HSBC Life Assurance (Malta) Ltd

Annual Report 2017

HSBC
Insurance

The HSBC Group

HSBC Life Assurance (Malta) Ltd. is a fully owned subsidiary of HSBC Bank Malta p.l.c. which is a member of the HSBC Group, whose ultimate parent company is HSBC Holdings plc. Headquartered in London, HSBC Holdings plc is one of the largest banking and financial services organisations in the world. The HSBC Group's international network comprises around 3,900 offices in 67 countries and territories in Europe, Asia, North America, Latin America, and the Middle East and North Africa.

HSBC Life Assurance (Malta) Ltd.
Registered in Malta: C18814
Registered Office and Head Office:
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Malta
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Contents

2 Directors' Report

5 Independent Auditor's Report

Separate Financial Statements:

12 Statement of Financial Position

13 Statement of Changes in Equity

14 Statement of Profit or Loss and Other Comprehensive Income

16 Statement of Cash Flows

17 Notes on the Financial Statements

For the Year Ended 31 December 2017

The directors present their report together with the audited financial statements of HSBC Life Assurance (Malta) Ltd ("the Company") for the year ended 31 December 2017.

Board of directors

The Directors of the Company who held office during the year were:

Andrew Beane (Chairman)
Philip Farrugia
Mary Grace Demicoli
Rashid Daurov
Harpal Karlcut
Daniel Robinson
Ingrid Azzopardi (appointed on 16 January 2017)
Stuart John Fairbairn (appointed on 17 February 2017)
Ian Moore (resigned on 31 August 2017)

Principal activities

The Company is authorised to carry on the business of insurance by the Malta Financial Services Authority (MFSA), regulated by the Insurance Business Act, (Chapter 403, Laws of Malta). The principal activity of the Company is to carry on long term business of insurance in and from Malta. The Company is also passported, under the Freedom of Services Legislation into several European countries and is also licensed to offer business of insurance in Jersey, Channel Islands.

Business review

The Company reported a profit before tax of €7.3m for 2017, which is in line with prior year.

Gross premium income for the year was 33% higher than prior year. This was largely due to substantial growth in the single premium business and a 2% increase in protection business gross written premiums.

Investment income from non-unit linked investments was €12.6m lower than 2016 out of which €1.7m related to shareholders' investments. This was due to the poor performance of the local market and negative currency movements. The investment performance benefited by the international equity rally in 2017.

The Company continued the diversification of its fixed interest assets in order to reduce the reinvestment risk and the dilution of the yield to maturity of the fixed income portfolio. The Company introduced new asset classes with low correlation to traditional fixed income, while avoiding the volatility of traded stocks. The diversification also aims to facilitate a competitive bonus distribution in line with the policyholders expectations, whilst assuring prudent liability matching.

During the year under review, movements in the Euro interest rate yield curve and inflation impacted the Company's financial results positively by €1.8m.

As a result of the healthy with-profits smoothing reserves and the positive investment performance, the Company was able to maintain its philosophy of paying terminal bonus to eligible policies which matured during the year. The Board declared a 0.5% top-up revisionary bonus for 2017, in addition to the 1.25% which was declared upfront in the beginning of the year. Furthermore, the Board also declared a guaranteed bonus of 1.25% for 2018. This is payable to policyholders net of tax. In line with the bonus philosophy, this rate is based on conservative assumptions, with the difference to actual experience made up through the final terminal bonus. A discretionary top up bonus may be declared at the year end.

At 31 December 2017, total assets are recorded at €1,451.4m, a reduction of €224.8m from prior year's level. This reduction is largely attributable to surrenders of unit-linked investment policies which formed part of the 2014 acquired business.

On 9 November 2017, the Company entered into a Portfolio Transfer Agreement with Lombard International Assurance S.A. for the sale of a group of policies forming part of the Wealth Insurance Italy portfolio acquired by the Company in 2014. The transfer is expected to be completed in 2018, subject to regulatory approvals and consequently the assets and liabilities pertaining to the Portfolio Transfer Agreement have been treated as held for sale in accordance with IFRS 5. This transaction will not have a significant impact on the future years' profits.

At the end of 2017, the Company is adequately capitalised with an unaudited Solvency Ratio well in excess of the Solvency Capital Requirement stipulated by the Solvency II regime.

Future developments

The Company is focused on growth within the core domestic market during 2018, leveraging on the current Maltese economic environment, pensions legislation and HSBC's financial planning and wealth management capabilities. The Company is committed to increase its focus in product innovation and customers' need for protection and long-term savings.

Risks and uncertainties

A major challenge which the Company will be facing over the next twelve months is the adoption of the various regulatory changes which will come into force, namely The Insurance Distribution Directive, MFSA Conduct of Business Rule Book and Global Data Protection Regulations.

The Company is a part of the wider HSBC Group and places a reliance on the Group as the primary distributor of its products. The Company has limited influence over the focus placed on the distribution of its products compared to other priorities. Given new business sales are the key contributor to the Company's income this creates a risk.

The current low interest rate environment also poses a challenge to the Company mainly due to the lack of high quality fixed interest instruments with adequate risk versus return ratios.

Further information with respect to insurance and financial risks is included in notes 5.1 and 5.2.

Dividends

The Company did not pay or declare any dividend during the year ending 31 December 2017.

No final dividends are being recommended.

Reserves

The directors propose that the balance of retained earnings amounting to €57.6m is to be carried forward to the next financial year.

Statement of directors' responsibilities

The directors are required by the Maltese Insurance Business Act, (Chapter 403, Laws of Malta) and the Maltese Companies Act, (Chapter 386, Laws of Malta) to prepare financial statements which give a true and fair view of the state of affairs of the Company at the end of each financial year and of the profit or loss for that year.

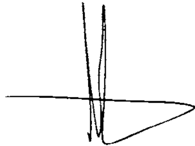
In preparing the financial statements, the directors are responsible for:

- ensuring that the financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU;
- selecting and applying appropriate accounting policies;
- making accounting estimates that are reasonable in the circumstances;
- ensuring that the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Company will continue in business as a going concern.

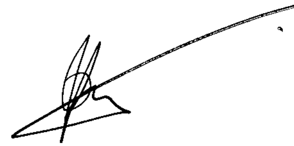
The directors are also responsible for designing, implementing and maintaining internal controls relevant to the preparation and the fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, and that comply with the Maltese Insurance Business Act, (Chapter 403, Laws of Malta) and with the Maltese Companies Act, (Chapter 386, Laws of Malta). They 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.

The financial statements of HSBC Life Assurance (Malta) Ltd for the year ended 31 December 2017 are included in the Annual Report 2017, which is published in hard-copy printed form and may be made available on the Company's website. The directors are responsible for the maintenance and integrity of the Annual Report on the website in view of their responsibility for the controls over, and the security of, the website. Access to information published on the Company's website is available in other countries and jurisdictions, where legislation governing the preparation and dissemination of financial statements may differ from requirements or practice in Malta.

Approved by the Board of Directors on 16 February 2018 and signed on its behalf by:



Andrew Beane, *Chief Executive Officer*



Harpal Karlcut, *Non-executive Director*

Registered Office

80 Mill Street
Qormi QRM 3101
Malta

Report on the audit of the financial statements

Our opinion

In our opinion:

- HSBC Life Assurance (Malta) Ltd's financial statements (the "financial statements") give a true and fair view of the company's financial position as at 31 December 2017, and of its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU; and
- The financial statements have been prepared in accordance with the requirements of the Maltese Companies Act (Cap. 386).

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

HSBC Life Assurance (Malta) Ltd's financial statements, set out on pages 12 to 76, comprise:
- the statement of financial position as at 31 December 2017;
- the statement of changes in equity for the year then ended;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements section of our report.*

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

Independence

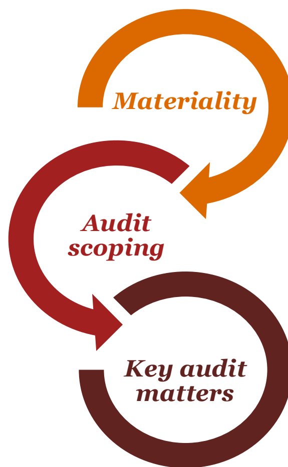
We are independent of the company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act (Cap. 281) that are relevant to our audit of the financial statements in Malta. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the company are in accordance with the applicable law and regulations in Malta and that we have not provided non-audit services that are prohibited under Article 18A of the Accountancy Profession Act (Cap. 281).

The non-audit services that we have provided to the company, in the period from 1 January 2017 to 31 December 2017, are disclosed in note 11 to the financial statements.

Our audit approach

Overview



Overall materiality: €769,000, which represents 1% of gross premiums written.

Measurement of insurance contract provisions and the present value of in-force business (PVIF)

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered 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. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the accounting processes and controls, and the industry in which the company operates.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall materiality	€769,000
How we determined it	1% of gross premiums written
Rationale for the materiality benchmark applied	We chose gross premiums written as reflected in the statement of profit or loss as the benchmark because, in our view, it is a key financial statement metric used in assessing the performance of the company, and is not as volatile as other profit and loss measures. We selected 1% based on our professional judgement, noting that it is also within the range of commonly accepted revenue-related benchmarks.

We have applied a higher materiality of €9,000,000 solely for the purpose of identifying and evaluating the effect of misstatements that are likely only to lead to a reclassifications between line items within assets and liabilities.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above €76,900 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters 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.

Key audit matter	How our audit addressed the Key audit matter
Measurement of insurance contract provisions and the present value of in-force business (PVIF)	
Management's valuation of the provisions for the settlement of future claims attributable to life insurance contracts, and of the PVIF involves complex and subjective judgements about future events, both internal and external to the business, for which small changes in assumptions can result in material impact to the valuation of these items. We focused on this area due to the materiality and subjectivity of the judgements made. Economic assumptions (investment return and associated discount rates) and non-economic assumptions (mortality, lapse rates and expenses associated with servicing policies), including the respective margins applied, are the key inputs to which the carrying amounts of these long-term liabilities and intangible asset are highly sensitive. Relevant references in the financial statements are: • Significant accounting policies: Notes 3.1 and 3.8; • Critical accounting judgements and estimates: Note 4; • Note on intangible assets: Note 16; and	Our audit procedures addressing the valuation of the company's life insurance contract liabilities, and of the PVIF. included the following procedures using our actuarial specialist team members: • we tested the accuracy of the underlying data utilised for the purposes of measurement by reference to its source; • we applied our industry knowledge and experience in comparing the methodology, models and assumptions used to recognised actuarial practices; and • we tested management's controls in respect of the valuation and assumption setting processes, and we assessed management's key judgements throughout the processes. In respect of the assumptions underlying the measurement of the life insurance contract liabilities, we performed the following procedures using our actuarial specialist team members: • we assessed the assumptions for investment mix and projected investment returns by reference to company-specific and market observable data (euro swap curve); • we considered the appropriateness of the mortality assumptions by reference to company and industry data on historical mortality experience and expectations of future mortality; and • we tested the future expense assumption by understanding and challenging the basis on which expenses are allocated between new business and renewal, and by reference to market observable data (inflation curve). The following procedures addressing the assumptions underlying the valuation of the PVIF were performed, also through the involvement of our actuarial specialist team members: • we leveraged the testing performed in relation to those assumptions that are aligned with the insurance contract liability valuation, reviewing the differences in margins applied between the two; and • we considered the appropriateness of the lapse rate assumptions by reference to company data, considering the results of management's analysis of recent lapse experience. In respect of all the assumptions referred to above, we have reviewed management's approach to setting the assumptions, assessed the assumptions' appropriateness based on internal and external data,

Key audit matter	How our audit addressed the Key audit matter
• Note on insurance liabilities: Note 19.	and tested management's governance and controls over the assumption basis review. We also reviewed the modelled results and manual adjustments, and we assessed the reasonableness of management's analysis of the changes in the carrying amounts. Based on the results of our work, we concluded that the data and assumptions used by management were reasonable.

Other information

The directors are responsible for the other information. The other information comprises the Directors' Report (but does not include the financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report.

Our opinion on the financial statements does not cover the other information, including the directors' report.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above 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.

With respect to the Directors' report, we also considered whether the Directors' report includes the disclosures required by Article 177 of the Maltese Companies Act (Cap. 386).

Based on the work we have performed, in our opinion:

- The information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Directors's report has been prepared in accordance with the Maltese Companies Act (Cap. 386).

In addition, in light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we are required to report if we have identified material misstatements in the Directors' report and other information that we obtained prior to the date of this auditor's report. We have nothing to report in this regard.

