



# **SOLVENCY & FINANCIAL CONDITION REPORT**

## **KBC Group Re 2016**

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## Summary

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The SFCR is the annual Solvency and Financial Condition Report that all insurance undertakings and groups have to disclose to the public. The report provides qualitative and quantitative information on Business and Performance, System of Governance, Risk Profile, Valuation for Solvency purposes and Capital Management of the undertaking.

The report has a harmonized structure that is defined by Annex XX to the Solvency II Delegated Acts Regulation and includes templates defined by Implementing Regulation containing quantitative information (Quantitative Reporting Templates (QRTs)).

All amounts in this report are presented in millions of euros unless otherwise stated.

Since this is the first time publication of this report in its current structure no comparison is made with previous versions and reference to 2015 figures is not systematic since Solvency II valuated data were not completely available at that time.

### Highlights

- KBC Group Re is the reinsurance subsidiary of KBC Group, specializing in protecting the group's bank and insurance entities.
- KBC Group Re has a medium risk profile in line with the Risk Appetite Statement.
- KBC Group Re is strongly capitalized both in terms of level and quality of capital. The Solvency II ratio per 31/12/2016 amounts to 619% (including volatility adjustment).
- The LuxGaap result for 2016 amounted to 81 million EUR in 2016 mainly due to a diminution of the equalization provision. Earned premiums went up 61% totalling 22,3 million EUR. Combined ratio for 2016 amounted to 94,5%.
- A continued implementation of the KBC Group 'Three Lines of Defence' model is operated.

### Remarks

The information provided in this document has not been subject to an external audit. Disclosures have however been checked for consistency with other existing reports and were subjected to the screening of authorized management representatives to ensure quality.

The 2016 Solvency & Financial Condition Report was distributed to the Board of Directors to ensure the appropriate approval of the management body as requested under Solvency II.

The Solvency and Financial Condition Report is available in English on the website of KBC Group Re and is updated on a yearly basis. Next update is scheduled for May 2018.

## A. Business & performance

### A.1 Business

<b>Area of operation</b>	
<p>KBC Group Re SA is the Luxembourg reinsurance subsidiary belonging to the KBC Group. The company was incorporated on 20 March 1989.</p> <p>The company specializes in protecting the group's bank and insurance entities.</p>	
<b>Shareholders</b>	
<p>KBC Group Re is wholly owned by KBC Insurance NV, which is in turn wholly owned (directly and indirectly) by KBC Group NV. KBC Group NV is a listed company.</p>	
<b>Long-term credit ratings (24 October 2016)</b>	
	Standard & Poor's
KBC Group Re SA	A-
<b>Management</b>	
Day-to-day management	Ivo Bauwens
Chairman of the Board of Directors	Hans Verstraete
<b>Address</b>	
<p>KBC Group Re SA 4 rue du Fort Wallis L-2714 Luxembourg</p>	
<b>Supervisory authorities</b>	
KBC Group Re SA	KBC Group NV
Commissariat aux Assurances 7, boulevard Joseph II, L-1840 Luxembourg	Nationale Bank van België De Berlaimontlaan 14 1000 Brussel

<b>External auditor</b>
PwC Luxembourg 2 Rue Gerhard Mercator L-2182 Luxembourg
<b>Number of FTEs</b>
As at 31 December 2016 the company employed 9,05 persons (Full time equivalent)

The strategy of the company is embedded in the strategy of the KBC Group. For more detailed information, please see the KBC Group annual report for 2016.

KBC Group is an integrated bank-insurance group whose core markets are Belgium, the Czech Republic, Slovakia, Hungary, Bulgaria and Ireland, for a total of more than 10 million clients. Its network is organized around 1 456 bank branches (2016 figure), insurance sales via own agents and other channels, as well as various electronic channels. The group employed some 36 000 FTEs (2016 figure).

KBC Group is structured around three business units, which focus on local activities and contribute to sustainable earnings and growth. The units are Belgium, the Czech Republic and International Markets.

KBC Group Re is the reinsurance subsidiary of KBC Group, specializing in protecting the group's bank and insurance entities. The underwriting activities of KBC Group Re consist in the 2 following segments:

1. The reinsurance of KBC insurance risks
2. The reinsurance of KBC operational risks

The KBC Insurance risks segment comprises acceptances that are made for optimization of the group's insurance retention and increasing capital flexibility within the KBC Insurance Group by deploying currently redundant capital of the company. For implementing this optimization, KBC Group Re has been chosen as centralizing placement vehicle for major reinsurance programs on property and liability. KBC Group Re also participates in the other reinsurance placements of KBC direct insurance entities that are open to the external reinsurance market.

The KBC Operational risks segment includes classical operational risks for a bank-insurer which are typically placed on facultative "program" basis as covers for professional liability, fraud, cybersecurity and the various property belonging to KBC Group. It comprises also some specialty covers as safe deposit covers for clients of the bank or other para-banking insurance covers for bank clients (e.g. insurances linked to bank cards). KBC Group Re supports the placement of those KBC programs by filling the gap between the deductibles/risk retentions of the individual KBC companies (original insureds) and the group deductible, by retaining - on behalf of KBC - the result volatile priority layers where capacity in the market is hardly available, and by facilitating access to the international price-worthy (re-)insurance capacity.

The income statement (LuxGaap) of KBC Group Re is the following:

(X 1.000 EUR)	2016	2015	Change in amount	Change in %
<b>Net earned premiums Non-Life</b>	<b>22 308</b>	<b>13 864</b>	<b>8 444</b>	<b>61%</b>
Gross Earned premiums	34 689	23 637	11 052	47%
Ceded reinsurance premiums	-12 381	-9 773	-2 608	27%
<b>Net claims incurred</b>	<b>-18 187</b>	<b>4 686</b>	<b>-22 873</b>	<b>-488%</b>
Gross claims incurred	-16 403	-5 860	-10 543	180%
Reinsurers' share in claims incurred	-1 784	10 547	-12 330	-117%
<b>Net operating expenses</b>	<b>-2 905</b>	<b>-3 410</b>	<b>505</b>	<b>-15%</b>
Net acquisition costs	-977	-1 475	498	-34%
Administrative expenses	-1 928	-1 935	7	0%
<b>Investments Incomes</b>	<b>13 674</b>	<b>39 585</b>	<b>-25 911</b>	<b>-65%</b>
Interest income	13 140	14 578	-1 438	-10%
Dividend income	0	4 439	-4 439	-100%
Net realized result from investments	679	21 709	-21 030	-97%
Other investments related incomes/costs	-145	-1 142	997	-87%
<b>Net other income</b>	<b>-30</b>	<b>287</b>	<b>-317</b>	<b>-110%</b>
<b>Change in the equalization provision</b>	<b>99 591</b>	<b>-25 409</b>	<b>125 000</b>	<b>-492%</b>
<b>Taxes</b>	<b>-33 496</b>	<b>-3 763</b>	<b>-29 733</b>	<b>790%</b>
<b>Result after tax</b>	<b>80 955</b>	<b>25 840</b>	<b>55 114</b>	<b>213%</b>

Table 1 Income statement, using LuxGAAP rules

The LuxGaap result of KBC Group Re amounted to 81 million EUR in 2016 (+213%) mainly due to a diminution of the equalization provision with 99,6 million EUR (before tax). More details on the underwriting and investment performance are given in the following two sections.

## A.2 Underwriting performance

Earned premiums totalled 22,3 million EUR in 2016, showing an increase of 61% from 13,9 million EUR in 2015. This is principally due to a reinforcement of the role of KBC Group Re as centralizing placement vehicle for reinsurance optimization within the KBC Group.

	2016	2015
Net claims ratio	81,5%	-33,8%
Net expense ratio	13,0%	24,6%
Combined ratio	94,5%	-9,2%

Table 2 Non-life ratios

Volatility in earnings and ratios is unavoidable for KBC Group Re, which is in line with the mission of being the internal reinsurer of the KBC Group and due to the small size of the portfolio.

The net claims ratio rose from -33,8% to 81,5% due to important storm and liability claims registered on the reinsurance programs of KBC Insurance. The year 2015 additionally showed an

atypical negative claims ratio due to the cancellation – following a favorable evolution - of prudential reserves that were made for some past large claims.

The expense ratio went down from 24,6% to 13,0% due to lower acquisition costs on the 2016 business (increase of the non-proportional reinsurance) and non-recurrent adjustments to commissions of some previous years contracts (reduction of profit commission).

As a result, the combined ratio increased from -9,2% to 94,5%, a rise attributable mainly to the higher claims ratio.

