Solvency & Financial Condition Report 2017
KBC Verzekeringen NV, Belgium

Contact details: Investor Relations Office

investor.relations@kbc.com

www.kbc.com

KBC Group NV, Investor Relations Office, Havenlaan 2, 1080 Brussels, Belgium.

Contact details: Press Office

Viviane Huybrecht (General Manager, Group Communication).

+ 32 2 429 85 45

pressofficekbc@kbc.be

KBC Group NV, Group Communication, Havenlaan 2, 1080 Brussels, Belgium.

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Management
summary

Management Summary

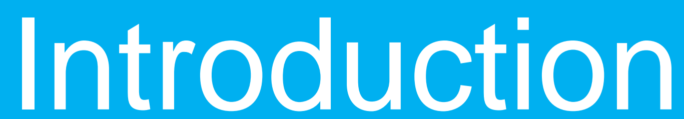
The Solvency & Financial Condition Report (SFCR) has to be published each year by all insurance undertakings and groups. It provides qualitative and quantitative information on the business and performance, the system of governance, the risk profile, the valuation for solvency purposes and capital management of the undertaking.

The report has a harmonised structure that is defined in Annex XX to the Solvency II Delegated Acts Regulation[1] and includes templates defined by the Implementing Regulation[2] that contain quantitative information, Quantitative Reporting Templates (QRTs).

All amounts quoted in this report and in the tables are in millions of euros, unless otherwise stated. Since this is the second time that this report has been published, comparisons are made with available Solvency II-related data of the previous year.

1 Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 (CDR EU 2015_35)

2 Commission Implementing Regulation (EU) 2015/2452 of 2 December 2015 (CIR EU 2015-2452)


Introduction

Introduction

This document is the Solvency and Financial Condition Report (SFCR) of KBC Insurance NV in Belgium according to the Solvency II directive and Commission Delegated Regulation (EU) 2015/35 – Title 1 Chapter XII (Delegated Acts). The structure of the SFCR is as described in annex XX of the Delegated Acts. The figures presented in this report are in line with the Quantitative Reporting Templates (QRT) which are published simultaneously on https://www.kbc.com

A separate section (section F) is reserved for the SFCR of fire reinsurance company *Maatschappij voor Brandherverzekering CVBA* (MVBh for short). The insurance activities of KBC Insurance NV in Belgium include their reinsurance subsidiary MVBh. The pertaining QRTs of MVBh are published separately on https://www.kbc.com.

Business and
Performance

A. Business and Performance

A.1. Business

KBC Insurance NV is an insurance group catering mainly for retail, small and medium-sized enterprises (SME) and mid-cap clients on its core market Belgium.

Address: Professor Roger van Overstraetenplein 2
3000 Leuven
BELGIUM

Supervisory authority: National Bank of Belgium
Contact information: de Berlaimontlaan 14
1000 Brussels

Corporate bodies:

KBC Insurance NV has a dual model:

- the Board of Directors (‘Raad Van Bestuur’) is the supervisory body of KBC Insurance NV and has, among other things, the task of setting strategy and supervising operational management,
- the Executive Committee (‘Directiecomité’) is the Executive Body of KBC Insurance NV and is responsible for the operational management of the company.

Contact details: KBC Group
Corporate Communications
Havenlaan 2 - GCM
1080 Brussels
BELGIUM

External auditor: PWC Belgium
Contact details: Woluwegarden – Woluwedal 18
1932 Brussels
BELGIUM

Management: CEO Johan Thijs
Chairman of the Board of Directors Thomas Leysen

Disclosure policy

In line with its general communication policy, KBC aims to be as open as possible when communicating to the market about its exposure to risk. Risk management information is therefore provided in a separate section of the 2017 Annual Report of KBC Group NV and – more extensively – in this publication.

The most important regulations governing risk and capital management are the Solvency II capital framework applying to insurance entities and Basel III capital requirements applying to banking entities. Solvency I has been replaced by the fundamentally reformed Solvency II framework, which officially entered into force in January 2016.

To ensure that a comprehensive view is provided, the credit risk inherent in KBC Insurance's activities has also been included in the section on credit risk management. Detailed information on the technical insurance risk borne by KBC Insurance has been included.

Information is disclosed at the highest consolidated level. For more detailed information, please refer to the local capital disclosures of the entity concerned (for instance, those provided on their websites).

KBC ensures that a representative picture is given at all times in its disclosures. The scope of the reported information – which can differ according to the matter being dealt with – is clearly indicated.

The information provided in this document has not been subject to an external audit. However, the disclosures have been checked for consistency with other existing risk reports and were subjected to a final screening by authorised risk management representatives to ensure quality.

In addition, the 2017 Solvency & Financial Condition Report was distributed to the Group Executive Committee, the Board of Directors, as well as to the Risk & Compliance Committee to ensure the appropriate approval of the management body as requested under Solvency II.

One-on-one comparison of figures presented in the annual report and figures presented in this report cannot always be made due to the different risk concepts used under IFRS and Solvency II. In order not to compromise on the readability of this document, relevant parts of the annual report have been reproduced here or, where relevant, clarification is given to understand the differences between the accounting values and the Solvency II values.

This Solvency and Financial Condition report is available in English on the KBC website and is updated on a yearly basis. KBC's next update is scheduled for the beginning of May 2019. Depending on market requirements, KBC may however decide to provide more frequent updates.

A.2 Underwriting Performance of KBC Insurance NV

The following annual account of KBC Insurance NV has been prepared according to Belgian Generally Accepted Accounting Principles (B-GAAP).

(mln euros)	31-12-2017	31-12-2016	% difference
Non-Life			
Gross earned premiums	1058	1031	2,7%
Gross claims incurred	-638	-637	0,2%
Gross technical result	420	393	6,8%
Investment income	74	64	15,4%
General operating expenses	-329	-322	2,3%
Net ceded reinsurance result	-17	-10	68,1%
Result of the technical account Non-Life	**148**	**126**	**17,6%**
Net loss ratio non-life	56,9%	60,5%	-3,6 pp
Net cost ratio non-life	31,7%	32,0%	-0,3 pp
Combined ratio non-life	88,5%	92,4%	-3,9 pp
Life			
Guaranteed-interest (Branch 21) and Capitalisation (Branch 26) insurance			
Gross earned premiums	923	1214	-24,0%
Gross technical charges	-1108	-1445	-23,3%
Gross technical result	-186	-231	-19,6%
Net investment income life	512	540	-5,3%
General operating expenses	-115	-117	-1,6%
Net ceded reinsurance result	1,3	-1,3	-197,2%
Result Branch 21 and 26	212	191	10,9%
Branch 23: net result	**50**	**41**	**22,2%**

Result of the technical account Life	**261**	**232**	**12,9%**
Non-technical			
Net investment income	169	104	62,9%
Other income and expenses	-5	-6	-23,6%
Extraordinary result	0	0	0,0%
Non-technical Result	164	97	68,4%
Result before tax	**573**	**455**	**26,1%**
Income tax	-326	-149	119,0%
Changes in untaxed reserves	-0,3	0.3	-237,3%
Result for the period available for appropriation	**247**	**306**	**-19,3%**

Table 1 Income statement, using BGAAP

Non-life insurance

Earned premiums went up by 2.7%. An increase in the ABEX index pushed up the level of premiums collected in the 'Fire' segment. Growth in the 'Home' segment was attributable to a straight-line increase in premium rates and the rise in production (number of policies). Premiums from 'Comprehensive car insurance' were up 6%. The increase in premiums from 'Assistance' (+7.2%) was notably lower than the increase in 2016 (+27.2%) due to the fact that the acquisition of the group travel insurance portfolio from VAB NV has now been almost entirely included in the figures.

Gross claims incurred rose by 0,2% mainly due to an increase in ordinary and large claims, a higher allocation to the equalisation reserve and an adjustment being made to the MTPL & GTPL reserves based on more up-to-date mortality tables (higher cost associated with longer life expectancy). These factors were offset by the change in provisions set aside for the terrorist attacks in March 2016, the impact of the introduction of statutory interest rate and indicative tables in 2016, the impact of the new age of retirement in 2016 (these three factors had a negative impact in 2016) and a decline in storm-related claims.

	31-12-2017	31-12-2016	% difference
Net claims ratio for non-life insurance	56,9%	60,5%	-3,6 pp
Net expense ratio for non-life insurance	31,7%	32,0%	-0,3 pp
Combined ratio for non-life insurance	88,5%	92,4%	-3,9 pp

Table 2 Non-life ratios

The net claims ratio fell by 3,6 percentage points to 56,9%, due to the increase in premiums and the lower level of claims (excluding equalisation).

The net expense ratio (the ratio of net operating expenses to net written premiums) fell by 0,3 percentage points to 31,7%.

The combined ratio (the sum of the net claims ratio and net expense ratio) decreased by 3,9 percentage points to 88,5%, a decline attributable to the lower claims ratio.

Life insurance

The life insurance business consists of guaranteed-interest (Branch 21), unit-linked (Branch 23) and capitalisation (Branch 26) insurance policies. Compared with the guaranteed-interest and unit-linked policies, sales of capitalisation insurance remained very limited.

Guaranteed-interest insurance products

- Earned premiums (i.e. investment capital received) for guaranteed-interest products fell by - 291 million euros mainly on account of a decline in the 'Life Future 8' product.
- Claims incurred were 337 million euros less than at year- end 2016, a decrease attributable primarily to lower life insurance provisions being set aside as a result of the decline in premiums collected and lower 'uprenting' costs due to scaling back the 'Life Capital' portfolio.

The result for unit-linked insurance products increased by 9 million euros, attributable mainly to the higher level of internal transfers.

A.3 Investment Performance

At 754 million euros, net investment income (excluding unit-linked products) increased by 46 million euros in 2017. The main movements are:

- the decline in bonds because of lower yields (yields generated by many of the bonds that had reached maturity or were sold were higher than those for reinvestments);
- less interest being paid on time deposit accounts as a result of declining volumes;
- an increase in interest generated by mortgage loans;
- a drop in dividend income due primarily to lower average volumes and slightly lower dividend yields compared to 2016;
- an increase in the net realised result on shares, accounted for by the portfolio management strategy;
- lower value adjustments for shares;
- an increase in internal dividend income;
- a decline in interest on swaps, due to forward swap contracts that had been concluded in the past starting to generate interest as of 2016;
- a reduction in charges for put options, the use of which was discontinued in the first quarter of 2017.

System of
Governance

B. System of Governance

The activities of KBC Insurance NV are part of the KBC Insurance Group. Therefore the governance of KBC Insurance Group is also applicable to KBC Insurance NV. We present in this section the global system of Governance of the KBC Insurance Group level in which these activities are imbedded. Explicit references to the Non-Belgian entities of KBC Insurance Group and possible pertaining narratives are left out since they have their own SFCR described by their country's legislation.

B.1. Governance of the KBC Insurance Group

B.1.1. Main insurance companies of the KBC Insurance Group

The main entities of the KBC Insurance Group are:

- KBC Insurance NV (Belgium) and
- Its subsidiaries:
  - ČSOB Pojišťovna a.s. (Czech Republic);
  - ČSOB Poisťovňa a.s. (Slovak Republic);
  - K&H Insurance Zrt. (Hungary);
  - DZI Life Insurance Jsc (including DZI General Insurance Jsc) (Bulgaria);
  - KBC Group Re (Luxembourg).

The activities of these main entities of the KBC Insurance Group are organised in Business Units:

- The Belgian activities of KBC Insurance NV are part of the Business Unit Belgium and are organised in the Directorate KBC Insurance Products BE;
- ČSOB Pojišťovna a.s. is part of the Czech Republic Business Unit;
- ČSOB Poisťovňa a.s., K&H Insurance Zrt. and DZI Life Insurance Jsc (including DZI General Insurance Jsc) are part of the International Markets Business Unit.
- KBC Group Re is part of Group Centre

B.1.2. Shareholder structure and corporate bodies of KBC Insurance NV and governance of the Belgian activities of KBC Insurance NV

B.1.2.1. Shareholder structure

The shareholder structure of KBC Insurance NV is:

Shareholders	Number of shares	Percentage
KBC Group	1 002 016	95,3%
KBC Bank	1	0.0%
KBC Insurance	48 889	4,7%
	1 050 906	**100%**

Table 3 Shareholder structure of KBC Insurance NV

B.1.2.2. Corporate bodies of KBC Insurance NV

KBC Insurance NV is managed according to the dual model. This means that a distinction is made between:

- the 'Board of Directors' (BoD), which is tasked with determining strategy and supervising operational management;
- the 'Executive Committee' (ExCo) is responsible for the operational management of the company.

The tasks and the functioning of the Board of Directors and the Executive Committee are described in the 'Corporate Governance Charter of KBC Insurance NV' (Chapters 5 and 7). Reference is made several times to this Charter: the full document can be found on www.kbc.com.

The Board of Directors is assisted by the following advisory committees:

- The Audit Committee;
- The Risk & Compliance Committee;
- The Remuneration Committee of KBC Group NV;
- The Nomination Committee of KBC Group NV.

The tasks and the functioning of the Audit Committee and the Risk & Compliance Committee of KBC Insurance NV are described in the 'Corporate Governance Charter of KBC Insurance NV' (Chapter 6). The 'Corporate Governance Charter of KBC Group NV' contains the tasks and the rules of procedure of the Remuneration Committee and the Nomination Committee (Chapters 6.4 and 6.5):

- While it is legally not recommended for an insurance company to establish a nomination committee, the option was made in the KBC group to establish a nomination committee at the level of KBC Group NV, functioning also as nomination committee of KBC Insurance NV.
- The Remuneration Committee of KBC Group NV (mixed financial holding and parent company of the KBC Insurance Committee) functions as remuneration committee of KBC Insurance NV.

B.1.2.3. Governance of the Belgian activities of KBC Insurance NV ('KBC Insurance Products BE')

Management Committees at the level of the Belgium Business Unit

The insurance activities of KBC Insurance NV are part of the Belgium Business Unit.
The following management committees have been set up at the level of the Belgium Business Unit:

- The Belgium Business Unit Management Committee: accountable for designing and proposing the strategy and for managing the execution of the strategy in the Belgium Business Unit (BU), fitting the strategy of KBC Group NV and KBC Insurance NV, and, given the bank-insurance strategy of the KBC group, also for covering KBC Bank NV.
- The Risk, ALM and Capital Committee for the Belgium Business Unit: dedicated to risk topics, covering all risk types.
- The ALM Insurance Committee: supports management in respect of Asset & Liability insurance matters.

The Senior General Manager, responsible for the insurance activities of the Belgium Business Unit, is a member of these committees.

The Belgium Business Unit reports on its strategy, activities and results to the Executive Committee and to the Board of Directors of both KBC Group NV and KBC Insurance NV.

Management Committees at the level of Insurance Products Belgium

The activities of KBC Insurance Products BE are part of the directorate Insurance Products BE, headed by a Senior General Manager. This directorate has its own management committees to steer the activities, including:

- The Insurance Products Management Committee, which manages the KBC Insurance Products Directorate as a whole. It develops the overall strategy of KBC Insurance Products, fitting the strategy of KBC Group, KBC Insurance and of the Belgium Business Unit. It monitors the business and is responsible for risk management.
- The Insurance Products Risk Management Committee, which monitors Solvency II issues and assesses risks and risk mitigations within the directorate.
- The Life Insurance activities are steered by the following committees: a New & Active Product Process Committee, a Risk Management Committee and an Operational Management Committee.
- The Non-Life Insurance activities are steered by the following committees: a New & Active Product Process Committee, a Risk Management Committee and an Operational Management Committee.

Reporting of the control functions

The risk function, the compliance function and the actuarial function, given their role as second line of defence, and the audit function, given its role as third line of defence, will report on their findings regarding the activities of KBC Insurance Products BE to:

- the management of KBC Insurance Products BE;
- the Executive Committee of KBC Insurance NV;
- the Audit Committee, the Risk & Compliance Committee and the Board of Directors of both KBC Group NV and KBC Insurance NV.

B.1.3. Remuneration

KBC introduced the KBC Remuneration Policy in 2010, which defines general remuneration guidelines for all staff and specific remuneration guidelines for those employees who could have a material impact on the risk profile of the company, also known as ‘Key Identified Staff’. Due to the continuously changing legislation for financial institutions, the KBC Remuneration Policy is amended each year.

For additional details and background information on the remuneration policy, please see the 'Remuneration report for financial year 2017' section of the KBC Group 2017 Annual Report, which is available at https://www.kbc.com

On the other hand, the Compensation Report provides information on remuneration principles at the KBC Group level and discloses remuneration figures for financial year 2017 based on European and national legislation. This report can be found as well on https://www.kbc.com

B.1.4. Fit & proper

Separate policies were approved by the Board of Directors of KBC Group NV, KBC Bank NV and KBC Insurance NV for:

- the Board of Directors;
- the Executive Committee;
- the persons responsible for independent control functions, or 'Key Function Holders'.

The Fit & Proper Policy for the non-executive directors of KBC Group, KBC Bank and KBC Insurance among other things contains the following requirements:

- The Board of Directors must have sufficient expertise of the banking and insurance activities which are developed within the KBC group;
- The directors must have the capabilities to understand and critically assess, among other things, the strategy, the strategic planning, the effectiveness of the steps taken with a view to create effective governance, oversight and controls, and the risk reports, which are presented by the Executive Committee;
- The directors who are appointed in an advisory committee (Audit Committee, Risk & Compliance Committee, Nomination Committee and Remuneration Committee) must have relevant expertise with regard to the activities of the Committee;
- All directors, executive or not, independent or not, must have sufficient capacity to make independent judgment.

The Fit & Proper Policy for the members of the Executive Committee of KBC Group, KBC Bank and KBC Insurance among other things contains the following requirements:

- The Executive Committee must have a deep knowledge of the financial industry and of the banking and insurance activities which are developed within the KBC group;
- The ExCo members must have the knowledge and experience to lead the KBC group and must dispose in this respect of strategic insight and adequate knowledge and experience relating to finance, risk management, internal control, information management, organisation and regulatory issues;
- ExCo members must have leadership skills in line with the KBC leadership model;
- ExCo members must have sufficient capacity to make independent judgment;
- ExCo members live the values of the KBC group.

