MAPFRE | MIDDLESEA

MAPFRE Middlesea P.L.C

Solvency and Financial Condition Report
31st December 2019

Contents

Executive Summary

The Solvency and Financial Condition Report is aligned with the requirements of Directive 2009/138/EC (Solvency II Directive) and the Commission Delegated Regulation (EU) 2015/35.

A. Business and Performance

MAPFRE Middlesea plc (hereinafter the Company, MAPFRE Middlesea or MMS) is a composite insurance company with primary activities being underwriting of non-life and group life risk. It accepts risks on the following Solvency II lines of business:

- Medical expense insurance
- Income protection insurance
- Motor vehicle liability insurance
- Other Motor insurance
- Marine, Aviation and Transport insurance
- Fire and other damage to property insurance
- General liability insurance
- Assistance
- Miscellaneous financial loss
- Other life insurance

MAPFRE Middlesea is a subsidiary of MAPFRE S.A. and forms part of the MAPFRE Group, composed of MAPFRE S.A. and various companies operating in insurance, financial, property and service industries.

The company closed the year with written premiums amounting to €74.38 million, experiencing an increase of 6.7 percent over 2018, with growth registered in almost all non-life classes of business. Total gross claims incurred have increased by 1.2 percent over 2018 and amounted to €39.87 million.

MMS's net combined ratio at 90.3% shows an improvement of 2.6 percentage points compared to the previous year, with both years being impacted by significant loss events. The core business experienced an improvement in particular emanating from the motor line of business following an improvement in ultimate loss claim projections whilst run-off business returned an improved result following closure of long outstanding claims.

During 2019, MMS's technical results were impacted by the February windstorm that affected a number of classes but particularly Property. In Motor, large losses involving fatalities or grievous bodily injury, incurred during the year or adjusted from those reserved in previous years continue to take their toll on the technical results, particularly in accidents involving foreign nationals.

Total net investment income during the year amounted to €19.52 million compared with the €8.08 million registered in 2018. The main source remains the dividends received from Group companies.

B. System of Governance

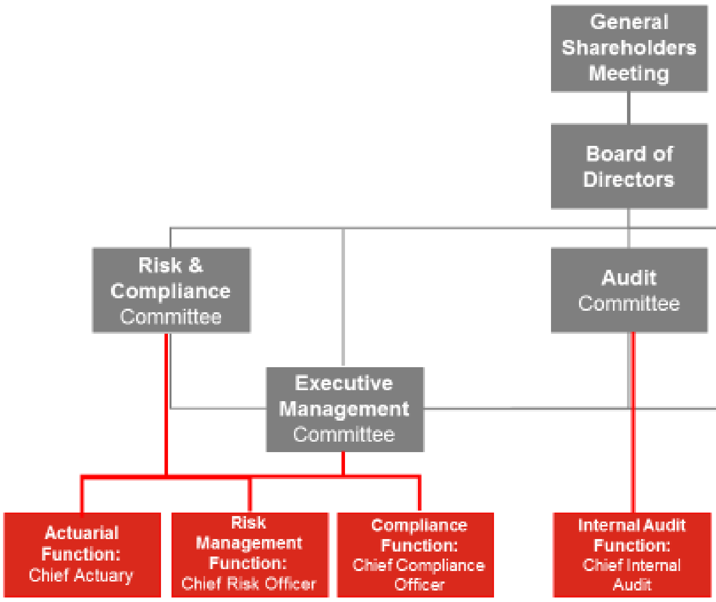
MMS's Governing Bodies at 31st December 2019 are set out below:

- Shareholder's Annual General Meeting
- Board of Directors
- Audit Committee

- Risk and Compliance Committee
- Investment Committee
- Remuneration Committee
- Management Committee

In addition to the above, MMS is supervised by the EURASIA Regional Management Committee within the MAPFRE GROUP, which directly supervises the management of regional Business Units.

The following organisation chart outlines the key functions and their respective reporting lines:



All of the governing bodies allow for adequate strategic and operational management and allow MMS to provide an adequate and timely response to events that may arise at any level within the organisation and within its business and corporate environment.

In order to ensure that MMS's system of governance has an adequate structure, MMS has a series of policies that govern the key functions (Risk Management, Compliance, Internal Audit and Actuarial) to ensure that these functions follow the regulatory requirements and are compliant with the lines of governance established by MMS and by the MAPFRE Group.

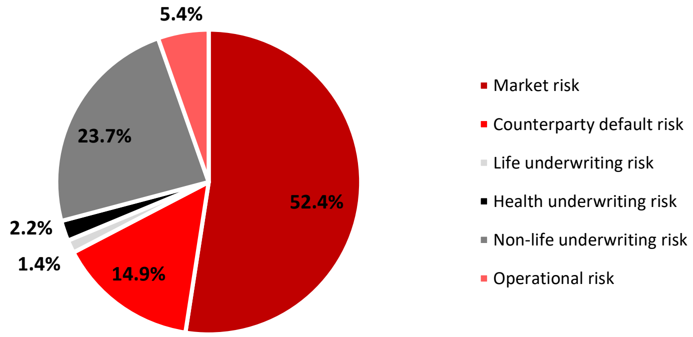
MMS's Board of Directors determines the policies and strategies regarding the Risk Management System, which are aligned with the policies and strategies defined by the Board of Directors of MAPFRE S.A.

C. Risk profile

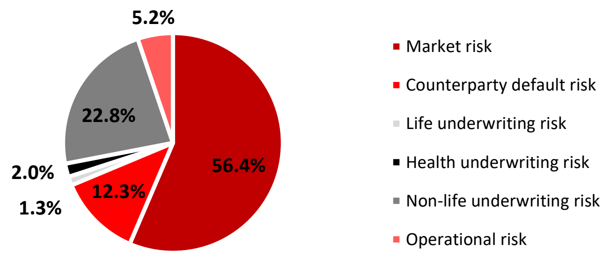
MMS calculates the Solvency Capital Requirement (SCR) using the standard formula.

