# NEWLINE INSURANCE COMPANY LIMITED

## REPORT AND ACCOUNTS

*31 DECEMBER 2018*

NEWLINE GROUP™

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## COMPANY INFORMATION
*AT 31 DECEMBER 2018*

Incorporated in England

Number 4409827

| | |
|---|---|
| **DIRECTORS** | J Christiansen<br>N D Duncan<br>S Kapur<br>R B Kastner<br>C A Overy<br>M Scales<br>J W J Spencer<br>M G Wacek<br>H J L Withinshaw |
| **SECRETARY** | H J L Withinshaw |
| **REGISTERED OFFICE** | Corn Exchange<br>55 Mark Lane<br>London<br>EC3R 7NE |
| **BANKERS** | Citibank<br>Citigroup Centre<br>Canada Square<br>Canary Wharf<br>London E14 5LB |
| **INDEPENDENT AUDITORS** | PricewaterhouseCoopers LLP<br>7 More London Riverside<br>London<br>SE1 2RT |

# STRATEGIC REPORT

*AS AT 31 DECEMBER 2018*

The Directors present their strategic report on the Company for the year ended 31 December 2018.

**REVIEW OF THE BUSINESS**

Newline Insurance Company Limited ("NICL") is a UK insurance company that operates under the Newline Group brand. NICL is a wholly owned subsidiary of Newline Holdings UK Limited ("NHUKL"), which is a wholly owned subsidiary of Odyssey Reinsurance Company ("ORC"), part of the Odyssey Group ("Group").

The principal activity of the Company is the underwriting of casualty (re)insurance business in the UK and other EU member states. The Company continues to focus on its core activities of writing casualty (re)insurance business.

The casualty (re)insurance cover provided by the Company includes the following lines of business:-

**Crime**
This line of business protects financial institutions and other organisations against losses that are discovered during the policy period arising from a variety of dishonest, fraudulent or criminal acts committed by either employees or third parties and includes coverage for robbery, hold-ups, forged documents or computer crime.

**Directors' and Officers' (D&O) Liability**
This line of business protects directors and officers of commercial entities, financial institutions and other organisations against claims that are made during the policy period alleging mismanagement and seeking to hold the directors and officers liable.

**Errors and Omissions (E&O)**
This line of business protects professional service firms, commercial entities and other financial institutions against claims made during the policy period by third parties alleging negligence and seeking to hold the company liable.

**General Liability**
This line of business protects companies against claims made by employees or third parties for losses, that occur during the policy period, arising from employee injuries at work or activities of the company that cause damage to third parties.

**Medical Malpractice**
This line of business protects hospitals and groups of individual physicians against claims made during the policy period by third parties alleging negligence and seeking to hold the hospitals and groups of individual physicians liable.

The property (re)insurance cover provided by the Company includes the following lines of business:

**Affinity and Special Risks**
This line of business provides motor-related warranty (extended warranty, GAP, and collision waiver), non-motor warranty (brown, white and yellow goods, mobile phones, etc.) and value-driven add-ons (e.g., excess waiver).

**Cargo and Specie**
This line of business provides physical damage coverage for all types of goods during transit, store, exhibition, consolidation, clearing, distribution, restoration and whilst at manufacturing centres.

**Results and performance**
The result for the calendar year is a loss before tax of £1.1m (2017: loss £1.1m). The shareholder's funds for the Company have increased by £4.1m during the year and total £33.2m (2017: £29.1m). During the year, the Company increased its share capital through the issue of 5.0m ordinary shares at par. NHUKL took up the additional shares for consideration of £5.0m.

Gross written premiums for the year were £21.9m (2017: £34.3m), in converted sterling terms; casualty business accounting for £23.0m (2017: £25.1m) of this premium. An Affinity contract from 2017 was cancelled in the early part of 2018, resulting in a return premium of £2.4m.

## STRATEGIC REPORT
*(CONTINUED)*

**Results and performance (continued)**
Net premiums written are £17.2m for the year ended 31 December 2018 (2017: £19.3m). Net premiums written and earned in 2017 were reduced by two 80% quota share reinsurance arrangements with ORC (one in respect of direct business underwritten by the Company which had been in place since 2006, and one for indirect business which was put in place during 2017), and additional reinsurance protection purchased by the company. With effect from 31st December 2017, these arrangements with ORC were cancelled on a cut-off basis.

The combined ratio for 2018 is 104.0% (2017: 112.1%), resulting in an underwriting loss, excluding investment return and other technical charges, of £0.8m (2017: loss £0.5m).

Investment return for the year was a negative £4.7m (2017: positive £4.2m) driven by losses on our equity investments. To mitigate market risk arising from the funds withheld by the Company in respect of the 80% quota share with ORC, all interest and dividend income and investment gains or losses in this portfolio, together with any fees charged by the Company's investment manager or by the financial institutions providing custodial services in respect of this portfolio, are credited or charged against this funds withheld balance in accordance with the agreement. As a result, £4.3m (2017: £3.6m charged) has been credited to the technical account, and charged to the funds withheld balance.

In 2017, an 80% quota share agreement was put in place with ORC for indirect insurance business under the terms of which, interest of LIBOR plus 225 basis points is applied to the funds withheld account. £nil has been charged as interest in 2018 to the technical account (2017: £nil), and £nil credited to the funds withheld balance.

Non-technical income of £0.7m represent net foreign exchange gains. Non-technical charges of £0.7m represents net foreign exchange gains attributable to the funds withheld financial assets and the funds withheld balance, and in accordance with the amended ORC quota share agreement for direct insurance, this has been charged to the non-technical account and credited to the funds withheld balance. Whereas in 2017, non-technical charges of £3.1m represent net foreign exchange losses of £2.7m and interest payable of £0.4m. Non-technical income of £2.0m represents net foreign exchange losses attributable to the funds withheld financial assets and the funds withheld balance, and in accordance with the amended ORC quota share agreement for direct insurance, this has been credited to the non-technical account and charged to the funds withheld balance.

With effect from 31st December 2017, ORC and the Company mutually agreed to the cancellation of the 80% quota share reinsurance agreements, on a cut-off basis. Funds withheld continue to be held by the Company in accordance with the agreements, as ORC remains liable for its proportionate share of outstanding losses (reported or unreported), on policies ceded to ORC prior to the cut-off. All earned premiums up to 31st December 2017 remained subject to the 80% quota share reinsurance agreements, however, unearned premiums of £16.4m at 31st December 2017 were not subject to these agreements.

Notwithstanding the cancellation of the 80% quota share reinsurance agreements, with effect from 1st January 2018, ORC has entered into an agreement with NICL to provide financial support to the Company should NICL's surplus of own funds over its Solvency Capital Requirement ("SCR") fall below a ratio of 115%. The prospective SCR for 2019 is £23.6m. This agreement shall remain in effect until terminated by 365 days prior written notice by ORC or the Company.

**Business environment**
Competition between insurance entities can be based on a number of factors, inter alia product, price, service, coverage, financial strength, distribution channels, enhanced commissions and reputation. In 2018, the insurance market continued to be extremely competitive as the supply of capital continued to exceed demand. Our competitors include independent insurance companies, subsidiaries or affiliates of established worldwide insurance companies and MGAs, and syndicates underwriting at Lloyd's. Some of these competitors have longer operating histories and larger capital bases than ours and, in addition, greater underwriting, marketing, and administrative resources.

For the Company, as a whole, the rating environment has experienced improvements in 2018. Whilst we are experiencing shortage of capacity in some areas of the market at present allowing us to increase rates, we do expect this to stabilise in 2019.

## STRATEGIC REPORT
*(CONTINUED)*

**Business environment (continued)**
Casualty market participants continue to compete aggressively for business and we expect the rating environment to remain highly competitive, given the uncertainty of the global economy, and the changing landscape as the UK heads towards exiting the European Union.

**Strategy**
The Company views the development of excellent producer relationships as the key to providing commercial advantage in challenging market conditions.

Price is a primary means of competition in the insurance business. We continue to emphasise disciplined underwriting over premium growth, focusing on carefully selecting the risks we insure and determining the appropriate price for assuming such risks. We are committed to maintaining our discipline and underwriting standards; as a consequence, premium volumes within our product lines and in overall terms will vary in line with prevailing market conditions.

Key factors that enable us to select price and manage our business are experience, strict underwriting discipline, analytical tools, and access to real time data. We have invested considerable time and effort in developing our systematic approach to underwriting and placing an appropriate control environment around it. To ensure that underwriting objectives are properly understood, we have implemented strict review and referral processes, sophisticated and flexible rate engines, rate level monitoring, reporting, and enlisted the assistance of actuarial and claims personnel.

**Key performance indicators (KPI's) and metrics**

The Board monitors the progress of the Company by reference to the following KPI's and metrics:

| | 2018 | 2017 | |
|---|---|---|---|
| Gross Premiums Written | £21.9m | £34.3m | Gross Premiums Written, including acquisition costs, in respect of insurance contracts |
| Net Premiums Written | £17.2m | £19.3m | Gross Premiums Written less outward reinsurance in respect of insurance contracts |
| Technical result | £(1.1)m | £0.0m | Balance on technical account for general business |
| Net loss ratio | 59.6% | 52.5% | Ratio of net claims incurred to net earned premiums |
| Combined ratio | 104.0% | 112.1% | Ratio of net claims, commissions and net operating expenses to net earned premiums |

**PRINCIPAL RISKS AND UNCERTAINTIES**
The process of risk acceptance and risk management is addressed through a framework of policies, procedures and internal controls. All policies are subject to Board approval and ongoing review by management, risk management and internal audit. All key risks identified have been fully documented and assessed. The control environment operating around these key risks is regularly reviewed to ensure that controls are operating effectively. The main risks and uncertainties to our business arise from exposure to insurance risk and financial risk. These risks are considered and discussed at length in the section of this report and accounts dealing with financial risk and insurance risk management. In addition, the Company is exposed to the following risk:

**Operational risk**
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people or systems, or external events other than those covered above. The Company has a detailed risk register and procedures for continuously monitoring the impact of such risks and the effectiveness of the controls in place to mitigate them in accordance with the agreed risk appetite.

## STRATEGIC REPORT
*(CONTINUED)*

**Financial instruments**
Information on the use of financial instruments by the Company and its management of financial risk is disclosed in Note 16 to the annual accounts. In particular, the Company's exposures to market risk, credit risk and liquidity risk are separately disclosed in that note. The Company's exposure to cash flow risk is addressed under the headings of 'Credit risk', 'Liquidity risk' and 'Market risk'.

