16th each year from 1 January 2017. As at 31 December 2020, solvency estimates allow for amortisation of 4/16ths of transitional solvency relief (2019: 3/16ths).

Rothesay received approval to use a PIM from 31 December 2018, so from that date the SCR relating to credit and counterparty risk is calculated using the Rothesay's bespoke models and the standard formula is used to calculate the SCR for all other risk components and for aggregation across risk components.

Capital in excess of that required to meet the technical provisions is known as Own Funds. As at 31 December 2020, Own Funds for Rothesay were £7,277m (2019: £6,132m) made up as follows:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Total IFRS equity | **4,875** | 3,776 |
| Liability valuation differences and other regulatory adjustments | **906** | 901 |
| **Total Tier 1** | **5,781** | 4,677 |
| Tier 2 debt valuation | **984** | 1,059 |
| Tier 3 debt valuation | **512** | 396 |
| **Own Funds** | **7,277** | 6,132 |

Rothesay holds both debt and equity to optimise its capital structure and improve shareholder return. During the prior year, £700m of equity, £400m of Tier 2 debt and £400m of Tier 3 debt were issued by Rothesay.

## Note F — Risk and capital management (continued)

### *F.1 Capital management (continued)*

The capital position is sensitive to changes in market conditions, due to changes in the value of the assets and the effect that changes in investment conditions may have on the value of the liabilities. Rothesay seeks to mitigate these risks through the close matching of asset and liability cash flows, and through the use of derivative hedges and reinsurance. Management monitors market conditions and emerging longevity experience on a regular basis. As these conditions change, management will take remedial action such as adjustment of hedging strategies and re-investment of assets as appropriate.

### *F.2 Risk management and analysis*

Rothesay is exposed to credit, market and liquidity risk through its financial assets and financial liabilities. Rothesay is exposed to insurance risk through its insurance liabilities and to operational risk as a result of its activities. These risks are described below and are managed in accordance with risk management policies and procedures established by Rothesay. Please see pages 36 to 44 of the strategic review for further detail on risk management arrangements and the governance framework within Rothesay.

### *F.2.1 Credit risk*

Credit risk represents the potential for loss, or solvency deterioration, due to the default or deterioration in credit quality of a counterparty or an investment we hold. Credit risk also arises from cash placed with banks or money market funds, collateralised financing transactions (i.e. resale and repurchase agreements) and receivables from third parties.

Management is responsible and accountable for managing credit risks within prescribed limits. Effective management of credit risk requires disciplined underwriting, accurate and timely information, strong collateral management, a high level of communication and knowledge of customers, countries, industries and products.

The independent risk function, led by the CRO, has responsibility for ensuring an appropriate framework is in place for assessing and monitoring credit risk. All credit exposures are actively monitored by the risk function, including the use of regular sector and position reviews and a number of early warning indicators, resulting in regular reporting to the investment team and key governance bodies such as the BRC.

#### *Risk mitigants*

Rothesay manages credit risk in its investment portfolio by diversifying exposures across and within sectors, controlling position sizes through limits, and regular monitoring and oversight of investments.

To mitigate the credit exposures on derivatives and collateralised agreement transactions, Rothesay obtains collateral from counterparties on an upfront or contingent basis. Rothesay also enters into netting agreements with counterparties that permit it to offset receivables and payables with such counterparties for transaction settlements and upon a counterparty default.

When Rothesay does not have sufficient visibility into a counterparty's financial strength, or when it believes a counterparty requires support from its parent company, Rothesay may obtain third party guarantees of the counterparty's obligations. Rothesay also mitigates its investment and counterparty credit risk using credit derivatives.

#### *Credit exposures*

Rothesay is exposed to credit risk from its receivables from third parties. Receivables from counterparties are generally comprised of collateralised receivables related to derivatives or collateralised agreements transactions and have minimal credit risk due to the value of the collateral received. In addition, Rothesay invests in assets that are typically highly rated, or assets where there is underlying structural security in the event of a default. These assets include supranationals, sovereign bonds, sub sovereign bonds, covered bonds, higher education bonds, infrastructure assets, unsecured corporate bonds and secured residential lending.

# Notes to the financial statements

**continued**

## Note F — Risk and capital management (continued)

***F.2.1 Credit risk (continued)***

***Credit exposures (continued)***

Further information is provided below:

**Cash and cash equivalents.** Cash and cash equivalents include both interest bearing and non-interest bearing deposits and investment in money market funds. To mitigate the risk of credit loss, Rothesay diversifies its exposure and places its deposits with multiple banks, typically with minimum ratings in the 'A' rating category. Rothesay only invests in 'AAA' rated money market funds.

**Reinsurance.** Long-term business is ceded to reinsurers under collateralised contracts to transfer part of the insurance risk associated with the underlying insurance contracts. The amounts that will be recoverable from reinsurers are estimated based upon the gross provisions, having due regard to collectability. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of the reinsurance company.

**Collateralised agreements.** Collateralised agreements are reported at fair value or contractual value before consideration of collateral received on the balance sheet. Rothesay bears credit risk related to sale and repurchase agreements and securities borrowing only to the extent that cash advanced to the counterparty exceeds the value of the collateral received or charges over assets. Therefore, Rothesay's credit exposure on the transactions is significantly lower than the amounts recorded on the balance sheet. Rothesay also has credit exposure on repurchase agreements and securities loaned, which are liabilities on its consolidated statement of financial position, to the extent that the collateral pledged for these transactions exceeds the amount of cash received.

The following table identifies derivatives and collateralised agreements covered by enforceable netting arrangements (netting under master netting agreements, cash collateral and security collateral) which do not qualify for netting under IAS 32. We have excluded all other assets as we feel the presentation below increases clarity of the disclosure. 2019 comparatives have been restated accordingly.

| | | 2020 | | | |
|---|---|---|---|---|---|
| | | Related amounts not offset | | | |
| | Financial assets presented in the statement of financial position £m | Netting under master netting agreements £m | Cash collateral £m | Security collateral and charges £m | Net credit exposures £m |
| Derivative assets | **30,700** | **(26,173)** | **(865)** | **(3,595)** | **67** |
| Collateralised agreements and financing | **1,727** | **—** | **(104)** | **(1,623)** | **—** |
| **Total** | **32,427** | **(26,173)** | **(969)** | **(5,218)** | **67** |
| Derivative liabilities | **(30,359)** | **26,713** | **306** | **3,913** | **33** |
| Collateralised financing agreements | **(894)** | **—** | **—** | **894** | **—** |
| **Total** | **(31,253)** | **26,173** | **306** | **4,807** | **33** |

## Note F — Risk and capital management (continued)
### *F.2.1 Credit risk (continued)*
### *Credit exposures (continued)*

| | 2019 restated[1] | | | | |
|---|---|---|---|---|---|
| | | Related amounts not offset | | | |
| | Financial assets presented in the statement of financial position £m | Netting under master netting agreements £m | Cash collateral £m | Security collateral and charges £m | Net credit exposures £m |
| Derivative assets | 19,508 | (16,000) | (529) | (2,960) | 19 |
| Collateralised agreements and financing | 1,875 | — | (33) | (1,842) | — |
| **Total** | 21,383 | (16,000) | (562) | (4,802) | 19 |
| Derivative liabilities | (19,741) | 16,000 | 351 | 3,216 | (174) |
| Collateralised financing agreements | (879) | — | — | 879 | — |
| **Total** | (20,620) | 16,000 | 351 | 4,095 | (174) |

1 As at 31 December 2019 we have reclassified a financial liability of £203m from derivative financial instruments to collateralised financing agreements following a review of the classification of derivative contracts.