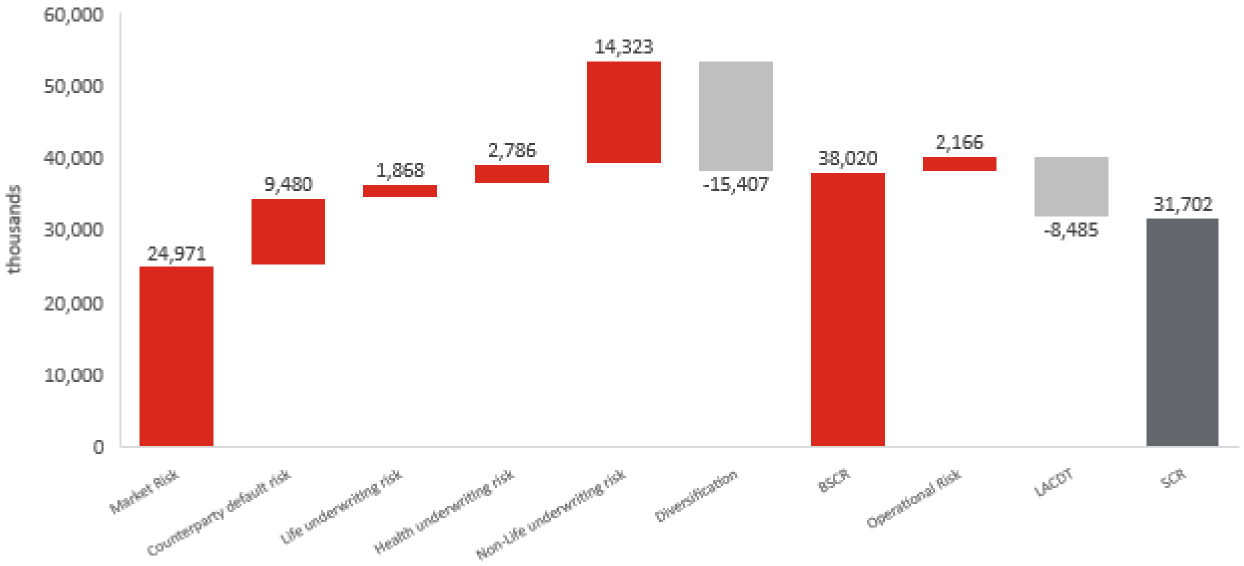
The following reflects the composition of MMS's risk profile based on the risks included under the standard formula methodology as well as the regulatory capital necessary for each risk.

31/12/2019



31/12/2018





MMS's risk profile is skewed towards Market Risk, due to MMS's strategic investment in MAPFRE MSV
Life p.l.c. This risk is followed by Non-Life Underwriting Risk and Counterparty Default Risk.

Other risks to which MMS is exposed to include those derived from the effects of the coronavirus pandemic, cybersecurity and reputational risk as outlined in Section C.6.

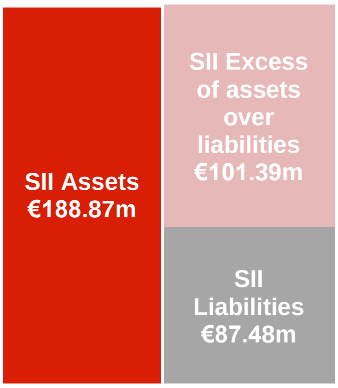
MMS also analyzes the sensitivity of its solvency position with respect to certain severe but plausible events, the results of which show that the Company complies with regulatory capital requirements even under the considered adverse scenarios.

D. Valuation for solvency purposes

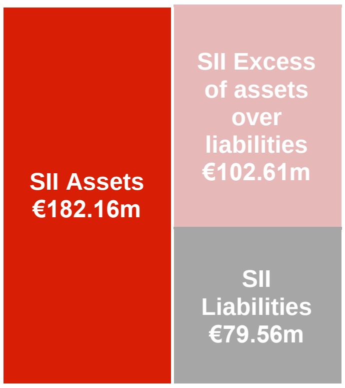
The Solvency II value of assets amount to €188.87 million, while the Accounting value (IFRS value) is equal to €175.55 million. The differences between the Solvency II value and the IFRS arose due to the different valuation criteria used for deferred acquisition costs, intangible assets, investments and reinsurance recoverables.

The Solvency II value of liabilities amounts to €87.48 million, while the IFRS value is equal to €102.74 million. The main difference between the Solvency II value and the IFRS value arose from the different valuation criteria used for technical provisions. Section D.2 provides an explanation on the actuarial methodology and assumptions used in the calculation of the technical provisions (best estimate and risk margin).

31/12/2019



31/12/2018



The excess of assets over liabilities for Solvency II purposes amounted to €101.39 million under Solvency II, which represents a 39.3% increase over the IFRS value of equity. As at 31st December 2019, the excess of assets over liabilities decreased by €1.22 million when compared to 2018.

There have been no significant changes in valuation criteria for assets and liabilities when compared to the previous year.

E. Capital Management

MMS has the appropriate structure and processes necessary to manage and oversee its own funds, and has a policy and a medium-term capital management plan to maintain the solvency levels within the limits established by the legislation and by MMS's own risk appetite.

The following table shows details of MMS's solvency ratio.

	31/12/2019	31/12/2018
Solvency Capital Requirement (SCR)	31,702	31,660
Own funds eligible for SCR coverage	88,392	85,608
Solvency ratio (SCR coverage)	**278.8%**	**270.4%**

Figures in thousand euro

MMS's Solvency Capital Requirement amounted to €31.70 million. The SCR corresponds to the own funds that MMS must hold to limit the probability of bankruptcy to one case per 200, or that MMS is 99.5% confident to be able to meet its commitments to insurance beneficiaries during the following year.

Eligible own funds to cover MMS's SCR represent €88.39 million, of which €87.68 million are classified as unrestricted Tier 1 and €0.71 million were classified as Tier 3. Tier 1 capital has the characteristics set out in Article 93(1)(a) and (b) of Directive 2009/138/EC, fully paid up and available to absorb losses.

To calculate the solvency ratio, MMS does not make use of matching and volatility adjustments, or transitional measures for technical provisions.

The Solvency II regulation also establishes a Minimum Capital Requirement (MCR), which is the minimum level of security under which financial resources should never fall. MMS's MCR amounted to €9.64 million and the ratio of eligible own funds to cover the MCR stood at 909.5%.

COVID-19 is expected to result in a reduction in the regulatory reported solvency ratio. However, although, at time of writing, it is not possible to have a full impact assessment, given the continuously evolving situation, as things stand, the Company is confident that its solvency ratio will remain above the regulatory required amounts.

A. Business and Performance

A.1. Business

A.1.1. Company Businesses

MAPFRE Middlesea plc is a composite insurance company specialising in the underwriting of non-life and group life business.

MMS underwrites risks, which are exclusively located in the Maltese territory. Legacy business, which originated from MMS's previous branches outside the Maltese territory, is now in run off.

The registered address is: MAPFRE Middlesea plc

Middlesea House

Floriana, Malta

MMS is a subsidiary of MAPFRE S.A, with registered address: MAPFRE S.A

Carretera de Pozuelo

Majadahonda, Spain

and is part of the MAPFRE GROUP, composed of MAPFRE S.A. and various companies operating in the insurance, financial, investments, and service industries.