The process among other things contains the following steps:

- The Nomination Committee discusses, assesses and gives an advice to the Board of Directors regarding the composition of the Board, its advisory committees and of the Executive Committee;
- It discusses and proposes to the Board the required profile of the new directors;
- It assesses the candidates;
- It assesses the fitness and propriety of the directors (in case of re-appointment) or of the candidate directors (in case of appointment) taking into account the regulatory requirements and the requirements mentioned in the aforementioned policies. It does this assessment based on the files which are prepared for submission to the supervisor. It presents its advice to the Board of Directors.

The Fit & Proper Policy for the Key Function Holders of KBC Group, KBC Bank and KBC Insurance among other things contains the following requirements:

- The Key Function Holder must have the appropriate knowledge and experience for the corresponding position and with respect to the applicable legal framework and the direction of the Institution, through education and training (diploma/on the job) or relevant work experience (in principle 3 to 5 years is advisable);
- The Key Function Holder must show professional behaviour and have sufficient guarantees to fulfil the position in a conscientious and independent manner, with specific attention to the independence (conflict of interests) and pastime;
- The Key Function Holder must have specific competences such as client- and quality-focus, risk-mindedness, leadership, loyalty and stress resistance;
- The Key Function Holder must be able to fulfil the position in an honest, dedicated, independent and ethical manner and with integrity;
- The Key Function Holder may not have been subject to any of the listed forbidden convictions, or criminal, civil or administrative convictions, disciplinary actions, penalty procedures, arrangements or settlements inappropriate to the standard of reliability that the person is required to meet;
- The Actuarial Function Holder should possess the ability to interpret the undertaking's financial and actuarial information, identify key issues, put in place appropriate controls and take necessary measures based on this information.

The process among other things contains the following steps:

- The Corporate HR department discusses, assesses and gives an advice to the Executive Committee regarding the appointment of a Key Function Holder;
- It discusses and proposes to the Executive Committee the required profile of the Key Function Holder;
- It assesses the candidates;
- It assesses the fitness and propriety of the Key Function Holders (in case of re-appointment) or of the candidate Key Function Holders (in case of appointment) taking into account the regulatory requirements and the requirements mentioned in the internal policies. It does this assessment based on the files which are prepared for submission to the supervisor;
- It presents its advice to the Executive committee for approval.

B.2. Risk Management of the KBC Insurance Group

B.2.1. Risk governance

Main elements in our risk governance model:

- The Board of Directors, assisted by the Risk & Compliance Committee (RCC), which decides on and supervises the risk appetite and risk strategy each year. It is also responsible for the development of a sound and consistent group-wide risk culture, based on a full understanding of the risks the group faces and how they are managed, taking into account the group risk appetite;
- Integrated architecture centred on the Executive Committee that links risk appetite, strategy and performance goal setting;
- The Risk Management Committee and activity-based risk committees mandated by the Executive Committee;

- Risk-aware business people, who act as the first line of defence for conducting sound risk management in the group;
- A single, independent risk function that comprises the Group Chief Risk Officer (CRO), local CROs, local risk functions and the group risk function. The risk function (among others) acts as the second line of defence, while Internal Audit is the third line.

Relevant risk management bodies and control functions:

1. Executive Committee:
   - Makes proposals to the Board of Directors about risk and capital strategy, risk appetite, and the general concept of the risk management framework;
   - Decides on the non-strategy-related building blocks of the risk management framework and monitors its implementation throughout the group;
   - Allocates capital to activities in order to maximize the risk-adjusted return;
   - Acts as the leading risk committee, covering material issues that are channelled via the specific risk committees or the Group ALCO;
   - Monitors the group's major risk exposure to ensure conformity with the risk appetite.

2. Group ALCO (Asset & Liability Committee):
   - A business committee that assists the Executive Committee in the domain of (integrated) balance sheet management at the group level. It handles matters related to ALM and liquidity risk.

3. Risk committees:
   - The Risk Management Committee supports the Executive Committee in assessing the adequacy of, and compliance with, the KBC Risk Management Framework and defines and implements the vision, mission and strategy for the CRO Services of the KBC group.
   - The activity-based Group Risk Committees for respectively lending, markets and insurance support the Executive Committee in setting and monitoring limits at group level for these activities. Liquidity and ALM issues related to these activities are addressed in the Group ALCO.
     - *The Group Lending Committee*
       The Group Lending Committee supports the Executive Committee's time in setting, monitoring and following up limits for lending activities (funding, liquidity and ALM issues related to lending activities remain the responsibility of the Group Executive Committee/Group ALCO). With regard to KBC Insurance, the role of the Group Lending Committee relates to the credit part of the assets of KBC Insurance and to reinsurance contracts.
     - *The Group Markets Committee*
       The Group Markets Committee (GMC) decides upon and periodically reviews a framework of limits and policies on trading activities that is consistent with this Group Risk Appetite.
     - *The Group Insurance Committee*
       The Group Insurance Committee supports the Executive Committee in setting, monitoring and following up limits for insurance activities at KBC group level, including the KBC Insurance Group. It assists the Executive Committee with risk and capital monitoring regarding the insurance activity in close cooperation with business as first line of defence.
     - *The Asset & Liability Committee*
       The Asset & Liability Committee is a business committee that assists the Executive Committee in the domain of (integrated) balance sheet management at KBC group level, including the KBC Insurance Group. It handles matters related to ALM and liquidity risk.
   - The Group Internal Control Committee (GICC) supports the Executive Committee in monitoring and strengthening the quality and effectiveness of KBC's internal control system.

4. In order to strengthen the voice of the risk function and ensure that the decision-making bodies of the business entities are appropriately challenged on matters of risk management and are given expert advice, KBC has established independent Chief Risk Officers (CROs) throughout the group according to a logical segmentation based on entity and/or business unit. Close collaboration with the business is assured since they take part in the local decision-making process and can exercise a veto if needed. Independence of the CROs is achieved through a direct reporting line to the Group CRO.

5. Group Risk and Group Credit Risk (known collectively as 'the group risk function') have a number of responsibilities, including monitoring risks at an overarching group-wide level, developing risk and capital models (while business models are developed by business), performing independent validations of all risk and capital models, developing risk frameworks and advising/reporting on issues handled by the Executive Committee and the risk committees.

Performance is assessed on a yearly basis as part of the Internal Control Statement.

A simplified schematic of our risk governance model is shown below:

Figure 1 Simplified risk governance structure

B.2.2. Risk Management Framework & building blocks

- Risk management is a key component of the strategic management of KBC Group. It refers to the coordinated set of activities to manage the risks that can affect KBC Group in its ability to achieve its objectives.

- The KBC Risk Management Framework (KBC RMF) describes how risk management is performed on a continuous basis throughout the entire KBC group. As such, it is the single point of entry for all documentation on the risk management process within KBC Group. The risk management framework consists of following steps:

  - ✓ Risk identification
  - ✓ Risk measurement

- ✓ Setting and cascading risk appetite
- ✓ Risk analysis, reporting and follow-up

• The KBC RMF finds it origin in KBC's overall risk strategy, as defined by the KBC Risk Appetite (the amount and type of risk that KBC is able and willing to accept in pursuit of its strategic objectives) as decided on by the Board of Directors. It consists of:

- ✓ A number of generic fundamental risk standards, concepts and tools that are applicable to all risk types, e.g. a common risk map, risk measurement standards and risk appetite standards.
- ✓ A set of risk-type-specific risk management frameworks.
- ✓ An integrated risk management framework describing how to integrate all risk-type-specific information in order to provide a complete view of the risk profile of KBC Group and its subsidiaries.

• As the ultimate purpose of the KBC Risk Management Framework is to install an effective risk management process throughout the group it defines minimum standards that all entities within the group must adhere to. A local deviation of the group wide standards can be granted if needed, e.g. due to local regulations.

• The implementation of the KBC Risk Management Framework is organized on the basis of the risk type specific frameworks, each having an implementation checklist to evaluate its implementation status. In every entity or business unit of the group, a Chief Risk Officer is responsible for implementing the framework within the local risk function, and supporting the local business line management with the implementation of the framework in the business processes.

• As the risk management landscape is in a state of constant flux due to changes in internal and external contextual elements (industry trends, regulatory requirements, expectations of key stakeholders, organisational structure, etc.), the components of the KBC RMF are reviewed on a regular basis to ensure their ongoing effectiveness.

B.2.3. Own Risk & Solvency Assessment

The KBC Insurance Group and its insurance and reinsurance subsidiaries undertake on a regular basis an Own Risk and Solvency Assessment (ORSA) to monitor and ensure that business is managed in a sound and prudent way.

KBC's ORSA policy describes the general KBC approach with respect to the ORSA process and its outcome. It defines and describes the components, principles and characteristics of the ORSA process within the KBC Insurance Group. The ORSA Policy is reviewed on an annual basis.

The ORSA is an integral part of the business strategy and is taken into account on an on-going basis in the strategic decisions of the KBC Insurance Group.

The KBC Insurance Group has decided to undertake the ORSA assessments at the level of the KBC Insurance Group and at the level of the individual material subsidiaries pertaining to the Insurance Group, thereby aiming at a high level in processes and reporting across the KBC Insurance Group.

The main processes underlying the regular ORSA are executed on an annual basis and are closely linked to the Strategic Planning Process (Alignment of Planning Cycles or APC) which also follows an annual

cycle. The APC streamlines the processes of financial planning, strategy review, risk appetite setting and internal solvency and capital adequacy assessment.

Taking into account the fact that KBC's insurance business is sufficiently mature, this annual periodicity is deemed adequate.

On a quarterly basis, insurance integrated risk reporting reports on: risk signals; the evolution of the risk profile; results of deep dives, stress & scenario testing. These reports are discussed up to the level of the Executive Committee and the Board of Directors and allow them to steer stress & scenario testing, request (ad-hoc) mid- and long-term risk assessments and review the internal model and underpinning ambition and approach.

The Executive Committee of KBC Insurance can decide to perform an additional ad-hoc ORSA in case:

- major deviations versus the business plan (APC) are observed; and/or
- major changes to the group structure or group composition occur.

The annual ORSA process assesses the situation and the data per 31 December and is submitted to the Supervisory authority before 30 June of the following year. KBC does not differentiate between the internal and the supervisory ORSA report. Each ORSA report is complemented with an ORSA record which contains all documents that have been used in the different steps of the ORSA.

The process for setting risk appetite is strongly intertwined with and part of the strategic planning process (or APC process), which streamlines the processes of financial planning, strategy review and internal solvency and capital adequacy assessment. APC thus constitutes the process for setting and cascading risk appetite.

The figure below shows the five phases of the APC process:

Figure 2 Scheme of the annual Aligned Planning Cycles (APC)

Based on the outcome of the above processes and assessments a conclusion is included in the ORSA report that will indicate to what extent the available capital is sufficient to cover the capital requirements. It will link this conclusion to the:

- evolution of amount and composition of available regulatory capital over a three-year horizon and under different economic circumstances;
- evolution of required regulatory capital over the three-year planning horizon, taking into account expected changes to the risk profile of the entity/group;
- impact of scenario analyses and sensitivities on required and available regulatory capital.

KBC relies on the Solvency II standard formula to assess its overall solvency needs. On an annual basis an assessment is performed to check whether the standard formula is appropriate in relation to the risk profile of KBC.

B.3. Other key functions of the KBC Insurance Group

B.3.1. Actuarial Function

The Actuarial function is one of the key control functions that are defined in the Solvency II regulatory framework. Solvency II requires an Actuarial function to be installed in each insurance entity and at the Insurance Group level. Basically, the task of such a function is to ensure that the company's Board of Directors or Supervisory Board is fully informed in an independent manner. It does this, for example, by:

- advising on the calculation of the technical provisions (e.g., appropriateness of methodologies, appropriateness and quality of data used, experience analysis);
- expressing an opinion on the overall underwriting policy;
- expressing an opinion on the adequacy of reinsurance arrangements;
- contributing to the effective implementation of the Risk Management system (risk modelling underlying the SCR calculations, assisting with the internal model, contributing to the ORSA process);
- reporting and giving recommendations to the supervisory body of the entity.

Implementation of the Actuarial Function:

- The Actuarial Function at KBC Group level operates under the ultimate accountability of the Board of Directors;
- An 'Actuarial Function Holder' is appointed for every local entity and also at KBC Group level. The Actuarial Function Holder is to be registered on the pay-roll of the entity they are representing. Their duties cannot be outsourced to a party external to the entity;
- The Actuarial Function Holder coordinates the activities of the Actuarial Function. In general, 'a function' is the administrative capacity to undertake particular governance tasks and is – as such – not limited to one specific person or one organisational unit but can be assigned to several persons or departments subject to an adequate segregation of duties;
- The Actuarial Function Holder's basic task is to ensure the independent 'second pair of eyes' needed for the Actuarial Function Holder to fulfil all of the assigned obligations. The Actuarial Function gives input to the Actuarial Function Holder, e.g. in forming opinions, proposing recommendations and assisting in writing the Actuarial Function Report.

B.3.2. Compliance Function

With a view to centralisation, consistency and synergy, the Compliance function of KBC Insurance is exercised by Group Compliance. Group Compliance plays a double role with regard to the domains in scope of Compliance:

- An advisory role to support the business entities with the implementation and application of requirements, set up internal procedures and provide necessary training and awareness communication;

- A monitoring role by performing second-line controls on compliance with requirements.

An Intragroup Service Agreement has been drawn up defining the way this is organised.

Within the Compliance Department there are several technical units, each dealing with specific Compliance domains:

- Financial Markets including the AssurMiFID rules of conduct applicable to the insurance business and the rules of insurance mediation and distribution in general;
- Consumer and Data Protection;
- Embargo Management;
- Anti-Money Laundering (AML) (including OFAC, the Know Your Customer part of FATCA and the Common Reporting Standard, the EU Regulation on accompanying transfers of funds), financing of terrorism and preventing the funding of the proliferation of weapons of mass destruction;
- Ethics & Fraud.

The AML and Ethics & Fraud domain are split between a Policy unit and an Investigations unit.

Both the governance of the Compliance function and its policies within the scope as defined by the Circular on the Compliance Function (Circular FSMA-2012-21 dated 4 December 2012), fulfil the foreseen requirements. In its chapter about the Compliance function (chapter 5.4.), the NBB Circular _2016_31 (of 5 July 2016) regarding the governance for the insurance sector confirms the point of view also reflected in article 55 of the Bill of 13 March 2016 regarding the statute and the control on the insurance undertakings: the Compliance function has to focus on integrity and rules of conduct.

Based on the same NBB Governance Circular, two specific additional tasks are included in the Compliance domain. An inventory of the Solvency II-related policies is made, and a control on the structure of these policies is being installed in order to ensure that, at a minimum, each policy includes its objectives, the tasks to be performed by the responsible person/function, the applicable reporting processes and the requirement to inform all risk-related and actuarial functions where relevant. Additionally, Compliance will check consistency of governance topics sensu stricto in the main NBB reports (the governance memorandum, the SFCR and the RSR). These governance topics include ownership, management structure, fit & proper policy, incompatibility of mandates, loans and insurance policies for leaders, independent control functions, remuneration, conflicts of interest and outsourcing.

The legal department of KBC is charged with the follow-up of laws and regulations and their changes in the Solvency II context as well as of the communication to the businesses concerned.

It is vital to ensure that the crucial pieces of legislation, such as the 4th AML Directive, the GDPR, PRIIPS and IDD, falling under the Compliance domains, are adequately implemented by the businesses within the organisation in 2017-2018.

The key function holder for Compliance at KBC Insurance is the CRO of KBC Insurance, who is also a member of the Executive Committee (ExCO). The Head of the Compliance function of KBC Insurance has a direct reporting line to this member and a functional line with the CEO of KBC Insurance. The Compliance reports are formally submitted every quarter to the ExCO and RCC of KBC Insurance.

Within Compliance there is also a dedicated Coordinating Compliance Officer who is responsible for coordinating, supporting and following up in respect of the Insurance Products Directorate. The Head of

Compliance ensures sufficient resources are dedicated from the department to deal with KBC Insurance. The ExCo of KBC Insurance decides on the annual Compliance plans and submits them to the RCC for confirmation. The Head of Compliance reports to and attends the quarterly meetings of the KBC Insurance RCC. A separate and specific Compliance Charter and Integrity Policy have been drawn up for KBC Insurance, describing the scope, tasks and responsibilities of every party involved at several levels of the organisation. There are two Compliance Risk Managers (CORM) at the level of Insurance Products, one for life insurance and one for non-life insurance. They are not part of the second line of defence (Compliance) but instead are fully incorporated into the business entity. They are facilitators in implementing and following up on Compliance issues and support the Senior General Manager and General Managers of Insurance Products in their responsibilities with regard to Compliance. The Insurance Products Coordinating Compliance Officer and the CORMs work closely together, have regular meetings and report to the business entities' management.