**FUTURE DEVELOPMENTS**
Our client focus remains the mid-market and corporate sector in the UK and Continental Europe.

With the UK's decision to leave the European Union ("EU") being taken in 2016, the Company has been actively reviewing its position, and ways in which it can retain access to EU markets and business with its existing EU clients. This commenced with the opening of a new branch office in Cologne, Germany, which began underwriting Financial Lines and General Liability in early 2017, and has concluded with the company establishing a German insurance company based in Cologne. In September 2018, the Company incorporated a European holding company, which is the parent company of this European insurance company. Regulatory approval from the German regulator, Bundesanstalt für Finanzdienstleistungsaufsicht ("BaFin") to operate as an insurance company was received on 21st March 2019, and the company was officially registered on the German commercial register as Newline Europe Versicherung AG on 26th March 2019.

To further complement the Company's product offering, the Company commenced underwriting new business lines during 2017, focussed on UK and International Affinity and Special Risks products, an area in which we foresee significant opportunity in the coming years.

The Company will continue to seek to take advantage, through its expertise, of opportunities arising in its selected markets and chosen fields as and when they develop.

**SOLVENCY II**
The Company is using the Standard Formula to determine its Solvency Capital Requirement, as we consider it the most appropriate approach.

On behalf of the Board

**S Kapur**
*Director*
17 April 2019

# DIRECTORS' REPORT

*AS AT 31 DECEMBER 2018*

The Directors present their report and audited financial statements of the Company for the year ended 31 December 2018.

## FUTURE DEVELOPMENTS

Likely future developments in the business are discussed in the Strategic report.

## DIVIDENDS

The Directors do not recommend the payment of a final dividend (2017: £nil).

## DIRECTORS

The Directors listed below have held office from 1 January 2018 to the date of this report unless otherwise stated.

J Christiansen
N D Duncan
S Kapur
R B Kastner
C A Overy
M Scales
J W J Spencer
M G Wacek
H J L Withinshaw

None of the Directors had any beneficial interests in the Company during the period covered by this report.

The Company Secretary is H J L Withinshaw.

Third-party indemnity providing cover for claims for actual or alleged acts, errors, omissions, misstatements, misleading statements, neglect or breach of duty in the rendering of professional services is in place for the above directors.

## BRANCHES OUTSIDE THE UK

The Company has operated a branch office in Cologne, Germany.

## FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments and risk management are discussed within the Strategic report under 'Principal Risks and Uncertainties'.

## EVENTS AFTER THE BALANCE SHEET DATE

On 8th March 2019, the board approved the issue of 5.0m ordinary £1 shares to its immediate parent, Newline Holdings UK Limited, for consideration of £5.0m.

On 11th March 2019, the board approved a payment of €9.95m to Newline Europe Holdings GmbH as an additional payment to the capital reserve.

On 21st March 2019, regulatory approval from the German regulator, Bundesanstalt für Finanzdienstleistungsaufsicht ("BaFin") for the subsidiary of Newline Europe Holdings GmbH to operate as an insurance company was received, and the company was officially registered on the German commercial register as Newline Europe Versicherung AG on 26th March 2019.

## DIRECTORS' REPORT
*(CONTINUED)*

### STATEMENT OF DISCLOSURE OF INFORMATION TO AUDITORS

Each of the persons who is a director at the date of this report confirms that:

- so far as each of them is aware, there is no information relevant to the audit of the Company's financial statements for the year ended 31 December 2018 of which the auditors are unaware; and
- each director has taken all steps that they ought to have taken in their duty as a director in order to make themselves aware of any relevant audit information and to establish that the Company auditors are aware of that information.

### INDEPENDENT AUDITORS

The Company's independent auditors are PricewaterhouseCoopers LLP. A resolution proposing their reappointment will be submitted at the annual general meeting.

### STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland", and applicable law). Under company law the 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 company and of the profit or loss of the company 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 United Kingdom Accounting Standards, comprising FRS 102, 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 company will continue in business.

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

On behalf of the Board

**S Kapur**
*Director*
17 April 2019

# INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED

**Report on the audit of the financial statements**

**Opinion**

In our opinion, Newline Insurance Company Limited's financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland", and applicable law); and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Report and Accounts (the "Annual Report"), which comprise: the balance sheet as at 31 December 2018; the profit and loss and the statement of comprehensive income; the statement of changes in equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

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

**Basis for opinion**

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

*Independence*

We remained independent of the company 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 public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

We have provided no non-audit services to the company in the period from 1 January 2018 to 31 December 2018.

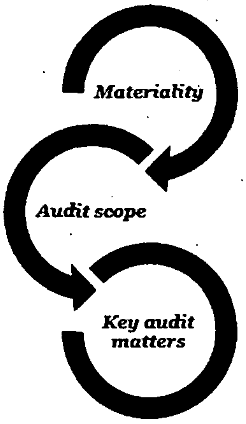
**Our audit approach**

*Context*

Newline Insurance Company Limited (NICL) is a UK insurance company that operates under the Newline Group brand. The principal activity of the company is the underwriting of casualty (re)insurance business in the UK and other EU states.

# INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

*Overview*




- Overall materiality: £330,000 (2017: £394,000), based on 10% of average profit on ordinary activities before tax over the last 3 years.

- The scope of our audit is driven by statutory and regulatory requirements in the UK and EU. Our audit objective is to obtain sufficient relevant and reliable audit evidence to enable us to issue opinions on the statutory financial statements.

- The key audit matters to report are the valuation of claims outstanding and fraud in revenue recognition.

*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. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

*Capability of the audit in detecting irregularities, including fraud*
Based on our understanding of the company and its industry, we identified that the principal risks of non-compliance with laws and regulations related to breaches of UK and European regulatory principles, such as those governed by the Prudential Regulation Authority and the Financial Conduct Authority (see page 44 of the Annual Report), and we considered the extent to which non-compliance might have a material effect on the financial statements of the company. We also considered those laws and regulations that have a direct impact on the financial statements of the company such as the United Kingdom Accounting Standards, including Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"), Financial Reporting Standard 103, "Insurance Contracts" ("FRS 103"), the Companies Act 2006, the Financial Conduct Authority's and Prudential Regulation Authority's regulations, and UK tax legislation. 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 to increase revenue of the company, management bias in accounting estimates, judgmental areas of the financial statements such as the valuation of claims outstanding, and other relevant fraud criteria. Audit procedures performed by the engagement team included:

- Discussions with the Audit Committee of the Board, management, internal audit, senior management involved in the Risk and Compliance functions and the company's General Counsel, including consideration of known or suspected instances of non-compliance with laws and regulation and fraud;
- Reviewing the results of management's internal controls designed to prevent and detect irregularities;
- Reading key correspondence with regulatory authorities which includes, the Prudential Regulation Authority and the Financial Conduct Authority in relation to compliance with laws and regulations;
- Reviewing internal audit reports in so far as they related to non-compliance with laws and regulations and fraud;
- Challenging assumptions and judgements made by management in their significant accounting estimates, in particular, the valuation of claims outstanding and premium from delegated underwriting authorities as described in the related key audit matter below;
- Identifying and testing journal entries, in particular inappropriate journal entries to increase revenue of the company, management bias in accounting estimates, judgmental areas of the financial statements such as the valuation of gross claims outstanding, as well as any journal entries posted in seldom used accounts or posted by senior management.

## INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

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

| ***Key audit matter*** | ***How our audit addressed the key audit matter*** |
|---|---|
| ***Valuation of Claims Outstanding*** | |
| Subjectivity in the Key Reserving Assumptions<br>The valuation of claims outstanding is the most material estimate in the financial statements and their valuation involves a significant degree of judgement. Any errors or management bias could lead to material misstatement. The assumptions and methodologies applied by management are therefore areas of focus for us.<br><br>The total claims outstanding for year ended 31 December 2018 are £100.0m.The liabilities are based on the estimated ultimate cost of all claims incurred but not yet settled at the valuation date, whether reported or not, together with any related claims handling costs. These estimates are based on assumptions relating to the expected settlement amounts and settlement patterns of claims and are subject to complex projections, which include application of management's judgement. There is also inherent uncertainty around the claims outstanding estimation process as a consequence of the limited period of NICL's own historical data.<br><br>The company mainly writes long-tailed classes of business, where there is a greater length of time between initial claim event and settlement. These classes tend to be more volatile in nature, and display greater variability between initial estimates and eventual settlements. | Historical claims data is a key input into the actuarial reserving process, and as such, we test the completeness, accuracy and reliability of the underlying data, to support the actuarial valuation processes.<br><br>In order to test the estimates, we are assisted by our actuarial specialist team members who performed independent re-projections on selected classes of business, particularly focusing on the largest and most volatile classes as these were considered higher risk. For these classes, we used our independent claims reserve estimates to assess management's estimates. Where significant differences arose, we investigated them.<br><br>Methodology and assumptions reviews are performed on the remaining classes. We noted that the majority of the underlying methodology and assumptions used have been consistent year-on-year.<br><br>*Based on the work performed, we found that the assumptions and methodology used to be appropriate.* |

## INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

| *Key audit matter* | *How our audit addressed the key audit matter* |
|---|---|
| ***Fraud in Revenue Recognition*** | |
| Measurement of premium from delegated underwriting authorities, including pipeline premiums<br><br>NICL writes premiums both directly and from delegated underwriting authorities. Approximately 69% of gross written premiums for NICL come through delegated authorities.<br><br>Revenue relating to delegated underwriting authorities have the most inherent risk of fraud. This is because the estimation of premium revenue from delegated underwriting authorities provides opportunities for inappropriate recording of premium revenue. In addition, there is also a lower level of direct underwriting control, which requires a greater level of monitoring to review performance and to ensure the accuracy and timeliness of reported data.<br><br>Additionally, these premiums will included an element of judgement in the calculation of pipeline premium, otherwise known as estimated premium income (EPI). As a result of the early close process, NICL estimates the premiums relating to the month of December and where necessary, makes adjustments at the period end. It is important that the methodology is appropriate and consistently applied period on period. | We have performed testing over the design and operating effectiveness of the controls surrounding the following areas:<br>- the receipt and recording of premium data;<br>- the setting of EPI, and how this is monitored; and<br>- management's review over data from holders of delegated underwriting authorities and assessment of audits of those parties.<br><br>As part of our substantive work, we have agreed a sample of binders to supporting documentation and delegated authorities' bordereaux. The methodology and assumptions adopted in calculating pipeline premium is assessed. We further reviewed the post year-end income from delegated authorities and compared to the year-end estimates, to consider whether there were any material differences.<br><br>We also assessed the historical accuracy of the premium estimates by comparing management's prior year estimates to actual premium received subsequently.<br><br>We reviewed the premium income earning methodology, and its appropriate application in the year.<br><br>*Based on the work performed, no instances of fraud were identified. We identified no indications of management bias in the calculation of binder premium estimates.* |

*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 company, the accounting processes and controls, and the industry in which it operates.