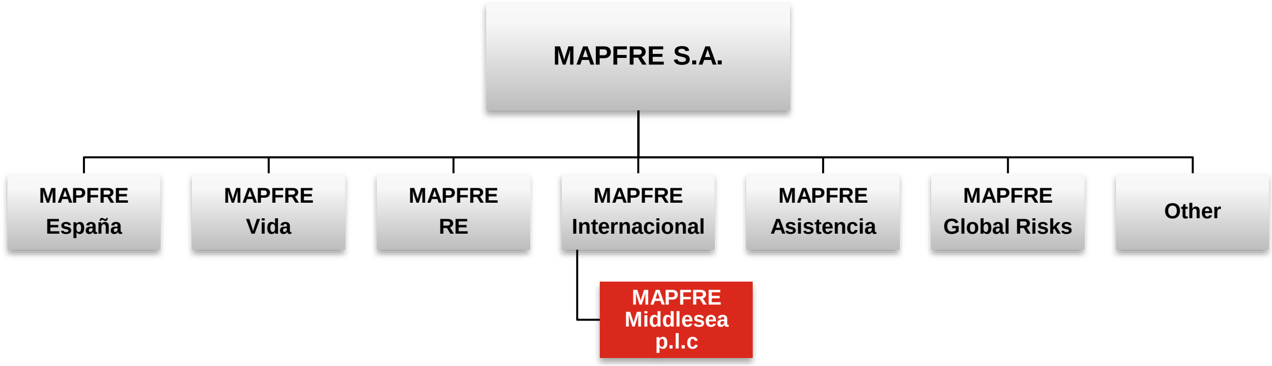
The ultimate controlling entity within the Group is FUNDACIÓN MAPFRE, a non-profit institution domiciled in Madrid at Paseo de Recoletos 23.

The following table shows the companies, which hold qualifying investments in MMS:

Name	Type of interest	Location	Percentage of ownership*
MAPFRE Internacional	Limited Liability	Spain	54.6%
Bank of Valletta p.l.c.	Limited Liability	Malta	31.1%

**The ownership interest and voting rights are the same.*

An organizational chart is presented below showing the position held by MMS within the simplified legal structure of the MAPFRE Group:



MMS is the parent company of a number of subsidiaries with main activities being insurance, financial and assistance services. Annex I to this report provides details of these companies.

MAPFRE Group presents a consolidated report for the Group and individual reports for the insurance and reinsurance companies belonging to the Group.

Supervision of the Company

The Malta Financial Services Authority (hereinafter MFSA) is responsible for the financial supervision of MMS. The MFSA is located at Triq l-Imdina, Zone 1

Central Business District

Birkirkara, CBD 1010

and its website is https://www.mfsa.mt/.

The Directorate General for Insurance and Pension Funds (DGSFP) is responsible for the financial supervision of MAPFRE Group since its parent, MAPFRE S.A., is located in Spain. The DGSFP is located in Madrid and its website is www.dgsfp.mineco.es.

External Audit

On 12th March 2020, KPMG Malta issued an unqualified audit opinion in its audit report on the individual and consolidated financial statements prepared by MMS as at 31st December 2019. KPMG is located at Portico Building

Marina Street

Pieta’, PTA 9044

Lines of business

Although a composite insurer, MMS is primarily a general insurer and accepts risks for the following lines of business:

- Medical expense insurance
- Income protection insurance
- Motor vehicle liability insurance

- Other motor insurance
- Marine, Aviation and Transport insurance
- Fire and other damage to property insurance
- General liability insurance
- Assistance
- Miscellaneous Financial Loss
- Other life insurance

Geographic areas

MMS does not underwrite any risks which are situated outside Malta, unless there is a specific Maltese interest. Previous business underwritten by the company branches outside Malta is now in run off.

A.1.2. Events with material repercussions

The result of the Non-Life technical account was €6.87 million at 31st December 2019 (2018 €4.99 million) whilst that for Life business amounted to €0.88 million (2018 €1.35 million) which, together with the result from the non-technical account resulted in a profit before taxes of €23.82 million up from the €11.42 million achieved in 2018. This included a special dividend of €12.17 million received from the subsidiary MAPFRE MSV Life p.l.c. from prior year profits.

During 2019, earned premiums net of reinsurance from direct business totalled €56.07 million (2018 €52.98 million), due to the favorable development of the business.

MMS's net combined ratio at 90.3% shows an improvement of 2.6 percentage points compared to the previous year, with both years being impacted by significant loss events. The core business experienced an improvement in particular emanating from the motor line of business following an improvement in ultimate loss claim projections whilst run-off business returned an improved result following closure of long outstanding claims.

During 2019, MMS's technical results was impacted by the February windstorm that affected a number of classes but particularly Fire and other damage to property insurance. In Motor, large losses involving fatalities or grievous bodily injury, incurred during the year or adjusted from those reserved in previous years continue to take their toll on the technical results, particularly in accidents involving foreign nationals.

MMS's solvency ratio stands at 278.8%. This shows that MMS holds sufficient capital to execute its long-term strategy and good resilience in challenging business scenarios.

A.2. Underwriting results

Below is a comparison of the quantitative information regarding the activity and underlying results for 2019 and 2018 by line of business.

	Line of Business for: non-Life insurance and reinsurance obligations (direct insurance and proportional accepted reinsurance)																		Line of Business for: accepted non-proportional reinsurance		Total	
	Medical expense insurance		Income Protection insurance		Motor vehicle liability insurance		Other motor insurance		Marine, aviation and transport insurance		Fire and other damage to property insurance		General liability insurance		Assistance		Miscellaneous financial loss		Property			
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
Premiums written																						
Gross - Direct Business	11,074	10,725	962	981	16,650	16,274	20,904	18,789	2,133	2,078	13,474	12,230	4,667	4,010	2,303	2,140	53	69			72,218	67,296
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-			-	-
Gross - Non-proportional reinsurance accepted																			-	3	-	3
Reinsurers' share	162	25	23	43	2,045	1,761	340	170	278	264	10,511	9,455	331	283	55	93	25	36		-	13,770	12,130
Net	10,912	10,700	939	938	14,605	14,513	20,563	18,619	1,855	1,814	2,963	2,775	4,336	3,727	2,247	2,047	28	33	-	3	58,449	55,169
Premiums earned																						
Gross - Direct Business	10,331	10,032	942	986	16,130	15,762	20,251	18,198	1,988	1,993	12,979	11,790	4,354	3,857	2,285	2,114	67	59			69,328	64,792
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-			-	-
Gross - Non-proportional reinsurance accepted																			-	3	-	3
Reinsurers' share	162	25	23	43	2,045	1,761	183	189	284	257	10,127	9,142	346	321	55	51	32	28	-	-	13,257	11,817
Net	10,169	10,007	919	944	14,085	14,001	20,069	18,009	1,705	1,736	2,852	2,648	4,008	3,536	2,230	2,062	35	30	-	3	56,071	52,978
Claims Incurred																						
Gross - Direct Business	4,015	5,126	485	256	17,303	21,970	7,189	4,850	2,783	1,384	5,214	3,300	1,603	651	638	1,444	7	-			39,239	38,980
Gross - Proportional reinsurance accepted	-	-	-	-	(22)	-	(13)	-	-	-	(18)	(2)	(281)	2	-	-	-	-			(334)	-
Gross - Non-proportional reinsurance accepted																			-	9	-	9
Reinsurers' share	(7)	(6)	(33)	43	2,961	5,715	1,810	1,262	1,117	89	4,010	2,564	1,066	9	(176)	(42)	-	-		-	10,748	9,634
Net	4,022	5,132	519	213	14,320	16,255	5,366	3,588	1,666	1,295	1,186	734	255	644	814	1,486	7	-	-	9	28,156	29,355
Changes in other technical provisions																						
Gross - Direct Business	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-			-	-
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-			-	-