More information about the underwriting performance can be found in the Quantitative Reporting Templates (QRT):

- S.05.01.02 – Premiums, claims and expenses by line of business
- S.05.02.01 – Premiums, claims and expenses by country

### A.3 Investment performance

At 13,7 million EUR at year-end 2016, total net investments income was down by 25,9 million EUR (-65%) as a result of:

- Lower interest incomes due to a declining portfolio volume (in comparison with the portfolio of beginning 2015) and to a decrease in the return on the bonds portfolio caused by lower reinvestment yields
- The full divestment of the equity portfolio in 2015, which explains the high decrease of dividend income and realized results from investments

Other investments related incomes/costs reduced significantly due to:

- Lower custodian and asset management fees.
- Lower withholding taxes

In the LuxGaap financial statements, investments in bonds are measured at amortized cost, minus impairments when it is expected that the impairment in value is permanent in nature. Table 3 shows the amount of unrealized gains and losses.

(X 1.000 EUR)	31/12/2016	31/12/2015	Change in amount	Change in %
Market value	577 733	579 122	-1 389	0%
Book value	539 571	538 789	782	0%
Unrealized gains/losses	38 162	40 333	-2 171	-5%

Table 3 Unrealized gains/losses on the bonds portfolio

Portfolio volume was quite stable in comparison with previous year.

KBC Group Re does not have any investments in securitisation.

#### **A.4 Performance of other activities**

No other activities are material.

#### **A.5 Any other information**

No other information to report.



## **B. System of governance**

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### **B.1 General information on the system of governance**

#### ***Management structure of KBC Group Re***

In accordance with the Articles of Association, the Company is managed by a Board of Directors. The Board of Directors is responsible for developing and approving the strategy and general policy for the company, including a risk, compliance and audit framework, and monitoring their implementation. The Board is also responsible for the appointment of the Managing Director.

The Managing Director's responsibilities include implementing and monitoring (together with the Board) the strategic plans, appointing all staff members, being the primary contact point between staff members and the Board, providing strong leadership to, and effective management of, the Company and otherwise carrying out the day to day management of the Company. This Managing Director does also assume the responsibilities and role of 'Dirigeant agréé' as defined in the Luxembourg regulation 'Loi modifiée du 6 décembre 1991 sur le secteur des assurances'.

The Board also acts as Audit, Risk and Compliance Committee (see infra).

The Board is composed of at least 3 members (currently 4) appointed by the General Meeting. Directors of KBC Group Re are not remunerated. The Managing Director is the sole Executive Director.

#### ***Audit Risk and Compliance Committee***

Within KBC Group Re, the Audit, Risk and Compliance Committee is not set up as a separate committee and the Board directly exercises its responsibilities regarding those topics within the audit, risk and compliance domains, i.e. the integrity of the financial reporting, the effectiveness of the internal control measures and risk management processes, and the implementation of the compliance rules.

Following persons, or their representative, participate as permanent guests during these Audit Risk and Compliance Committee meetings:

- The Internal auditor;
- The Chief Risk Officer (CRO) of the Business Unit Belgium of KBC;
- The Compliance Officer.

The external auditors are invited at least once a year.

#### ***Reporting of the control functions***

The local risk function, compliance function and actuarial function, and the group audit function report on their findings to the Board of Directors when acting as Audit Risk and Compliance Committee.

Group Risk, Group Compliance and the Actuarial Function Holder Group will, at the level of the KBC Insurance Group and KBC Group, report on their findings to:

- The Executive Committee of KBC Insurance NV and KBC Group NV.

- The Audit Committee, the Risk & Compliance Committee and the Board of Directors of KBC Insurance NV and KBC Group NV.

## B.2 Fit and proper requirement

Fit and proper requirements for the members of the Board of Directors are part of the company's Corporate Governance Charter which indicates the conditions of appointment of new board members, as well as the training requirements. Appointment conditions aim at a balanced composition of the Board, ensuring that the board members have adequate insurance and reinsurance expertise, general corporate management expertise and broader societal experience.

For the persons having a key function, propriety and fitness checks are part of the human resources management policy. This policy includes the request of showing the criminal record. Fitness checks are part of the recruitment process: formal qualification is checked as well as previous experience. Human resources procedures also include training requirements aiming at maintaining the qualification of employees.

## B.3 Risk management system including the own risk and solvency assessment

### *Risk management framework*

Risk management is a key component of the strategic management within 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 describes how risk management is performed on a continuous basis throughout the whole of KBC Group. As such, it is the single point of entry for all documentation on the risk management process within KBC Group.

The KBC Risk Management Framework is based upon the Risk Strategy which specifies the objectives, mandate and ambition level of KBC Group with regard to risk management, as decided by the Board of Directors of KBC Group.

Risk management within KBC Group is organized on a risk-type basis. This is reflected in risk-type specific Risk Management Frameworks, each elaborating the specific measures, methods, tools ... that are most suited for the particular risk type. Where relevant, the risk-type specific frameworks differentiate between minimum standards for Banking, Insurance and Asset Management (the 3 main sectors of activities of KBC as integrated bank-insurance group). Generic elements applicable to all risk types are described in the overarching risk management framework. Next to the risk type specific frameworks, an integrated risk management framework describes the integrated cross-silo approach.

The overarching risk management framework also introduces a number of fundamental risk concepts and tools, such as:

- A common risk map, i.e. an overall picture of all the predominant risk types and subtypes which are used within the KBC risk universe, indicating how these are interrelated.
- Risk measurement standards.
- Stress testing standards.

The KBC Risk Management Framework defines minimum standards that all entities within the group must adhere to. Group frameworks must therefore be endorsed by local entities, including KBC Group Re. At the same time the implementation of each framework can be adjusted on the basis of local conditions.

As the risk management landscape is in constant evolution due to changes in internal as well as external contextual elements, the components of the KBC Risk Management Framework are reviewed on a regular basis to ensure their ongoing effectiveness.

The risk management process consists of following steps:

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

As the risk management process is a continuous effort, these process-steps are not strictly sequential and interact with one another.

### ***Risk governance***

Main components of the risk governance model for KBC Group Re are:

- The Board of Directors which decides on and supervises the risk appetite and risk strategy each year.
- The 'three lines of defence' model that is further described in the next section.
- The 'Investment Committee' that assists the Board of Directors in the domain of investments and balance sheet management.

### ***Own risk and solvency assessment***

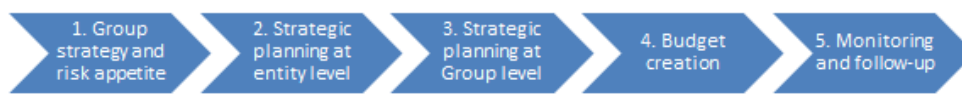
The KBC Insurance Group and its insurance and reinsurance subsidiaries undertake on a regular basis an Own Risk and Solvency Assessment (ORSA) to monitor and ensure that business is managed in a sound and prudent way.

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. KBC Group Re has locally endorsed the Group ORSA Policy, completed by a local addendum specifying the local legal, regulatory and organizational features of the company.

The ORSA is an integral part of the business strategy and is taken into account on an ongoing basis in the strategic decisions within the KBC Insurance Group. KBC Insurance Group has decided to perform 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.

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.

The figure below shows the 5 phases of the APC process:



The monitoring and follow-up of the risk appetite and limits is implemented formally via the integrated risk reporting.

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 links this conclusion to the:

- Evolution of amount and composition of available regulatory capital over a 3-year horizon and under different economic circumstances.
- Evolution of required regulatory capital over the 3-year planning horizon, taking into account expected changes to the risk profile of the entity/group.
- The impact of scenario analyses and sensitivities on required and available regulatory capital.

KBC Group Re 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 the company.

The annual ORSA process assesses the situation and the data per 31 December and is submitted to the Supervisory authority before 30th 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.

## B.4. Internal control system

### *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. 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:
  - o Is responsible for identifying, measuring, monitoring and reporting risk on a group-wide basis, independently from the first line of defence.
  - o Sets the standards via the KBC Risk Management Framework and supports the business in its implementation.
  - o Challenges the business on their risk identification, measurement and response.
  - o Creates oversight over 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.



This “Three lines of defence” model ultimately reinforces the resilience of KBC's risk and control environment and safeguards the sustainability of the business model.

### **Compliance function**

The compliance function is part of the 2nd line of defence.

The compliance charter details the scope, responsibilities and governance of the compliance function. The Compliance Officer ensures that the charter is approved by the Board of Directors when acting as Audit Risk and Compliance Committee. The Compliance Charter was updated and approved in April 2016.

### **Function holders**

For KBC Group Re, the compliance function is locally grouped with the Risk Management function due to the size of the entity and the nature of its risks. The Local CRO is the key function holder for both functions.

## **B.5 Internal audit function**

The internal audit function of KBC Group Re is exercised by KBC Group Corporate Audit. The responsibilities of Internal Audit are:

- To provide independent assurance to the Board of Directors and management on the effectiveness and efficiency of the processes of risk management, internal control and corporate governance that are in place.
- To support the Board of Directors and management in taking up their responsibilities in these processes.

- To report any serious issues or risks which it becomes aware of and to undertake any required investigations into high-risk situations.
- To make clear and actionable recommendations which address weaknesses noted during its work and to follow up on the implementation status of these recommendations.
- To carry out any assignment or projects entrusted to it by the Board of Directors or the management.