The company's operations are primarily in the United Kingdom, with a branch in Germany. A full scope audit is performed for the company, including the branch, as its financial information is maintained in the UK.

## INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

*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:

| | |
|---|---|
| ***Overall materiality*** | £330,000 (2017: £394,000). |
| ***How we determined it*** | 10% of average profit before tax over the last 3 years. |
| ***Rationale for benchmark applied*** | We have adopted to measure materiality based on the average profit before tax over the last 3 years. Profit before tax is chosen because, in our view, it is the benchmark against which the performance of the company is most commonly measured by users, and is a generally accepted benchmark. We have applied an average to the benchmark in order to take into account the volatility in earnings driven by loss events, movements in valuation of the investment portfolio and foreign exchange fluctuations. |

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £16,500 (2017: £19,700) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

**Conclusions relating to going concern**

ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report on the above matters.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the company's ability to continue as a going concern. For example, the terms on which the United Kingdom may withdraw from the European Union are not clear, and it is difficult to evaluate all of the potential implications on the company's trade, customers, suppliers and the wider economy.

**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.

## INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

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

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

*Strategic Report and Directors' Report*
In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 December 2018 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 company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report.

**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 set out on page 8, 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 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 company or to cease operations, or have no realistic alternative but to do so.

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

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

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

# INDEPENDENT AUDITORS' REPORT TO THE MEMBER OF NEWLINE INSURANCE COMPANY LIMITED
*(CONTINUED)*

## 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 received 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 financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

### Appointment

Following the recommendation of the audit committee, we were appointed by the directors on 1 January 2006 to audit the financial statements for the year ended 31 December 2006 and subsequent financial periods. The period of total uninterrupted engagement is 13 years, covering the years ended 31 December 2006 to 31 December 2018.

Mark Bolton

Mark Bolton (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
17 April 2019

## PROFIT & LOSS ACCOUNT: TECHNICAL ACCOUNT – GENERAL BUSINESS

*FOR THE YEAR ENDED 31 DECEMBER 2018*

| | Note | 2018 £'000 | 2017 £'000 |
|---|---|---|---|
| **EARNED PREMIUMS, NET OF REINSURANCE** | | | |
| Gross premiums written | 5 | **21,931** | 34,283 |
| Outwards reinsurance premiums | | **(4,778)** | (14,968) |
| Net premiums written | | **17,153** | 19,315 |
| Change in the gross provision for unearned premiums | | **3,131** | (9,493) |
| Change in the provision for unearned premiums, reinsurers' share | | **197** | (5,441) |
| Change in the net provision for unearned premiums | | **3,328** | (14,934) |
| **Earned premiums, net of reinsurance** | | **20,481** | 4,381 |
| **Allocated investment return transferred from the non-technical account** | | **(4,651)** | 4,157 |
| **CLAIMS INCURRED, NET OF REINSURANCE** | | | |
| Gross claims paid | | **(7,143)** | (6,294) |
| Reinsurers' share | | **5,008** | 4,831 |
| Net claims paid | | **(2,135)** | (1,463) |
| Change in the gross provision for claims | | **(7,447)** | (924) |
| Reinsurers' share | | **(2,617)** | 89 |
| Change in the net provision for claims | | **(10,064)** | (835) |
| **Claims incurred, net of reinsurance** | | **(12,199)** | (2,298) |
| **Net operating expenses** | 8 | **(9,102)** | (2,612) |
| **Other technical credits / (charges), net of reinsurance** | 9 | **4,306** | (3,625) |
| **Balance on the technical account for general business** | | **(1,165)** | 3 |

All operations are continuing.

The accompanying notes on pages 20 to 44 form an integral part of these annual accounts.

## PROFIT & LOSS ACCOUNT: NON-TECHNICAL ACCOUNT

*FOR THE YEAR ENDED 31 DECEMBER 2018*

| | Note | 2018 £'000 | 2017 £'000 |
|---|---|---|---|
| **BALANCE ON THE TECHNICAL ACCOUNT FOR GENERAL BUSINESS** | | **(1,165)** | 3 |
| Investment income | 11 | **330** | 1,042 |
| Net unrealised (losses) / gains on investments | 11 | **(4,794)** | 3,417 |
| Investment expenses and charges | 11 | **(187)** | (302) |
| | | **(4,651)** | 4,157 |
| Allocated investment return transferred to the general business technical account | | **4,651** | (4,157) |
| Other charges, including value adjustments | 12 | **(674)** | (3,051) |
| Other income, including value adjustments | 12 | **690** | 1,993 |
| **LOSS ON ORDINARY ACTIVITIES BEFORE TAX** | | **(1,149)** | (1,055) |
| Tax credit on ordinary activities | 7 | **187** | 192 |
| **LOSS ON ORDINARY ACTIVITIES AFTER TAX** | | **(962)** | (863) |

## STATEMENT OF COMPREHENSIVE INCOME

*FOR THE YEAR ENDED 31 DECEMBER 2018*

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Loss for the financial year** | **(962)** | (863) |
| **Other comprehensive income** | - | - |
| Fair value movements of investment in group undertaking | - | - |
| **OTHER COMPREHENSIVE INCOME FOR THE YEAR** | - | - |
| **TOTAL COMPREHENSIVE EXPENSE FOR THE YEAR** | **(962)** | (863) |

The accompanying notes on pages 20 to 44 form an integral part of these annual accounts.

# BALANCE SHEET

*AS AT 31 DECEMBER 2018*

***Company Number: 4409827***

| | Note | 2018 £'000 | 2017 £'000 |
|---|---|---|---|
| **ASSETS** | | | |
| **Investments** | | | |
| Investment in group undertaking | 13 | **77** | - |
| Financial investments | 14 | **66,520** | 56,842 |
| **Reinsurers' share of technical provisions** | | | |
| Provision for unearned premiums | | **1,775** | 1,558 |
| Claims outstanding | | **76,873** | 78,776 |
| **Debtors** | | | |
| Deposits with ceding undertakings | 18 | **4,180** | 6,968 |
| Arising out of direct insurance operations, due from intermediaries | | **8,948** | 8,179 |
| Arising out of reinsurance operations | | **3** | 3,646 |
| Other debtors | 19 | **377** | 190 |
| **Other assets** | | | |
| Tangible assets | 20 | **34** | 42 |
| Cash at bank and in hand | | **19,308** | 18,576 |
| **Prepayments** | | | |
| Accrued interest and rent | | **6** | 70 |
| Deferred acquisition costs | 21 | **2,173** | 2,465 |
| Other prepayments and accrued income | | **70** | 46 |
| **TOTAL ASSETS** | | **180,344** | 177,358 |
| **LIABILITIES** | | | |
| **Capital and reserves** | | | |
| Called up share capital | 23 | **42,500** | 37,500 |
| Profit & loss account | | **(9,341)** | (8,379) |
| **Total shareholder's funds** | | **33,159** | 29,121 |
| **Technical provisions** | | | |
| Provision for unearned premiums | | **15,218** | 17,912 |
| Claims outstanding | | **99,978** | 91,569 |
| **Creditors** | | | |
| Arising out of direct insurance operations, due to intermediaries | | **173** | 372 |
| Arising out of reinsurance operations | | **5,151** | 4,177 |
| Other creditors including taxation and social security | | **33** | 490 |
| Amount due to Group undertakings | 24 | **25,672** | 32,808 |
| **Accruals and deferred income** | | **960** | 909 |
| **TOTAL LIABILITIES AND EQUITY** | | **180,344** | 177,358 |

Approved by the Board of Directors on 17April 2019.

S Kapur
Director

The accompanying notes on pages 20 to 44 form an integral part of these annual accounts.

## STATEMENT OF CHANGES IN EQUITY
*FOR THE YEAR ENDED 31 DECEMBER 2018*

| | Called up share capital | Profit and loss account | Total |
|---|---|---|---|
| | £'000 | £'000 | £'000 |
| **At 1 January 2017** | **37,500** | **(7,516)** | **29,984** |
| Loss for the year | - | (863) | (863) |
| **Total comprehensive income for the year** | - | **(863)** | **(863)** |
| **Total transactions with owner, recognised in equity** | - | - | - |
| **At 31 December 2017** | **37,500** | **(8,379)** | **29,121** |
| Loss for the year | - | (962) | (962) |
| **Total comprehensive income for the year** | - | **(962)** | **(962)** |
| Issue of share capital | 5,000 | - | 5,000 |
| **Total transactions with owner, recognised in equity** | **5,000** | - | **5,000** |
| **At 31 December 2018** | **42,500** | **(9,341)** | **33,159** |

The accompanying notes on pages 20 to 44 form an integral part of these annual accounts.

# NOTES TO THE ACCOUNTS
*FOR THE YEAR ENDED 31 DECEMBER 2018*

## 1) GENERAL INFORMATION

The principal activity of the Company is the underwriting of casualty (re)insurance business in the UK and other EU member states. The registered office is Corn Exchange, 55 Mark Lane, London, EC3R 7NE.

## 2) ACCOUNTING POLICIES

The individual financial statements of Newline Insurance Company Limited ("NICL") have been prepared in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"), Financial Reporting Standard 103, "Insurance Contracts" ("FRS 103"), and the Companies Act 2006.

No cash flow statement is presented since FRS 102 exempts the Company from the requirement to do so as the consolidated financial statements of the ultimate parent of the Company, Fairfax Financial Holdings Limited, include a group cash flow statement.

NICL has further taken advantage of section 401 (1) of the Companies Act 2006 and has not prepared consolidated accounts, as the financial statements of Fairfax Financial Holdings Limited include consolidated accounts.

Where disclosure exemptions have been taken, the shareholder of the company has been notified in writing and does not object to the use of disclosure exemptions.

## 3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated. The FRC published a triennial review of FRS 102 in December 2017, resulting in a number of amendments and clarifications to the standard. These amendments are effective for accounting periods beginning on or after 1 January 2019, with early adoption available. NICL has adopted these amendments in 2018. The majority of amendments to the standard are editorial in nature and will have no impact on the financial statements of NICL.

