Rothesay

Building for the future

Rothesay Life Plc
Annual report
and accounts 2022

Our purpose

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

Rothesay refers to Rothesay Life Plc (RLP) and its subsidiaries, together, the Group.

Overview

Strategic report

Financial statements

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

Who we are

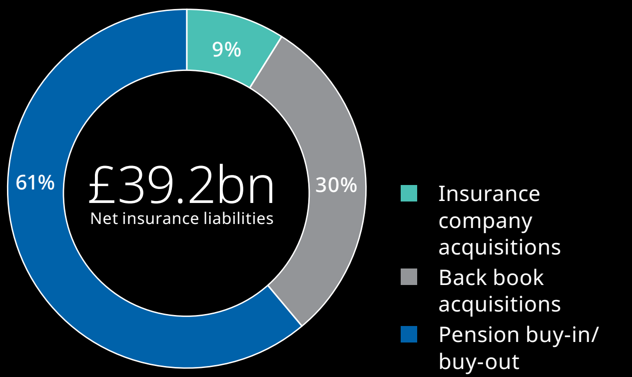
Rothesay is the UK's largest specialist pensions insurer, purpose-built to protect pension schemes and their members' pensions. Our singular focus is to secure pension annuities for the future, providing certainty as well as genuine service excellence for all our policyholders.

Our careful approach to investment and prudent underwriting mean we are trusted by the pension schemes of some of the UK's best known companies to provide pension solutions, including Asda, British Airways, Cadbury, the Civil Aviation Authority, the Co-operative Bank, William Hill, National Grid, Morrisons, Post Office and telent.

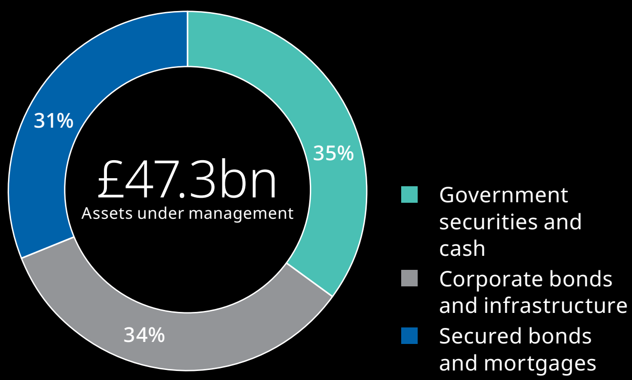
Underpinned by sophisticated risk management, our expert in-house investment team is continually developing new ways to drive predictable, dependable returns that reduce risk and create real security.

Today, we manage over £47bn in assets, secure the pensions of over 825,000 people, and pay out, on average, over £200m in pension payments each month. We are securing the future for every one of our clients and policyholders, and providing value to our shareholders over the long term.

Securing pension annuities from pension schemes and other insurers



Backed by high quality investments



2022 performance

258%
Solvency capital requirement (SCR) **APM** coverage of 258% (272% on a pro forma basis[1]) (2021: 229%), giving us significant capital for future growth opportunities.

£3.3bn
New business premiums of £3.3bn (2021: £3.0bn). We are also exclusive on a further £4.4bn of business.

£176m
Record operating profit **APM** of £1,020m (2021: £908m). IFRS profit before tax of £176m (2021: £918m).

Over £8bn
Invested over £8bn of assets according to our long-term investment strategy including new lifetime mortgages of £1.6bn.

7% reduction
Second annual Environmental, Social and Governance (ESG) report shows a 7% reduction in the carbon intensity of Rothesay's investment portfolio.

2022 awards
Insurance Company of the Year at the Insurance Asset Management Awards and Pensions Insurance Firm of the Year from European Pensions Awards.

Gold standard
Re-accredited with the Gold standard by the Pensions Administration Standards Association.

A2 rating
Upgraded to A2 by Moody's Investors Service.

[1] In order to provide flexibility in transitioning assets to our long-term investment strategy, some Matching Adjustment eligible new business was written into the non-Matching Adjustment fund. Adjusting for this on a pro forma basis would increase solvency coverage from 258% to 272%.

Performance at a glance

New business premium (APM)[1]

2022: £3.3bn
2021: £3.0bn
2020: £7.0bn

£3.3bn

Paid to policyholders in the year

2022: £2.9bn
2021: £2.9bn
2020: £2.8bn

£2.9bn

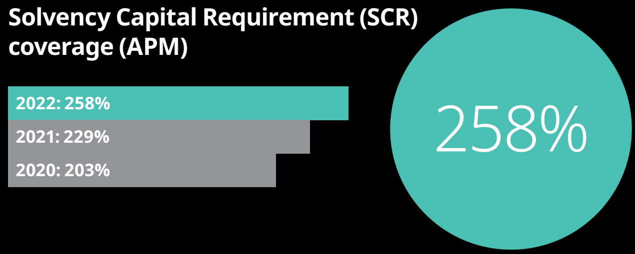
Number of policies

2022: 825,466
2021: 837,721
2020: 847,839

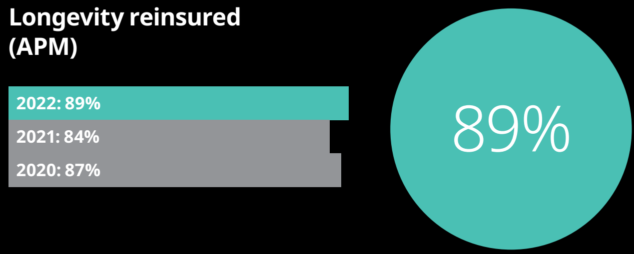
825,466

[1] **(APM)** – Alternative Performance Measure; please see page 28 for further details.

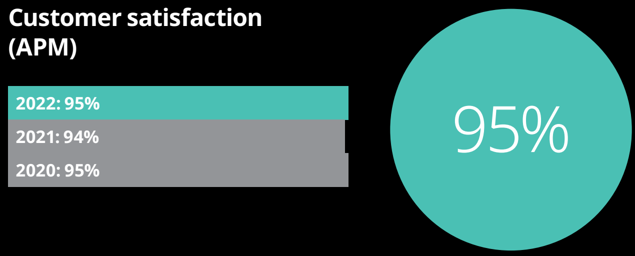
Solvency Capital Requirement (SCR) coverage (APM)



Longevity reinsured (APM)



Customer satisfaction (APM)



IFRS profit before tax

Assets under management (APM)

Own funds

A glossary of terms used can be found on page 128.

Strategic Report

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

"Our strong capital position means we are well-placed in a pension de-risking market which has never been more buoyant."

Tom Pearce
Chief Executive Officer

Chief Executive's statement

It is a huge privilege to become Rothesay's new CEO following Addy Loudiadis' outstanding leadership of the business over the past fifteen years.

I am proud of the business Rothesay is today: the leading specialist insurer in the market and as relentlessly focused on excellence as when we first started. Every day, we remain committed to performing to the highest standards for our policyholders, shareholders and colleagues. On a personal note, Addy has been a huge inspiration to me along with so many others in our industry and I look forward to continuing to benefit from her insight and expertise as we build on our success to date and deliver on our ambitions for the business in the years ahead.

The last 12 months have seen extraordinary turbulence in financial markets as a result of Russia's invasion of Ukraine, the lasting economic impact of COVID-19, the cost of living crisis and the instability caused by the UK's mini-budget. Volatile markets have been accompanied by significant increases in interest rates and inflation, substantial movements in UK sovereign debt and credit spread widening.

As a business, Rothesay is designed to protect pensions through even the most difficult times. Current market conditions are demonstrating once again the value of our purpose-built risk management systems and focus on operational excellence. Regular stress testing and live monitoring of the financial and solvency position of Rothesay allows us to respond dynamically as the market evolves, ensuring that we ended the year with a very robust SCR coverage ratio of 258% (2021: 229%), substantially above our target operating range. Rothesay was not directly impacted by the Liability Driven Investment (LDI) crisis and our focus on liquidity risk management meant that our liquidity position remained robust throughout the market turmoil of 2022.

During 2022, we assisted nine pension schemes to de-risk, generating £3.3bn of new business premiums (2021: £3.0bn) . We are also exclusive on a further £4.4bn of new business.

We were delighted to see our performance recognised in the European Pensions Awards 2022, where we were named Pensions Insurance Firm of the Year, and in the Insurance Asset Management Awards 2022, where we were awarded Insurance Company of the Year.

During 2021, we decided that we would start to undertake pension buy-in administration in house, rather than outsourcing this activity, and we are now doing the work in-house for ten schemes. Good progress is also being made on the development of Rothesay's technology platform.

In 2022, we opened new offices in New York to accommodate the expansion of Rothesay Asset Management North America (formerly known as Rothesay Asset Management US) as well as opening an office in Sydney for Rothesay Asset Management Australia. Having a presence in those markets is important in helping us to build an internationally-diversified investment portfolio.

Chief Executive's statement continued

Group performance

The significant rise in long-term interest rates resulted in large movements in both assets and liabilities. Close duration matching means that assets and insurance liabilities fell in tandem, with the Group's assets under management reducing to £47.3bn (2021: £62.6bn). and insurance liabilities reducing by a similar amount to £38.1bn (2021: £54.0bn).

Throughout the year, we invested new business premiums received in prior periods according to our long-term strategy and in line with our underwriting targets. When we underwrite new business, we assume it will take time to invest the premiums and this allows us to be patient in making investments. The IFRS profits generated from investment allowed us to generate record operating profits of £1,020m (2021: £908m). These profits were then largely offset by the impact of credit spread widening and the increase in long-term interest rates to give IFRS pre-tax profits of £176m (2021: £918m).

More details on our IFRS performance can be found in the financial review on page 26.

Risk and capital management

As noted above, 2022 has seen very volatile markets and rapidly increasing real interest rates. The duration of our liabilities means that Rothesay's assets and liabilities are particularly sensitive to long-term interest rates and our sophisticated risk management systems again proved vital in managing this and responding quickly to a challenging economic environment.

Our investment portfolio is focused on highly rated assets, many of which benefit from high quality collateral. We have no direct exposure to Russia or Ukraine. The quality of our investment portfolio, combined with active monitoring and management of our credit portfolio, means that we continue to be well positioned to withstand adverse market conditions.

Rothesay's strong and long-term focus on the Group's liquidity, as well as its solvency, has proved essential over 2022, with the Group's liquidity position remaining robust throughout the ongoing market turmoil seen, particularly in the second half of the year.

Rothesay's SCR is currently calculated using a partial internal model (PIM) but we have now made an application to use a full internal model (FIM), extending the PIM to cover the risk components not covered by the PIM. We will start using the FIM once we have received approval to do so from the Prudential Regulation Authority (PRA).

We continue to hedge market and longevity risk exposures and benefit from robust collateral arrangements which mitigate counterparty risk. We entered into five new longevity reinsurance agreements in 2022, as a result of which we have now reinsured 89% of our longevity exposure (2021: 84%).

Solvency and accounting reform

In November 2022, HM Treasury announced the introduction of the new Solvency UK regime which is, in part, designed to facilitate increased investment in UK infrastructure and clean energy. The details of the reforms have not yet been finalised so they are unlikely to be implemented until 2024. Had the reforms been implemented as at 31 December 2022 then we estimate that our solvency coverage ratio would have increased by around 17% after allowing for recalculation of transitional solvency relief (see Capital Management section).

Rothesay has spent a considerable amount of time and effort preparing for the implementation of IFRS 17, the accounting standard for insurance contracts, from 1 January 2023. The implementation of IFRS 17 is expected to lead to a significant reduction in total equity and lower restated comparative profits for 2022 because under IFRS 17 the release of profit is spread over the lifetime of the contract and this change is applied retrospectively to business that was written in the past. To mitigate the reduction in retained earnings at transition, the Board approved a capital reorganisation resulting in a reduction of £2.0bn in share premium and a corresponding increase in the profit and loss reserve. Following the introduction of IFRS 17, we expect that our ability to pay dividends will continue to be driven by our solvency balance sheet.

Our policyholders

Providing over 825,000 policyholders with a safe and secure pension is at the heart of what we do. We pride ourselves on the level of service we provide and I am pleased to say that we maintained our high service standards during the period despite continuing hybrid working, with over 95% **(APM)** (2021: 94%) of customers rating the quality of service received as good or excellent.

I am also pleased to say that in January 2022, the Pensions Administration Standards Association (PASA) confirmed our re-accreditation. PASA promotes and improves the quality of pensions administration services for UK pension schemes. Our continued Gold standard accreditation demonstrates Rothesay's ongoing commitment to delivering outstanding service.

Our people

Our people are a key strength of Rothesay and we were happy to welcome staff back to the office post the COVID-19 pandemic once it was safe to do so. Taking the time to reconnect in person and being able to meet together and collaborate is invaluable, facilitating creativity and learning, and enhancing our culture.

During 2022, we continued to recruit, particularly to strengthen our control functions in line with our planned growth and to support the continuing development of our technology platform. We were also pleased to welcome a new Chief People Officer, Monique Brown, and a new General Counsel, Lorna Tennent.

Environmental, social and governance matters

Rothesay is determined to play its part in combatting climate change and global warming. Our own operations are now carbon neutral (as certified by The CarbonNeutral Protocol) and we are making progress in reducing the carbon intensity of our investment portfolio. We have committed to reducing the carbon intensity of our portfolio by 20% in the five-year period to 2025 and have achieved a 7% reduction so far.

For more information, see our 2021 Environmental, Social and Governance Report, which is available on the Rothesay Limited website.

LTA partnership

During 2022, Rothesay became the exclusive pensions partner to the LTA, the national governing body of tennis for Great Britain, supporting the future of British tennis and helping to open up tennis to more people of any age, ability and background. Rothesay is now the title sponsor of the Rothesay Summer Series: the Rothesay Open Nottingham, Rothesay Classic Birmingham and Rothesay International Eastbourne.

Charitable donations

The conflict in Ukraine is deeply concerning for us all. In response, Rothesay made a donation of £500,000 to the International Committee of the Red Cross. In addition, we are encouraging our people to make monetary donations to support the relief effort in Ukraine, by matching donations on a 3-to-1 basis.

The cost of living crisis is affecting large numbers of pensioners throughout the UK. In response, the Rothesay Foundation partnered with Iceland Foods to launch the 'Summer Cheer' campaign, giving £2m worth of vouchers to pensioners in need to spend on food and other essentials. The campaign supported over 80,000 pensioners with a £30 voucher and also provided them with Age UK's information guide on financial advice following research showing that, despite record levels of poverty, over 770,000 pensioner households are still missing out on pension credit payments.

Looking forward

Our risk management strategy has performed robustly in turbulent financial markets, securing and supporting our very strong capital position. Improved pension scheme funding levels driven by the rising interest rates environment are making de-risking increasingly affordable for pension schemes and many scheme sponsors are reconsidering the benefit of pension de-risking in the light of recent market turbulence. This is creating some exciting new business opportunities and a very substantial new business pipeline. We are fortunate in having two long-term, supportive shareholders and this, combined with our disciplined approach to underwriting, our track record of executing large complex transactions, our patient and innovative investment strategy and our robust financial position, means that we are in a strong position to take advantage of the growth opportunities we can see.

I am confident as we look to the year ahead that Rothesay will continue to build on its significant growth over the past fifteen years, delivering market-leading transactions while providing pension security for our policyholders and value to our shareholders over the long term.

Tom Pearce
Chief Executive Officer
10 February 2023

Our markets

1. Pension risk transfer

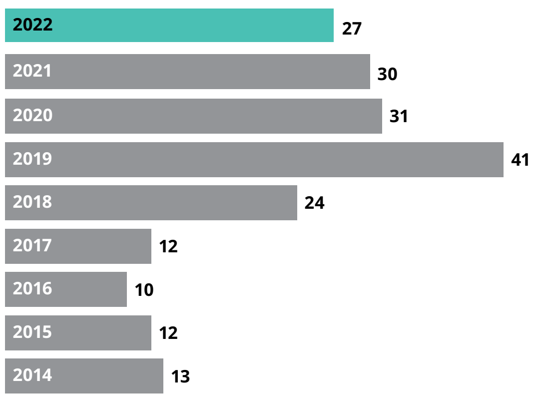
Rothesay's core market is expected to grow strongly

Rothesay's core market is in pension risk transfer. 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 buy-out.

The turmoil in financial markets in the second half of 2022 has highlighted the ongoing risk to pension scheme sponsors of running a pension scheme. More and more schemes are looking at buy-out as the end goal and rising interest rates, contributions from sponsors, liability management and the run-off of closed schemes means that this is increasingly affordable for them. As a result, the pipeline is looking strong, with commentators suggesting that the next few years could see pension risk transfer volumes of up to £50bn a year.

We will remain disciplined when underwriting to ensure that returns on new business are appropriate but with such a strong pipeline, we are optimistic about likely future new business volumes.

Pension risk transfer market (£bn)



Showing UK pension risk transfers completed per year. 2022 projected figures are based on WTW estimates.

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 pension schemes.

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 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 the 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.

2. Wholesale annuity

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

With our financial strength and track record, we are well positioned to acquire back books of annuities. However such acquisitions will always be opportunistic and hence it is difficult to predict when and whether such opportunities will arise in the future.

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. At this point, we takeover the administration as well as the economic exposure.

Timeline for our wholesale annuity transactions

	2011	2014	2015	2016	2018
Transaction	Acquisition of Paternoster	Acquisition of MetLife Assurance Limited	Purchase of annuity portfolio from Zurich UK Life (reinsurance followed by Court-approved transfer in 2017), with three follow-on transactions	Purchase of annuity portfolio from Aegon UK (reinsurance followed by Court-approved transfer in 2017)	Purchase of annuity portfolio from Prudential (reinsurance followed by Court-approved transfer of the majority of the portfolio in 2021)[1]
Size of transaction	£3bn	£3bn	£1bn	£6bn	£12bn
Number of policies	42,000	24,000	28,000	187,000	400,000
Type of business	Bulk annuities	Bulk annuities	Individual and bulk annuities	Individual and bulk annuities	Individual and bulk annuities

[1] Although the transfer was approved in 2021, the administration of these policies is expected to transfer to Capita, Rothesay's preferred administrator, in early 2023.

Our business model:

Securing the future for our policyholders.

Underwrite the liabilities

We provide maximum pre-deal certainty for trustees and pension scheme members 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 appropriate returns for our investors.

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.

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 liquidity requirements, meet our environmental objectives and provide an appropriate risk-adjusted return.

Our portfolio is focused on highly rated assets and is made up of three diverse categories:

1. Cash and Government bonds.

2. Corporate bonds and other infrastructure.

3. Secure, illiquid assets.

Deliver the pension benefits

We have strategic partnerships with well established pension administrators – WTW, Mercer and Capita Pension 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 systems to eliminate discrepancies and deliver excellent customer service.

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 market leadership.

Purpose-built

We were founded with a single purpose: to secure UK pensions at scale 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 a 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 teams 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

Original thinking

Service excellence

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.

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.

We support clients through every step of the process and leave no stone unturned from initial proposal 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 investments

Good progress has been made with investing assets in line with our long-term investment strategy.

Our in-house team is responsible for the management of Rothesay's £47.3bn asset portfolio. Assets are sought which match our liability cash flows and which provide an appropriate risk-adjusted return as well as being in line with our responsible investment policy. Rothesay has a careful approach to investment 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.

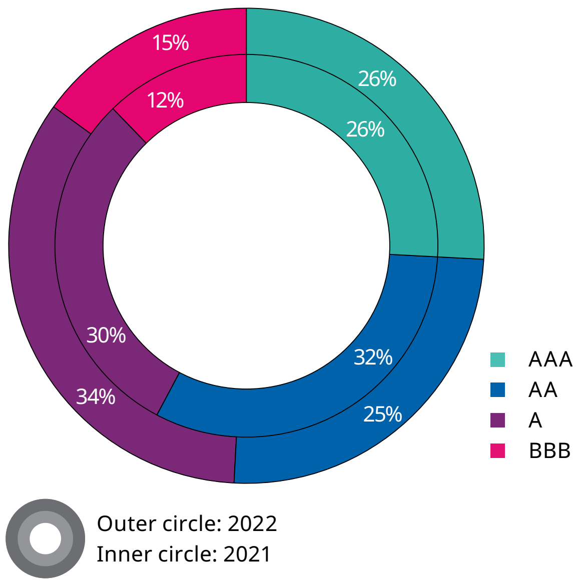
At the end of 2021, Rothesay had substantial cash and gilts to deploy into longer-term assets due to the new business written in prior years. We are patient when making such investments and make allowance for the potential time it might take to invest the premiums when we underwrite new business. Wider credit spreads and volatile market conditions in 2022 have meant that we have been able to invest assets according to Rothesay's long-term investment strategy. We have succeeded in investing over £8bn of assets more quickly than envisaged when the business was originally underwritten and at better risk-adjusted returns. Investments include the purchase of a £687m portfolio of lifetime mortgages from Just Group Plc and two substantial commercial real estate loans.

During 2022, we also upgraded around £3bn of the portfolio by selling assets and replacing them with assets of higher credit quality, lower carbon intensity or increased yield.

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 Agreement 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.

Rothesay's investment portfolio is focused on highly rated assets with over half of our rated assets having a rating of AAA or AA. This can be seen in the chart below.

Investment by rating (%)



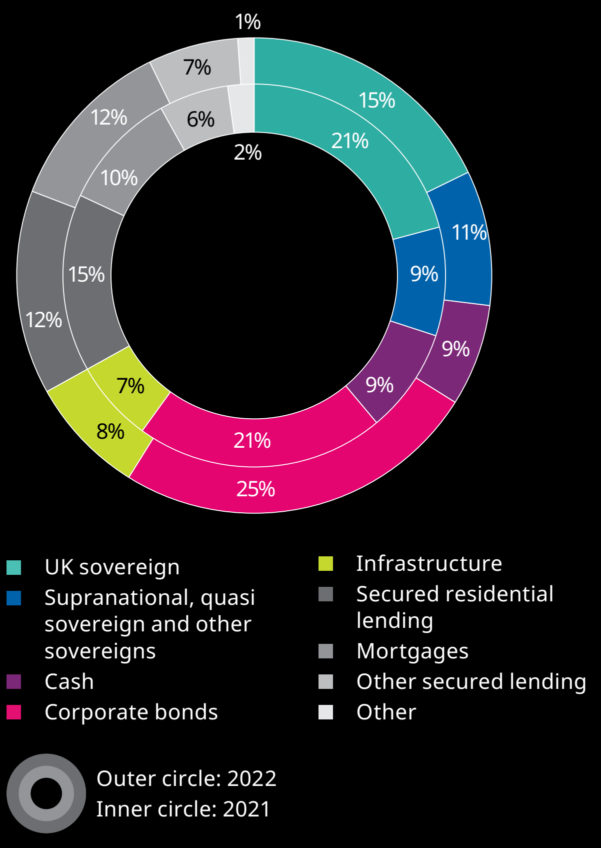
The portfolio can be divided into three broad categories:

- **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 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, mortgages 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.

We are already a leading lender to the social housing sector and are very supportive of the Government's objective to secure more investment in long-term illiquid infrastructure assets, remaining closely involved with the Government's Productive Finance Working Group.

The following charts provide a breakdown of our investment portfolio at 31 December 2022 and 31 December 2021 by sector. The chart shows an increase in investment in corporate bonds and mortgages.

Our investments



Our investments continued

Corporate bonds and infrastructure

Given recent market conditions, many of the new investments have been in more liquid, highly rated corporate bonds, including US rate reduction bonds, universities and healthcare providers.