To safeguard its independence and objectivity:

- Internal Audit reports and is accountable to the Board of Directors (acting as Audit Risk and Compliance 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 of KBC Group.
- 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, subject to proper reporting to the Board of Directors.
- Internal Audit has the authority to inform directly, and at its own initiative, the Chairman of the Board of Directors, the Managing Director, the 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.

Internal Audit periodically examines and evaluates the most risky areas of its scope and an audit plan is approved at least once a year by the Board of Directors when acting as Audit Risk and Compliance Committee.

The approach followed in performing the audit assignments is 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 that will communicate the status of this follow-up regularly to Internal Audit, for monitoring purposes.

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



## B.6 Actuarial function

The Actuarial function is one of the key control functions that is defined in the Solvency II regulatory framework. Basically, the task of this function is to ensure that the company's Board of Directors is fully informed in an independent manner. It does this by:

- Advising on the calculation of the technical provisions (a.o. 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
- Reporting and giving recommendations.

Within the KBC Insurance Group, the Actuarial Function is implemented as follows:

- The Actuarial Function operates under the ultimate accountability of the Board of Directors.
- An 'Actuarial Function Holder' is appointed for every local entity and also on KBC Insurance Group level. The Actuarial Function Holder is to be registered on the pay-roll of the entity he/she is representing. Her/his 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 organizational unit but can be assigned to several persons or departments subject to an adequate segregation of duties.
- The Actuarial Function has as basic task 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 a.o. in forming opinions, proposing recommendations and assisting in writing the Actuarial Function Report.

## B.7 Outsourcing

### *Outsourcing principles*

KBC Group Re outsources some of its activities.

In order to manage the risks relating to outsourcing, KBC Group Re has drafted an Outsourcing policy. This policy is applicable on intragroup and external outsourcing, and ensures that the company remains fully responsible of the outsourced activities and that the risks relating to these activities are well managed. The policy sets out:

- the definition of outsourcing as applied within KBC Group
- the restrictions, roles and responsibilities relating to outsourcing
- a high level process description, including the monitoring requirements
- principles and necessary clauses for the outsourcing agreements

### *Intragroup outsourcing*

As already stated in the previous sections, part of the control activities are exercised on group level with a view to centralization, independence, consistency and synergy. This includes parts of the Solvency II requirements: Solvency capital requirements calculation, elements of the Best

Estimate of technical provisions (e.g. Risk Margin), automated compilation of part of pillar 3 quantitative reports, ...

The Internal audit function is fully outsourced to KBC Group.

Asset management is outsourced to KBC Asset Management NV.

#### ***External outsourcing***

KBC Group Re outsources parts of its ICT to a certified Luxembourg 'Professionnel du Secteur Financier'.

### **B.8 Any other information**

No other information to report.



## C. Risk profile

KBC Group Re is exposed to a number of typical industry-specific risks such as movements in interest rates and exchange rates, insurance risks, credit risks, operational risks, etc.

The Risk Appetite Statement of KBC Group Re reflects the view of the Board of Directors and management on risk taking in general and in particular on the acceptable level and composition of risks in coherence with the desired return. For the most material risks, this leads to the following risk appetite and risk profile:

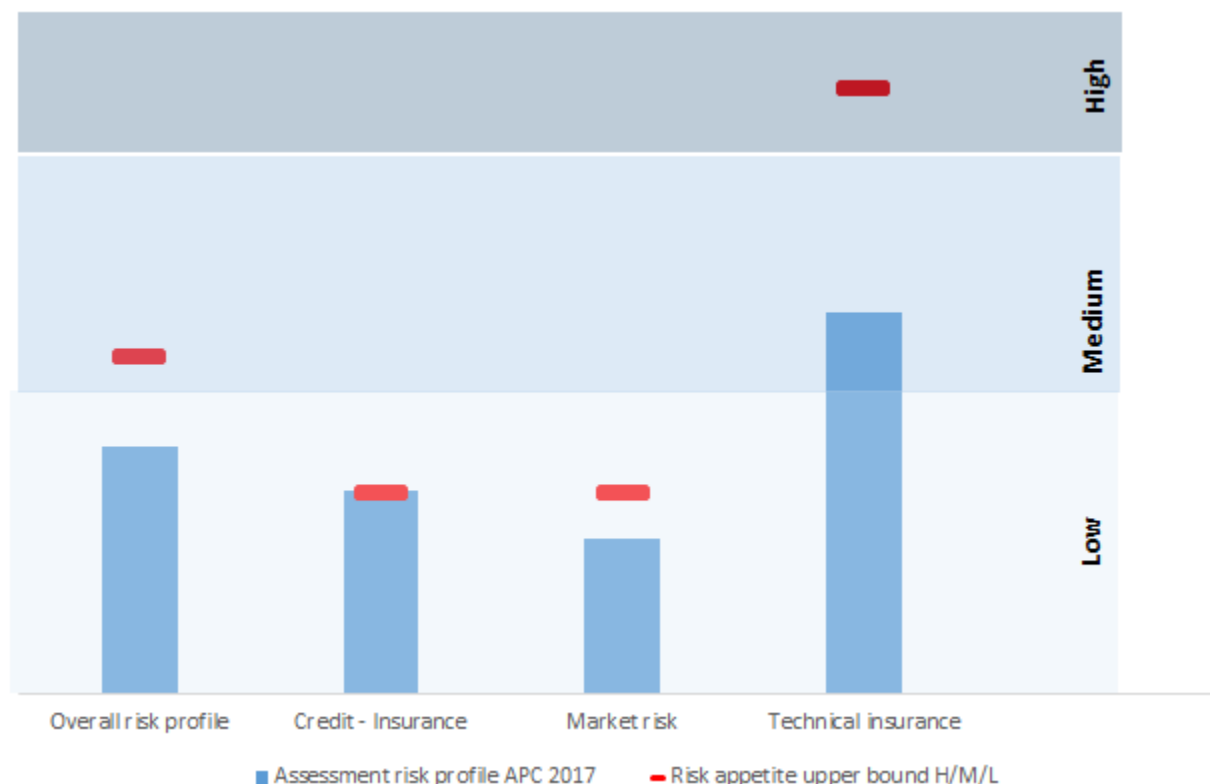


Figure 1 2017 Risk profile and Risk appetite of KBC Group Re

The latest assessment of the risk profile shows that, overall as well as for every risk type separately, the company remains within its risk appetite.

Figure 2 shows the amount of capital requirement based on the standard model as prescribed by the Solvency II regime which is in place since 01/01/2016. The required capital stood at 54,2 million EUR at year-end 2016, compared to an amount of available capital of 335,6 million EUR: the solvency ratio consequently amounts to 619%.

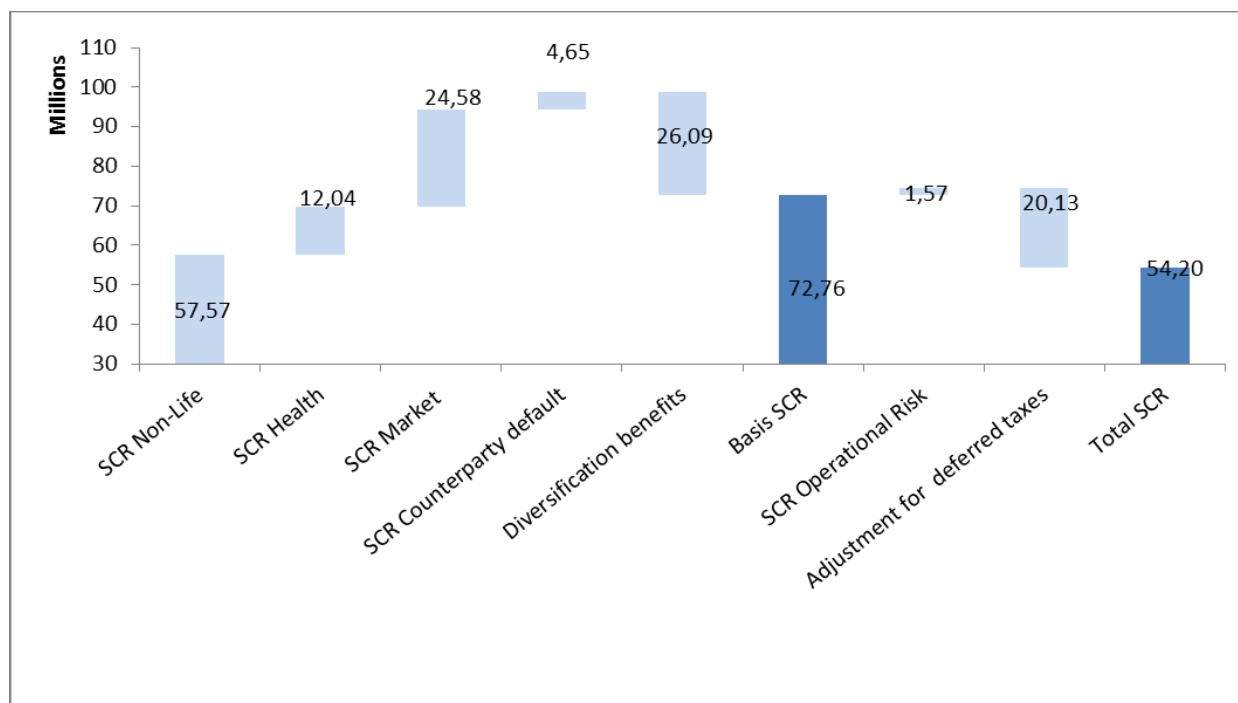


Figure 2 KBC Group Re Solvency II capital requirement as at 31/12/2016

## C.1 Underwriting risk

The 'Underwriting risk' or 'Technical Insurance risk' stems from uncertainty regarding the frequency of insured losses and how extensive they will be. As KBC Group Re is not active in life reinsurance, underwriting risk manifests itself in the non-life portfolio only (including health).