	Line of Business for: non-Life insurance and reinsurance obligations (direct insurance and proportional accepted reinsurance)																		Line of Business for: accepted non-proportional reinsurance		Total	
	Medical expense insurance		Income Protection insurance		Motor vehicle liability insurance		Other motor insurance		Marine, aviation and transport insurance		Fire and other damage to property insurance		General liability insurance		Assistance		Miscellaneous financial loss		Property			
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
Gross - Non-proportional reinsurance accepted																			-	-	-	-
Reinsurers'share	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Expenses incurred	4,126	3,700	490	427	6,451	6,406	6,915	5,978	841	695	1,398	450	1,686	1,391	1,055	1,084	57	36	-	19	23,018	20,186
Other expenses																					-	-
Total expenses																					23,018	20,186

Figures in thousand euro

	Line of Business for: life insurance obligations			
	Other life insurance		Total	
	2019	2018	2019	2018
Premiums written				
Gross	2,165	2,386	2,165	2,386
Reinsurers' share	191	191	191	191
Net	1,974	2,195	1,974	2,195
Premiums earned				
Gross	2,165	2,386	2,165	2,386
Reinsurers' share	191	191	191	191
Net	1,974	2,195	1,974	2,195
Claims incurred				
Gross	984	418	984	418
Reinsurers' share	154	(52)	154	(52)
Net	830	470	830	470
Changes in other technical provisions				
Gross	(29)	83	(29)	83
Reinsurers' share	-	-	-	-
Net	(29)	83	(29)	83
Expenses incurred	354	359	354	359
Other expenses			-	-
Total expenses			354	359

Figures in thousand euro

The preceding tables only present the columns related to the lines of business in which MMS operates.

MMS closed the year with gross written premiums amounting to €74.38 million, experiencing and increase of 6.7 percent over 2018. Total gross claims incurred have increased by 1.2 percent over 2018 and amounted to €39.89 million.

A.3. Investment performance

A.3.1. Information on income and expenses arising from investments

The following tables present quantitative information regarding income and expenses from investments:

Financial income	2019	2018
INVESTMENT INCOME		
Investment properties	809	748
Income from the held-to-maturity portfolio	-	-
Income from the available-for-sale portfolio	162	197
Income from the fair value through profit or loss portfolio	204	201
Dividend income from Group Companies	18,025	6,843
Other financial income	5	6
TOTAL INVESTMENT INCOME	**19,205**	**7,995**
REALIZED AND UNREALIZED GAINS		
Net realised gains		
Investment properties	1	-
Held-to-maturity investment portfolio	-	-
Available-for-sale investment portfolio	-	-
Fair value through profit or loss portfolio investments	-	-
Other	-	-
Net unrealised gains		
Increase in the fair value of the trading portfolio and profits from derivatives	770	456
Other	-	-
TOTAL GAINS	**771**	**456**
OTHER FINANCIAL INCOME FROM THE INSURANCE BUSINESS		
Gains on investments on behalf of policyholders bearing the investment risk	-	-
Gains on exchange	6	-
Other	26	16
TOTAL OTHER FINANCIAL INCOME FROM THE INSURANCE BUSINESS	**32**	**16**
TOTAL INCOME FROM THE INSURANCE BUSINESS	**20,008**	**8,467**
FINANCIAL INCOME FROM OTHER BUSINESSES	**-**	**-**
TOTAL FINANCIAL INCOME	**20,008**	**8,467**

Figures in thousand euro

Financial Expenses	2019	2018
INVESTMENT EXPENSES		
Investment properties	(4)	-
Expenses from the held-to-maturity portfolio	-	-
Expenses from the available-for-sale portfolio	5	-
Expenses from the trading portfolio	-	-
Other financial expenses	90	53
TOTAL INVESTMENT EXPENSES	**91**	**53**

Financial Expenses	2019	2018
REALISED AND UNREALISED LOSSES		
Realised losses		
Investment properties	-	-
Held-to-maturity investment portfolio	-	-
Available-for-sale investment portfolio	-	-
Fair value through profit or loss portfolio investments	-	-
Other	-	-
Unrealised losses		
Decrease in the fair value of the trading portfolio and losses on derivatives	355	311
Other	-	-
TOTAL LOSSES	**355**	**311**
OTHER FINANCIAL EXPENSES FROM THE INSURANCE BUSINESS		
Losses on investments on behalf of policyholders bearing the investment risk	-	-
Losses on exchange	-	9
Other	44	14
TOTAL OTHER FINANCIAL EXPENSES FROM THE INSURANCE BUSINESS	**44**	**23**
TOTAL EXPENSES FROM THE INSURANCE BUSINESS	**490**	**387**
FINANCIAL EXPENSES FROM OTHER BUSINESSES	-	**-**
TOTAL FINANCIAL EXPENSES	**490**	**387**

TOTAL INCOME FROM THE INSURANCE BUSINESS	**20,008**	**8,467**
TOTAL EXPENSES FROM THE INSURANCE BUSINESS	**490**	**387**
FINANCIAL RESULT FROM THE INSURANCE BUSINESS	**19,518**	**8,080**
TOTAL INCOME FROM OTHER BUSINESSES	**-**	**-**
TOTAL EXPENSES FROM OTHER BUSINESSES	**-**	**-**
TOTAL FINANCIAL RESULT FROM OTHER BUSINESSES	**-**	**-**
TOTAL FINANCIAL RESULT	**19,518**	**8,080**

Figures in thousand euro

Total net investment income during the year amounted to €19.52 million (2018: €8.08 million). The increase is mainly derived from Group dividends, in particular due to two special dividends received from MAPFRE MSV Life p.l.c. amounting to €12.17 million.