Responsibilities of the directors and those charged with governance for the financial statements

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Maltese Companies Act (Cap. 386), and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the 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 has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the company's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs 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.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

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

Report on other legal and regulatory requirements

Other matters on which we are required to report by exception

We also have responsibilities under the Maltese Companies Act (Cap. 386) to report to you if, in our opinion:

- Adequate accounting records have not been kept, or that returns adequate for our audit have not been received from branches not visited by us.
- The financial statements are not in agreement with the accounting records and returns.
- We have not received all the information and explanations we require for our audit.
- Certain disclosures of directors' remuneration specified by law are not made in the financial statements, giving the required particulars in our report.

We have nothing to report to you in respect of these responsibilities.

Appointment

We were first appointed as auditors of the company on 22 April 2015. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 3 years.

PricewaterhouseCoopers
78, Mill Street
Qormi
Malta

Romina Soler
Partner

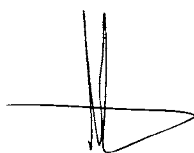
16 February 2018

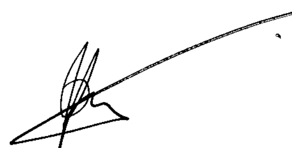
Statements of Financial Position at 31 December 2017

	Note	2017 €000	2016 €000
Assets			
Property and equipment	*14*	**1**	3
Investment properties	*15*	**3,100**	2,846
Intangible assets	*16*	**59,488**	62,350
Financial investments:	*17*		
– Equities		**14,887**	18,949
– Debt securities – available-for-sale		**1,213**	4,648
– Debt securities – at fair value through profit or loss		**260,079**	283,723
– Collective investment schemes		**42,728**	34,205
– Net assets held to cover linked liabilities		**410,538**	1,052,891
Assets of disposal group classified as held for sale	*18*	**473,797**	–
Reinsurance assets	*19*	**85,887**	85,228
Current tax assets		**128**	5,047
Insurance and other receivables	*20*	**4,803**	5,170
Cash at bank	*21*	**94,751**	141,175
Total assets		**1,451,400**	1,696,235
Liabilities			
Insurance contract provisions:	*19*		
– Claims outstanding		**3,824**	3,524
– Non-linked business		**432,201**	436,897
– Linked business		**222,767**	205,140
Liabilities of disposal group classified as held for sale	*18*	**473,797**	–
Financial liabilities:			
– Investment contracts at fair value	*22*	**203,136**	930,936
Reinsurance payables		**1**	90
Provision for liabilities and charges	*23*	**689**	–
Insurance payables, other payables and deferred income	*24*	**8,606**	9,391
Deferred tax liabilities	*25*	**20,766**	29,369
Total liabilities		**1,365,787**	1,615,347
Net assets		**85,613**	80,888
Shareholders' equity			
Share capital	*27.1*	**27,961**	27,961
Retained earnings		**57,642**	52,820
Fair value reserve	*27.2*	**10**	107
Total shareholders' equity		**85,613**	80,888

The notes on pages 17 to 57 are an integral part of these financial statements.

The financial statements on pages 12 to 57 were approved and authorised for issue by the Board of Directors on 16 February 2018 and signed on its behalf by:





Andrew Beane, *Chief Executive Officer*

Harpal Karlcut, *Non-executive Director*

Statements of Changes in Equity for the year ended 31 December 2017

	Share capital	*Revaluation reserve*	*Retained earnings*	*Total equity*
	€000	**€000**	**€000**	**€000**
Balance at 1 January 2016	27,961	55,905	207	84,073
Comprehensive income for the year				
Profit for the year				
Other comprehensive income	–	4,741	–	4,741
Net fair value movement on available-for-sale financial assets, net of tax	–	–	(100)	(100)
Total comprehensive income for the year	–	4,741	(100)	4,641
Transactions with owners, recorded directly in equity				
Accumulated Reserves acquired from amalgamation of subsidiary company	–	148	–	148
Share-based payments acquired from amalgamation of subsidiary company	–	26	–	26
Dividends (note 28.3)	–	(8,000)	–	(8,000)
Net distributions to owners	–	(7,826)	–	(7,826)
Balance at 31 December 2016	27,961	52,820	107	80,888
Balance at 1 January 2017	**27,961**	**52,820**	**107**	**80,888**
Comprehensive income for the year				
Profit for the year	**–**	**4,822**	**–**	**4,822**
Other comprehensive income				
Net fair value movement on available-for-sale financial assets, net of tax	**–**	**–**	**(97)**	**(97)**
Total other comprehensive income	**–**	**4,822**	**(97)**	**4,725**
Balance at 31 December 2017	**27,961**	**57,642**	**10**	**85,613**

The notes on pages 17 to 57 are an integral part of these financial statements.

Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2017

	Note	2017 €000	2016 €000
Technical Statement			
Earned premiums, net of reinsurance			
Gross premiums written	*6*	**76,984**	57,921
Outward reinsurance premiums		**(3,482)**	(4,543)
Net premiums written		**73,502**	53,378
Investment contracts fee income	*7*	**2,375**	2,575
Investment income	*8*	**28,581**	108,796
		104,458	164,749
Claims incurred and benefits accrued, net of reinsurance			
Claims paid:			
– Gross amount		**(64,180)**	(39,959)
– Reinsurers' share		**2,267**	3,413
		(61,913)	(36,546)
Change in provisions for claims:			
– Gross amount	*19.3*	**(300)**	3,080
– Reinsurers' share	*19.4*	**477**	(3,219)
		177	(139)
Change in technical provisions, net of reinsurance			
Long term business:			
– Gross amount	*19.3*	**9,462**	(9,275)
– Reinsurers' share	*19.4*	**304**	5,332
		9,766	(3,943)
Movement in technical provisions for linked insurance contracts	*19.3*	**(17,627)**	(14,405)
		(7,861)	(18,348)
Bonuses and rebates, net of reinsurance	*19.3*	**(4,766)**	(8,304)
Balance carried forward		**30,095**	101,412
Balance brought forward		**30,095**	101,412
Investment contract benefits	*9, 22, 18.4*	**(13,290)**	(86,910)
Change in present value of in-force business	*16*	**(1,674)**	(1,688)
Acquisition costs	*10*	**(1,912)**	(1,833)
Administrative expenses	*11*	**(7,086)**	(6,334)
Net investment management charges		**(12)**	(104)
Balance on the Technical Statement		**6,121**	4,543

The notes on pages 17 to 57 are an integral part of these financial statements.

Statement of Profit or Loss and Other Comprehensive Income
for the year ended 31 December 2017 (continued)

	Note	**2017** €000	2016 €000
Non-Technical Statement			
Balance on the Technical Statement		**6,121**	4,543
Investment income	*8*	**332**	1,879
Investment management charges		**(4)**	(3)
Administrative expenses	*11*	**(390)**	(310)
Commission receivable		**1,272**	1,230
Profit before tax		**7,331**	7,339
Tax expense	*13*	**(2,509)**	(2,598)
Profit for the year		**4,822**	4,741
Other comprehensive income – items that may be reclassified to profit or loss			
Net fair value movement on available-for-sale financial assets:			
– Policyholders' investment portfolio		**(78)**	(74)
– Shareholder's investment portfolio		**(72)**	(80)
– Income tax on other comprehensive income		**53**	54
Other comprehensive income		**(97)**	(100)
Total comprehensive income		**4,725**	4,641

The notes on pages 17 to 57 are an integral part of these financial statements.

Statements of Cash Flows for the year ended 31 December 2017

	Note	**2017**	2016
		€000	€000
Cash flows from operating activities			
Insurance premiums received		**76,705**	57,900
Reinsurance premiums paid		**(3,448)**	(4,489)
Fees and commissions received		**3,637**	3,805
Interest received		**26,674**	27,379
Dividends received		**4,391**	4,662
Rental Income from investment property received		**45**	49
Claims and benefits paid as adjusted for movements in claims payable		**(63,303)**	(38,045)
Reinsurance claims received		**2,267**	3,413
Investment contract receipts		**6,203**	7,946
Investment contract benefits paid		**(222,713)**	(150,258)
Payments to employees and suppliers		**(6,867)**	(6,581)
Policyholders' investments portfolio:			
– Acquisition of investments		**(426,319)**	(309,984)
– Proceeds from sale of investments		**599,636**	374,436
Tax paid		**(6,148)**	(400)
Net cash used in operating activities		**(9,240)**	(30,167)
Cash flows from investing activities			
Interest received		**1,518**	1,536
Acquisition of intangible assets		**(116)**	(145)
Shareholder's investments portfolio:			
– Acquisition of investments		**(5,319)**	(962)
– Proceeds from sale of investments		**5,944**	1,896
Acquisition of investment property		**(26)**	(14)
Disposal of investment property		**–**	1,945
Received from amalgamation of subsidiary company		**–**	120
Net cash from investing activities		**2,001**	4,376
Cash flows from financing activities			
Dividends paid		**–**	(8,000)
Interest paid		**–**	(136)
Repayment of Subordinated loan advanced by parent bank		**–**	(8,200)
Cash used in financing activities		**–**	(16,336)
Net decrease in cash and cash equivalents		**(7,239)**	(42,127)
Cash and cash equivalents at 1 January		**141,175**	183,302
Cash and cash equivalents at 31 December	*21*	**133,936**	141,175

The notes on pages 17 to 57 are an integral part of these financial statements.

1 Reporting entity

HSBC Life Assurance (Malta) Ltd ("the Company") is a limited liability Company domiciled and incorporated in Malta.

2 Basis of preparation

2.1 *Statement of compliance*

The financial statements have been prepared and presented in accordance with International Financial Reporting Standards as adopted by the EU. All references in these financial statements to IAS, IFRSs or SIC/IFRIC interpretations refer to those adopted by the EU. They have also been drawn up in accordance with the provisions of the Companies Act, (Chapter 386, Laws of Malta) and the Insurance Business Act, (Chapter 403, Laws of Malta).

The balance sheet is organised in increasing order of liquidity, with additional disclosures on the current or non-current nature of the Company's assets and liabilities provided within the notes to the financial statements.

2.2 *Basis of measurement*

Assets and liabilities are measured at historical cost except for the value of in-force long-term assurance business within intangible assets which is measured at present value, and the following which are measured at fair value:

– derivative financial instruments;

– financial instruments designated at fair value through profit or loss;

– financial instruments classified as available-for-sale; and

– investment property.

2.3 *Functional and presentation currency*

Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). These financial statements are presented in euro, which is the Company's functional and presentation currency.

2.4 *Use of estimates and judgements*

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

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

In particular, information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in note 4.

2.5 *Standards, interpretations and amendments to published standards effective in 2017*

In 2017, the Company adopted new standards, amendments and interpretations to existing standards, that are mandatory for the Company's accounting period beginning on 1 January 2017. The adoption of these revisions to the requirements of IFRSs as adopted by the EU did not result in substantial changes to the Company's accounting policies.

2 Basis of preparation *(continued)*

2.6 New standards, interpretations and amendments to published standards not yet adopted

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2018, and have not been applied in preparing these financial statements. The Company is considering the implications of the below standards on the Company's financial results and position, and the timing of their adoption, taking cognisance of the endorsement process by the European Commission.

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income and fair value through profit or loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in other comprehensive income not recycling. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities, there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39. The requirements of IFRS 9 'Financial Instruments' will be adopted from 1 January 2018. No material impact is expected as a result of adoption.

IFRS 15, 'Revenue from contracts with customers' deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The Company will adopt the standard from 1 January 2018. No material impact is expected as a result of adoption.

IFRS 17, 'Insurance contracts' was issued in May 2017 but is not yet endorsed by the EU and will replace IFRS 4 once effective. It sets out the requirements that an entity should apply in accounting for insurance contracts it issues and reinsurance contracts it holds. IFRS 17 introduces an accounting model that measures groups of insurance contracts based on fulfilment cash flows and a contractual service margin. Through the new measurement model and presentation and disclosure requirements, IRFS 17 aims to allow for greater comparability and transparency in relation to the profitability of new and in-force business.

The separate presentation of underwriting and financial results will give more insight of the financial situation, source of profits and quality of earnings of insurance companies to the users of the financial statements. IFRS 17 is effective from 1 January 2021, and the Company is considering its impact.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

3.1 Insurance and investment contracts

3.1.1 Classification

The Company issues contracts that transfer insurance risk and/or financial risk.

Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk. As a general guideline, the Company defines significant insurance risk as the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefits payable if the insured event did not occur.

3 Significant accounting policies *(continued)*

3.1 Insurance and investment contracts (continued)

3.1.1 Classification (continued)

Investment contracts (note 3.1.2) are those contracts that transfer financial risk with no significant insurance risk.

A number of insurance contracts contain a Discretionary Participation Feature (DPF). This feature entitles the holder to receive, as a supplement to guaranteed benefits, additional bonuses:

– that are likely to be a significant portion of the total contractual benefits;

– whose amount or timing is contractually at the discretion of the Company; and

– that are contractually based on investment returns on a specified pool of assets held by the Company.