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

Sector (%)	2022	2021
Infrastructure	**8**	7
Banking & insurance	**6**	5
Real estate	**5**	5
Education	**3**	3
Communications & media	**2**	2
Consumer goods & services	**2**	1
Healthcare	**2**	1
Technology & electronics	**2**	1
Automotive & transportation	**1**	1
Industrial & energy	**1**	1
Retail	**1**	1
Total	**33**	28

Of our £18bn holding of corporate bonds and infrastructure, around 33% (or 11% of our investments) is rated BBB and of those only £0.2bn is rated BBB- (2021: £18bn with 31% rated BBB and £0.3bn rated BBB-). The vast majority of the remainder are rated A or above. As at 31 December 2022, Rothesay holds only £11m of sub-investment grade bonds (2021: £Nil).

Residential mortgages

As noted above, in February 2022, Rothesay purchased a £687m portfolio of lifetime mortgages from Just Group Plc. That, combined with strong volumes during 2022, meant that as at 31 December 2022, our total lifetime mortgage portfolio is now £5.1bn (2021: £5.3bn), with new origination largely offsetting the fall in value as a result of the significant increase in interest rates. We remain cautious in underwriting mortgages, with newly originated lifetime mortgages having an average loan-to-value ratio of 34% (2021: 29%). Lifetime mortgages now represent 11% of assets under management (2021: 8%).

We also continue to fund long-term, fixed rate mortgages in both the UK, where the product is new, and in the Netherlands, where the product is better established. As at 31 December 2022, our long-term, fixed rate mortgage portfolio has grown to £1.1bn (2021: £1.0bn).

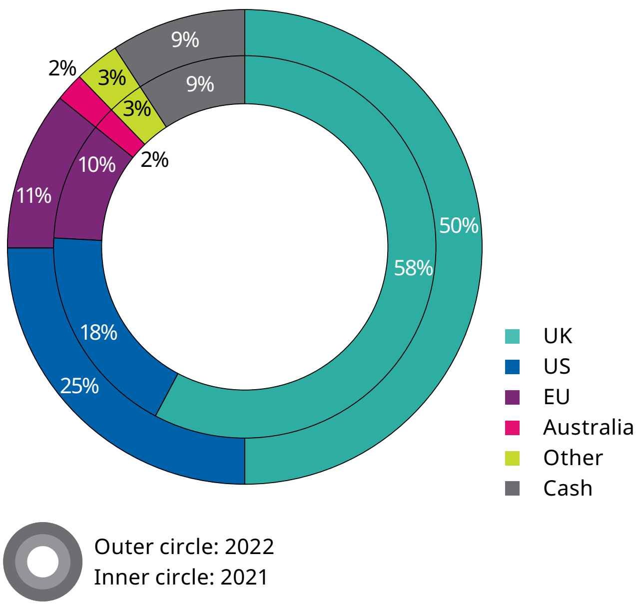
International diversification

In 2017, we set up Rothesay Asset Management North America (formerly known as Rothesay Asset Management US) to help Rothesay to originate assets in the US. We have recently opened larger offices in New York and continue to grow the team there. Around 25% (2021: 18%) of our portfolio is now invested in the US.

We already have a small portfolio of Australian investments and, following the success of Rothesay Asset Management North America, we have now set up a similar operation, Rothesay Asset Management Australia, to help us to originate assets in Australia.

The chart below provides a breakdown of our investment portfolio at 31 December 2022 by geography. The chart shows an increase in allocation to USD-denominated assets (partly as a result of the strengthening of the USD relative to sterling).

International diversification



Our strategy and KPIs:

Measuring progress

Financial security

	2021	2022
SCR coverage (APM) Indicates capital strength through comparing how the Group is capitalised relative to the regulatory requirement	229%	**258%**
Assets under management (APM) Measures business size to indicate ability to diversify and potential for economies of scale	£62.6bn	**£47.3bn**
External ratings Impartial indicators of our financial strength	A3 Moody's Investors Service A+ Fitch Ratings	**A2 Moody's Investors Service** **A+ Fitch Ratings**

2022 progress:

- Significant improvement in solvency position as long-term interest rates increased. Surplus capital of £4.9bn (2021: £4.7bn) means that we are well-placed for future growth opportunities.
- Following the annual review by the credit rating agencies, Fitch reaffirmed our rating and Moody's increased our rating to A2.
- The increase in interest rates also meant that Rothesay's assets under management fell to £47.3bn primarily as a result of the significant increase in long-term interest rates (2021: £62.6bn). Because of the way in which we closely duration match our assets and liabilities, Rothesay's insurance liabilities also reduced by a similar amount to £38.1bn (2021: £54.0bn).
- Reinsured £2.1bn of liabilities giving effective reinsurance coverage of 89% (2021: £2.6bn to give 84% coverage).
- Submitted application for the full internal model (FIM).

Opportunities in 2023 and beyond:

- Continue to maintain a robust solvency position.
- Continue to develop our climate risk modelling and measurement capabilities.
- Implement the FIM covering all risks, subject to approval by the Prudential Regulation Authority.
- Continue to optimise our capital structure through appropriate levels of equity and debt.

Steady growth

New business premiums (APM) Signals the Group's growth	2021	2022
	£3.0bn	**£3.3bn**

2022 progress:

- We have maintained our disciplined approach to new business, remaining patient in a competitive environment to ensure returns are appropriate. In 2022, we de-risked the liabilities of nine pension schemes, which generated £3.3bn of new business (2021: £3.0bn). We also entered into exclusivity in relation to a further £4.4bn of new business.
- Grew the Rothesay team by 37 talented individuals across the Group.
- Opened new, larger offices in New York, facilitating the growth of Rothesay Asset Management North America.
- Rothesay Asset Management Australia established to originate investments for Rothesay in Australia.

Opportunities in 2023 and beyond:

- Continue to assist pension schemes to de-risk using buy-in and buy-out policies. Given the strength of the pipeline, we anticipate significant new business opportunities in 2023 and beyond.
- Continue to develop our in-house IT platform.
- Capitalise on the opportunities presented by our sponsorship of the LTA to promote the Rothesay brand.
- Continue to strengthen Rothesay's profile as an investor overseas, to allow us to continue to diversify investments.

Our strategy and KPIs continued

Service excellence

	2021	2022
Service quality (APM) Measures the number of policyholders who rate our service 'good' or 'excellent'	94%	**95%**
Complaints (APM) Measures satisfaction through number of complaints upheld per 1,000 customers	0.51	**0.47**

2022 progress:
- Performance throughout the year has generally been above our stringent benchmarks across all our strategic administration partners.
- Maintained low complaint rates and high satisfaction.
- Continued to roll out our online service to our policyholders.
- Continued to bring in-house the administration of pensioner buy-ins.
- Prepared for the transfer of the Prudential portfolio to Rothesay's preferred third party administrators.
- Established Board-level Customer Conduct Committee to focus on customer service.
- Re-accredited with the PASA's Gold standard.

Opportunities in 2023 and beyond:
- Continue to excel in customer service.
- Transfer administration of the Prudential portfolio to Rothesay's preferred third party administrators so that the Prudential policyholders can benefit from Rothesay's outstanding customer service.
- Continue to migrate some existing pensioner buy-ins to the new in-house model and build on our in-house capabilities so that we can leverage our risk management systems to improve accuracy and efficiency.
- Implement plans for complying with the new Consumer Duty which comes into force in July 2023.

Reliable performance over time

	2021	2022
IFRS profit before tax Measures profitability, by capturing all recurring and non-recurring items	£918m	**£176m**
Employee engagement Measures the number of employees who say they are proud to work at Rothesay	92%	**91%**
Carbon intensity Measures carbon intensity of Rothesay's investment portfolio	211t CO_2e/m USD[1]	**197t** **CO_2e/m USD borrower revenue**

2022 progress:

- Invested assets received from 2021 and 2022 new business in accordance with our underwriting targets, contributing to 2022 IFRS operating profits of £1,020m (2021: £908m). These were largely offset by credit spread widening and the increase in long-term interest rates to give IFRS pre-tax profits for the year of £176m (2021: £918m).
- Maintained market-leading levels of employee engagement.
- Published our second ESG report setting out detailed carbon intensity data and showing a 17% reduction in the carbon intensity of our publicly traded corporate debt and a 7% reduction in the overall portfolio.
- Maintained carbon neutrality of our own operations and entered into a partnership with Climeworks that should ensure neutrality for the next ten years.

Opportunities in 2023 and beyond:

- Increase our market penetration – the total market volume has grown considerably in the last few years, but only around 10% of the UK's £2.1tn of pension liabilities are fully insured.
- Maintain employee engagement and unique Rothesay culture despite the continuing growth of the Company, making improvements where we can.
- Capitalise on economies of scale.
- Continue to make progress towards our ambitious environmental targets and formalise the way in which social and governance issues are considered when evaluating investment opportunities.

[1] Comparative has been rebased due to improvements in our Sovereign and UK Mortgage methodologies, and the availability of new data for a number of our material assets.

Strong operating profits driven by investment of assets in line with our long-term strategy.

Andrew Stoker
Chief Financial Officer

Financial review

The financial review describes the financial performance of Rothesay Life Plc and its subsidiaries.

IFRS financial performance
Rothesay made an operating profit before tax of £1,020m (2021: £908m) **(APM)** as we were able to invest cash and gilts received as new business premiums according to our long-term investment strategy. Credit spread widening and the impact of the increase in long-term interest rates then meant that we made profit before tax of £176m (2021: £918m). 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 125.

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 £246m (2021: £213m).

We are patient when investing the premiums received which meant that we began 2022 with cash and gilts to invest according to our long-term strategy. Attractive investment opportunities in 2022 means that we have now effectively invested all of the premiums received as new business, leading to no temporary reduction in profits (2021: a reduction of £201m) **(APM)**. Widening credit markets meant that we have also invested all the assets received as premiums in prior years leading to profits from investing prior year premiums for the year of £201m (2021: £547m) **(APM)**.

Profits generated on the in-force book were £801m (2021: £403m) **(APM)**. These profits mainly arose from investment activity, where we have been able to take advantage of attractive investment opportunities in weaker credit markets, and the release of prudent margins as the business runs off.

A combination of demographic and expense assumption changes led to a reduction in profits of £18m (2021: an increase in profits of £142m) **(APM).** Further detail is provided in note E.3.

Note that for 2021, borrowing costs include interest of £29m paid on the sterling-denominated RT1 notes. From 1 January 2022, these costs are treated as an appropriation of profit as and when the interest on the notes is paid. Further detail is provided in note A.4.

Rothesay made economic losses in the year of £730m (economic profits 2021: £149m) **(APM)**. Economic (losses)/profits **(APM)** represent the change in value of assets from changes in economic conditions less the change in value of liabilities from those changes. In 2022, economic losses arose from the impact of credit spread widening, rising interest rates and other changes in economic conditions.

Financial review continued

Financial performance (Alternative analysis of profit generation) (APM)	2022 £m	2021 £m
New business profit (assuming assets fully invested)	**246**	213
Impact of temporarily being invested in gilts	**–**	(201)
Profit from investing prior year's premiums	**201**	547
Performance of in-force book	**801**	403
Non-economic assumption changes and model refinement	**(18)**	142
Acquisition costs	**(147)**	(137)
Administration expenses	**(63)**	(59)
Operating profit before tax	**1,020**	908
Borrowing costs	**(95)**	(114)
Project and other one-off expenses	**(19)**	(25)
Economic (losses)/profits	**(730)**	149
IFRS profit before tax	**176**	918

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 125, 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 significant increase in long-term interest rates resulted in very material reductions in both assets under management and insurance liabilities. The key line items in the consolidated statement of comprehensive income for Rothesay are summarised in the table below:

Income statement highlights	2022 £m	2021 £m	Commentary
Gross premiums written	**3,579**	3,205	Gross written premiums are made up of new business of £3.3bn (2021: £3.0bn) and regular premiums of £0.2bn (2021: £0.2bn) generated on the inwards longevity reinsurance business written in prior years.
Net premiums written	**1,404**	1,569	Net premiums written represent the gross premiums written less the £2,175m (2021: £1,636m) of regular premiums ceded to reinsurers.
Investment return	**(15,376)**	48	Assets and insurance liabilities are closely matched which means that both fell by a similar amount due to changes in economic conditions and the run-off of the business. This fall was partly offset by new business.
Total revenue	**(13,972)**	1,617	
Net claims paid	**(862)**	(1,380)	Claims paid represent the total payments due to policyholders during the year of £2.9bn (2021: £2.9bn) less the reinsurers' share of such claims of £2.0bn (2021: £1.5bn).
Change in net insurance liabilities	**15,433**	1,018	Assets and insurance liabilities are closely matched which means that both fell by a similar amount due to changes in economic conditions and the run-off of the business. This fall was partly offset by new business.
Operating expenses	**(229)**	(221)	Operating expenses consist of £63m (2021: £59m) of administration expenses, £147m (2021: £137m) of acquisition expenses and £19m (2021: £25m) of non-recurring and project expenditure.
Finance costs	**(194)**	(116)	Finance costs represent interest payable on borrowings and on collateral. Interest payable on collateral has increased in 2022 in part because of the significant increase in interest rates. Note that 2021 finance costs include interest paid on the sterling-denominated RT1 notes.
Total claims and expenses	**14,148**	(699)	
Profit before tax	**176**	918	
Income tax	**(30)**	(176)	Rothesay's effective tax rate is 16.1% (2021: 19%).
Profit after tax	**146**	742	

Financial review continued

IFRS statement of financial position highlights

The key line items in the consolidated statement of financial position for Rothesay are summarised in the following table:

Statement of financial position highlights	2022 £m	2021 £m
Financial investments	**90,928**	83,845
Reinsurance assets	**185**	641
Other assets	**3,529**	1,525
Total assets	**94,642**	86,011
Share capital and share premium	**510**	2,463
Tier 1 notes	**793**	793
Reserves	**4,958**	2,883
Total equity	**6,261**	6,139
Insurance contract liabilities	**38,112**	54,030
Reinsurance liabilities	**1,245**	1,217
Payables and financial liabilities	**47,126**	22,784
Borrowings	**1,764**	1,725
Other	**134**	116
Total liabilities	**88,381**	79,872
Total equity and liabilities	**94,642**	86,011

Financial investments and liabilities

Derivatives are used to manage market and credit risk. The significant increase in long-term interest rates resulted in a very material increase in the value of both derivative assets and derivative liabilities since they have a similar and largely offsetting exposure to interest rates. As at 31 December 2022, the value of derivative assets increased to £37.8bn (2021: £20.8bn) and the value of derivative liabilities increased to £37.8bn (2021: £20.7bn). The net value of derivatives fell from £81m as at 31 December 2021 to £11m as at 31 December 2022 but under IFRS it is the gross values that must be disclosed.

The increase in the value of derivative assets more than offset the fall in the value of the other financial investments leading to an increase in the value of financial investments from £83.8bn as at 31 December 2021 to £90.9bn as at 31 December 2022. The increase in the value of derivative liabilities was in part responsible for the increase in the value of payables and financial liabilities from £22.7bn at 31 December 2021 to £47.1bn at 31 December 2022.

Assets under management

Assets under management **(APM)** adjusts for the gross up of derivative values and can be derived by adjusting total assets for reinsurance, payables, derivatives and collateralised financing. Assets under management have decreased from £62.6bn as at 31 December 2021 to £47.3bn as at 31 December 2022. They have fallen as a result of the increase in long-term interest rates, as well as credit spread widening, and, given our close duration matching of assets and liabilities, a similar movement can be seen in insurance contract liabilities. A reconciliation of assets under management is provided in the notes on Alternative Performance Measures on page 125.

Reinsurance

During 2022, we entered into five new longevity reinsurance agreements 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 the number of contracts where this is the case fell in 2022, i.e. some contracts switched from being a reinsurance asset to a reinsurance liability due to the change in economic conditions and demographic assumption changes. Overall, reinsurance represents a net liability of £1,060m (2021: a net liability of £576m).

Total equity

The increase in total equity (an increase of £122m from £6,139m at 31 December 2021 to £6,261m at 31 December 2022) was driven by IFRS net profit during 2022.

The introduction of IFRS 17 from 1 January 2023 is expected to lead to a reduction in Group equity of between £1.0bn and £1.5bn (see Transition to IFRS 17 below). In anticipation of this change, in November 2022 the Board approved a capital reorganisation leading to a reduction in share premium of £2.0bn and a corresponding increase in the profit and loss reserve which was subsequently approved by the Court. See note C.3.

Insurance liabilities

Insurance contract liabilities reduced from £54.0bn as at 31 December 2021 to £38.1bn as at 31 December 2022. This move was largely driven by an increase in the valuation interest rate used to discount the liabilities, partially offset by the impact of new business net of the run-off of the liabilities (see note E.3(e)).

Transition to IFRS 17 and IFRS 9

Rothesay will apply IFRS 17, the accounting standard for insurance contracts, and IFRS 9, the accounting standard for financial instruments from 1 January 2023. IFRS 17 will bring significant changes to the accounting for insurance and as a result, we will be required to re-state comparatives and the opening balance sheet as at 1 January 2022. IFRS 9 is expected to have an immaterial impact on Rothesay's balance sheet as financial investments are already fair valued and we do not expect re-measurement and re-designation between asset classes under the new standard.

The IFRS 17 standard will have a significant impact on the way that Rothesay's results are reported because the standard rebuilds performance measurement 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.

The standard introduces a model that measures groups of contracts based on a best estimate of the present value of future cash flows that are expected to arise as Rothesay fulfils the contracts (the best estimate liabilities or BEL), an explicit risk adjustment for non-financial risk and a contractual service margin (CSM) that is released over the duration of the contract. The BEL, the risk adjustment and the CSM then collectively form the insurance liabilities.

The introduction of the CSM creates a significant store of future value that will result in a stream of more predictable insurance profits compared to the position under current accounting.

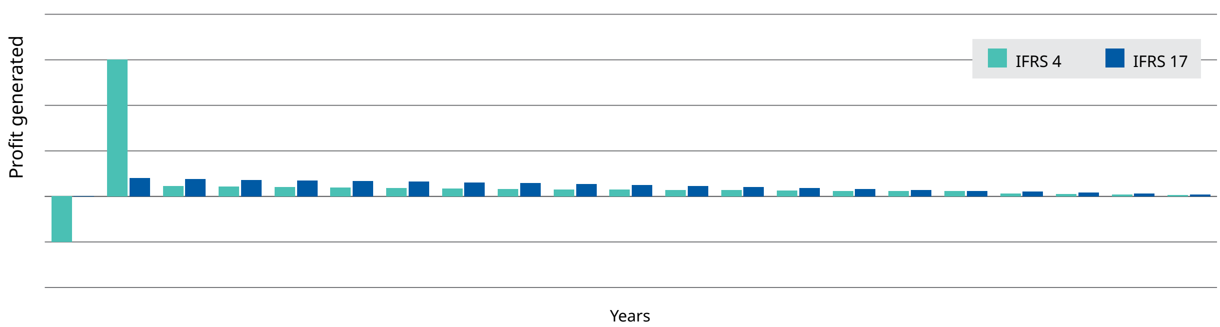
Under IFRS 17, profits and losses arise largely from:

a. One year's run-off of insurance liabilities, namely the release of risk adjustment and amortisation of CSM on existing business;
b. Net investment returns in excess of those assumed in calculating the insurance liabilities; and
c. Economic profits or losses from the impact of the changes in economic conditions.

Profits on new business and from experience and non-financial assumption changes are largely held back as adjustments to the CSM and amortised over time. Losses are recognised on day one for insurance contracts that are onerous but Rothesay currently does not have any such contracts.

Over the full duration of the contract, the same profit is expected to be generated, but IFRS 17 leads to a slower emergence of IFRS profit than under the existing insurance standard, IFRS 4. This can be seen in the profit signatures in the chart which shows the profit anticipated on a representative contract covering both immediate and deferred annuities. Under IFRS 4, the valuation rate of interest is derived from the assets held to back the liabilities. As a result, the chart shows that there is a day one loss as the premium is received as cash and gilts and this then turns into profit as the premium is invested according to Rothesay's long-term investment strategy (shown as year one in the chart). Profits under IFRS 4 are then made as prudent margins are released. This contrasts with IFRS 17 where: (i) the discount rate reflects the characteristics of the liability

Comparison of profit signatures (illustrative)



Financial review continued

and so is not impacted by investment of premiums; and (ii) no day one profit is made and a CSM and risk adjustment are established. Profits under IFRS 17 are then made as the risk adjustment is released and the CSM amortised.

IFRS 17 balance sheet as at 1 January 2022

The standard applies IFRS 17 retrospectively to historic business which means that much of the historic profit generated under IFRS 4 is required to be held back as the CSM. The combined impact of the retrospective changes required under IFRS 17 is shown in the chart below and is expected to lead to a reduction in Group equity of between £1bn and £1.5bn as at 1 January 2022 compared to those published under IFRS 4.

The CSM and risk adjustment set up on transition of around £5bn provide a view of the stored value that will be released over time as the existing business runs off.

As noted previously, to mitigate the reduction in retained earnings at transition, in November 2022 the Board approved a capital reorganisation leading to a reduction of £2.0bn in share premium and a corresponding increase in the profit and loss reserve which was subsequently approved by the Court.

Outlook

As Rothesay has grown very rapidly, with the majority of business being written in the last few years, the slower release of profits under IFRS 17 means that we expect materially lower operating profits for 2022 compared to IFRS 4. In addition, under IFRS 17, only part of the insurance liabilities (the best estimate liabilities and risk adjustment) is exposed to the impact of changes in economic conditions; the CSM is not impacted by such changes. As a result, the IFRS 17 balance sheet responds to changes in economic conditions in a way which is closer to MCEV than the IFRS 4 balance sheet. Given Rothesay's approach to hedging interest rate and inflation risk is to hedge somewhere between MCEV and solvency, we are effectively over-hedged on an IFRS 17 basis and so the IFRS 17 balance sheet is much more sensitive to interest rate movements than the IFRS 4 balance sheet. Under IFRS 17, the impact of the very significant increase in interest rates combined with widening credit spreads is expected to more than offset operating profits under IFRS 17. Consequently, the restated comparative for 2022 is expected to show material pre-tax losses under the new standard.

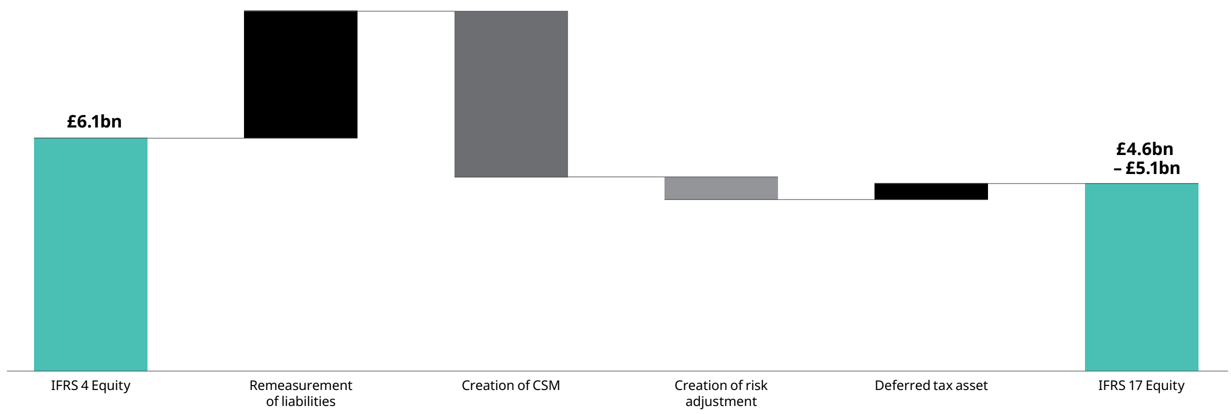
Under the tax regulations relating to IFRS 17, the tax relief on the losses arising from the adoption of IFRS 17 will be equally spread over a transitional period of ten years from 1 January 2023.