Credit default swaps have been purchased to protect Rothesay from the default of some of its counterparties. The table above does not reflect the protection provided. Rothesay calls margins, receivable in cash and gilt instruments, against this exposure and other derivative positions.

In a distressed situation the value of collateral may vary depending on credit quality and interest rates. The effectiveness of collateral as a credit risk mitigant will depend on the operational expertise of the collateral manager and the ability to seize, value and sell the collateral in a distressed scenario.

Rothesay has the right of offset for certain financial assets and liabilities. Netting under master netting agreements of £26,173m (2019: £16,000m) reflects the offsetting of derivative assets with liabilities for which Rothesay has a right to set off in the event of default. Cash and security collateral have been offset to the extent there are credit exposures on the balance sheet.

### *Credit ratings*
The table below shows Rothesay's credit exposure from financial investments (excluding derivatives), receivables and cash based on external and internal ratings, consistent with management's view of credit risk. The external rating is generally based on the median of the ratings assigned by Standard & Poor's, Moody's and Fitch. For the purpose of Solvency II, unrated assets are internally rated by Rothesay's independent credit risk function under a framework which has been externally validated. 2019 comparatives have been restated.

| | AAA £m | AA £m | A £m | BBB £m | BB £m | Unrated £m | Total £m |
|---|---|---|---|---|---|---|---|
| 2020 | **12,892** | **21,477** | **17,568** | **6,961** | **314** | **5,022** | **64,234** |
| 2019 | 14,600 | 17,882 | 14,004 | 5,905 | — | 3,011 | 55,402 |

# Notes to the financial statements
**continued**

## Note F — Risk and capital management (continued)
### *F.2.1 Credit risk (continued)*
### *Credit ratings (continued)*
We have excluded derivatives and other assets in the table as the derivatives are collateralised and we feel the presentation above increases clarity of the disclosure and corresponds more closely to the way in which we measure the credit risk. The difference between the total assets shown in the table above and the assets under management (APM) is:
- derivative assets of £30,700m (2019: £19,508m); and
- other assets of £710m (2019: £803m); less
- payables and financial liabilities of £33,607m (2019: £21,999m).

AAA rated assets include supranational bonds, sub sovereigns, covered bonds, US not-for-profit private universities and certificates of deposit. AA rated assets include gilts and corporate bonds. Other net credit exposures rated A and BBB include investments in regulated infrastructure assets and commercial real estate loans, as well as unsecured corporate bonds. One commercial real estate loan has been downgraded by Rothesay's credit risk team to BB under their cautious approach to internal ratings.

Unrated assets are UK and Dutch residential mortgages that are not individually rated.

Other than a small number of equity release mortgages, as of the current and prior year end there were no financial assets past due.

### *F.2.2 Market risk*
Market risk is the risk of changes in the value of Rothesay's net financial position due to changes in market prices. Financial investments are accounted for at fair value and, therefore, fluctuate on a daily basis. Certain liabilities are also exposed to market risk. Categories of market risk include the following:
- Interest rate risk arises from discounting cash flow mismatches across all future dates. Profits and losses are generated through changes in the level, slope and curvature of interest rate curves. The risk is hedged closely by matching assets and liabilities and by using interest rate swaps. Consideration is given to Rothesay's IFRS, MCEV and solvency risk positions when determining the appropriate hedging strategy.
- Inflation rate risk results from mismatches in the index linkage of liabilities and assets. Profits and losses are generated through changes to the level, slope and curvature of inflation curves. The risk is hedged by closely matching assets and liabilities and by using inflation swaps.
- Currency rate risk results from mismatches in the denomination of liabilities and assets. Profits and losses are generated due to changes in the level of foreign exchange rates. The risk is hedged using spot foreign exchange and cross currency swaps.
- Property risk results from investments that are secured on commercial or residential properties. Profits and losses may be generated by material movements in spot or forward property prices. This risk is mitigated through strict underwriting criteria, aggregated risk monitoring and low loan-to-value limits. Where the property risk becomes more material then prudent allowance is made for this within the credit risk adjustment.

Rothesay manages market risk by diversifying exposures, controlling position sizes through limits and regular stress and scenario testing and establishing economic hedges in related securities, derivatives and insurance liabilities.

Sensitivities to market risk are shown in note E.2 (f).

## Note F — Risk and capital management (continued)

### *F.2.3 Liquidity risk*

Liquidity risk arises where timing differences and/or uncertainties occur between cash inflows and cash outflows. The objective of liquidity management is to ensure that Rothesay is capable of honouring all cash flow commitments on both an ongoing basis and in highly stressed scenarios, without incurring significant cost or business disruption.

Rothesay's liquidity policy is designed to ensure the availability of sufficient funds to meet cash flow requirements on a timely basis via:

- Maintenance of substantial excess liquidity. Rothesay seeks to enter into long-term, illiquid investments that match its liabilities in order to maximise the value of the illiquidity premium. To mitigate residual liquidity risk, Rothesay maintains substantial excess liquidity to meet a broad range of potential cash outflows in a stressed environment including collateral outflows and financing obligations.
- Conservative asset/liability management. Rothesay seeks to maintain funding sources that are sufficiently long-term in order to withstand a prolonged or severe liquidity-stressed environment. Only the most liquid assets held on Rothesay's balance sheet are assumed to be available to meet potential stressed liquidity requirements.
- Maintenance of a comprehensive liquidity contingency plan.

The liquidity management framework is designed to ensure that a prudent level of liquidity is maintained on a spot basis, but also under stressed market conditions, at which time liquidity may leave Rothesay through collateral outflows and ongoing business obligations such as expenses and undrawn investments.
A comprehensive analysis of all sources of liquidity risk to which the Group is exposed is maintained. Based upon this analysis, an extensive suite of stresses is considered as part of the liquidity management framework, including onerous market shocks, against which limits are applied by the Board.

Management is responsible and accountable for managing liquidity risks within prescribed limits that are set by the Board and are overseen by the BRC. The second line Risk function ensures that an appropriate framework is in place for assessing, monitoring and managing liquidity risk. Liquidity is managed for Rothesay as a whole, in addition to at a Solvency II fund level. Risks are monitored and controlled through strong oversight and independent control and support functions across the business.

The following table details Rothesay's financial liabilities and assets by contractual maturity including interest that was accrued where Rothesay is entitled to repay the liability before its maturity. Financial assets and liabilities are presented at their fair value (with the exception of receivables, cash, accrued interest and borrowings) as this is consistent with the values used in the liquidity risk management of these instruments. The table excludes insurance liability and reinsurance cash flows, totals of which are included in note E.2. The table also excludes equity release mortgage cash flows which are included in note D.1 and leasehold cash flows which are included in note I.5.