Board policy and the terms and conditions of these contracts set out the bases for the determination of the amounts on which the additional discretionary benefits are based and within which the Company may exercise its discretion as to the amount and timing of their payment to contract holders. At least 90% of the eligible investment return must be attributed to contract holders as a group while the amount and timing of the distribution to individual contract holders is at the discretion of the Company, subject to the advice of the Approved Actuary.

Long-term insurance contracts with fixed and guaranteed term

These contracts insure events associated with human life (for example death or survival) over a long duration. Premiums are recognised as revenue when they become payable by the contract holder. Premiums are shown before deduction of commission, and are inclusive of policy fees receivable.

Death benefits are recorded as an expense when they are incurred.

3.1.2 Recognition and measurement of contracts

A liability for contract benefits that are expected to be incurred in the future is recorded when the premiums are recognised. The liability is determined by a discounted cash flow approach incorporating margins for adverse deviations in the assumptions. The liability is based on assumptions as to mortality, maintenance expenses and investment income.

The liabilities are recalculated by the Company at each reporting date using the assumptions established at the measurement date.

Creditor insurance contracts

For the creditor protection business (in run-off since December 2009), premiums are earned or deferred depending on the period of risk that the premiums relate to. Earned premiums are premiums whose risk relates to the accounting period and are recorded as revenue. Unearned premiums are premiums relating to periods of risk subsequent to the accounting period. Premiums are shown before commission.

Claims incurred comprise the settlement of claims paid, including handling costs, and outstanding claims arising from events occurring during the financial year together with adjustments to prior year claims provisions. All claims are recorded on the basis of notifications received up to the reporting date.

Long-term insurance contracts with DPF and unit-linked insurance contracts

These contracts insure human life events (for example death or survival) over a long duration. Premiums are accounted for on a receivable basis, except for premiums relating to linked contracts which are accounted for in the period in which the corresponding liability is established. In this case, insurance premiums are recognised in profit or loss and simultaneously within liabilities. These liabilities are increased by credited interest (in the case of savings with-profit) and change in unit prices (in the case of unit-linked contracts) and are decreased by policy administration fees, mortality and surrender charges and any withdrawals. These liabilities are the contract holders' account balances.

3 Significant accounting policies *(continued)*

3.1 Insurance and investment contracts (continued)

3.1.2 Recognition and measurement of contracts (continued)

Long-term insurance contracts with DPF and unit-linked insurance contracts (continued)

Savings with-profit contracts contain a DPF that entitles the holders to a credit of bonus declared by the Company from the DPF investment income (i.e. all interest and, realised and unrealised gains and losses arising from assets backing these contracts) accumulated to date. The Company has an obligation to eventually pay to contract holders up to 90% of the DPF eligible investment return. Any portion of this investment return that is not declared as a bonus and credited to the individual contract holders is reserved as a liability for the benefit of all contract holders until declared and credited to them individually in future periods. For contracts with DPF or unit-linked business a further non-unit liability is recorded in respect of any additional mortality and expense risks. This liability is calculated using the same method for contracts with fixed and guaranteed term.

Reinsurance

Contracts entered into by the Company with reinsurers under which the Company is compensated for losses on one or more contracts issued by the Company and that meet the classification requirements for insurance contracts as described above are classified as reinsurance contracts held.

The Company cedes reinsurance in the normal course of business for the purpose of limiting its net loss potential through the diversification of its risks. Reinsurance arrangements do not relieve the Company from its direct obligations to its policyholders. Reinsurance commission is recognised as it is received unless the amounts receivable can be reliably measured.

Outward reinsurance premiums are accounted for in profit or loss on an accruals basis. For reinsurance of the creditor protection business (in run-off since December 2009), reinsurance premiums are accounted for and earned in the same manner as the relative premiums, with the un-expensed portion of ceded reinsurance premiums included in reinsurers' share of technical provisions. Reinsurance assets for this run-off portfolio also include recoveries due from reinsurance companies in respect of claims incurred.

Premiums ceded and benefits reimbursed are presented in the primary statements on a gross basis other than for creditor protection business which is fully reinsured. The Company is only exposed to credit risk in this respect, and assets and liabilities are therefore not set off.

Only contracts that give rise to a significant transfer of insurance risk are accounted for as insurance. Amounts recoverable under such contracts are recognised in the same year as the related claim.

The benefits to which the Company is entitled under its reinsurance contracts held are recognised as reinsurance assets. These assets consist principally of longer term receivables (classified as reinsurance assets) that are dependent on expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

The Company assesses its reinsurance assets for impairment. If there is objective evidence that the reinsurance asset is impaired, the Company reduces the carrying amount of the reinsurance asset to its recoverable amount and recognises that impairment loss in the profit or loss. The Company gathers the objective evidence that a reinsurance asset is impaired using the same process adopted for financial assets held at amortised cost. The impairment loss is calculated following the same method used for these financial assets. These processes are described in note 3.10.

Liability adequacy test

Contract liabilities are tested for adequacy by discounting current estimates of all future contractual cash flows and comparing this amount to the carrying value of the liability. Where a shortfall is identified, an additional provision is made and the Company recognises the deficiency in profit or loss for the year.

3 Significant accounting policies *(continued)*

3.1 Insurance and investment contracts (continued)

3.1.2 Recognition and measurement of contracts (continued)

Investment contracts

Amounts collected on investment contracts are accounted for using deposit accounting, under which the amounts collected are credited directly to the Statement of Financial Position as an adjustment to the liability to the policyholder.

Investment contracts are financial liabilities whose fair value is dependent on the fair value of underlying financial assets, (also known as unit-linked investment contracts) and are designated at fair value through profit or loss from inception.

The best evidence of the fair value of these financial liabilities at initial recognition is the transaction price (that is, the fair value received).

The Company's main valuation techniques incorporate all factors that market participants would consider and make maximum use of observable market data. For the traditional unit-linked business, the fair value of financial liabilities for investment contracts is determined using the current unit values in which the contractual benefits are denominated. These unit values reflect the fair values of the financial assets contained within the Company's unitised investment funds linked to the financial liability. The fair value of the financial liabilities is obtained by multiplying the number of units attributed to each contract holder at the end of the reporting period by the unit value for the same date. For a portion of the 2014 acquired business the fair value of the financial liabilities for investment contracts is determined using the current net asset values of the policies' underlying assets.

When the investment contract has an embedded surrender option, the fair value of the financial liability is never less than the amount payable on surrender.

Some investment contracts issued include the provision of investment management services. These services are accounted for in accordance with IAS 18, Revenue, where the revenue associated with the service component is recognised by reference to the stage of completion of the transaction and deferred over the duration of the investment contract.

The incremental costs directly related to the acquisition of new investment contracts are capitalised and amortised over the period of the provision of the investment management services.

Receivables and payables related to insurance contracts and investment contracts

Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders. If there is objective evidence that the insurance receivable is impaired, the Company reduces the carrying amount of the insurance receivable accordingly and recognises that impairment loss in the income statement. The Company gathers the objective evidence that an insurance receivable is impaired using the process adopted for receivables. The impairment loss is calculated under the same method used for these financial assets. These processes are described in note 3.10.

3.2 Revenue

3.2.1 Insurance and investment contracts

The accounting policy in relation to revenue from insurance and investment contracts is disclosed in note 3.1.

3.2.2 Fees and commission income

Fees and commission income includes fees on investment management services contracts and are recognised in profit or loss as the services are provided. Certain upfront payments received for asset management services ('front-end fees') are deferred and amortised in proportion to the stage of completion of the service for which they were paid.

3 Significant accounting policies *(continued)*

3.2 Revenue (continued)

3.2.2 Fees and commission income (continued)

The Company charges its customers for investment management and other related services using the following different approaches:

- Front-end fees are charged to the client on inception. This approach is used particularly for single premium contracts. The consideration received is deferred as a liability and recognised over the life of the contract on a straight-line basis; and
- Regular fees are charged to the customer periodically (monthly, quarterly or annually) either directly or by making a deduction from invested funds.

Surrender charges and policy administration charges are recognised in profit or loss when the service is provided.

3.2.3 Investment income

Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date the Company's right to receive payment is established which, in the case of quoted securities is usually the ex-dividend date.

Rental income from investment property is recognised in profit or loss on a straight line basis over the term of the lease.

Policyholders' fund financial income and expenses are accounted for through the Technical Statement, while shareholders' fund financial income and expenses are accounted for through the non-Technical Statement of Profit or Loss and Other Comprehensive Income.

3.2.4 Net income from other financial instruments at fair value

Net income from other financial instruments at fair value relates to non-trading derivatives held for risk management purposes that do not form part of a qualifying hedge relationship and financial assets and liabilities designated at fair value through profit or loss. Net income includes all realised and unrealised fair value changes, interest, dividends and foreign exchange differences.

3.3 Employee benefits

3.3.1 Defined contribution plan

The Company contributes towards the State pension defined contribution plan in accordance with local legislation, and to which, it has no commitment beyond the payment of fixed contributions. Obligations for contributions are recognised as employee benefit expense in profit or loss in the periods during which services are rendered by employees.

3.3.2 Share based payment transactions

Share-based payment arrangements in which the Company receives goods or services as consideration for equity instruments in the ultimate parent Company are accounted for as equity-settled share-based payment transactions.

The grant date fair value of awards granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards.

The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting date.

3.4 Tax

Tax expense comprises current and deferred tax. Tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or in other comprehensive income. In this case, the tax is also recognised in other comprehensive income or directly in equity respectively.

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

3 Significant accounting policies *(continued)*

3.4 Tax (continued)

Deferred tax is recognised, using the liability method, in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

Deferred tax related to fair value re-measurement of available-for-sale investments, which are charged or credited directly in other comprehensive income, is also credited or charged directly to other comprehensive income and subsequently recognised in the profit or loss together with the deferred gain or loss.

3.5 Foreign currency transactions

Transactions in foreign currencies are translated to the Company's functional currency at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate ruling at that date. Foreign currency gains and losses arising on retranslation are recognised in profit or loss.

Translation differences on financial assets and liabilities held at fair value through profit or loss are reported as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale financial assets are included in 'Other comprehensive income'.

3.6 Property and equipment

3.6.1 Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset.

When parts of an item of property and equipment have different useful lives, they are accounted for as separate components of property and equipment.

The gain or loss on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment, and is recognised net within other income/other expense in profit or loss.

3.6.2 Subsequent costs

The cost of replacing a component of an item of property and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

3.6.3 Depreciation

Depreciation is based on the cost of an asset less its residual value. Significant components of individual assets are assessed and if a component has a useful life that is different from the remainder of that asset, that component is depreciated separately.

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each component of an item of property and equipment.

3 Significant accounting policies *(continued)*

3.6 Property and equipment (continued)

3.6.3 Depreciation (continued)

The estimated useful lives for the current and comparative periods are as follows:

– office furniture	10	years
– office equipment	4	years
– computer equipment	3	years
– telecommunication equipment	5	years

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

3.7 Investment properties

Property held for long-term rental yields and/or capital appreciation that is not occupied by the Company is classified as investment property.

Investment property comprises land and buildings and is measured at cost on initial recognition and subsequently at fair value with any changes therein recognised in profit or loss. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If the information is not available the Company uses alternative valuation methods such as discounted cash flow projections.

Valuations are prepared by considering the aggregate of the net annual rents receivable from the properties and associated costs where relevant, as well as open market valuations, where available. These valuations are reviewed annually by a valuation expert.

Changes in fair values are reported in the profit or loss account.

3.8 Intangible assets

3.8.1 Present value of in-force ('PVIF') long-term assurance business

A prudent valuation of future earnings expected to emerge from life assurance business currently in-force is determined annually by the directors. The value of in-force business is based on the advice of the Company's Approved Actuary. The valuation represents the discounted value of projected future transfers to shareholders from life assurance business currently in-force, after adjusting for the effective rate of taxation. In determining this valuation, assumptions relating to the future mortality, persistency and levels of expenses are based on experience of the type of business concerned. Gross investment returns assumed are based on the market risk free rates which the directors derive from the Euro Swap Curve.

Annual movements in the value of in-force business are recognised in the profit or loss.

3.8.2 Deferred acquisition costs

Incremental costs that are incurred in acquiring investment management contracts and creditor protection business are deferred and amortised as the related revenue is recognised. All deferred acquisition costs are reviewed regularly to determine if they are recoverable from future cash flows on the associated contracts.

Deferred acquisition costs that are not deemed to be recoverable are charged to profit or loss. The test for recoverability is performed at a portfolio level, on portfolios of relatively homogeneous contracts. Deferred acquisition costs are amortised in profit or loss on a straight line basis over the estimated useful life of the contract.

3.8.3 Computer software

Acquired computer software is capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These intangible assets are measured at cost less accumulated amortisation and any accumulated impairment losses.