Adoption of the new standard is not expected to materially impact Rothesay's solvency position or the ultimate profitability of new business. As a result, changes to IFRS accounting are not expected to impact new business pricing or our business strategy. In addition, the rating agencies such as Fitch Ratings have indicated that they expect to treat CSM reserves as equity for the purposes of financial leverage ratios and so the implementation of IFRS 17 is not expected to impact our credit ratings.

Although the implementation of IFRS 17 is expected to lead to a significant impact on total equity and would have resulted in lower profits for 2022, we expect that our ability to pay dividends will continue to be driven by our solvency balance sheet.

We will publish full results under IFRS 17 as part of our interim results for the six months to 30 June 2023 including comparatives for full year and half year 2022.

Indicative impact on RLP equity as at 1 January 2022



Capital management

The Group's capital position has significantly increased throughout 2022 as a result of rising interest rates.

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). We started the year with capital surplus well above our target operating range and Rothesay's solvency position has increased significantly throughout the year as a result of increases in long-term interest rates. As we write more new business, the solvency coverage is expected to move closer to our target operating range.

We operate a dynamic capital management framework which uses interest rate and other hedging to try and protect both the solvency position and the embedded value of the business by hedging somewhere between the two. This is facilitated by our access to real-time solvency information. During 2022, we were careful to avoid over-trading in difficult market conditions.

Given our robust solvency position, some of the new business written in 2022 has been written into the non-Matching Adjustment fund in order to provide flexibility in transitioning assets to our long-term investment strategy. The new business is eligible for inclusion in the Matching Adjustment fund and moving the business would improve both Own Funds and the SCR requirement because the Matching Adjustment could then be used in calculating the technical provisions. We estimate that after allowing for the 14% impact on coverage of moving new liability trades to the Matching Adjustment fund, as at 31 December 2022, Rothesay would have had an SCR coverage ratio **(APM)** of 272% on a pro forma basis (2021: 229%), giving us significant excess capital to write new business.

The solvency positions of RLP is summarised in the table below.

Solvency position of RLP	2022 £m	2021 £m
Tier 1 capital	**6,868**	6,925
Tier 2 capital	**849**	948
Tier 3 capital	**434**	488
Own Funds **(APM)** available to meet SCR	**8,151**	8,361
SCR	**3,162**	3,657
Surplus above SCR	**4,989**	4,704
SCR coverage (APM)	**258%**	229%
Adjusted SCR coverage (APM)	**272%**	n/a
SCR coverage without transitional solvency relief	**235%**	181%

Capital management continued

Given the significant change in economic conditions in 2022, the value of transitional solvency relief was recalculated on 30 June 2022 and again on 31 December 2022. Transitional solvency relief reduces by 1/16th on 1 January each year. The impact of recalculation on 31 December 2022 was to decrease the transitional solvency relief to £388m net of the associated impact of tax on Own Funds and allowing for amortisation of 6/16ths (2021: £1,091m allowing for amortisation of 5/16ths). As long-term interest rates have increased, the transitional solvency relief has fallen in value, with transitional solvency relief now covering 32% of the risk margin (2021: 50%).

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. An application to use a full internal model, extending the PIM to cover other risk components, was submitted to the PRA in October 2022 but for now the standard formula is used to calculate the SCR for all other risk components and for aggregation across risk components.

The following table 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 change in the composition of the SCR during 2022 reflects the increase in investment, the significant increase in long-term interest rates as well as the impact of additional longevity reinsurance.

Composition of SCR (%)	2022	2021
Market risk	72	64
Insurance risk	17	24
Operational risk	6	6
Counterparty risk	5	6

An analysis of the change in surplus above SCR is shown in the table on the following page. Largely as a result of increases in real interest rates, surplus above SCR has increased from £4,704m to £4,989m (after allowing for amortisation of 1/16th of transitional solvency relief on 1 January 2022). The impact of moving new liability trades to the Matching Adjustment fund would be an increase in surplus of £245m.

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. All numbers are shown net of tax impacts and allow, where relevant, for changes in transitional solvency relief.

Change in surplus	2022 £m	2021 £m
Opening surplus	**4,704**	**3,730**
Amortisation of 1/16th of transitional on 1 January	**(133)**	(133)
New business (on a fully invested basis)	**(264)**	(172)
Impact of temporarily being invested in gilts	**–**	120
Impact from investing prior year's premiums	**(120)**	51
Performance of in-force book	**1,013**	612
Non-economic assumption changes	**7**	135
Acquisition costs and administration expenses	**(210)**	(196)
Operating surplus generation	**293**	**417**
Borrowing costs	**(129)**	(114)
Non-recurring and project expenditure	**(19)**	(25)
Economic conditions	**532**	82
Impact of LACDT	**(147)**	(98)
Impact of new business not in MA fund	**(245)**	n/a
New capital issuance	**–**	712
Surplus generation	**285**	**974**
Closing surplus	**4,989**	**4,704**
Closing surplus with new liabilities in MA fund	**5,234**	**n/a**

Solvency II borrowing costs are £34m higher than under IFRS due to the coupons paid on sterling-denominated RT1 notes being recognised as a deduction from Own Funds, whereas on IFRS they are treated as an appropriation of profit.

Solvency II reform

In November 2022, HM Treasury announced its response to the consultation on Solvency II reform. The main changes from a capital perspective are:

1. The risk margin reduction is to be calibrated to give a 65% reduction for long-term life insurance business;
2. The fundamental spreads used in derivation of the matching adjustment will be made more granular, by introducing rating notches, for example the fundamental spread for an A+ rated asset will be lower than the spread used for an A- rated asset;
3. The matching adjustment on sub-investment grade assets will no longer be capped at the spread on an investment grade asset; and
4. There will be a mechanism to allow firms to make voluntary add-ons to the fundamental spreads.

The details of the reforms have not yet been finalised so the reforms are unlikely to be implemented until 2024. Had the reforms listed above been implemented as at 31 December 2022 then we estimate that our solvency coverage ratio would have increased by around 17%, after allowing for recalculation of transitional solvency relief.

> The market turmoil of 2022 has brought the management of liquidity risk to the fore.

Peter Shepherd
Chief Risk Officer

Risk management

Risk management is at the heart of Rothesay's culture, systems and processes.

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 ensure that our policyholders receive excellent customer service.
- 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.

To do this we have a well established process of identifying, managing and monitoring risks, on a continuous basis. This allows the rapid, informed decision-making that enables Rothesay to manage through adverse conditions.

The risk management framework is designed to ensure that:

- risks are well understood and can be explained to all stakeholders;
- risk management and business strategy are aligned;
- all staff are aware of their individual responsibilities; and
- risks are monitored and managed in accordance with defined risk appetites.

Risk management is a continuous process and the risks to which Rothesay is exposed change over time. The framework is also designed to be responsive and is regularly reviewed to ensure that it remains highly effective. We have continued to invest in the risk function, but we also recognise that effective risk management starts with the staff who manage risks day in and day out, and so we have worked hard on ensuring effective communication between teams, and that systems, data and other tools are providing the information to enable staff to make timely informed decisions – with risk management at the core of these decisions.

Risks can be quantifiable, such as market risks, or non-quantifiable such as reputational or strategic risks, or could be a mix of both. Some risks have been a core part of the financial landscape for decades or more, while others, such as cyber risk, have emerged more recently and it requires an agile risk framework to adapt to these. Risks can materialise rapidly, such as a change in market conditions, or could emerge slowly over a number of years such as the outlook for life expectancy.

Risk management continued

Risk management framework

Rothesay has a risk management framework (RMF) which is aligned to the 'three lines of defence model'. Fundamental to this is that every employee knows how they contribute to the effective identification, management, mitigation and monitoring of all types of risks.

The RMF ensures that accountabilities and responsibilities are clearly agreed and documented, and that there are appropriate checks and balances, including segregation of responsibilities.

The 'three lines of defence' model is widely used in financial services, and sets the boundaries between the different areas, making sure that there are no gaps in risk management or unexpected overlaps in accountability.

- **First line – Risk owners**
  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 first line control functions, who are responsible for ensuring the integrity of Rothesay's operations and reporting. These include Operations, Finance and Legal.

- **Second line – Risk oversight**
  Design and maintenance of the risk management framework as well as risk oversight is provided by the Chief Risk Officer (CRO), his team and risk management committees. The Chief Compliance Officer and his team report to the CRO. The Executive Risk Committee (ERC) is chaired by the CRO and consists of relevant senior managers working within a delegated risk management framework. This committee reviews all material new investment, hedging or liability transactions.

- **Third line – Risk assurance**
  Internal Audit provides the Board and Executive with comprehensive, independent, objective assurance over governance, risk management and internal control.

The Board is responsible for oversight of the management of exposure to risks and is supported by the Board Risk Committee 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.

This model of separation of responsibilities is also aligned to the Senior Managers & Certification Regime, which ensures that individuals have very clear allocation of responsibilities.

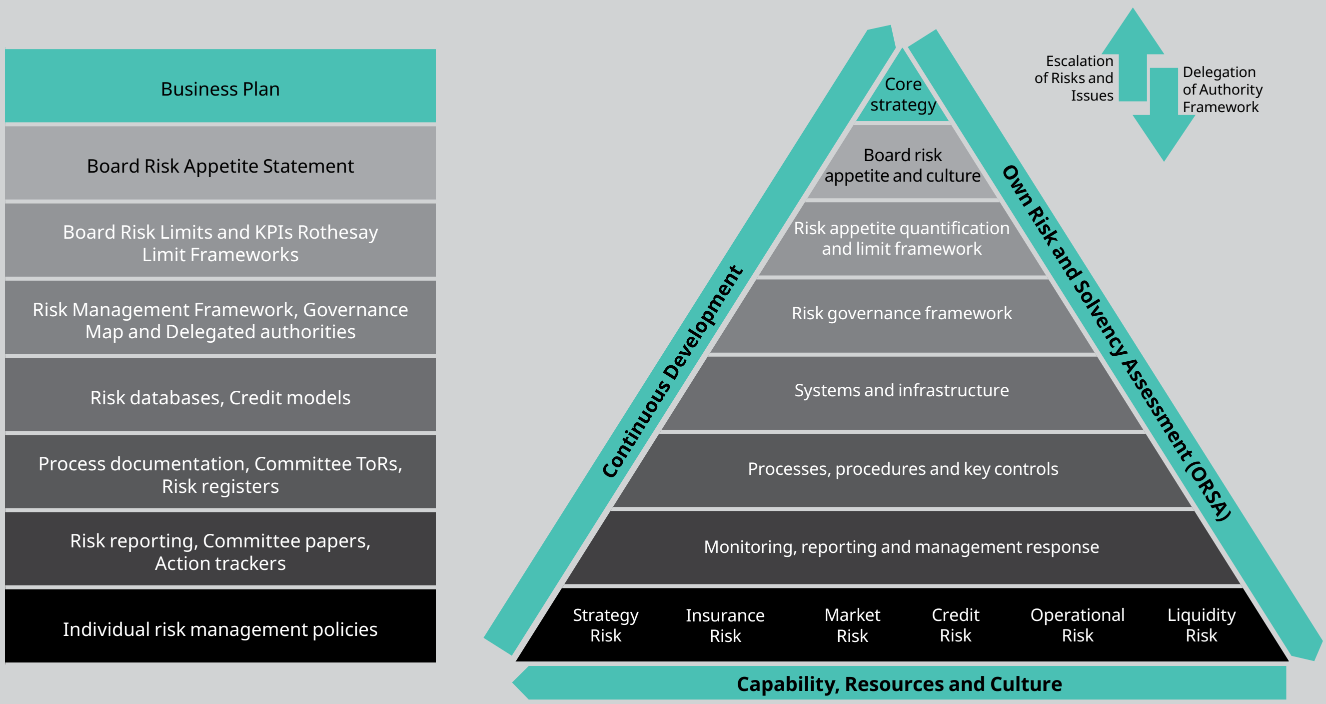
Building on this model, the RMF then adds the detail such that risk management ownership, responsibilities and processes are clear. This both informs and is directed by Rothesay's business strategy. The foundation of the RMF is the clear identification of the risks that Rothesay faces. From this, the RMF can then go on to define detailed aspects including;

- risk appetites and risk limits;
- how risks should be measured and reported on;
- processes for controlling or managing risks; and
- individual accountability for risk topics.

In order to do this Rothesay has defined a Risk Taxonomy, which is a consistent way of describing and subdividing risks consistently across Rothesay and between time periods. This is regularly reviewed to ensure that it is complete. The six key risks identified are set out in the table below.

Risk category	Definition
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, project risk and cyber security risk.

These risks are then split into more granular risks, for example market risk includes interest rate risk, inflation risk, currency risk and so on.



Risk management continued

Board risk appetite and culture

Rothesay's risk appetite expresses the types of risk that Rothesay is willing to take 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 also aim to protect regulatory surplus, manage liquidity and minimise balance sheet volatility.

Risk taking is 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, tolerated or undesired.

Risk preference	Description	Examples
DESIRED	**Desired risks** are those that we need to seek directly in order to deliver our core strategic goals. We will actively seek to take on these risks because taken together they are expected to deliver a good risk-adjusted return. These are also risks we believe we have the capability and capacity to manage effectively within risk appetite limits.	Most **Insurance Risks** (given that our key business line is writing annuities), some **Credit Risks** (given our desire to make a return through backing annuities with credit assets) and some **Strategy Risks** (given our clearly defined strategy).
TOLERATED	**Tolerated risks** are those that we incur indirectly as a result of implementing our core strategy, and where we may be willing to accept some exposure. We will invest to ensure that these risks are adequately managed. We may seek to partially or fully reduce these risks depending on relative risk-adjusted returns.	Tolerated risks therefore mostly relate to **Market Risks,** where our business model naturally exposes us to these risks but we seek to reduce or hedge them partially or fully.
UNDESIRED	**Undesired risks** are those that we incur indirectly as a result of implementing our core strategy, and where we would ideally seek to fully eliminate the exposure. These typically include risks where there is no compensation for holding the risk e.g. Operational Risk, but also risks which we do not feel sufficiently competent to manage. We are willing to invest in order to avoid or manage these risks as far as possible. Even where significant action is taken, some residual risk may be unavoidable.	Undesired risks include most **Liquidity Risks** (as we have no desire to fail to pay our policyholders and counterparties), and **Operational Risks** (as these are unrewarded).

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 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 supports compliance with the Senior Managers and Certification Regime (SMCR).

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

Rothesay has developed appropriate processes and documented procedures, appropriate controls and other risk mitigation techniques in order to effectively manage risks. The policy framework ensures that an appropriate suite of risk management policies is maintained which sets out the principles and standards for risk identification, measurement, mitigation, control and monitoring.

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.

Rothesay's risk culture is set from the top down, with the Board and Senior Management ensuring that risk management is embedded throughout the organisation, and demonstrating day-to-day how risk management informs decisions big and small. Risk management and conduct are an integral part of Rothesay's performance review process, ensuring that all Rothesay employees are held to the highest standards.

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.

Risk management continued

Principal risks and uncertainties facing Rothesay

Rothesay's principal risks are credit, insurance, climate, 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 over time

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

Risk	Mitigation	Strategic priority	Change from 2021 annual report
Credit risk The risk that a borrower's creditworthiness deteriorates or that the borrower 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. 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	↑ Rising interest rates and inflation combined with potential recession may adversely impact some of our borrowers.
Counterparty default risk 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. Derivative and reinsurance contracts are subject to margining requirements to ensure exposures are appropriately collateralised. Rothesay actively monitors counterparties for downgrade risk, and may also purchase credit protection to mitigate specific exposures.	1,4	↑ Rising interest rates and inflation combined with potential recession may adversely impact some of our counterparties.
Insurance risk 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. Rothesay aims to reinsure a majority of its longevity exposure. As at 31 December 2022, Rothesay had reinsured 89% of its longevity risk (2021: 84%) **(APM)**.	1,4	→ The impact of COVID-19 on future longevity remains uncertain.

Risk	Mitigation	Strategic priority	Change from 2021 annual report
Market risk 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, inflation 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. 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 continued in 2022.
Property risk 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 lifetime mortgages. 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	↑ Rising interest rates and potential recession mean that there is downwards pressure on property prices.
Liquidity risk 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 2022 led to large collateral calls. However, Rothesay's liquidity position has remained robust throughout.
Climate change Rothesay's assets are exposed to the potential impact of climate change. Such risks include: • physical risks such as increasing frequency and severity of flooding; and • transition risks which can arise from the process of adjustment towards a low-carbon economy.	Rothesay has established an ESG Working Group to focus on improving the way in which we manage this risk. 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. In addition, Rothesay considers flood risk as part of its lending policies.	1,4	→ Rothesay has become a member of the NZAOA and we have set the interim goal of reducing emissions by 20% over the next five years.

Risk management continued

Risk	Mitigation	Strategic priority	Change from 2021 annual report
Operational risk The risk of operational failure, including project risk, cyber risk and 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. The Customer Conduct Committee is responsible for ensuring that stakeholders are treated fairly by Rothesay and its strategic business partners. Strategic projects are monitored by Rothesay's change management function and relevant committees and are required to operate according to our project management framework. 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. 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 strategic business partners have demonstrated operational resilience. Cyber and financial crime risk continue to be heightened. Rothesay has experienced pressure on staff retention and recruitment.
Strategic, political and regulatory risk 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. Rothesay's potential exposure to leasehold reform is mitigated by structural protections in the loans advanced. 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. 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. as well as ongoing regulatory change in the UK. The Government's planned reform of the leasehold market could have an adverse impact on Rothesay's loans secured on ground rents.

Changes in Rothesay's risk profile and emerging risks

2022 has brought a real-life stress test that would have been hard to imagine just 12 months earlier, with considerable volatility in interest rates, exchange rates and inflation. Market levels of interest rates are now considerably higher than at the end of 2021, and inflation has spiked driven by higher global energy and food prices bringing pressure to many industries. As a result, credit market conditions have also deteriorated.

The invasion of Ukraine by Russia has led to continuing volatility in the global macroeconomic environment. We have no direct credit exposure to the region through our investment portfolio, but continue to carefully monitor and manage the wider macroeconomic implications of the conflict and associated sanctions imposed on Russia.

Rothesay's biggest inflation exposure is to long-term rates of inflation because our insurance liabilities are often inflation-linked. We closely hedge our inflation exposure using derivatives and inflation-linked assets and we stress inflation as part of our stress and scenario testing. We have also reviewed our investment portfolio to ensure that our borrowers can withstand the impact of higher levels of realised inflation, given potential impacts on input costs and margins.

Our market-leading risk management systems, including access to real-time information about our risk positions, have allowed us to respond quickly to interest rate and exchange rate volatility, protecting the strength of our balance sheet and ensuring that we are able to continue to execute our business plans. Our ongoing focus on liquidity risk management means that the Group's liquidity position remained robust throughout 2022.

Despite the successful operation of our risk management framework in 2022, we are constantly reviewing and improving the entire framework to ensure that it continues to provide the insights to ensure effective risk-based decision making at all levels of the organisation.

In 2022, Rothesay wrote £3.3bn of new business. We manage assets of over £47bn and insure the pensions of over 825,000 individuals.

We also entered into five new longevity reinsurance agreements, three of which are in relation to historic business and two are in relation to new business written in 2022. This means our reinsurance coverage is now 89% (2021: 84%). 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. During 2022, we have continued to invest in lifetime mortgages and now hold a portfolio of £5.1bn. We also continue to fund Dutch residential mortgages and long-term, fixed rate mortgages in the UK. Although these types of mortgage are secured on residential property, the risk profiles of lifetime mortgages and fixed-for-term mortgages are quite different. Where possible, we have continued to switch assets to improve risk-adjusted returns or to reduce the risk of our portfolio. This includes consideration of climate-related risks. We continue to actively monitor and manage potential downgrade risk across the investment portfolio, particularly as continued sustained inflation and uncertain central bank monetary responses, may drive macro and individual counterparty weakness.

A combination of economies entering into recession and rising interest rates has led to pressure on property prices and although our loans tend to be low loan-to-value and secured on higher quality properties, falling property values may lead to credit downgrades (in the case of commercial real estate), increased costs of providing the no negative equity guarantee on lifetime mortgages and increased solvency risk capital.

The long-term impact of COVID-19 is still unclear. We will need to accept COVID-19 as a part of the healthcare landscape, similar to seasonal influenza. Increased NHS backlogs and funding pressure may also adversely impact longevity, particularly in the near term.

Rothesay has continued to strengthen its control functions and the risk function, bringing in additional experts in credit risk, compliance and ESG. Work has commenced on the project to comply with the new Consumer Duty regulations which come into force in July 2023. We have also strengthened our in-house internal audit capabilities.

Good progress is being made on the development of Rothesay's technology platform. As part of this, we continue to make significant investment in our in-house technology capabilities including the management of cloud and cyber risks.

Risk management continued

There continue to be changes in accounting regulation, asset trading markets, pensions and tax, the effects of which are 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 working on changes to prudential regulation now that the UK is outside the EU (see Solvency II reform).

Transition from LIBOR

The interest rate London Interbank Offer Rate (LIBOR) benchmark ceased on 31 December 2021 and our preparations meant that the transition to alternative rates went smoothly. USD LIBOR will cease on 30 June 2023 and we are ensuring that we are appropriately prepared for this and the transition of other benchmarks.

We are now using SONIA as the basis for setting the risk-free rate under IFRS, and Solvency II.

Solvency II reform

In November 2022, HM Treasury announced its response to the consultation on Solvency II reform. In addition to the changes described earlier under capital management, HM Treasury announced that:

- The PRA will have the powers to seek assurance on internal ratings.
- Fundamental spreads will be reviewed again in five years.
- There will be a widening of Matching Adjustment eligibility rules to include "highly predictable cash flows", with prudent haircuts.
- There will also be a strengthened role of stress testing for insurers with results to be published by the firm.
- A Senior Manager will need to attest to the appropriateness of the Matching Adjustment.

The changes will result in a modest capital release for Rothesay and will facilitate investment in a wider range of assets, particularly infrastructure and other productive assets.

Also in November, the PRA published consultation paper CP14/22 'Review of Solvency II: Reporting Phase 2'. This contains further PRA proposals to streamline current Solvency II reporting and disclosure requirements for insurers, and to tailor reporting more appropriately to the UK insurance sector and the PRA's own supervisory needs. The proposed changes are intended to make regulatory disclosure less onerous though the PRA is also proposing the introduction of new disclosure requirements.

Leasehold reform

The Leasehold Reform (Ground Rent) Act 2022 came into force on 30 June 2022. It prohibits ground rents for new, qualifying long residential leasehold properties in England and Wales but does not cover the extension of existing leases. The Act has not therefore had a significant impact on our loans secured on ground rents.

We continue to monitor developments in this sector to understand the implications of potential future reforms and we participate in consultations to ensure that our interests are protected for the benefit of our stakeholders.

Emerging risks

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 and evolving global relationships.

Over the longer term there are risks relating to climate change and the way in which these could impact Rothesay's investments. The management of climate-related risks is discussed in more detail in the ESG Section.