A.3.2. Information regarding losses and gains recognised under equity

The following is the quantitative information regarding gains and losses arising from investments broken down by type of asset, and recognized directly in equity during 2019 and 2018:

Investments	Income recognised in equity		Losses recognised in equity		Net difference	
	2019	2018	2019	2018	2019	2018
I. Investment properties	**-**	**-**	**-**	**-**	**-**	**-**
II. Financial investments	**10**	**-**	**16**	**236**	**(6)**	**(236)**
Available for sale portfolio	10	-	16	236	(6)	(236)
- Equity instruments	10	-	-	123	10	(123)
- Debt securities	-	-	16	113	(16)	(113)
- Unit-linked	-	-	-	-	-	-
III. Investments in associates accounting for using the equity method	**50**	**(36)**	**-**	**-**	**50**	**(36)**
IV. Deposits established for accepted reinsurance	**-**	**-**	**-**	**-**	**-**	**-**
V. Other investments	**-**	**-**	**-**	**-**	**-**	**-**
Overall performance	**60**	**(36)**	**16**	**236**	**44**	**(272)**

Figures in thousand euro

Available for sale investments registered a net loss of €0.01 million as compared to a loss of €0.24 million in 2018. Whilst gains were registered on most of the Equity holdings, bonds registered a negative movement as securities approach their maturity dates. A positive movement of €0.05 million was recorded directly in equity representing the share of reserves movement of an associate company.

A.3.3. Information about asset securitisation

MMS did not have any securitisation investments in this or the comparative year.

A.4. Performance of other activities

A.4.1 Other income and expenses in the non-technical account

During the year, MMS has recognized the following "other" income and expenses other than deriving from the insurance business and investments, including:

	2019	2018
Other income	-	-
Other expenses	1,958	1,767

Figures in thousand euro

Other expenses relate to administrative expenses which are allocated to shareholders and therefore to the non-technical account.

A.4.2 Lease Agreements

Finance leases

MMS has no financial leases in which it is the lessor.

Operating leases

MMS is the lessee/lessor under operating leases involving property and lease of vehicles. MMS leases out commercial property to a number of tenants with leases ranging from 2 year to 32 year leases with di fermo periods never exceeding 5 years. Contracts have renewal and cancellation options with fixed notification periods.

On the other hand, MMS leases from third parties the premises from which it operates and company cars used by management.

A.5. Any other information

There is no additional information that has not been included in the preceding sections.

B. System of Governance

B.1. General Information on the system of governance

The structure, composition, and functions of MMS's governing bodies are defined in the Institutional, Business, and Organisational Principles, and in the internal regulations regarding MAPFRE subsidiaries' Board of Directors, approved by the MAPFRE S.A. Board of Directors; together with its bylaws and the Regulations of the Board of Directors.

Apart from the above mentioned Group structure, MMS has its individual governing bodies.

MMS's governing bodies, which are listed below:

i) allow for adequate strategic, commercial and operational management of MMS,
ii) enable MMS to appropriately respond in a timely manner to any issues which might arise throughout its different organisational levels and business and corporate environment, and
iii) are considered appropriate with regards to the nature, volume, and complexity of the risks inherent to its activity.

The policies derived from the Solvency II regulations are reviewed on an annual basis, although changes may be approved at any time when it is deemed appropriate.

B.1.1 System of Governance

The following outlines the main functions and responsibilities of MMS's governing bodies:

- **Shareholder's Annual General Meeting**: the highest governing body, in that its decisions bind all shareholders. Both ordinary and extraordinary Annual General Meetings are called by the Board of Directors.

- **Board of Directors**: the body in charge of managing, administering, and representing the company. It acts as the maximum decision-making and supervisory body at MMS, whereas ordinary management is the responsibility of the management and executive bodies. Where necessary, it establishes the roles of the Management Committee and its delegated Committees, designating its members, where necessary.

- **Audit Committee**: The main role of this committee is to protect the interest of the shareholders and assist the Board of Directors to effectively make informed decisions based on accurate, reliable and timely reported financial statements.

- **Risk and Compliance Committee**: The purpose of this committee is to assist the company through its oversight role in fulfilling its responsibility relating to the effective identification, measuring, monitoring and management of risk, compliance, prevention of money laundering and other aspects associated with its business.

- **Investment Committee**: This committee advises the Board of Directors on investment management policies to be adopted by the company to protect the value, marketability, and return of the investment portfolio. Furthermore, the committee is also responsible to oversee the management of the investment portfolio in order to ensure compliance with the Investment policy.

- **Remuneration Committee:** This committee is responsible to ensure a coherent remuneration policy and practices, which enable MMS to attract and retain executives and directors who create good value for the shareholders whilst supporting MMS's mission statement. Further to this, it is also under the committee's responsibility to reward executives in the context of the company's performance and the general pay environment.

- **Management Committee**: This committee is the body responsible for directly supervising MMS's management and for promoting all its global projects. It provides regular reports on its proposals, actions, and decisions to MMS's Board of Directors.

- **Security and Environment Committee:** The main role of this management committee is to direct and provide oversight to the Security and Environment function within MMS.

MMS has a management model underpinned by rigorous control and supervision at all levels: local, regional and global. This allows a broad delegation of authority in the execution and development of the responsibilities assigned to each function, ensuring that material decisions are analysed in-depth before and after their execution, by all of the senior executive teams.

Apart from the above-mentioned administration and supervisory bodies, MMS is supervised by the EURASIA Regional Management Committee within the MAPFRE GROUP, which directly supervises the management of regional Business Units.

B.1.2. Key functions

In order to ensure that the governance system has an adequate structure, MMS has policies which regulate the key functions (Risk Management, Compliance, Internal Audit, and Actuarial). These policies ensure that the key functions follow the requirements defined by the regulator and that they are in accordance with the governance structures established by MMS and by the MAPFRE Group. MMS's Board of Directors approved the Actuarial, Risk Management, Compliance, and Internal Audit policies at its meeting held on the 25th June 2019.

The above-mentioned policies ensure the operational independence of the key functions and their direct reporting to the governing body, which delegates the authority necessary to support its functions. The Board of Directors and/or the relevant committees receive reports at least annually from the responsible areas at MMS. The information and advice provided to the Board of Directors by the key functions are detailed in their respective sections. The names of the parties responsible for the key functions have been communicated to the MFSA.

The key functions have the resources that are necessary to perform the functions assigned to them under their respective policies.

B.1.3. Relevant resolutions adopted by the General Meeting and the administrative body regarding the governance system

During 2019, there were no significant changes to MMS's governance structure.

B.1.4. Remuneration

Remuneration paid to the members of MMS's governing body and employees is determined in accordance with current regulations as well as its Remuneration Policy, approved by the Board of Directors on 25th October 2019.

The Remuneration Policy endeavors to establish adequate remuneration based on the post or position, as well as performance, to thereby foster sufficient and effective risk management, making it unattractive to assume risks that exceed the MMS's tolerance level and to avoid conflicts of interest. Its main principles are as follows:

- Based on each job/function, it includes measures designed to avoid any conflicts of interest;
- It takes into account merit, technical knowledge, professional skills and performance;
- Ensures equality, without discrimination based on criteria to gender, race, or ideology;
- Transparency;
- Flexible in structure, adaptable to different market groups and circumstances;
- Aligned with MMSV's strategy and its risk profile, objectives, risk-management practices, and long-term interests;
- Market competitiveness.