***Basis of preparation***

The Directors of the Company have prepared the financial statements on the basis that the Company will continue to underwrite business in the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

The result for the year is determined on the annual basis of accounting in accordance with UK GAAP.

The preparation of financial statements in conformity with FRS 102 requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.

***a) Premiums written***
Premiums written relate to business which incepted during the year, together with any differences between booked premiums for prior years and those previously accrued, and include estimates of premiums due but not yet receivable or notified to the Company. Premiums are stated gross of acquisition costs payable, and exclude taxes and duties levied on them.

***b) Insurance contracts***
Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk. The Company considers significant insurance risk to exist where there is a reasonable possibility of a significant claim arising on the occurrence of an insured event. The Company's insurance products are classified as insurance contracts.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

***c) Unearned premiums***
Unearned premiums represent the proportion of premiums written in the year that relate to unexpired terms of policies in force at the balance sheet date, calculated on the basis of established earning patterns on a time apportionment basis as appropriate.

***d) Acquisition costs***
Acquisition costs represent commissions and are deferred to the extent that they are attributable to premiums unearned at the balance sheet date.

***e) Reinsurance premiums ceded***
Outward reinsurance premiums are accounted for in the same accounting period as the premiums for the related inwards business being reinsured.

***f) Reinsurance***
Contracts entered into by the Company with reinsurers, under which the Company is compensated for claims on one or more contracts issued by the Company and that meet the classification requirements for insurance contracts are classified as reinsurance contracts. Contracts that do not meet these classification requirements are classified as financial instruments. Insurance contracts entered into by the Company under which the contract holder is another insurer (inwards reinsurance) are included within insurance contracts; provided there is significant transfer of insurance risk.

In addition to reinsurance protection purchased, the Company was until 31 December 2017 party to two 80% quota share reinsurance arrangements with ORC; one in respect of direct business underwritten by the Company and the other in respect of indirect business. The latter arrangement was put in place during 2017 as the former arrangement did not permit the cession of indirect business to ORC. For direct business underwritten by the Company and ceded under the 80% quota share, financial assets held by the Company are assigned to this funds withheld balance. All interest and dividend income and investment gains or losses in this portfolio, together with any fees charged by the Company's investment manager or by the financial institutions providing custodial services in respect of this portfolio, are credited or charged against the funds withheld account. For indirect business underwritten by the Company and ceded under the 80% quota share, interest of LIBOR plus 225 basis points is credited to this funds withheld balance.

The investment return of the funds withheld portfolio in respect of direct business ceded under the 80% quota share is reported in the technical account, and any foreign exchange gains or losses, attributable to the funds withheld financial assets and the funds withheld balance is reported in the non-technical account; these are subsequently charged or credited against the funds withheld balance.

The amounts that will be recoverable from reinsurers are estimated based upon the gross claims provisions, having due regard to collectability. Reinsurance recoveries in respect of estimated claims incurred but not reported are assumed to be consistent with the historical pattern of such recoveries, adjusted to reflect changes in the nature and extent of the Company's reinsurance programme over time. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of each of the reinsurance companies. The reinsurers' share of claims incurred, in the profit and loss account, reflects the amounts received or receivable from reinsurers in respect of those claims incurred during the period. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised in the profit and loss account as 'Outward reinsurance premiums' when due.

***g) Claims incurred***
Gross claims incurred comprise claims and related expenses paid in the year and changes in the provisions for outstanding claims, including provisions for claims incurred but not reported and related expenses, together with any other adjustments to claims from previous years. Where applicable, deductions are made for salvage and other recoveries.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

***h) Claims provisions and related reinsurance recoveries***
Provision is made for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported to the Company. The estimated cost of claims includes expenses to be incurred in settling claims and a deduction for the expected value of salvage and other recoveries. The Company takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different to the original liability established. Large claims impacting a class of business are generally assessed separately, being measured on a case-by-case basis or projected separately in order to allow for the possible distortive effect of the development and incidence of these claims.

Provisions are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers based upon the gross provisions and having a due regard to collectability.

***i) Unexpired risk provision***
A provision for unexpired risks is made where claims and related expenses arising after the end of the financial period in respect of contracts concluded before that date are expected to exceed the unearned premiums, after the deduction of any acquisition costs deferred. The provision for unexpired risks is calculated separately by classes of business which are managed together, after taking into account the relevant investment return.

***j) Financial instruments***
The Company has chosen to adopt the provisions of Sections 11 and 12 of FRS 102 in respect of the valuation of financial instruments, which are designated by the Company at fair value through profit or loss.

*i) Financial assets*
Financial investments, including shares and other variable yield securities and units in unit trusts, debt and other fixed income securities are designated at fair value through profit and loss. Other receivables, including short term debtors arising out of direct insurance and reinsurance operations, are initially recognised at transaction price, less any impairment.

The fair value of financial investments at the balance sheet date are determined through quoted bid prices in an active market for identical instruments. When quoted prices are unavailable, the price of a recent transaction for an identical asset provides evidence of fair value as long as there has not been a significant change in economic circumstances or a significant lapse of time since the transaction took place. If the market for the asset is not active and recent transactions of an identical asset on their own are not a good estimate of fair value, the Company estimates the fair value by using a valuation technique.

Receivables are initially recognised at transaction price, and are reviewed for impairment as part of the impairment review of receivables. This basis of valuation is viewed by the Directors as having prudent regard to the likely realisable value.

*ii) Cash and cash equivalents*
Cash and cash equivalents includes cash at bank and in hand, deposits held at call with banks, other short term highly liquid investments with an original maturity date of three months or less and bank overdrafts. Bank overdrafts, when applicable, are shown within borrowings in current liabilities.

*iii) Financial liabilities*
Short term creditors, including creditors arising out of direct insurance and reinsurance operations are measured at transaction price.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

*iv) Derivative instruments*
The Company may use forward foreign exchange contracts to reduce exposure to foreign exchange rates. Derivative financial instruments are initially measured at fair value on the date on which a derivative contract is entered into, and are subsequently re-measured at fair value. Derivatives are carried as assets when the fair value is positive and as a liability when the fair value is negative.

The Company applies hedge accounting for transactions entered into to manage the foreign exchange exposure and has designated them as a fair value hedge. Changes in fair value of foreign exchange hedges are reported directly in profit and loss. Derivatives under hedge accounting are carried as assets when the fair value is positive and liabilities when the fair value is negative.

***k) Investment in group undertakings***
Investment in group undertakings are valued at fair value. Any changes in fair value are recorded in other comprehensive income.

***l) Investment return***
Investment return comprises all investment income, interest receivable and dividends received plus realised gains and losses on the disposal of investments and movements in unrealised gains and losses, net of investment expenses.

Dividend income is recognised when the right to receive payment is established. Interest and expenses are accounted for on an accruals basis.

Realised gains and losses on investments carried at market value are calculated as the difference between net sale proceeds and purchase price.

Unrealised gains and losses on investments represent the difference between the valuation at the balance sheet date and their purchase price or their valuation at the previous balance sheet date. The movement in unrealised investments gains and losses includes an adjustment for previously recognised unrealised gains and losses of those investments disposed of in the accounting period.

Investment expenses and charges comprise investment management expenses.

Investment return is initially recorded in the non-technical account. A transfer is made from the non-technical account to the general business technical account to reflect the investment return on the funds supporting the underwriting obligations arising from insurance policies.

***m) Foreign currencies***
*i) Functional and presentation currency*
The Company's functional and presentation currency is the Pound Sterling.

*ii) Transactions and balances*
Income and expenditure in US Dollars, Canadian Dollar, Egyptian Pound and Euros are translated at the average rates of exchange for the period. Underwriting transactions denominated in other foreign currencies are translated at the rates of exchange ruling at the date the transaction is processed. Assets and liabilities denominated in foreign currencies are translated into the functional currency at the rates of exchange prevailing at the balance sheet date.

Realised exchange gains / (losses) are included in the non-technical account within other income / (charges).

*iii) Translation*
Exchange differences arising from translating the result from average rates of exchange to closing rates of exchange, and the translation of the opening balance sheet to closing rates of exchange are taken through the non-technical account.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

***n) Net operating expenses***
Expenses which are incurred jointly for other Group entities and the Company are apportioned between the group entities and the Company depending on the amount of work performed, resources used and the volume of business transacted. Short term benefits (including holiday pay) and annual bonus arrangements for employees are included within this expense.

***o) Pension costs***
Newline Underwriting Management Limited operates a Group Personal Pension Plan which is on a defined contribution basis. Pension contributions relating to NICL's share of costs are charged to the Company and included within net operating expenses.

***p) Taxation***
UK taxation in the profit and loss account is based on the profit for the year as determined in accordance with the relevant tax legislation, together with adjustments for prior years.

***q) Deferred taxation***
Provision is made for deferred tax liabilities, on all material timing differences between taxable profits and total comprehensive income as reported in the financial statements. Deferred tax is calculated at the rates at which it is expected that the tax will arise. Deferred tax assets are recognised to the extent that they are regarded as more likely than not recoverable.

Deferred tax is recognised in the profit and loss account for the period, except to the extent that it is attributable to a gain or loss that is recognised directly in other comprehensive income. Deferred tax balances are not discounted.

***r) Related party transactions***
The Company discloses transactions with related parties which are not wholly owned within the same Group. Where appropriate, transactions of a similar nature are aggregated unless, in the opinion of the Directors of NICL, separate disclosure is necessary to understand the effect of the transactions.

***s) Tangible assets***
Depreciation of tangible fixed assets is calculated using the straight line convention method by reference to cost at rates estimated to write off the relevant assets over their expected useful lives, taking into account normal commercial and technical obsolescence.

The estimated useful lives are:

| | |
|---|---|
| Computer equipment | 3 – 5 years |
| Furniture, fittings & equipment | 5 years |

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 4) SIGNIFICANT JUDGEMENTS AND ESTIMATES

Preparation of the financial statements requires management to make significant judgements and estimates. The items in the financial statements where judgements and estimates have been made include:

*Estimation of claims incurred but not reported*
The estimation of claims incurred but not reported ("IBNR") is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Company, where more information about the claim event is generally available. Claims IBNR may often not be apparent to the insured until many years after the event giving rise to the claim has happened. Classes of business where the IBNR proportion of the total reserve is high will typically display greater variation between initial estimates and final outcomes because of the greater degree of difficulty of estimating these reserves. Classes of business where claims are typically reported relatively quickly after the claim event tend to display lower levels of volatility. This uncertainty varies between classes written by NICL, but is typically highest for those classes where there are significant delays in the settlement of the final claims amount, more specifically from Liability and other long-tail direct and long-tailed reinsurance classes.