B.3.3. Audit Function

The internal audit function of KBC Insurance NV is exercised by KBC Group Corporate Audit. It is regulated by NBB circular NBB_2015_11. The responsibilities of Internal Audit are to:

- provide independent assurance to the Board of Directors, the Audit Committee and the Executive Committee on the effectiveness and efficiency of the processes of risk management, internal control and corporate governance that are in place;
- support the Board of Directors, the Audit Committee and the Executive Committee in taking up their responsibilities in these processes;
- report any serious issues or risks which it becomes aware of and to undertake any required investigations into high-risk situations;
- make clear and actionable recommendations which address weaknesses noted during its work and to follow up on the implementation status of these recommendations;
- carry out any assignment or projects entrusted to it by the Board of Directors, the Audit Committee or the Executive Committee;

To safeguard its independence and objectivity:

- Internal Audit reports and is accountable to the Audit Committee;
- the internal audit activity remains free from interference by any part of the organisation, including matters of audit selection, procedures, frequency, timing or report content;
- the appointment and dismissal of the head of Internal Audit belongs to the authority of the Audit Committee;
- internal auditors are, during the exercise of their professional duties, authorised to have direct communication with any member of staff, as well as to access all premises and any records, files or data that are relevant to the performance of an assignment, subject to compliance with local regulations. All members of staff are requested to assist Internal Audit in fulfilling its roles and responsibilities;
- Internal Audit has the authority to perform assignments at its own initiative in all entities, departments, establishments and functions within its scope, subject to proper reporting to the local Executive and Audit Committees;
- Internal Audit has the authority to inform directly, and at its own initiative, the Chairman of the Board of Directors or Supervisory Board of the audited entity, the chairman of its respective Audit

Committee, the members of its Executive Committee, its Statutory Auditors or the local Supervisory Authorities;
- internal auditors must always be objective and impartial and seek to avoid any conflict of interest;
- internal auditors are not directly involved in the operational organisation of an entity, nor in deciding, developing, introducing or implementing risk management and internal control measures;
- internally recruited auditors respect a ‘cooling-off’ period;
- whenever practicable and without jeopardising competence and expertise, internal audit staff will periodically rotate within the internal audit function to boost independence.

The scope of Internal Audit covers all entities, all activities and all divisions, including the various control functions, of KBC Insurance NV. To this end Internal Audit will periodically – and at least once a year – examine and evaluate the areas within its scope. The audit plan is defined applying a risk-based approach while ensuring adequate coverage of matters of legal or regulatory interest. The audit plan is supplemented with a statement on the necessary resources to execute the plan. The audit plan must be approved by the Audit Committee. Deviations from the audit plan must be reported to the Audit Committee at least once a year.

The approach followed in performing the audit assignments should be described in all resulting audit reports so that their readers can consider the findings against the approach followed. A risk-based approach is used as the primary auditing method. The level of assurance, which may be gained from Internal Audit’s work, is relative to the nature and extent of work carried out. It is therefore essential that the auditor involved, when giving a reasoned opinion, documents the nature and the extent of the work undertaken.

The implementation of the audit recommendations is the responsibility of line management, who will communicate the status of this follow-up regularly to Internal Audit, for monitoring purposes.

To facilitate a consistent approach to Internal Audit across all entities within the KBC Insurance Group, the heads of local internal audit departments are accountable to their supervising Audit Committee and are steered by the Internal Auditor of KBC Group NV. The co-operation between the different internal audit departments is organised in a matrix structure where the competence-based axis intersects with the geographical responsibility axis.

The independence and objectivity of Internal Audit is assured by the KBC Insurance Internal Audit Charter approved by the Board of Directors. The Charter also describes the functioning and organisation of the Internal Audit function.

B.3.4. Internal Control System

B.3.4.1. Three lines of defence concept

In order to promote clear accountability for risk taking, oversight and independent assurance, a ‘Three lines of defence’ concept is implemented at the KBC Group level. All the relevant internal stakeholders (and their roles & responsibilities) related to risk management are positioned within this model. The three lines of defence are defined as follows:

- Business line management, as the first line of defence, is responsible for identifying and managing the risks inherent in the products, activities, processes and systems for which it is accountable. Business line management is also responsible for determining its risk appetite.

- The second line of defence (of which the Risk Function is part) includes all independent Support & Oversight Functions. The Risk function:
    - is responsible for identifying, measuring, monitoring and reporting risk on a group-wide basis, independently from the first line of defence;
    - sets the standards via the KBC Risk Management Framework and supports the business in its implementation;
    - challenges the business on their risk identification, measurement and response;
    - creates oversight of the Group's control environment and risk exposure.
- The third line of defence is provided by internal and external audit, assuring an independent review and challenge of the Group's risk management processes.

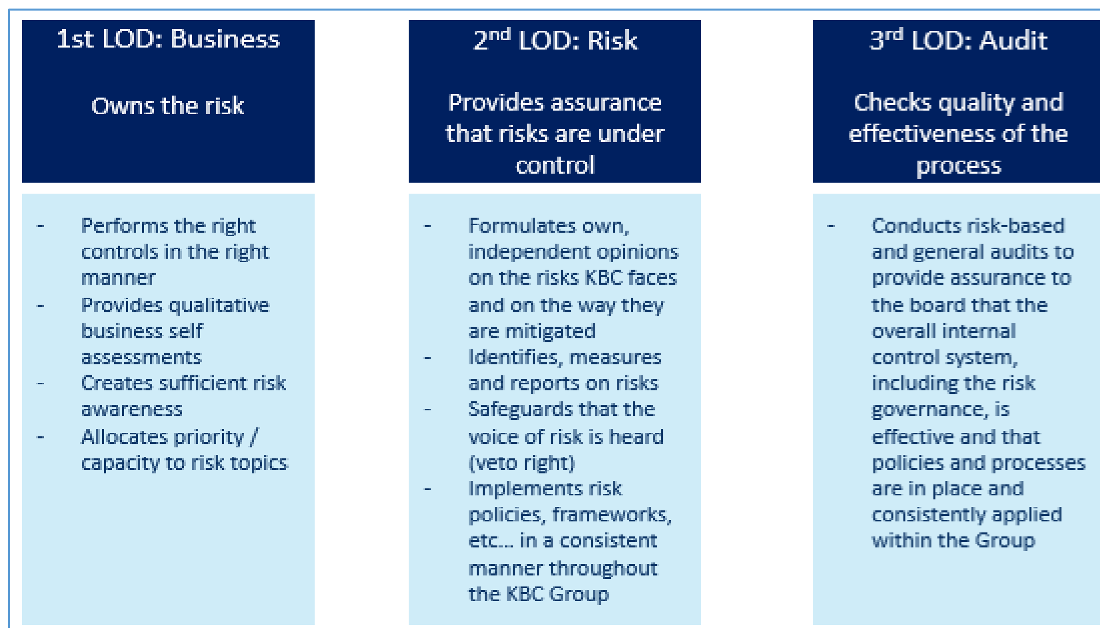


Figure 3 Three Lines of Defence structure

This 3 LOD model (as reviewed at the end of 2015) ultimately reinforces the resilience of KBC's risk and control environment and safeguards the sustainability of our business model.

Led by CRO Services, the 3 LOD program and its reviewed model continued to be implemented in 2017, enhancing:

- the quality and effectiveness of KBC's risk and control environment;
- the effectiveness of risk management;
- risk control.

B.4. Outsourcing

B.4.1. General outsourcing approach at the KBC group level

The KBC group has set the following strategic goals:

- KBC strives to offer its clients a unique bank-insurance experience;

- KBC develops the group with a long-term perspective and therefore achieves sustainable and profitable growth and respects solid risk, capital and liquidity boundaries;
- KBC puts its clients' interests at the heart of everything it does and offers them high-quality service and relevant solutions;
- KBC takes its responsibility towards society and local economies very seriously and aims to reflect that in its everyday activities.

The outsourcing approach of the KBC group is embedded in the above-mentioned cornerstones:

- KBC aims to maximise the retention and development of its internal knowledge of all aspects related to the bank-insurance model, as well as the related processes and activities;
- In particular, functions, processes and activities that include KBC-specific proprietary information, intellectual property rights, trade secrets, know-how presenting a competitive market advantage for KBC compared to peers ('Core KBC Know-How'), can never be outsourced to a third party, i.e., an entity outside the KBC group ('External outsourcing');
- To the extent that technological or economic developments justify the outsourcing of some activities, the KBC group strives for a maximal retention of knowledge and control of these activities. Therefore initially, the KBC group makes an appeal to the shared services centres (SSC) within the group ('Internal Outsourcing');
- In case of outsourcing, KBC aims for the highest possible quality level in order to ensure and guarantee long-term objectives and clients' interests.

B.4.2. Outsourcing principles

KBC group has an extensive policy on regulated outsourcing. This policy also applies to internal and external outsourcing. The policy describes the definition of outsourcing as applied within the group, a high-level process description, the group coordination and central notification and the monitoring principles.

For every outsourcing file, an outsourcing coordinator has to be appointed. This coordinator has an internal notification duty to a group-wide coordinator. This notification is not only required for new files, but for material changes in existing outsourced activities and for renewals as well.

The outsourcing entity is accountable for the risk assessment of an outsourcing initiative. The outsourcing entity needs to write a mandatory risk assessment, accompanied with a mandatory advice of the control functions, covering, among others:

- operational risk (as described in the group-wide key controls and zero tolerances);
- legal risk (possible legal showstoppers, provided by the (local) legal department);
- compliance risk (provided by the (local) compliance function);
- the risks controlled by the actuarial function (if applicable).

Within the group strategy, KBC Insurance develops its own approach on outsourcing. Core values in this approach are client centricity (putting the clients' interests first), maximal synergy and efficiency and the appeal on external expertise; in case this expertise exceeds the internal knowledge or capacities.

B.4.3. Intragroup outsourcing

KBC Group provides the following functions on behalf of KBC Insurance:

- Audit
- Compliance
- Risk
- Finance
- Asset liability management (ALM)
- ICT

In respect of KBC Insurance all these activities are considered to be critical or important operational functions or activities.

In addition, KBC Insurance relies on other KBC entities for specific insurance-related tasks:

- VAB, a Belgian-based subsidiary of KBC Insurance, provides services through its contact centre related to insurance obligations which cover assistance to persons (including their goods and/or motor vehicles) who encounter difficulties while traveling. VAB receives and adjust claims, and provides assistance on behalf of KBC Insurance.
    - VAB's Belgian-based contact centre registers claim reports made by telephone for other non-life insurance products. VAB advises clients on behalf of KBC Insurance, and initiates the claims handling process in urgent cases.
- In connection with Branch 23 life insurance policies, KBC Asset Management NV (Belgium) and KBC Asset Management SA (Luxembourg) services KBC Insurance for the set-up and management of Luxemburg- and Irish-based investment funds.

KBC Insurance also considers these activities to be critical and important operational functions and activities.

B.4.4. Outsourced critical and important operational functions and activities

KBC Insurance entrusts its own operational tasks to insurance intermediaries for the acceptance and claims handling of non-life insurance contracts. These activities are only entrusted to Belgian intermediaries, specifically for contracts concerning the relationship with the client.

Outsourcing to tied agents is done in a standardised manner. These agents can perform limited tasks related to the collection of insurance premiums, the settlement of claims with limited scope and the provision of green cards. Outsourcing contracts with insurance brokers follow a case-by-case approach and may include a wider range of tasks relating to contract management and claims settlement.

KBC Insurance is serviced by a number of Belgian-based self-employed consulting physicians, for specialised medical services (for acceptance for certain health and life insurance policies, claims handling of files that involve complicated medical aspects).

For second-pillar pension products, an external partner processes the annual statement of benefits.

Risk Profile

C. Risk Profile

In this section, we focus on the most material sector-specific risks we face.

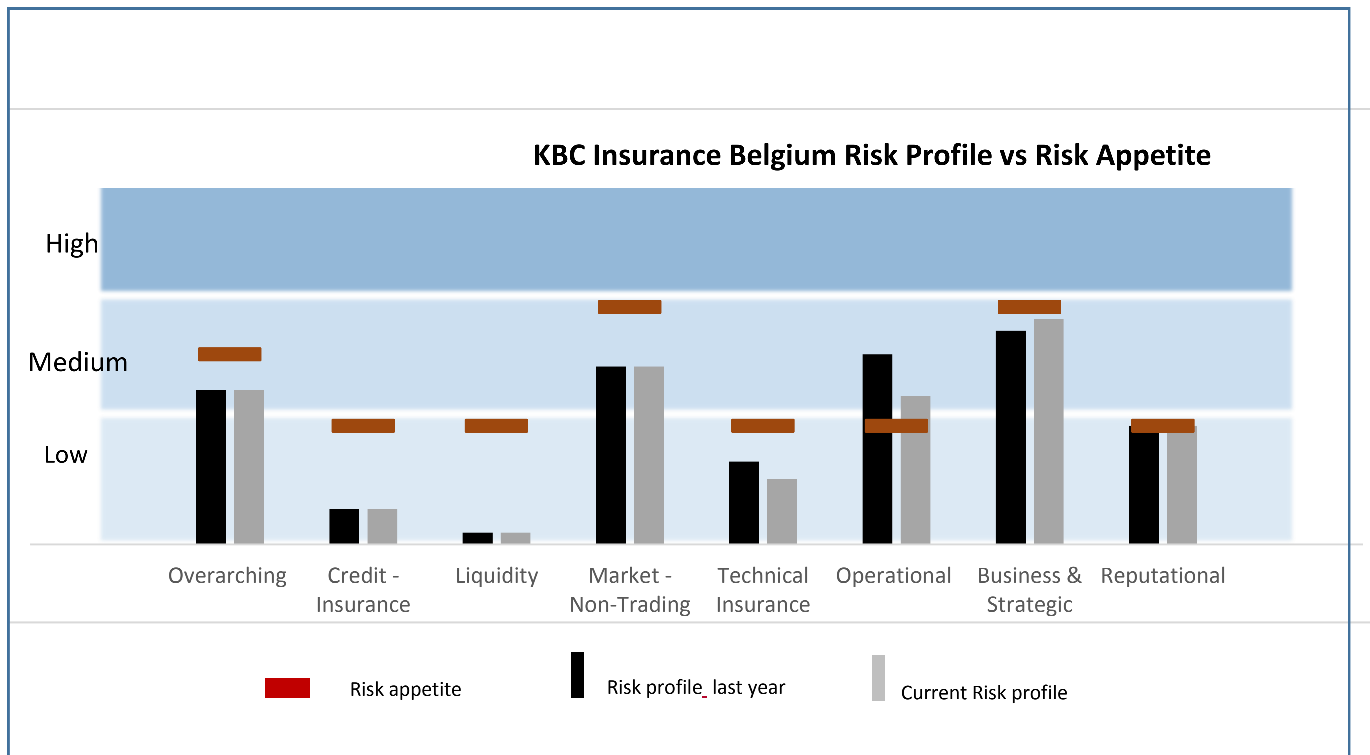


Figure 4 2017 Risk profile and Risk appetite of KBC Insurance NV

The KBC Insurance NV Risk Appetite Statement reflects the view of the Board of Directors and top management on risk-taking in general and in particular on the acceptable level and composition of risks in coherence with the desired return. This statement includes a specification of the risk profile and the risk appetite for each risk type into Low risk, Medium risk and High risk.

For KBC Insurance NV, this leads to the following risk appetite and risk profile:

The risk profile of KBC Insurance NV is depicted in Figure 4. For every risk type, as well as overall, the risk profile is evaluated and compared to the risk appetite.

The next paragraphs describe the assessment of the risk profile per risk type. To come to an overall appreciation of the risk profile, the management has aggregated the risk profile per risk type and concluded that KBC Insurance NV has a medium overall risk profile. Furthermore, the discussion revealed that no large changes to the risk profile of KBC Insurance NV occurred in 2017. Compared to last year the overall risk appetite was lowered. Several projects were set up to reduce operational risk in order to return within the risk appetite. This resulted in a decrease of the assessment of operational risk. Significant effort will continue to be invested throughout the next years, with the expectation that operational risk will return within

its limit when the ongoing projects are implemented. Overall, as well as for each individual risk type except operational risk, KBC Insurance NV remains within its risk appetite.

C.1 Underwriting risk

Insurance risk

Insurance risk is the risk that future claims and benefits cannot be covered by the premium and investment income. Or, the insurance liabilities are not sufficient because the assumptions made and used in determining the best estimate liability differ from the future expenses, claims and benefits.

Insurance risk can be seen both in the Life and Non-Life portfolios.

To reduce and contain the volatility of results, mitigating measures are used. Risk mitigating also helps to decrease the possible negative impact on value as an alternative for the capital requirement. Proper pricing, underwriting, reinsurance, claims management and diversification are the main mitigating actions for insurance risks. One of the most important elements of the risk profile is KBC Insurance NV's nature as a diversified retail insurer. As such, KBC Insurance NV can rely on a broad client, product and intermediary base to absorb risks at different levels. This is realised by:

- offering a full product range, including all important Life and Non-Life products;
- focusing on retail clients, providing services to a large number of private persons, SMEs and the self-employed;
- operating through tied agents, who deal exclusively with KBC Insurance NV. Hence, all policies clients serviced by a KBC agent are placed with KBC Insurance NV;
- being active in the full Belgian territory through a fine-meshed network, that also comprises the KBC bank branches.

These elements result in diversification, geographically as well as over a large number of clients, different branches and products.

KBC holds a solvency buffer to cover the risk that claims may exceed the available insurance provisions and to ensure its solidity. In order to comply with the requirements set by the regulator, solvency ratios are monitored on a monthly basis.

For Life business also the Value of New business (VNB)/Value of Business In force (VBI) are calculated which are both widely used industry standards to measure the profitability of the life insurance operations

Life risk

The products sold are insurance products, in cash or unit-linked contracts. For cash products, the investment risk is fully borne by the insurer. Unit-linked life insurance investments (Branch 23) are not dealt with here, since this activity does not entail any market risk for KBC.

The insurance risks involved are:

Mortality risk:

Mortality risk pertains to the (re)insurance obligation, such as endowment or term assurance policies, where a payment or payments are made in case of the policyholder's death during the term of the contract. An increase in mortality rates is applied to the obligations pertaining to mortality risk.

The required capital for this risk is calculated according to article 52 of the European delegated regulations 2015-35. It comes down to calculating the impact on basic own funds following an instantaneous permanent increase of 15% in the mortality rates used for the calculation of the best estimate.

Longevity risk:

Longevity risk is associated with the (re)insurance obligation where payments are made until the policyholder's death and where a decrease in mortality rates results in higher provisions.

The required capital for this risk is calculated as the change in own funds using a permanent decrease of mortality rates by 20%. The decrease in mortality rates is applied to those portfolios where payments are contingent on longevity risk.

Disability – morbidity risk:

Disability or morbidity risk is associated with all types of insurance compensating or reimbursing losses (for example loss of income, adverse changes in the best estimate of the liabilities) caused by changes in the disability or morbidity rates.