# Notes to the financial statements
**continued**

## Note F — Risk and capital management (continued)
### *F.2.3 Liquidity risk (continued)*

| | 2020 | | | |
|---|---|---|---|---|
| | **Less than 1 year £m** | **1 to 5 years £m** | **Over 5 years £m** | **Total £m** |
| **Financial assets** | | | | |
| Financial investments | **5,641** | **5,947** | **77,902** | **89,490** |
| Accrued income and prepayments | **663** | **—** | **—** | **663** |
| Receivables | **914** | **15** | **—** | **929** |
| Cash and cash equivalents | **293** | **—** | **—** | **293** |
| | **7,511** | **5,962** | **77,902** | **91,375** |
| **Financial liabilities** | | | | |
| Financial liabilities | **(895)** | **(1,554)** | **(28,804)** | **(31,253)** |
| Payables | **(2,354)** | **—** | **—** | **(2,354)** |
| Borrowings | **—** | **(249)** | **(1,177)** | **(1,426)** |
| Accruals and deferred income | **(72)** | **—** | **—** | **(72)** |
| | **(3,321)** | **(1,803)** | **(29,981)** | **(35,105)** |
| **Net** | **4,190** | **4,159** | **47,921** | **56,270** |

| | 2019 | | | |
|---|---|---|---|---|
| | Less than 1 year £m | 1 to 5 years £m | Over 5 years £m | Total £m |
| **Financial assets** | | | | |
| Financial investments | 6,589 | 6,183 | 58,301 | 71,073 |
| Accrued income and prepayments | 755 | — | — | 755 |
| Receivables | 905 | — | — | 905 |
| Cash and cash equivalents | 263 | — | — | 263 |
| | 8,512 | 6,183 | 58,301 | 72,996 |
| **Financial liabilities** | | | | |
| Financial liabilities | (281) | (1,499) | (18,840) | (20,620) |
| Payables | (1,379) | — | — | (1,379) |
| Borrowings | (100) | — | (1,327) | (1,427) |
| Accruals and deferred income | (80) | — | — | (80) |
| | (1,840) | (1,499) | (20,167) | (23,506) |
| **Net** | 6,672 | 4,684 | 38,134 | 49,490 |

***Note F — Risk and capital management (continued)***
### *F.2.4 Operational risk*
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Rothesay manages operational risk through the development and maintenance of an effective risk management framework which ensures that a comprehensive internal control environment is in place. This is supported by regular risk and control self-assessments coordinated, challenged and reported by the second line, which allow risk levels to be measured and control enhancements to be developed in line with Rothesay's risk appetite.

Rothesay also uses scenario analysis to explore key areas of operational risk, ensuring that the implications of adverse operational risk events crystallising are well understood and that, where appropriate, additional controls or contingency plans are introduced to improve operational resilience.

Rothesay has important outsourcing arrangements in place, which are subject to extensive due diligence at the point of entering into them, but also to ongoing review, with oversight provided by the Third Party Oversight Committee. Oversight of these arrangements considers the information security risk that Rothesay is exposed to, the performance of the third party with respect to service level agreements, and other relevant information (e.g. their ongoing creditworthiness, and where relevant, their readiness to accommodate Rothesay's growth).

The management of the operational risk associated with Brexit, the COVID-19 pandemic and the transition from LIBOR is discussed in the risk management section of the Strategic Report.

Operational risk also includes the risk of conduct failure — a risk that is managed by the Compliance function and overseen by the Customer and Conduct Committee.

### *F.2.5 Insurance risk*
Insurance risk is the risk of changes in the value of Rothesay's net position due to changes in the insurance contract liabilities. Insurance risk may occur either through changes in actual demographic experience or revised expectations of future experience. The main categories of insurance risk include the following:
- Demographic risk arises from current mortality or spouse/dependant experience being lighter than that assumed. The risk is hedged by external reinsurance.
- Longevity improvement risk represents the risk of future mortality rates improving at a faster rate than assumed. The risk is hedged by external reinsurance.
- Expense risk results from future expenses required to maintain the business being higher than expected. This risk is managed through budgeting and robust expense management.

As at 31 December 2020 87% of longevity risk was reinsured (2019: 78%). Risks are monitored and controlled by the actuarial function and overseen by the Chief Actuary and the risk function.

# Notes to the financial statements
**continued**

## Note G — Other statement of consolidated financial position notes
### *G.1 Deferred tax assets*

*Deferred income tax is provided using the liability method on temporary differences at the financial statement date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.*

*Deferred income tax and liabilities are recognised for all taxable temporary differences except:*
- *when the deferred income tax liability arises from the initial recognition of goodwill or from an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit or loss nor taxable profit or loss; and*
- *in respect of taxable temporary differences associated with investments in subsidiary undertakings, associates and interests in joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.*

*The carrying amount of deferred income tax assets is reviewed at each financial reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each financial reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.*

*Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the financial reporting date.*

*Deferred income tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred income tax relates to the same taxable entity and the same taxation authority.*

Deferred tax balances comprise:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Temporary differences between the financial statements and the tax deductions | **5** | 2 |
| **Total temporary differences** | **5** | 2 |

The movements in the deferred tax balances were as follows:

| | **2020 £m** | 2019 £m |
|---|---|---|
| At 1 January | **2** | 1 |
| Timing difference | **3** | 1 |
| **At 31 December** | **5** | 2 |

Deferred tax assets are only recognised to the extent that, based on management's assessment, they are regarded as recoverable.

## Note H — Interests in subsidiaries and associates

### *H.1 Investment in unconsolidated structured entities*

Rothesay has interests in investments which are classified under IFRS as unconsolidated structured entities. A structured entity is an entity that has been designed so that voting or similar rights are not the dominating factor in deciding who controls the entity, such as when voting rights might relate to administrative tasks only and the relevant activities are directed by means of contractual arrangement. Structured entities include those entities that have restricted activities or a narrow and well-defined objective. These structured entities have not been consolidated as Rothesay does not have the power to affect their returns.

Rothesay has interests in unconsolidated structured entities as described below:
- loans granted to and notes issued by special purpose vehicles (SPVs) secured by the assets held by the SPV such as commercial or residential real estate;
- debt securities issued by SPVs secured by financial receivables; and
- loans granted to SPVs secured by financial receivables.

As at 31 December 2020, our total interest in such entities, reflected on Rothesay's statement of financial position and classified as financial investments held at fair value through profit or loss, was £7,314m (2019: £7,555m). The recorded fair value represents Rothesay's maximum loss exposure to these unconsolidated structured entities. The £241m decrease in the balance was predominantly driven by a loan repayment.

The interest income recognised in relation to these investments was £184m (2019: £153m).