We are also exposed to the risk of significant longevity improvements arising from developments such as new medical technologies and pharmacological breakthroughs. Rothesay manages exposure to longevity risk through extensive use of longevity reinsurance and we also hold capital to cover a range of longevity scenarios.

More broadly, Rothesay continues to manage its affairs prudently such that we are not overexposed to one particular risk and so that we only accept risks which we understand and which are consistent with our risk appetite.

Viability and going concern

Viability statement

Rothesay's strategy and business model 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 policyholders' pensions.

The period we assess

Making a viability assessment requires the principal risks 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 Own Risk and Solvency Assessment (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 January 2023, 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 does not consider there to be any going concern or viability issues beyond this timeframe.

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. The scenarios are considered appropriately severe even following the experience of 2022. Financial market stresses are calibrated to ensure that they capture the potential impact of climate change on our investments. More details on point-in-time stress testing 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 believe 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 December 2022. 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.

Our assessment of viability and going concern

Given Rothesay's significant surplus capital, the analysis showed that the Group can withstand very material adverse shocks. Based on the results of this analysis and consideration of viability were the Group to be holding surplus capital within its target operating range, 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.

Report of the Directors

The Directors present their annual report and the audited consolidated financial statements for Rothesay Life Plc, registered number 06127279, (the Company, Rothesay or RLP) for the year ended 31 December 2022. Comparative information has been presented for the year ended 31 December 2021.

1. General information

RLP is a registered public 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 RLP and its subsidiaries (the Group or Rothesay) for the year are set out in the consolidated statement of comprehensive income on page 62. All likely future developments and material assessments of the Group's performance is discussed in the Strategic Report. There were no post balance sheet events.

3. Registered office

RLP is a registered public limited company incorporated and domiciled in the United Kingdom. The registered office and principal place of business is The Post Building, 100 Museum Street, London WC1A 1PB.

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. 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 RLP during the year and at the date of approval of the financial statements.

5. Disclosure of information to auditors

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

- so far as each Director is 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.

6. Auditors

The Company has passed elective resolutions in accordance with the Companies Act 1985 to dispense with the holding of annual general meetings, the laying of accounts and reports before general meetings and the annual reappointment of auditors. PricewaterhouseCoopers LLP will, accordingly, continue in office as auditors of the Company pursuant to Section 487(2) of the Companies Act 2006.

7. Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Accounts 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 the Company financial statements in accordance with UK-adopted international accounting standards. 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 UK-adopted international accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Company will continue in business.

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

The Directors are also responsible for keeping adequate accounting records that are sufficient to show and explain the Group's 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. The Directors are responsible for the maintenance and integrity of the Company's financial statements published on the ultimate parent Company's website.

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

8. Internal control and risk management systems

The Company 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; and
- 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.

9. Stakeholder statement

The Company operates under the governance framework of the Rothesay Limited Group and an explanation of how the Rothesay Limited Group Board has considered the matters set out in s.172 is detailed within the ESG section of the Rothesay Limited Group annual report (which does not form part of this report but which can be obtained from the Company Secretary, The Post Building, 100 Museum Street, London WC1A 1PB). The RLP Board of Directors has also considered relevant matters where appropriate.

10. Streamlined Energy and Carbon Reporting

Rothesay Limited has prepared Streamlined Energy and Carbon Reporting (SECR) for the Rothesay Group. The Rothesay Limited Group SECR can be found in the ESG section of the Rothesay Limited Group annual report (which does not form part of this report but which can be obtained from the Company Secretary, The Post Building, 100 Museum Street, London WC1A 1BP).

11. Changes in Directors

- Jane Hanson CBE and Ray King stood down from the Board on 30 June 2022;
- Jackie Hunt and Angela Darlington were appointed to the Board as new independent Non-Executive Directors on 12 July 2022 and 1 August 2022 respectively;
- Geoff Craddock and Arjun Gupta were appointed to the Board as new Shareholder Directors on 20 January 2023; and
- Addy Loudiadis retired as CEO from September. Addy will continue to serve on Rothesay's Board as Founder Director.

12. Date of authorisation of issue

The financial statements were authorised for issue by the Board of Directors on 10 February 2023.

On behalf of the board
Tom Pearce
Chief Executive Officer
10 February 2023

Rothesay Life Plc Board of Directors

Chairman
Naguib Kheraj

Executive Directors
Tom Pearce
Andrew Stoker

Founder Non-Executive Director
Addy Loudiadis

Shareholder Non-Executive Directors
Tim Corbett
Robin Jarratt
Geoff Craddock
Arjun Gupta

Independent Non-Executive Directors
Stan Beckers
Angela Darlington
Ed Giera
Jackie Hunt
Heather Jackson
Terry Miller
Charles Pickup
Bill Robertson

Independent auditors' report to the members of Rothesay Life Plc

Report on the audit of the financial statements

Opinion
In our opinion, Rothesay Life Plc'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 2022 and of the Group's profit and the Group's and Company's cash flows for the year then ended;
- have been properly prepared in accordance with UK-adopted international accounting standards as applied in accordance with the provisions 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 2022 (the "Annual Report"), which comprise: Consolidated and Company statements of financial position as at 31 December 2022; the Consolidated statement of comprehensive income, the Consolidated and Company cash flow statements, and the Consolidated and Company statements 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.

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)"), International Standards on Auditing issued by the International Auditing and Assurance Standards Board ("ISAs") and applicable law. Our responsibilities under ISAs (UK) and ISAs 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 the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code), 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 either the FRC's Ethical Standard or Article 5(1) of Regulation (EU) No 537/2014 were not provided.

Other than those disclosed in note B.7 Auditors' remuneration, we have provided no non-audit services to the Company or its controlled undertakings 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.

Key audit matters
- Valuation of insurance contract liabilities - Longevity Methodology and Assumptions (Group and Parent)
- Valuation of insurance contract liabilities - Credit Default Risk Methodology and Assumptions (Group and Parent)
- Valuation of investments classified as Level 3 under IFRS 13 (Group and Parent)
- Disclosure of the expected impact of initial application of IFRS 17 in accordance with IAS 8 (Group and Parent).

Materiality
- Overall Group materiality: £75,000,000 (2021: £75,000,000) based on a materiality value that is an equivalent of 1.2% of Total Equity.
- Overall Company materiality: £75,000,000 (2021: £75,000,000) based on a materiality value that is an equivalent of 1.2% of Total Equity.
- Performance materiality: £56,250,000 (2021: £56,250,000) (Group) and £56,250,000 (2021: £56,250,000) (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.

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.

Disclosure of the expected impact of initial application of IFRS 17 in accordance with IAS 8 is a new key audit matter this year. 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 and Parent)	
As disclosed in note E.2 Reinsurance assets/liabilities and E.3 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 and relevant key controls 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 2021.	• Assessed the methodologies used to derive the mortality assumptions and the appropriateness of expert judgements used. For example, the derivation of the mortality assumptions, appropriateness of experience data, the selection and parameterisation of the CMI model including the calibration of parameters (e.g. smoothing parameter, long-term rate) and choice of base mortality table, and the determination of the prudential margin applied;
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; • Considered management's assessment of the potential impact of the COVID-19 pandemic on longevity assumptions; and • Assessed the disclosure of the longevity assumptions and the associated financial impact on the liabilities arising from changes in these assumptions over 2022. 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.

Independent auditors' report to the members of Rothesay Life Plc continued

Key audit matter	How our audit addressed the key audit matter
Valuation of insurance contract liabilities Credit Default Risk Methodology and Assumptions (Group and Parent)	
As disclosed in note E.3 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) for both liquid and illiquid asset classes with reference to relevant rules and actuarial guidance and by applying our industry knowledge and experience;
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 has also increased the uncertainty in relation to the credit default assumptions made. For 2022 year end, adjustments have been made to calibrations to the credit default modelling assumptions for the illiquid asset classes to reflect the most up to date information available.	• Tested controls performed by management over the approval and implementation of credit default assumptions (to the extent available); • Validated significant assumptions used by management against market observable data (to the extent available and relevant) and our experience of market practices; • Compared the assumptions selected against those adopted by peers (to the extent available); • 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 • Assessed the disclosure of the credit default risk assumptions and the associated financial impact on the liabilities from changes in these assumptions over 2022. 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 investments classified as Level 3 under IFRS 13 (Group and Parent)	
As disclosed in notes D.2 Financial Investments, D.3 Derivatives, and D.7 Payables and financial liabilities	The procedures to assess the appropriateness of the valuation of investments classified as Level 3 included the following:
Financial investments classified as Level 3 under the IFRS 13 fair value hierarchy is a material balance and comprise investments in Loans secured on property which include commercial real estate loans, loans secured on ground rents, Dutch residential mortgages (DRM), investments in lifetime mortgages, and Limited Price Indexation (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 lifetime mortgage portfolio has continued to increase significantly in the current year following the acquisition of one new lifetime mortgage back book portfolios 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;

Key audit matter	How our audit addressed the key audit matter
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.	• Understood the valuation models used by management and obtained evidence to support the model's operation is in line with methodology; • Engaged our relevant experts to assess the appropriateness of management's methodology and internal credit rating methodology; • Independently revalued a sample of investments, including revaluation of the lifetime mortgage portfolio at year end using an independent model; • Tested significant inputs into the valuation of Level 3 financial investments to external sources, where possible. This included consideration of possible external factors on these inputs such as those related to climate change or the wider economic environment; • Considered the appropriateness of the spreads that represent the unobservable input to the valuation of the LPI derivative portfolio; and • Assessed the adequacy of disclosures in the financial statements. Based on the procedures performed and evidence obtained, we consider the valuation of Level 3 financial investments to be appropriate.
Disclosure of the expected impact of initial application of IFRS 17 in accordance with IAS 8 (Group and Parent)	
Refer to Note A.4 Accounting policies and change in accounting policies.	We performed the following procedures to assess the reasonableness of the disclosure of estimated impact of the initial adoption of IFRS 17:
International Accounting Standard 8: Accounting Policies, Changes in Accounting Estimates and Errors (IAS 8), requires the disclosure of reasonably estimable information relevant to assessing the possible impact of new accounting standards issued but not yet effective. International Financial Reporting Standard 17, Insurance Contracts, (IFRS 17 or the standard) became effective for periods beginning on or after 1st January 2023. The related IAS 8 disclosures in these financial statements are intended to provide users with an understanding of the estimated impact of the new standard, and as a result, are more limited than the disclosures which will be required within the 2023 interim and annual reports.	• Considered whether the accounting policies chosen were in accordance with the standard, and the models developed were in line with those policies;
We have determined the disclosure of the impact of IFRS 17 to be a key audit matter because of the significant changes introduced under the new standard, and subjectivity in the level of IAS 8 disclosure of information relevant for the estimated impact.	• Understood the relevant controls and governance process for the determination and approval of accounting policies, including the key methodologies, judgments and assumptions;

Independent auditors' report to the members of Rothesay Life Plc continued

Key audit matter	How our audit addressed the key audit matter
IFRS 17 adoption is expected to significantly reduce the Group's total equity as at the transition date. This is due to the slower release of profits under IFRS 17 compared to IFRS 4 under the mechanism by which profits are deferred within the Contractual Service Margin (CSM) and amortised over the duration of a contract.	• Obtained an understanding of and challenged the key methodologies, judgements and assumptions used to develop and calculate the IFRS 17 estimate impacts. We involved PwC actuarial specialists to evaluate the key actuarial judgments made including the approach to the fair value CSM calculation, the calculation of the fully retrospective CSM at inception, and an estimation of the amortisation of the CSM at the transition date;
The implementation of IFRS 17 requires the Group to interpret the requirements of the new standard and make significant judgments and assumptions to develop its accounting policies. Key judgments made include the determination of the date before which it is impracticable to apply the fully retrospective approach, the approach for how the fair value and fully retrospective CSM have been determined for both insurance and reinsurance contracts, and the CSM amortisation approach for deferred annuities.	• Performed controls and substantive testing, including the involvement of actuarial specialists, over the calculation that has been developed to determine the disclosed range of impacts to Group equity on transition; and
New models and processes are required in order to calculate the key components of the transition impact. An estimated range of the impact as at 1st January 2022 has been disclosed, alongside the key estimation uncertainties used in determining the range.	• Reviewed the IAS 8 quantitative and qualitative disclosures. This included the consideration of whether the valuation of the range disclosed is appropriate, and whether the quantitative and qualitative disclosure is in line with IAS 8. Based on the audit procedures performed and evidence obtained, we consider the disclosures related to the initial impact of IFRS 17, and key judgments and assumptions 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.

The Group consists of 5 subsidiary companies and the Parent Company, Rothesay Life Plc. Of the companies within the Group, the most significant component is the Company, which conducts all of the insurance business of the Group. PwC UK is the Group and Company auditors for components requiring statutory audits.

Based on the output of our risk assessment, along with our understanding of the Group structure, we performed a full scope audit over the Company.

We completed review procedures over the other components not subject to full scope audits.

The impact of climate risk on our audit

As part of our audit we made enquiries of management to understand the process adopted to assess the extent of the potential impact of climate risk on the Group's Annual Report and Accounts and support the disclosures made.

Management have made disclosures in the Group's Environment, Social and Governance Report section of the Annual Report and Accounts in relation to climate change (including the Task Force on Climate-related Financial Disclosures (TCFD)). Management have made commitments to achieving net zero emissions by 2050 and to transitioning their investment portfolio to net zero greenhouse gas emissions by 2050, aligned with a maximum temperature rise of 1.5°C above pre-industrial levels as outlined in the Paris Agreement. Detailed disclosure relating to this is included within Rothesay's Environmental, Social and Governance Report 2021 which is published separately. We have considered these disclosures as part of our consideration of other Information disclosed in the Annual Report and Accounts as set out in the 'Reporting on other information' section of this report.

The key area of the financial statements where management evaluated that climate risk has a potential impact is in the valuation of financial investments. We agree that this is the key area of potential impact and that the relevant disclosures that have been made within the financial statements are appropriate.

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	£75,000,000 (2021: £75,000,000).	£75,000,000 (2021: £75,000,000).
How we determined it	a materiality value that is an equivalent of 1.2% of Total Equity	a materiality value that is an equivalent of 1.2% of Total Equity
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 determine a materiality value for the Company using the same rationale as for the benchmark applied to the Group financial statements.

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% (2021: 75%) of overall materiality, amounting to £56,250,000 (2021: £56,250,000) for the Group financial statements and £56,250,000 (2021: £56,250,000) for the Company financial statements.

Independent auditors' report to the members of Rothesay Life Plc continued

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 £3,750,000 (Group audit) (2021: £3,750,000) and £3,750,000 (Company audit) (2021: £3,750,000) 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:

- obtaining management's updated going concern assessment and material assumptions made using our knowledge of Group and Company's business performance, review of regulatory correspondence and obtaining further corroborating evidence;
- considering management's assessment of the regulatory solvency coverage and liquidity position in the forward looking scenarios considered, which have been driven by the Group's ORSA;
- considering 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; and
- inquiring and understanding the actions taken by management to mitigate the identified risks, 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.

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 2022 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) and ISAs 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.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, 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 and the Financial Conduct Authority, 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 financial statements such as 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 insurance contract liabilities and the valuation of investments classified as Level 3 under IFRS 13. Audit procedures performed by the engagement team included:

- Discussions with the Board, management, Internal Audit, senior management involved in the Risk and Compliance functions and the Group'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 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 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; the valuation of investments classified as Level 3 under IFRS 13 described in the related key audit matters; as well as considering 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; and
- 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.

Independent auditors' report to the members of Rothesay Life Plc continued

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. 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.

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 in accordance with ISAs (UK) is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group and Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group and Company audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

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 16 years, covering the years ended 30 November 2007 to 31 December 2022.

Sue Morling (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

10 February 2023

Section

2

Financial statements

The financial statements set out the consolidated results for Rothesay Life Plc and its subsidiaries for the year ended 31 December 2022.

Consolidated statement of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2022

	Note	2022 £m	2021 £m
Income			
Gross premiums written	B.1	**3,579**	3,205
Premiums ceded to reinsurers		**(2,175)**	(1,636)
Net premiums written		**1,404**	1,569
Investment return	B.2	**(15,376)**	48
Total revenue		**(13,972)**	1,617
Expenses			
Policyholder claims		**(2,913)**	(2,901)
Less: reinsurance recoveries		**2,051**	1,521
Change in insurance contract liabilities	E.3	**15,918**	1,216
Change in the reinsurers' share of insurance contract liabilities	E.1	**(485)**	(198)
Net claims and change in insurance liabilities		**14,571**	(362)
Acquisition and administration expenses	B.3	**(229)**	(221)
Finance costs	B.4	**(194)**	(116)
Total expenses		**14,148**	(699)
Profit before tax		**176**	918
Income tax expense	B.8	**(30)**	(176)
Profit for the financial year		**146**	742

	Note	2022 £m	2021 £m
Profit for the financial year		**146**	742
Other comprehensive income			
Items that are or may be reclassified to profit or loss:		**–**	–
Cash flow hedges:			
Fair value gains during the year	C.3	**3**	1
Total comprehensive income for the year		**149**	743

All income and expenses are related to continuing operations.

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

Consolidated statement of financial position

AS AT 31 DECEMBER 2022

	Note	2022 £m	2021 £m
Assets			
Property, plant and equipment	D.1	**18**	11
Deferred tax asset	G.1	**2**	–
Lease - right of use asset	I.5	**27**	30
Financial investments	D.2	**90,928**	83,845
Reinsurance assets	E.1	**185**	641
Accrued interest and prepayments	D.4	**806**	641
Receivables	D.5	**2,433**	511
Cash and cash equivalents	D.6	**243**	332
Total assets		**94,642**	86,011
Equity and liabilities			
Equity			
Share capital	C.1	**510**	510
Tier 1 notes	C.2	**793**	793
Share premium	C.3	**–**	1,953
Hedging reserve	C.3	**4**	1
Retained earnings	C.3	**4,954**	2,882
Total equity		**6,261**	6,139
Liabilities			
Reinsurance liabilities	E.1	**1,245**	1,217
Insurance contract liabilities	E.3	**38,112**	54,030
Payables and financial investment liabilities	D.7	**47,126**	22,784
Leasehold liabilities	I.5	**39**	42
Borrowings	D.8	**1,764**	1,725
Deferred tax liabilities	G.1	**–**	5
Accruals	D.9	**95**	69
Total liabilities		**88,381**	79,872
Total equity and liabilities		**94,642**	86,011

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

The financial statements were approved by the Board of Directors on 10 February 2023 and signed on its behalf by:

Tom Pearce
Chief Executive Officer
10 February 2023
Company number 06127279

Consolidated statement of changes in equity

FOR THE YEAR ENDED 31 DECEMBER 2022

	Notes	Share capital £m	Share premium £m	Tier 1 notes £m	Hedging reserve £m	Profit and loss reserve £m	Total equity £m
As at 1 January 2022		**510**	**1,953**	**793**	**1**	**2,882**	**6,139**
Other comprehensive income for the year		**–**	**–**	**–**	**3**	**–**	**3**
Capital reorganisation	C.3	**–**	**(1,953)**	**–**		**1,953**	**–**
Tier 1 note coupon	C.2, C.3	**–**	**–**	**–**	**–**	**(34)**	**(34)**
Tier 1 coupon tax relief	C.2, C.3	**–**	**–**	**–**	**–**	**7**	**7**
Profit for the financial year	C.3	**–**	**–**	**–**	**–**	**146**	**146**
As at 31 December 2022		**510**	**–**	**793**	**4**	**4,954**	**6,261**

FOR THE YEAR ENDED 31 DECEMBER 2021

	Notes	Share capital £m	Share premium £m	Tier 1 notes £m	Hedging reserve £m	Retained earnings £m	Total equity £m
As at 1 January 2021		510	1,953	347	–	2,143	4,953
Prior year adjustment		–	–	–	–	(3)	(3)
Issuance of RT1 notes	C.2	–	–	446	–	–	446
Other Comprehensive income for the year		–	–	–	1	–	1
Profit for the financial year	C.3	–	–	–	–	742	742
As at 31 December 2021		510	1,953	793	1	2,882	6,139

Consolidated cash flow statement

FOR THE YEAR ENDED 31 DECEMBER 2022

	Notes	2022 £m	2021 £m
Cash flows from operating activities			
Profit for the financial year		**146**	742
Adjustments for non-cash movements in net profit for the financial period			
FX on USD borrowings		**35**	–
Prior year adjustment		**–**	(3)
Depreciation	D.1	**2**	1
Leasehold depreciation	I.5	**3**	4
Amortisation of debt costs	B.4	**4**	9
Financing charge on leasehold	I.5	**1**	1
Interest income	B.2	**(1,788)**	(1,445)
Interest expense	B.4	**189**	105
Income tax expense	B.8	**38**	139
Hedging reserve	C.3	**3**	1
Net (increase)/decrease in operational assets			
Financial investments	D.2	**(7,083)**	9,867
Reinsurance asset	E.1	**456**	(25)
Receivables	D.5	**(1,880)**	459
Prepayment	D.4	**(24)**	6
Net (decrease)/increase in operational liabilities			
Insurance contract liabilities	E.1	**(15,918)**	(1,216)
Reinsurance liabilities	E.1	**28**	224
Financial investment liabilities	D.7	**20,635**	(10,152)
Other payables	D.7	**3,714**	(520)
Deferred tax	G.1	**(7)**	5
Accruals	D.9	**–**	(8)
Net cash flows used in operating activities		**(1,446)**	(1,806)
Interest paid		**(163)**	(98)
Interest received		**1,648**	1,460
Tax paid		**(81)**	(229)
Net cash flows used in operating activities		**(42)**	(673)
Cash flows used in financing activities			
Interest payment on Tier 1 note	C.3	**(34)**	–
Cash flow on leasehold	I.5	**(4)**	–
Proceeds from issuance of debt (net of issuance costs)	D.8	**–**	290
Proceeds from issuance of Tier 1 notes (net of issuance costs)	C.2	**–**	446
Net cash flows (used)/generated from in financing activities		**(38)**	736
Net cash outflows used in investing activities			
Acquisition of property, plant and equipment	D.1	**(9)**	(5)
Net cash outflows used in investing activities		**(9)**	(5)
Net (decrease)/increase in cash and cash equivalents		**(89)**	58
Cash and cash equivalents at 1 January	D.6	**332**	274
Cash and cash equivalents at 31 December	D.6	**243**	332

Company statement of financial position

AS AT 31 DECEMBER 2022

	Note	2022 £m	2021 £m
Assets			
Investment in subsidiaries	H.2	**13**	13
Property, plant and equipment	D.1	**18**	11
Deferred tax asset	G.1	**339**	–
Lease - right of use asset	I.5	**27**	30
Financial investments	D.2	**90,720**	83,845
Reinsurance assets	E.1	**185**	641
Accrued interest and prepayments	D.4	**806**	641
Receivables	D.5	**2,676**	785
Cash and cash equivalents	D.6	**195**	159
Total assets		**94,979**	86,125
Equity and liabilities			
Equity			
Share capital	C.1	**510**	510
Tier 1 notes	C.2	**793**	793
Hedging reserve	C.3	**4**	1
Share premium	C.3	**–**	1,953
Retained earnings	C.3	**4,954**	2,882
Total equity		**6,261**	6,139
Liabilities			
Reinsurance liabilities	E.1	**1,245**	1,217
Insurance contract liabilities	E.3	**38,112**	54,030
Payables and financial liabilities	D.7	**47,463**	22,784
Leasehold liabilities	I.5	**39**	42
Borrowings	D.8	**1,764**	1,725
Deferred tax liabilities	G.1	**–**	119
Accruals	D.9	**95**	69
Total liabilities		**88,718**	79,986
Total equity and liabilities		**94,979**	86,125