The required capital for this risk is calculated using an increase of 35% in disability rates over the next year and 25% in subsequent years, combined with a decrease in recovery rate of 20%.

Expense risk:

Expense risk is the risk that the cost of expenses is more than anticipated.

The required capital for this risk is calculated using a permanent increase in costs of 10% and an increase in the cost inflation of 1% per year. In case of policies with adjustable costs, realistic management actions are taken into account.

Lapse risk:

Lapse risk is the risk of losses (or adverse changes in the best estimates of the pertaining liabilities) due to higher or lower policy lapses that were not anticipated, changes to premium payments and surrenders.

The required capital for this risk is calculated as the maximum of the results in case of a permanent increase in lapse rates of 50%, a permanent decrease of 50% in lapse rates or a mass lapse event. The latter comes down to a lapse of 70% of the insurance policies in collective pension funds or 40% of the remaining insurance policies. The mass lapse is only applied to portfolios where this leads to a higher best estimate.

The required capital for mass lapse is reduced by the recoverables expected from reinsurance.

Revision risk:

Revision risk is the potential negative deviation from the expected value of an insurance contract or a portfolio thereof due to unexpected revisions of claims. Only to be applied to annuities where the amount of the annuity may be revised during the next year.

Life catastrophe risk:

Catastrophe risk arising from extreme events which are not covered by the other life insurance risks, such as the pandemic threat of bird flu or accidental events.

The required capital for this risk is calculated using 1.5 per mille increase in mortality rates for the (re)insurance obligations where the increase in mortality rates leads to an increase in technical provisions.

Non-life Insurance risk

The Non-life insurance risks can be divided into two main types:

Catastrophe risks and non-catastrophe risks. Non-life non-catastrophe risks cover the premium risk, reserve risk and lapse risk related to non-life insurance contracts.

The overall underwriting policy of KBC Insurance NV is guided by the principle of ‘profitable’ growth. This principle is reflected in the risk appetite statement, in the objectives set on growth and profitability in the annual planning cycle (APC) as well as in the underwriting process and procedures.

To achieve its objectives, KBC Insurance NV mainly aims at the segments of private persons, the self-employed and small enterprises (retail + Small to Medium Enterprises (SME)). Underwriting is selective and based on the combination client, sector and risk profile, with specific attention on the gravity risk.

KBC strives for a balanced proportion between its retail and SME portfolio on the one hand and its midcap and corporate portfolio on the other.

KBC Insurance NV is a multi-line insurer who is not active in the lines of business railway rolling stock, aircraft, ships (sea, lake and river and canal vessels), aircraft liability and liability for ships (sea, lake and river and canal vessels). Neither is KBC active in credit and surety ship insurance and it takes a reserved position in markets dominated by niche players such as a number of specific professional liability insurances.

Taking also into account:

- the stable and low combined ratio of KBC Insurance NV (88.5% at the end of 2017, 92.4% at the end of 2016);
- the limitation of the volatility of the technical result by the reinsurance cover bought;
- KBC’s nature as a diversified retail insurer as described above.

It is concluded that KBC Insurance NV has a low risk profile for non-life insurance risk.

Health Insurance risk

Health insurance is a Solvency II-specific definition. See Chapter D - Internal_segmentation

The Health insurance portfolio can be divided into two main product types as is shown in the next two figures.

KBC Internal Branch		Solvency II Lines of Business				
		Health SLT		Health NSLT		
		Health Ins.	Annuities from Non-life contracts	Medical Expenses	Income Protection	Worker's compensation
Guaranteed Income - Ind.	Pre-claim	x				
	Post-claim	x				
Guaranteed Income - Coll.	Pre-claim				x	
	Post-claim	x				
Hospitalisation - Ind.	Pre-claim					
	Post-claim			x		
Hospitalisation - Coll.	Pre-claim			x		

Post-claim		x

Figure 5 Health managed by Life

KBC Internal Branch		Solvency II Lines of Business				
		Health SLT		Health NSLT		
		Health Ins.	Annuities from Non-life contracts	Medical Expenses	Income Protection	Worker's compensation
Accident	Pre-claim			x	x	
	Post-claim			x	x	
Worker's compensation	Pre-claim					x
	Post-claim					x
Worker's compensation annuities	Pre-claim					
	Post-claim		x			

Figure 6 Health managed by Non-life

Health SLT ('similar to life techniques') and Health NSLT ('non similar to life techniques').

The SLT Health Risk

This risk is applicable to the SLT Health portfolio.

The required capital of this risk is scenario-based. The scenarios are similar to the scenarios that are used to calculate the Life insurance risk.

Mortality Risk

Mortality risk pertains to the (re)insurance obligation, such as endowment or term assurance policies, where a payment or payments are made in case of the policyholder's death during the term of the contract. An increase in mortality rates is applied to the obligations pertaining to mortality risk.

The required capital for this risk is calculated based on the impact on basic own funds following an instantaneous permanent increase of 15% in the mortality rates used for the calculation of the best estimate (for all ages and each policy).

Longevity risk:

Longevity risk is associated with the (re)insurance obligation where payments are made until the policyholder's death and where a decrease in mortality rates results in higher provisions.

The required capital for this risk is calculated as the change in own funds using a permanent decrease of mortality rates by 20%. The decrease in mortality rates is applied to those portfolios where payments are contingent on longevity risk.

Disability – morbidity risk:

Disability or morbidity risk is the main risk of the SLT Health portfolio. It is associated with all types of insurance compensating or reimbursing losses (for example loss of income, adverse changes in the best estimate of the liabilities) caused by changes in the disability or morbidity rates.

The required capital for this risk is calculated using an increase of 35% in disability rates over the next year and 25% in subsequent years, combined with a decrease in recovery rate of 20%.

Expense risk:

Expense risk is the risk that the cost of expenses is more than anticipated.

The required capital for this risk is calculated using a permanent increase in costs of 10% and an increase in the cost inflation of 1% per year. In case of policies with adjustable costs, realistic management actions are taken into account.

Lapse risk:

Lapse risk is the risk of losses (or adverse changes in the best estimates of the pertaining liabilities) due to higher or lower policy lapses that were not anticipated, changes to premium payments and surrenders.

The required capital for this risk is calculated as the maximum of the results in case of a permanent increase in lapse rates of 50%, a permanent decrease of 50% in lapse rates or a mass lapse event. The latter comes down to a lapse of 70% of the insurance policies in collective pension funds or 40% of the remaining insurance policies. The mass lapse is only applied to portfolios where this leads to a higher best estimate, which is the case for the SLT Health portfolio.

The required capital for mass lapse is reduced by the recoverables expected from reinsurance.

The NSLT Health Risk

Premium Risk:

The premium risk is the risk that the premium that will be earned next year will not be enough to cover all liabilities resulting from claims in this portfolio, due for instance to the fact that the number of claims will be higher than expected (frequency problem) or the severity of the claims will be higher than expected (severity problem).

The required capital of the premium risk is calculated over the maximum of the expected written premium of the next year and the written premium of the current year.

Reserve risk:

The reserve risk is the risk that the liabilities stemming from claims, which have occurred in the past, but have still to be finally settled, will turn out to be more expensive than expected.

Health catastrophe risk:

Income protection

The required capital is calculated for policies for which an increase in mortality rates or morbidity rates or disability rates leads to an increase in the best estimate.

There are three scenarios which are calculated for all the SLT and NSLT Health portfolios.

Scenario 1 Mass accident

This scenario comprises the following elements: an accident takes place during a major public event. The risk is that 10% of the attendees are killed, 1.5% are disabled permanently, 5% are disabled for ten years, 13.5% are disabled for one year and 30% of the attendees need medical attention.

Scenario 2 Concentration accident

This scenario comprises the following elements: most of the insured of KBC are at the same location. The risk is that 10% of the attendees are killed, 1.5% are disabled permanently, 5% are disabled for ten years, 13.5% are disabled for one year and 30% of the attendees need medical attention.

Scenario 3 Pandemic scenario

This scenario comprises the following elements: 1% of those affected must be hospitalised and 20% need to see a local practitioner.

An important risk for KBC Insurance NV is posed by the Health Insurance products with ageing reserves. For health insurance products, the risk premium increases significantly with age. To keep the premiums affordable to the client, a fixed premium is charged instead of the actual risk premium. At younger ages, this fixed premium is higher than the risk premium and the excess premium is used to build up ageing reserves. At higher ages, the increasing premium is paid partially from this reserve. The calculation of the ageing reserve takes into account the expected evolution of numerous parameters, such as the costs of hospitalisation and care for the elderly, claims frequency, mortality rate, lapses, yield curve, …. The evolution of these parameters is very uncertain, and the term of the products is very long. Hence, small parameter changes can have a very big effect.

Reinsurance

The insurance portfolios are protected against the impact of large claims or the accumulation of losses due, for instance, to a concentration of insured risks by means of reinsurance. We divide these reinsurance programmes into three main groups, i.e., property insurance, liability insurance and personal insurance, and we re-evaluate and renegotiate them every year.

The reinsurance program adequately covers KBC Insurance NV's need for protection against adverse claims experience and complies with the maximum retention limits framework which has been decided upon by KBC group's insurance risk committee.

Most of our reinsurance contracts are concluded on a non-proportional basis, which provides cover against the impact of large claims or loss events. The independent insurance risk management function is also responsible for advising on the restructuring of the reinsurance programmes. This approach has resulted in the optimisation of the retention of the KBC group, particularly in respect of its exposure to natural catastrophe risk, but also in respect of other lines of business.

We are convinced that the reinsurance program of KBC Insurance NV is appropriate. The highest risk is that something that is excluded in the reinsurance contract will be insured in the direct policy. The process to be followed in case of product development or product change, e.g., the New and Active Product Process, mitigate this risk. For an adaptation of the conditions in a specific policy, stringent acceptation rules and competence levels for deciding and executing this exist, but human error can never be excluded.

To protect KBC Insurance NV from important changes in loss ratio due to an exceptionally high number of medium and large claims, a multi-line program was subscribed for the period 2013-2015. This program was renewed for 2016 and 2017.

C.2 Market risk

Market risk is the risk of potential losses due to adverse movements in financial market variables. Market risk exposure can be measured by the impact of the (adverse) movements in the financial variables.

For more details see: https://www.kbc.com, for the:

'Solvency & Financial Condition Report of KBC Insurance Group 2017'.

Interest rate risk

One of the most important risks for insurance companies in the current economic low yield environment is interest rate risk.

The negative impact of low yields on the available capital is rather straightforward, given the longer duration of the liabilities versus the assets and the increased impact of the convexity effect[3] following from these persistent low yields.

The main technique used to measure interest rate risks is the 10 BPV (Base Point Value) method, which measures the extent to which the value of the portfolio would change if interest rates were to go up by ten basis points across the entire swap curve (negative figures indicate a decrease in the value of the portfolio). We also use other techniques such as gap analysis, the duration approach, scenario analysis and stress testing (both from a regulatory capital perspective and from a net income perspective).

The evolution of the Base Point Value of KBC Insurance NV during 2017 is partly due to changes in the risk-free interest rates. Other changes are due to a methodological change in modelling of mortgages and investment strategy. A further (relatively small) change of the BPV was driven by portfolio evolution.

The non-unit-linked life activities (Branch 21) combine a guaranteed interest rate with a discretionary participation feature (DPF) fixed by the insurer. The main risks to which the insurer is exposed as a result of such activities are a low-interest-rate risk (the risk that return on investments will drop below the guaranteed level) and a risk that the investment return will not be sufficient to give customers a competitive profit-sharing rate. The risk of low interest rates is managed via a cash-flow-matching policy, which is applied to that portion of the life insurance portfolios covered by fixed-income securities. Unit-linked life insurance investments (Branch 23) are not included here, since this activity does not entail any market risk for KBC.

Asset mix

The investment strategy was updated at the end of 2015, and the results of the implementation can be seen in the asset mix evolution throughout 2016 and 2017. The share of investments in bonds slightly

[3] The present value of fixed-interest-rate-sensitive cash flows does not react linearly on interest rate changes. The lower the interest rate the larger the effect on present value of an absolute interest rate change. This effect is called interest rate convexity.

increased in 2017. The Life Other portfolio consists of pension liabilities, health insurance, and funeral and long-term care reserves. These liabilities do in general have a long maturity profile and are mainly hedged with fixed income investments. Additional investments were made in sovereign bonds to hedge the interest rate gap of these products. The rating distribution of the bonds portfolio remains stable, as can be seen in Table 4

	31/12/2016		31/12/2017	
Rating	market value		market value	
AAA	1546	8%	1375	8%
AA	9108	49%	8438	49%
A	3661	20%	3078	18%
BBB	2761	15%	2649	15%
BB	281	2%	186	1%
B	0	0%	0	0%
CCC or lov	12	0%	0	0%
unrated	1344	7%	1480	9%
Total	18712	100%	17206	100%

Table 4 Rating distribution of the bond portfolio

The country distribution of the sovereign bond portfolio remained relatively stable. An increased diversification in in euro-zone government bonds can be noted: exposure on Belgium remains stable, while the position in French bonds was decreased.

Sovereign Bonds - Geographic Distribution	31-12-2016		31-12-2017	
Market Value - in EUR	Market Value	Proportion (%)	Market Value	Proportion (%)
Europe	**11.464**	**93%**	**10.543**	**93%**
Eurozone	**10.708**	**87%**	**10.059**	**89%**
Belgium	5.171	*42%*	4.885	*43%*
Germany	723	*6%*	760	*7%*
France	2.056	*17%*	1.637	*14%*
Italy	735	*6%*	695	*6%*
Luxembourg	136	*1%*	168	*1%*
Other Euro-zone	1.888	*15%*	1.914	*17%*
Other European countries	**755**	***6%***	**485**	***4%***
US	**78**	**1%**	**76**	**1%**
Rest of the world	**743**	**6%**	**727**	**6%**
Total	**12.284**	**100%**	**11.346**	**100%**

Table 5 Country distribution of the sovereign bond portfolio

KBC Insurance NV pursues a prudent policy with regard to currency exposure, essentially seeking to avoid currency risk. Foreign exchange exposures are hedged if material. Equity holdings in non-euro currencies that are part of the investment portfolio are not hedged and the volatility stemming from foreign exchange evolutions are seen as equity risk.

C.3 Credit risk

Credit risk is the potential negative deviation from the expected value of a financial instrument arising from the non-payment or non-performance by a contracting party (for instance a borrower), due to that party's insolvency, inability or lack of willingness to pay or perform, or to events or measures taken by the political or monetary authorities of a particular country (country risk). Credit risk thus encompasses default risk and country risk, but also includes migration risk, which is the risk for adverse changes in credit ratings.

We manage our credit risk at both the transactional and the portfolio level. Managing credit risk at the transactional level means that we have sound practices, processes and tools in place to identify and measure the risks before and after accepting individual credit exposures. Limits and delegations are set to determine the maximum credit exposure allowed and the level at which acceptance decisions are taken. Managing the risk at the portfolio level encompasses, inter alia, periodic measuring and analysing of risk embedded in the consolidated loan and investment portfolios and reporting on it, monitoring limit discipline, conducting stress tests under different scenarios and taking risk-mitigating measures.

For more details see: https://www.kbc.com, for the:

'Solvency & Financial Condition Report of KBC Insurance Group 2017.

C.4 Liquidity risk

Liquidity risk is the risk that an organisation will be unable to meet its payment obligations as they come due, without incurring unacceptable losses.

The principal objective of our liquidity management is to enable the core business activities of the group to continue to generate revenue, even under adverse circumstances.

The nature of liquidity risk of insurance entities is not comparable to that of banking entities, mainly because of the different structure of the asset/liability profile. Banking activities normally have to cope with assets that have longer durations than the corresponding liabilities. Insurance activities typically have assets that are shorter and much more liquid than the corresponding liabilities. Insurance liabilities are rather stable and illiquid.

KBC has developed a Liquidity Risk Management Framework for Insurance entities (LRMF-I). This should allow for an enhanced risk management practice including identification, measurement, reporting and response and follow-up on liquidity risk for Insurance entities.' For insurance entities, the distinction is made between liquidity risk of life and non-life insurance activities.

Non-Life liquidity risk

Within non-life insurance business, liquidity risk could arise if a catastrophe (e.g., a natural disaster) would take place leading to huge claims and, consequently, large cash demands. There are some reasons, however, why this risk exposure differs materially from the liquidity risk to which life insurance businesses

are exposed to. The cash outflows will typically take place over a longer time horizon (i.e., assessment of damage, legal procedures, etc.) and certain claims are covered by re-insurance contracts.

KBC's reinsurance policy states that sufficient claims payment clauses have to be negotiated to ensure that the risk related to a timing mismatch between claims' payments and reinsurance recoverable is restricted as much as possible. More specifically, reinsurance contracts should include provisions allowing to make a request for immediate claim payment for large losses outside the usual accounting periods ('cash loss' clauses). In order to follow up on these (remaining) risks, the (re)insurance exposure point risk will be assessed in the near future. Furthermore, the worst-case exposure to liquidity risk will be analysed including the impact of re-insurance versus the default of re-insurance counterparties under a specific scenario and the quantity and quality of the options to cover outflows in the above scenario (e.g., liquid asset buffer, liquidity lines received, etc.).

Life liquidity risk

Life business consists of long-term pension business and medium-term savings business. Life insurance business might be confronted with liquidity risk as a result of:

- changing market circumstances (e.g., movement in rates, competition, etc.) leading to a surge in early redemptions;
- changing regulatory environment (e.g., change in beneficial tax regime) leading clients to switch to other non-insurance products (market-wide scenario);
- an idiosyncratic scenario where clients question the insurance company's credit worthiness and build down their exposure;
- a combination of the above (combined scenario).

These scenarios would result in a mass lapse of the portfolio. In all of these scenarios, the insurance company should have an adequate liquidity buffer (cash, liquid assets, contingent credit lines, etc.) to cope with these cash outflows. Except for the idiosyncratic scenario, the time horizon in which the cash flows will take place, is expected to be rather long (i.e., longer than 1 month) hence decreasing the risk of not being able to meet the liabilities at an acceptable cost (e.g., as a result of a fire sale at high haircuts). The liquidity risk of life insurance activities will be assessed by an internal stress-test ratio as defined in the LRMF.