Based on the aforementioned policy, employee remuneration is comprised of five items: fixed remuneration, variable remuneration/incentives, recognition programs, social benefits and in-kind benefits.

The remuneration system for Directors has the following characteristics:

- Transparent reporting in the remuneration paid to Directors;
- It provides an incentive to reward dedication, qualifications and responsibility, without constituting an obstacle to the duty of loyalty;
- It consists of a fixed amount for membership on the Board of Directors and, as appropriate, the Committee, which may be higher for people with positions on the Board or who hold the position of Chairman of the Committee. This remuneration may be supplemented by other non-monetary remuneration (life or health insurance, discounts on products sold by companies in the MAPFRE Group, etc.) that have been established for the company's staff in general;
- It does not include variable components or those linked to share value;
- Directors are reimbursed for traveling expenses and other costs undertaken in order to attend company meetings or in the performance of their responsibilities.

MMS does not have any Executive Directors.

B.1.5 Additional information

In the normal course of business operations, a number of transactions took place between MMS and its parent company. These transactions related to sales of insurance contracts and other services (e.g. commissions received and claims recovered) and purchases of products and services (e.g. Reinsurance premium, staff training, computer maintenance, and software development).

B.2. Fit and proper requirements

MMS has a Fit and Proper Policy in place, which was approved by MMS's Board of Directors on 25th June 2019. The policy establishes the applicable Relevant Personnel[1] requirements, as follows:

- They should have the appropriate qualifications, knowledge, and expertise to ensure that MMS is professionally managed and supervised.

- The expertise and experience of Relevant Personnel will include academically-acquired knowledge and experience appropriate to the respective individual responsibilities assigned.

MMS's Board members and Directors must have:

- Collectively: the appropriate qualifications, experience, and knowledge in at least the following areas:

  a) Insurance and financial markets
  b) Strategies and business models
  c) System of Governance.
  d) Financial and actuarial analyses
  e) Regulatory Framework.

- Individually: training and experience appropriate to the professional profile, specifically in the insurance and financial services area, with practical experience acquired from prior positions held during a sufficient period of time.

Relevant and, where applicable, Outsourced Personnel, must have proven personal, professional, and commercial honorability based on trustworthy information on their personal and professional conduct and reputation, covering any criminal, financial, and supervisory aspects considered pertinent.

Company designation procedures.

Parties proposed for executing Relevant Personnel roles requiring notification to Supervisory Authorities or, where applicable, those of Outsourced Personnel, must provide a prior, truthful, and complete statement regarding their personal, family, professional, or business endeavors.

The above statement must be made in the Company's model forms established for this purpose.

The aforementioned parties must ensure that their statements are continually updated, and must communicate any relevant changes in their situations, and participate in periodic updates when required to do so by the MMS's Board of Directors, including the re-evaluation of any fit and proper requirements

[1] Relevant Personnel: Directors, Management and Heads of key functions, as well as other parties outlined in prevailing legislation at any given time, must meet fit and proper requirements.

B.3. Risk management system, including the self-assessment of risk and solvency

B.3.1 Governance framework

The Risk Management System (RMS) is an integral part of MMS's organizational structure. MMS's RMS follows the three lines of defense model (described in section B.4.1). This ensures ownership by all employees for risks and corresponding controls, in line with their roles and responsibilities, and objectives.

The Board of Directors of MMS is ultimately responsible for ensuring the Risk Management System's effectiveness and for determining the company's risk profile and tolerance limits. Further to this, the Board of Directors is also responsible for approving the Risk Management Strategies and policies within the Risk Management Framework. In performing these functions, MMS's Board of Directors is supported by the Risk and Compliance Committee.

The Group's Risk Corporate Office provides oversight and monitors all aspects related to the management of the risks within all MAPFRE subsidiaries. This is done by setting group guidelines, policies, tolerance, and reporting structures.

MMS's Risk Management Function facilitates the application of the Risk Management System. Its functions include the coordination of the strategies, processes and procedures that are necessary to continually identify, measure, monitor, manage and report on the risks to which MMS is exposed to, or may be exposed to.

The Risk Management Function reports to the Risk and Compliance Committee (and the Board of Directors) any risk exposures, taking into account their interdependencies, and compliance with established limits, including the Own Risk Assessment.

MMS's Chief Risk Officer has a dual reporting responsibility – hierarchically to MMS's CEO and functionally to the Corporate Risk Office.

B.3.2 Risk management objectives, policies, and processes

The main objectives of the Risk Management System are the following:

- To promote a solid culture and an effective system of risk management.
- To ensure that risk analysis is part of the decision-making process.
- To preserve MMS's financial solvency and strength.

The RMS is based on integrated management of every business process and on the adaptation of risk levels in the established strategic objectives.

To implement an effective risk management approach, MMS has formulated a set of Risk Management policies, also in line with Solvency II requirements. One of these policies is the Risk Management Policy, which serves as a framework for the management of risks and, in turn, for the development of policies regarding specific risks.

Each policy aims to:

- Set general guidelines, basic principles and a general action framework for the type of risk concerned, ensuring coherent application at the Company.

- Assign responsibilities, strategies, processes and the reporting procedures required to identify, measure, monitor, manage and report the risks included within their scope.
- Establish reporting structures and communication channels for the business area responsible for the risk.

Capital is generally estimated in line with the budget for the following year and is periodically reviewed throughout the year according to risk development, to ensure compliance with the established Risk Appetite limits. The Board of Directors is responsible to approve internal regulations and establish the level of risk that the company is willing to accept in order to meet the business objectives without relevant deviations.

The Governing Bodies of MMS receive information regarding the quantification of the main risks to which MMS is exposed and the capital resources available to confront them, as well as information regarding compliance with Risk Appetite limits.

The Board of Directors decides the actions to be taken with respect to identified risks and is immediately informed of any risks which:

- Exceed the established risk limits, due to its development;
- Could lead to losses that are equal to or higher than the established risk limits; or
- May put compliance with the solvency requirements or continuity of operation of the Company at risk.