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

The profit for the financial year of the Company was £146m (2021: profit of £742m). 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 10 February 2023 and signed on its behalf by:

Tom Pearce
Chief Executive Officer
10 February 2023
Company number 06127279

Company statement of changes in equity

FOR THE YEAR ENDED 31 DECEMBER 2022

	Share capital £m	Share premium £m	Tier 1 notes £m	Hedging reserve £m	Profit and loss reserve £m	Total equity £m
As at 1 January 2022	**510**	**1,953**	**793**	**1**	**2,882**	**6,139**
Capital reorganisation	**–**	**(1,953)**	**–**	**–**	**1,953**	**–**
Profit for the financial year	**–**	**–**	**–**	**–**	**146**	**146**
Tier 1 note coupon	**–**	**–**	**–**	**–**	**(34)**	**(34)**
Tier 1 coupon tax relief	**–**	**–**	**–**	**–**	**7**	**7**
Other comprehensive income for the year	**–**	**–**	**–**	**3**	**–**	**3**
As at 31 December 2022	**510**	**–**	**793**	**4**	**4,954**	**6,261**

FOR THE YEAR ENDED 31 DECEMBER 2021

	Share capital £m	Share premium £m	Tier 1 notes £m	Hedging reserve £m	Retained earnings £m	Total equity £m
As at 1 January 2021	510	1,953	347	–	2,140	4,950
Profit for the financial year	–	–	–	–	742	742
As at Tier 1 note issuance	–	–	446	–	–	446
Other comprehensive income for the year	–	–	–	1	–	1
As at 31 December 2021	510	1,953	793	1	2,882	6,139

Company cash flow statement

FOR THE YEAR ENDED 31 DECEMBER 2022

	Note	2022 £m	2021 £m
Cash flows from operating activities			
Profit for the financial year		**146**	742
Adjustments for non-cash movements in net profit for the year			
FX on USD borrowings		**35**	–
Depreciation	D.1	**2**	1
Leasehold depreciation	I.5	**3**	4
Amortisation of debt costs	B.4	**4**	9
Financing charge on leasehold	I.5	**1**	1
Interest income	B.2	**(1,788)**	(1,445)
Interest expense	B.4	**189**	105
Income tax expense	B.8	**489**	139
Hedging reserve	C.3	**3**	1
Net (increase)/decrease in operational assets			
Financial investments	D.2	**(6,875)**	9,867
Reinsurance asset	E.1	**456**	(25)
Receivables	D.5	**(1,850)**	339
Prepayment	D.4	**(24)**	6
Net (decrease)/increase in operational liabilities			
Insurance contract liabilities	E.1	**(15,918)**	(1,216)
Reinsurance liabilities	E.1	**28**	224
Financial investment liabilities	D.7	**20,635**	(10,152)
Other payables	D.7	**3,601**	(520)
Deferred tax	G.1	**(458)**	37
Accruals		**–**	(8)
Net cash flows used in operating activities		**(1,321)**	(1,891)
Interest paid		**(163)**	(98)
Interest received		**1,648**	1,460
Tax paid		**(81)**	(229)
Cash flows generated through/(used) in operating activities		**83**	(758)
Cash flows used in financing activities			
Interest payment on Tier 1 note		**(34)**	–
Cash flow on leasehold	I.5	**(4)**	–
Proceeds from issuance of debt (net of issuance costs)	D.8	**–**	290
Proceeds from issuance of Tier 1 notes (net of issuance costs)	C.2	**–**	446
Net cash flows (used in)/generated from financing activities		**(38)**	736
Net cash outflows from investing activities			
Acquisition of property, plant and equipment	D.1	**(9)**	(5)
Net cash outflows from investing activities		**(9)**	(5)
Net increase/(decrease) in cash and cash equivalents		**36**	(27)
Cash and cash equivalents at 1 January	D.6	**159**	186
Cash and cash equivalents at 31 December	D.6	**195**	159

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 UK-adopted International Accounting Standards. The accounting policies have been applied consistently. The financial statements have been prepared on a going concern basis.

The Directors have considered the appropriateness of adopting the going concern basis for the preparation of the consolidated financial statements. The Board has considered forward-looking scenarios intended to test the impact of stresses and scenarios that may impact Rothesay's ability to execute its business plan. The results demonstrate the robustness of Rothesay's solvency. Management and the Board believe Rothesay is well capitalised on both a regulatory and economic capital basis and therefore the Board believes it is appropriate to continue to adopt the going concern basis of accounting (see viability and going concern section).

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 66.

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 reassesses 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.

Notes to the financial statements continued

Note A - Significant accounting policies (continued)

A.1 Basis of preparation and consolidation (continued)

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. 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).
- Assessment as to whether there is sufficient reasonable and supportable information available for the fully retrospective approach to be used for the transition to IFRS 17 (see note A.4).

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.2).
- Measurement of net insurance contract liabilities (see notes E.2 and E.3).
- The impact of the adoption of IFRS 17 in relation to the measurement of the fulfilment cash flows and the contractual service margin for all historical business (see note A.4).

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 2023; and
- explanation of any changes made to past assumptions if the uncertainty is unresolved.

A.2 Contract classification

Using judgement, 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 currency transactions

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. The results and financial position of all Group companies that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- asset and liabilities are translated at the closing rate;
- income, expenses and cash flows denominated in foreign currency are translated at average exchange rates; and
- all resulting exchange differences are recognised through the statement of consolidated comprehensive income and taken to the currency transaction reserve within equity.

Note A - Significant accounting policies (continued)

A.4 Accounting policies and change in accounting policies

Accounting policies have been consistently applied in these consolidated financial statements. Where accounting policies can be directly attributed to a specific note, the policy is presented in that note.

Historically, interest on the RT1 notes classified as equity has been incorrectly included in interest payable on third party borrowings. From 1 January 2022, this interest has been accounted for as an appropriation of equity, net of tax, consistent with the relevant accounting standard (see note B.4). This matter is considered to be immaterial and therefore a prior year reclassification has not been made. Rothesay has not adopted any new standards or any changes to existing standards, including matters of significant judgement and use of estimates.

The following standards and amendments were issued before 30 September 2022 with effective date for accounting periods ending on or after 1 October 2022.

Amendments to IFRS 3, 'Business combinations':

The amendment updates a reference in IFRS 3 to the conceptual framework for financial reporting without changing the accounting requirements for business combinations. The amendment has no impact on Rothesay.

Amendments to IAS 16, 'Property, plant and equipment':

The amendments prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the assets of its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss. The amendment has no impact on Rothesay.

Amendments to IAS 37, 'Provisions, contingent liabilities and contingent assets':

The amendment specifies which costs a company includes when assessing whether a contract will be loss-making. The amendment has no impact on Rothesay.

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'. These amendments are not expected to have any impact on Rothesay.

The following standards are effective for annual periods on or after 1 January 2023:

IFRS 17, 'Insurance contracts', as amended in June 2020:

IFRS 17, the accounting standard for insurance contracts, is effective for reporting periods beginning on or after 1 January 2023. The standard will have a significant impact on the way Rothesay's results are reported because the standard rebuilds performance measurement 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 retrospectively for all business. 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 2022, we have made significant progress in refining our approaches, models, business operations and systems in readiness for transition to IFRS 17. At this stage, we are refining our IFRS 17 methodologies, however we are able to set out our key accounting policies and approaches below.

Under IFRS 17, we will use the General Measurement Model (GMM) for the derivation of all our insurance liabilities. Under the GMM, our liabilities will comprise the following building blocks:

- **Best estimate liability (BEL):** An explicit and unbiased estimate of future cash flows that will arise as Rothesay fulfils the contracts discounted using an approach that reflects the characteristics of the liability.
- **Risk adjustment (RA):** This reflects the compensation that Rothesay requires for bearing the non-financial uncertainty in the liabilities.
- **Contractual Service Margin (CSM):** This represents the unearned profit that Rothesay will recognise over time as it provides services in the future of the insurance contract.

Notes to the financial statements continued

Note A - Significant accounting policies (continued)

A.4 Accounting policies and change in accounting policies (continued)

Best estimate liabilities (BEL)

In determining the BEL, we will use best estimate assumptions based on available market data in an unbiased way. Where possible, we will use assumptions which are consistent with those used for deriving the best estimate liabilities under other financial reporting metrics such as MCEV and Solvency II.

Risk adjustment (RA)

In determining the RA, we will use the provision for adverse deviation approach (the PAD approach) under which we will apply margins to the best estimates for demographic and expense risk. Allowance will also be made for operational risk. These allowances will reflect Rothesay's compensation for bearing the uncertainty around these risks. A consistent technique will be applied to both insurance and reinsurance contracts, with the RA related to reinsurance reflecting the amount of RA ceded as a result of transacting reinsurance contracts.

Contractual service margin (CSM)

The CSM is calculated at the inception of the contract and is released as profit as the liability is discharged.

We will calculate the CSM as the difference between the premium received by Rothesay and the fulfilment cash flows (the sum of BEL and RA). For reinsurance contracts, the CSM represents the net cost or gain on purchasing reinsurance based on the net outflow to the reinsurer and the associated reduction in RA.

In determining the CSM amortisation, we consider the services delivered under the contract and define the coverage units that should be used to amortise the CSM over time. The services delivered include both the insurance service and the investment return service. We define the quantity of benefit provided as part of the insurance service as the expected payment due to the policyholder in each period contingent on the insured event occurring (i.e. survival until the payment date). The quantity of benefits provided as part of the investment return service includes both the value generated to the policyholder by investing the deferred policy premiums, and the value that Rothesay stands ready to pay the policyholder upon exercise of their member options before the in-payment period. The blended coverage unit will be calculated by appropriately weighting the expected insurance and investment return service coverage units such that by the time a deferred annuitant reaches retirement, the CSM is in line with that of an equivalent annuitant.

Discount rates

We are required to use discount rates to measure the BEL and RA and to determine the interest to accrete on the CSM, and measure the impact of adjustments to the CSM. We already use a number of methods to determine discount rates under current reporting bases and intend, where possible, to leverage existing methodologies for determining the appropriate discount rates under IFRS 17. The chosen discount rates will vary depending on the characteristics of the liabilities being valued. We will use separate discount rates to value our insurance contracts and our longevity only reinsurance contracts.

- For insurance contracts, we will use a top-down approach to deriving the discount curve based on the market consistent rate of return on a reference portfolio of assets appropriate to back the liabilities. Such an approach is consistent with that used under MCEV.
- For collateralised longevity only reinsurance contracts, we will reflect the comparatively higher liquidity of collateralised cash flows (namely the actual claims made and the premiums paid) by deriving a discount curve from the assets that can be posted as collateral under the relevant contracts.

The locked in rate used for the CSM calculations for insurance contracts will be in line with the discount rates used to discount the projected BEL and RA at initial recognition.

Transition

As part of the transition to IFRS 17, we will need to determine a CSM for all historic business. Where possible (in practice, for business written from 2016 onwards), we will use the fully retrospective approach for determining the CSM. Where this approach is not practicable as reasonable and supportable information is not readily available (determined to be business written before 2016), we will use the fair value approach under which the CSM is calculated as the fair value of the liabilities less the best estimate of the liabilities and risk adjustment as at transition date (1 January 2022). The fully retrospective approach is not practicable for business written prior to 1 January 2016 due to data and system constraints which existed pre the introduction of Solvency II, particularly in relation to subsequent changes in assumptions and estimates.

Note A - Significant accounting policies (continued)

A.4 Accounting policies and change in accounting policies (continued)

Under the fully retrospective approach, we will calculate the CSM on the date the business was written as described above. The CSM is then rolled forward, allowing for interest accretion, CSM adjustments at the locked in rate, and amortisation, to derive the CSM at the valuation date.

Under the fair value approach, the relevant fair value premiums will be derived by applying an appropriate discount rate to the best estimate cash flows. The appropriate discount rate will be determined using the rate of discount that would need to be applied to the best estimate cash flows to derive the premiums paid for business written at around the valuation date (based on business written by Rothesay and our competitors). We will use different discount rates for immediate and deferred annuitants to derive an overall premium for each trade. For reinsurance contracts, the CSM will reflect the net cost or gain on purchasing reinsurance at a fair value on the date of transition based on the net outflow to the reinsurer and the associated reduction in RA.

Modification and de-recognition

Pension scheme de-risking is generally a two-step process starting with a pension buy-in contract between Rothesay and the pension scheme and followed by conversion from buy-in to buy-out at which point individual contracts are issued to pension scheme members. We do not consider conversion from buy-in to buy-out as a modification and de-recognition event given the terms and conditions of a buy-out are set out in the original buy-in contract and the benefits provided are unchanged. As a result, such conversions have no impact on the results.

When Rothesay acquires books of annuities from other insurers this is usually achieved by entering into a reinsurance contract between Rothesay and the insurer selling the block, followed by a Part VII transfer where the individual annuity contracts transfer from the insurer to Rothesay along with any associated reinsurance. At the Part VII date, we will de-recognise the carrying amount of the CSM and set up a new CSM based on the fair value of the scheme or group at that date.

Estimated impact of the adoption of IFRS 17

We estimate that after allowing for a deferred tax asset of 25% of the transitional impact on 1 January 2022, the combined impact of the retrospective changes required under IFRS 17 will lead to a reduction in Group equity of between £1bn and £1.5bn as at 1 January 2022 compared to that published under IFRS 4. We have presented a range of outcomes to facilitate disclosure as there remains some uncertainty over the final impact of the introduction of the standard. The upper and lower bounds of the range have been determined on a top down basis by applying amortisation profiles based on cash flows (for the upper end) and linear run-off (for the lower end) to the known inception CSM positions and then adding an additional margin for prudence. Given the breadth of the range and the results from our more detailed modelling, we are confident that the final result will fall in this range.

We expect finalisation of the impact over the next few weeks as we complete our internal governance of the modelling of the CSM and amortisation under the fully retrospective approach. This includes for example the testing of the final controls over the end to end reporting under IFRS17.

As Rothesay has grown very rapidly, with the majority of business being written in the last few years, the slower release of profits under IFRS 17 means that we expect materially lower operating profits for 2022 compared to IFRS 4. In addition, under IFRS 17, only part of the insurance liabilities (the best estimate liabilities and risk adjustment) is exposed to the impact of changes in economic conditions; the CSM is not impacted by such changes. As a result, the IFRS 17 balance sheet responds to changes in economic conditions in a way which is closer to MCEV than the IFRS 4 balance sheet. Given Rothesay's approach to hedging interest rate and inflation risk is to hedge somewhere between MCEV and solvency, we are effectively over-hedged on an IFRS 17 basis and so the IFRS 17 balance sheet is much more sensitive to interest rate movements than the IFRS 4 balance sheet. Under IFRS 17, the impact of the very significant increase in interest rates combined with widening credit spreads is expected to more than offset operating profits under IFRS 17. Consequently, the restated comparative for 2022 is expected to show material pre-tax losses under the new standard.

Adoption of the new standard is not expected to materially impact Rothesay's solvency position or the ultimate profitability of new business. As a result, changes to IFRS accounting are not expected to impact new business pricing or our business strategy. In addition, the rating agencies such as Fitch Ratings have indicated that they expect to treat CSM reserves as equity for the purposes of financial leverage ratios and so the implementation of IFRS 17 is not expected to impact our credit ratings.

Notes to the financial statements continued

Note A - Significant accounting policies (continued)

A.4 Accounting policies and change in accounting policies (continued)

Estimated impact of the adoption of IFRS 17 (continued)

Although the implementation of IFRS 17 is expected to lead to a significant impact on total equity and would have resulted in lower profits for 2022, we expect that our ability to pay dividends will continue to be driven by our solvency balance sheet.

We will publish full results under IFRS 17 as part of our interim results for the six months to 30 June 2023 including comparatives for full year and half year 2022.

IFRS 9, Financial Instruments:

IFRS 9, Financial Instruments, sets out the principles for recognition (and derecognition), classification and measurement of financial assets and financial liabilities, and supersedes IAS 39, Financial Instruments: Recognition and Measurement. 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.

The initial recognition requirement under IFRS 9 is consistent with IAS 39. IFRS 9 divides financial assets into two classifications: amortised cost and fair value. Where assets are measured at fair value, gains and losses can be recognised through profit or loss (fair value through profit or loss, FVTPL) or recognised in other comprehensive income (fair value through other comprehensive income).

Financial assets that meet the following two conditions must be measured at amortised cost, unless the asset is designated at FVTPL under the fair value option:
- **Business model test:** the objective of the entity's business model is to hold the financial asset to collect contractual cash flows (rather than to sell the asset prior to its contractual maturity); and
- **Cash flow characteristic test:** the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Because Rothesay's financial assets are held to meet liabilities, they are designated upon initial recognition at FVTPL in line with the matching exemption in IFRS 9, which allows financial assets to be held at fair value where they back financial liabilities at fair value. Rothesay's financial investments are already fair valued under IAS 39 and we do not expect re-measurement and re-designation between asset classes under IFRS 9. As a result, we expect immaterial to no impact to Rothesay's balance sheet on transition to IFRS 9.

Receivables, cash and cash equivalents, and accrued interest will continue to be carried at amortised cost. This is the same classification and measurement under IFRS 9 and IAS 39. Rothesay will continue to apply IAS 39 Hedge accounting rules as permitted by the standards.

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, 'Operating segments'.

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	
	2022 £m	2021 £m	2022 £m	2021 £m
Pension bulk annuities	**255**	253	**3,324**	2,952
Total gross premiums written	**255**	253	**3,324**	2,952

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 generally 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 (loss)/return includes fair value gains and losses. Interest is accounted for on an accrual basis.

	2022 £m	2021 £m
Interest income on financial investments at fair value through profit and loss	**1,788**	1,445
Unrealised losses on financial investments	**(13,989)**	(1,564)
Realised (losses)/gains on financial investments	**(3,100)**	237
Investment management expenses	**(75)**	(70)
Total investment (loss)/return	**(15,376)**	48

Notes to the financial statements continued

Note B - Income statement notes (continued)

B.2 Investment return (continued)

Given the close duration matching of assets and insurance liabilities, the realised and unrealised losses on financial investments in the period were matched by similar movements in net insurance liabilities. The movements were driven by the increase in long-term interest rates over the period and credit spread widening.

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

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:

	2022 £m	2021 £m
Acquisition costs	**147**	137
Administration expenses - recurring	**63**	59
Administration expenses – project and other one-off expenses	**19**	25
Total operating expense	**229**	221

Acquisition and Group costs increased as a result of the growth in the business.

The following items have been included in operating expenses:

	2022 £m	2021 £m
Property, plant and equipment depreciation	**2**	2
Lease – right of use asset depreciation	**3**	5
	5	7

Project and one-off expenses include reinsurance fees and charitable contributions. Projects include the development of Rothesay's technology platform, the costs associated with the adoption of IFRS 17 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.

	2022 £m	2021 £m
Interest payable on collateral	**61**	1
Interest payable on collateralised agreements and financing	**38**	1
Total interest payable on collateral and collateralised agreements	**99**	2
Interest payable on borrowings from related parties	**18**	19
Interest payable on third party borrowings	**76**	94
Financing charge on leasehold asset	**1**	1
Total borrowing costs	**95**	114
Net finance costs	**194**	116

Note B - Income statement notes (continued)

B.4 Finance costs (continued)

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

For 2021, the interest payable on third party borrowings included interest of £29m paid on the sterling-denominated RT1 notes. From 1 January 2022, this is being treated as an appropriation of profit as and when the interest on the notes is paid, as shown in note C.3 (see note A.4).

B.5 Employee information

All persons involved in the Company's operations are employed by wider group undertakings, Rothesay Pensions Management Limited (RPML) and Rothesay Asset Management NA. The charges made by RPML and Rothesay Asset Management NA for the services provided (personnel and other) to the Company are included in the management fees charged by group undertakings. Details of the employees of the Rothesay Limited Group are as follows:

	2022 No.	2021 No.
Average number of staff employed during the year	**378**	332
Employees by department at year end		
Management	**27**	25
New business origination	**27**	25
Investments	**57**	50
Technology	**90**	72
Finance, legal and HR	**74**	67
Operations and project management	**79**	77
Risk and Internal Audit	**42**	43
	396	359

Staff costs for the Rothesay Limited Group during the financial year (including Directors' salaries and other pension costs) are as follows:

	2022 £m	2021 £m
Wages and salaries	**112**	117
Social security costs	**17**	17
Other pension costs	**4**	3
Total employee benefits expense	**133**	137

The increase in wages and salaries as a result of the increase in headcount was more than offset by the reduction in expenses in relation to share-based payments between 2021 and 2022. 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.

Notes to the financial statements continued

Note B - Income statement notes (continued)

B.5 Employee information (continued)

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

	2022 £m	2021 £m
Directors' remuneration		
Aggregate emoluments	**4**	4
Company pension contributions to money purchase schemes	**–**	–
Total Directors' remuneration	**4**	4
Highest paid Director		
Total amount of emoluments	**2**	1
Company pension contributions to money purchase schemes	**–**	–
Total highest paid Director	**2**	1

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 2022, Directors received no emoluments for non-qualifying services which are required to be disclosed. Three Directors have been granted shares in Rothesay Limited (2021: three) 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 £4m (2021: £3m). There were no outstanding contributions as at 31 December 2022 (2021: £Nil).

B.7 Auditors' remuneration

Fees paid and payable to Rothesay's auditors are as follows:

	2022 £000s	2021 £000s
Remuneration receivable by the Company's auditors for the audit of the consolidated and Company financial statements	**2,457**	1,397
Remuneration receivable by the Company's auditors for the audit of the financial statements of the Company's subsidiaries	**119**	99
Total audit	**2,576**	1,496
Required by regulation	**251**	228
Audit-related assurance services	**239**	217
Other assurance services	**51**	119
Non-audit services	**—**	—
Total fees	**3,117**	2,060

Note B - Income statement notes (continued)

B.7 Auditors' remuneration (continued)

Fees for the audit of the financial statements includes some non-recurring work in relation to the transition to IFRS 17. Other assurance services provided in 2022 relate to work associated with the establishment of the Euro Medium Term Note Programme. Other assurance services provided in 2021 relate to work associated with the issuance of the RT1 notes. These services are 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 2022 and 31 December 2021 are:

	2022 £m	2021 £m
Current income tax:		
UK corporation tax	**37**	171
Prior year adjustment	**1**	–
Total current income tax	**38**	171
Deferred tax:		
Origination and reversal of temporary differences	**(8)**	5
Total deferred tax	**(8)**	5
Total tax expense in the consolidated statement of comprehensive income	**30**	176

The tax expense in the consolidated statement of comprehensive income for the financial year and the standard rate of corporation tax in the UK of 19% (2021: 19%) is reconciled below:

	2022 £m	2021 £m
Profit on ordinary activities before taxation	**176**	918
Tax calculated at UK standard rate of corporation tax of 19% (2021: 19%)	**33**	174
Prior year adjustments	**1**	–
Other adjustments	**(339)**	38
Disallowable expenditure	**337**	(38)
Group relief (surrendered)/claimed for nil consideration	**(2)**	2
Total tax expense reported in the consolidated statement of comprehensive income	**30**	176

In the Spring Budget 2021, the Government announced that from 1 April 2023 the corporation tax rate would increase from 19% to 25%. This was enacted into law on 10 June 2021. On 23 September 2022, The UK Chancellor of the Exchequer announced that the intended increase in the UK corporation tax rate referred to above would be cancelled. On 14 October Liz Truss, the then Prime Minister reversed that decision made as part of the 'Mini Budget' and confirmed that the corporation tax rate will increase to 25% from the current 19% rate as of 1 April 2023. As a consequence, at balance sheet date deferred tax is still reflected at 25% in these financial statements.