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as incurred.

3 **Significant accounting policies** *(continued)*

3.8 Intangible assets (continued)

3.8.3 Computer software (continued)

Amortisation is based on the cost of the asset less its residual value.

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The estimated useful life for the current and comparative periods of computer software is three years.

Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

3.9 Financial instruments

3.9.1 Non-derivative financial instruments

Non-derivative financial instruments are recognised initially at fair value and adjusted for any directly attributable costs. Subsequent to initial recognition, financial instruments are measured as described below.

3.9.2 Cash and cash equivalents

Cash and cash equivalents comprise cash balances and deposits with contractual maturity of less than three months. Subsequent to initial recognition cash equivalents are measured at amortised cost.

3.9.3 Financial instruments at fair value through profit or loss

A financial asset is classified into this category at inception if acquired principally for the purpose of selling in the short term, if it forms part of a portfolio of financial assets in which there is evidence of short term profit-taking or if so designated by management. All investments of the Company which are classified as instruments at fair value through profit or loss are designated at inception.

3.9.3.1 Valuation of financial instruments

Regular purchases and sales of investments are recognised on trade date – the date on which the Company commits to purchase or sell the investment. All financial instruments are recognised initially at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is generally its transaction price (that is, the fair value of the consideration given or received). However, sometimes the fair value will be based on other observable current market transactions in the same instrument, without modification or repackaging, or on a valuation technique whose variables include only data from observable markets, such as interest rate yield curves, option volatilities and currency rates. When such evidence exists, the Company recognises a trading gain or loss on day 1, being the difference between the transaction price and the fair value. When significant unobservable parameters are used, the entire day 1 gain or loss is deferred and is recognised in profit or loss over the life of the transaction until the transaction matures, is closed out, the valuation inputs become observable, or when the Company enters into an offsetting transaction.

The fair value of financial instruments is generally measured on an individual basis. However, in cases where the Company manages a group of financial assets and liabilities according to its net market or credit risk exposure, the Company measures the fair value of the group of financial instruments on a net basis but presents the underlying financial assets and liabilities separately in the financial statements, unless they satisfy the IFRSs offsetting criteria.

The best evidence of fair value is a quoted price in an actively traded principal market. In the event that the market for a financial instrument is not active, and the valuation technique uses only observable market data, the reliability of the fair value measurement is high. However, when valuation techniques include one or more significant unobservable inputs, they rely to a greater extent on management judgement and the fair value derived becomes less reliable. In the absence of observable valuation inputs, due to lack of or a reduced volume of similar transactions, management judgement is required to assess the price at which an arm's length transaction would occur under normal business conditions, in which case management may rely on historical prices for that particular financial instrument or on recent prices for similar instruments.

3 Significant accounting policies *(continued)*

3.9 Financial instruments (continued)

3.9.3 Financial instruments at fair value through profit or loss (continued)

3.9.3.1 Valuation of financial instruments (continued)

The main assumptions and estimates which management consider when applying a model with valuation techniques are:

- the likelihood and expected timing of future cash flows on the instrument; judgement may be required to assess the counterparty's ability to service the instrument in accordance with its contractual terms. Future cash flows may be sensitive to changes in market rates;
- judgement to determine what model to use to calculate fair value in areas where the choice of valuation model is particularly subjective, for example, when valuing complex derivative products.

When applying a model with unobservable inputs, estimates are made to reflect uncertainties in fair values resulting from a lack of market data inputs, for example, as a result of illiquidity in the market. For these instruments, the fair value measurement is less reliable. Inputs into valuations based on unobservable data are inherently uncertain because there is little or no current market data available from which to determine the level at which an arm's length transaction would occur under normal business conditions. However, in most cases there is some market data available on which to base a determination of fair value, for example historical data, and the fair values of most financial instruments are based on some market observable inputs even when unobservable inputs are significant.

3.9.3.2 Control framework

Fair values are subject to a control framework designed to ensure that they are either determined, or validated, by a function independent of the risk-taker.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Company will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors that are considered in this regard are, inter alia:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the reporting date; and
- the manner in which the data was sourced.

For fair values determined using a valuation model, the control framework may include, as applicable, development or validation by independent support functions of (i) the logic within valuation models; (ii) the inputs to those models; (iii) any adjustments required outside the valuation models; and, where possible, (iv) model outputs. Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an ongoing basis.

3.9.3.3 Determination of fair value

Fair values are determined according to the following hierarchy:

- Level 1 – quoted market price: financial instruments with quoted prices for identical instruments in active markets.
- Level 2 – valuation technique using observable inputs: financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

3 Significant accounting policies *(continued)*

3.9 Financial instruments (continued)

3.9.3 Financial instruments at fair value through profit or loss (continued)

3.9.3.3 Determination of fair value (continued)

- Level 3 – valuation technique with significant unobservable inputs: financial instruments valued using models where one or more significant inputs are unobservable.

The best evidence of fair value is a quoted price in an actively traded market. The fair values of financial instruments that are quoted in active markets are based on bid prices for assets held and offer prices for liabilities issued. Where a financial instrument has a quoted price in an active market, the fair value of the total holding of the financial instrument is calculated as the product of the number of units and quoted price. In the event that the market for a financial instrument is not active, a valuation technique is used.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process. Transfers between levels of the fair value hierarchy are deemed to have occurred at the end of the reporting period.

3.9.3.4 Valuation techniques

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them the derivation of fair value is more judgemental. An instrument in its entirety is classified as valued using significant unobservable inputs if, in the opinion of management, a significant proportion of the instrument's inception profit ('day 1 gain or loss') or greater than 5% of the instrument's carrying value is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used). All fair value adjustments are included within the levelling determination.

Changes in fair value are generally subject to a profit and loss analysis process. This process disaggregates changes in fair value into two high level categories; (i) portfolio changes, such as new transactions or maturing transactions, (ii) market movements, such as changes in foreign exchange rates or equity prices.

3.9.3.5 Basis of valuing assets and liabilities measured at fair value

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Company will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable.

The fair value of investments in other funds that are not quoted in an active market is determined primarily by reference to the latest available redemption price of such units of each investment fund, as determined by the administrator of such fund. The Company may make adjustments to the reporting net asset value of various investment funds based on considerations such as:

- Liquidity of the investment fund or its underlying funds
- The value date of the net asset value provided;
- Any restrictions on redemptions; and
- The basis of accounting and, in instances where the basis of accounting is other than fair value, fair valuation information provided by the investee fund's advisors.

3 Significant accounting policies *(continued)*

3.9 Financial instruments (continued)

3.9.4. Available-for-sale

Available-for-sale (AFS) securities are initially measured at fair value plus direct and incremental transaction costs. They are subsequently re-measured at fair value, and changes therein are recognised in other comprehensive income and presented in the fair value reserve in equity, until the securities are sold or impaired. When available-for-sale securities are sold, cumulative gains or losses previously recognised in equity are recognised in profit or loss.

3.9.5 Other

Other financial instruments are subsequently measured at amortised cost using the effective interest method. Loans and receivables mainly comprise cash and cash equivalents and receivables.

3.9.6 Derivative financial instruments

Derivatives are initially recognised and subsequently measured at fair value. Fair values are obtained from quoted market prices in active markets, or by using valuation techniques, including recent market transactions, where an active market does not exist. Valuation techniques include discounted cash flow models and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. Notes 17 and 18 contain further information in this respect.

3.9.7 Derecognition of financial assets and liabilities

Financial assets are derecognised when the right to receive cash flows from the assets has expired or when the Company has transferred its contractual right to receive the cash flows of the financial assets, and either:

- substantially all the risks and rewards of ownership have been transferred; or
- substantially all the risks and rewards have neither been retained nor transferred but control is not retained.

The Company derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

3.9.8 Offsetting of financial assets and liabilities

Financial assets and liabilities are offset and the net amount presented in the Statement of Financial Position when, and only when, the Company has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

3.10 Impairment

3.10.1 Non-derivative financial assets

A financial asset not carried at fair value through profit or loss is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor and restructuring of an amount due to the Company on terms that the Company would not consider otherwise and indications that a debtor or issuer will enter bankruptcy.

The Company considers evidence of impairment for receivables at a specific asset level. All individually significant receivables are assessed for specific impairment.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between the carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognised. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

3 Significant accounting policies *(continued)*

3.10 Impairment (continued)

3.10.1 Non-derivative financial assets (continued)

Impairment losses on available-for-sale financial assets are recognised by reclassifying the losses accumulated in the fair value reserve in equity, to profit or loss. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss recognised previously in profit or loss. Changes in impairment provisions attributable to the application of the effective interest method are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognised in profit or loss, then the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

3.10.2 Non-financial assets

The carrying amounts of the Company's non-financial assets, other than deferred tax assets and investment property, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3.11 Provision for liabilities and charges

A provision for contingent liabilities and charges is recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation that has arisen as a result of past events and for which a reliable estimate can be made.

3.12 Assets and liabilities forming part of a disposal group

Assets and liabilities forming part of a disposal group are classified as held for sale when their carrying amounts will be recovered principally through sale rather than through continuing use. Held for sale assets are generally measured at the lower of their carrying amount and fair value less cost to sell, except for those assets and liabilities that are not within the scope of the measurement requirements of IFRS 5 'Non-current Assets held for sale and Discontinued Operations', such as those measured in accordance with IAS39.

Immediately before the initial classification as assets held for sale, the carrying amounts of the relevant assets and liabilities are measured in accordance with applicable IFRSs. On subsequent remeasurement of a disposal group, the carrying amounts of any assets and liabilities that are not within the scope of the measurement requirements of IFRS 5, but are included in a disposal group classified as held for sale, are remeasured under applicable IFRSs before the fair value less costs to sell of the disposal group is determined.

3.13 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

3.14 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit or loss over the period of the borrowings using the effective interest method.

3.15 Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Company's financial statements in the period in which the dividends are approved by the Company's shareholders.

4 Critical accounting estimates and judgements

The Company makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are frequently re-evaluated and based on product assessment of historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 *Policyholder claims and benefits*

The estimation of future benefit payments and premiums arising from long-term insurance contracts is the Company's most critical accounting estimate. The determination of the liabilities under long-term insurance contracts is dependent on estimates made by the Company. Estimates are made as to the expected number of deaths for each of the years in which the Company is exposed to risk. The Company bases these estimates on industry standard mortality tables that reflect recent historical mortality experience, adjusted where appropriate to reflect the Company's own experience. The estimated number of deaths determines the value of future benefit payments. The main source of uncertainty is that epidemics such as AIDS, SARS, pandemic flu, swine flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the Company has significant exposure to mortality risk. New estimates are made each subsequent year to reflect the current long term outlook.

Estimates are also made as to future investment income arising from the assets backing long-term insurance. These estimates are based on current market returns as well as expectations about future economic and financial developments. Interest rate assumptions for the purposes of valuing liabilities at reporting date are based on the Euro swap rates curve.

Appropriate margins were taken for bond portfolio and equities/property portfolio.

If the average future investment returns differ by +/-1% from management's estimates, the insurance liability would decrease by €16,670,000 (2016: €19,316,000) or increase by €21,838,000 (2016: €26,198,000). In this case there is no relief arising from reinsurance contracts held.

If the number of deaths in future years differ by +/-10% from management's estimate, the liability would increase by €1,153,000 (2016: €1,148,000) or decrease by €1,248,000 (2016: €1,193,000). These impacts are calculated before considering changes to other assets and liabilities which may offset the gross impacts of these changes.

Further information is disclosed within notes 5.1 and 19.

4.2 *Present value of in-force long-term assurance business (PVIF)*

The PVIF measures the shareholder's share of the future profits that are expected to be earned in future years attributable to the long-term life insurance business in force at the valuation date. Policies classified as investment contracts are excluded. The approach is to take a present value of the expected future shareholder cash flows, discounted using the risk discount rate.

The risk free rate of return used within the valuation is the Euro swap rate curve as at the 29th December 2017 (2016: same approach). The risk discount rate is based on the risk free curve with an additional 0.5% margin (2016: 0.5% margin) to allow for operational risk. The PVIF valuation assumes lapse rates varying by product and duration in-force that range from 0% to 18.7% p.a. (2016: from 0% to 18.7% p.a.). Expense inflation is calculated as a blend of wage inflation and price inflation, with the latter based on an adjusted French inflation curve. This results in a term dependent expense inflation assumption increasing from 2.0% p.a. to 2.7% p.a. (2016: 2.0% p.a. to 2.9% p.a.).