Underwriting risks can be divided into the following main types:

- Premium and reserve risks, which result from fluctuations in the timing, frequency and severity of insured events, and in the timing and amount of claim settlements
- Catastrophe risks, which result from significant uncertainty of pricing and provisioning assumptions related to extreme or exceptional events

All these risks are kept under control through appropriate underwriting, claims reserving and reinsurance policies, and through independent insurance risk management.

As described in section A.1, KBC Group Re is the reinsurance subsidiary of KBC Group, specializing in protecting the group's bank and insurance entities. In line with this role of internal reinsurer, some volatility in earnings is allowed as risks are not diversified over a large number of clients or products as for traditional (re)insurance companies. This explains why the risk profile of underwriting risk is predominant in Figure 1 and Figure 2.

Adequate procedures are in place allowing to maintain a sound quality of underwriting with good overall profitability over a complete underwriting cycle and within the prescribed retention limits,

ensuring adherence to the group and local risk appetite. KBC Group Re on top of that holds a large solvency buffer to ensure its solidity.

As seen in Figure 2, SCR for underwriting together represent 69,6 million EUR accounting for 70% of the undiversified basic Solvency II pillar 1 capital requirement. Table 4 highlights a predominance of ‘catastrophe’ risks in line with the company’s role within the KBC Group.

	<i>mln EUR</i>	<b>31/12/2016</b>
SCR Non Life		57,6
<i>Premium and reserve risk</i>		23,2
<i>Catastrophe</i>		47,2
<i>Diversification benefit</i>		-12,8
SCR Health		12,0
<i>Premium and reserve risk</i>		0,8
<i>Catastrophe</i>		11,8
<i>Diversification benefit</i>		-0,6
<b>Total SCR Underwriting risks before diversification</b>		<b>69,6</b>

Table 4 SCR Underwriting Risk of KBC Group Re (31/12/2016)

## C.2 Market risk

Market risk is the risk of potential losses resulting from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments.

The various types of market risk which are discussed in this section are:

- Interest rate risk
- Spread risk
- Currency risk
- Concentration risk

Exposure of KBC Group Re to ‘Equity risk’ and ‘Property risk’ is highly immaterial.

As seen in Figure 2, SCR for market risk represents 24,6 million EUR accounting for 25% of the undiversified basic Solvency II pillar 1 capital requirement. Table 5 shows the predominance of interest rate risks in line with the prudent asset allocation strategy of KBC Group Re (no equity or derivative and moderate exposure to corporate risks).

	<i>mln EUR</i>	<b>31/12/2016</b>
Interest rate risk		19,4
Spread risk		13,4
Currency risk		0,6
Concentration risk		6,0
<b>Total SCR market risk before diversification</b>		<b>39,5</b>
Diversification benefits		14,9
<b>Total SCR after diversification</b>		<b>24,6</b>

Table 5 SCR Market Risk of KBC Group Re (31/12/2016)

### Interest rate risk

Interest rate risk is the risk that the value of assets, liabilities and financial instruments will change due to fluctuations in interest rates.

The main technique used to measure and monitor interest rate risk is the 10 BPV (basis 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 curve. Other techniques such as duration approach and stress testing are also used.

The required capital for interest risk is determined by calculating the impact on the available capital due to changes in the yield curve, and is the maximum loss resulting from (i) an upward shock or (ii) a downward shock according to the prescribed methodology. Due to its high capital buffer and to the low duration of its liabilities, it is the 'upward' shock that applies for KBC Group Re.

### Spread risk

Spread risk is the risk that the value of assets, liabilities and financial instruments will change due to changes in the level or in the volatility of credit spreads over the risk-free interest rates.

This risk is managed via a strategic asset allocation that ensures a well-diversified high-quality investment grade portfolio. Where relevant, credit ratings provided by the external rating agencies are used to select assets and set and monitor limits. A predominant part of the portfolio relates to sovereign exposures as shown in Table 6.

ASSET MIX				
	31/12/2015		31/12/2016	
<i>mln EUR</i>	amount	in %	amount	in %
Cash	5,5	0,9%	15,0	2,5%
<i>of which term deposits</i>	0,0	0,0%	0,0	0,0%
<i>of which cash at bank</i>	5,5	0,9%	15,0	2,5%
Government Bonds	402,0	67,5%	371,3	61,6%
Corporate Bonds	187,9	31,6%	216,2	35,9%
<b>Total</b>	<b>595,3</b>	<b>100,0%</b>	<b>602,6</b>	<b>100,0%</b>

Table 6 Asset Mix KBC Group Re

As shown in Table 7, a limited part of the corporate bonds portfolio is not externally rated. These however relate to high quality issuers.

CORPORATE BONDS - RATING DISTRIBUTION				
Rating	31/12/2015		31/12/2016	
Market value - mln EUR	amount	in %	amount	in %
AAA	42,5	22,6%	18,9	8,8%
AA	25,0	13,3%	51,3	23,7%
A	74,2	39,5%	98,2	45,4%
BBB	31,1	16,5%	31,0	14,3%
BB	8,3	4,4%	2,1	1,0%
Non rated	6,8	3,6%	14,7	6,8%
<b>Total</b>	<b>187,9</b>	<b>100%</b>	<b>216,2</b>	<b>100%</b>

Table 7 Rating distribution of the Corporate bonds portfolio

Table 8 highlights that the country distribution of the sovereign bonds portfolio remained relatively stable.

SOVEREIGN BOND - COUNTRY DISTRIBUTION				
Geographic distribution	31/12/2015		31/12/2016	
Market value - mln EUR	amount	in %	amount	in %
Europe	393,3	97,8%	344,2	92,7%
Supranational	68,2	17,0%	63,2	17,0%
Italy	41,0	10,2%	39,7	10,7%
Spain	36,5	9,1%	36,0	9,7%
Luxemburg	34,7	8,6%	35,8	9,6%
Poland	30,4	7,6%	29,9	8,1%
Belgium	28,4	7,1%	23,5	6,3%
France	33,9	8,4%	23,2	6,2%
Ireland	14,2	3,5%	22,5	6,0%
Latvia	19,1	4,7%	19,9	5,4%
Lithuania	17,2	4,3%	14,6	3,9%
Netherlands	11,7	2,9%	11,4	3,1%
Finland	10,8	2,7%	10,4	2,8%
Other Euro-zone	37,0	9,2%	7,3	2,0%
Other European countries	10,2	2,5%	6,9	1,9%
US	0,0	0,0%	0,0	0,0%
Rest of the world	8,7	2,2%	27,2	7,3%
<b>Total</b>	<b>402,0</b>	<b>100%</b>	<b>371,3</b>	<b>100%</b>

Table 8 Country distribution of the Sovereign bonds portfolio

Within the standard formula of the Solvency II regime, required capital for spread risk is equal to the sum of capital requirement for bonds, structured products and credit derivatives. Of those only the capital requirement for bonds is relevant for KBC Group Re in the absence of structured products or derivatives in the portfolio. The capital requirement depends on (i) the market value, (ii) the modified duration and (iii) the credit quality category.

### Currency risk

Currency risk is the risk that the value of assets, liabilities and financial instruments will change due to changes in the level or in the volatility of currency exchange rates.

Table 9 below provides a view on the exposures.

31 December 2016 (X 1.000 EUR)	CZK	PLN	USD	HUF	BGN
Net Assets			45	43	
Net Liabilities	453	52			10
<b>Net exposure</b>	<b>453</b>	<b>52</b>	<b>45</b>	<b>43</b>	<b>10</b>

Table 9 Exposure to currency risk (31/12/2016)

Currency risk is currently not hedged as materiality is low. A risk budget is determined and followed up.

### Concentration risk

Concentration risk is the risk of an accumulation of exposures with the same counterparty.

To mitigate concentration risk, limits per (non-sovereign) issuer are foreseen in the investment strategy.