A summary of Rothesay's interest in unconsolidated structured entities is provided below:

| | **2020 £m** | 2019 £m |
|---|---|---|
| Government sub sovereign and agency obligations | **53** | 63 |
| Corporate bonds and other corporate debt | **1,503** | 1,545 |
| Loans secured on property | **5,758** | 5,947 |
| **Total** | **7,314** | 7,555 |

### *H.2 Investments in subsidiaries*

The financial statements include the financial statements of Rothesay Limited and the subsidiaries listed in the following table:

| **Group undertakings** | **Country of incorporation** | **Primary business operation** | **2020 £m** | 2019 £m | **2020 % equity interest** | 2019 % equity interest |
|---|---|---|---|---|---|---|
| Rothesay Pensions Management Limited | UK | Service company | **11** | 22 | **100%** | 100% |
| Rothesay Life Plc (formerly known as Rothesay Life Limited) | UK | Life insurance | **2,464** | 2,464 | **100%** | 100% |
| Rothesay Assurance Limited (formerly known as MetLife Assurance Limited) | UK | Service company | **—** | — | **100%** | 100% |
| LT Mortgage Financing Limited | UK | Service company | **6** | 5 | **100%** | 100% |
| Rothesay MA No.1 Limited | UK | Service company | **5** | 5 | **100%** | 100% |
| Rothesay MA No.2 Limited | UK | Service company | **—** | — | **100%** | 100% |
| Rothesay MA No.3 Limited | UK | Service company | **2** | — | **100%** | 100% |
| Rothesay MA No.4 Limited | UK | Service company | **—** | — | **100%** | 100% |
| Rothesay Asset Management UK Limited | UK | Service company | **5** | 5 | **100%** | 100% |
| Rothesay Asset Management US LLC | US | Service company | **5** | 5 | **100%** | 100% |

Subsidiaries are held at the lower of cost and net realisable value.

# Notes to the financial statements
**continued**

## Note H — Interests in subsidiaries and associates (continued)
### *H.2 Investments in subsidiaries (continued)*
The above subsidiary undertakings, with the exception of Rothesay Asset Management US LLC, are registered in the United Kingdom. The registered office and principal place of business for all UK subsidiary undertakings, except Rothesay Assurance Limited, is The Post Building, 100 Museum Street, London WC1A 1PB. The registered address of Rothesay Assurance Limited is 55 Baker Street, London W1U 7EU.

Rothesay Asset Management US LLC is registered in Delaware, United States of America. The registered office is Corporate Trust Center, 1209 Orange Street, Wilmington, Delaware 19801, New Castle County.

Rothesay MA No.2 Limited was incorporated during March 2019. Rothesay MA No.4 Limited was incorporated during November 2019. Both entities remain dormant.

Rothesay MA No.3 Limited was incorporated during November 2019 and began trading in December 2020.

On 3 October 2016, the PRA granted an application to cancel the permissions of Rothesay Assurance Limited. As it is now no longer needed, steps have been taken to remove it from Rothesay, and the company was placed into members' voluntary liquidation on 4 June 2019. The company will be dissolved once the liquidation is completed.

During October 2019 Rothesay established a charitable foundation, the Rothesay Foundation; this entity is not incorporated into the consolidated financial statements as the charity is controlled by its trustees rather than Rothesay Limited or the Group.

## Note I — Other notes

### *I.1 Company loss*

The loss for the financial year of the Company was £7m (2019: loss of £7m). As permitted by Section 408 of the Companies Act 2006, the Company's statement of comprehensive income has not been included in these financial statements.

### *I.2 Share-based payments*

*Historically the cost of equity-based transactions with employees has been measured based on grant-date sale value.*

*The fair value was determined at grant date and expensed on a straight-line basis over the vesting period in profit and loss. At each reporting date Rothesay revised its estimate of the number of shares that were expected to be issued and recognised the impact of the revision of original estimates.*

*During December 2020, Rothesay amended its remuneration policy in relation to the deferred equity award plan (previously known as the Long Term Stock Incentive Plan) to give employees the choice of receiving cash or equity for vestings from December 2021 onwards. For these awards, the fair value of the grant will now be reassessed at each reporting period and any change charged to the profit and loss.*

*Share-based employee awards that require future services are amortised over the relevant service period. Expected forfeitures are included in determining share-based employee compensation expenses.*

During the year ended 31 December 2015, Rothesay created a stock incentive plan, now known as the deferred equity award plan which provided for grants of restricted stock units (RSUs).

Rothesay issued RSUs to the employees under the deferred equity award plan, primarily in connection with year-end compensation. These RSUs vest and deliver as outlined in the applicable RSU agreements. Vesting is subject to the recipient not having left employment or having left employment as a result of death, permanent illness or redundancy. Delivery of the RSUs is in the form of shares or an equivalent amount of cash (subject to the approval of the Remuneration Committee). All RSUs have a future service requirement.

The activity related to the deferred equity award plan RSUs is set out below:

| | **2020 No. of RSUs** | 2019 No. of RSUs |
|---|---|---|
| Outstanding at the beginning of the year | **15,122,186** | 15,452,083 |
| Forfeited during the year | **(23,030)** | (329,612) |
| Vested during the year | **(5,211,453)** | (4,553,187) |
| Granted during the year | **4,159,213** | 4,552,902 |
| **Outstanding at the end of the year** | **14,046,916** | 15,122,186 |

On 3 March 2020, the Company established a new HMRC-approved employee share plan known as the Employee Share Incentive Plan (ESIP). Under the ESIP, Rothesay offered shares to all eligible UK employees as part of year-end compensation. The rules governing withdrawal of the shares from the ESIP Trust and subsequent tax treatment are set by HMRC. They are disclosed as employee scheme shares until they are withdrawn. The ability to withdraw shares is generally subject to the recipient not having left employment before three years from grant date.

# Notes to the financial statements

**continued**

## Note I — Other notes (continued)

### *I.2 Share-based payments (continued)*

The activity related to the ESIP RSUs is set out below:

| | **2020 No. of RSUs** | 2019 No. of RSUs |
|---|---|---|
| Outstanding at the beginning of the year | **—** | — |
| Forfeited during the year | **(3,600)** | — |
| Vested during the year | **—** | — |
| Granted during the year | **226,800** | — |
| **Outstanding at the end of the year** | **223,200** | — |

Historically, the fair value of RSUs was determined by taking 100% of Rothesay's MCEV and dividing by the number of ordinary shares. The weighted average fair value of the RSUs at 31 December 2019 was £3.90. During 2020 the methodology for calculating the fair value of the RSUs was amended to give a price consistent with the price paid by MassMutual and GIC for Blackstone's shareholding. The weighted average fair value of the RSUs at 31 December 2020 was £4.00.

### *Share appreciation plan*

During December 2020 a new long-term share appreciation plan (the SARs plan) was created which provides for grants of cash-settled share appreciation rights (SARs). The SARs provide the right to receive the upside on a fixed proportion of an agreed value of Rothesay shares over a defined time horizon, paid out in cash, subject to achievement of returns above an agreed hurdle. The SARs will be awarded for the first time during 2021 and vest and deliver as outlined in the applicable agreement. Vesting is subject to the recipient not having left employment or having left employment as a result of death, permanent illness or redundancy. All SARs have a future service requirement.

The valuation of the SARs will be based on an option pricing model.

### *Expenses in relation to share-based payment schemes*

Expenses of £15m (2019: £10m) have been charged to the profit and loss of Rothesay during the year in relation to the various share-based payment schemes. The year-on-year increase includes £2m which arises from the change in remuneration policy and associated change in accounting.