A breakdown of the processes for the identification, measurement, management, monitoring and reporting of risks, by type, is set out below:

Type of Risk	Measurement and management	Monitoring and reporting
Underwriting risk – Premium risk – Reserve risk – Catastrophic risk – Reinsurance Mitigation	Standard formula	Annual
Market risk – Interest rate – Equity – Property – Spread – Concentration – Currency	Standard formula	Annual
Credit Risk Reflects any possible losses arising from unexpected default by counterparties and debtors.	Standard formula	Annual
Operational risk Risk of possible losses deriving from the inadequacy or malfunction of internal processes, personnel or systems, or from external events (excluding the risks deriving from strategic decisions and reputational risks).	Standard Formula	Annual
	Dynamic qualitative analysis of the risks using processes (RiskM@p)	Annual
	Recognition and monitoring of operational risk events	Continuous
Liquidity Risk Risk that MMS might not be able to realise its investments and other assets in order to meet its	Liquidity position Liquidity indicators	Continuous

Type of Risk	Measurement and management	Monitoring and reporting
financial commitments at maturity.		
Non-compliance risk Risk of losses due to legal/regulatory penalties or reputation losses arising from the failure to comply with laws and regulations, or with applicable administrative requirements.	Monitoring and recognition of significant events	Annual
Strategic and Corporate Governance Risk Includes the following risks: – Business ethics and good corporate governance – Organisational structure – Alliances, mergers and acquisitions – Market competition	Application of MAPFRE Group's Institutional, Business, and Organisational Principles.	Continuous

All of the calculations deriving from the standard formula are updated when there is a material change in the risk profile. The Board of Directors is regularly informed of the risks to which MMS is exposed to.

B.3.3 Own Risk and Solvency Assessment (ORSA)

The Own Risk and Solvency Assessment (hereinafter ORSA) is an integrated process in MMS's Risk Management System. The ORSA is a mechanism, which identifies, measures, monitors, manages, and reports any short or long-term risks identified by MMS throughout the period reflected in the strategic plan. It is also used to measure the sufficiency of capital resources based on the understanding of the actual solvency needs. Based on these objectives, it includes all the significant and potential sources of risk that MMS faces, and facilitates the taking of initiatives for their management and mitigation.

B.4. Internal Control System

B.4.1. Internal Control

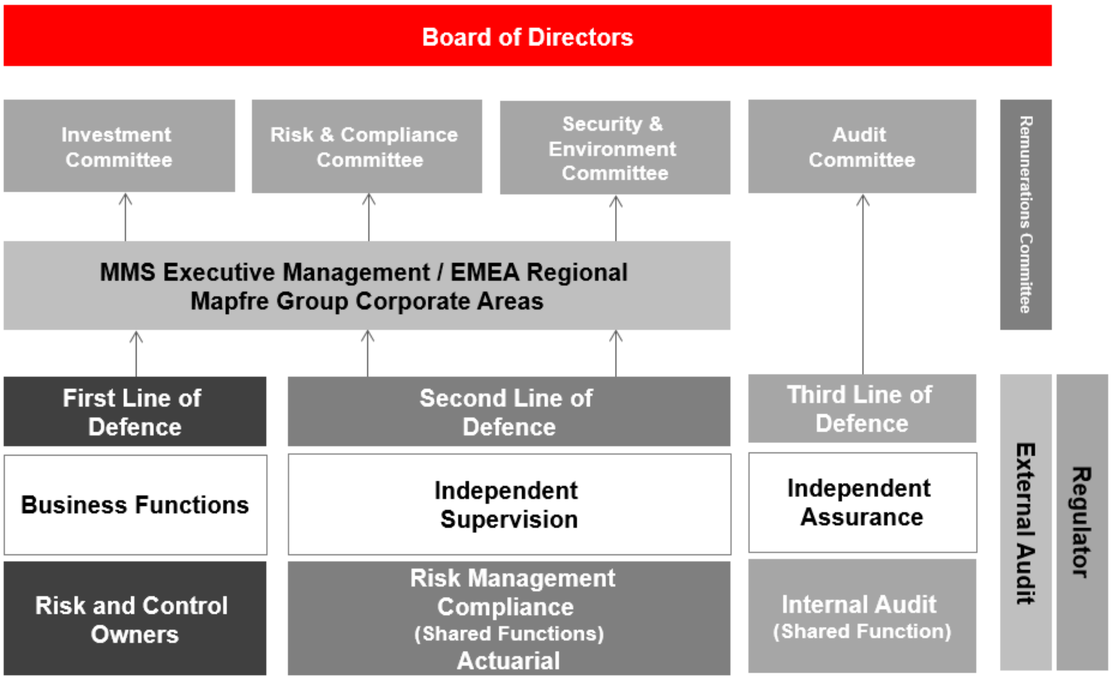
MMS's Internal Control Policy has been approved on 25th June 2019. This policy establishes the actions which must be developed in order to maintain an optimal and effective Internal Control System.

MMS's Internal Control System involves all personnel, irrespective of their position within the organization who collectively contribute to provide reasonable assurance on the achievement of the objectives, mainly regarding:

- Operational objectives: Effectiveness and efficiency of operations, differentiating insurance operations (mainly underwriting, claims, reinsurance and investment) from the support operations and functions (Human resources, administration, commercial, legal, IT, etc.).
- Reporting objectives: Reliability of information (financial and non-financial, both internal and external) regarding its accuracy, timeliness or transparency, among others.
- Compliance objectives: Compliance with applicable laws and regulations.

The Internal Control System is integrated into the organisational structure under the three lines of defense model, by assigning responsibilities and ensuring compliance with the internal control objectives in line with the model:

1. The first line of defense consists of employees, management, and the business, operational and supporting areas that are responsible for maintaining effective control of activities carried out as an inherent part of their day-to-day work. Therefore, these units are responsible to manage the risks, design and apply the control mechanisms that are necessary to mitigate the risks associated with the processes that they carry out and to ensure that they do not exceed established limits.
2. The second line of defense is made up of the risk management, actuarial and compliance key functions, as well as other assurance functions, which provide an independent assurance that the internal control system is present and functioning.
3. The third line of defense made up of Internal Audit, which provides an independent assessment of the adequacy, appropriateness and effectiveness of the Internal Control System, and communicates potential deficiencies timely to the parties responsible for taking the corrective measures, including top management and governing bodies, as appropriate.



MMS's Internal Control System consists of tasks and actions present in all the organisation's activities and, accordingly, they are fully integrated into its organizational structure.

B.4.2. Compliance Function

The Compliance Function has the objective to enable MMS to operate within the framework of regulatory compliance, in order to achieve a global compliance environment. For this purpose, it assumes the responsibility of advising the Board of Directors on compliance with the laws, regulations and administrative provisions that affect MMS and compliance with internal regulations. It also performs an identification and assessment of the impact of any changes in the legal environment affecting MMS's operations and the identification and assessment of non-compliance risk.

MMS's Compliance Function is structured based on the specific applicable regulatory requirements, as well as the principle of proportionality based on its business volume and the nature and complexity of the risks assumed by the Company.

MMS employs its own strategy for implementing and carrying out the Function, in accordance with the reference criteria shared by the Group's Compliance Area Management.

MMS's Compliance Policy was approved by the Board of Directors on 25th June 2019. The policy provides a detailed outline of the scope of the function, its structure, the assigned responsibilities, as well as the established reporting processes. The management of legal and non-compliance risks is carried out in accordance with the common methodology defined by the Corporate Compliance Office.

B.5. Internal Audit function

MMS's governance structure is based on the three lines of defense model, with the Internal Audit Function being the third line of defense. This function provides an independent opinion in respect of appropriateness and effectiveness of the Internal Control System, as well as other elements of the system of governance.