Especially in the case of KBC Insurance NV, clients do not benefit from a fiscal advantage in case of early surrender. Surrender risk is therefore partially mitigated through fiscal rules.

An insurance entity's liquidity is managed by matching cash flows and ensuring that sufficient investments are made in liquid assets, thereby guaranteeing that unexpectedly high lapses can be covered by selling or 'repo-ing' liquid assets. As a result, insurance entities are less sensitive to 'real' liquidity risk.

C.5 Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes and systems, human error or sudden external events, whether man-made or natural. Operational risks include non-financial risks such as information and compliance risks, but exclude business, strategic and reputational risks.

The operational risk profile is underpinned by means of a number of metrics covering different aspects of operational risk (people, processes and systems), combined with expert opinion on a number of qualitative

aspects. The aspects evaluated in determining the operational risk profile are required to keep the operational losses at a low level on the long term.

The indicators for an adequate number of people and adequately skilled people are based amongst others on the yearly employee survey . This gives an indication of part of the operational risk linked to people. This points to a low risk profile. A good score is also noted for control culture, reflecting the risk attitude of the management. Cyber resilience also scores in the green, pointing out the maturity of our governance with regard to cyber risks.

The level of change, indicating the degree to which business experiences process redesigns or other changes and associated elevated risks, points at a medium risk profile, as well as the number of incidents and length of downtime of critical systems.

Managing operational risk

We have a single, global framework for managing operational risk across the entire group.

The Group risk function is primarily responsible for defining the operational risk management framework. The development and implementation of this framework is supported by an extensive operational risk governance model covering all entities of the group.

In early 2016, a new Competence Centre for Operational Risk was set up following a review of the 'Three Lines of Defence' model. It sets the standards for managing and monitoring operational risks within the group and also includes the Competence Centre for Information Risk Management, which deals with cyber risk, among other things.

The main tasks of the Competence Centre for Operational Risk are to:

- plan and perform independent 'in-depth' challenges of internal controls on behalf of senior management;
- provide oversight and reasonable assurance on the effectiveness of controls executed to reduce operational risk;
- inform senior management and oversight committees on the operational risk profile;
- define the operational risk management framework and approach for the group;
- create an environment where risk specialists (in various areas, including information risk management, business continuity and disaster recovery, compliance, anti-fraud, legal, tax and accounting matters) can work together (setting priorities, using the same language and tools, uniform reporting, etc.). It is assisted by the local risk management units, which are likewise independent of the business.

The qualitative aspects assessed by expert judgment relate external evolutions and changes to KBC's business model that may entail operational risk.

Overall, the operational risk profile is considered to be medium, versus a low risk appetite. Drafting an action plan is difficult as the medium score of the risk profile is mainly the result of external factors and not so much of internal factors. Several projects however are already ongoing, at the local as well as at the BU and the group level. These projects will result in a decrease of the risk profile once they are finished.

Internal Control Environment

The strength of the internal control environment, based on a self-assessment by business and challenged by second-line functions, is stated in the Internal Control Statement (ICS).

The Non-Life insurance segment is well controlled and subject to limited improvements only. For Life insurance segment substantial improvements are required in domains with high degree of manual processes (mainly situated in the area of group insurances). Several actions were put in place during 2017 in order to tackle this issue.

This opinion is based on the evaluation of the opinions of the businesses and local Risk Department per process, the evaluation of the review by the Audit Department, as well as the evaluation of the controls in the domains covered by the Compliance Department.

C.6 Other material risks

Concentration risk

We monitor the largest risk concentrations via periodic and ad-hoc reports. Limits are in place at the borrower/guarantor, issuer or counterparty level, at the sector level and for specific activities or geographic areas. Moreover, we perform stress tests on certain types of credit, as well as on the full scope of credit risk.

We have the largest exposure in Belgian Government bonds (18% of total assets), French government bonds (9%) and KBC Group (5%) assets.

Business & strategic risk

Business risk is the risk arising from changes in external factors (the macroeconomic environment, regulations, client behaviour, etc.) that impact the demand for and/or profitability of our products and services.

Strategic risk is the risk due to not taking a strategic decision, taking a strategic decision that does not have the intended effect or not adequately implementing strategic decisions.

Business and strategic risks are assessed as part of the strategic planning process starting with a structured risk scan that identifies the top financial and non-financial risks. Exposure to the identified business and strategic risks is monitored on an ongoing basis. Besides the risk scan, business and strategic risks are continually monitored by means of risk signals being reported to top management. In addition, these risks are discussed during the aligned planning process and are quantified under different stress-test scenarios and long-term earnings assessments.

Under the pillar 2 approach to capital, business risk is incorporated by performing a one-year stress test on profit or loss.

Business risk is scored medium as a result of the qualitative assessment of our business model by the management and stays in line with Risk Appetite.

Over the coming years, our business model will be challenged by multiple factors, such as changing customer behaviour, the choice the customer has between different service channels and the rise of new technologies. Especially the level playing ground for 'traditional' insurance companies and FinTech-based companies leads to new challenges. Existing legislation will have to be adapted to take the new possibilities offered by the digital economy into account.

The business is preparing itself for those challenges by means of its new strategy and the implementation thereof through multiple projects. However, these decisions are rolled out, the new approach will have to

prove its effectiveness in practice. KBC Insurance NV also aims to limit its vulnerability to changes in the external environment by fostering diversity and flexibility in its business mix, client segments and distribution channels.

Reputational risk

Reputational risk is the risk arising from the negative perception on the part of clients, counterparties, shareholders, investors, debt-holders, market analysts, other relevant parties or regulators that can adversely affect a financial institution's ability to maintain existing, or establish new business relationships and to have continued access to sources of funding (for instance, through the interbank or securitisation markets).

Reputational risk is mostly a secondary or derivative risk since it is usually connected to and will materialise together with another risk. We refined the Reputational Risk Management Framework in 2017, in line with the KBC Risk Management Framework. The pro-active and re-active management of reputational risk is the responsibility of the business, supported by many specialist units (including Group Communication and Group Compliance). Under the pillar 2 approach to capital, the impact of reputational risk on the current business is covered in the first place by the capital charge for primary risks (including credit or operational risk).

C.7 Any other information

Sensitivity analyses and stress testing

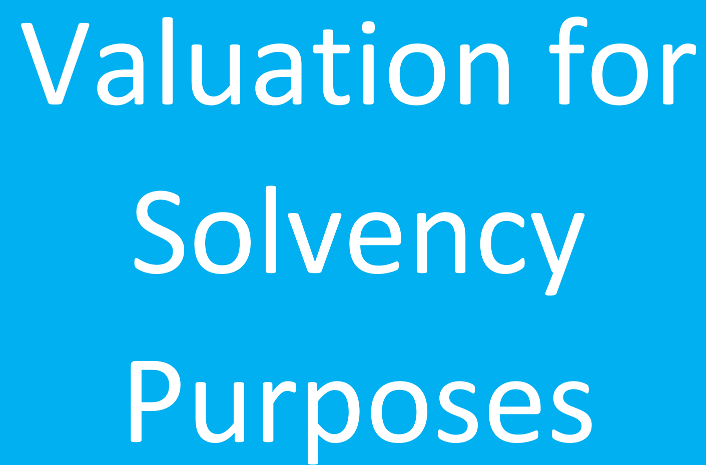
Risk-sensitivity and stress-testing exercises are set up to uncover risks that otherwise stay unidentified and also allow us to observe how risk measurements would evolve under stressed conditions. These sensitivity exercises are performed on a regular basis.

Sensitivity analysis reveals that the sensitivity of the Best Estimate to the interest rate curve is much higher than the sensitivity to the different non-economic parameters (such as mortality, longevity and lapses).

Stress testing is an important risk management tool that adds value both to strategic processes and to day-to-day risk management (risk identification, risk appetite, limit setting, etc.). As such, stress testing is an integral part of our risk management framework, and an important building block of the ORSA (Own Risk and Solvency Assessment).

Stress tests are initiated by the regulator (EIOPA[4] or local regulators) on a regular basis or are performed internally within the insurance group or at the local entity level. KBC also performs ad-hoc integrated stress tests to test its vulnerability for specific risks and potential adverse conditions that may arise.

[4] EIOPA: European Insurance and Occupational Pensions Authority


Valuation for
Solvency
Purposes

D. Valuation for Solvency Purposes

This chapter provides information about the balance items. The following table provides a qualitative and quantitative explanation for each material class of assets and liabilities of the significant differences between the valuation for solvency purposes and those used for their valuation in financial statements. The classes are grouped together when their values are immaterial under IFRS and Solvency II or when the principles to determine these values are equal. A description of how these values are determined, the bases, methods and main assumptions applied, can be found in the sections below. Note that these values are valued differently under BGAAP.

Valuation of the **assets** is calculated on the basis of the fair value. Section D.1 gives a description of the calculation of each material class of assets.
Valuation of the **technical provision** is calculated as the sum of the best estimate and the risk margin. The best estimate includes the intrinsic value and the time value of options and guarantees.
Section D.2 outlines the calculation of the different items of the technical provision.
Finally, in section D.3, the other liabilities are described.

Reconciliation Solvency II and IFRS balance sheet as at 31 December 2017:

(mln euros)	IFRS	Difference	Solvency II
Participations	698	523	1.221
Equities (excl participations)	1.344	-14	1.330
Bonds	16.381	859	17.240
Unit linked Assets	13.303	0	13.303
Cash, Loans and deposits	2.664	253	2.917
Technical Provisions recoverable	114	-12	101
Other Assets	654	318	972
Total Assets	35.157	1.928	37.085
Technical provisions - Non-Life (excl Health)	1.681	-318	1.363
Technical provisions - Life (excl. Index and Unit Linked and Health)	13.575	1.531	15.106
Technical provisions Index and Unit-Linked	13.370	-84	13.286
Technical provisions Health SLT	568	-115	452
Technical provisions Health NSLT	392	-131	261
Other liabilities	2.681	88	2.769
Total liabilities	32.268	970	33.238
Total assets minus total liabilities	2889		3847
Foreseeable dividends	-244		-244
Own shares			-203
Excess assets over liabilities (corrected for dividend and own shares)	**2.644**		**3.399**

Table 6 Simplified overview of assets and liabilities.

For more details on this table, see QRT S.02.01.02 and below in the following chapters.

IFRS parent shareholder's equity	2.644
Valuation differences between IFRS and SII	
of which: valuation difference participations	521
of which: valuation difference real estate at fair value (after tax)	62
of which: valuation difference fair value L&R (after tax)	208
of which: valuation difference fair value HTM bonds (after tax)	651
of which: valuation difference technical liabilities (after tax)	-671
of which: other	-16
Assets over liabilities SII, incl. VA	3.399
Tier 2 subordinated loan	500
SII available capital	3.899

Table 7 Reconciliation Excess assets over Liabilities under SII and IFRS.

D.1 Assets

SOLVENCY II VALUE

Goodwill

Goodwill is valued at zero according to *Delegated Regulation (EU) 2015/35 article 12*.

Deferred taxes

Deferred taxes, other than deferred tax assets arising from the carry-forward of unused tax credits and the carry-forward of unused tax losses, are valued on the basis of the difference between the Solvency II values and the values ascribed to assets and liabilities as recognised and valued for tax purposes, according to Delegated Regulation (EU) 2015/35 article 15.

Bonds, Equity Instruments and Loans & Mortgages

For Solvency II purpose bonds, equity instruments and loans & mortgages are valued at the amount for which they could be exchanged between knowledgeable willing parties in an arm's length transaction. This definition is in line with the IFRS definition of fair value.

KBC Insurance NV defines 'fair value' as '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'. Fair value is not the amount that an entity would receive or pay in a forced transaction, involuntary liquidation or distress sale. A deviation from IFRS is however applicable for the valuation of financial liabilities, as Solvency II explicitly imposes that the fair value may not reflect the own credit risk, according to Delegated Regulation (EU) 2015/35 article 14.

All internal valuation models used at KBC are validated by an independent Risk Validation Unit. In addition, the Executive Committee has appointed a Group Valuation Committee (GVC) to ensure that KBC Insurance NV and its entities meet all the legal requirements for measuring financial assets and liabilities at fair value. The GVC monitors consistent implementation of the KBC Valuation Framework, which consists of various

guidelines, including the Group Market Value Adjustments Policy and the Group Parameter Review Policy. The GVC meets at least twice a quarter to approve significant changes in valuation methods including, but not limited to, models, market data and inputs or deviations from group policies for financial assets and liabilities measured at fair value. The committee is made up of members from Finance, Risk Management and the Middle Office. Valuation uncertainty measurements are made and reported to the GVC every quarter. Lastly, certain fair values generated by valuation models are challenged by a team set up specifically for this purpose.

Market value adjustments are recognised on all positions that are measured at fair value to cover close-out costs, adjustments for less liquid positions or markets, mark-to-model-related valuation adjustments, counterparty risk and funding costs. Credit value adjustments (CVAs) are used when measuring derivatives to ensure that the market value of the derivatives is adjusted to reflect the credit risk of the counterparty. In making this adjustment, both the mark-to-market value of the contract and its expected future fair value are taken into account. These valuations are weighted based on the counterparty credit risk that is determined using a quoted credit default swap (CDS) spread, or, if there is no such spread, on the counterparty credit risk that is derived from bonds whose issuers are similar to the derivative counterparty in terms of rating, sector and geographical location. A funding value adjustment (FVA) is a correction made to the fair value of uncollateralised derivatives in order to ensure that the (future) funding costs or income attached to entering into and hedging such instruments are factored in when measuring the value of the instruments.

The IAS 39 fair value hierarchy prioritises the valuation techniques and the respective inputs into three levels.

Level 1: Fair value based on quoted prices in active markets accessible to KBC Insurance NV
The fair value hierarchy gives the highest priority to 'level 1 inputs'. This means that, when there is an active market, quoted prices have to be used to measure the financial assets or liabilities at fair value. Level 1 inputs are prices that are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and that are quoted in active markets accessible to KBC. They represent actual and regularly occurring market transactions on an arm's length basis. The fair value measurement of financial instruments with quoted prices is based on a mark-to-market valuation derived from currently available transaction prices. No valuation technique (model) is involved.

If there are no price quotations available, the reporting entity establishes fair value using a model based on observable or unobservable inputs. The use of observable inputs needs to be maximised, whereas the use of unobservable inputs has to be minimised.

Level 2: Fair value based on observable market data
Observable inputs are also referred to as 'level 2 inputs' and reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Observable inputs reflect an active market. Examples of observable inputs are the risk-free rate, exchange rates, stock prices and implied volatility. Valuation techniques based on observable inputs include discounted cash flow analysis, reference to the current or recent fair value of a similar instrument, or third-party pricing, provided that the third-party price is in line with alternative observable market data.

Level 3: Fair value not based on observable market data
Unobservable inputs are also referred to as 'level 3 inputs' and reflect the reporting entity's own assumptions that market participants would use in pricing the asset or liability including assumptions regarding the risks involved. Unobservable inputs reflect a market that is not active. For example, proxies and correlation factors can be considered to be unobservable in the market.

<u>Assets held for index-linked and unit-linked funds</u>

Assets held for index-linked and unit-linked contracts, classified in line of business 31, Branch 23, as defined in Annex I of Delegated Regulation (EU) 2015/35.

<u>Deposits other than cash equivalents</u>

Deposits other than cash equivalents are measured at fair value. The same principles are applied as discussed for ‘Bonds and Loans & mortgages’.

Own shares

This is the total amount of own shares held directly by the group, also referred to as Treasury shares under IFRS.

IFRS value

To determine the IFRS value, reference can be made to the IFRS valuation rules applicable within KBC as included in the Annual Report of KBC Group, ‘Notes on the accounting policies’.

See: https://www.kbc.com, for the Annual Report of KBC Group 2017

Goodwill

Goodwill is defined as any excess of the cost of the acquisition over the acquirer’s interest in the fair value of the identifiable assets acquired and liabilities and contingent liabilities assumed at the date of acquisition. It is recognised as an intangible asset and is carried at cost less impairment losses. Goodwill is not amortised, but is tested for impairment at least once a year or if there is either internal or external evidence for doing so. An impairment loss is recognised if the carrying amount of the cash-generating unit to which the goodwill belongs exceeds its recoverable amount. Impairment losses on goodwill cannot be reversed. For each new business combination, KBC has to choose whether to measure minority interests at fair value or as their proportionate share of the acquirer’s net identifiable assets. This choice determines the amount of goodwill recognised.

Deferred taxes

Deferred tax assets are recognised for all deductible temporary differences between the carrying amount of assets and liabilities and their tax base, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised.

Bonds, Equity Instruments and Loans & Mortgages

All financial assets and liabilities – including derivatives – must be recognised in the balance sheet according to the IAS 39 classification system. Each classification is subject to specific measurement rules.

The IAS 39 classifications are as follows:
Loans and receivables (L&R). These include all non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These financial assets are measured at amortised cost minus impairments.

Held-to-maturity assets (HTM). These are all non-derivative financial assets with a fixed maturity and fixed or determinable payments that KBC intends and is able to hold to maturity. Similar to the L&R category, these assets are also measured at amortised cost minus impairments.

Financial assets at fair value through profit or loss. This category includes held-for-trading (HFT) assets and any other financial assets designated at fair value through profit or loss (FIFV). Held-for-trading assets are assets held for the purpose of selling them in the short term or assets that are part of a portfolio of assets held for trading purposes. All derivatives with a positive replacement value are considered to be held for trading unless they are designated and effective hedging instruments. Other financial assets initially recognised at fair value through profit or loss are measured in the same way as held-for-trading assets. KBC may use the fair value option when doing so results in more relevant information, because it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as ‘an

accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases. The fair value option may also be used for financial assets with embedded derivatives.

Available-for-sale assets (AFS). These are all non-derivative financial assets that do not come under one of the above classifications. These assets are measured at fair value, with all fair value changes being recognised in equity until the assets are sold or until there is an impairment in value. In this case, the cumulative revaluation gain or loss will be recognised in income for the financial year.