Notes to the financial statements continued

Note C - Equity

C.1 Share capital

In preparation for the issuance of the new RT1 notes (see note C.2), on 29 September 2021, each ordinary share of £1 was redesignated as an A ordinary share of £1 each.

At 31 December 2022 and 31 December 2021 share capital comprised:

	2022 No.	2022 £m	2021 No.	2021 £m
Authorised share capital (ordinary shares of £1 each)	**510,528,697**	**510**	510,528,697	510

All of the shares in issuance are A ordinary shares.

No changes have been made to equity share capital in 2022.

C.2 Restricted Tier 1 notes - sterling

Under IFRS, the sterling-denominated Restricted Tier 1 (RT1) notes meet the definition of equity and are therefore recognised as such. The USD-denominated RT1 notes do not meet this definition and are recognised as borrowings (see note D.8).

The table below provides a summary of Rothesay's sterling-denominated RT1 notes:

				Carrying amount	
Notional amount	Issue date	Callable at par at the option of the Group from	Coupon	2022 £m	2021 £m
Loan notes issued through public debt markets					
£350m	12 September 2018	12 September 2028	6.875%	**347**	347
£450m	13 October 2021	13 October 2031	5%	**446**	446
				793	**793**

On 13 October 2021, Rothesay issued £450m of Restricted Tier 1 notes with a fixed 5% 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 13 October 2031. If the notes are not repaid by 13 April 2032, the 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 on all RT1 notes 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.

then either:
(i) in the case of the £350m of RT1 notes (issued on 5 September 2018), the full principal amount of each note issued is irrevocably and automatically reduced to zero on a permanent basis; or
(ii) in the case of the £450m of RT1 notes (issued on 13 October 2021) the notes convert into a new class B of non-voting ordinary shares of RLP.

Note C - Equity (continued)

C.3 Share premium account and reserve

	Share premium £m	Hedging reserve £m	Profit and loss reserve £m
1 January 2022	**1,953**	**1**	**2,882**
Other comprehensive income for the year	**–**	**3**	**–**
Capital reorganisation	**(1,953)**	**–**	**1,953**
Tier 1 note coupon	**–**	**–**	**(34)**
Tier 1 coupon tax relief	**–**	**–**	**7**
Profit for the financial year	**–**	**–**	**146**
31 December 2022	**–**	**4**	**4,954**

Note that for 2021, the interest payable on the sterling-denominated RT1 notes was included in finance costs (see note B.4) rather than as an appropriation of profit (see note A.4).

In 2022 and in anticipation of the impact of the introduction of IFRS 17 on Rothesay's balance sheet, the Company enacted a court approved capital reorganisation leading to a reduction in share premium of £1,953m and a corresponding increase in the profit and loss reserve. This increase in the profit and loss reserve will be partially offset by the equity impact of the transition to IFRS 17 on the date of implementation of the standard.

	Share premium £m	Hedging reserve £m	Retained earnings £m
1 January 2021	1,953	–	2,143
Prior year adjustment	–	–	(3)
Other comprehensive income for the year	–	1	–
Profit for the financial year	–	–	742
31 December 2021	1,953	1	2,882

Hedging reserve

A foreign currency exposure arises on the RT1 notes issued in USD and the associated coupon payments (see note D.8). The risk arises from the fluctuation in exchange rates, which would cause volatility in the biannual coupon payments and the principal repayment at the call date.

A cash flow hedge has therefore been put in place to remove the volatility caused by exchange rate movements, using a bespoke fixed-for-fixed cross currency swap. The swap is designated as a hedge of a probable forecasted transaction, being the foreign currency sterling costs of the coupons and principal. As the hedging instrument is a bespoke derivative any ineffectiveness is expected to be immaterial.

We have not provided additional disclosures in relation to the cash flow hedges as the fair value of the hedges was only £48m as at 31 December 2022 (2021: £7m) which is not material in the context of Rothesay's total derivative position.

C.4 Dividends on ordinary shares

The Directors have recommended no payment of interim dividends during the year ended 31 December 2022 (2021: £Nil). The Directors have recommended no final ordinary dividend in respect of the year ended 31 December 2022 (2021: £Nil).

Notes to the financial statements continued

Note D - Financial assets and liabilities

D.1 Property, plant and equipment

Equipment is stated at cost less accumulated depreciation/amortisation and accumulated impairment losses. Depreciation is calculated on a straight-line basis over the useful life of the following classes of assets:

- *Computer equipment: 3 years*
- *Furniture and fittings: 5 years*
- *Software: 10 years*

Development expenditure on internally developed software is recognised as an asset only if Rothesay can demonstrate the technical feasibility to complete the development of the software, its intention and the availability of resources to complete the development and to use the software, and its ability to use the software to generate probable future economic benefits and to measure the expenditure reliably. Subsequent expenditure on internally developed software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as it is incurred. Amortisation of the intangible asset begins when development is complete, and the asset is available for use. It is amortised over the period of expected future benefit. During the period of development, the intangible asset is tested for impairment annually.

Group and Company	Software £m	Computer equipment £m	Furniture and fittings £m	Total £m
Cost				
As at 1 January 2022	**4**	**–**	**10**	**14**
Additions	**9**	**–**	**–**	**9**
As at 31 December 2022	**13**	**–**	**10**	**23**
Accumulated depreciation				
As at 1 January 2022	**–**	**–**	**(3)**	**(3)**
Charge for the year	**–**	**–**	**(2)**	**(2)**
As at 31 December 2022	**–**	**–**	**(5)**	**(5)**
Net book value				
As at 31 December 2022	**13**	**–**	**5**	**18**
As at 31 December 2021	**4**	**–**	**7**	**11**

At 31 December 2022 and 31 December 2021, Rothesay conducted an impairment review of the software asset not yet available for use and found no impairment necessary. The software asset capitalised relates to assets which remain under development.

D.2 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, mortgages and collateralised agreements and financing.

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

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 if (i) 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 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.

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.

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)
D.2 Financial investments (continued)

Hedge accounting
In 2021, Rothesay designated a certain derivative as a hedging instrument in order to effect cash flow hedges. At the inception of the hedge Rothesay documented the relationship between the hedging instrument and the hedged item. In addition, Rothesay has and will continue to document whether the hedging instrument is highly effective in offsetting changes in fair value or cash flows of the hedge item. Note C.3 provides further details.

Where a cash flow hedging relationship exists, the effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated under the heading of hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss, and is included in net investment income.

Amounts previously recognised in other comprehensive income and accumulated in equity will be reclassified to profit and loss in the accounting period when the hedged item affects profits or loss, in the same line as the hedged item. Hedge accounting will be discontinued when Rothesay cancels the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting. Any gain or loss recognised in other comprehensive income and accumulated in equity at that time is recycled to profit or loss over the period the hedged item impacts profits or loss.

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.

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

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

Group	2022 £m	2021 £m
Financial investments carried at fair value through profit and loss, designated at initial recognition	**90,928**	83,845

Company	2022 £m	2021 £m
Financial investments carried at fair value through profit and loss, designated at initial recognition	**90,720**	83,845

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.

When assessing the fair value of our Level 3 financial investments, we consider and allow for the extent to which the investments may be vulnerable to climate change, either because of vulnerability to physical climate risk or the risk of being stranded assets in the drive to net zero carbon emissions. The valuation of Level 1 and Level 2 financial investments is also assumed to allow for climate change exposure.

The following tables show an analysis of financial investments recorded at fair value by level of the fair value hierarchy for 2022 and 2021 (please refer to note D.7 for financial liabilities):

Group 31 December 2022	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Collective investment schemes	**4,585**	**–**	**–**	**4,585**
Government sub sovereign and agency obligations	**5,139**	**6,919**	**–**	**12,058**
Corporate bonds and other corporate debt	**–**	**24,116**	**756**	**24,872**
Derivative assets (see note D.3)	**–**	**35,993**	**1,817**	**37,810**
Collateralised agreements and financing	**–**	**430**	**–**	**430**
Loans secured on property	**–**	**111**	**5,846**	**5,957**
Lifetime mortgages	**–**	**–**	**5,086**	**5,086**
Certificate of deposits	**–**	**130**	**–**	**130**
Total financial investments at fair value	**9,724**	**67,699**	**13,505**	**90,928**

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)
D.2 Financial investments (continued)

Company 31 December 2022	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Collective investment schemes	**4,377**	**–**	**–**	**4,377**
Government sub sovereign and agency obligations	**5,139**	**6,919**	**–**	**12,058**
Corporate bonds and other corporate debt	**–**	**24,116**	**756**	**24,872**
Derivative assets (see note D.3)	**–**	**35,993**	**1,817**	**37,810**
Collateralised agreements and financing	**–**	**430**	**–**	**430**
Loans secured on property	**–**	**111**	**5,846**	**5,957**
Lifetime mortgages	**–**	**–**	**5,086**	**5,086**
Certificate of deposits	**–**	**130**	**–**	**130**
Total financial investments at fair value	**9,516**	**67,699**	**13,505**	**90,720**

Group and Company 31 December 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Collective investment schemes	5,405	–	–	5,405
Government sub sovereign and agency obligations	8,356	9,773	–	18,129
Corporate bonds and other corporate debt	–	25,265	1,092	26,357
Derivative assets (see note D.3)	–	17,048	3,721	20,769
Collateralised agreements and financing	–	262	–	262
Loans secured on property	–	107	7,304	7,411
Lifetime mortgages	–	–	5,329	5,329
Certificate of deposits	–	183	–	183
Total financial investments at fair value	13,761	52,638	17,446	83,845

Rothesay discloses offsetting derivative asset and derivative liability contracts separately in line with IAS 32 requirements and the value of both has increased significantly in the period due to changes in economic conditions. However, the movement in the value of derivative assets is offset by the movement in the value of derivative liabilities such that on a net basis the value of derivatives fell by £70m in 2022 (2021: fell by £260m).

Collective investment schemes represent money market funds with same-day liquidity. Rothesay utilise these funds as an additional form of financial investment to back insurance contract liabilities.

Approximately 15% (2021: 21%) of the total financial assets recorded at fair value are valued based on estimates and recorded as Level 3 investments.

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

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 lifetime mortgages which are discussed in the lifetime mortgages section of note D.2 below):

Group and Company	Corporate debt £m	Loans secured on property £m	Derivative assets £m	Total £m
At 1 January 2022	**1,092**	**7,304**	**3,721**	**12,117**
Total gains in the statement of comprehensive income:				
Unrealised losses	**(139)**	**(2,291)**	**(1,909)**	**(4,339)**
Realised gains	**7**	**6**	**–**	**13**
Transfer into Level 3	**36**	**–**	**–**	**36**
Transfer out of Level 3	**–**	**–**	**–**	**–**
Net purchases/addition/(sales)	**(240)**	**827**	**5**	**592**
At 31 December 2022	**756**	**5,846**	**1,817**	**8,419**
At 1 January 2021	1,186	6,523	3,555	11,264
Total gains in the statement of comprehensive income:				
Unrealised (losses)/gains	(42)	567	166	691
Realised gains	–	21	–	21
Transfer out of Level 3	(55)	–	–	(55)
Net purchases/additions	3	193	–	196
At 31 December 2021	1,092	7,304	3,721	12,117

Please see note D.7 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. £36m of corporate debt was transferred from Level 2 to Level 3 during the year (2021: £Nil). No corporate debts were transferred from Level 3 to Level 2 in 2022 (2021: £55m).

The unrealised losses on Level 3 financial investments were mainly driven by the increase in long-term interest rates. The loss observed in Level 3 derivative assets largely offsets with the gain from Level 3 derivative liabilities.

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

Lifetime mortgages

Lifetime 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 lifetime 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.

Lifetime 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 lifetime 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.

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 lifetime mortgages, the instruments are recorded as Level 3 assets. The table below provides an analysis of the movement in the value of lifetime mortgages. New business includes both the acquisition of back books of lifetime mortgages and new origination through Rothesay's strategic partners. The impact of the change in economic assumptions for 2022 is dominated by the significant increase in interest rates but also includes changes in property prices.

Group and Company	2022 £m	2021 £m
Carrying amount at 1 January	**5,329**	4,222
Increase in respect of new business	**1,675**	1,377
Redemptions/repayments	**(310)**	(280)
Accrued interest for the financial year	**249**	179
Change in economic assumptions	**(1,859)**	(168)
Change in demographic assumptions	**2**	(1)
Closing balance at end of the year	**5,086**	5,329

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

Group and Company	2022 £m	2021 £m
Less than one year	**414**	301
One to five years	**1,210**	1,117
Over five years	**3,462**	3,911
Total	**5,086**	5,329

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

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:

	2022		2021	
	Asset £m	Related liability £m	Asset £m	Related liability £m
Government and agency obligations	**3,881**	**3,628**	440	414
Total collateralised agreements	**3,881**	**3,628**	440	414

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 2022, the total cash collateral received was £5,234m (2021: £1,537m). 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.2 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 following table also shows the potential impact on profit before tax (PBT) and equity of the same alternative assumptions, assuming that all other pricing inputs remain constant.

Group and Company Impact on financial assets and PBT	Main assumptions	Changes in assumptions	2022 Current FV £m	(Decrease)/ increase in FV £m	(Decrease)/ increase in PBT £m	(Decrease)/ increase in equity £m
Financial assets						
Corporate bonds and other corporate debt	Liquidity premium	+25bps	**756**	**(10)**	**(1)**	**(1)**
		-25bps	**756**	**10**	**1**	**1**
Loans secured on property	Liquidity premium	+25bps	**5,846**	**(176)**	**–**	**–**
		-25bps	**5,846**	**188**	**–**	**–**
Loans secured on property	Property prices	+10%	**5,846**	**14**	**25**	**20**
		-10%	**5,846**	**(18)**	**(38)**	**(31)**
Lifetime mortgages	Liquidity premium	+25bps	**5,086**	**(126)**	**–**	**–**
		-25bps	**5,086**	**131**	**–**	**–**
Lifetime mortgages	House prices	+10%	**5,086**	**48**	**46**	**37**
		-10%	**5,086**	**(65)**	**(62)**	**(51)**
Derivative assets	LPI bid-mid spread	+15bps	**1,817**	**7**	**7**	**5**
		-15bps	**1,817**	**(7)**	**(7)**	**(5)**
Financial liabilities						
Derivative liabilities	LPI bid-mid spread	+15bps	**1,882**	**88**	**88**	**72**
		-15bps	**1,882**	**(88)**	**(88)**	**(72)**
Collateralised financing agreements	Liquidity premium	+25bps	**113**	**6**	**6**	**5**
		-25bps	**113**	**(6)**	**(6)**	**(5)**

Note D - Financial assets and liabilities (continued)

D.2 Financial investments (continued)

Sensitivity of level 3 financial investments measured at fair value to changes in key assumptions (continued)

Group and Company Impact on financial assets and PBT	Main assumptions	Changes in assumptions	2021 Current FV £m	(Decrease)/ Increase in FV £m	(Decrease)/ Increase in PBT £m	(Decrease)/ Increase in Equity £m
Financial assets						
Corporate bonds and other corporate debt	Liquidity premium	+25bps	1,092	(16)	(3)	(2)
		-25bps	1,092	17	3	2
Loans secured on property	Liquidity premium	+25bps	7,304	(310)	–	–
		-25bps	7,304	335	–	–
Loans secured on property	Property prices	+10%	7,304	19	28	23
		-10%	7,304	(37)	(63)	(51)
Lifetime mortgages	Liquidity premium	+25bps	5,329	(161)	–	–
		-25bps	5,329	169	–	–
Lifetime mortgages	House prices	+10%	5,329	84	84	68
		-10%	5,329	(107)	(108)	(88)
Derivative assets	LPI bid-mid spread	+15bps	3,721	6	6	5
		-15bps	3,721	(6)	(6)	(5)
Financial liabilities						
Derivative liabilities	LPI bid-mid spread	+15bps	4,035	158	158	128
		-15bps	4,035	(158)	(158)	(128)
Collateralised financing agreements	Liquidity premium	+25bps	213	13	13	11
		-25bps	213	(13)	(13)	(11)

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)

D.3 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 large movement in the fair value of assets and liabilities has been driven by the change in economic conditions over the year. The total net fair value of Rothesay's derivative assets and liabilities has moved by a smaller amount, from an asset of £81m as at 31 December 2021 to an asset of £11m as at 31 December 2022.

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

	2022			2021		
Group and Company	Assets £m	Liabilities £m	Notional amount £m	Assets £m	Liabilities £m	Notional amount £m
Derivatives held for risk management						
Interest rate swap	**26,488**	**(27,046)**	**336,554**	14,741	(15,006)	344,678
Inflation swap	**4,276**	**(3,991)**	**78,332**	3,729	(3,354)	69,076
Currency swap	**5,133**	**(4,746)**	**120,174**	1,660	(1,689)	96,920
Credit derivative	**1,899**	**(1,831)**	**18,010**	575	(602)	20,490
Forwards	**14**	**(185)**	**3,819**	64	(37)	3,773
Total	**37,810**	**(37,799)**	**556,889**	20,769	(20,688)	534,937

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. 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.4 Accrued interest and prepayments

Group and Company	2022 £m	2021 £m
Accrued interest	**558**	417
Prepaid expenses	**248**	224
Total accrued interest and prepayments	**806**	641

Note D - Financial assets and liabilities (continued)

D.5 Receivables

Receivables are recognised initially at fair value of the amount recoverable. Receivables are subsequently stated at amortised cost.

Group	2022 £m	2021 £m
Deposits pledged as collateral to third parties	**2,060**	444
Amounts due from group undertakings	**82**	49
Tax receivable	**41**	–
Other receivables	**250**	18
Total receivables	**2,433**	511

Company	2022 £m	2021 £m
Deposits pledged as collateral to third parties	**2,060**	444
Amounts due from group undertakings	**82**	163
Tax receivable	**41**	–
Other receivables	**493**	178
Total receivables	**2,676**	785

Other receivables includes deferred premiums and trade date adjustments.

Receivables of £2,324m (2021: £503m) are due within one year for the Group and £2,567m (2021: £777m) for the Company. The fair value of receivables is £2,433m (2021: £511m) for the Group and £2,676m (2021: £785m) for the Company. At 31 December 2022 and 31 December 2021 Rothesay conducted an impairment review of the receivables and found no impairment necessary.

The net exposure to certain OTC derivatives is collateralised through cash posted, as per the terms of the OTC contracts. At 31 December 2022, the total cash collateral posted was £2,060m (2021: £444m). Further details of the full extent of collateral usage can be found in the credit risk disclosure in note F.2.1

D.6 Cash and cash equivalents

Cash and cash equivalents comprise cash balances and short-term deposits with an original maturity term of three months or less at the date of placement held for the purpose of meeting short-term cash commitments.

The cash at bank and in hand of Rothesay at the year end is as follows:

Group	2022 £m	2021 £m
Cash at bank and in hand	**243**	332
Total cash and cash equivalents	**243**	332

Company	2022 £m	2021 £m
Cash at bank and in hand	**195**	159
Total cash and cash equivalents	**195**	159

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)
D.7 Payables and financial liabilities

Financial investment liabilities are recognised at fair value. Payables are recognised initially at fair value of the amount payable. Payables are subsequently stated at amortised cost.

Group	2022 £m	2021 £m
Derivative financial instruments	**37,799**	20,688
Collateralised financing agreements	**3,628**	414
Government, sub sovereign and agency obligations	**310**	–
Total financial investment liabilities	**41,737**	21,102
Deposits received as collateral from third parties	**5,234**	1,537
Amounts due to Group undertakings	**108**	101
Current tax payable	**–**	7
Other payables	**47**	37
Total payables	**5,389**	1,682
Total payables and financial investment liabilities	**47,126**	22,784

Company	2022 £m	2021 £m
Derivative financial instruments	**37,799**	20,688
Collateralised financing agreements	**3,628**	414
Government, sub sovereign and agency obligations	**310**	–
Total financial investment liabilities	**41,737**	21,102
Deposits received as collateral from third parties	**5,234**	1,537
Amounts due to Group undertakings	**445**	101
Current tax payable	**–**	7
Other payables	**47**	37
Total payables	**5,726**	1,682
Total payables and financial investment liabilities	**47,463**	22,784

Other payables include reinsurance fees and trade date adjustments.

Financial liabilities are recorded at fair value, of which £1,995m are valued using Level 3 techniques (2021: £4,248m). The Level 3 financial liabilities are predominantly LPI linked derivatives. The remainder of the financial liabilities are valued using Level 1 and Level 2 techniques.

No financial liabilities were transferred from Level 2 to Level 3 in 2022 (2021: £Nil), £2m financial liabilities were transferred from Level 3 to Level 2 (2021: £Nil). Level 3 financial liabilities have decreased in market value by £2,253m in the year as a result of changes in economic conditions (2021: £489m decrease).

Note D - Financial assets and liabilities (continued)

D.7 Payables and financial liabilities (continued)

The impact on the fair value of Level 3 financial liabilities of using reasonably possible alternative assumptions is included in note D.2.

Payables and financial liabilities of the Group £16,648m and Company £16,985m (2021: £7,710m Group and Company) are all due within one year. Please note, that for financial liabilities the balance is calculated using undiscounted expected contractual cash flows consistent with note F.2.3.

The net exposures to certain OTC derivatives are collateralised through cash. As at 31 December 2022, the total cash collateral received was £5,234m (2021: £1,537m). Other OTC contracts are collateralised with fixed income securities which are not recognised on the consolidated statement of financial position for Rothesay.

D.8 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:

Group and Company	2022 £m	2021 £m
Subordinated loans from related parties	**299**	299
Subordinated loan notes	**1,135**	1,131
US$400m contingent convertible RT1 notes	**330**	295
Total borrowed	**1,764**	1,725

On 27 October 2021, Rothesay Life Plc (RLP) issued $400m of contingent convertible RT1 notes. The notes have no fixed maturity date and interest is payable at the sole discretion of RLP. A fixed 4.875% coupon is payable biannually in arrears. If an interest payment is not made it is cancelled and it does not accumulate or become payable at any time thereafter.

The notes are callable on or after 13 April 2027. If the notes are not repaid by 13 October 2027, the fixed rate of interest per annum will be reset. The notes are direct, unsecured and subordinated obligations of the issuer.

The notes contain a contingent settlement provision which is linked to the occurrence of a 'Capital Disqualification Event'. Such an event is deemed to have taken place where, as a result of a change to the Solvency II regulations, the notes no longer qualify as Own Funds. On the occurrence of such an event and where RLP has chosen not to use its corresponding right to redeem the notes, RLP is no longer able to exercise its discretion to cancel any interest payments due. Accordingly, the notes are considered to meet the definition of a financial liability for financial reporting purposes.

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.

The notes then convert into a new class B of non-voting ordinary shares of RLP.