### *I.3 Related parties disclosures*

### Ultimate holding companies

Based on the percentage nominal share capital owned, the shareholdings of Rothesay's institutional investors are as follows:

- GIC Private Limited: 49%
- MassMutual Financial Group: 49%

The remaining percentage is owned by the Directors, management, employees, the Trust and the ESIP Trust (see note C.1).

## Note I — Other notes (continued)
### *I.3 Related parties disclosures (continued)*
### *Related party transactions*
Rothesay entered into various transactions with fellow participating interests which are subject to common control from the same source. No changes to the table below are required as a result of the change in ownership.

| | **2020 £m** | 2019 restated[1] £m |
|---|---|---|
| **Statement of comprehensive income** | | |
| Change in the reinsurers' share of insurance contract liabilities and reinsurance recoveries | **115** | 48 |
| Finance costs | **(21)** | (26) |
| Operating expenses | **(8)** | (8) |
| **Statement of financial position** | | |
| Reinsurance liabilities | **159** | 44 |
| Borrowings | **298** | 398 |
| Capital | **1,548** | 1,548 |

1 As at 31 December 2019, both change in reinsurers' share of insurance contract liabilities and reinsurance liabilities have been restated to reflect the correct position due to omission of a contract during the prior period. The change in reinsurers' share has changed from a charge of £2m to a credit of £48m. The reinsurance liabilities have increased from £6m to £44m.

### *Transactions with key management personnel*
Key management personnel comprise the Directors of the Company, Directors of subsidiary undertakings and certain members of senior management.

There are no material transactions between Rothesay and its key management personnel other than transactions discussed below:

| | **2020 £m** | 2019 restated[2] £m |
|---|---|---|
| Salaries, bonus and other employee benefits | **20** | 23 |
| Equity-based compensation payments | **8** | 6 |
| Total transactions | **28** | 29 |

2 As at 31 December 2019 key management personnel has been restated to include independent Non-Executive Directors in line with our definition of Directors being key management personnel. This resulted in an increase in 2019 salaries from £21m to £23m.

On 19 March 2020, members of key management personnel and their families sold new B ordinary shares to the Employment Benefit Trust for consideration of £8.1m.

On 1 December 2020, members of key management personnel and their families sold 18,766,215 new B ordinary shares to GIC, MassMutual and the Employment Benefit Trust for consideration of £69.7m, £25.3m of which is deferred for one year. They also sold 73,500,000 H shares to GIC and MassMutual for consideration of £176.2m, £88.4m of which is payable over three years from 2021 to 2023.

# Notes to the financial statements
**continued**

## Note I — Other notes (continued)
### *I.3 Related parties disclosures (continued)*
On 4 April 2019, members of key management personnel and their families sold new B ordinary shares to the Employee Benefit Trust for consideration of £7.8m.

The tables below represent transactions between Rothesay Limited and its subsidiaries RPML, RAM UK and RLP.

| Transactions with RPML | 2020 £m | 2019 £m |
|---|---|---|
| **Statement of financial position** | | |
| Other receivables | — | 8 |
| Other payables | 11 | 3 |
| Capital | 11 | 22 |

| Transactions with RLP | 2020 £m | 2019 £m |
|---|---|---|
| **Statement of comprehensive income** | | |
| Cost transfer | (5) | (5) |
| **Statement of financial position** | | |
| Other payables | 41 | 13 |
| Capital | 2,464 | 2,464 |

| Transactions with Rothesay Asset Management UK | 2020 £m | 2019 £m |
|---|---|---|
| Capital | 5 | 5 |

### Transactions with LT Mortgage Financing Ltd
In 2018, £1.3bn of ERMs were transferred from RLP to its subsidiary LT Mortgage Financing Limited (LTMF). During 2019 and 2020, a further £0.6bn and £1.2bn respectively of ERMs were transferred. In each case, LTMF became the beneficial owner in the ERMs in exchange for the issue of loan notes. These transactions took place on an arm's length basis using the fair value of the equity release mortgages. Under IAS 39 the loans cannot be derecognised from the Company as RLP effectively maintains all the risk and rewards and control of the mortgages after the securitisations through the loan notes. For the purposes of determining the valuation rate of interest under IFRS 4, these securitisations are ignored.

### Transactions with Rothesay MA No.1 Limited
During December 2018, £778m of ground rent loans were transferred from RLP to its subsidiary Rothesay MA No.1 Limited (RMA1). RMA1 became the beneficial owner in the ground rent loans in exchange for the issue of loan notes. These transactions took place on an arm's length basis using the fair value of the ground rent loans. Under IAS 39 the loans cannot be derecognised from the Company as RLP effectively maintains all the risk and rewards and control of the loans after the securitisations through the loan notes. For the purposes of determining the valuation rate of interest under IFRS 4, this securitisation is ignored.

### Transactions with Rothesay MA No.3 Limited
During December 2020, €0.5bn of Dutch mortgage loans were transferred from RLP to its subsidiary Rothesay MA No.3 Limited (RMA3). RMA3 became the beneficial owner in the Dutch mortgage loans in exchange for the issue of loan notes. These transactions took place on an arm's length basis using the fair value of the Dutch mortgages. Under IAS 39 the loans cannot be derecognised from the Company as RLP effectively maintains all the risk and rewards and control of the mortgages after the securitisations through the loan notes. For the purposes of determining the valuation rate of interest under IFRS 4, this securitisation is ignored.

## Note I — Other notes (continued)

### *I.4 Financial commitments and contingencies*

### Lease commitment

From 1 January 2019, IFRS 16 Leases became effective. IFRS 16 replaced the guidance in IAS 17. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet).

IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a right of use asset for virtually all lease contracts (see note I.5). The new standard has affected the balance sheet and related ratios.

Rothesay relocated its UK-based operations to The Post Building during the second half of 2019 in order to accommodate the growth of the business. As a result:

- Rothesay has entered into a lease for space in The Post Building, which has been accounted for under IFRS 16 (see note I.5).
- Rothesay exercised its break clause under the lease for Level 25 of The Leadenhall Building. The cash flows for 2019 were therefore accounted for on a cash flow basis. There have been no future cash flows in relation to this lease.
- Rothesay identified a new tenant for Level 32 of The Leadenhall Building and therefore terminated the lease. The cash flows for 2019 were therefore accounted for on a cash flow basis. There have been no future cash flows in relation to this lease.

### Other commitments

During previous years Rothesay executed transactions to purchase partly funded bonds and forward settling bonds. During 2020 Rothesay purchased additional partly funded bonds and forward settling bonds. Rothesay also signed up to a number of multi-year contracts. Rothesay expects to pay a further £999m within the next five years (2019: £1,043m), £561m of this being due within 12 months of the financial reporting date (2019: £436m).

| | **2020 £m** | 2019 £m |
|---|---|---|
| Not later than one year | **561** | 436 |
| Later than one year and no later than five years | **438** | 607 |
| Later than five years | **—** | — |
| **Total other commitments** | **999** | 1,043 |

### *I.5 Leases*

### a) Amounts included in the statement of financial position

On adoption of IFRS 16, Rothesay recognised lease liabilities on the lease on the new premises entered into during May 2019, which would previously have been classified as ‘operating leases’ under the principles of IAS 17 Leases.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments, less any lease incentives receivable;
- amounts expected to be payable by Rothesay under residual value guarantees;
- payments of penalties for terminating the lease; and
- lease payments to be made under reasonably certain extension options.