Held-for-trading liabilities. These are liabilities held with the intention of repurchasing them in the short term. All derivatives with a negative replacement value are also considered to be held for trading unless they are designated and effective hedging instruments. These liabilities are measured at fair value, with any fair value changes reported in profit or loss.

Financial liabilities designated at fair value through profit or loss (FIFV). These are measured in the same way as held-for-trading liabilities. This fair value option may be used under the same conditions as FIFV assets. Additionally, this classification may be used to account for (unbundled) deposit components (i.e., financial liabilities not including a discretionary participation feature) as defined in IFRS 4.

Other financial liabilities. These are all other non-derivative financial liabilities that are not classified under one of the two liability classifications above. They are measured at amortised cost.

Hedging derivatives. These are derivatives used for hedging purposes.

Assets held for index-linked and unit-linked funds

Assets held for index-linked and unit-linked funds are recognised as investment contracts in Financial Assets designated at fair value through profit or loss (FIFV).

Deposits other than cash equivalents

Deposits other than cash equivalents are measured at amortised cost.

Own shares

If an entity reacquires its own equity instruments, those instruments ('treasury shares') are not to be recognised as an asset on the balance sheet but should be deducted from equity.

D.2 Technical provisions

Technical Provisions and their segmentation under the Solvency II regulatory framework.

Insurance is the transfer of risk from the policyholder to the insurer. Policyholders pay a premium to protect themselves against future risks, while the insurance companies can add value by diversification, management of the risk and investment return.

Technical provisions represent the amount required to fulfil the insurance obligations and settle all expected commitments to policyholders and other beneficiaries arising over the lifetime of the insurer's portfolio of insurance contracts. It should be noted that these insurance obligations not only comprise the payments for the benefit of the insured party, but more in general are defined as 'all cash flows needed to service the contract'. So claims handling expenses internal and external to the insurance company, IT costs, personnel salaries, etc. are included in the amount of the technical provisions.

From a regulatory point of view, the technical provisions are split up in different segmentations:

- **Segmentation according to technique used**

Segmentation according to the technique used to calculate the amount of the technical provisions: The insurance liabilities have to be segmented between life and non-life insurance obligations. However, when applying this segmentation, the so-called 'substance over form' prevails: the segmentation principles that are proposed are not based on the legal classes of insurance activities. Indeed, the segmentation should be based on the nature of the risk underlying the contract (substance), rather than on the legal form of the contract (form).
Under the assumption that the valuation technique used to calculate the technical provisions is an indicator for the nature of the liabilities, 'the substance', the life and non-life insurance obligations can be defined as follows:

- **Life insurance obligations**:
  Insurance obligations which are pursued on a similar technical basis to that of life insurance, even if they are non-life insurance from a legal perspective.
- **Non-life insurance obligations**:
  Insurance obligations which are not pursued on a similar technical basis to that of life insurance, even if they are life insurance from a legal perspective.

Also, **health[5] insurance** liabilities need to be segmented between these life and non-life obligations based on the actuarial techniques used. This leads to the two sub-levels **Health SLT** ('Similar to Life Techniques') and **Health NSLT** ('Non-Similar to Life Techniques').
Sometimes a certain type of contract covers risks which bear both SLT and NSLT characteristics. In that case, the (re)insurance company needs to unbundle these contracts, so as to be able to assign the different parts to the appropriate segment defined by the Solvency II regulatory framework.

In this document, whenever we mention the legal definition of life/non-life (i.e., Branches 01-18 versus Branches 21-26) we will use the term life or non-life activities.

- **Segmentation according to regulatory defined 'Lines of Business'**

For reporting purposes, the regulator defines 36 so-called lines of business. Each (re)insurance company should, as a minimum, split up their technical provisions into these lines of business. If needed, technical provisions on certain types of contracts must be unbundled, in order to assign the underlying obligations to the right line of business.

[5] Health insurance is a Solvency II-specific definition. It means an insurance obligation which covers one or both of the following:

- The provision of medical treatment or care including preventive or curative medical treatment or care due to illness accident or infirmity, or financial compensation for such treatment care;
- Financial compensation arising from illness, accident, disability or infirmity.

No.	Solvency II Line of Business (LoB) name	Category
1	Medical expense insurance	Health NSLT
2	Income protection insurance	Health NSLT
3	Workers' compensation insurance	Health NSLT
4	Motor vehicle liability insurance	Non-Life
5	Other motor insurance	Non-Life
6	Marine, aviation and transport insurance	Non-Life
7	Fire and other damage to property insurance	Non-Life
8	General liability insurance	Non-Life
9	Credit and surety ship insurance	Non-Life
10	Legal expenses insurance	Non-Life
11	Assistance	Non-Life
12	Miscellaneous financial loss	Non-Life
13 - 15	Proportional reinsurance obligations which relate to the obligations included in LoBs 1 to 3 respectively	Health NSLT
16-24	Proportional reinsurance obligations which relate to the obligations included in LoBs 4 to 12 respectively	Non-Life
25	Non-proportional health reinsurance	Health NSLT
26	Non-proportional casualty reinsurance	Non-Life
27	Non-proportional marine, aviation and transport reinsurance	Non-Life
28	Non-proportional property reinsurance	Non-Life
29	Health insurance	Health SLT
30	Insurance with profit participation	Life
31	Index-linked and unit-linked insurance	Life
32	Other life insurance	Life
33	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Health SLT
34	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	Life
35	Health reinsurance	Health SLT
36	Life reinsurance	Life

Table 8 Regulatory defined lines of business and assignment to Life, Non-Life, SLT Health or NSLT Health.

The aim of the segmentation under Solvency II is to achieve an accurate valuation. For this reason the Solvency II regulatory framework states that it may be appropriate to further break down the prescribed Solvency II Lines of Business into so-called ‘Homogeneous Risk Groups’.

A homogeneous risk group is a set of (re)insurance obligations which are managed together and which have similar risk characteristics in terms of, for example, underwriting policy, risk profile of policyholders, expected policyholder behaviour, product features (including guarantees), etc. The risks in each group should be sufficiently similar to allow for a reliable valuation of technical provisions, including a meaningful statistical analysis. Determination of the homogenous risk groups is at the discretion of the (re)insurance company and can be very diverse.

- **Internal segmentation within KBC Insurance NV**

Within KBC Insurance NV, Life and Non-life activities are parts of different directorates. This split-up doesn’t entirely follow the legal or Solvency II segmentation. The internal segmentation follows the legal definition

of life and non-life, with the exception of Branch 02 (illness), which is legally non-life but internally handled by the life directorate.

When referring to the internal segmentation life/non-life within KBC Insurance NV, the terms managed by life and non-life will be used.

Valuation of the technical provisions

The technical provisions represent the biggest part of the liabilities on the balance of a (re)insurance company. For this reason an accurate calculation of these technical provisions (Life, Non-Life, Health) is of utmost importance, and forms the cornerstone of the calculation methods prescribed by the Solvency II regulatory framework.

Next follows a preview of the methodological calculation requirements.

With respect to the valuation of technical provisions, the main principle of the Solvency II regulatory framework is the definition of the 'market-consistent valuation':

'The value of technical provisions shall correspond to the current amount insurance and reinsurance undertakings would have to pay if they were to transfer their insurance and reinsurance obligations immediately to another insurance or reinsurance undertaking'.

Further to this principle, the value of the technical provisions must be consistent with:

- the principle of **transfer value**: 'the current amount (re)insurance undertakings would have to pay if they were to transfer their (re)insurance obligations immediately to another (re)insurance undertaking';
- the principle of **market-consistent value**: 'the calculation shall make use of and be consistent with information provided by the financial markets and generally available data on underwriting risks'. This market-consistent value for insurance liabilities is different from current local accounting principles.

Best estimate and risk margin

In the majority of cases, the value of insurance liabilities is not available in the information provided by the financial markets. In this case, the value of the insurance obligations must be valued 'Mark to Model'.

The Solvency II regulatory framework requires calculating the technical provision as the sum of the best estimate and the risk margin. The intrinsic value and the time value of options and guarantees (TVOG) are included in the best estimate.

- The **best estimate** corresponds to the probability-weighted average of future cash flows, taking into account the time value of money, using the relevant risk-free interest rate term structure.

- The **risk margin** is calculated by determining the cost of providing an amount of eligible own funds equal to the Solvency Capital Requirement necessary to support the insurance and reinsurance obligations over the lifetime thereof.

- The calculation of the **Time Value of Options and Guarantees** uses stochastic techniques with respect to the interest scenarios.

However, where future cash flows associated with insurance obligations can be replicated reliably using financial instruments for which a reliable market value is observable, the value of technical provisions associated with those future cash flows shall be determined 'as a whole' based on the market value of those financial instruments. In this case, separate calculations of the best estimate and the risk margin are not required. In practice, this principle applies, for example, to the value of the Unit-Linked funds in Branch 23.

Pre-claim and post-claim provisions

Specifically for non-Life and Health NSLT provisions, the Solvency II regulatory framework requires calculating the best estimate separately for the premium provisions and for the provisions for claims outstanding:

- The **premium provisions** relate to claim events that still have to occur (= 'pre-claim provision'), after the valuation date and during the remaining coverage period of existing policies held by the undertaking.
- The **provisions for claims outstanding** relate to claim events that have already occurred (= 'post-claim provision') but that are not settled yet, regardless of whether the claims arising from these events have been reported or not.

Graphically:

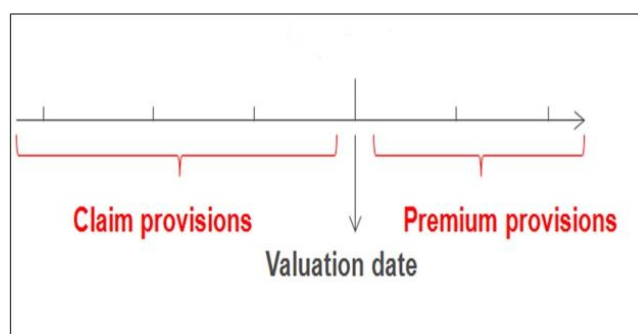


Figure 7 Graphical representation of the pre-claim and post-claim provisions

The best estimate shall be calculated gross of reinsurance, i.e., without deduction of the amounts recoverable from reinsurance contracts and special purpose vehicles. The amounts recoverable shall be calculated separately. The technical provisions net of reinsurance recoverables are referred to as '**Net technical provisions**'.

Discounting of cash flows

As mentioned above, the calculation of the best estimate of the insurance obligations must take into account the time value of money, using the relevant risk-free interest rate term structure.

Relevant risk-free interest rate term structure

The term structure used for discounting the cash flows is prescribed by the Solvency II regulatory framework.

This curve is derived on the basis of interest rate swap rates for interest rates for subject currency. This curve is adjusted to take account for credit risk.

The regulator also leaves the possibility to apply a so-called ‘volatility adjustment’. This adjustment is calculated based on the spreads applicable to the bonds on the asset side: if the spread on the bonds causes the asset value to fluctuate, this fluctuation can be mirrored in the liability valuation too.

Discounting of the cash flows

The cash flows are discounted according to documented methods, where

$$Discounted\ CF = \sum_t \frac{CF(t)}{\left(1+r_t\right)^{t}}$$ Equation 1

With r_t being the interest rate that corresponds to the term point t of the interest rate curve, and t the time between the valuation point, and the projected timing of the cash flow.

Methods for intra- and extrapolation of the interest rate curve and calculation of t are set according to documented conventions.

Risk Margin

Next to the Best Estimate described in the previous section, the technical provisions shall also include a risk margin (RM). The latter is determined in such a way that the value of the technical provisions is equivalent to the amount that insurance and reinsurance undertakings would be expected to require in order to take over and meet the insurance and reinsurance obligations (transfer value). Indeed: a third party taking over a portfolio of insurance liabilities would require a take-over price higher than the best estimate. Also, some compensation for the uncertainty inherent to insurance obligations would be required to be compensated for. This compensation is represented by the risk margin.

In practice, and as stipulated by the solvency II regulatory framework, the risk margin is calculated according to a so-called ‘Cost of Capital method’:

$$\mathrm{RM} = \mathrm{CoC} * \sum_{t\geq 0} \frac{\mathrm{SCR}_{\mathrm{RU}}(t)}{(1+r_{t+1})^{t+1}}$$ Equation 2

Where:

$SCR_{RU}(t)$:	SCR for year t as calculated for the reference undertaking
CoC:	Cost-of-Capital rate which currently equals 6% (set by the regulator)
r_t	Risk-free rate over period t, not including a volatility adjustment

The risk margin has to be calculated for life and non-life activities. The total risk margin is the sum of the risk margin for the life activities and the risk margin of the non-life activities.

D.3 Other liabilities

SOLVENCY II VALUE

Deferred taxes

Deferred taxes liabilities, unlike deferred tax assets arising from the carry-forward of unused tax credits and the carry-forward of unused tax losses, are valued on the basis of the difference between the Solvency II values and the values ascribed to assets and liabilities as recognised and valued for tax purposes according to Delegated Regulation (EU) 2015/35 article 15.

IFRS VALUE

To determine the IFRS value, reference can be made to the IFRS valuation rules applicable within KBC as included in the Annual Report of KBC Group – Notes on the accounting policies.

See: https://www.kbc.com, for the Annual Report of KBC Group 2017.

Deferred taxes

Deferred tax liabilities are recognised for all taxable temporary differences between the carrying amount of an asset or liability and its tax base. They are measured using the tax rates in effect on realisation of the assets or settlement of the liabilities to which they relate.

Capital
Management

E. Capital Management

E.1 Own funds

Eligible own funds

(mln euros)	Tier 1	Tier 2	Tier 3
	2016 | 2017	2016 | 2017	2016 | 2017
Ordinary share capital (gross of own shares)	65 | 65	-	-
Share premium account related to ordinary share capital	1 086 | 1 086	-	-
Reconciliation reserve	1 968 | 2 248	-	-
Subordinated liabilities	-	500 | 500	-

Table 9 Eligible own funds 2016 and 2017, per tier.

Tier 1: available and eligible capital comprises only unrestricted capital.

(mln euros)	Tier 1	Tier 2	Tier 3
	2016 | 2017	2016 | 2017	2016 | 2017
Total available own funds to meet the SCR	3.119 | 3.399	500 | 500	-
Total available own funds to meet the MCR	3.119 | 3.399	500 | 500	-
Total eligible own funds to meet the SCR	3.119 | 3.399	500 | 500	-
Total eligible own funds to meet the MCR	3.119 | 3.399	160 | 162	-

Table 10 Total own funds per tier to cover SCR and MCR at the end of 2016 and 2017.

For more details see the QRTs: S.22.01.21 and S.23.01.21, which are published separately on the website: https://www.kbc.com

Solvency II regulations require the (re)insurance companies to classify own-fund items into three tiers. The classification of those items in general depends upon whether they are basic own-fund or ancillary own-fund items.

Tier 1: if the item is available, or can be called up on demand, to fully absorb losses on a going-concern basis, as well as in the case of winding- up (permanent availability).

Tier 2: if in the case of winding-up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations towards policy holders and beneficiaries of insurance and reinsurance contracts, have been met (subordination).

Tier 3: if basic own funds or ancillary own funds do not fall under (a) or (b).

Since not all financial resources provide full absorption of losses in the case of winding-up and on a going-concern basis, own-fund items are limited, but only to determine the solvency standing; there is no further restriction with respect to the internal capital management.

Overall capital management is administered at the Group level; we refer to the Group's Solvency and Financial Condition Report for more details.

No ancillary own funds are taken into account as these funds are not available.

The excess of assets over liabilities as calculated for solvency purposes, including the Volatility Adjustment at the end of 2016 was 3.628 million euros. By the end of 2017, this increased to 3.847 million euros. The Available Capital, 3.899 million euro, is calculated as shown in Table 11

(mln euros)	Solvency II	
Excess Assets over Liabilities		3.847
Subordinated liabilities	500	
Own shares	-203	
Foreseeable dividends	-244	
		53
Available Capital		3.899

Table 11 Available capital for SCR purposes.

E.2 Solvency Capital Requirement and Minimum Capital Requirement

Combined with the end-of-year 2017 SCR, the Available Capital from Table 11 leads to a Solvency II ratio of 217%.

The SCR is reported on a quarterly basis, whereas, on a non-quarterly basis, the SCR is calculated in order to check the outcome and test the tools and systems needed for these calculations.

The waterfall graph, Figure 8 shows the different SCRs per component and its corresponding amount.

The SCR can be calculated as the sum of the different components. KBC Insurance NV uses the following distinguishable components: SCR Market, SCR Counterparty, SCR Life, SCR Health and SCR Non-Life to calculate the Basic SCR (BSCR). Some of these components are grouped to improve the readability. Because there is some risk overlap, diversification reduces the Risk involved and the pertaining SCR. After calculating the Basic SCR, three components are needed to be able to calculate the SCR.