Notes to the financial statements continued

Note D - Financial assets and liabilities (continued)

D.8 Borrowings (continued)

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

Notional amount	Issue date	Redemption date	Callable at par at the option of the Group from	Coupon	Carrying amount 2022 £m	Carrying amount 2021 £m	Fair value 2022 £m	Fair value 2021 £m
Subordinated loans from related parties								
£300m	19 September 2017	19 September 2028	19 September 2023 and annually thereafter	6.05%	**299**	299	**294**	308
Subordinated loans								
£250m	30 October 2015	30 October 2025	No call option	8%	**250**	249	**258**	301
£500m	12 July 2019	12 July 2026	No call option	3.375%	**490**	487	**450**	522
£400m	17 September 2019	17 September 2029	17 September 2024	5.5%	**395**	395	**390**	432
$400m	27 October 2021	Perpetual	13 April 2027	4.875%	**330**	295	**255**	294

For the year ended 31 December 2022, an interest expense of £97m (2021: £85m) was recognised in the consolidated statement of comprehensive income in respect of these borrowings. For 2021, the interest payable on third party borrowings included interest of £29m paid on the sterling-denominated RT1 notes. From 1 January 2022, this is being treated as an appropriation of profit as shown in note C.3.

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:

Group and Company	1 January 2022 £m	Cash flows £m	Non-cash flows £m	31 December 2022 £m
Subordinated loans from related parties	**299**	**–**	**–**	**299**
Subordinated loan notes	**1,131**	**–**	**4**	**1,135**
US$400m contingent convertible RT1 notes	**295**	**–**	**35**	**330**
Total borrowings	**1,725**	**–**	**39**	**1,764**

Group and Company	1 January 2021 £m	Cash flows £m	Non-cash flows £m	31 December 2021 £m
Subordinated loans from related parties	298	–	1	299
Subordinated loan notes	1,128	–	3	1,131
US$400m contingent convertible RT1 notes	–	290	5	295
Total borrowings	1,426	290	9	1,725

D.9 Accruals

Group and Company	2022 £m	2021 £m
Accrued interest	**59**	33
Accrued expenses	**36**	36
Total accruals	**95**	69

Note E - Insurance contracts and reinsurance

E.1 Insurance contract liabilities, net of reinsurance

The table below shows insurance contract liabilities, net of reinsurance. Insurance contract liabilities include reinsurance inwards, i.e. where the Group 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.

Group and Company	2022 £m	2021 £m
Insurance contract liabilities	**38,112**	54,030
Reinsurance assets	**(185)**	(641)
Reinsurance liabilities	**1,245**	1,217
Insurance contract liabilities, net of reinsurance	**39,172**	54,606

Rothesay's reinsurance is presented as an asset on an IFRS basis where the present value of projected claims exceeds the present value of the regular premiums due on the longevity reinsurance contracts. The number of contracts classified as an asset decreased in 2022, i.e. some contracts switched from being a reinsurance asset to a reinsurance liability, due to the change in economic conditions and demographic assumption changes.

Net insurance contract liabilities fell by £15.4bn in 2022 largely as a result of the increase in the valuation interest rate used to discount the liabilities.

E.2 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.

It is still unclear as to whether COVID-19 will materially impact long-term future mortality. In valuing our insurance and reinsurance assets and liabilities we have not made any changes to our long-term 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.

Notes to the financial statements continued

Note E - Insurance contracts and reinsurance (continued)

E.2 Reinsurance assets/liabilities (continued)

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. Additional longevity reinsurance has been transacted over the year in respect of £2.1bn of new business written during the year and liabilities previously not reinsured.

At 31 December 2022 and 31 December 2021 Rothesay conducted an impairment review of the reinsurance assets and found no impairment necessary.

E.3 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

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:

	2022		2021	
	Pensions originated	Insurance originated	Pensions originated	Insurance originated
Males	**105.7% S3PMA**	**102.1% S3PMA**	104.9% S3PMA	99.5% S3PMA
Females	**105.7% S3PFA**	**102.1% S3PFA**	104.9% S3PFA	99.5% S3PFA

Note E - Insurance contracts and reinsurance (continued)
E.3 Insurance contract liabilities (continued)
Key valuation assumptions (continued)
(a) Mortality assumptions (continued)

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.

Recent mortality experience is analysed annually for each pension scheme and for insurance originated business. The last review was carried out during 2022. The best estimate base mortality assumptions used in the valuation are based on this actual mortality experience. For 2022, mortality experience from 2020 and 2021 has been compared to expected levels with allowance for population level experience, hence heavy experience due to the COVID-19 pandemic has not been projected indefinitely. Mortality assumptions are generally set with reference to a Rothesay-specific suite of mortality tables. For the purpose of our reporting disclosures, these have been expressed as a single adjustment equivalent to the CMI S3 series of mortality tables drawn up by the Continuous Mortality Investigation (CMI) of the Institute and Faculty of Actuaries. The S3 tables are based on industry-wide experience. For the S3 tables, past mortality improvements are applied assuming the base mortality rates are as at 2013.

The changes to the single equivalent rates over 2022 reflect the inclusion of new business, differences from expected mortality in recent years and the impact of updating the mortality improvements used to roll the base tables forward to the current date.

Mortality improvements used to roll base tables forward to the current date use an advanced calibration of the CMI 2021 model with limited period smoothing and including 2020 and 2021 experience in order to represent realised population mortality improvements. This is allowed for in the base table and mortality improvement equivalents shown in the preceding/proceeding tables.

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. During 2022 mortality improvement assumptions were updated to reflect recent mortality improvements, including adoption of the CMI 2021 improvement model. The CMI 2021 model places no weight on 2020 or 2021 data, removing the impact of COVID-19 from our improvement projections. For both 2021 and 2022, 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 improvement rates remain unchanged from 2021. The assumed initial rates of improvements as at 31 December 2022 remain consistent with those used at 31 December 2021. The initial adjustment parameter has not been adopted, with adjustment to the initial rate of mortality improvements continuing to be made through the Sk parameter.

Best estimate improvements are equivalent to those shown in the table below:

	Future mortality improvements (excluding margins)	
Group and Company	**2022**	**2021**
Males	**CMI_2021*_M[1.7%; Sκ=7.5]**	CMI_2020*_M[1.7%; Sκ=7.5]
Females	**CMI_2021*_F[1.7%; Sκ=7.5]**	CMI_2020*_F[1.7%; Sκ=7.5]

* 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 1.5 years (2021: 1.6 years). No changes have been made to prudent margins during 2022.

Notes to the financial statements continued

Note E - Insurance contracts and reinsurance (continued)

E.3 Insurance contract liabilities (continued)

Key valuation assumptions (continued)

(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 2022. For the purposes of this calculation, any assets held by LT Mortgage Financing Limited, Rothesay MA No.1 Limited and Rothesay MA No.3 Limited are treated as if they were held directly and inter-company arrangements ignored. Where assets are assumed to be reinvested, we assume that they achieve a yield of SONIA (2021: a yield of SONIA).

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. (2021: 3bps p.a.).

The result is equivalent to using the valuation rate of interest set out in the table below:

Group and Company	2022	2021
Equivalent rate of interest	**4.91% p.a.**	1.77% 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 2022 and 31 December 2021.

Group and Company	Average yield deduction	
Asset class	2022	2021
UK Government approved securities	**0 bps**	0 bps
Secured lending	**25 bps**	29 bps
Supranational/other sovereign	**23 bps**	21 bps
Secured residential lending	**37 bps**	28 bps
Corporate bonds (without covering credit default swaps)	**71 bps**	61 bps
Infrastructure	**79 bps**	65 bps
Lifetime mortgages	**38 bps**	74 bps
Other	**57 bps**	41 bps
Overall yield deduction	**43 bps**	33 bps

Since the end of 2021, the average yield deduction has increased in aggregate. The aggregate increase in default allowances is mainly due to changes in market conditions during the year, most notably the widening of credit spreads. The yield deduction for lifetime mortgages has reduced as explained in the following paragraph.

Note E - Insurance contracts and reinsurance (continued)

E.3 Insurance contract liabilities (continued)

Key valuation assumptions (continued)

(b) Economic assumptions including valuation rate of interest (continued)

Allowance is made for the risks associated with lifetime 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.2 and for the valuation rate of interest is calculated on a prudent basis allowing for future property price growth at a rate equivalent to 2.74% net of dilapidation costs and cost of sale (2021: 1.36%) and house price volatility equivalent to 13% (2021: 13%). The house prices used in the valuation of the NNEG are based on the latest available market prices with no allowance made for potential near term falls in house prices. The increase in the future property price growth reflects the increase in interest rates and this reduces the likelihood future mortgage balances will exceed property values, lowering the deduction in yield required for the NNEG.

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, there is not a sufficiently deep, liquid market to support setting the rate of limited price indexation (LPI). We have therefore projected these rates using LPI models based on realised LPI and other market inputs.

(c) Expense assumption

The allowance made for future maintenance expenses was updated at the end of 2022 following an investigation into the total costs incurred by Rothesay during 2022 and projected 2023 expenses. As part of this investigation, costs have been split between acquisition and maintenance expenses.

The insurance contract liabilities include both the projected expenses payable under the third party administration agreements and the long-term business overhead expenses expressed as an amount per policy. The average per policy allowance is £44 per policy per annum (2021: £38 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 (2021: 0.25% p.a.).

(d) Member option and dependants assumptions and provisions for data risk

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, the proportion of deferred annuitants opting to take a proportion or all of their benefit as a lump sum and the provision required to cover data risk.

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 note E.3(b) on the previous page).

When deferred annuitants have passed the scheme's 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's normal retirement date are assumed to start receiving pension payments immediately.

As part of pension de-risking Rothesay sometimes provides insurance against residual data risk. Examples of such risks include the risk that there are beneficiaries of a pension scheme missing from the data, the risk that a policyholder's data is inaccurate or the risk that scheme rules have been inaccurately interpreted. Appropriately prudent provisions are established following detailed due diligence.

Notes to the financial statements continued

Note E - Insurance contracts and reinsurance (continued)

E.3 Insurance contract liabilities (continued)

Key valuation assumptions (continued)

(e) Movement in insurance contract liabilities, net of reinsurance

The table below details 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.

Group and Company	2022 £m	2021 £m
Carrying amount at 1 January	**54,606**	55,624
Increase in respect of new business	**2,941**	2,927
Release of liabilities	**(1,531)**	(2,435)
Effect of assumption changes and model refinement	**(16,844)**	(1,510)
Other	**–**	–
Closing balance at financial statement date	**39,172**	54,606

The following table shows the impact on the insurance contract liabilities, net of reinsurance, of changes in the assumptions used:

Net decrease in liabilities	2022 £m	2021 £m
Change in assumptions used		
Valuation rate of interest	**(17,923)**	(3,611)
Inflation	**1,061**	2,243
Effect of economic assumption changes	**(16,862)**	(1,368)
Demographics	**(14)**	(71)
Member options	**–**	–
Expenses	**32**	(32)
Model refinement	**–**	(39)
Effect of non-economic assumption changes and model refinement	**18**	(142)
Total effect of assumption changes	**(16,844)**	(1,510)

As shown previously, the valuation rate of interest increased by 314bps over the year, which led to the £17.9bn decrease in the net liability shown. The effect of rising interest rates was partially offset by the impact of the rise in near-term future inflation rates.

Note E - Insurance contracts and reinsurance (continued)

E.3 Insurance contract liabilities (continued)

Key valuation assumptions (continued)

(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 impacts of many of the sensitivities have reduced in absolute terms due to the increase in discount rate over the year reducing the size of the balance sheet. Given the significant volatility in interest rates during 2022 a 200bp sensitivity is also disclosed for 2022, along with 100bps used historically.

2022 Group and Company	Change in assumptions	(Decrease)/ increase in net liabilities £m	Increase/ (decrease) in PBT £m	Impact on equity £m
Annuitant mortality	+5% qx	**(76)**	**88**	**72**
Annuitant mortality	-5% qx	**83**	**(96)**	**(78)**
Interest rate	+100bps	**(3,894)**	**(10)**	**(8)**
Interest rate	-100bps	**4,754**	**10**	**8**
Interest rate	+200bps	**(7,097)**	**(73)**	**(59)**
Interest rate	-200bps	**10,609**	**141**	**114**
Inflation	+100bps	**2,109**	**(74)**	**(60)**
Inflation	-100bps	**(1,963)**	**149**	**121**
Credit spread widening	+50bps	**(930)**	**(358)**	**(290)**
Change in property prices	+10%	**(8)**	**70**	**57**
Change in property prices	-10%	**17**	**(100)**	**(81)**
Expenses	+10%	**103**	**(103)**	**(84)**

2021 Group and Company	Change in assumptions	(Decrease)/ increase in net liabilities £m	Increase/ (decrease) in PBT £m	Impact on equity £m
Annuitant mortality	+5% qx	(186)	180	146
Annuitant mortality	-5% qx	201	(195)	(158)
Interest rate	+100bps	(6,932)	(280)	(227)
Interest rate	-100bps	8,664	489	396
Inflation	+100bps	3,401	159	129
Inflation	-100bps	(3,177)	19	15
Credit spread widening	+50bps	(1,208)	(386)	(313)
Change in property prices	+10%	(9)	112	91
Change in property prices	-10%	27	(171)	(139)
Expenses	+10%	140	(140)	(114)

The sensitivities shown capture non-linearity effects, which may be significant following large market movements.

Notes to the financial statements continued

Note E - Insurance contracts and reinsurance (continued)

E.3 Insurance contract liabilities (continued)

Key valuation assumptions (continued)

(f) Sensitivity analysis (continued)

The risk management strategy adopted can result in Rothesay being immunised to market movements in either direction. Given the increase in interest rates in 2022, the -100bps and -200bps interest rate sensitivities result in interest rates remaining positive at all durations (2021: fell below zero at some durations).

The impact of reinsurance on the sensitivity to mortality risk is a reduction of 89% (2021: 84%). In 2022 the impact of reinsurance has changed due to additional reinsurance transacted through the year, new business and changes in economic conditions.

The annuitant mortality sensitivity is defined in terms of a qx stress, where qx represents the probability of a life dying during the period. 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:

	2022			
	Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Insurance contract cash flows net of reinsurance	**2,761**	**9,522**	**26,889**	**39,172**

	2021			
	Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Insurance contract cash flows net of reinsurance	2,624	10,310	41,672	54,606

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 its regulatory obligations;
- to match the profile of its 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 operates under the Solvency II regime. Rothesay had sufficient capital available to meet its regulatory capital requirements at all times during the year ended 31 December 2022.

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 has been recalculated as at 31 December 2022 and amortises by 1/16th each year from 1 January 2017. As at 31 December 2022, solvency estimates allow for amortisation of 6/16ths of transitional solvency relief (2021: 5/16ths). The 31 December 2022 recalculation is in response to the significant change in economic conditions since the last time transitional relief was recalculated.

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. An application to use a full internal model, extending the PIM to cover other risk components, was submitted to the PRA in October 2022 but for now 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 2022, Own Funds for Rothesay were £8,151m (2021: £8,361m) made up as follows:

Group and Company	2022 £m	2021 £m
Total IFRS equity	**6,261**	6,139
Liability valuation differences and other regulatory adjustments	**607**	786
Total Tier 1	**6,868**	6,925
Tier 2 debt valuation	**849**	948
Tier 3 debt valuation	**434**	488
Own Funds	**8,151**	8,361

Rothesay holds both debt and equity to optimise its capital structure and improve shareholder return. During 2021, £450m of Tier 1 GBP RT1 notes and $400m of USD Tier 1 RT1 notes were issued by Rothesay.

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 reinvestment of assets as appropriate.

Notes to the financial statements continued

Note F - Risk and capital management (continued)

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.

Climate change risk is considered within the relevant risk type, for example credit risk includes the potential impact of climate change on the creditworthiness of counterparties.

Please see pages 36 to 46 of the strategic review report for further detail on risk management arrangements and the governance framework within Rothesay. Please refer to Rothesay's latest ESG report for further detail on our commitments and progress towards net zero.

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. In some instances this risk may arise as a result of climate change, for example the risk of stranded assets, potential litigation exposure or the impact of climate change on a counterparty's assets and/or liabilities. 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. We continue to actively monitor and manage potential downgrade risk across the investment portfolio, particularly as continued sustained inflation and uncertain central bank monetary responses, may drive macro and individual counterparty weakness.

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 Board Risk Committee.

Risk mitigants

Rothesay manages our investments in-house which allows us to pro-actively manage the composition of our investment portfolio. We are able to diversify exposures across and within sectors, controlling position sizes through limits, and regular monitoring and oversight of investments. For more liquid investments, we are able to actively reduce exposure where we have credit or other concerns.

When making new investments, Rothesay considers the potential exposure to climate change risk and other ESG factors. Where such risks are likely to be material over the life of the transaction then this will be considered during the internal credit rating assessment. Such considerations can also lead to investment in shorter duration assets and avoidance of risk exposure, for example when Rothesay funds the origination of residential mortgages, our lending criteria includes a specification of the type of properties that are acceptable including factors such as construction, location and environmental perils such as flood risk.

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.

Note F - Risk and capital management (continued)

F.2.1 Credit risk (continued)

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.

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.

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.

Notes to the financial statements continued

Note F - Risk and capital management (continued)

F.2.1 Credit risk (continued)

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.

Group and Company	2022 Net amount of financial assets presented in the statement of financial position £m	Related amounts not offset: Netting under master netting agreements £m	Cash collateral £m	Security collateral and charges £m	Net credit exposures £m
Derivative assets	**37,810**	**(33,633)**	**(2,399)**	**(1,738)**	**40**
Collateralised agreements and financing	**430**	**–**	**–**	**(430)**	**–**
Total	**38,240**	**(33,633)**	**(2,399)**	**(2,168)**	**40**
Derivative liabilities	**(37,799)**	**33,633**	**1,346**	**2,793**	**(27)**
Collateralised financing agreements	**(3,628)**	**–**	**–**	**3,628**	**–**
Total	**(41,427)**	**33,633**	**1,346**	**6,421**	**(27)**

Group and Company	2021 Net amount of financial assets presented in the statement of financial position £m	Related amounts not offset: Netting under master netting agreements £m	Cash collateral £m	Security collateral and charges £m	Net credit exposures £m
Derivative assets	20,769	(16,326)	(654)	(3,743)	46
Collateralised agreements and financing	262	–	(88)	(174)	–
Total	21,031	(16,326)	(742)	(3,917)	46
Derivative liabilities	(20,688)	16,326	208	4,087	(67)
Collateralised financing agreements	(414)	–	–	414	–
Total	(21,102)	16,326	208	4,501	(67)

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. Bilateral derivative transactions have benefitted from additional collateral security in the form of Initial Margin since 1 September 2021.

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 £33,633m (2021: £16,326m) 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.

Note F - Risk and capital management (continued)

F.2.1 Credit risk (continued)

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.

Group	AAA £m	AA £m	A £m	BBB £m	BB £m	B £m	Unrated £m	Total £m
2022	**12,582**	**12,369**	**16,775**	**7,404**	**148**	**1**	**6,515**	**55,794**
2021	14,692	18,504	17,052	6,883	310	–	6,479	63,920

Company	AAA £m	AA £m	A £m	BBB £m	BB £m	B £m	Unrated £m	Total £m
2022	**12,373**	**12,369**	**16,728**	**7,404**	**148**	**1**	**6,758**	**55,781**
2021	14,692	18,504	16,880	6,883	310	–	6,752	64,021

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 £37,810m (2021: £20,769m); and
- other assets of Group £853m, Company £864m (2021: Group £682m, Company £695m); less
- payables and financial liabilities of Group £47,126m, Company £47,463m (2021: Group and Company £22,784m).

AAA rated assets include Government bonds, supranational bonds, sub sovereigns, covered bonds, US not-for-profit private universities, rate reduction bonds 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.

Unrated assets are UK and Dutch residential mortgages that are not individually rated.

Other than a small number of residential 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 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.

Notes to the financial statements continued

Note F - Risk and capital management (continued)

F.2.2 Market risk (continued)

- Property risk results from investments that are secured on commercial or residential properties. In some instances, this risk may arise from the potential impact of climate change on properties (including the need to improve the carbon efficiency of buildings). Profits and losses may be generated by material movements in spot or forward property prices. This risk is mitigated through strict underwriting criteria, aggregate risk monitoring, consideration of ESG risks 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.3 (f).

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.
- Entering into repurchase agreements and derivative and reinsurance agreements that allow Rothesay to post corporate bonds as collateral rather than just cash and gilts.
- 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 Board Risk Committee. 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.

Action was taken throughout the year to ensure that the Group's liquidity position remained robust during 2022, particularly when markets were at their most volatile.

The following table details Rothesay's financial liabilities and assets by maturity. Cash flows arising from financial investments and liabilities have been disclosed using undiscounted expected contractual cash flows. The cash flows have been adjusted for credit risk as this is the best estimation of the flows used to back the liabilities. Further details of the probability of default are included in note E.3(b). The table excludes insurance liability and insurance cash flows, totals of which are included in note E.3. The table also excludes lifetime mortgage cash flows which are included in note D.2 and leasehold cash flows which are included in note I.5. Prior year comparatives have been re-presented to remove prepayments which have already been paid as these do not meet the definition of a financial asset.

Note F - Risk and capital management (continued)
F.2.3 Liquidity risk (continued)

	2022			
Group	Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Financial assets				
Financial investments	**18,774**	**26,704**	**88,574**	**134,052**
Accrued interest	**558**	**–**	**–**	**558**
Receivables	**2,324**	**109**	**–**	**2,433**
Cash and cash equivalents	**243**	**–**	**–**	**243**
	21,899	**26,813**	**88,574**	**137,286**
Financial liabilities				
Financial liabilities	**(11,259)**	**(15,305)**	**(30,146)**	**(56,710)**
Payables	**(5,389)**	**–**	**–**	**(5,389)**
Borrowings	**–**	**(743)**	**(1,021)**	**(1,764)**
Accruals	**(86)**	**(9)**	**–**	**(95)**
	(16,734)	**(16,057)**	**(31,167)**	**(63,958)**
Net	**5,165**	**10,756**	**57,407**	**73,328**

	2021 restated			
Group	Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Financial assets				
Financial investments	14,290	13,167	69,182	96,639
Accrued interest	417	–	–	417
Receivables	503	8	–	511
Cash and cash equivalents	332	–	–	332
	15,542	13,175	69,182	97,899
Financial liabilities				
Financial liabilities	(6,028)	(2,717)	(14,907)	(23,652)
Payables	(1,682)	–	–	(1,682)
Borrowings	–	(742)	(983)	(1,725)
Accruals	(69)	–	–	(69)
	(7,779)	(3,459)	(15,890)	(27,128)
Net	7,763	9,716	53,292	70,771

Notes to the financial statements continued

Note F - Risk and capital management (continued)

F.2.3 Liquidity risk (continued)

Company	2022 Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Financial assets				
Financial investments	**18,566**	**26,704**	**88,574**	**133,844**
Accrued interest	**558**	**–**	**–**	**558**
Receivables	**2,567**	**109**	**–**	**2,676**
Cash and cash equivalents	**195**	**–**	**–**	**195**
	21,886	**26,813**	**88,574**	**137,273**
Financial liabilities				
Financial liabilities	**(11,259)**	**(15,305)**	**(30,146)**	**(56,710)**
Payables	**(5,726)**	**–**	**–**	**(5,726)**
Borrowings	**–**	**(743)**	**(1,021)**	**(1,764)**
Accruals	**(86)**	**(9)**	**–**	**(95)**
	(17,071)	**(16,057)**	**(31,167)**	**(64,295)**
Net	**4,815**	**10,756**	**57,407**	**72,978**

Company	2021 restated Less than 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
Financial assets				
Financial investments	14,290	13,167	69,182	96,639
Accrued interest	417	–	–	417
Receivables	777	8	–	785
Cash and cash equivalents	159	–	–	159
	15,643	13,175	69,182	98,000
Financial liabilities				
Financial liabilities	(6,028)	(2,717)	(14,907)	(23,652)
Payables	(1,682)	–	–	(1,682)
Borrowings	–	(742)	(983)	(1,725)
Accruals	(69)	–	–	(69)
	(7,779)	(3,459)	(15,890)	(27,128)
Net	7,864	9,716	53,292	70,872

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. Operational risk includes project risk and cyber risk. 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 Business Controls 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). Strategic projects are monitored by Rothesay's change management function and relevant committees and are required to operate according to our project management framework.