In calculating the estimated cost of unpaid claims the company uses a variety of estimation techniques, generally based upon statistical analyses of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which create distortion in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in company processes which might accelerate or slow down the development and/or recording of paid or incurred claims compared with the statistics from previous periods;
- changes in the legal environment;
- the effects of inflation;
- changes in the mix of business;
- changes in underlying terms and conditions;
- the impact of large losses; and
- movements in industry benchmarks.

In setting the provision for insurance liabilities, a best estimate is determined on an undiscounted basis. For areas of specific uncertainty, it may be necessary to include a loading as part of the reserve estimate, known as the Management Adjustment. At 31 December 2018, the carrying value of gross claims IBNR is £81.4m (2017: £70.8m) and the Management Adjustment in excess of the best estimate of net reserves before the ORC quota share is £1.1m (2017: £1.1m), and £0.2m after the ORC quota share (2017: £0.2m).

*Premium income*
Written premium include estimates of premiums due but not yet received or notified to the Company, known as pipeline premium. The estimation of pipeline premium is based upon prior year experience and current year business volumes. The pipeline premium included within gross written premium is £545k (2017: £2.0m); of that £488k is unearned at 31 December 2018 (2017: £1.9m).

*Fair values of financial instruments*
The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The carrying value of these instruments is £6.0m (2017: £13.3m). The Company uses its judgement to select an appropriate method and makes assumptions that are mainly based on market conditions existing at the end of each reporting period.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 5) SEGMENTAL INFORMATION

An analysis of the underwriting result before investment return is as follows:

| | **Gross premiums written £'000** | **Gross premiums earned £'000** | **Gross claims incurred £'000** | **Gross operating expenses £'000** | **Reinsurance balance £'000** |
|---|---|---|---|---|---|
| **2018** | | | | | |
| ***Direct insurance*** | | | | | |
| Third party liability | **21,856** | **21,619** | **(13,685)** | **(8,869)** | **(1,584)** |
| Motor | **-** | **-** | **260** | **-** | **(200)** |
| Fire and other damage to property | **781** | **612** | **(627)** | **(148)** | **7** |
| Other direct classes | **94** | **102** | **(64)** | **(50)** | **(28)** |
| **Total direct** | **22,731** | **22,333** | **(14,116)** | **(9,067)** | **(1,805)** |
| ***Reinsurance acceptances*** | **(800)** | **2,729** | **(474)** | **(158)** | **(262)** |
| **Total** | **21,931** | **25,062** | **(14,590)** | **(9,225)** | **(2,067)** |

| | Gross premiums written £'000 | Gross premiums earned £'000 | Gross claims incurred £'000 | Gross operating expenses £'000 | Reinsurance balance £'000 |
|---|---|---|---|---|---|
| **2017** | | | | | |
| ***Direct insurance*** | | | | | |
| Third party liability | 24,537 | 23,976 | (7,046) | (10,201) | (8,299) |
| Motor | - | - | 45 | - | 978 |
| Fire and other damage to property | 206 | 13 | (10) | (2) | - |
| Other direct classes | 125 | 33 | (33) | (16) | - |
| **Total direct** | 24,868 | 24,022 | (7,044) | (10,219) | (7,321) |
| ***Reinsurance acceptances*** | 9,415 | 768 | (174) | (282) | (279) |
| **Total** | 34,283 | 24,790 | (7,218) | (10,501) | (7,600) |

All business has been underwritten in the United Kingdom and the German branch of the company. Gross direct business underwritten by geographical area is as follows:

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| United Kingdom | **14,589** | 34,283 |
| Germany | **7,342** | - |
| | **21,931** | 34,283 |

*Insurance risk concentrations*

The Company monitors and reports internally on insurance risk concentrations by reserving classes that have similar risk profiles and durations. Reserving classes are determined by factors such as the industry sector, insured event and insurance risk coverage offered by the insurance contract. The reserving classes are determined to be Third Party Liability, Motor, and Fire and Other Damage to Property and Other.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 6) MOVEMENT IN PRIOR YEAR'S PROVISION FOR CLAIMS OUTSTANDING

The movement in prior year's provision for claims outstanding, net of reinsurance recoveries is a favourable development of £0.3m primarily relating to Third Party Liability of £0.2m and Motor £0.1m (2017: deterioration of £0.2m primarily relating to Third Party Liability of £0.4m, partially offset by a release of £0.2m relating to Motor).

## 7) TAX CREDIT ON ORDINARY ACTIVITIES

| | **2018** | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| **(a) Analysis of credit for the year** | | |
| **Current taxation** | | |
| Current tax credit on ordinary activities | **(187)** | (190) |
| Adjustments in respect of prior periods | **-** | (2) |
| Current year losses carried forward | **187** | 190 |
| | **-** | (2) |
| **Deferred taxation** | | |
| Origination and reversal of timing differences (note 22) | **(187)** | (190) |
| | **(187)** | (190) |
| **Tax credit on ordinary activities** | **(187)** | (192) |
| **(b) Factors affecting the tax credit** | | |
| Loss on ordinary activities before tax | **(1,149)** | (1,055) |
| UK corporation tax 19.00% (2017: 19.25%) | **(218)** | (203) |
| Tax effect of: | | |
| Expenses not deductible for tax purposes | **31** | 13 |
| Adjustments in respect of prior periods | **-** | (2) |
| Tax credit for the period (note 7a) | **(187)** | (192) |

## NOTES TO THE ACCOUNTS
*(CONTINUED)*

### 8) NET OPERATING EXPENSES

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Acquisition costs | 7,023 | 8,893 |
| Change in deferred acquisition costs | 327 | (201) |
| Administrative expenses | 1,875 | 1,809 |
| Reinsurers' commissions and profit participations | (123) | (7,889) |
| | 9,102 | 2,612 |

Total commissions for direct insurance accounted for in the year amounted to £4.8m (2017: £6.2m).

Administrative expenses include:

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Auditors' remuneration** | | |
| **Audit services** | | |
| Company audit fees | 50 | 44 |
| **Non-audit services** | | |
| Audit related assurance services | - | 33 |
| | 50 | 77 |

### 9) OTHER TECHNICAL CREDITS / (CHARGES), NET OF REINSURANCE

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **(Charge) / credit to funds withheld** | | |
| Interest income on financial assets at fair value through profit and loss | 263 | 409 |
| Dividend income | 160 | 122 |
| Realised losses on realisation on investments | (387) | - |
| Realised gains on realisation of investments | 13 | 77 |
| Net unrealised (losses) / gains on investments | (4,274) | 3,133 |
| Investment management expenses | (81) | (116) |
| | (4,306) | 3,625 |

All interest and dividend income and investment gains or losses in respect of the ORC funds withheld portfolio for direct business, together with any fees charged by the Company's investment manager or by the financial institutions providing custodial services in respect of this portfolio, are credited or charged against the ORC funds withheld account.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 10) DIRECTORS' EMOLUMENTS AND STAFF COSTS

All employees are employed by Newline Underwriting Management Limited ("NUML"), a fellow subsidiary. A management charge from NUML of £2.7m has been borne by the Company during 2018 (2017: £3.7m).

The management charge includes the following amounts in respect of emoluments paid to Directors for their services to the Company:

| | **2018** | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| Emoluments | **126** | 156 |
| Contribution to pension scheme | **2** | 8 |

Retirement benefits are accruing for three Directors (2017: five) under money purchase schemes.

The highest paid director received the following remuneration:

| | **2018** | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| Emoluments | **40** | 48 |
| Contribution to pension scheme | **-** | 3 |

There are no Key Management Personnel other than the directors above.

## 11) INVESTMENT INCOME

| | **2018** | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| **Investment income (including realised gains and losses on investments)** | | |
| Interest income on financial assets at fair value through profit and loss | **409** | 415 |
| Dividend income | **177** | 122 |
| Realised gains on realisation of investments | **131** | 505 |
| Realised losses on realisation of investments | **(387)** | - |
| | **330** | 1,042 |
| **Net unrealised (losses) / gains on investments** | **(4,794)** | 3,417 |
| **Total investment expenses and charges** | | |
| Investment management expenses | **(187)** | (302) |
| | **(187)** | (302) |
| **Total investment return** | **(4,651)** | 4,157 |

All gains and losses are from investments designated at fair value through profit and loss.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 12) OTHER NON-TECHNICAL INCOME AND CHARGES

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| **Other non-technical charges** | | |
| Net foreign exchange losses | - | (2,675) |
| Net foreign exchange gains credited to funds withheld | **(674)** | - |
| Interest payable | - | (376) |
| | **(674)** | (3,051) |
| **Other non-technical income** | | |
| Net foreign exchange gains | **690** | - |
| Net foreign exchange losses charged to funds withheld | - | 1,993 |
| | **690** | 1,993 |

All foreign exchange gains and losses in respect of the ORC funds withheld portfolio and funds withheld account for direct business, are credited or charged against the funds withheld account.

## 13) INVESTMENT IN GROUP UNDERTAKING

| | Investment in subsidiary £'000 |
|---|---|
| As at 1 January 2018 | - |
| Acquisition costs | 77 |
| Fair value movement | - |
| **As at 31 December 2018** | 77 |

The subsidiary undertaking is as follows:

| **Name** | **Activity** | **Holding** | **Registered** |
|---|---|---|---|
| Newline Europe Holdings GmbH | Non-trading holding company | 100% | Germany |

During the year, NICL established an intermediate non-trading holding company (Newline Europe Holdings GmbH). This company is the sole owner of the common stock of Newline Europe Versicherung AG. Both companies registered address is Schanzenstrasse 28a, 51063 Köln, Germany. Neither company has traded during 2018.

## 14) FINANCIAL INVESTMENTS

| | 2018 £'000 Fair value | 2017 £'000 Fair value | 2018 £'000 Cost | 2017 £'000 Cost |
|---|---|---|---|---|
| Shares and other variable yield securities | **20,949** | 25,538 | **21,706** | 21,035 |
| Debt securities and other fixed income securities | **45,571** | 31,124 | **45,547** | 31,559 |
| Other | - | 180 | - | 212 |
| | **66,520** | 56,842 | **67,253** | 52,806 |

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 14) FINANCIAL INVESTMENTS *(CONTINUED)*

Of the above financial investments, £18.8m of shares and other variable yield securities (2017: £22.8m), £5.2m of debt securities and other fixed income securities (2017: £6.8m) and £nil other investments (2017: £0.2m) have been assigned to the ORC funds withheld portfolio.