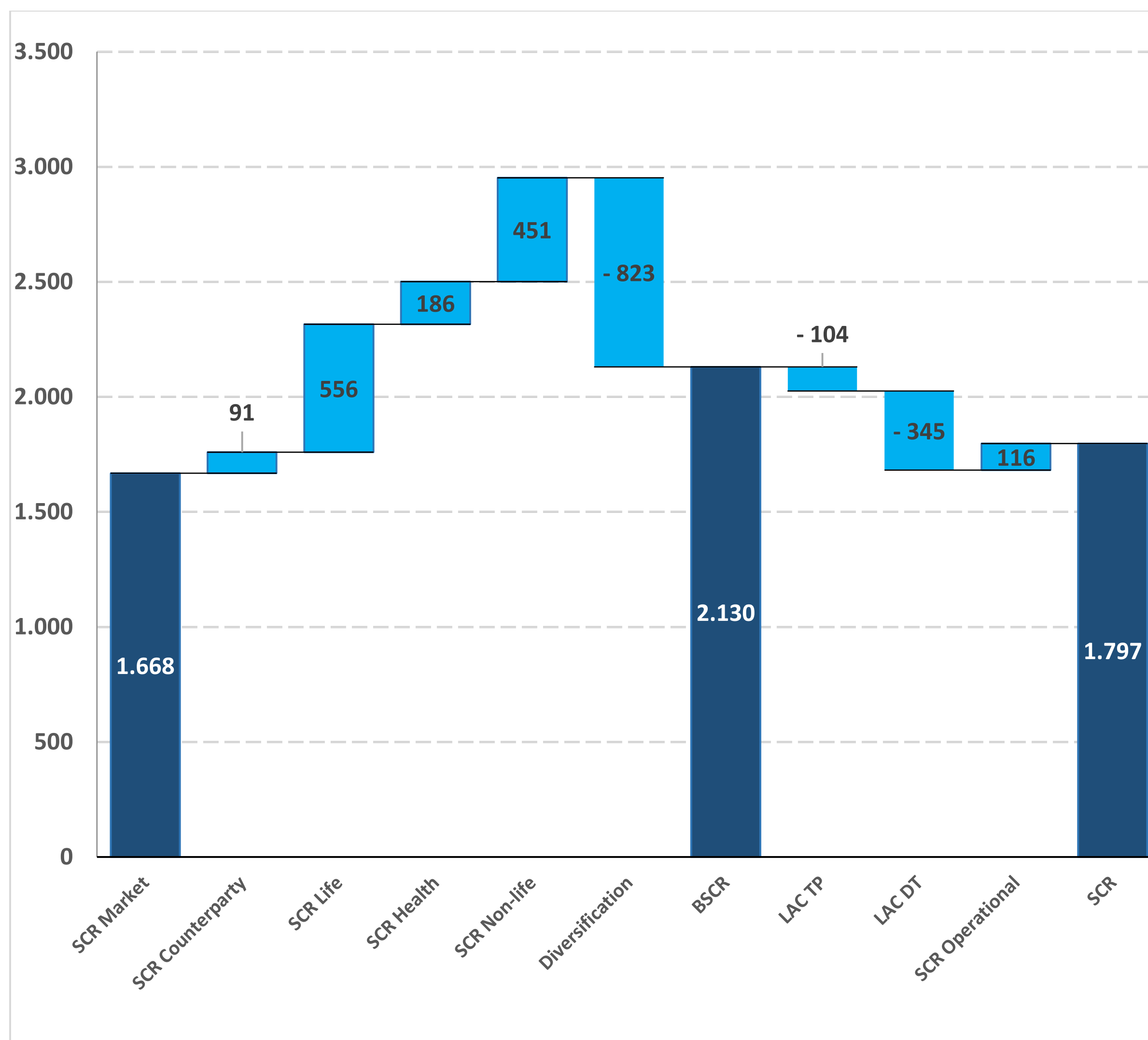


Figure 8 The Solvency Capital Required (SCR) for 2017.

To complete the SCR, the Loss Absorbing Capacity of the Technical Provisions, the Loss Absorbing Capacity of the Deferred Taxes and the SCR Operational pertaining to the Operations Risk are added together.

The Loss Absorbing Capacity of the Technical Provisions (LAC TP) is calculated according to article 206 of Delegated Regulation 2015-35 and takes into account any legal, regulatory or contractual restrictions in the distribution of future discretionary benefits.

The adjustment for the Loss Absorbing Capacity of the Deferred Taxes (LAC DT) is calculated according to article 207 of Delegated Regulation 2015-35, whereby a decrease in deferred tax liabilities or an increase in deferred tax assets shall result in a negative adjustment for the loss-absorbing capacity of deferred taxes. If this adjustment is positive, the adjustment is nil.

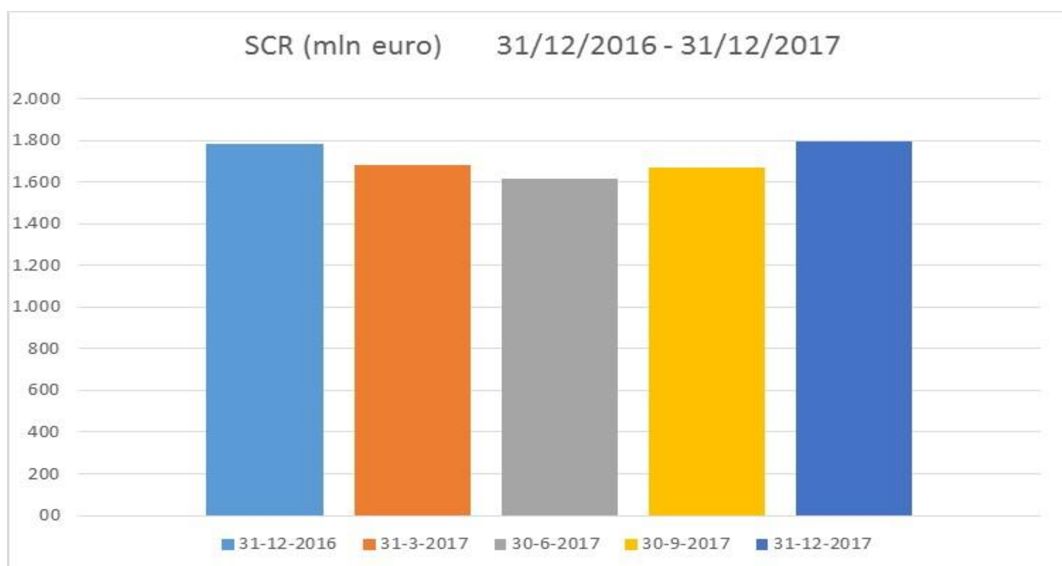


Figure 9 Movement of the Solvency Capital Required during 2017

Figure 9 shows the Solvency Capital Required (SCR) in million euros every quarter during the reporting year 2017. The SCR moved between 1.600 million euro and 1.800 million euro during the reporting year 2017. By the end of 2017, the SCR amounted to 1.797 million euro. These results are calculated using a standard formula for all risk modules. This means that no internal model or simplifications are used when using the standard formula. Note that for SCR 31-12-2016 calculation Belgian legislation required a CAP.

The Minimum Capital Required is calculated as 45% of the Solvency Capital Required.
Since the Minimum Capital Required is calculated as a percentage of the Solvency Capital Required, the main driver of both requirements is the same: market risk.

E.3 Use of the duration-based equity risk sub-module in the calculation of the Solvency Capital Requirement

Ring-fenced funds do not exist in Belgium. Therefore the Solvency Capital Required calculation method using a duration-based equity risk sub-module is not applicable.

E.4 Differences between the standard formula and any internal model used

KBC Insurance NV, Belgium does not use any internal model, only the standard formula is used.

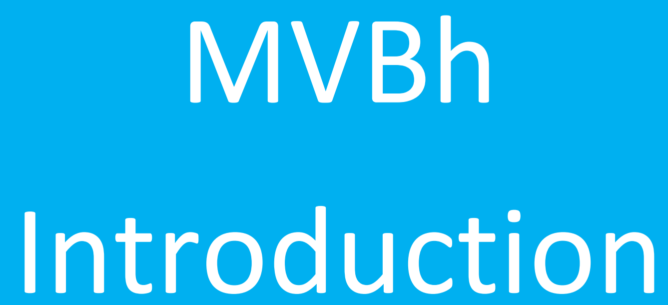
E.5 Non-compliance with the Minimum Capital Requirement and non-compliance with the Solvency Capital Requirement

KBC Insurance NV, Belgium is compliant with the Minimum Capital Requirement as well as with the Solvency Capital Requirement.

F. Solvency and Financial Condition Report MVBh

Maatschappij voor Brandherverzekering CVBA (MVBh) 2017

Based on situation as at 31 December 2017


MVBh
Introduction

F.1. Introduction

Insurance activities of KBC Insurance NV in Belgium include their reinsurance subsidiary Maatschappij voor Brandherverzekering CVBA (MVBh), a fire reinsurance company, which is discussed in this section.

In general the policies which are applicable to KBC Insurance NV are applicable as well to MVBh, taking into account the limited nature, small scale and simplicity of the risks inherent in its business.

MVBh
Business and
Performance

F.2. Business and performance

F.2.1. Business

Business model

Local insurers, characterised by the very local nature of their activities, still have a role to play in society and therefore remain socially relevant since they belong to a local community's social network that mutualises its risks. Their risk profile is generally defensive and well under control. They are very often legally incorporated as 'mutual insurance association' or in some cases as 'insurance cooperative'.

MVBh's mission is to provide adequate protection to these local insurers against volatility of their underwriting results.

Since underwriting results of all affiliated insurers are mutualised within MVBh, a stable revenue stream for local insurers can be generated through yearly profit participation.

Except for KBC Insurance NV, MVBh doesn't accept shareholders other than local insurers, and all these shareholders – local insurers are MVBh's (only) clients as well. KBC Insurance NV is the largest shareholder, holding 24 799 shares, out of a total of 27 500. The remaining shares are owned by 33 local insurers, all geographically located in the provinces of West and East Flanders.

MVBh was incorporated on 10 April 1917, as published in the enclosures to the Belgian Official Gazette dated 21 May 1917, charter n°. 1763. Its mission is to conclude reinsurance contracts against fire damage and ancillary perils with the above-mentioned local insurers, MVBh's shareholders, in order to allow them to maintain their cooperative structure.

MVBh's size is small since reinsurance activities are limited to local insurers which do not grow in number and have limited growth opportunities due to their local character.

Name, legal form and address

Maatschappij voor Brandherverzekering CVBA

Professor Roger Van Overstraetenplein 2

3000 Leuven

BELGIUM

Supervisory authority

National Bank of Belgium

de Berlaimontlaan 14

1000 Brussels

BELGIUM

External auditor

BCVBA PwC Bedrijfsrevisoren (Auditors)

Woluwedal 18

1932 Sint-Stevens-Woluwe

BELGIUM

Representative: Tom Meuleman

F.2.2. Underwriting performance

The following table has been derived from statutory financial statements and demonstrates the historical underwriting profitability of the company:

	2013	2014	2015	2016	2017
Gross earned premium (amount x 1.000 EUR)	6.579,788	6.604,408	6.735,868	7.245,893	7.277,620
Gross earned premium (100%)	100,00%	100,00%	100,00%	100,00%	100,00%
Gross incurred losses	-40,03%	-47,90%	-29,46%	-34,06%	-20,41%
Change in equalization reserves	-2,50%	0,60%	-0,59%	3,73%	-7,50%
Profit participation to clients	-13,50%	-13,00%	-20,00%	-24,85%	-20,10%
Expenses and commissions	-25,67%	-25,62%	-25,52%	-25,21%	-25,49%
Other items	0,25%	0,02%	-0,02%	-0,26%	-0,13%
Gross technical balance	18,55%	14,10%	24,41%	19,34%	26,37%
Investment income and expenses	5,03%	3,29%	5,43%	6,79%	11,21%
Gross technical - financial balance	23,58%	17,39%	29,84%	26,13%	37,58%
Retrocession balance	-18,62%	-14,91%	-23,95%	-21,32%	-26,57%
Net balance	4,96%	2,48%	5,89%	4,82%	11,01%

Table 12 Statutory financial statement, underwriting profitability

F.2.3. Investment performance

The following information has been copied from statutory financial statements:

x 1.000 EUR	2013	2014	2015	2016	2017
Investment income					
Dividends	78,347	75,977	64,299	67,285	63,373
Fixed income	164,689	152,420	149,271	138,976	120,946
Term deposits	1,483	2,166	2,166	0,688	
	244,519	230,562	215,736	206,949	184,320
Impairment reversals	243,432	62,222	52,075	129,962	161,041
Realized capital gains	18,171	12,402	184,781	368,689	696,968
Other	0,000	0,006	0,000	0,142	0,000
	506,122	305,193	452,591	705,743	1.042,328
Investment expenses					
Asset management expenses	6,664	5,674	7,241	12,734	14,438
Investment management expenses	0,000	20,219	25,552	26,675	28,054
Impairments	1,803	16,766	53,784	45,029	1,620
Realized capital losses	166,376	45,264	0,078	129,075	182,039
	174,843	87,923	86,655	213,512	226,151
Investment income, net of expenses	331,279	217,269	365,936	492,231	816,177
Average statutory balance sheet total	10.768,871	11.042,577	11.423,126	12.258,561	13.133,170
Return on average balance sheet total	3,08%	1,97%	3,20%	4,02%	6,21%

Table 13 Investment performance

MVBh
System of
Governance

F.3. System of Governance

F.3.1. Legal management structure

Dual structure

- MVBh is managed according to a dual model, which draws a distinction between:
    - The ‘board of directors’, which has the task of setting strategy, determining general policy, supervising operational management and performing acts which are reserved to the board of directors in accordance with applicable legislation and MVBh’s bylaws.
    - The ‘executive committee’, which is responsible for the operational management of the company.
- The board of directors is composed of at least seven directors (currently 9), who are nominated by the general assembly. The board of directors is composed of executive directors, who constitute the executive committee and are in charge of MVBh’s operational management, and non-executive directors. They are exclusively natural persons.
- The non-executive directors, who are therefore no members of the executive committee, always constitute a majority within the board of directors. The chairman of the board of directors is a non-executive director.
- The board of directors assumes final accountability for MVBh. Therefore the board of directors determines and controls more specifically:
    - MVBh’s strategy and objectives;
    - the risk policy, including general risk tolerance limits.

Moreover, the board of directors oversees the executive committee and its functioning.

- The executive committee is composed of three executive members of the board of directors (natural persons) together constituting a board. They are nominated and dismissed by the board of directors.
- The executive committee is accountable for elaborating, executing and pursuing the strategy decided upon by the board of directors, taking into account MVBh’s values, risk appetite and policies.

Committees

Based upon article 52 of the Insurance and Reinsurance Supervision Act dated 13 March 2016, the tasks assigned to the audit committee, the remuneration committee and the risk committee are executed by the board of directors of MVBh as a whole.

F.3.2. Operational management structure

MVBh has no employees on its payroll.

Activities which are not performed by members of the executive committee, are performed by KBC Group NV, KBC Bank NV and KBC Insurance NV staff.

F.3.3. (Regulated) outsourcing

The outsourcing approach of MVBh is embedded in the approach of KBC Group and KBC Insurance. With the aim of providing its clients the best possible service, MVBh appeals to the knowledge and efficiency present in the Belgian-based entities of KBC Group. No activities or functions are outsourced to external parties.

KBC Group NV provides audit, finance and tax services. The compliance function is not formally outsourced; necessary guidance and support from KBC Group NV, Group Compliance division is, however, provided.

KBC Insurance NV supports MVBh with the following services:

- Settlement of claims reported by the mutual insurers and insurance cooperatives;
- Back-up for the underwriting and acceptance of insurance policies;
- Administration of incoming and outgoing reinsurance contracts;
- Actuarial tasks in execution of the calculation of the solvency position;
- End user computing services;

- Risk management.

The first two services are performed by KBC Insurance NV as part of a retrocession agreement between MVBh and KBC Insurance NV, and are therefore not to be considered as regulated outsourcing.

MVBh considers all these activities to be critical or important functions or activities.

The executive committee's chairman oversees and coordinates the activities which are related to outsourcing, except those relative to outsourced 2nd line of defence management activities which are coordinated by MVBh's CRO.

F.3.4. Independent control functions

General

The persons executing the independent control functions are independent of the business units and operational functions of MVBh. They report at least once a year directly to the board of directors about the execution of their task and inform the executive committee.

Risk management function, compliance function and actuarial function

In accordance with article 56, §3, 2nd subsection, 2° of the Insurance and Reinsurance Supervision Act, the head of the risk management function is a member of the executive committee of MVBh. This executive committee member is the acting Chief Risk Officer (CRO) and also takes accountability for the compliance and actuarial functions. These three independent control functions are executed independently from one another.

The risk management function within MVBh is outsourced towards KBC Insurance NV, under the general supervision of the CRO of MVBh (key function holder). The person accountable for the risk management function is actively involved in determining MVBh's risk strategy and in all policy decisions having a significant impact on the risks and can provide a full picture of the whole range of risks MVBh is exposed to.

The compliance function ascertains that MVBh, the directors, employees and authorised representatives comply with legal and regulatory provisions regulating the reinsurance activity (in particular the rules with respect to integrity and behaviour applying to this activity). The compliance function also assesses potential consequences of changes in the legal framework for MVBh's activities and identifies and assesses compliance risks.

The actuarial function ascertains that MVBh uses an adequate underwriting methodology, coordinates and controls the calculation of the technical provisions and provides an opinion on MVBh's retrocession programme, in accordance with article 59 of the Insurance and Reinsurance Supervision Act.

Internal audit function

The internal audit of MVBh is outsourced towards KBC Group NV, under the general supervision of the CEO of MVBh (key function holder). The internal audit function provides the board of directors and executive committee with an independent assessment of the quality and effectiveness of the internal controls, risk management and governance system of MVBh.

The person who is accountable for the internal audit function or the person designated for these purposes communicates their findings and recommendations with the board of directors and executive committee.

F.3.5. Remuneration policy

Members of the executive committee receive a fixed remuneration. There is no variable component.

Apart from a pension plan for MVBh’s chairman of the executive committee there are no supplementary pension or early retirement schemes for the members of the administrative, management or supervisory body and other key function holders.

F.3.6. Fit & proper requirements

MVBh's requirements concerning skills, knowledge and expertise applicable to the persons who effectively run MVBh or have other key functions as well as its process for assessing their fitness and propriety are virtually identical to the ones applicable for KBC Group.

No loans, credits or suretyships have been granted to members of the board of directors (whether smaller or larger than 100 000 euros).

MVBh
Risk Profile

F.4. Risk Profile

F.4.1. Underwriting risk

MVBh only writes reinsurance business with local Belgian mutual insurers and limits underwriting to fire business and allied perils. Reinsurance is on a 100% quota–share basis.

Mutual insurers only write policies against fire damage and ancillary perils for ‘simple risks’ (together with the minor liability and legal expenses insurance cover that can typically be included in these fire policies), mainly located in their local municipality or neighbouring municipalities in West and East Flanders. Underlying policies relative to product offering, underwriting, pricing, reserving and claims settlement are copied from the ones applied by KBC Insurance.