## C.3 Credit risk

Credit risk or counterparty default risk reflects in the Solvency II standard formula possible losses due to unexpected default or deterioration in the credit standing of the counterparties and debtors. Assets that are in scope of spread risk are, by definition, not in scope of counterparty default risk, and vice versa.

For KBC Group Re, this affects the following types of exposures or assets:

- Reinsurance
- Cash and deposits
- Deposits with ceding undertakings
- Receivables

In the Solvency II standard formula a distinction is made between two types of exposures:

- Type 1: Exposures that are low diversified but usually have a rating
- Type 2: Exposures that are generally diversified with unrated counterparties

The total requirement for counterparty risk is an aggregation of the capital requirement for type 1 exposure and the capital requirement for type 2 exposure by taking a 75% correlation.

As seen in Figure 2, SCR for counterparty default risk represents 4,7 million EUR accounting for 5% of the undiversified basic Solvency II pillar 1 capital requirement. Further details can be found in Table 10.

<i>mIn EUR</i>	<b>31/12/2016</b>
Type 1	1,8
Type 2	3,2
Diversification benefit	-0,3
<b>SCR Counterparty risk</b>	<b>4,7</b>

**Table 10 SCR Counterparty Risk (31/12/2016)**

To mitigate the risk in respect of reinsurance, minimum target Financial Strength Ratings are required when entering into a reinsurance contract. More stringent requirements apply for long-tail business (like liability).

On top of that, from a KBC Group perspective, entities are limited in taking credit concentration risk in their portfolios by the Portfolio Limit System (PLS). Limits are monitored per asset class, where ceded reinsurance is one class (note that this system also mitigates credit risk in respect of investments). This particular type of credit risk is measured by means of a nominal approach (the maximum loss under reinsurance contracts) and expected loss, among other techniques. Name concentration limits apply, using internal or external ratings.

## **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. Liquidity risk is not quantified in the Solvency Capital Requirement under the Solvency II regime.

Currently, the liquidity risk is managed through monitoring of the Investment Policy. This policy ensures that the investment portfolio consists mainly of highly liquid positions. Recourse to 'repos' transactions is also allowed up to 25 million EUR. Liquidity risk is on top of that mitigated by the possibility figuring in retrocession contracts to request cash claim from reinsurers once contractually determined thresholds have been exceeded.

Table 11 illustrates that 68% of the total assets is considered as having a high liquidity value (the remaining being mostly composed of corporate bonds whose liquidity is important as well taking into account the fact that most bonds are investment grade). The ratio of liquid assets went down due to the increase of corporate bonds in the portfolio, and decrease of covered bonds amongst those corporate investments.

mIn EUR	31/12/2015	31/12/2016
Cash & Bank Deposits	5,5	15,0
Sovereign	402,0	371,3
Covered bonds	42,5	25,0
<i>Covered bonds - credit quality step 1</i>	42,5	13,7
<i>Covered bonds - credit quality step 2</i>	-	11,3
<b>Total liquid assets</b>	<b>449,9</b>	<b>411,3</b>
<b>Total assets</b>	<b>595,3</b>	<b>602,6</b>
<b>Liquid assets as a % of total assets</b>	<b>76%</b>	<b>68%</b>

Table 11 Liquidity of the assets of KBC Group Re

Table 12 shows the maturity profile of assets and liabilities. Assets are in all cases much larger than liabilities, which demonstrates that the company is not exposed to cash shortfall risk even in case of severe deterioration of the liabilities. This is due to the highly comfortable capital situation of KBC Group Re (large amount of surplus in comparison to liabilities).

mIn EUR	2 017	2 018	2 019	2 020	2 021	2 022	2 023	2 024	2 025	2 026	> 2027
Assets	150,2	92,0	92,3	48,7	55,3	35,7	39,8	47,2	29,8	10,0	37,8
Liabilities	15,0	15,0	10,6	5,3	2,3	1,8	1,1	0,9	0,5	0,4	4,4
<b>GAP</b>	<b>135,2</b>	<b>76,9</b>	<b>81,7</b>	<b>43,3</b>	<b>52,9</b>	<b>33,9</b>	<b>38,7</b>	<b>46,3</b>	<b>29,4</b>	<b>9,6</b>	<b>33,4</b>

Table 12 Assets and liabilities gap (31/12/2016)

## 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.

As seen in Figure 2, the SCR operational risk represents 1,6 million EUR accounting for 1,6% of the undiversified basic Solvency II pillar 1 capital requirement.

A single, global framework for managing operational risk applies across the entire group, defined by the Group risk function. In accordance with this framework, operational risk is measured via inter alia:

- Evaluation of the status of internal control for each processes
- Evaluation of the individual risk profile for each specific risk within each process
- Evaluation of the control effectiveness for the controls mitigating those specific risks
- Estimation of the potential impact of the effective operational loss events

Operational risk is mitigated by:

- Controls (group-wide and locally defined)
- Risk transfer via insurance



## C.6 Other material risks

### *Business & strategic risk*

Business risk is the risk arising from changes in external factors (the macroeconomic environment, regulations, client behaviour, competitive landscape, socio-demographic environment, etc.) that impact the demand for and/or profitability of 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 via a risk scan that identifies the top financial and non-financial risks. Besides the risk scan, business and strategic risks are continually monitored by means of risk signals being reported to management.

### *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.

Reputational risk is mostly a secondary or derivative risk since it is usually connected to and will materialise together with another risk. KBC Group refined the Reputational Risk Management Framework in 2016, in line with the KBC Risk Management Framework. The pro-active and re-active management of reputational risk is the responsibility of the business. 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.

## 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 observing how risk measurements would evolve under stressed conditions. These sensitivity exercises are performed on a regular basis.

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 and limit setting, etc.). As such, stress testing is an integral part of the risk management framework, and an important building block of ORSA (the Own Risk and Solvency Assessment).

Stress tests can be initiated by the regulators (EIOPA, group regulator or local regulator), or be performed internally (within the insurance group or locally).

## D. Valuation for solvency purposes

This chapter contains information regarding the valuation of the balance sheet items. A detailed situation as per end 2016 can be found in Table 13. A more detailed composition of the Solvency II values can be found in the QRT S.02.01.02 regarding the "Balance Sheet".

For each material class of assets or liabilities:

- The bases, methods and main assumptions used for valuation for solvency purposes are described
- A quantitative and qualitative explanation of any material difference between the valuation for solvency purposes and the valuation in the financial statements is given.

31/12/2016 (X 1.000 EUR)	LuxGaap Value	Solvency II Value	Delta
Intangible assets	71	0	-71
Investments	549 259	587 556	38 297
<i>Equities</i>	1	1	0
<i>Bonds</i>	549 258	587 555	38 297
Deposits to cedants	16 188	16 188	0
Technical provisions - part of reinsurance	12 963	4 794	-8 169
Receivables	5 508	5 508	0
Cash	15 017	15 016	0
Tangible assets	86	86	0
Other assets	5 559	5 559	0
<b>TOTAL ASSETS</b>	<b>604 649</b>	<b>634 707</b>	<b>30 057</b>
Technical provisions	431 060	67 626	-363 434
<i>TP representing liabilities</i>	74 857	52 266	-22 591
<i>Risk Margin</i>		15 361	15 361
<i>Equalization Provision</i>	356 203	0	-356 203
Other provisions	39 060	39 060	0
Deposits from reinsurers	2 978	2 978	0
Payables	1 914	1 914	0
Deferred taxes	0	106 557	106 557
Other liabilities	0	0	0
<b>TOTAL LIABILITIES</b>	<b>475 012</b>	<b>218 136</b>	<b>-256 876</b>
<b>Excess of Assets over liabilities</b>	<b>129 637</b>	<b>416 571</b>	<b>286 934</b>

Table 13 Valuation of assets and liabilities in the financial statements and within Solvency II

## D.1 Assets

### D.1.1 FAIR VALUE MEASUREMENT

In line with the Delegated regulation, valuation of financial assets for solvency purposes is based on 'fair value'. The following three hierarchical levels are used to determine the fair value:

#### **Level 1: Fair value based on quoted prices in active markets**

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. They represent actual and regularly occurring market transactions on an arm's length basis. No valuation technique (model) is in this case involved.

#### **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 independent sources. 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 about the 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.

### D.1.2 MAIN ASSETS CATEGORY

#### *Intangible assets*

Intangible assets cannot be sold separately and are not recognized in the Solvency II framework: valuation for solvency purposes is set to nil.

In the LuxGaap financial statements, those assets (mostly software licenses) are valued at acquisition costs, and depreciated on a straight-line basis over their estimated useful lives.

#### *Investments*

Investments of KBC Group Re are mostly composed of bonds (99,99%).

Valuation for solvency purposes is based on 'fair value' as defined in section D.1.1.

In the LuxGaap financial statements, investments in bonds are measured at amortised cost, minus impairments when it is expected that the impairment in value is permanent in nature

#### *Technical provisions – part of reinsurance*

See section D.2.