# Notes to the financial statements
**continued**

## Note I — Other notes (continued)
### *I.5 Leases (continued)*
Lease payments are discounted using Rothesay's incremental borrowing rate of 3.374%. The incremental borrowing rate represents the cost of funding to Rothesay at the date that the lease was entered into.

Lease payments are allocated between principal and finance cost. The finance cost is charged to the statement of income over the lease period so as to produce a constant rate of interest on the remaining balance of the liability for each period.

Right of use assets are measured at cost comprising the following:
- amount of any initial measurement of lease liability;
- leased payments made before the commencement date less any lease incentives received;
- initial direct costs; and
- restoration costs.

Right of use assets are depreciated over the lease term on a straight-line basis.

Rothesay did not have any leases previously classified as finance leases that would be impacted by measurement adjustments for adoption of IFRS 16.

Additions to the right of use asset recognised by Rothesay in prior year relate to the lease on the new UK office which was executed in May 2019, therefore there was a nil balance at 1 January 2019. The lease for The Post Building has a duration of 17 years with a break clause at 12 years which we have assumed is exercised.

Rothesay's right of use asset also includes a lease on our US office which was executed in May 2019. Rothesay was not a lessor during the period.

### *Right of use assets*

| | **2020 £m** | 2019 £m |
|---|---|---|
| Right of use asset | **34** | 37 |
| Right of use asset — property | | |
| Balance at 1 January | **37** | — |
| Depreciation charge for the period | **(3)** | (2) |
| Additions | **—** | 39 |
| **Closing balance at 31 December** | **34** | 37 |

### *Lease liabilities*

| | **2020 £m** | 2019 £m |
|---|---|---|
| **Lease liability** | **40** | 39 |
| Maturity analysis based on undiscounted liabilities | | |
| **Current liabilities:** | | |
| Less than one year | **—** | — |
| **Non-current liabilities:** | | |
| One to five years | **22** | 16 |
| More than five years | **20** | 33 |
| **Total undiscounted lease liabilities** | **42** | 49 |

## Note I — Other notes (continued)

### *I.5 Leases (continued)*

### (b) Amounts recognised in the statement of comprehensive income

| | 2020 £m | 2019 £m |
|---|---|---|
| Depreciation charge of right of use assets — property | **3** | 2 |
| Financing charge on lease liabilities (included in note B.4 Finance costs) | **1** | 1 |

### (c) Amount recognised in statement of cash flows

| | 2020 £m | 2019 £m |
|---|---|---|
| Depreciation charge of right of use assets — property | **3** | 2 |
| Financing charge on lease liabilities | **1** | 1 |
| Total cash flows for leases | **—** | 1 |

# Alternative Performance Measures (unaudited)

As noted on page 30, throughout the financial statements Rothesay has used a variety of measures to provide stakeholders with the necessary information on the performance and financial position of Rothesay. Where it is possible to reconcile to the financial statements this has been referenced, however some of these measures are not on a consistent basis with IFRS and therefore the methodology is explained in the table below. Where relevant, we have used accounting policies and assumptions that are consistent with the IFRS financial statements.

| Alternative Performance Measure | Definition | Why is this meaningful | Reconciliation to IFRS |
|---|---|---|---|
| **Assets under management** | Assets adjusted for reinsurance, derivatives and collateralised financing. | By netting down the derivative gross up Rothesay provides a more meaningful value for the assets managed and a useful measure of the size of the business. | A full reconciliation is provided in the financial review on page 32. |
| **Market consistent embedded value (MCEV)** | The risk-adjusted value of the in-force business, allowing for the unwind of IFRS margins and cost of capital. | Rothesay considers that embedded value reporting provides investors with a useful measure of the future profit streams of Rothesay's long-term business. | The shareholders' equity on an MCEV basis is consistent with the sum of the shareholders' equity on an IFRS basis on page 103 plus the value of in-force business reduced by debt valuation on an MCEV basis. |
| **New business premiums** | Premiums paid on new business transacted during the period and adjustments to new business premiums from prior periods. | New business premiums are a key indicator of the growth of the business. | New business premiums are a subset of gross written premiums and are made up of premiums paid on new business transacted in the period and premium adjustments from prior periods provided in note B.1. |
| **Own Funds** | Available capital under the Solvency II regime. | Provides a measure of regulatory capital. | A reconciliation of Own Funds to IFRS equity is provided in note F.1. |
| **Solvency capital requirement (SCR)** | Under Solvency II, capital requirement to withstand a 1-in-200-year event. | Provides a measure of risk exposure of Rothesay. | It would not be possible to reconcile the SCR to the IFRS financial statements. |
| **SCR coverage %** | Own Funds (capital in excess of technical provisions) divided by the SCR and expressed as a percentage. | Provides a measure of the financial strength of Rothesay. | It would not be possible to reconcile the SCR to the IFRS financial statements. |

| Alternative Performance Measure | Definition | Why is this meaningful | Reconciliation to IFRS |
|---|---|---|---|
| **Longevity reinsurance %** | The longevity reinsurance percentage provides an indication of the extent to which Rothesay is protected from fluctuations in longevity through reinsurance. | Demonstrates how Rothesay has mitigated exposure to longevity fluctuations through reinsurance. | The longevity reinsurance percentage is derived from the IFRS sensitivity (see note E.2.f) to changes in assumed longevity. |
| **Customer satisfaction** | Policyholder feedback surveys are sent to all policyholders following interaction with them (apart from complaints and bereavement). | Rothesay prides itself on the quality of the service that it provides and this APM provides a measure of the quality of that service. | It would not be possible to reconcile to the IFRS financial statements. |
| **Complaints received and upheld** | The number of complaints received and upheld per 1,000 policyholders. | Complaints provide a useful indication of customer (dis)satisfaction. | It would not be possible to reconcile to the IFRS financial statements. |
| **Operating profit before tax** | Gross IFRS profit less the impact of market fluctuations, exceptional expenses and financing costs. | Measure of longer-term profitability designed to remove the distorting impact of market fluctuations and exceptional expenses. | The operating profit before tax measure involves apportioning the items in the income statement across the various drivers of profit. When taken together with the other items in the alternative analysis of profit generation, the items can be reconciled to the IFRS financial statements. See page 30. |
| **New business profit** | IFRS new business profit projected to be realised once the premium is invested according to Rothesay's long-term investment strategy, before release of IFRS margins. | This is one of the metrics used by Rothesay when underwriting new business. | New business profit is calculated on an IFRS basis by comparing the premium received with the insurance liabilities taken on. The discount rate used in calculating the insurance liabilities assumes full investment of premiums according to the Rothesay’s long-term investment strategy. When taken together with the other items in the alternative analysis of profit generation, the items can be reconciled to the IFRS financial statements. See page 30. |