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. Operational risk also includes the risk of conduct failure – a risk that is managed by the business and overseen by the Compliance function and the Customer 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.
- Data risk arises from the risk that the cost of correcting residual data errors exceeds the provisions held against this risk. This risk is managed through detailed due diligence, exclusion of known data issues and prudence in quantifying appropriate provisions.

As at 31 December 2022, 89% of longevity risk was reinsured (2021: 84%). 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/(liabilities)

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.

The carrying amount of deferred income tax assets/liabilities 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:

Group	2022 £m	2021 £m
Other temporary differences	**2**	(5)
Total temporary differences	**2**	(5)

Company	2022 £m	2021 £m
Differences between amortised cost and fair value basis	**339**	(119)
Total temporary differences	**339**	(119)

The movements in the deferred tax balances were as follows:

Group	2022 £m	2021 £m
At 1 January	**(5)**	–
Deferred tax on other comprehensive income	**(1)**	–
Current year charge	**8**	(5)
At 31 December	**2**	(5)

Company	2022 £m	2021 £m
At 1 January	**(119)**	(82)
Deferred tax on other comprehensive income	**(1)**	–
Current year charge	**459**	(37)
At 31 December	**339**	(119)

Note G - Other statement of consolidated financial position notes (continued)

G.1 Deferred tax assets/(liabilities) (continued)

Deferred tax assets are only recognised to the extent that, based on management's assessment, they are regarded as recoverable. Management considers it appropriate to recognise a deferred tax asset in light of forecast future profits and the history of profits within the Group.

Other temporary differences are the results of differences between the accounting and tax basis which will reverse over time.

In the Spring Budget 2021, the Government announced that from 1 April 2023 the corporation tax rate would increase from 19% to 25%. This was enacted into law on 10 June 2021. On 23 September 2022, The UK Chancellor of the Exchequer announced that the intended increase in the UK corporation tax rate referred to above would be cancelled. On 14 October Liz Truss, the then Prime Minister reversed that decision made as part of the 'Mini Budget' and confirmed that the corporation tax rate will increase to 25% from the current 19% rate as of 1 April 2023. As a consequence, at balance sheet date deferred tax is still reflected at 25% in these financial statements.

Notes to the financial statements continued

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:
- investment in collective investment schemes which allows Rothesay to receive profit or income from the underlying assets held in the schemes. These are all large established money market funds of which the total asset value of the funds was £353bn (2021: £282bn);
- 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

The value of Rothesay's interests is included within financial investments (see note D.2).

As at 31 December 2022, 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 £11,471m (2021: £13,271m). The recorded fair value represents Rothesay's maximum loss exposure to these unconsolidated structured entities. The £2bn decrease in the balance was predominantly driven by the mark-to-market decrease in the value of loans secured on property.

The interest income recognised in relation to these investments was £281m (2021: £193m).

A summary of Rothesay's interest in unconsolidated structured entities is provided below and has been recognised on the balance sheet:

Group and Company	2022 £m	2021 £m
Collective investment schemes	**4,585**	5,405
Government sub sovereign and agency obligations	**40**	50
Corporate bonds and other corporate debt	**2,057**	1,556
Loans secured on property	**4,789**	6,260
Total	**11,471**	13,271

Note H - Interests in subsidiaries and associates (continued)

H.2 Investments in subsidiaries

The financial statements include the financial statements of Rothesay Life Plc and the subsidiaries listed in the following table:

Company undertakings	Country of incorporation	Primary business operation	2022 £m	2021 £m	2022 % equity interest	2021 % equity interest
LT Mortgage Financing Limited	UK	Service company	**6**	6	**100%**	100%
Rothesay Property Partnership 1 LLP	UK	Service company	**–**	–	**100%**	100%
Rothesay MA No.1 Limited	UK	Service company	**5**	5	**100%**	100%
Rothesay Mortgages Limited (formerly known as Rothesay MA No.2 Limited)	UK	Service company	**–**	–	**–**	100%
Rothesay MA No.3 Limited	UK	Service company	**2**	2	**100%**	100%
Rothesay MA No.4 Limited	UK	Service company	**–**	–	**100%**	100%

Subsidiaries are held at cost less impairment.

The above subsidiary undertakings, are registered in the United Kingdom. The registered office and principal place of business for all subsidiary undertakings is The Post Building, 100 Museum Street, London WC1A 1PB.

Rothesay Property Partnership 1 LLP was incorporated during March 2021 and has not commenced trading.

Rothesay Mortgages Limited (formerly known as Rothesay MA No.2 Limited) was incorporated during March 2019 and underwent a name change in September 2022. The entity ownership was transferred to the Group holding Company Rothesay Limited during the year.

Rothesay MA No.4 Limited (RMA4) was incorporated during November 2019, RMA4 remains dormant.

Notes to the financial statements continued

Note I - Other notes

I.1 Company profit

The profit for the financial year of the Company was £146m (2021: profit of £742m). 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 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 issues 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, redundancy or retirement (subject to Remuneration Committee approval). 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. Note that we have provided an estimate for the number of RSUs granted during the year because, although the awards have been approved in principle by the Remuneration Committee, the actual number will not be finalised until after the financial statements have been approved.

The activity related to the deferred equity award plan RSUs is set out below:

	2022 No. of RSUs	2021 No. of RSUs
Outstanding at the beginning of the year	**11,503,926**	14,046,916
Forfeited during the year	**(102,461)**	(238,851)
Vested during the year	**(5,813,603)**	(6,587,517)
Granted during the year	**5,227,239**	4,283,378
Outstanding at the end of the year	**10,815,101**	11,503,926

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.

Note I - Other notes (continued)

I.2 Share-based payments (continued)

The activity related to the ESIP RSUs is set out below:

	2022 No. of RSUs	2021 No. of RSUs
Outstanding at the beginning of the year	**492,300**	223,200
Forfeited during the year	**(56,973)**	(35,100)
Granted during the year	**269,382**	304,200
Outstanding at the end of the year	**704,709**	492,300

The methodology for calculating the fair value of the RSUs is intended to give a price consistent with the price paid by MassMutual and GIC for Blackstone's shareholding at the end of 2020. The weighted average fair value of the RSUs at 31 December 2022 was £3.86 (31 December 2021: £4.15).

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 were awarded for the first time in 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, redundancy or retirement (subject to Remuneration Committee approval). All SARs have a future service requirement. Share appreciation rights were granted in January 2021, December 2021 and December 2022.

The valuation of the SARs is based on a Black-Scholes option pricing model and uses the same methodology for valuing shares as is used for share-based payments but with adjustments for payment of dividends in the vesting period. The weighted average fair value and assumptions used to determine the fair value of the SARs are as follows:
- Weighted average fair value at grant date: £0.69
- Expected volatility: 30%
- Outstanding vesting period: three years from issue
- Risk free interest rate: nil

The number of SARs awarded is as follows:

	2022 No. of SARs	2021 No. of SARs
Outstanding at the beginning of the year	**50,726,066**	—
Forfeited during the year	**—**	—
Vested during the year	**—**	—
Granted during the year	**25,966,977**	50,726,066
Outstanding at the end of the year	**76,693,043**	**50,726,066**

Expenses in relation to share-based payment schemes

Expenses of £20m (2021: £38m) 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 decrease has been driven in part by the reduction in share price.

Notes to the financial statements continued

Note I - Other notes (continued)
I.3 Related parties disclosures
Ultimate holding company
At the financial statement date, the immediate and ultimate parent company was Rothesay Limited, which is incorporated in the United Kingdom. Group financial statements are prepared for Rothesay Limited, copies of which can be obtained from the Company Secretary, The Post Building, 100 Museum Street, London WC1A 1PB.

Related party transactions
Rothesay entered into various transactions with fellow participating interests which are subject to common control from the same source.

	2022 £m	2021 £m
Statement of comprehensive income		
Change in the reinsurers' share of insurance contract liabilities and reinsurance recoveries	**(168)**	40
Finance costs	**(18)**	(18)
Operating expenses	**(5)**	(7)
Statement of financial position		
Financial investments	**187**	–
Reinsurance	**31**	199
Borrowings	**299**	299
Capital	**2,463**	2,463

Financial investments represent a loan secured on property which is subject to common control from one of our shareholders. We have written a number of reinsurance contracts with our shareholder MassMutual. All related party transactions were discussed and approved by the Board.

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 the transactions discussed below:

Group and Company	2022 £m	2021 £m
Salaries, bonus and other employee benefits	**24**	21
Equity-based compensation payments	**14**	15
Pension costs	**1**	–
Total transactions	**39**	36

On 29 March 2022, members of key management personnel and their families sold 1,683,216 B ordinary shares to the employment benefit trust for consideration of £7m. On 31 March 2022 members of key management personnel and their families bought 4,819,277 B ordinary shares from the employment benefit trust for consideration of £20m.

Note I - Other notes (continued)

I.3 Related parties disclosures (continued)

The tables below represent transactions between RLP, its parent Rothesay Limited, its subsidiaries LTMF, RMA1 and RMA3 and other group companies RPML and Rothesay Asset Management North America LLC.

Transactions with RL	2022 £m	2021 £m
Statement of comprehensive income		
Interest income	**1**	–
Cost transfer	**5**	5
Statement of financial position		
Other receivables	**80**	49
Capital	**2,463**	2,463

Transactions with LT Mortgage Financing Limited	2022 £m	2021 £m
Statement of financial position		
Other receivables	**–**	67
Other payables	**224**	–
Capital	**6**	6

Transactions with Rothesay MA No.1 Limited	2022 £m	2021 £m
Statement of financial position		
Other receivables	**–**	40
Other payables	**73**	–
Capital	**5**	5

Transactions with Rothesay MA No.3 Limited	2022 £m	2021 £m
Statement of financial position		
Other receivables	**–**	6
Other payables	**39**	–
Capital	**2**	2

Transactions with RPML	2022 £m	2021 £m
Statement of comprehensive income		
Cost transfer	**(126)**	(113)
Statement of financial position		
Other payables	**104**	100

Notes to the financial statements continued

Note I - Other notes (continued)
I.3 Related parties disclosures (continued)

Transactions with Rothesay Asset Management North America LLC	2022 £m	2021 £m
Statement of comprehensive income		
Service fee	**(9)**	(6)
Statement of financial position		
Other receivables	**1**	–
Other payables	**3**	1

Transactions with Rothesay Asset Management Australia Pty	2022 £m	2021 £m
Statement of comprehensive income		
Transaction fee	**–**	–
Service fee	**(1)**	
Statement of financial position		
Other receivables	**–**	–
Other payables	**1**	–

Transactions with LT Mortgage Financing Limited
Between 2018 and 2021, £4.1bn of lifetime mortgages were transferred from RLP to its subsidiary LT Mortgage Financing Limited (LTMF). In September 2022, a further £0.8bn of lifetime mortgages were transferred. Whenever lifetime mortgages were transferred, LTMF became the beneficial owner of the lifetime mortgages in exchange for the issue of loan notes. These transactions took place on an arm's length basis using the fair value of the lifetime 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, £0.8bn 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 2020 and 2021, €1.0bn of Dutch mortgage loans were transferred from RLP to its subsidiary Rothesay MA No.3 Limited (RMA3). In each case, RMA3 became the beneficial owner in the Dutch mortgage loans in exchange for the issue of loan notes. This transaction 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.

On consolidation all balances relating to the securitisations, other than the mortgages and ground loans are eliminated, excluding £244m (LTMF £217m and RMA3 £27m) cash available for prepayments (2021: £161m; LTMF £144m and RMA3 £17m), which is included within Other receivables of the Company (see note D.5).

Note I - Other notes (continued)

I.4 Financial commitments and contingencies

During previous years, Rothesay executed transactions to purchase partly funded bonds and forward settling bonds. Rothesay expects to pay a further £667m within the next five years (2021: £784m), £631m of this being due within 12 months of the financial reporting date (2021: £508m).

Group and Company	2022 £m	2021 £m
Not later than one year	**631**	508
Later than one year and no later than five years	**36**	276
Later than five years	**–**	–
Total other commitments	**667**	784

I.5 Leases

(a) Amounts included in the statement of financial position

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.*

Lease payments are discounted using Rothesay's incremental borrowing rate. 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's right-of-use assets represents the lease on the UK office executed in May 2019. The lease for the UK office, The Post Building, has a duration of 17 years with a break clause at 12 years which we have assumed is exercised. The incremental borrowing rate was 3.37%.

Rothesay was not a lessor during the period.

Notes to the financial statements continued

Note I - Other notes (continued)
I.5 Leases (continued)

Right-of-use assets

Group and Company	2022 £m	2021 £m
Right-of-use asset	**27**	30
Right-of-use asset – property		
Balance at 1 January	**30**	34
Depreciation charge for the year	**(3)**	(4)
Additions	**–**	–
Closing balance at 31 December	**27**	30

Lease liabilities

Group and Company	2022 £m	2021 £m
Lease liability	**39**	42
Maturity analysis based on undiscounted liabilities		
Current liabilities		
Less than one year	**5**	5
Non-current liabilities		
One to five years	**26**	21
More than five years	**12**	12
Total undiscounted lease liabilities	**43**	38

(b) Amounts recognised in the statement of comprehensive income

Group and Company	2022 £m	2021 £m
Leasehold depreciation	**3**	4
Financing charge on lease liabilities (included in note B.4 Finance costs)	**1**	1

(c) Amounts recognised in statement of cash flows

Group and Company	2022 £m	2021 £m
Leasehold depreciation	**3**	4
Financing charge on lease liabilities	**1**	1
Total cash flows for leases	**4**	–

Alternative Performance Measures

As noted on page 28, 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 is referenced; however, some of these measures are not on a consistent basis with IFRS and therefore the methodology is explained below. Where relevant, we have used accounting policies and assumptions that are consistent with the IFRS financial statements.

These measures are included in the monthly management information circulated and discussed by the Board.

Assets under management

Assets under management can be derived by adjusting total assets for reinsurance, payables, derivatives and collateralised financing as shown in the table below. 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.

Assets under management (APM)	2022 £m	2021 £m
Total assets	**94,642**	86,011
Less reinsurance assets	**(185)**	(641)
Less payables and financial liabilities	**(47,126)**	(22,784)
Assets under management	**47,331**	62,586

Alternative presentation of IFRS profits

The alternative presentation of IFRS profits seeks to provide an explanation of the way in which profits have been generated by considering the movement in assets alongside the movement in liabilities. 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 28.

Alternative Performance Measures continued

Measure	Reconciliation to IFRS
New business profit – IFRS new business profit projected to be realised (before release of IFRS margins)	New business premium (note B.1) less increase in net insurance liabilities as a result of new business assuming that the premiums are invested in line with the long-term investment strategy. This analysis has been prepared to reflect that as at 31 December 2022, premiums from new business have been fully invested into the intended target assets, with an overall risk-adjusted yield of 4.91% p.a. across all assets. At 31 December 2021 the future investment of new business premiums was expected to increase the risk-adjusted return across all assets by 2bps compared to a yield of 1.77% p.a.
Impact of temporary investment delay	The difference between the new business profit based on the actual assets held to back the liabilities at the reporting date and the new business profit above if applicable. Where there is such an impact, we anticipate that this will reverse as assets are invested according to the long-term investment strategy. The impact will be reduced to the extent that the investment mix on new business has changed between inception and the reporting date. No such delay was experienced in 2022.
Investment profit from prior year – IFRS profits from investment of prior year premiums	The effect of economic assumption changes on net insurance liabilities due to change of investment mix in relation to business in force at the start of the period. 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).
Performance of in-force book – Profits or losses generated on the in-force book of business	Investment return* expected on the assets held plus reinsurance recoveries and release of net insurance liabilities less premiums ceded to reinsurers and policyholder claims. This represents the profit that can be attributed to: • the release of prudent margins as the business runs off (including credit default allowances and expense reserves) and as members exercise their options; • the impact of actual demographic experience versus assumptions; and • the investment return on surplus assets. Note that for 2022, this also includes the benefit from investment activity not captured in new business profit and investment profit from prior year.
Non-economic assumption changes – profits or losses generated from non-economic assumption changes	Effect of non-economic assumption changes on net insurance liabilities (note E.3(c)).
Acquisition costs	Acquisition costs from note B.3.
Maintenance expenses	Administration expenses - recurring from note B.3.
Operating profit before tax – gross IFRS profit adjusted for the impact of market fluctuations, exceptional expenses and financing costs	Sum of the rows above.
Borrowing costs	Interest payable on borrowings. This is a subset of the finance costs shown in note B.4.
Project and other one-off expenses	Administration expenses - project and other one-off expenses from note B.3.

* Includes interest paid on collateral and collateralised agreements (note B.4).

Measure	Reconciliation to IFRS
Economic profits – profit or losses generated as a result of changes in economic conditions	Change in asset valuation due to changes in economic conditions less the effect of economic assumption changes on net insurance liabilities (note E.3(c)). Changes in economic conditions include movements in interest rates, inflation, exchange rates, credit spreads, credit default allowances, actual defaults and property prices. The release of credit default allowances over time is included in the performance of the inforce book.
Profit before tax	Sum of the above and consistent with reported profit.

Solvency measures

Rothesay is a regulated entity under the Solvency II regulatory framework and therefore uses a number of APMs that are derived from Solvency II measures in addition to those that are derived from IFRS-based measures. The assumptions and methodology used in the calculation of solvency is subject to review and approval by the Board.

Own Funds represent the capital in excess of technical provisions and provide a measure of regulatory capital. A reconciliation of Own Funds to IFRS equity is provided in note F.1.

Under Solvency II, the capital required to withstand a 1-in-200-year event is known as the solvency capital requirement (SCR). **SCR coverage** is then Own Funds (capital in excess of technical provisions) divided by the SCR and expressed as a percentage. For 2022, an adjustment has been made to reflect the 14% impact on coverage of moving new liability trades to the Matching Adjustment fund. SCR coverage provides a measure of the financial strength of Rothesay. It is not possible to reconcile the SCR or the SCR coverage to the IFRS financial statements.

Other APMs

The **longevity reinsurance percentage** provides an indication of the extent to which Rothesay is protected from fluctuations in longevity through reinsurance. The percentage is derived by comparing the IFRS sensitivity of net insurance liabilities with the sensitivity of gross insurance liabilities to changes in assumed longevity (see note E.3(f)).

For the following APMs, it is not possible to reconcile to the IFRS financial statements:

Measure	Definition	Why is this used
Customer satisfaction	Policyholder feedback surveys are sent to all policyholders following interaction with them (apart from complaints and bereavements).	Rothesay prides itself on the quality of the service that it provides and this APM provides a measure of the quality of that service.
Complaints received and upheld	The number of complaints received and upheld by Rothesay per 1,000 policyholders.	Complaints provide a useful indication of customer (dis) satisfaction.

These metrics are regularly discussed by the Customer Conduct Committee.

Glossary of terms

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.
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, Rothesay therefore uses a number of Alternative Performance Measures which focus on value creation and capital strength.
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 and IFRS 17, 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.
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.
Carbon intensity	A measure of emissions that allows for comparison between entities of different size. It is measured in t CO_2e/million USD of revenue annually.
Collateralised agreements/ investments	Loans secured on property or other collateral.
Collective investment schemes	A way of investing money alongside other investors.
Contractual Service Margin (CSM)	Defined within the IFRS 17 standard as unearned profit on a group of contracts that relate to future service to be provided.
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.
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.
Currency translation	Gains and losses incurred when translating the overseas subsidiaries into the sterling consolidated balance sheet.
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.
Equity-based compensation	Share-based transactions awarded under incentive plans.
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.
Fixed-for-term mortgages	Residential mortgages where the interest rate payable is fixed at outset for the whole term of the mortgage.
Full internal model (FIM)	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.
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.
Inwards reinsurance	Reinsurance where Rothesay is acting as the reinsurer.
Lifetime mortgages	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.
Limited Price Indexation (LPI)	LPI is a pricing index used to calculate increases in components of scheme pension payments in the UK.

Glossary of terms continued

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 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.
Loss Absorbing Capacity of Deferred Taxes (LACDT)	The Loss Absorbing Capacity of Deferred Taxes adjustment reflects the fact that new deferred tax assets would be created in the event that Rothesay incurred unexpected losses, resulting in an increase of Own Funds. The LACDT reduces the SCR.
LTMF	LT Mortgage Financing Limited.
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.
Matching adjustment fund	A ring-fenced fund set up for Solvency II purposes. Liabilities written into the fund are discounted at risk free plus a matching adjustment derived from the assets in the fund. Such assets must meet eligibility criteria.
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.
Net premiums	Life insurance premiums, net of reinsurance premiums paid to third party reinsurers.
New business	New insurance contracts and reinsurance inwards sold during the period. Includes business acquired through purchase of companies.
New business premium	Premiums paid on new business transacted during the period and adjustments to new business premiums from prior periods.
New business profit	See Alternative Performance Measures.
No negative equity guarantee (NNEG)	Lifetime mortgages 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).
NZAOA	The UN-convened Net-Zero Asset Owner Alliance is a group of global asset owners setting and reporting ambitious interim targets for net-zero emissions by 2050.
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	Assets in excess of those required to meet the Solvency II technical provisions. See also 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 (PIM)	Under Solvency II, insurer's own model used to calculate the solvency capital requirement in relation to particular risks approved by the PRA.
Performance of in-force book	See Alternative Performance Measures.
Pillar 1	Under Solvency II, represents the solvency capital requirement calculated using a standard formula or (partial) internal model.
Pillar 2	Under Solvency II, represents the required risk management principles and practices relating to the risk and capital estimates covered by Pillar 1.
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.
qx	qx is actuarial notation used to represent the probability of a life aged x dying during the year.
Rate reduction bonds	A rate reduction bond is the securitisation of a stream of cash flows generated by a fee charged to utility consumers.
Regular premiums	Payments of premium made regularly over the duration of the policy.
Reinsurance	Protection sold to or purchased from another insurance company.
Risk adjustment	Defined within IFRS 17 as the compensation that Rothesay requires for bearing the non-financial uncertainty in the liabilities.
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.
RML	Rothesay Mortgages Limited (formerly known as 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.
S2PMA/S2PFA	S2PMA/S2PFA refer to mortality tables drawn up by the Continuous Mortality Investigation (CMI) of the Institute and Faculty of Actuaries. These represent version 2 of the industry standard tables derived from pensioner data from self-administered pension schemes. Separate tables are utilised for males and females.
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 model determining the weighting on recent experience. Given recent improvements, a higher Sk than adopted by RL 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, the Company is required to hold the greater of the capital required under the new Solvency II Pillar 1 framework and the capital required under its own economic capital models Solvency II Pillar 2.
SONIA	The Sterling Overnight Index Average, abbreviated to 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 Solvency II, 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.
Yield	A measure of the income received from an investment compared to the price paid for the investment. Normally expressed as a percentage.

Rothesay Life Plc
The Post Building
100 Museum Street
London WC1A 1PB

www.rothesay.com
T: 020 7770 5300