### **Deposits to cedants**

Deposits to cedants are valued at their nominal value, both in LuxGaap and for solvency purposes. Value adjustments are made when the realisable value is uncertain.

### **Receivables**

Receivables are valued at their nominal value, both in LuxGaap and for solvency purposes. Value adjustments are made when the realisable value is uncertain.

### **Cash**

Cash is valued at fair value, both in LuxGaap and in Solvency II.

## **D.2 Technical provisions**

KBC Group Re is exclusively active in non-life reinsurance (this includes health which is underwritten according to non-life principles). Technical Provisions of pure non-life and health policies are measured in a common process with identical methods and main assumptions. As such, both can be considered as a single business activity.

### **D.2.1 TECHNICAL PROVISIONS – VALUATION FOR SOLVENCY PURPOSES**

In general, the technical provisions on the Solvency II economical balance sheet have to be calculated as the sum of a Best Estimate and a risk margin:

- 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 (re)insurance obligations over their lifetime. The cost of capital is defined by the regulator and is set at 6%.

When calculating the Best Estimate, a projection of the estimated future cash flows is consequently made. Those cash flows are subsequently discounted using the risk free interest rate term structure, prescribed by the regulator.

The calculation of the Best Estimate requires the contracts to be split up in homogeneous risk groups. These are groups with similar characteristics and dynamics, for which the same assumptions are then used when projecting the cash flows in the future. The company therefore makes a distinction between 'short-tail' and 'long-tail' lines of business.

Solvency II requires calculations to be performed separately for 'premium provisions' and 'provisions for claims outstanding'. Both types of provisions are calculated according to different (standard) actuarial techniques.

Part of the reinsurers in both types of provisions is determined as the difference between the gross and the net of reinsurance provisions, less an adjustment for expected (mean) reinsurers' default.

### **Premium provision**

The premium provision relates to claim events occurring after the valuation date and during the remaining in-force period (coverage period) of existing policies held by the undertaking.

The calculation of the gross Best Estimate of the premium provisions relates to:

- All expected future premiums for existing policies
- All future claim payments for existing policies, arising from future events past the valuation date.
- All expenses related to the above: allocated or unallocated claims expenses, ongoing administration of these policies, future acquisition costs, overhead expenses, ...

The premium provision is calculated on the assumption that the portfolio of policies in the risk group is stable enough, such that claims experience from the past can be used to make predictions of claims that will occur in the future. Also the assumptions regarding the timing of future cash flows are based upon past claims experience.

### **Provisions for claims outstanding**

The provisions for claims outstanding relate to claim events that have already occurred but are not settled yet, regardless of whether the claims arising from these events have been reported or not.

Different techniques are used, depending on the claim size: attritional claims are valued using actuarial techniques while large claims are valued on an individual claim level. An estimate is also made for those claims that have already occurred but have not yet been reported at valuation date. The Best Estimate for claims outstanding also includes provisions for claim handling costs, both internal and external.

### **Impact of volatility adjustment**

KBC Group Re applies the volatility adjustment for discounting cash flows to determine the Best Estimate. Table 14 shows the moderate impact of this volatility adjustment.

31/12/2016 (X 1.000 EUR)	Amount with Volatility adjustment	Impact of volatility adjustment set to zero
Technical provisions	62 832	212
Basic own funds	335 616	-155
Eligible own funds to meet Solvency Capital Requirement	335 616	-155
Solvency Capital Requirement	54 199	0
Eligible own funds to meet Minimum Capital Requirement	335 616	-155
Minimum Capital Requirement	13 550	0

**Table 14 Impact of the volatility adjustment (31/12/2016)**

### **Level of uncertainty**

In line with the Solvency II requirements, the uncertainty on the Technical Provisions is assessed. Within the KBC Group this is done via a 'Measurement risk assessment' process.

Due to its role of internal reinsurer of KBC Group, gross results of KBC Group Re are very volatile and single large claims dominate the technical provisions. For KBC Group Re, the 'Measurement risk assessment' consequently reveals that uncertainty around the final amount of Technical provisions is high. The Best Estimate calculation process is to an important extent based on expert judgement for the large claims and a large amount of uncertainty cannot be avoided.

KBC Group Re compensates this phenomenon with a sound capital and reinsurance policy.

### ***D.2.2 TECHNICAL PROVISIONS – LUXGAAP VALUATION***

In LuxGaap a distinction is made between the following types of provisions:

- Provision for unearned premiums
- Provision for claims outstanding
- Equalization provision

Those provisions are not discounted.

#### ***Provision for unearned premiums***

The provision for unearned premiums comprises the amount representing the part of premiums written which is to be allocated to subsequent financial years. It is computed separately for each contract.

This applies to gross premiums and premiums ceded to reinsurers.

#### ***Provision for claims outstanding***

The provision for claims is established on the basis of reports and individual estimates received from the ceding companies, where necessary supplemented with other information available. The amount of provision ceded to reinsurers is then calculated based on contractual agreements.

For 'claims incurred but not reported' at balance sheet date, an IBNR (Incurred But not Reported) provision is set aside. This IBNR provision is calculated using actuarial techniques.

A provision for the internal costs of settling claims is calculated at a percentage that is based on past experience.

#### ***Equalization provision***

In accordance with the rules applicable for reinsurance companies in Luxembourg, an equalization provision must be established by KBC Group Re. Based on the grand du cal regulation relating to the supervision of reinsurance companies, the annual allocation to this provision equals the sum of the technical results and a share of the financial result until the provision reaches a ceiling. This ceiling is determined by applying to the net reinsurance premiums a multiple based on actuarial methods and approved by the local supervisor (multiples depend on the risk bucket).

In the event of a loss in a subsequent accounting period, a share of the equalization provision must be reintegrated into the result of the year in order to compensate for the loss.

This provision is not recognized under the Solvency II regime and set to nil. This complies with the fair value valuation principle.

## D.3 Other liabilities

Other liabilities mainly relate to tax provisions and deferred taxes:

- Current tax provisions: the estimated amount of taxes payable until valuation date serves as valuation amount both for solvency purposes and in the LuxGaap financial statements.
- Deferred taxes result from the netting of deferred tax liabilities over deferred tax assets. Those deferred taxes are not recognized in the LuxGaap statements and arise from:
  - o Carry forwards of unused tax losses (deferred tax asset)
  - o Temporary differences between the SII value of assets and liabilities and their value as recognized for tax purposes
  - o

Net deferred tax liability amounts as per 31/12/2016 to 106,6 million EUR, mainly due to a difference in the valuation of technical provisions (non-recognition of the equalization provision in Solvency II).

## D.4 Alternative methods for valuation

Not applicable for KBC Group Re.

## D.5 Any other information

Other material information about valuation does not apply.

## E. Capital Management

The solvency of KBC Group Re is calculated on the basis of the Solvency II regime.

The minimum solvency ratio required by the regulator amounts to 100% of the Solvency Capital Requirement (SCR). Within KBC Group, the capital management process aims at reaching an optimal balance between regulatory requirements, rating agencies views, market expectations and management ambitions. It is a key management process relating to all decisions on the level and composition of the capital, both at group level and locally.

An important process in this context is the Alignment of Planning Cycles (APC). As explained in Chapter B, this yearly process aims to create an integrated three-year plan in which the strategy, finance, treasury and risk perspectives are collectively taken into account. In this process, the risk appetite of the group is set and cascaded by setting risk limits at entity level. The APC is not only about planning: it is also about closely monitoring the execution of the plan in all its aspects.

Next to APC, an Own Risk and Solvency Assessment (ORSA) is conducted on a regular basis, in accordance with Solvency II requirements. The aim of the ORSA is to monitor and ensure that business is managed in a sound and prudent way and that the company is adequately capitalised in view of its risk profile and the quality of its risk management and control environment.

### E.1 Own funds

Solvency II regulations require the (re)insurance companies to classify own-fund items in accordance with quality criteria into three tiers. Classification depends upon whether they are basic own fund or ancillary own-fund items, and the extent to which they possess the following characteristics:

- 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)
- 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 1** capital consists of basic own funds that present both the permanent availability and subordination characteristics

**Tier 2** capital consists of ancillary own funds and of basic own funds that present only the subordination characteristics

**Tier 3** capital consists of any basic or ancillary own funds that are not classified as tier 1 and tier 2.

Table 15 details the capital position of KBC Group Re, which is exclusively composed of Tier 1 items.



(X 1.000 EUR)	31/12/2016	31/12/2015
<b>Own funds - Tier 1</b>	335 616	393 251
LuxGaap shareholders equity	129 637	71 702
Dividend payout (-)	-80 955	-25 840
Deduction intangible fixed assets	-71	-83
Valuation difference investments	38 297	40 333
Valuation difference technical liabilities	355 265	452 275
<i>of which equalization provision</i>	<i>356 203</i>	<i>455 794</i>
Deferred taxes	-106 557	-145 136

**Table 15 Capital position of KBC Group Re**

An extensive explanation of the reconciliation from the LuxGaap equity to the Solvency II eligible own funds is presented in Chapter D.