4 Critical accounting estimates and judgements *(continued)*

4.2 Present value of in-force long-term assurance business (PVIF) (continued)

As the valuation models are based upon assumptions, changing the assumptions will change the resultant estimate of PVIF. The following table shows the effect on the PVIF of reasonably possible changes in the main assumptions across the insurance business:

		PVIF Impact	
		2017	2016
Assumptions	**Movement**	**€000**	€000
Risk free rate	+100 basis points	**(1,440)**	(2,837)
Risk free rate	-100 basis points	**3,845**	7,497
Expenses inflation	+10%	**(1,168)**	(964)
Expenses inflation	-10%	**1,231**	1,043
Lapse rate	+100 basis points	**1,490**	1,291
Lapse rate	-100 basis points	**(2,259)**	(1,994)

Assumptions are reviewed annually by the Company's Board of Directors.

5 Management of insurance and financial risk

The Company issues contracts that transfer insurance risk or financial risk or both. This section summarises these risks and the way the Company manages these contracts.

5.1 Insurance risk

The risk under any insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, this risk is random and therefore unpredictable.

For a portfolio of insurance contracts where the theory of probability is applied to pricing and provisioning, the principal risk that the Company faces under its insurance contracts is that the actual claims and benefit payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or severity of claims and benefits are greater than estimated. Insurance events are random and the actual number and amount of claims and benefits will vary from year to year and from the estimate established using statistical techniques.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. The Company uses reinsurance appropriately to reduce variability of the expected outcome. Factors that aggravate insurance risk include lack of risk diversification in terms of type and amount of risk and geographical location. For contracts with DPF, the participating nature of these contracts result in a significant portion of the insurance risk being shared with the insured party.

Frequency and severity of claims

For contracts where death is the insured risk, the most significant factor that could increase the overall frequency of claims are epidemics or wide spread changes in lifestyle resulting in earlier or more claims than expected.

At present these risks do not vary significantly in relation to the location of the risk insured by the Company. However, undue concentration by amounts could have an impact on the severity of benefit payments on a portfolio basis.

For contracts with fixed and guaranteed benefits and fixed future premiums, there are no mitigating terms and conditions that reduce the insurance risk accepted. For contracts with DPF, the participating nature of the contracts results in a portion of the insurance risk being reduced over the term of the policy. Investment contracts with DPF carry negligible insurance risk.

The Company manages its insurance risk through strict underwriting limits and claims management; approval procedures for new products and pricing reviews; close monitoring of reinsurance arrangements and monitoring of emerging issues.

5 Management of insurance and financial risk *(continued)*

5.1 *Insurance risk (continued)*

The Company's underwriting strategy is intended to ensure that the risks underwritten are well diversified in terms of type of risk and the level of insured benefits. For example, the Company balances death risk across its portfolio. Medical selection is also included in the Company's underwriting procedures, with premium varied to reflect the health condition and family medical history of the applicants.

Sources of uncertainty in the estimation of future benefit payments and premium receipts

Uncertainty in the estimation of future benefit payments and premium receipts for long term insurance contracts arises from the unpredictability of long term changes in overall levels of mortality, and the variability in contract holder behaviour. The Company uses appropriate base tables of standard mortality according to the type of contract being written. The Company does not take credit for future lapses in determining the liability of long term contracts. Further details on the process for estimation and other key assumptions, is provided in note 19.2 to these financial statements.

The following table provides an analysis of the insurance risk exposures by type of business on gross reinsurance basis:

	2017	2016
	€000	€000
Life insurance (non-linked)		
Insurance contracts with discretionary participation feature	**318,296**	324,996
Term assurance and other long-term contracts	**117,239**	114,976
Total non-linked	**435,535**	439,972
Life insurance (linked)	**223,257**	205,589
Liabilities under insurance contracts	**658,792**	645,561

5.2 *Financial risk*

The Company is exposed to financial risk through its financial assets, financial liabilities (investment contracts), reinsurance assets and insurance liabilities. In particular, the key financial risk is that the proceeds from its financial assets are not sufficient to fund the obligations arising from its insurance and investment contracts. The most important components of this financial risk are market risk, credit risk and liquidity risk.

For unit-linked insurance and investment contracts, the Company matches all the liabilities on which the unit prices are based with assets in the unit-linked portfolios. There is therefore no direct equity price, currency, credit or interest risk exposure for these contracts which is borne by the Company.

5.2.1 *General nature of participation feature*

The Company offers savings with-profit policies which participate in the investment returns of the with-profit funds. Up to 90% of the eligible investment return is attributed to the contract holders. Policyholders receive regular (reversionary) bonus. A regular bonus rate is declared yearly in advance. This rate may be reviewed upwards during the course of the year based on the performance of the fund. This provides a progressive build-up of guaranteed benefits over the lifetime of the policy. Regular bonuses are set by the Board of Directors on the recommendation of the Approved Actuary. The Company is exposed to adverse market conditions which could lead to the value of assets backing the liabilities to fall below the guaranteed benefit at policy maturity, which could lead to a potential loss to the shareholders.

5.2.2 *Market risk*

Market risk can be described as the risk of change in cash flows or fair value of a financial instrument due to changes in interest rates, exchange rates or equity prices.

Interest rate risk

The Company's exposure to interest rate changes is concentrated in its non-linked investment portfolio. Changes in investment values attributable to interest rate changes are mitigated by partially offsetting changes in the economic value of insurance provisions. The Company monitors this exposure through periodic reviews of its asset and liability positions. Estimates of future cash flows, as well as the impact of interest rate fluctuations on its investment portfolio and insurance liabilities, are modelled and reviewed quarterly. The Company minimises interest rate risks primarily by matching estimated future cash outflows to be paid to policyholders by expected cash flows from assets. The pool of investments backing liabilities is managed to duration targets that aim to make the net effect of interest rate changes on assets and liabilities manageable.

5 Management of insurance and financial risk *(continued)*

5.2 Financial risk (continued)

5.2.2 Market risk (continued)

Exchange risk

The Company is exposed to currency risk on the shareholder's investment portfolio and to 10% of the investments backing contracts with DPF. The net exposure for the Company amounts to €4,761,000 (2016: €4,272,000) and a sensitivity analysis is not deemed necessary on the basis of significance.

Equity price risk

The Company manages the equity risk arising from its holdings of equity securities by setting limits on the maximum market value of equities that it holds. Equity risk is also monitored by estimating the effect of predetermined movements in equity prices on the profit and total net assets of the insurance underwriting business.

Sensitivity analysis

The Company performs various sensitivity analyses as summarised below. An immediate and permanent movement in interest yield curves or equity prices at the reporting date would have the following impact on the profit for the year and net assets at that date:

	Impact on profits and net assets for the year	
	2017	2016
	€000	€000
+100 basis points shift in yield curves	**195**	(248)
-100 basis points shift in yield curves	**(1,030)**	(79)
+10 per cent increase in equity prices	**902**	756
-10 per cent decrease in equity prices	**(1,081)**	(782)

The impact of the above sensitivity analysis on other comprehensive income is negligible in light of the amount of available-for-sale investments held.

5.2.3 Credit risk

The Company has exposure to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. The main 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;

– investment portfolios of debt securities;

– insurance and other receivables; and

– call and term deposits.

Investments in bonds are made within the credit limits permitted within the investment credit risk mandate conferred by HSBC Group.

The Company structures the levels of credit risk it accepts by placing limits on its exposure to investment grade single counterparty, or groups of counterparties, and to geographical and industry segments. Investment credit exposures positions are reviewed on a quarterly basis by the Company's Asset Liability Committee.

The selection of reinsurers also includes restrictions designed to minimise the risk of credit exposure.

The Company currently manages the majority of reinsurance risk by using reinsurers with a minimum rating of AA-. The creditworthiness of reinsurers is confirmed from public rating information and considered on an annual basis by reviewing their financial strength prior to finalisation of any contract.

Cash and cash equivalents held with third party banks amount to €42,975,000 (2016: €69,851,000) out of which €39,185,000 are classified as Assets held for sale and the counterparties are rated A- and above. The remaining cash at bank comprises amounts held with the immediate parent Company, HSBC Bank Malta p.l.c, and other related parties.

5 Management of insurance and financial risk *(continued)*

5.2 Financial risk (continued)

5.2.3 Credit risk (continued)

Insurance and other receivables amount to €4,803,000 (2016: €5,170,000). This balance includes accrued interest amounting to €3,947,000 (2016: €4,641,000) which would follow a similar rating profile to debt securities below.

The following table presents the analysis of debt securities by rating agency (Standard and Poor's Rating Agency):

Financial Investments

	Debt securities – Unit linked		*Debt securities – Others*		*Total*	
	2017	2016	**2017**	2016	**2017**	2016
	€000	€000	**€000**	€000	**€000**	€000
AAA	**–**	11,651	**10,418**	16,479	**10,418**	28,130
AA+ to AA-	**–**	7,655	**58,456**	78,819	**58,456**	86,474
A+ to A-	**–**	57,918	**135,808**	138,353	**135,808**	196,271
BBB+ to BBB-	**402**	61,163	**42,674**	42,178	**43,076**	103,341
BB+ to B-	**1,190**	149,026	**1,721**	1,642	**2,911**	150,668
Lower than B-	**158**	19,001	**–**	–	**158**	19,001
Unrated	**790**	49,024	**12,215**	10,900	**13,005**	59,924
Total	**2,540**	355,438	**261,292**	288,371	**263,832**	643,809

Assets held for sale

	Debt securities – Unit linked	
	2017	2016
	€000	€000
AAA	**9,382**	–
AA+ to AA-	**5,646**	–
A+ to A-	**24,954**	–
BBB+ to BBB-	**44,599**	–
BB+ to B-	**164,295**	–
Lower than B-	**6,687**	–
Unrated	**25,265**	–
Total	**280,828**	–

The Company is not exposed to credit risk in respect of unit-linked business, although the relevant credit information is disclosed.

5.2.4 Liquidity risk

It is an inherent characteristic of almost all insurance contracts that there is uncertainty over the amount and the timing of settlement of claims liabilities that may arise, and this leads to liquidity risk. As part of the management of this exposure, estimates are prepared for most lines of insurance business of cash flows expected to arise from insurance funds at the reporting date.

The Company actively manages its assets in such a manner as to achieve a competitive rate of return within the prevailing risk objectives delineated by asset liquidity and credit quality, and asset-liability matching. The Company's Asset Liability Committee reviews and approves investment strategies on a periodic basis, ensuring that assets are managed efficiently within approved risk mandates.

The assets pertaining to a disposal group have been analysed by contractual maturity in line with the requirements of IFRS 7 but classified as current in the statement of financial position (note 18) in line with the requirements of IFRS 5.

The following table shows the cash flows expected to arise pertaining to insurance and investment liabilities as well as the contractual maturity of financial assets as at reporting date.

5 Management of insurance and financial risk *(continued)*

5.2 Financial risk (continued)

5.2.4 Liquidity risk (continued)

	No fixed maturity	*Due within 3 months*	*Due between 3 and 12 months*	*Due between 1 year and 5 years*	*Due after 5 years*	*Total*
	€000	€000	€000	€000	€000	€000
At 31 December 2017						
Financial investments	466,829	1,011	9,929	90,826	160,850	729,445
Reinsurance assets	85,887	–	–	–	–	85,887
Cash	94,751	–	–	–	–	94,751
Asset held for sale:						
– Financial investments	153,783	7,044	10,751	47,285	215,749	434,612
– Cash	39,185	–	–	–	–	39,185
	840,435	8,055	20,680	138,111	376,599	1,383,880

	On demand	*Due within 3 months*	*Due between 3 and 12 months*	*Due between 1 year and 5 years*	*Due after 5 years*	*Gross nominal outflow*
	€000	€000	€000	€000	€000	€000
At 31 December 2017						
Liabilities to customers:						
– insurance contracts	–	23,463	53,055	213,819	413,973	704,310
– investment contracts	167,697	237	653	7,027	33,113	208,727
Liabilities held for sale:						
– investment contracts	473,797	–	–	–	–	473,797
	641,494	23,700	53,708	220,846	447,086	1,386,834

5 Management of insurance and financial risk *(continued)*

5.2 Financial risk (continued)

5.2.4 Liquidity risk (continued)

	No fixed maturity	*Due within 3 months*	*Due between 3 and 12 months*	*Due between 1 year and 5 years*	*Due after 5 years*	*Total*
	€000	€000	€000	€000	€000	€000
At 31 December 2016						
Financial investments	750,607	13,715	47,055	177,593	405,446	1,394,416
Reinsurance assets	85,228	–	–	–	–	85,228
Cash	141,175	–	–	–	–	141,175
	977,010	13,715	47,055	177,593	405,446	1,620,819

	On demand	*Due within 3 months*	*Due between 3 and 12 months*	*Due between 1 year and 5 years*	*Due after 5 years*	*Gross nominal outflow*
	€000	€000	€000	€000	€000	€000
Liabilities to customers:						
– insurance contracts	–	20,376	60,717	231,483	377,204	689,780
– investment contracts	898,760	230	521	6,113	29,746	935,370
	898,760	20,606	61,238	237,596	406,950	1,625,150

The methodology used for estimating cash outflows on liabilities to customers can be found below:

- Linked insurance reserves: derived via undiscounted cash flows. No future premiums are assumed and investment returns are not included in the provisions. All decrements are considered.
- Non-linked reserve: derived via undiscounted reserves run-off on a reporting basis. All future premiums are considered and provisions based on all expected decrements. The timing of cash flows is based on the expected run-off of the reserves.
- Linked investment reserves: derived via undiscounted cash flows but only considering contractual maturities and no other form of decrement. When there is no contractual maturity, the reserve is placed within the 'on demand' bucket.