*Listed investments*
Included within the carrying values above are amounts in respect of listed investments as follows:

| | 2018 | 2017 |
|---|---|---|
| | £'000 | £'000 |
| Shares and other variable yield securities | 8,345 | 6,834 |
| Debt securities and other fixed income securities | 45,571 | 28,923 |
| | 53,916 | 35,757 |

## 15) FAIR VALUE HIERARCHY

**Determination of fair value**
The table below reports on the hierarchy that reflects the significance of the inputs in determining the fair value of the financial assets and liabilities.

*Level 1*
The fair value is based on the unadjusted quoted price in an active market, for identical assets or liabilities that the Company can access at the measurement date.

*Level 2*
Inputs to level 2 fair values are inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly or indirectly.

*Level 3*
Level 3 financial instruments are financial assets and liabilities for which the values are based on prices or valuation techniques that require inputs that are both unobservable, and significant, to the fair value measurement.

During the year ended 31 December 2018 the Company held £6.0m (2017: £13.3m) of financial instruments that are classified as Level 3. Financial instruments classified as Level 3 include assets invested in common stock and limited partnerships.

Common stocks are valued utilising observable price to book multiples of peer companies and applying such to the most recently available book value per share.

Limited partnerships are valued based on the net asset values received from the general partners. These limited partnerships invest in securities that trade in active markets, and as a result, their net asset values reflect their fair values. The unobservable inputs in valuing limited partnerships include inputs such as time lags in receiving distributions by the general partners.

The Company uses a market approach, based on quoted prices and other information from independent pricing sources, to determine fair values for its fixed income financial instruments, adjusted for a risk premium for credit risk.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 15) FAIR VALUE HIERARCHY *(CONTINUED)*

| **2018** | **Fair value hierarchy** | | | | |
|---|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Assets held at fair value** | **Balance sheet total** |
| | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** |
| **Financial assets** | | | | | |
| Shares and other variable yield securities | 6,135 | 8,863 | 5,951 | 20,949 | 20,949 |
| Debt securities and other fixed income securities | 45,571 | - | - | 45,571 | 45,571 |
| Other | - | - | - | - | - |
| | 51,706 | 8,863 | 5,951 | 66,520 | 66,520 |

| **2017** | Fair value hierarchy | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Assets held at fair value | Balance sheet total |
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Financial assets** | | | | | |
| Shares and other variable yield securities | 6,834 | 5,544 | 13,160 | 25,538 | 25,538 |
| Debt securities and other fixed income securities | 28,923 | 2,201 | - | 31,124 | 31,124 |
| Other | - | - | 180 | 180 | 180 |
| | 35,757 | 7,745 | 13,340 | 56,842 | 56,842 |

## 16) FINANCIAL RISK MANAGEMENT

The Company is exposed to a range of financial risks. The key financial risk is that the proceeds of sale from financial assets are insufficient to fund the obligations arising from insurance policies and investment contracts as they fall due. The most important components of this financial risk are market risk (including interest rate risk, price risk and currency risk), credit risk and liquidity risk.

The process of risk acceptance and risk management is addressed through a framework of policies, procedures and internal controls as set out in the Risk Management Framework. This ensures that all risks are identified, recorded, assessed, taken into account and managed through the asset liability management ("ALM") framework. The control environment operating around these key risks is regularly reviewed to ensure that controls are operating effectively.

All key policies are approved by the Board and the framework is subject to ongoing review by management, Risk Management and Internal Audit as part of the ORSA process. An ORSA report is presented to the Board on at least a quarterly basis. The ORSA report sets out the risk profile and key risk indicators of the Company, together with the resulting impact on the SCR, and confirmation that sufficient own and ancillary funds are in place.

The Company has sought to further mitigate market risk from the funds withheld in respect of the 80% quota share reinsurance agreement with ORC for direct business ceded. During 2016, this arrangement was amended whereby financial assets held by the Company were specifically assigned to the funds withheld balance, and, in accordance with the quota share reinsurance agreement, all interest and dividend income and investment gains or losses in this portfolio, together with any fees charged by the Company's investment manager or by the financial institutions providing custodial services in respect of this portfolio, are credited or charged against the funds withheld account.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 16) FINANCIAL RISK MANAGEMENT (CONTINUED)

The investment return of the funds withheld portfolio is reported in the technical account, and any foreign exchange gains or losses, attributable to the funds withheld financial assets and the funds withheld balance is reported in the non-technical account; these are subsequently charged or credited against the funds withheld balance. This reinsurance agreement has been cancelled, on a cut-off basis, with effect from 1 January 2018.

The following table reconciles the balance sheet to the categories used in the asset / liability management framework, between those supporting the underwriting obligations arising from insurance policies and capital.

| 2018 | Insurance £'000 | Corporate £'000 | Total £'000 |
|---|---|---|---|
| Investment in group undertaking | - | 77 | 77 |
| Financial investments | 33,782 | 32,738 | 66,520 |
| Provision for unearned premiums | 1,775 | - | 1,775 |
| Reinsurers' share of claims outstanding | 76,873 | - | 76,873 |
| Deposits with ceding undertakings | 4,180 | - | 4,180 |
| Arising out of direct insurance operations | 8,948 | - | 8,948 |
| Arising out of reinsurance operations | 3 | - | 3 |
| Other debtors | - | 377 | 377 |
| Tangible assets | 34 | - | 34 |
| Cash at bank and in hand | 19,308 | - | 19,308 |
| Accrued interest and rent | 6 | - | 6 |
| Deferred acquisition costs | 2,173 | - | 2,173 |
| Other prepayments and accrued income | 70 | - | 70 |
| **Total assets** | 147,152 | 33,192 | 180,344 |
| Provision for unearned premiums | 15,218 | - | 15,218 |
| Claims outstanding | 99,978 | - | 99,978 |
| Arising out of direct insurance operations | 173 | - | 173 |
| Arising out of reinsurance operations | 5,151 | - | 5,151 |
| Other creditors including taxation and social security | - | 33 | 33 |
| Amount due to Group undertakings | 25,672 | - | 25,672 |
| Accruals and deferred income | 960 | - | 960 |
| **Total liabilities** | 147,152 | 33 | 147,185 |
| **Shareholder's funds** | - | 33,159 | 33,159 |

## NOTES TO THE ACCOUNTS
*(CONTINUED)*

### 16) FINANCIAL RISK MANAGEMENT *(CONTINUED)*

| 2017 | Insurance £'000 | Corporate £'000 | Total £'000 |
|---|---|---|---|
| Financial investments | 27,438 | 29,404 | 56,842 |
| Provision for unearned premiums | 1,558 | - | 1,558 |
| Reinsurers' share of claims outstanding | 78,776 | - | 78,776 |
| Deposits with ceding undertakings | 6,968 | - | 6,968 |
| Arising out of direct insurance operations | 8,179 | - | 8,179 |
| Arising out of reinsurance operations | 3,646 | - | 3,646 |
| Other debtors | - | 190 | 190 |
| Tangible assets | 42 | - | 42 |
| Cash at bank and in hand | 18,576 | - | 18,576 |
| Accrued interest and rent | 70 | - | 70 |
| Deferred acquisition costs | 2,465 | - | 2,465 |
| Other prepayments and accrued income | 46 | - | 46 |
| Total assets | 147,764 | 29,594 | 177,358 |
| Provision for unearned premiums | 17,912 | - | 17,912 |
| Claims outstanding | 91,569 | - | 91,569 |
| Arising out of direct insurance operations | 372 | - | 372 |
| Arising out of reinsurance operations | 4,177 | - | 4,177 |
| Other creditors including taxation and social security | 17 | 473 | 490 |
| Amount due to Group undertakings | 32,808 | - | 32,808 |
| Accruals and deferred income | 909 | - | 909 |
| Total liabilities | 147,764 | 473 | 148,237 |
| Shareholder's funds | - | 29,121 | 29,121 |

The Company has exposure to the following key areas of risk:

**Market risks**
*Interest rate risk*
Interest rate risk arises primarily from holding investments in fixed interest securities. In addition, to the extent that claims inflation is correlated to interest rates, liabilities to policyholders are exposed to interest rate risk. The Company monitors interest rate risk by modelling the impact of changes in interest rates (+/-100 bps, +/-200 bps) on the values of the fixed interest securities and liabilities. The Investment Committee monitors the sensitivity of the investment portfolio to movements in current interest rates. Holding a proportion of the investment portfolio in cash and cash equivalents also helps to mitigate interest rate risk.

The impact on the measurement of interest bearing securities held at reporting date of a change in interest rates of ± 0.5% on profit for the year and net assets is shown in the following table:

| | | **2018 £'000** | 2017 £'000 |
|---|---|---|---|
| Investments - Debt securities and other fixed income securities | **+0.5%** | - | (15) |
| | **-0.5%** | - | 16 |

As exposure to interest rate risk is largely held by assets specifically assigned to the ORC funds withheld account, the Company has minimal exposure to interest rate risk at December 2018 and 2017.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 16) FINANCIAL RISK MANAGEMENT *(CONTINUED)*

**Market risks *(continued)***

*Price risk*
Price risk is the risk that changes in equity market prices will impact upon the fair value of financial instruments held by the Company, whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded on the market. The impact on the measurement of investments held at reporting date of a change in equity values of ± 5% on profit for the year and net assets is shown in the following table:

| | | 2018<br>£'000 | 2017<br>£'000 |
|---|---|---|---|
| Investments – equity and related investments | +5% | 120 | 158 |
| | -5% | (120) | (158) |

As exposure to price risk sensitivity is largely held by assets specifically assigned to the ORC funds withheld account, the Company has minimal exposure to price risk sensitivity at December 2018 and 2017.

*Currency risk*
Currency risk is the risk of loss arising from adverse exchange rate movements in unhedged foreign exchange exposures. The Company writes business internationally, and so is exposed to foreign exchange risk from various activities conducted in the normal course of business. The Company monitors currency exposure, and through its Investment Committee, mitigates this risk by appropriately matching significant foreign currency denominated liabilities with assets denominated in the same currency and the purchase or sale of the relevant currencies and forward exchange contracts.