# Alternative Performance Measures (unaudited)
**continued**

| Alternative Performance Measure | Definition | Why is this meaningful | Reconciliation to IFRS |
|---|---|---|---|
| **Impact of temporary investment delay** | The difference between new business profit on a fully invested basis and the new business profit actually achieved by the reporting date. | When taken with the new business profit, this provides an indication of new business profit achieved by the reporting date. | Impact of temporary investment delay is calculated on an IFRS basis by comparing new business profit with the new business profit calculated using the discount rate derived from the investments held. When taken together with the other items in the alternative analysis of profit generation, the items can be reconciled to the IFRS financial statements. See page 30. |
| **Investment profit from prior year** | IFRS profits from investment of prior year premiums. | Shows the extent to which prior year temporary investment delays have been reversed. | Calculated by considering profits generated from investment of assets received as premiums in prior years as a result of the impact on the discount rate. Any profits made from investment in excess of those disclosed in prior years as the impact of temporary investment delay would offset the current year's impact of temporary investment delay (if applicable). See page 30. |

| Alternative Performance Measure | Definition | Why is this meaningful | Reconciliation to IFRS |
|---|---|---|---|
| **Performance of in-force book** | Profits or losses generated on the in-force book of business. | Provides a more granular analysis of financial performance. | Calculated by considering the net movement in assets and liabilities that can be attributed to:<br>• the release of prudent margins as the business runs off (including credit default allowances and expense reserves) and as members exercise their options;<br>• the impact of actual demographic experience versus assumptions;<br>• and the investment return on surplus assets.<br><br>When taken together with the other items in the alternative analysis of profit generation, the items can be reconciled to the IFRS financial statements. See page 30. |
| **Non-economic assumption changes and model refinement** | Profits or losses generated as a result of non-economic assumption changes and model refinement. | Provides a more granular analysis of financial performance. | See note E.2. |

# Alternative Performance Measures (unaudited)

**continued**

| Alternative Performance Measure | Definition | Why is this meaningful | Reconciliation to IFRS |
|---|---|---|---|
| **Economic profits** | Profits or losses generated as a result of changes in economic conditions. | Provides a more granular analysis of financial performance. | Calculated by considering the net change in assets and liabilities attributable to changes in economic conditions allowing for the cost of hedging. Changes in economic conditions include movements in interest rates, inflation, exchange rates, credit spreads, credit default allowances, actual defaults and property prices.<br><br>The release of credit default allowances over time is included in the performance of the in-force book. When taken together with the other items in the alternative analysis of profit generation, the items can be reconciled to the IFRS financial statements. See page 30. |
| **Value of new business on an MCEV basis** | The risk-adjusted value of the business written in the period, allowing for the unwind of margins and cost of capital. | This provides a measure of the profitability of new business once all margins have been released. | It is not possible to reconcile to the IFRS financial statements. |

# Glossary of terms (unaudited)

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| **Acquisition costs** | Acquisition costs comprise the expenses associated with the origination of new business, including annual compensation for employees. |
| **Administration expenses — recurring** | Administration costs (shown in note B.3) represent the cost of administering the in-force book of business. They include both outsourcing costs and other costs incurred by Rothesay. |
| **Annuity** | A series of regular payments made to an individual until their death. Payments may be indexed. |
| **Assets under management** | See Alternative Performance Measures. |
| **Best estimate liability (BEL)** | The liabilities of Rothesay calculated on a best estimate basis under Solvency II, i.e. where all the assumptions made in the calculation are best estimate. |
| **Bid price** | A bid price is the price a buyer is willing to pay for a security. |
| **Borrowing costs** | Interest payable on borrowings. This is a subset of the finance costs shown in note B.4. |
| **Brexit** | The UK's withdrawal from the European Union. |
| **Bulk annuity** | A bulk annuity, sometimes referred to as a bulk purchase annuity, is a contract between a defined benefit pension scheme and an insurance company, whereby an insurance company insures some or all of the annuities being paid by the pension scheme. |
| **Buy-in** | Held as an asset of the pension scheme, a bulk annuity buy-in is a contract that covers all or some of the benefits for a subset of scheme members. The scheme retains responsibility for paying pensions to members but the contract protects the scheme against all risks relating to the insured benefits, for example longevity risk and inflation risk. |
| **Buy-out** | The bulk annuity buy-out is a contract that covers all of the benefits for all or a subset of scheme members. The insurer issues individual policies to members under which pensions are paid. Once all benefits are covered, the pension scheme can be wound up. |
| **Capital contribution reserve** | The capital contribution reserve relates to equity based compensation awards. |
| **Collateralised agreements/ investments** | Loans secured on property or other collateral. |
| **Collective investment schemes** | A way of investing money alongside other investors. |
| **Corporate bonds and other corporate debt** | These are debt securities issued by corporations which are not guaranteed by governments. |
| **Covered bonds** | Covered bonds are debt securities issued by a bank or mortgage institution and collateralised against a pool of assets. |

# Glossary of terms (unaudited)

**continued**

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| **Credit risk** | The risk of loss or of adverse change in the financial situation resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors. |
| **Currency rate risk** | The risk that asset or liability values, cash flows, income or expenses will be affected by changes in exchange rates. Also referred to as foreign exchange risk. |
| **Customer satisfaction** | See Alternative Performance Measures. |
| **Deferred annuities** | Annuities or pensions due to be paid from a future date or when the policyholder reaches a specified age. |
| **Demographics** | Statistical data relating to the population and particular groups within it. |
| **Distributable profits** | A company's profits available for distribution are its accumulated realised profits. |
| **Economic profits** | See Alternative Performance Measures. |
| **Employee benefit trust (EBT)** | A trust established to purchase and hold shares of the Company for delivery under employee share schemes. |
| **Employee Share Incentive Plan (ESIP) Trust** | A trust established to purchase and hold shares of the Company for delivery under a HMRC-approved employee share schemes. |
| **Equity-based compensation** | Share-based transactions awarded under incentive plans. |
| **Equity release mortgages (ERMs)** | Mortgages extended to older customers (aged 55 and over) against their residential property at low loan-to-value percentage. Unlike a typical residential mortgage, no interest is paid monthly by the customer. Instead, the interest is simply added to the principal loan amount with the loan only repayable on death or entry into long-term care of the last remaining homeowner. |
| **Fair value** | Amount that would be received on sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. |
| **Finance costs** | Represent interest payable on borrowings. |
| **Full internal model** | Under Solvency II, insurer's own model used to calculate the solvency capital requirement in relation to particular risks approved by the PRA. |
| **Government, sub sovereign and agency obligations** | A bond issued by a country's government or corporate debt which is guaranteed by a government to repay borrowed money at a specific time. |
| **Gross premiums written** | Premiums received by RLP on new business and generated through regular premiums. |
| **In-force** | An insurance policy or contract reflected on records that has not expired, matured or otherwise been surrendered or terminated. |