By the end of 2016, Tier 1 Own funds amounted 335,6 million EUR, eligible to cover both the Minimum Capital Requirement and Solvency Capital Requirement. The decrease compared to year-end 2015 is due to a reduction of the equalization provision in the LuxGaap financial statements that gave rise to a large dividend pay-out.

More information about the “Own funds” can be found in the QRT S.23.01.22.

## **E.2 Solvency Capital Requirement & Minimum Capital Requirement**

The Solvency Capital Requirement and Minimum Capital requirement are calculated based on the standard model. No (partial or full) internal model is used. KBC Group Re does not use simplifications or undertaking specific parameters when applying the standard formula.

A detailed split of Solvency Capital Requirement by risk modules can be found in Figure 2 in Chapter C, where individual risk profiles are also extensively discussed.

KBC Group Re met the solvency requirements. As can be seen in Table 16, the solvency ratio stood at 619% at 31/12/2016.

(X 1.000 EUR)	31/12/2016
<b>Own funds - Tier 1</b>	67 779
Solvency capital requirement (SCR)	54 199
Ratio of Eligible own funds to SCR	619%
Minimum capital requirement (MCR)	13 550
Ratio of Eligible own funds to MCR	2477%

**Table 16 Solvency ratios of KBC Group Re (31/12/2016)**

More information can be found in the Quantitative Reporting Template (QRT) S.25.01.22.

### **E.3 Use of the duration-based equity risk sub-module in the calculation of SCR**

Not applicable for KBC Group Re.

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

Not applicable for KBC Group Re.

### **E.5 Non-compliance with the MCR and non-compliance with the SCR**

KBC Group Re is compliant with the Minimal Capital Requirement as well as with the Solvency Capital Requirement.

### **E.6 Any other information**

No other information to report.

# ANNEXES

## S.02.01.02 – Balance sheet (x 1.000 EUR)

		Solvency II value		Solvency II value
		C0010		C0010
<b>Assets</b>			<b>Liabilities</b>	
Goodwill	R0010		Technical provisions – non-life	R051067626,188
Deferred acquisition costs	R0020		Technical provisions – non-life (excluding health)	R052064227,501
Intangible assets	R0030	0	Technical provisions calculated as a whole	R05300
Deferred tax assets	R0040	0	Best Estimate	R054050710,951
Pension benefit surplus	R0050	0	Risk margin	R055013516,55
Property , plant & equipment held for own use	R0060	85,617	Technical provisions - health (similar to non-life)	R05603398,687
Investments (other than assets held for index-linked and unit-linked contracts)	R0070	587555,822	Technical provisions calculated as a whole	R05700
Property (other than for own use)	R0080	0	Best Estimate	R05801554,682
Holdings in related undertakings, including participations	R0090	0	Risk margin	R05901844,005
	R0100	0,799	Technical provisions - life (excluding index-linked and unit-linked)	R06000
Equities	R0110	0	Technical provisions - health (similar to life)	R06100
Equities - listed	R0120	0,799	Technical provisions calculated as a whole	R06200
Equities - unlisted	R0130	587555,023	Best Estimate	R06300
Bonds	R0140	371348,498	Risk margin	R06400
Government Bonds			Technical provisions – life (excluding health and index-linked and unit-linked)	R06500
Corporate Bonds	R0150	216206,525	Technical provisions calculated as a whole	R06600
Structured notes	R0160	0	Best Estimate	R06700
Collateralised securities	R0170	0	Risk margin	R06800
Collective Investments Undertakings	R0180	0	Technical provisions – index-linked and unit-linked	R06900
Derivatives	R0190	0	Technical provisions calculated as a whole	R07000
Deposits other than cash equivalents	R0200	0	Best Estimate	R07100
Other investments	R0210	0	Risk margin	R07200
Assets held for index-linked and unit-linked contracts	R0220	0	Other technical provisions	R0730
Loans and mortgages	R0230	0	Contingent liabilities	R07400
Loans on policies	R0240	0	Provisions other than technical provisions	R075039059,722
Loans and mortgages to individuals	R0250	0	Pension benefit obligations	R07600
Other loans and mortgages	R0260	0	Deposits from reinsurers	R07702978,194
Reinsurance recoverables from:	R0270	4794,356	Deferred tax liabilities	R0780106557,482
Non-life and health similar to non-life	R0280	4794,356	Derivatives	R07900
Non-life excluding health	R0290	4794,356	Debts owed to credit institutions	R08000
Health similar to non-life	R0300	0	Financial liabilities other than debts owed to credit institutions	R08100
Life and health similar to life, excluding health and index-linked and unit-linked	R0310	0	Insurance & intermediaries payables	R082032,094
Health similar to life	R0320	0	Reinsurance payables	R08301837,258
Life excluding health and index-linked and unit-linked	R0330	0	Payables (trade, not insurance)	R084044,694
Life index-linked and unit-linked	R0340	0	Subordinated liabilities	R08500
Deposits to cedants	R0350	16187,735	Subordinated liabilities not in Basic Own Funds	R08600
Insurance and intermediaries receivables	R0360	4527,264	Subordinated liabilities in Basic Own Funds	R08700
Reinsurance receivables	R0370	980,417	Any other liabilities, not elsewhere shown	R08800
Receivables (trade, not insurance)	R0380	0	<b>Total liabilities</b>	R0900218135,632
Own shares (held directly)	R0390	0	<b>Excess of assets over liabilities</b>	R1000416570,931
Amounts due in respect of own fund items or initial fund called up but not yet paid in	R0400	0		
Cash and cash equivalents	R0410	15016,409		
Any other assets, not elsewhere shown	R0420	5558,943		
<b>Total assets</b>	R0500	634706,563		

## S.05.01.02 – Premiums, claims and expenses by line of business (non-life insurance and reinsurance obligations) (x 1.000 EUR)

Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted proportional reinsurance)																		Line of Business for:					
accepted non-proportional reinsurance																		Total					
Medical expense insurance																		Property					
Income protection insurance																		Marine, aviation, transport					
Workers' compensation insurance																		Casualty					
Motor vehicle liability insurance																		Health					
Other motor insurance																		Miscellaneous financial loss					
Marine, aviation and transport insurance																		Credit and surety ship insurance					
Fire and other damage to property insurance																		General liability insurance					
C0070																		C0080					
C0090																		C0100					
C0110																		C0120					
C0130																		C0140					
C0150																		C0160					
C0200																		C0200					
Premiums written																							
Gross - Direct Business																							
R0110																							
Gross - Proportional reinsurance accepted																							
R0130																							
Gross - Non-proportional reinsurance accepted																							
R0140																							
Reinsurers' share																							
Net																							
Premiums earned																							
Gross - Direct Business																							
R0210																							
Gross - Proportional reinsurance accepted																							
R0220																							
Gross - Non-proportional reinsurance accepted																							
R0230																							
Reinsurers' share																							
Net																							
Claims incurred																							
Gross - Direct Business																							
R0310																							
Gross - Proportional reinsurance accepted																							
R0330																							
Gross - Non-proportional reinsurance accepted																							
R0340																							
Reinsurers' share																							
Net																							
Changes in other technical provisions																							
Gross - Direct Business																							
R0410																							
Gross - Proportional reinsurance accepted																							
R0420																							
Gross - Non-proportional reinsurance accepted																							
R0430																							
Reinsurers' share																							
Net																							
Expenses incurred																							
R0550																							
Other expenses																							
R1200																							
Other expenses																							
R1300																							

## S.05.02.01 – Premiums, claims and expenses by country (non-life obligations) (x1.000 EUR)

		Home Country	Top 5 countries (by amount of gross premiums written) - non-life obligations					Total Top 5 and home country
		C0010						C0070
	R0010		BE	BG	CZ	IE	GB	
		C0080						C0140
<b>Premiums written</b>								
Gross - Direct Business	R0110							
Gross - Proportional reinsurance accepted	R0120	0	14467	35	594	824	799	16718
Gross - Non-proportional reinsurance accepted	R0130	0	11620	1566	3171	0	0	16357
Reinsurers' share	R0140	0	8592	884	1916	0	0	11392
Net	R0200	0	17495	716	1849	824	799	21683
<b>Premiums earned</b>								
Gross - Direct Business	R0210							
Gross - Proportional reinsurance accepted	R0220	1	14467	35	594	737	799	16633
Gross - Non-proportional reinsurance accepted	R0230	0	11620	1566	3171	0	0	16357
Reinsurers' share	R0240	0	8592	884	1916	0	0	11392
Net	R0300	1	17495	716	1849	737	799	21598
<b>Claims incurred</b>								
Gross - Direct Business	R0310							
Gross - Proportional reinsurance accepted	R0320	87	-8914	0	107	332	158	-8229
Gross - Non-proportional reinsurance accepted	R0330	-28	21385	554	2888	-2	0	24796
Reinsurers' share	R0340	582	-3865	-244	1710	18	21	-1778
Net	R0400	-524	16336	798	1285	313	138	18345
<b>Changes in other technical provisions</b>								
Gross - Direct Business	R0410							
Gross - Proportional reinsurance accepted	R0420							
Gross - Non- proportional reinsurance accepted	R0430							
Reinsurers' share	R0440							
Net	R0500							
<b>Expenses incurred</b>	R0550	-56	1396	223	603	355	134	2655
<b>Other expenses</b>	R1200							
<b>Total expenses</b>	R1300							2655