5.2.5 Capital management and allocation

It is the Company's policy to maintain a strong capital base to support the development of its business and to meet regulatory capital requirements imposed by the MFSA at all times. The Company recognises the impact on shareholder returns of the level of its equity capital employed and seeks to maintain a prudent balance between the advantages and flexibility afforded by a strong capital position and the higher returns on equity possible with greater leverage.

The annual budget and planning process takes into account projected capital demands with the objective of ensuring regulatory solvency and maintaining capital adequacy at all times. The Company regularly monitors its capital requirements and applies limits to asset balances with respect to asset types and counterparty exposures.

The Company defines its capital as the excess of assets over liabilities as valued in accordance with the respective regulatory requirements. In order to maintain or adjust the capital structure, the Company may issue new shares or capitalise contributions received from its shareholders.

5 Management of insurance and financial risk *(continued)*

5.2 Financial risk (continued)

5.2.5 Capital management and allocation (continued)

As from 1 January 2016, the Company was subject to the requirements of the EU Solvency II directive. The Solvency II regime establishes a new set of EU-wide capital requirements, risk management and disclosure standards. The Company must hold eligible own funds to cover the Solvency Capital Requirement (SCR) and eligible basic own funds to cover the Minimum Capital Requirement (MCR). The SCR shall be calculated either in accordance with the standard formula or using a full or partial internal model (PIM) as approved by the Regulator. The Company must immediately inform the Regulator where it observes that its SCR or MCR are no longer complied with or where there is risk of non-compliance in the following six months for SCR and three months for MCR.

The Company opted for the standard formula under the Solvency II regime to calculate the SCR as the assumptions underlying the standard formula are considered to be a good fit for the Company's risk profile. At 31 December 2017, the Company's eligible own funds adequately covered the required SCR, and amounted to €71,643,000 (2016: €65,475,000) (unaudited).

6 Premiums

Insurance premiums written by the Company are mainly premiums from direct business received from contracts written in Malta. Insurance premiums are analysed below:

	2017	2016
	€000	€000
Gross premiums written in Malta		
Individual business	**75,177**	55,707
Group/block business	**1,807**	2,214
	76,984	57,921
Premium:		
Single	**19,933**	–
Periodic	**57,051**	57,921
	76,984	57,921
Insurance contracts:		
Non-participating	**14,010**	14,152
Insurance contracts with DPF	**40,457**	21,521
Premiums for which investment risk is borne by policyholders	**22,517**	22,248
	76,984	57,921

Outward reinsurance premiums relate to non-participating insurance contracts, and are net of commission received of €1,500,000 in relation to lives reinsured on contracts written up to 2014.

7 Investment contracts fee income

	2017	2016
	€000	€000
Fixed fees	**166**	203
Change in deferred income	**189**	245
Annual management charges on transferred portfolio	**2,020**	2,127
	2,375	2,575

8 Investment income – net

	2017	2016
	€000	€000
Technical Statement		
Income on available-for-sale assets	85	107
Interest on cash and cash equivalents	–	39
Net gains from financial assets held at FVTPL	2,137	13,059
Rental income from investment properties	–	92
Net gains from policyholders' unit-linked investments held at FVTPL	26,359	95,499
	28,581	108,796
Non-technical Statement		
Interest on loans with group companies	–	(130)
Net gains from financial assets	332	2,009
	332	1,879

9 Investment contract benefits

These comprise single and regular premium individual life non-participating unit-linked business where the investment risk is borne by the policyholder and the insurance risk is not significant. The benefits from unit-linked investment contracts accrue to the account of the contract holder at the fair value of the gains/(losses) arising from the underlying linked assets and are credited/(debited) to financial liabilities – investment contracts at fair value through profit or loss. These contracts are all designated as at fair value through profit or loss and were designated in this category upon initial recognition.

10 Acquisition costs

Acquisition costs include commissions and deferred acquisition costs as follows:

	2017	2016
	€000	€000
Commissions payable	765	676
Change in deferred acquisition costs – Investment contracts	198	254
Allocated administrative expenses	949	903
	1,912	1,833

11 Administrative expenses

11.1 Administrative expenses include auditors' remuneration pertaining to the annual statutory audit amounting to €70,775 exclusive of VAT.

Other fees, exclusive of VAT, charged by the appointed independent auditors, comprise:

	2017	2016
	€000	€000
Tax compliance services	–	2
Other assurance services	42	–
	42	2

11 Administrative expenses *(continued)*

11.2 Profit before tax is stated after charging:

	2017	2016
	€000	€000
Depreciation	**74**	59
Investment management and administrator fees	**2,105**	2,091
Actuarial services	**754**	504
Computer software licence fees	**641**	764
Provisions for future losses on onerous contract (note 23)	**689**	–

11.3 Administrative expenses included in the Technical Statement of Profit or Loss and Other Comprehensive Income include commissions payable amounting to €749,000 (2016: €774,000).

12 Personnel expenses

12.1 Personnel expenses incurred by the Company during the year are analysed as follows:

	2017	2016
	€000	€000
Wages, salaries and allowances	**2,009**	2,054
Redundancy costs	**89**	53
Compulsory social security costs	**119**	115
	2,217	2,222

All employees are seconded from the immediate parent company and other related parties.

Included in salaries is an amount of €273,500 (2016: €341,175) payable to the directors.

12.2 The weekly average number of persons employed by the Company during the year is analysed as follows:

	2017	2016
	No.	No.
Operating	**32**	30
Management and administration	**21**	21
	53	51

12.3 Share-based payments

In order to align the interests of employees with those of shareholders, share options in ordinary shares of HSBC Holdings p.l.c. (the "ultimate parent Company") are offered to HSBC Group (the "Group") employees under all-employee share plans and achievement shares awarded to the Group senior management, under discretionary incentives plans. The Company offered two types of share option schemes to its employees.

Under the HSBC Holdings savings-related share option plans, options are offered at nil consideration at an exercise price discounted at a rate of 20 per cent of the market value immediately preceding the date of invitation. The options are exercisable either on the first, third or fifth anniversary of the commencement of the relevant savings contract.

Options awarded up to May 2005 under the HSBC Holdings Group Share Option Plan were offered for nil consideration and granted at market value and were normally exercisable between the third and tenth anniversaries of the date of grant, subject to vesting conditions.

Shares in HSBC Holdings plc awarded under the discretionary HSBC Holdings Group Achievement Share Scheme are offered at nil consideration. Shares are released to individuals after three years provided they remain employed by the Group. There is no performance condition attached to these awards. For those receiving share awards, additional awards will be made during the three year life of the award, representing equivalent value to dividends reinvested in shares. At the end of the three year period, the value of the award will have grown in line with HSBC's total shareholder return over the same period.

13 Tax expense

13.1 Recognised in profit or loss

	2017	2016
	€000	€000
Current tax expense		
Current year	**(11,059)**	(1,111)
Deferred tax expense		
Origination and reversal of temporary differences	**8,550**	(1,487)
	(2,509)	(2,598)

13.2 Reconciliation of tax expense

	2017	2016
	€000	€000
Profit before tax	**7,331**	7,339
Income tax using the Company’s domestic tax rate of 35%	**(2,566)**	(2,569)
Tax effect of:		
– tax exempt dividends	**2**	7
– non-deductible expenses	**(3)**	(102)
– profits taxed at different rates	**–**	19
– property sales tax consequences	**58**	47
Total income tax expense in profit or loss	**(2,509)**	(2,598)

13.3 During 2017, the Commissioner of Inland Revenue authorised the Company not to adjust for any fair value movements through profit and loss in computing taxable income as from financial year 2017. Any such movements will be adjusted to tax and claimed as a deduction in the year in which such movements are accounted for. Also, the Commissioner of Inland Revenue authorised that the balance of €7,779,968 representing the deferred tax on fair value movement of investments through the profit and loss as at 31 December 2016, be transferred to current tax. The balance, net of the amounts of tax recoverable, was settled during 2017.

14 Property and equipment

	Office furniture and equipment	*Computer equipment*	*Total*
	€000	**€000**	**€000**
Cost			
Balance at 1 January 2016	103	143	246
Acquired from amalgamation of subsidiary company	16	3	19
Balance at 31 December 2016	119	146	265
Balance at 1 January 2017	119	146	265
Balance at 31 December 2017	**119**	**146**	**265**
Depreciation			
Balance at 1 January 2016	101	139	240
Depreciation on assets acquired from amalgamation of subsidiary company	16	2	18
Depreciation charge for the year	1	3	4
Balance at 31 December 2016	118	144	262
Balance at 1 January 2017	118	144	262
Depreciation charge for the year	1	1	2
Balance at 31 December 2017	**119**	**145**	**264**
Carrying amounts			
At 1 January 2016	2	4	6
At 31 December 2016	1	2	3
At 1 January 2017	1	2	3
At 31 December 2017	**–**	**1**	**1**

15 Investment properties

15.1

	2017	2016
	€000	€000
Balance at 1 January	**2,846**	4,583
Additions	**27**	14
Disposals	**–**	(1,945)
Fair value adjustments	**227**	194
Balance at 31 December	**3,100**	2,846
Cost of acquisition	**2,488**	2,461

15 Investment properties *(continued)*

15.2 Investment property is carried at fair value. In estimating fair value, the directors consider valuations determined by professional valuers who applied recognised valuation techniques, together with open market valuations provided by real estate agents, where this information is available.

The Company has in place set benchmarks to ensure that professional valuers hold the necessary recognised and relevant professional qualifications as well as the knowledge and experience depending on the location and category of the investment property being valued.

The valuations provided by the architect are based on expected future rental earnings discounted using market rates existing at the reporting date. The main unobservable inputs used by the architect in valuing the investment property include the capitalisation rate which amounted to 5% (2016: 5.5%) and the future rental cash flows. These valuations are considered to be level 3 in the fair value hierarchy.

The values of the properties has been capped at the value indicated by a local real estate agent and the value stipulated in a promise for sale. These values do not exceed that provided by the architect.

15.3 At 31 December 2017, investment property comprises of two (2016: two) commercial properties. For all properties, their current use equates to the highest and best use. The properties are currently held for capital appreciation.

No rental income was generated from investment properties during the year (2016: €91,574) (note 8).

16 Intangible assets

	PVIF	*Deferred acquisition costs*	*Computer software*	*Total*
	€000	**€000**	**€000**	**€000**
Carrying amount				
Balance at 1 January 2016	61,859	4,082	185	66,126
Additions	–	–	145	145
Movements/amortisation through profit or loss:				
– Addition from new business	5,898	48	–	5,946
– Movement in in-force business	(7,586)	–	–	(7,586)
– Amortisation	–	(2,122)	(55)	(2,177)
– Impairment	–	–	(104)	(104)
Balance at 31 December 2016	60,171	2,008	171	62,350
Balance at 1 January 2017	60,171	2,008	171	62,350
Additions	–	–	116	116
Movements/amortisation through profit or loss:				
– Addition from new business	4,458	108	–	4,566
– Movement in in-force business	(6,132)	–	–	(6,132)
– Amortisation	–	(1,341)	(71)	(1,412)
Balance at 31 December 2017	**58,497**	**775**	**216**	**59,488**
Accumulated amortisation				
Balance at 1 January 2016	–	–	1,103	1,103
Balance at 31 December 2016	–	–	1,158	1,158
Balance at 1 January 2017	–	–	1,158	1,158
Balance at 31 December 2017	**–**	**–**	**1,229**	**1,229**

The effect of the theoretical changes in the main economic assumptions on PVIF at the reporting date is analysed in note 4.2.

17 Financial investments

17.1 All assets within this note are carried at fair value through profit or loss (designated at initial recognition) except where otherwise stated.