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| **Infrastructure** | Investments in infrastructure such as water, energy and transportation. |
| **Insurance risk** | The risk of loss or of adverse change in the value of insurance liabilities, due to inadequate pricing and provisioning assumptions. |
| **International Financial Reporting Standards (IFRS)** | Accounting standards that are applied in preparing Rothesay's consolidated financial statements. |
| **Investment profit from prior year** | See Alternative Performance Measures. |
| **Investment return** | Comprises all interest income on financial investments at fair value through profit and loss, realised investment gains and losses and movements in unrealised gains and losses, as well as expenses directly related to investments executed during the year. |
| **LIBOR** | LIBOR, the acronym for London Interbank Offer Rate, is the global reference rate for unsecured short-term borrowing in the interbank market and is due to be phased out at the end of 2021. |
| **Liquidity premium** | An addition to the risk-free rate used when projecting investment returns and discounting cash flows on certain types of contracts where the liabilities are illiquid and have cash flows that are predictable. |
| **Liquidity premium adjustment** | In calculating the MCEV, liabilities are discounted using the risk-free rate plus a liquidity premium adjustment, designed to capture the component of yield on a portfolio of assets that is attributable to liquidity rather than credit risk. |
| **Liquidity risk** | The risk of being unable to realise investments and other assets in order to settle financial obligations when they fall due. |
| **Longevity reinsurance (%)** | See Alternative Performance Measures. |
| **Longevity risk** | The risk that a company could be exposed to a higher payout as a result of increasing life expectancy. |
| **LTMF** | LT Mortgage Financing Limited. |
| **Market consistent embedded value (MCEV)** | See Alternative Performance Measures. |
| **Market risk** | The risk of loss or of adverse change resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. |
| **Matching adjustment** | The matching adjustment, a concept in Solvency II, is broadly equivalent to the illiquidity premium that can be earned on the illiquid assets held to back illiquid liabilities. |
| **Mortality tables** | A table which shows for each age, what the probability is that a person of that age and gender will die before their next birthday. |

# Glossary of terms (unaudited)

**continued**

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| **Net premiums** | Life insurance premiums, net of reinsurance premiums paid to third party reinsurers. |
| **Net worth** | Under MCEV, the value of equity plus the value of borrowings on an IFRS basis. |
| **New business** | New insurance contracts and reinsurance inwards sold during the period. Includes business acquired through purchase of companies. |
| **New business premium** | See Alternative Performance Measures. |
| **New business profit** | See Alternative Performance Measures. |
| **No negative equity guarantee (NNEG)** | ERMs provide what is known as a NNEG, which means that the mortgage repayment amount (loan principal plus interest on redemption) cannot exceed the sale proceeds of the property on which the loan is secured. |
| **Non-recurring and project expenditure** | Administration – project and other one-off expenses (see note B.3). |
| **Offer price** | Price at which a market maker is prepared to sell a specific security. |
| **Operating profit before tax** | See Alternative Performance Measures. |
| **Operational risk** | The risk arising from inadequate or failed internal processes, personnel or systems, or from external events. |
| **Own Funds** | See Alternative Performance Measures. |
| **Own risk and solvency assessment (ORSA)** | An assessment of the risk to which the business is exposed as well as solvency forecasting in a range of scenarios, including consideration of the stresses that could jeopardise Rothesay's business plans. |
| **Partial internal model** | Under Solvency II, insurer's own model used to calculate the solvency capital requirement in relation to particular risks approved by the PRA. |
| **Part VII transfers** | Court-approved transfer of a portfolio of contracts from one entity to another. |
| **Performance of in-force book** | See Alternative Performance Measures. |
| **Pillar I** | Under Solvency II, represents the solvency capital requirement calculated using a standard formula or (partial) internal model. |
| **Policyholders** | Rothesay generally uses the term policyholder to refer to the individual immediate and deferred annuitants whose benefits are insured by Rothesay regardless of whether the insurance is provided under a bulk annuity (where the contract is with the pension scheme) or a reinsurance policy (where the contract is with the insurance company). |
| **Prudential Regulation Authority (PRA)** | The PRA is the UK regulatory body responsible for prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. |

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| **qx** | qx is actuarial notation used to represent the probability of a life aged x dying during the year. |
| **RAL** | Rothesay Assurance Limited. Now being wound up. |
| **Regular premiums** | Payments of premium made regularly over the duration of the policy. |
| **Reinsurance** | Protection sold to or purchased from another insurance company. |
| **Reorganisation reserve** | Reflects the impact of Rothesay's reorganisation in 2013 which led to an increase in reserves of £132m, reflecting the excess of consolidated net assets to the historical cost of investment in subsidiary entities. |
| **Risk margin** | Under Solvency II, the cost of transferring non-hedgeable risks. |
| **RL** | Rothesay Limited. |
| **RLP** | Rothesay Life Plc, the Group’s regulated life company. |
| **RMA1** | Rothesay MA No.1 Limited. |
| **RMA2** | Rothesay MA No.2 Limited. |
| **RMA3** | Rothesay MA No.3 Limited. |
| **RMA4** | Rothesay MA No.4 Limited. |
| **RPML** | Rothesay Pensions Management Limited, the Group’s service company. |
| **RSUs** | Restricted share units. |
| **SARs** | Stock appreciation rights. |
| **SCR coverage %** | See Alternative Performance Measures. |
| **Secured investments** | Bespoke investments where very high levels of collateral have been negotiated and returns are generated through illiquidity premium. |
| **Single premiums** | Single premium policies of insurance are those that require only a single lump sum payment from the policyholder. |
| **Sk** | Smoothing parameter in CMI longevity improvement modelling determining the weighting on recent experience. Given recent improvements, a higher Sk will generally lead to a higher initial assumed rate of mortality improvement. |
| **Solvency capital requirement (SCR)** | See Alternative Performance Measures. |
| **Solvency II** | The solvency regime applicable from 1 January 2016. Under Solvency II, Rothesay is required to hold the greater of the capital required under the new Solvency II Pillar 1 framework and the capital required under our own economic capital models Solvency II Pillar 2. |

# Glossary of terms (unaudited)
**continued**

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| **SONIA** | The Sterling Overnight Index Average, abbreviated SONIA, is the effective overnight interest rate paid by banks for unsecured transactions in the British sterling market. |
| **Strategy risk** | The risk of loss in future earnings and capital arising from changes in the competitive, economic, legal or political environment, changing customer behaviour, or a failure to select appropriate strategic or long-term business plans. |
| **Subordinated loan** | A fixed interest issue or debt that ranks below other debt in order of priority for repayment if the issuer is liquidated. Holders are compensated for added risk through higher rates of interest. Under EU insurance regulation, subordinated debt is not treated as a liability and counts towards the coverage of the required minimum margin of solvency with limitations. |
| **Surrender** | The termination of a life insurance policy or annuity contract at the request of the policyholder after which the policyholder receives the cash surrender value, if any, of the contract. |
| **Third party administration (TPA) agreement** | Contract with pensions administrator to process claims and payroll on behalf of Rothesay. |
| **Unconsolidated structured entities** | A structured entity is an entity that has been designed so that voting or similar rights are not the dominating factor in deciding who controls the entity. These structured entities have not been consolidated as Rothesay does not have the power to affect their returns. |
| **Value of new business on an MCEV basis** | See Alternative Performance Measures. |
| **Yield** | A measure of the income received from an investment compared to the price paid for the investment. Normally expressed as a percentage. |

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