## SOLVENCY AND FINANCIAL CONDITION REPORT 2016

[illegible]

## S.22.01.22 – Impact of long term guarantees and transitional measures (X1.000 EUR)

		Amount with Long Term Guarantee measures and transitionals	Impact of transitional on technical provisions	Impact of transitional on interest rate	Impact of volatility adjustment set to zero	Impact of matching adjustment set to zero
		C0010	C0030	C0050	C0070	C0090
Technical provisions	<b>R0010</b>	62832			212	
Basic own funds	<b>R0020</b>	335616			-155	
Eligible own funds to meet Solvency Capital Requirement	<b>R0050</b>	335616			-155	
Solvency Capital Requirement	<b>R0090</b>	54199			0	
Eligible own funds to meet Minimum Capital Requirement	<b>R0100</b>	335616			-155	
Minimum Capital Requirement	<b>R0110</b>	13550			0	

## S.23.01.22 – Own funds (X1.000 EUR)

### Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35

Ordinary share capital (gross of own shares)  
 Share premium account related to ordinary share capital  
 Initial funds, members' contributions or the equivalent basic own - fund item for mutual and mutual-type undertakings  
 Subordinated mutual member accounts  
 Surplus funds  
 Preference shares  
 Share premium account related to preference shares  
 Reconciliation reserve  
 Subordinated liabilities  
 An amount equal to the value of net deferred tax assets  
 Other own fund items approved by the supervisory authority as basic own funds not specified above

### Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds

Own funds from the financial statements that should not be represented by the reconciliation reserve and do not meet the criteria to be classified as Solvency II own funds

### Deductions

Deductions for participations in financial and credit institutions

### Total basic own funds after deductions

### Ancillary own funds

Unpaid and uncalled ordinary share capital callable on demand  
 Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand  
 Unpaid and uncalled preference shares callable on demand  
 A legally binding commitment to subscribe and pay for subordinated liabilities on demand  
 Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC  
 Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC  
 Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC  
 Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC  
 Other ancillary own funds

### Total ancillary own funds

### Available and eligible own funds

Total available own funds to meet the SCR  
 Total available own funds to meet the MCR  
 Total eligible own funds to meet the SCR  
 Total eligible own funds to meet the MCR

### SCR

### MCR

### Ratio of Eligible own funds to SCR

### Ratio of Eligible own funds to MCR

### Reconciliation reserve

Excess of assets over liabilities  
 Own shares (held directly and indirectly)  
 Foreseeable dividends, distributions and charges  
 Other basic own fund items  
 Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds

### Reconciliation reserve

### Expected profits

Expected profits included in future premiums (EPIFP) - Life business  
 Expected profits included in future premiums (EPIFP) - Non- life business

### Total Expected profits included in future premiums (EPIFP)

	Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
	C0010	C0020	C0030	C0040	C0050
R0010	41692,987	41692,987		0	
R0030	0	0		0	
R0040	0	0		0	
R0050	0		0	0	0
R0070	6989,548	6989,548			
R0090	0		0	0	0
R0110	0		0	0	0
R0130	286933,854	286933,854			
R0140	0		0	0	0
R0160	0				0
R0180	0	0	0	0	0
R0220	0				
R0230	0	0	0	0	
R0290	335616,389	335616,389	0	0	0
R0300	0			0	
R0310	0			0	
R0320	0			0	0
R0330	0			0	0
R0340	0			0	
R0350	0			0	0
R0360	0			0	
R0370	0			0	0
R0390	0			0	0

	Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
	C0010	C0020	C0030	C0040	C0050
R0400	0			0	0
R0500	335616,389	335616,389	0	0	0
R0510	335616,389	335616,389	0	0	
R0540	335616,389	335616,389	0	0	0
R0550	335616,389	335616,389	0	0	
R0580	54198,69914				
R0600	13549,675				
R0620	619,2333%				
R0640	2476,9331%				

	C0060
R0700	416570,931
R0710	0
R0720	80954,542
R0730	48682,535
R0740	0
R0760	286933,854
R0770	0
R0780	4901,212
R0790	4901,212



## S.25.01.22 – Solvency capital requirement (for groups on Standard Formula) (X1.000 EUR)

	Gross solvency capital requirement	USP	Simplifications
	C0110	C0090	C0100
Market risk	R0010 24580,653		
Counterparty default risk	R0020 4654,793		
Life underwriting risk	R0030 0		
Health underwriting risk	R0040 12040,623		
Non-life underwriting risk	R0050 57568,97		
Diversification	R0060 -26086,761		
Intangible asset risk	R0070 0		
<b>Basic Solvency Capital Requirement</b>	R0100 72758,278		

### Calculation of Solvency Capital Requirement

	C0100
Operational risk	R0130 1567,969
Loss-absorbing capacity of technical provisions	R0140 0
Loss-absorbing capacity of deferred taxes	R0150 -20127,548
Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	R0160 0
<b>Solvency capital requirement excluding capital add-on</b>	R0200 54198,699
Capital add-on already set	R0210 0
<b>Solvency capital requirement</b>	R0220 54198,699
<b>Other information on SCR</b>	
Capital requirement for duration-based equity risk sub-module	R0400 0
Total amount of Notional Solvency Capital Requirement for remaining part	R0410 54198,699
Total amount of Notional Solvency Capital Requirements for ring fenced funds	R0420 0
Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	R0430 0
Diversification effects due to RFF nSCR aggregation for article 304	R0440 0

## S.28.01.01 Minimum Capital Requirement - Only life or only non-life insurance or reinsurance activity (X1.000 EUR)

### Linear formula component for non-life insurance and reinsurance obligations

MCRNL Result

	<b>C0010</b>
<b>R0010</b>	10883,3

Medical expense insurance and proportional reinsurance  
Income protection insurance and proportional reinsurance  
Workers' compensation insurance and proportional reinsurance  
Motor vehicle liability insurance and proportional reinsurance  
Other motor insurance and proportional reinsurance  
Marine, aviation and transport insurance and proportional reinsurance  
Fire and other damage to property insurance and proportional reinsurance  
General liability insurance and proportional reinsurance  
Credit and suretyship insurance and proportional reinsurance  
Legal expenses insurance and proportional reinsurance  
Assistance and proportional reinsurance  
Miscellaneous financial loss insurance and proportional reinsurance  
Non-proportional health reinsurance  
Non-proportional casualty reinsurance  
Non-proportional marine, aviation and transport reinsurance  
Non-proportional property reinsurance

	Net (of reinsurance/SPV ) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
	<b>C0020</b>	<b>C0030</b>
<b>R0020</b>	0	0
<b>R0030</b>	67,953	20,365
<b>R0040</b>	564,79	0
<b>R0050</b>	1,252	0
<b>R0060</b>	0	0
<b>R0070</b>	0	147,957
<b>R0080</b>	523,257	2811,763
<b>R0090</b>	10808,958	6243,851
<b>R0100</b>	0	0
<b>R0110</b>	0	0
<b>R0120</b>	25,015	35,74
<b>R0130</b>	1750,729	3156,039
<b>R0140</b>	921,939	180,106
<b>R0150</b>	15355,422	2515,67
<b>R0160</b>	63,509	172,36
<b>R0170</b>	17431,158	7195,686

### Linear formula component for life insurance and reinsurance obligations

MCRL Result

	<b>C0040</b>
<b>R0200</b>	0

Obligations with profit participation - guaranteed benefits  
Obligations with profit participation - future discretionary benefits  
Index-linked and unit-linked insurance obligations  
Other life (re)insurance and health (re)insurance obligations  
Total capital at risk for all life (re)insurance obligations

	Net (of reinsurance/SPV ) best estimate and TP calculated as a whole	Net (of reinsurance/SPV ) total capital at risk
	<b>C0050</b>	<b>C0060</b>
<b>R0210</b>		
<b>R0220</b>		
<b>R0230</b>		
<b>R0240</b>		
<b>R0250</b>		

### Overall MCR calculation

Linear MCR  
SCR  
MCR cap  
MCR floor  
Combined MCR  
Absolute floor of the MCR

	<b>C0070</b>
<b>R0300</b>	10883,3
<b>R0310</b>	54198,7
<b>R0320</b>	24389,4
<b>R0330</b>	13549,7
<b>R0340</b>	13549,7
<b>R0350</b>	1200
	<b>C0070</b>
<b>R0400</b>	13549,7

**Minimum Capital Requirement**