Underwriting limits, in terms of sums insured, as defined by the inward reinsurance contracts, must be strictly applied.

Technical insurance risk represents the largest risk within MVBh (cf. QRT S.25.01.21). Moreover, technical insurance performance is the decisive factor in determining how much profit is returned by MVBh to clients/mutual insurers. Therefore, limiting volatility of technical insurance performance is key.

The reinsurance portfolio, gross of proportional retrocession, is adequately protected by non-proportional retrocession cover, in terms of deductible, limit and amount of cover on an annual basis, against the consequences of claims in risk concentrations.

Due to the local character of MVBh’s ceding companies/local insurers, risk locations may be geographically highly concentrated. These concentrations are mapped on a regular basis. As explained in the previous paragraph, ensuing risks are adequately retroceded.

MVBh monitors the underwriting performance of individual mutual insurers, and encourages individual mutual insurers to eliminate systematic underperformance, compared to their peers.

MVBh conducts portfolio checks on (at least) a yearly basis, aiming at controlling compliance with the above-mentioned policies, monitoring evolution of claims ratios of individual local insurers, and detecting and rectifying potential errors and mistakes.

MVBh pays appropriate attention to opinions of the actuarial function holder, and takes appropriate measures, if necessary.

MVBh’s exposure to natural catastrophes (i.e., windstorm, flood and earthquake), man-made catastrophes, as well as large individual fire claims, are analysed on a regular basis and reported to the board of directors.

F.4.2. Market risk

Market risks represent the 3rd largest risk which MVBh is exposed to (cf. QRT S.25.01.21), triggered by (i) the investment of shareholders’ funds and (ii) differences between risk profiles of cash flows, originating from reinsurance liabilities on the one hand and assets, covering reinsurance liabilities on the other hand. Being exposed to market risks is an inevitable consequence of operating in the (re)insurance business.

MVBh relies on KBC Group's expertise with respect to market risk and investment portfolio management. So-called 'ALM limits' have been set specifically for MVBh. Compliance with these limits is reported on every meeting of the board of directors.

F.4.3. Credit risk

Counterparty default risk on issuers of financial instruments is managed within the 'ALM limits' framework mentioned above, relying on KBC Group's expertise with respect to credit risk management.

MVBh's credit risk largely stems from counterparty default risk exposure to KBC Insurance, originating from retrocession contracts. KBC Insurance is indeed MVBh's preferred retrocessionaire.

Although credit risk is quite significant within MVBh's overall risk profile because of counterparty default risk exposure to KBC Insurance – it is the 2nd largest risk MVBh is exposed to (cf. QRT S.25.01.21) – MVBh accepts this risk.

F.4.4. Liquidity risk

This risk may emerge when a catastrophic event occurs which generates high incurred claims in the reinsurance portfolio, more specifically when a time gap occurs between the moment MVBh is expected to pay these claims to its ceding companies on the one hand, and the moment the retroceded part can be recovered from the retrocessionaire on the other hand.

This risk has been neutralised by the retrocession contract through a clause which foresees the possibility for MVBh to request cash claims from its retrocessionaire once a contractually determined threshold has been exceeded.

F.4.5. Operational risk

Operational risk represents the fourth largest risk MVBh is exposed to (cf. QRT S.25.01.21).

MVBh endorses the group-wide framework for non-financial risk management and business continuity management.

In as far as relevant for MVBh, non-financial risk management tools such as group key controls, internal control statement, competition compliance program, etc. are applied.

For its business continuity plan, MVBh is obviously highly dependent on KBC Insurance and KBC Group.

MVBh analyses the adequacy of business processes both systematically and on an ad-hoc basis.

Compliance with the group-wide framework for non-financial risk management and business continuity management is ascertained by an adequate execution of the local operational risk manager's and business continuity manager's roles. Guidance and steering for the execution of these roles is provided by the KBC Belgium Business Unit's risk management and crisis management departments.

Audit recommendations are executed in a timely and correct manner. There are 9 outstanding audit recommendations at present.

F.4.6. Other material risks

Business risk

Portfolio growth depends to a large extent on local insurers' business managers' willingness to place business with the local insurer. Professional relationship management with these local business managers is key.

MVBh's development is very closely linked to local Belgian mutual insurers' development. Should, for example, their survival be compromised due to unrealistically high regulatory obligations, MVBh's future would inevitably be jeopardised.

The Insurance and Reinsurance Supervision Act imposes strict requirements on (re)insurance undertakings to ensure their solvency. Should mutual insurers have to comply with these requirements, they would inevitably have to cease business. Fortunately, the bill allows for a 'soft' regime in a number of cases, including for 'small' insurers.

Mutual insurers (i.e., MVBh's clients) have assumed the regime of 'small' insurers, which reinsure 100% of their insurance obligations, entailing a huge simplification of their solvency regime i.e.:

- The Insurance and Reinsurance Supervision Act is (quasi) not applicable;
- The insurance undertaking must submit an application file for registration with the National Bank of Belgium (NBB) and demonstrate it complies with all required conditions;
- NBB must approve the application for registration;
- Once approved, the insurance undertaking will be listed on a specific register to be published on NBB's website;
- NBB may decide at its discretion to further regulate all additional information requirements, either on an individual or a general basis.

Application files for registration have been submitted by the mutual insurers to the NBB, and approved by the NBB. They are now listed on the NBB's website.

Reputation risk

The reputation of MVBh is a strategic asset of the firm. We aim to protect and grow our reputation in the eyes of our clients by managing our business in a responsible manner.

MVBh champions a strong compliance culture and has zero tolerance for any intentional violation of mandatory legal norms that are sanctioned with criminal penalties against our company, its directors or employees or administrative measures which could result in the revocation, suspension, modification or nonrenewal of the licenses issued to MVBh.

Regular reporting to the KBC Group Compliance division is done in compliance with Group Compliance Rules.

Concentration risk

KBC Insurance is MVBh's preferred reinsurer. MVBh is also exposed to KBC Bank, through current, savings and investment accounts, as well as, potentially, term deposits and other securities. KBC Insurance and KBC Bank maintain close (commercial) relationships. Potential impact on MVBh of ensuing contagion risk is adequately monitored and kept under control.

The global limit relative to counterparty default risk, withheld in the ALM limit framework, applies to KBC group as a whole. On top of that comes exposure to KBC Insurance generated by MVBh's retrocession programme, as well as exposure to KBC Bank due to current and savings accounts which are held by MVBh with KBC Bank in view of its daily operations. Outstanding balances of these accounts are kept at a minimum level to ensure smooth daily operations. Surpluses are transferred to KBC Asset Management, and from then onwards fall within the global limit relative to counterparty default risk.

MVBh
Valuation for
Solvency
Purposes

F.5. Valuation for Solvency Purposes

F.5.1. Assets

Valuation bases for solvency purposes

These are identical to the ones used by KBC Insurance. Actual values can be found in QRT S.02.01.02.

Valuation bases in statutory financial statements

Impairments

For both financial fixed assets and unlisted shares, recorded under 'other financial assets', impairments are entered in the books in case of durable depreciations in value.

Listed shares are impaired in case their market value is sustainably (longer than one year) or significantly (more than 30%) lower than their book value, demonstrating that the depreciation in value is sufficiently durable.

The resulting impairments equal the difference between book value and market value.

The recorded impairments are reversed as soon as the market value is higher again, up to the purchase value at maximum.

For treasury investments, impairments are recorded when the realisation value of the investment at balance sheet date is lower than the purchase value.

For the other receivables and fixed income securities, impairments are recorded when reimbursement at maturity date is fully or partially uncertain or at risk.

Impairments are not maintained if, at fiscal year–end, they are higher than when based upon a current assessment, in accordance with the standards used at the time the impairments were recorded.

Provisions for risks and costs

At fiscal year–end, all foreseeable risks and charges which originated during the fiscal year are provisioned for, in accordance with the provisions of the Royal Decree of 17 November 1994.

Technical provisions

The technical provisions for claim payments to be made in the future are calculated per claim or per contract, taking known elements of the file into account.

Revaluations

Financial fixed assets as well as investment securities can be revalued when they show a certain and permanent capital gain compared to their purchase value.

Actual values can be found in template SE.02.01.16.

F.5.2. Technical provisions

Valuation bases and methods

In general, expected future cash flows related to reinsurance liabilities have been calculated and documented by KBC Insurance's non-life actuarial department in accordance with technical provisions guidelines as provided by KBC Group and taking into account the Risk Measurement Framework of KBC. We will briefly describe the main principles.

Pre-claim versus post-claim non-life obligations

For non-life obligations, separate cash-flow projections are made relative to:

- claim events that are expected to occur after the valuation date and during the remaining in-force period of existing contracts (pre-claim liabilities);
- claim events that have already occurred but that are not settled yet, regardless of whether the claims arising from these events have been reported or not (post-claim liabilities).

Gross liabilities versus retrocession recoverables

- Cash-flow projections are initially made on a gross basis, without deduction of retrocession recoverables;
- Retrocession recoverables are valued separately. They are included on the asset side of the economic balance sheet, and are calculated separately for non-life pre-claim and post-claim expected cash flows. Their valuation allows for expected losses due to counterparty default (i.e., the reinsurer); the impact thereof is however negligible.

Segmentation into homogeneous risk groups

Reinsurance liabilities have been grouped according to the nature of their risks, and calculations have been done separately for fire and allied perils (including natural catastrophes), general third-party liability ensuing from insured buildings, and legal expenses linked to the latter. These homogeneous risk groups have a one-to-one link with Solvency II lines of business (LOB) 19, 20 and 22:

- LOB 19 – proportional non-life reinsurance – fire and other damage to property insurance;
- LOB 20 – proportional non-life reinsurance – general liability insurance;
- LOB 22 – proportional non-life reinsurance – legal expenses insurance.

Where required by Solvency II regulations (i.e., if both parties are committed), future premiums on existing contracts are taken into account in valuing current liabilities. All contracts incept at 1 January, with a minimum 3-month cancellation period, ending on 30 September. Tacit renewal of these reinsurance contracts implies both parties are committed; therefore, in this case, at 31 December, the next generation of reinsurance contracts is within scope of the valuation of reinsurance liabilities.

Technical provisions are calculated according to the 'Mark to Model' method; i.e., a theoretical 'transfer value' is calculated at which the liabilities would be valued when transferred to another company. This includes the calculation of the:

- discounted best estimate of liabilities: models are used to generate cash-flow projections. The present value is then calculated at the risk-free discounting yield curve;
- risk margin: in such a manner as to ensure that the value of the technical provisions is equivalent to the amount that (re)insurance undertakings would be expected to require in order to take over and meet the (re)insurance obligations. It is calculated according to the cost of capital approach; i.e., the present value of the cost of holding expected required capital during the remaining lifetime of the liabilities.

At present only deterministic calculations are made.

The matching adjustment referred to in Article 77b of Directive 2009/138/EC, the volatility adjustment referred to in Article 77d, the transitional risk-free interest rate term structure referred to in Article 308c and the transitional deduction referred to in Article 308d are either not relevant or not applied.

Overview of Solvency II technical provisions

The enclosed table provides an overview, as at 31 December 2017 of Solvency II technical provisions (cf. also QRT S.17.01.02):

- broken down into pre-claim and post-claim obligations;
- broken down into gross and retroceded obligations;
- per Solvency II line of business.

All amounts in the SOLVENCY II columns are expressed in terms of 'liabilities'; i.e., a negative liability represents an asset. Gross pre-claim liabilities are negative since they represent the economic profit expected to be generated by the 2018 generation of inward reinsurance contracts.

The risk margin is very high compared to the discounted best estimate of gross liabilities. However, the latter is composed of a positive value for the discounted best estimate of gross post-claim liabilities, and a negative one, compensating almost entirely the positive one, for the best estimate of gross pre-claim liabilities. This negative value reflects the economic profits expected to be generated by the 2018 generation of inward reinsurance contracts; these expected economic profits are of course uncertain, and the risk margin represents the amount that (re)insurance undertakings would be expected to require in order to take over and meet the (re)insurance obligations.

Note that the risk margin is relevant only with respect to gross liabilities. A breakdown along the criteria used in the table is not available yet.

Comparison between Solvency II and statutory valuation

The enclosed table also compares Solvency II with statutory technical provisions.

Provisions for unexpired risks as at 31 December 2017 don't figure in the statutory balance sheet since (almost) all underlying policies have a principal premium due date at 1 January. As reinsurance contracts are renewed as at 1 January 2018, the Solvency II economic balance sheet contains pre-claim liabilities related to these renewed contracts.

The equalisation reserves do not figure in the Solvency II economic balance sheet.

All amounts in the SOLVENCY II and STATUTORY columns are expressed in terms of 'liabilities'; i.e., a negative liability represents an asset.

A negative (STATUTORY – SOLVENCY II) figure represents a statutory deficiency whereas a positive figure represents a statutory redundancy, compared to the Solvency II economic balance sheet.

Since statutory valuation bases are very prudent, not surprisingly, gross liabilities represent a statutory redundancy.

However, retroceded liabilities represent a statutory deficiency since:

- the statutory balance sheet doesn't contain pre-claim liabilities towards MVBh's retrocessionaire, whereas the Solvency II economic balance sheet does, since in Solvency II, gross pre-claim obligations are expected to generate a profit, part of which will be due to the retrocessionaire;
- post-claim retrocession recoveries are overestimated in the statutory balance sheet, compared to the Solvency II economic balance sheet.

Liabilities, net of retroceded obligations, represent a statutory redundancy, compared to the Solvency II economic balance sheet.

31/12/2017 (x 1.000 EUR)	SOLVENCY II			STATUTORY			STATUTORY - SOLVENCY II		
Reinsurance liabilities	Pre-claim	Post-claim	Total	Pre-claim	Post-claim	Total	Pre-claim	Post-claim	Total
Gross liabilities									
- LOB 19 (Fire)	-1.645,384	1.644,462	-0,923	0,000	1.934,439	1.934,439	1.645,384	289,977	1.935,362
- LOB 20 (General liability)	-5,916	12,035	6,118	0,000	21,806	21,806	5,916	9,771	15,688
- LOB 22 (Legal expenses)	-2,217	23,910	21,692	0,000	23,290	23,290	2,217	-0,620	1,598
- Risk margin			117,264				0,000	0,000	-117,264
- Equalization reserves				1.623,918		1.623,918	1.623,918		1.623,918
- Total	-1.653,518	1.680,406	144,152	1.623,918	1.979,535	3.603,453	3.277,436	299,129	3.459,301
Retroceded liabilities									
- LOB 19 (Fire)	1.396,835	-1.409,412	-12,577	0,000	-1.549,774	-1.549,774	-1.396,835	-140,362	-1.537,197
- LOB 20 (General liability)	14,269	-11,602	2,667	0,000	-21,806	-21,806	-14,269	-10,204	-24,473
- LOB 22 (Legal expenses)	6,480	-23,050	-16,569	0,000	-23,290	-23,290	-6,480	-0,240	-6,721
- Total	1.417,584	-1.444,063	-26,480	0,000	-1.594,870	-1.594,870	-1.417,584	-150,806	-1.568,390
Net liabilities									
- LOB 19 (Fire)	-248,550	235,050	-13,500	0,000	384,666	384,666	248,550	149,616	398,165
- LOB 20 (General liability)	8,352	0,433	8,785	0,000	0,000	0,000	-8,352	-0,433	-8,785
- LOB 22 (Legal expenses)	4,263	0,860	5,123	0,000	0,000	0,000	-4,263	-0,860	-5,123
- Risk margin	0,000	0,000	117,264				0,000	0,000	-117,264
- Equalization reserves				1.623,918	0,000	1.623,918	1.623,918	0,000	1.623,918
- Total	-235,934	236,343	117,672	1.623,918	384,666	2.008,583	1.859,852	148,323	1.890,911

Table 14 Overview of SII and BGAAP Technical Provisions as at 31/12/2017

F.5.3. Other liabilities

Valuation bases are identical to the ones used by KBC Insurance.

MVBh
Capital
Management

F.6. Capital Management

F.6.1. Own funds

We refer to QRT S.23.01.01 to show that total unrestricted tier 1 basic own funds of 9 946 310 euros are eligible and available to meet SCR and MCR. There are no ancillary own funds.

The origins of differences with statutory own funds are listed in the following table:

SE.02.01.16 x 1.000 EUR	Solvency II value	Statutory accounts value	Difference
Own funds	9.948,491	7.919,685	2.028,806
Foreseeable dividends	2,181	2,181	0,000
	9.946,310	7.917,504	2.028,806
ASSETS			
Listed equities	723,282	678,881	44,401
Government bonds	3.183,330	2.707,528	475,802
Corporate bonds	3.997,784	4.258,829	-261,045
Derivatives	0,000	0,826	-0,826
Reinsurance recoverables	26,480	1.594,869	-1.568,389
LIABILITIES			
Technical provisions	144,152	3.603,453	-3.459,301
Deferred tax liabilities	120,438	0,000	120,438
TOTAL [ASSETS - LIABILITIES]			2.028,806

Table 15 Differences between Solvency II and statutory valuations

F.6.2. Solvency Capital Requirement and Minimum Capital Requirement

MVBh's SCR calculations are based upon the standard formula. No (partial or full) internal model is used. As shown in QRT S.25.01.21, the SCR as at 31 December 2017 amounts to 2 227 216 euros, giving rise to a solvency ratio of 447% of SCR.

Non-life underwriting risk (1 244 211 euros), counterparty default risk (840 892 euros), market risk (707 575 euros), and operational risk (218 329 euros) are the largest risks MVBh is exposed to.

No simplified calculations, nor undertaking-specific parameters are used.

The MCR is considerably higher than the SCR i.e. 3 600 000 euros (as shown in QRT S.28.01.01), giving rise to a solvency ratio of 276% of MCR.

The Solvency II ratio with respect to the SCR is of course higher than the Solvency II ratio with respect to the MCR. When considering the solvency ratios, the SCR is less relevant in our case.