The table below sets out the significant currency exposures of the Company.

| 2018 | GBP<br>£'000 | USD<br>£'000 | EUR<br>£'000 | Other<br>£'000 | Total<br>£'000 |
|---|---|---|---|---|---|
| Investment in group undertaking | - | - | 77 | - | 77 |
| Financial investments | 38,214 | 18,533 | 3,980 | 5,793 | 66,520 |
| Deposits with ceding undertakings | - | 4,180 | - | - | 4,180 |
| Reinsurers' share of technical provisions | 44,110 | 1,707 | 32,831 | - | 78,648 |
| Cash and cash equivalents | 3,255 | 2,427 | 13,333 | 293 | 19,308 |
| Other assets | 7,609 | 978 | 2,993 | 31 | 11,611 |
| Total assets | 93,188 | 27,825 | 53,214 | 6,117 | 180,344 |
| | | | | | |
| Technical provisions | 61,991 | 9,113 | 44,092 | - | 115,196 |
| Insurance and reinsurance payables | 2,640 | 387 | 2,297 | - | 5,324 |
| Other creditors | 12,864 | 2,501 | 11,300 | - | 26,665 |
| Total liabilities | 77,495 | 12,001 | 57,689 | - | 147,185 |
| | | | | | |
| *The currency exposures are attributed to:* | | | | | |
| Funds withheld | (10,848) | 13,367 | (7,490) | 6,117 | 1,146 |
| Balance of shareholder's funds | 26,541 | 2,457 | 3,015 | - | 32,013 |
| | | | | | |
| Total shareholder's funds | 15,693 | 15,824 | (4,475) | 6,117 | 33,159 |

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 16) FINANCIAL RISK MANAGEMENT *(CONTINUED)*

**Market risks *(continued)***

| 2017 | GBP £'000 | USD £'000 | EUR £'000 | Other £'000 | Total £'000 |
|---|---|---|---|---|---|
| Financial investments | 23,967 | 21,577 | 4,418 | 6,880 | 56,842 |
| Deposits with ceding undertakings | - | 6,968 | - | - | 6,968 |
| Reinsurers' share of technical provisions | 42,818 | 2,330 | 35,186 | - | 80,334 |
| Cash and cash equivalents | 7,235 | 1,979 | 9,362 | - | 18,576 |
| Other assets | 7,095 | 1,903 | 5,640 | - | 14,638 |
| Total assets | 81,115 | 34,757 | 54,606 | 6,880 | 177,358 |
| Technical provisions | 54,562 | 11,574 | 43,345 | - | 109,481 |
| Insurance and reinsurance payables | 1,919 | 257 | 2,373 | - | 4,549 |
| Other creditors | 14,296 | 6,011 | 13,236 | 664 | 34,207 |
| Total liabilities | 70,777 | 17,842 | 58,954 | 664 | 148,237 |
| *The currency exposures are attributed to:* | | | | | |
| Funds withheld | (11,071) | 14,478 | (9,075) | 6,216 | 548 |
| Balance of shareholder's funds | 21,409 | 2,437 | 4,727 | - | 28,573 |
| Total shareholder's funds | 10,338 | 16,915 | (4,348) | 6,216 | 29,121 |

**Credit risks**

Credit risk is the risk of loss if another party fails to perform its obligations or fails to perform them in a timely fashion. Key areas where the Company is exposed to credit risk are:

- reinsurers' share of insurance liabilities;
- amounts due from reinsurers in respect of claims already paid;
- amounts due from insurance contract holders and intermediaries; and
- amounts due from investment counterparties.

The Company places limits on its exposure to a single counterparty or group of counterparties. Reinsurance is used to manage underwriting and reserving risk. This does not, however, discharge the Company's liability as primary insurer.

If a reinsurer fails to pay a claim, the Company remains liable for the payment to the policyholder. The creditworthiness of reinsurers is considered on an annual basis by reviewing their financial strength prior to finalisation of any contract. In addition, the recent payment history of reinsurers is used to update the reinsurance purchasing strategy.

*i) Premiums receivable and reinsurance debtors*

The maximum exposure to credit risk at the end of the reporting period is the carrying amount of receivables on the balance sheet.

## NOTES TO THE ACCOUNTS
*(CONTINUED)*

### 16) FINANCIAL RISK MANAGEMENT *(CONTINUED)*

**Credit risks *(continued)***

An ageing analysis for certain receivables is provided below. Other receivable balances have not been shown below as they either have no overdue amounts or represent an insignificant portion of overdue amounts.

| **2018** | **Neither due nor impaired** | **Up to 3 months** | **3 to 6 months** | **6 months to 1 year** | **Greater than 1 year** | **Total** |
|---|---|---|---|---|---|---|
| | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** | **£'000** |
| Deposits with ceding undertakings | **4,180** | **-** | **-** | **-** | **-** | **4,180** |
| Insurance debtors | **7,164** | **579** | **493** | **396** | **316** | **8,948** |
| Reinsurance debtors | **3** | **-** | **-** | **-** | **-** | **3** |
| **Total** | **11,347** | **579** | **493** | **396** | **316** | **13,131** |

| 2017 | Neither due nor impaired | Up to 3 months | 3 to 6 months | 6 months to 1 year | Greater than 1 year | Total |
|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Deposits with ceding undertakings | 6,968 | - | - | - | - | 6,968 |
| Insurance debtors | 7,171 | 452 | 315 | 128 | 113 | 8,179 |
| Reinsurance debtors | 3,646 | - | - | - | - | 3,646 |
| Total | 17,785 | 452 | 315 | 128 | 113 | 18,793 |

*ii) Credit rating of financial assets*
The following tables provide information regarding assets bearing credit risk that are neither overdue nor impaired, based on credit ratings produced by external rating agencies. These ratings for assets relating to reinsurers' share of claims outstanding relate to balances accumulated over a number of years and so will not necessarily align with the rating allocations for current reinsurance programs. The credit risk relating to investments is monitored and assessed within an agreed risk appetite.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 16) FINANCIAL RISK MANAGEMENT *(CONTINUED)*

**Credit risks *(continued)***
The maximum exposure to credit risk loss at the end of the reporting period is the carrying amount of the financial assets on the balance sheet as they are measured at fair value.

| Financial assets by credit rating | 2018 £'000 | 2017 £'000 |
|---|---|---|
| AAA | **8,165** | 6,227 |
| AA | **50,554** | 35,190 |
| A | **87,216** | 95,427 |
| BBB and below | **-** | 2,201 |
| Not rated | **20,949** | 25,763 |
| | **166,884** | 164,808 |

| Financial assets | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Shares and other variable yield securities | **20,949** | 25,538 |
| Debt securities and other fixed income securities | **45,571** | 31,124 |
| Other financial investments | **-** | 180 |
| Deposits with ceding undertakings | **4,180** | 6,968 |
| Reinsurers' share of claims outstanding | **76,873** | 78,776 |
| Reinsurance debtors | **3** | 3,646 |
| Cash at bank and in hand | **19,308** | 18,576 |
| | **166,884** | 164,808 |

**Liquidity risk**
Liquidity risk is the risk that sufficient financial resources are not maintained to meet liabilities as they fall due. The Investment Committee, a sub-committee of the Board, approves annually agreed limits on the minimum proportion of funds available to meet such calls, based on experience of claims settlement history and contemporaneous information. Management regularly review available funds to mitigate any cash flow risk.

A maturity analysis of the estimated net claims outstanding liability based on the remaining term to payment at the reporting date, and the investments that have a fixed term is provided below.

| | Gross outstanding claims liability | | Investments | |
|---|---|---|---|---|
| Maturity analysis | 2018 £'000 | 2017 £'000 | 2018 £'000 | 2017 £'000 |
| No stated maturity | **-** | - | **20,949** | 25,718 |
| Within 1 year or less | **9,625** | 9,793 | **45,571** | 28,923 |
| Within 1 to 2 years | **10,014** | 9,800 | **-** | - |
| Within 2 to 3 years | **9,381** | 9,983 | **-** | - |
| Within 3 to 4 years | **8,188** | 8,823 | **-** | - |
| Within 4 to 5 years | **7,053** | 6,894 | **-** | - |
| Over 5 years | **55,717** | 46,276 | **-** | 2,201 |
| | **99,978** | 91,569 | **66,520** | 56,842 |

The maturity of reinsurance claims recoveries follow the gross outstanding claims liability maturity analysis above.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 17) INSURANCE RISK MANAGEMENT

**Insurance risk**
Insurance risk is defined as the risk of loss arising from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities. Insurance risk is sub-divided into underwriting, reinsurance and reserving risks:

*Underwriting risk*
Underwriting risk arises from fluctuations in the frequency and severity of financial losses incurred as a result of acceptance of insurance policies. The Company manages underwriting risk by agreeing its appetite for these risks annually through the business plan, which sets out targets for volumes, pricing, line sizes and retention by class of business and through the purchase of reinsurance. Performance is monitored against the business plan on a regular basis.

A proportion of the Company's business is written through delegated authorities. A delegated authority management group monitors coverholder performance, carries out due diligence on new and existing coverholders and manages regulatory requirements. The Company has identified the areas of potential concentration of insurance exposure and monitors this and purchases reinsurance to protect against its gross effect.

*Reinsurance risk*
Reinsurance risk arises from the reinsurance purchased to protect the gross loss not responding as intended due to a mismatch with gross losses, poorly worded contracts, reinsurer counterparty risk or exhaustion of reinsurance limits. The primary purpose for our purchase of reinsurance cover is to reduce volatility associated with severe losses and systemic losses.

Reinsurance arrangements include excess of loss cover, and it is used to protect capital against underwriting risk volatility. Reinsurance creditworthiness is overseen by the reinsurance management group in placing cover.

*Reserving risk*
Reserving risk arises from claims reserves held on the balance sheet being understated or overstated. Reserves may be under or overstated due to the inherent uncertainty of knowing the ultimate timing and quantum of liabilities incurred. Claims provisions represent estimates, based on the internal reserving actuary's statistical projections. The Company estimates the ultimate settlement and administration costs of the claims incurred.

*Assumptions*
In order to determine the ultimate cost of claims, the Company uses statistical projections on the claims to be included within each reserving class and for each underwriting year. The projections use a number of methods, with chain-ladder and Bornhuetter-Ferguson being the most extensively used on both gross and ceded information.

The basic chain-ladder method uses cumulative data to derive a set of development factors based on historical information, and are most appropriate for those classes and underwriting years that have reached a relatively stable development pattern.