Financial investments include:

	2017	2016
	€000	€000
Equity securities – listed	**14,887**	18,949
Debt securities – fixed interest (Available-for-sale)	**1,213**	4,648
Debt securities – fixed interest:		
– Government bonds – listed	**179,698**	192,566
– other listed	**80,381**	91,157
	260,079	283,723
Collective investment schemes:		
– listed	**23,728**	17,551
– unlisted	**19,000**	16,654
	42,728	34,205
Unit-linked net financial investments:		
Equities – listed	**26,601**	76,841
Debt securities – Government bonds:		
– listed	**–**	35,213
Debt securities – Others:		
– listed	**2,504**	278,315
– unlisted	**36**	41,910
Collective investment schemes:		
– listed	**3,815**	70,451
– unlisted	**377,343**	564,804
Policyholders' loans	**–**	(20,050)
Net derivative financial (liabilities)	**–**	(765)
Accrued interest	**239**	6,172
	410,538	1,052,891
Total	**729,445**	1,394,416

Given that policy holders' loans and derivatives pertain to individual policies which are at all times in a net asset position (i.e. a positive policy account balance), these balances are netted off against assets within these financial statements. Derivatives pertain solely to policies on which the Company does not hold investment discretion.

	2017	2016
	€000	€000
Current	**12,154**	53,946
Non-current	**717,291**	1,340,470
	729,445	1,394,416

Investments with a fixed maturity date (i.e. debt securities) are classified as non-current unless they are expected to mature within twelve months or be realised within twelve months. All other investments without a fixed maturity date are considered to be substantially non-current in nature.

17 Financial investments *(continued)*

17.2 Derivatives

Derivatives held to cover linked liabilities

At 31 December 2017, all derivatives are classified as Assets held for sale (note 18.2).

	Notional amount	*Fair value assets*	*Fair value liabilities*
	€000	**€000**	**€000**
At 31 December 2016			
Currency derivatives			
– foreign exchange contracts	217,583	104	69
Equity derivatives			
– equity options	6,721	2	802
	224,304	106	871

17.3 Fair values

There are certain financial assets and liabilities that are carried at amortised cost. The fair value of these assets and liabilities is not disclosed given that the carrying amount is considered to be a reasonable approximation of fair value because they are either frequently re-priced to current market rates or short term in nature. A detailed analysis of the fair value level splits of financial assets and liabilities is provided in note 26.

18 Held for sale assets and liabilities

18.1 On 9 November 2017, the Company has entered into a Portfolio transfer agreement with Lombard International Assurance S.A for the sale of the policies of insurance governed by the Wealth Insurance Italy portfolio.

This portfolio forms part of a larger portfolio which was acquired in 2014 for nil consideration and is being sold for €1. The transaction is expected to be completed in 2018, subject to regulatory approvals.

In November, the assets and liabilities pertaining to this portfolio were categorised as a disposal group in accordance with IFRS 5 'Non-current Assets held for sale and Discontinued Operations'. They are consequently considered to be current in nature.

18 Held for sale assets and liabilities *(continued)*

18.1 (continued)

At 31 December 2017 the portfolio comprised:

	2017
	€000
Assets	
Financial Investments:	
Net assets held to cover linked liabilities	
Equities – listed	16,543
Debt Securities – Government bonds:	
– listed	100,846
– unlisted	4,999
Debt securities – Others:	
– listed	167,802
– unlisted	7,181
Collective investment schemes:	
– listed	37,920
– unlisted	130,557
Policyholders' loans	(37,427)
Net derivative financial assets	1,755
Accrued interest	4,436
Cash at bank	39,185
Total	473,797
Liabilities	
Financial liabilities:	
Investment contracts at fair value through profit or loss	473,797

Given that policy holders' loans pertain to individual policies which are at all times in a net asset position (i.e. a positive policy account balance), these balances are netted off against assets within these financial statements. Derivatives pertain solely to policies on which the Company does not hold investment discretion.

18.2 Derivatives

Derivatives held to cover linked liabilities

	Notional amount	*Fair value assets*	*Fair value liabilities*
	€000	€000	€000
At 31 December 2017			
Currency derivatives			
– foreign exchange contracts	9,872	39	2
Equity derivatives			
– equity options	339	30	–
– currency options	14,475	1,688	–
	24,686	1,757	2

18 Held for sale assets and liabilities *(continued)*

18.3 Liabilities held for sale

	2017	2016
	€000	€000
At 1 January	**–**	–
Transferred from investment contract liabilities (note 22)	**495,479**	–
Account balances paid on surrender and other termination during the year	**(582)**	–
Changes in unit prices and other movements	**(21,100)**	–
	473,797	–

18.4 Fair values

There are certain financial assets and liabilities that are carried at amortised cost. The fair value of these assets and liabilities are not disclosed given that the carrying amount is a reasonable approximation of fair value because they are either frequently re-priced to current market rates or short term in nature. A detailed analysis of the fair value level splits of financial assets and liabilities is provided in note 26.

19 Insurance liabilities and reinsurance assets

19.1 Analysis of insurance liabilities and reinsurance assets

	2017	2016
	€000	€000
Gross		
Claims outstanding:		
– Non-linked	**3,334**	3,074
– Linked	**490**	450
Total claims outstanding – gross	**3,824**	3,524
Long term insurance contracts:		
– Non-linked	**432,201**	436,897
– Linked	**222,767**	205,140
Total long term insurance contracts – gross	**654,968**	642,037
Total insurance liabilities – gross	**658,792**	645,561
Reinsurance assets		
Claims outstanding:		
– Non-linked	**2,574**	2,097
Long term insurance contracts:		
– Non-linked	**84,647**	84,343
Other reinsurance payables	**(1,334)**	(1,212)
Total reinsurance assets	**85,887**	85,228

19 Insurance liabilities and reinsurance assets *(continued)*

19.1 Analysis of insurance liabilities and reinsurance assets (continued)

	2017	2016
	€000	€000
Net		
Claims outstanding:		
– Non-linked	**760**	977
– Linked	**490**	450
Total claims outstanding – net	**1,250**	1,427
Long term insurance contracts:		
– Non-linked	**347,554**	352,554
– Linked	**222,767**	205,140
Total insurance liabilities – net	**570,321**	557,694
Other reinsurance payables	**1,334**	1,212
Total insurance contract provisions – net	**572,905**	560,333

Claims outstanding are considered to be current in nature. Long-term insurance contract liabilities are substantially non-current in nature.

19.2 Long-term life insurance contracts – assumptions, change in assumptions and sensitivity

The technical provisions in respect of long-term life insurance contracts are subject to quarterly valuations by the Approved Actuary based on data and information provided by the Company.

19.2.1 Process used for assumptions

For non-linked reserves on protection policies the long-term business provision is calculated on a net premium basis. This involves subtracting the present value of future net premiums from the present value of future benefits payable under a policy until it ceases on maturity or at death if earlier. For the with-profit and unit-linked business, a discounted cash flow approach is used, with a minimum reserve of the surrender benefit payable on the policies.

The reserves on the acquired creditor contracts are the sum of an unexpired premium reserve, an expense reserve and an outstanding claims reserve. These contracts are 100% reinsured and therefore have no net impact on the Statement of Financial Position.

The principal assumptions underlying the calculation of the long-term business provision are the following:

Mortality

A base mortality table is selected which is most appropriate for each type of contract. The mortality rates reflected in the table below are adjusted by the expected mortality based on a statistical investigation into the Company's mortality experience.

Reserving interest rates

Reserving interest rates for the current and comparative financial periods were determined based on Euro swap curves as at reporting dates. Rates for bond portfolio and equities/property portfolio were based on swap curves, which were considered as risk-free, and by adding appropriate margins. The reserving interest rates at different terms for With-Profits policy account, Non-linked reserves and Linked reserves were the weighted average of the constituents of the respective portfolio.

19 Insurance liabilities and reinsurance assets *(continued)*

19.2 Long-term life insurance contracts – assumptions, change in assumptions and sensitivity (continued)

19.2.1 Process used for assumptions (continued)

For many of the life insurance products, the interest rate risk is managed through asset/liability management strategies that seek to match the interest rate sensitivity of the assets to that of the underlying liabilities. The overall objective of these strategies is to limit the net change in value of assets and liabilities arising from interest rate movements. While it is more difficult to measure the interest rate sensitivity of the Company's insurance liabilities than those of the related assets, to the extent that the Company can measure such sensitivities, management believes that interest rate movements will generate asset value changes that substantially offset changes in the value of the liabilities relating to the underlying products.

Renewal expenses and inflation

The current level of renewal expenses is assumed to be an appropriate expense base. Expense inflation is based on the French inflation swap curve modified to estimate future inflation for Malta.

Taxation

The Company has assumed that current tax legislation and rates will not change.

Key assumptions

The principal assumptions used to value the life reserves of the main classes of business were as follows:

At 31 December 2017

Class of business	*Renewal expense (p.a.)*	*Mortality*
Term assurances	**€36.70**	**103.50% TM00 / 103.50%TF00**
Savings Plans	**€36.70**	**92% TM00 / 92%TF00**
Unit-Linked – Malta portfolio	**€36.70**	**92% TM00 / 92%TF00**

At 31 December 2016

Class of business	*Renewal expense (p.a.)*	*Mortality*
Term assurances	€34.80	103.50% TM00 / 103.50%TF00
Savings Plans	€34.80	92% TM00 / 92%TF00
Unit-Linked – Malta portfolio	€34.80	92% TM00 / 92%TF00

Savings plans and unit-linked policies are valued at the gross value of the policy account together with a non-unit provision. The non-unit provision allows for the future cost of expenses and mortality where these cannot be met from available margins in the plan.

Riders (other than term riders) are valued using approximate methods.

19.2.2 Change in assumptions

Assumptions are adjusted for changes in investment return and policy maintenance expenses to reflect changes in market conditions and experience. The effect of changes in current year's assumptions used to measure insurance liabilities and PVIF on current year's profit before tax and balance of insurance liabilities, net of the impact on PVIF, at the reporting date was as follows:

	Gross PVIF increase/ (decrease)	*Liabilities increase/ (decrease)*	*Profit/(loss)*
	€000	**€000**	**€000**
At 31 December 2017			
Economic	**195**	**(1,829)**	**2,024**
Lapse	**(1,126)**	**–**	**(1,126)**
Expenses	**(565)**	**500**	**(1,065)**
Expense inflation	**111**	**(180)**	**291**
Bond risk premium	**520**	**551**	**(31)**
Other	**(15)**	**(3)**	**(12)**

19 Insurance liabilities and reinsurance assets *(continued)*

19.2 Long-term life insurance contracts – assumptions, change in assumptions and sensitivity (continued)

19.2.2 Change in assumptions (continued)

	Gross PVIF increase/ (decrease)	*Liabilities increase/ (decrease)*	*Profit/(loss)*
	€000	**€000**	**€000**
At 31 December 2016			
Economic	**173**	**2,525**	**(2,352)**
Lapse	**399**	**–**	**399**
Expense unit cost	**(1)**	**42**	**(43)**
Margin review	**254**	**(357)**	**611**
Other	**–**	**526**	**(526)**

19.2.3 Sensitivity analysis

An analysis of sensitivity around various scenarios provides an indication of the adequacy of the Company's estimation process in respect of its life assurance contracts. The table presented below demonstrates the sensitivity of insured liability estimates to particular movements in assumptions used in the estimation process. Certain variables can be expected to impact life assurance liabilities more than others, and consequently a greater degree of sensitivity to these variables may be expected.

At 31 December 2017	*Movement*	*Reported value of net non-linked insurance liabilities*
	€000	**€000**
Base stress		
Interest rates increasing 100 basis points	**(16,670)**	**330,884**
Interest rates reducing 100 basis points	**21,838**	**369,392**
All mortality and morbidity rates increasing by 10%	**1,153**	**348,707**
All mortality and morbidity rates reducing by 10%	**(1,248)**	**346,306**
All expenses increase by 10%	**766**	**348,320**
All expenses reduce by 10%	**(700)**	**346,854**

At 31 December 2016	*Movement*	*Reported value of net non-linked insurance liabilities*
	€000	**€000**
Base stress		
Interest rates increasing 100 basis points	**(19,316)**	**333,238**
Interest rates reducing 100 basis points	**26,198**	**378,752**
All mortality and morbidity rates increasing by 10%	**1,148**	**353,702**
All mortality and morbidity rates reducing by 10%	**(1,193)**	**351,361**
All expenses increase by 10%	**877**	**353,431**
All expenses reduce by 10%	**(794)**	**351,760**

The analysis above has been prepared for a change in variable with all other assumptions remaining constant and ignores changes in the value of any related assets. As described in notes 3 and 5, linked insurance contract liabilities are not exposed to the above assumption changes and have consequently been excluded from the above analysis.