The Bornhuetter-Ferguson method is a standard actuarial method used to project a set of underwriting year claims ultimates, and is usually used for more recent underwriting years where there is little claims development. The Bornhuetter-Ferguson method weights two independent estimates of the ultimates, the estimate calculated from the basic chain-ladder method and another independent estimate of the claims ultimate.

There has been no change in the methodologies used in determining the ultimate cost of claims in the year.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 17) INSURANCE RISK MANAGEMENT *(CONTINUED)*

*Development*

The table below shows the development of gross and net undiscounted ultimate claims for the eight most recent underwriting years of account. All information presented in the table is reported at the current year-end rates of exchange.

Conditions and trends that have affected the development of the liabilities in the past may not occur in the future. Accordingly, conclusions about future results may not necessarily be derived from the information presented in the table below.

**Gross of reinsurance**

| | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | Total |
|---|---|---|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| At end of reporting year | 7,311 | 4,189 | 4,450 | 2,926 | 2,900 | 8,035 | 8,534 | 7,383 | |
| 1 year later | 16,922 | 12,736 | 16,750 | 12,523 | 6,915 | 13,704 | 20,324 | | |
| 2 years later | 17,257 | 13,404 | 18,434 | 18,369 | 7,277 | 14,938 | | | |
| 3 years later | 16,190 | 17,035 | 18,154 | 17,035 | 7,262 | | | | |
| 4 years later | 14,916 | 20,594 | 16,523 | 14,486 | | | | | |
| 5 years later | 13,756 | 19,545 | 15,246 | | | | | | |
| 6 years later | 11,024 | 18,323 | | | | | | | |
| 7 years later | 11,076 | | | | | | | | |
| **Cumulative payments** | 7,953 | 8,344 | 3,921 | 1,218 | 743 | 1,558 | 1,009 | 31 | 24,777 |
| **Estimated balance to pay** | 3,123 | 9,979 | 11,325 | 13,268 | 6,519 | 13,380 | 19,315 | 7,352 | 84,261 |
| **2010 & prior** | | | | | | | | | 15,717 |
| **Total gross provision included in the balance sheet** | | | | | | | | | 99,978 |

**Net of reinsurance**

| | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | Total |
|---|---|---|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| At end of reporting year | 1,252 | 710 | 718 | 2,122 | 387 | 1,202 | 1,162 | 5,502 | |
| 1 year later | 2,760 | 1,975 | 1,983 | 1,807 | 920 | 1,998 | 8,264 | | |
| 2 years later | 2,782 | 2,028 | 2,183 | 2,492 | 1,070 | 2,275 | | | |
| 3 years later | 2,530 | 2,586 | 2,135 | 2,398 | 1,082 | | | | |
| 4 years later | 2,409 | 3,262 | 2,371 | 2,163 | | | | | |
| 5 years later | 2,307 | 3,419 | 2,233 | | | | | | |
| 6 years later | 2,126 | 3,230 | | | | | | | |
| 7 years later | 2,129 | | | | | | | | |
| **Cumulative payments** | 1,590 | 1,644 | 762 | 241 | 145 | 311 | 673 | 31 | 5,397 |
| **Estimated balance to pay** | 539 | 1,586 | 1,471 | 1,922 | 937 | 1,964 | 7,591 | 5,471 | 21,481 |
| **2010 & prior** | | | | | | | | | 1,624 |
| **Total net provision included in the balance sheet** | | | | | | | | | 23,105 |

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 17) INSURANCE RISK MANAGEMENT *(CONTINUED)*

*Sensitivity*
The following table presents the sensitivity of the value of net insurance liabilities disclosed in this note to movements in the assumptions used in the estimation of insurance liabilities. The sensitivity impact on the result for the year and net assets is determined by applying the factors listed below separately to net claims reserves (excluding future claims handling costs), and future claims handling costs.

| | | 2018 | 2017 |
|---|---|---|---|
| **Impact on the result for the year and net assets** | | **£'000** | £'000 |
| Change in net claims reserves | **+1%** | **(217)** | (115) |
| | **-1%** | **217** | 115 |
| Changes in claims handling | **+10%** | **(14)** | (13) |
| | **-10%** | **14** | 13 |

## 18) DEPOSITS WITH CEDING UNDERTAKINGS

| | 2018 | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| Deposit held under group reinsurance arrangements | **4,180** | 6,968 |
| | **4,180** | 6,968 |

## 19) OTHER DEBTORS

| | 2018 | 2017 |
|---|---|---|
| | **£'000** | £'000 |
| Amounts due from fellow group undertakings | **190** | - |
| Deferred tax asset (see note 22) | **187** | 190 |
| | **377** | 190 |

Other debtors are due within one year.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 20) TANGIBLE ASSETS

| | Computer equipment £'000 | Fixtures, fittings and equipment £'000 | Total £'000 |
|---|---|---|---|
| **Cost:** | | | |
| 1 January, 2018 | 14 | 34 | 48 |
| Additions | - | 2 | 2 |
| 31 December, 2018 | 14 | 36 | 50 |
| **Accumulated depreciation:** | | | |
| 1 January 2018 | 3 | 3 | 6 |
| Charge for the year | 3 | 7 | 10 |
| 31 December, 2018 | 6 | 10 | 16 |
| **Net book value:** | | | |
| 31 December, 2017 | 11 | 31 | 42 |
| 31 December, 2018 | 8 | 26 | 34 |

## 21) DEFERRED ACQUISITION COSTS

All deferred acquisition costs relate to insurance contracts. The reconciliation of opening and closing deferred acquisition costs is as follows:

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| At 1 January | **2,465** | 2,222 |
| Expenses for the acquisition of insurance contracts | **7,023** | 8,893 |
| Amortisation of acquisition costs | **(7,350)** | (8,692) |
| Foreign exchange | **35** | 42 |
| At 31 December | **2,173** | 2,465 |

## 22) DEFERRED TAX

| | **2018 £'000** | 2017 £'000 |
|---|---|---|
| Tax effect of trading losses available for Group relief | **187** | 190 |
| Deferred tax asset at the start of the year | **190** | - |
| Taxation effect of trading losses Group relieved | **(190)** | - |
| Deferred tax credit in profit and loss account | **187** | 190 |
| **Deferred tax asset** | **187** | 190 |

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 23) CALLED UP SHARE CAPITAL

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Allotted, called up and fully paid | | |
| 42,500,000 (2017: 37,500,000) Ordinary shares of £1 each | **42,500** | 37,500 |

During the year, the Company issued 5.0m ordinary £1 shares to its immediate parent, Newline Holdings UK Limited, for consideration of £5.0m.

There is a single class of ordinary shares, with no restrictions on the distribution of dividends and the repayment of capital.

## 24) AMOUNT DUE TO GROUP UNDERTAKINGS

| | 2018 £'000 | 2017 £'000 |
|---|---|---|
| Amount due to fellow group undertakings | **1,142** | 807 |
| Deposit received from group reinsurance arrangements | **24,530** | 32,001 |
| | **25,672** | 32,808 |

## 25) ULTIMATE PARENT UNDERTAKING

The immediate parent of the Company is Newline Holdings UK Limited ("NHUKL"), a company incorporated in Great Britain. NHUKL is a wholly owned subsidiary of Odyssey Reinsurance Company ("ORC"), part of the Odyssey Group. The ultimate parent is Fairfax Financial Holdings Limited ("Fairfax"), a company incorporated in Canada. ORC and Fairfax are the smallest and largest group undertakings in which the Company is consolidated. Group accounts for Fairfax are available from the company secretary of NHUKL, Corn Exchange, 55 Mark Lane, London, EC3R 7NE.

## 26) TRANSACTIONS WITH RELATED PARTIES

As permitted by FRS 102 the Company has taken advantage of the exemption from disclosure of transactions with other members of the Fairfax Group.

Mr. J Spencer, a non-executive director of the Company is also a non-executive director of Markel Syndicate Management Limited and Markel International Insurance Company Limited. In 2018, the Company has placed outwards written premiums of £0.4m (2017: £0.2m) with companies associated with the Markel Group, on an arm's length basis. At the year end, £nil (2017: £nil) was due on recoveries.

# NOTES TO THE ACCOUNTS
*(CONTINUED)*

## 27) CAPITAL

The Company maintains a capital structure comprising only its equity shareholder's funds, consistent with its risk profile and the regulatory and market requirements of the business. The Company's objectives in managing its capital are to:

- match the profile of its assets and liabilities to the risk profile of the business
- satisfy the requirements of its policyholders and regulators
- retain financial flexibility by maintaining adequate liquidity

Regulatory capital requirements are determined under the EU Solvency II Directive using the Solvency II Standard Formula to determine its Solvency Capital Requirement ("SCR").

The Board has in place policies and procedures for managing compliance with regulatory capital requirements and its own capital management objective. The purpose is to balance risk and return while maintaining economic and regulatory capital in accordance with risk appetite. The Board has no appetite for the Company failing to maintain sufficient capital. To this end, the Company recalculates its SCR routinely at different points during the annual business cycle, and may also do so on an ad-hoc basis if the risk management framework identifies significant changes to the risk profile, or as required by the Board. In order to ensure that regulatory capital is maintained above the SCR, a minimum level of free assets above the SCR is set by the Board periodically.

With effect from 1st January 2018, ORC has entered into agreement with NICL to provide financial support to the Company should NICL's surplus of own funds over its SCR fall below a ratio of 115%. No support from ORC has been called upon from the 31st December 2018 and the signing of this Report and Accounts.

The Company is regulated by the Prudential Regulatory Authority ("PRA") and the Financial Conduct Authority ("FCA") and is subject to insurance solvency regulations which specify the minimum amount and type of capital that must be held in addition to the insurance liabilities. The Company manages capital in accordance with these rules and performs the necessary tests to ensure continuous and full compliance with such regulations. The level of capital held and capital requirements are reported to the Board on a regular basis.

## 28) EVENTS AFTER THE BALANCE SHEET DATE

On 8th March 2019, the board approved the issue of 5.0m ordinary £1 shares to its immediate parent, Newline Holdings UK Limited, for consideration of £5.0m.

On 11th March 2019, the board approved a payment of €9.95m to Newline Europe Holdings GmbH as an additional payment to the capital reserve.

On 21st March 2019, regulatory approval from the German regulator, Bundesanstalt für Finanzdienstleistungsaufsicht ("BaFin") for the subsidiary of Newline Europe Holdings GmbH to operate as an insurance company was received, and the company was officially registered on the German commercial register as Newline Europe Versicherung AG on 26th March 2019.