19 Insurance liabilities and reinsurance assets *(continued)*

19.3 Movements in insurance liabilities

	2017	2016
	€000	€000
Claims outstanding		
At 1 January	3,524	6,604
Movement for the year taken to profit or loss	300	(3,080)
At 31 December	3,824	3,524
Non-linked long-term business		
At 1 January	436,897	419,318
Movement for the year	(4,696)	17,579
At 31 December	432,201	436,897
Linked long-term business		
At 1 January	205,140	190,735
Premiums received	22,517	22,248
Account balances paid on surrender and other terminations during the year	(16,895)	(14,675)
Changes in unit prices and other movements	12,005	6,832
At 31 December	222,767	205,140

19.4 Movements in reinsurance assets

	2017	2016
	€000	€000
Claims outstanding		
At 1 January	2,097	5,316
Movement for the year taken to profit or loss	477	(3,219)
At 31 December	2,574	2,097
Non-linked long-term business		
At 1 January	84,343	79,011
Movement for the year	304	5,332
At 31 December	84,647	84,343

Linked long-term business

The Company did not cede any of these liabilities to its reinsurers during the current and comparative year

20 Insurance and other receivables

	2017	2016
	€000	€000
Current portion		
Receivables arising from insurance	839	978
Accrued income and prepayments	3,964	4,192
	4,803	5,170

21 Cash and cash equivalents

Balances of cash and cash equivalents are analysed below:

	2017	2016
	€000	€000
Cash at bank		
– Linked business	15,380	83,230
– Non-linked business	79,371	57,945
As per statement of financial position	94,751	141,175
Liabilities held for sale		
– Cash at bank within a disposal group of assets	39,185	–
As per statement of cash flows	133,936	141,175

22 Investment contract liabilities

Investment contracts at fair value through profit or loss (unit-linked):

	2017	2016
	€000	€000
At 1 January	930,936	987,008
Transferred to liabilities of disposal group classified as held for sale (note 18)	(495,479)	–
Premiums received	6,203	7,946
Account balances paid on surrender and other termination during the year	(272,914)	(150,928)
Changes in unit prices and other movements	34,390	86,910
	203,136	930,936

Surrenders stated above include an amount of €50,781,000 (2016: €55,786,000) were the Company transferred assets to the policy holder instead of cash.

Investment contract liabilities have been designated by the Company as at fair value through profit or loss. The maturity value of these financial liabilities is determined by the fair value of the linked assets, at maturity date. There will be no difference between the carrying amount and the maturity amount at maturity date.

23 Provision for liabilities and charges

The balance constitutes of a provision in relation to an onerous contract which results from a closed investment product where related income is based on balances under management, whilst related costs are fixed. The provision for liabilities and charges represents an estimate of future losses and is substantially not current in nature.

	2017	2016
	€000	€000
Contingent Liability		
At 1 January	–	–
Additions	689	–
At 31 December	689	–

24 Insurance payables, other payables and deferred income

	2017	2016
	€000	€000
Current Portion		
Direct insurance contract payables	**3,964**	3,993
Amounts due to related parties	**625**	485
Other payables and accrued expenses	**3,007**	2,641
Deferred income	**390**	405
Deferred commission on reinsurance	**620**	1,867
	8,606	9,391

24.1 Deferred income includes €136,000 (2016: €132,772) deferred under investment management services contracts that are recognised as revenue over the lifetime of the product.

24.2 Amounts due to related parties are unsecured, interest free and payable on demand.

25 Deferred tax assets and liabilities

25.1 Recognised deferred tax assets and liabilities

Deferred tax (assets) and liabilities are attributable to the following temporary differences:

	Assets		*Liabilities*		*Net*	
	2017	2016	**2017**	2016	**2017**	2016
	€000	€000	**€000**	€000	**€000**	€000
Property and equipment	**1**	(8)	**–**	–	**1**	(8)
Investment properties	**–**	–	**274**	252	**274**	252
Intangible assets	**–**	–	**20,474**	21,060	**20,474**	21,060
Financial assets	**–**	–	**–**	7,780	**–**	7,780
Insurance payables and deferred income	**–**	–	**271**	227	**271**	227
Share-based payments	**(51)**	(51)	**51**	51	**–**	–
Other provisions	**(259)**	–	**–**	–	**(259)**	–
Fair value reserves – AFS	**–**	–	**5**	58	**5**	58
	(309)	(59)	**21,075**	29,428	**20,766**	29,369

25.2 Movement in temporary differences during the year

	2017	2016
	€000	€000
At 1 January	**29,369**	27,979
Acquired from amalgamation of subsidiary company	**–**	(43)
Transfer to current tax (note 13.3)	**(7,780)**	–
Recognised in profit or loss	**(770)**	1,487
Recognised in equity	**(53)**	(54)
At 31 December	**20,766**	29,369

26 Financial assets and liabilities – basis of valuation

26.1 Fair value valuation

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Company sources alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable.

The table below analyses financial instruments carried at fair value, by valuation method.

	Level 1	Level 2	Level 3	Total
	€000	**€000**	**€000**	**€000**
At 31 December 2017				
Assets				
Equity securities	**41,488**	**–**	**–**	**41,488**
Debt securities	**263,832**	**–**	**–**	**263,832**
Collective investment schemes	**416,001**	**411**	**7,474**	**423,886**
Assets held for sale:				
– Equity securities	**16,543**	**–**	**–**	**16,543**
– Debt securities	**270,614**	**10,214**	**–**	**280,828**
– Collective investment schemes	**37,920**	**127,823**	**2,734**	**168,477**
– Net financial derivatives	**–**	**1,755**	**–**	**1,755**
Liabilities				
Investment contracts at fair value through profit or loss	**202,725**	**411**	**–**	**203,136**
Liabilities held for sale:				
– investment contracts at fair value through profit or loss	**331,271**	**139,792**	**2,734**	**473,797**
At 31 December 2016				
Assets				
Equity securities	95,790	–	–	95,790
Debt securities	621,153	22,656	–	643,809
Collective investment schemes	596,468	67,152	5,840	669,460
Liabilities				
Investment contracts at fair value through profit or loss	840,577	89,074	1,285	930,936
Net financial derivatives	–	765	–	765

As further explained in note 17 and 18, derivatives are netted off.

The analysis of investment properties is included in note 15.

Although the Company believes its estimates of fair value are appropriate, the use of different methodologies or assumptions could lead to different measurements of fair values, especially for Level 3 assets. Nonetheless, management is confident that changing one or more of the assumptions used to reasonably possible alternative assumptions would not change fair value significantly.

The following table shows a reconciliation from the opening balances to the closing balances of financial assets for fair value measurements classified within Level 3 of the fair value hierarchy.

26 Financial assets and liabilities – basis of valuation *(continued)*

26.1 Fair value valuation (continued)

	2017	2016
	€000	€000
Level 3		
Collective investment Schemes		
Financial investments – Net assets held to cover linked liabilities:		
At 1 January	**5,840**	2,402
Purchases	**2,787**	4,555
Transferred to Assets held for sale	**(1,003)**	–
Disposals	**(282)**	(1,027)
Gains/(losses) recognised in profit or loss	**132**	(90)
At 31 December	**7,474**	5,840
Assets held for sale:		
At 1 January	**–**	–
Transferred from financial investments – Net assets held to cover linked liabilities	**1,003**	–
Purchases	**250**	–
Transfer from level 1	**1,646**	–
Losses recognised in profit or loss	**(165)**	–
At 31 December	**2,734**	–

The collective investment schemes categorised in Level 3 on 1 January 2016, were acquired as part of the portfolio transfer of unit-linked investment contracts from HSBC Life (Europe) Limited in 2014.

During 2016, the Company invested in a European Mid-Market Debt Fund. This consists of predominantly senior debt to European mid-market companies concentrating on primary market transactions, within Western Europe, focusing on the largest economies. During 2017, the Company made a further investment in the European Mid-Market Debt Fund which is in line with the original commitment. The other collective investment schemes, which up to 2016 were categorised in Level 3 and consist of shares in alternative funds which are unlisted and have illiquid price sources, were transferred to Assets held for sale in November 2017 (note 18).

During 2017, an investment in a collective investment scheme of €1,646,000 was transferred from Level 1 to Level 3. The price for this fund is no longer being quoted on the market.

In view of no quoted market prices or observable inputs for modelling the value of collective investment schemes categorised in Level 3, the fair value of the shares held is derived using the net asset value as sourced from the respective custodians. The uncertainty in utilizing the net asset value lies in the availability of the financial statements of the alternative funds at 31 December 2017 and their respective audit opinion.

At 31 December 2017, €2,734,000 (2016: €1,285,000) of the collective investment schemes categorized in Level 3 are financial assets held to cover linked liabilities which are classified as Assets held for sale. The corresponding liabilities to customers under investment contracts in relation to these investments are also categorized in Level 3. Investment risk on these Level 3 assets is borne by the policyholder as it was the decision of the policyholder to invest in these assets.

27 Capital and reserves

27.1 Share capital

	Ordinary shares	
	2017	2016
	No.	No.
On issue at 1 January	**24,007,288**	24,007,288
On issue at 31 December – fully paid	**24,007,288**	24,007,288

At 31 December 2017, the authorised share capital comprised 30,000,000 (2016: 30,000,000) ordinary shares at a par value of €1.164686 each. All issued shares are fully paid up.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. All shares rank equally with regard to the Company's residual assets.

No dividends were distributed during the year.

27.2 Fair value reserve

Fair value reserve comprises the cumulative net change in the fair value of available-for-sale financial assets, net of deferred taxation. This balance is held in reserves until the investments are derecognised or impaired.

28 Related party transactions

28.1 Parent and ultimate controlling party

The Company is a wholly owned subsidiary of HSBC Bank Malta p.l.c., the registered address of which is 116, Archbishop Street, Valletta, Malta.

The Company's ultimate parent Company is HSBC Holdings plc, the registered office of which is 8, Canada Square, London E14 5HQ, United Kingdom.

HSBC Bank Malta p.l.c., prepares the consolidated financial statements of the Group of which HSBC Life Assurance (Malta) Ltd forms part. These financial statements are filed and available for public inspection at the Registrar of Companies in Malta.

HSBC Holdings plc in turn prepares the consolidated financial statements of which HSBC Bank Malta p.l.c. and its subsidiaries form part. These consolidated financial statements may be obtained from the ultimate parent Company.

28.2 Transactions with key management personnel

Directors' fees and emoluments are included in administrative expenses and are stated in note 12.

28 Related party transactions *(continued)*

28.3 Other related party transactions

	2017	2016
	€000	€000
Net income		
Fees and commissions income – other related parties	**768**	810
Investment income – parent	**(1)**	42
Debt security interests income – other related parties	**578**	353
Dividend income – other group	**40**	(100)
Interest expense on loan advanced by parent	**–**	(133)

Net income from related party transactions arises from:
– rebates of annual management charges;
– interest receivable on cash balances deposited;
– dividend receivable on equities;
– interest receivable on bonds; and
– interest payable on borrowings.

	2017	2016
Expenses		
Fees and commissions expense – parent	**1,437**	1,369
Fees and commission expense – other related parties	**20**	19
Other administrative expense – other related parties	**2,691**	2,341

Expenditure from related party transactions includes expenses incurred for the provision of services by related entities such as custodian and asset administraion, investment management and actuarial services. It also includes commissions payable to group companies in relation to sales of the Company's products. The Company's products are marketed and sold primarily by HSBC Bank Malta p.l.c. through its sales channels.

	2017	2016
	€000	€000
Dividend paid		
Nil (2016: 0.33) net dividend per share	**–**	8,000

Investment in Group Companies

The Company holds one share in HSBC Global Asset Management (Malta) Limited. This share has a par value of €2.329373 and was originally acquired at nil consideration.

Amalgamation of Subsidiary Company

On 1 January 2016, the Company, as a result of amalgamation, acquired its subsidiary HSBC Insurance Management Services (Europe) Limited. In accordance with Section 354 of the Companies Act, (Chapter 386, Laws of Malta), the Company has succeeded to all rights, obligations, assets and liabilities of HSBC Insurance Management Services (Europe) Limited.

The Company acquired the following assets, liabilities and reserves:

	2016
	€000
Assets	
Property and equipment	1
Deferred tax asset	43
Current tax asset	28
Insurance and other receivable	7
Cash at bank	240
Liabilities	
Insurance payables, other payables and deferred income	120
Retained earnings	174

28 Related party transactions *(continued)*

28.4 Related party balances

	2017	2016
	€000	€000
Year-end balances with related parties		
Assets		
Insurance and other receivables – other related parties	**142**	344
Cash and cash equivalents – parent	**81,146**	59,258
Cash and cash equivalents – other related parties	**9,815**	12,066
Debt securities – parent	**723**	755
Debt securities – other related parties	**–**	22,849
Collective investment schemes	**267,950**	311,690
Liabilities		
Insurance and other payables:		
– Parent	**237**	226
– Other related parties	**1,255**	1,495

29 Commitments

At 31 December 2017, the Company has open commitments to invest a further €1,600,000 (2016: €4,387,000) in private equities.

30 Comparative information

Certain amounts in these financial statements have been reclassified to conform with the current year's presentation.

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