In ensuring the principle of Independence, MMS's Internal Audit function reports to the Audit Committee, a board delegated committee. This guarantees the Internal Audit function independence from the company's management.

The Internal Audit Policy and bylaws, updated and approved by MMS's Board of Directors on the 25th June 2019, establish the mission, functions and attributes of the MMS´s Internal Audit Function. It also includes the rights and obligations of the MMS´s Internal Auditors as well as their code of ethics, which sets out the rules of conduct of the auditors based on integrity and honorability, objectivity, confidentiality and competence.

Additionally, one of the primary objective of this document is to communicate the main activities of internal audit, among others, the classification of audit work, recommendations and deadlines, treatment of audit reports, and any other general circumstances related to internal audit activities, which must be exclusively carried out by the MMS´s Internal Audit Unit.

The policy and bylaw are reviewed at least on a yearly basis. All changes that are made in these revisions are approved by the corresponding MMS´s governing bodies.

The Internal Audit Plan (IAP), which adopts a risk based approach, is approved by the Audit Committee, prepared annually and includes a report on all the work carried out during the previous year. The report covers the work related to the tasks to be performed during the year and the following year, with information provided in templates, a budget for the area and an analysis of the function's key management ratios.

B.6. Actuarial Function

MMS's Actuarial Function is responsible for preparing mathematical, actuarial, statistical and financial calculations. These allow the company to determine prices and technical provisions. Additionally, the Actuarial Function participates in risk modeling which is used as a basis for the calculation of MMS's capital requirements in close collaboration with the Risk Management Office.

The person responsible for the Actuarial Area at MMS was appointed by the Board of Directors and reports to the Corporate Actuarial Office.

The Corporate Actuarial Office sets the general principles and guidelines, which take into account the best statistical and actuarial practices within the MAPFRE Group, in order to coordinate and unify the Group's actuarial calculations.

The Corporate Actuarial Office ensures compliance with the general actuarial calculation principles and guidelines, promoting corrective actions in cases in which irregularities are detected, or when the general guidelines established by the Area have not been followed.

Considering the above, the Corporate Actuarial Office in cooperation with regional actuarial managers supports the Business Units Actuarial Areas that require collaboration in order to fulfill their corresponding individual responsibilities.

B.7. Outsourcing

MMS's Outsourcing Policy was approved on 25thJune 2019 by the Board of Directors and is in line with the Outsourcing Policy approved by MAPFRE S.A. Board for the Group, establishing the general principles, tasks, processes and the assignment of responsibilities in the event of the outsourcing of a critical or important function and/or activity.

The basic principle established by the Outsourcing Policy is that the Company will continue with full responsibility for meeting all obligations arising from the functions or activities susceptible to being outsourced, in the same manner as if they were to be performed internally.

B.8. Any other information

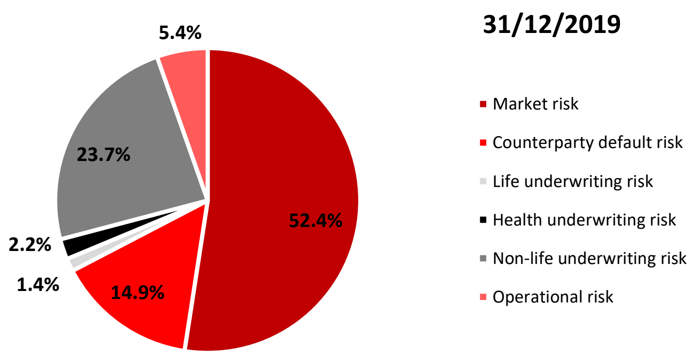
There is no other significant information regarding the system of governance that has not been included in the preceding sections.

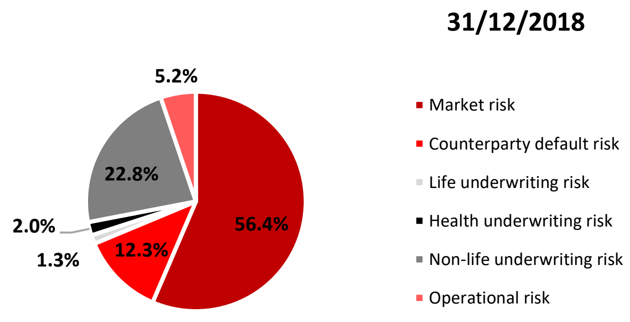
C. Risk profile

MMS calculates its Solvency Capital Requirement (SCR) using the standard formula as explained in Section E.2. For the main risk categories, the standard formula is considered an appropriate risk management tool for determining the company's risk exposure, as it recognises the capital charge corresponding to key risks (such as underwriting, market, counterparty and operational risk).

As explained in sections C.4 and C.6, MMS's exposure to other risks not included in the standard formula SCR (such as liquidity risk) is not considered significant, as MMS has effective measures in place for the management and mitigation of such risks. Moreover, in C.6, material risks due to the Coronavirus pandemic are classified as first-order impacts, stemming both from an increase in claims in certain business lines.

The following charts reflect the composition of MMS's risk profile based on the risks included under the standard formula methodology as at 31st December 2019 and 2018. Further information on the SCR calculation can be found in Section E.2.





From the above, it can be observed that MMS's risk profile mainly comprises of Market Risk (due to MMS's strategic investment in MAPFRE MSV Life p.l.c.), representing 52.4 percent of the total SCR. The risk is followed by Non-Life Underwriting risk and Counterparty Default Risk (23.7 percent and 14.9 percent of the total SCR respectively).

In 2019, the relative share of Underwriting, Operational and Counterparty default risk increased, while the relative share of Market risk decreased. Further information is available in Section E.2.1.

In 2019, there have been no significant changes with respect to the measures used to assess MMS's main risks.

MMS considers that with the exception of the coronavirus pandemic there have been no material changes in the significant risks to which it is exposed to, which are described in Section C.6.

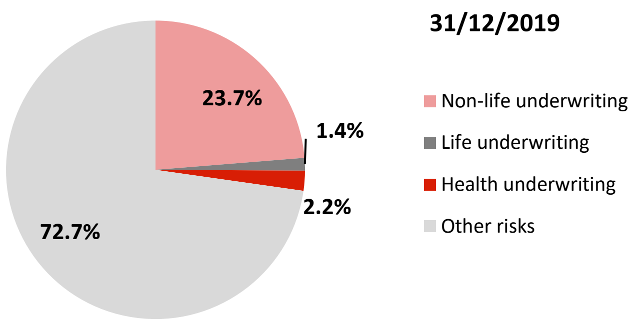
This section provides detail on the breakdown of the capital requirement under Solvency II by risk module. It also includes a description of the reduction and mitigation techniques used by MMS to minimise its risks. Any possible concentrations are also indicated.

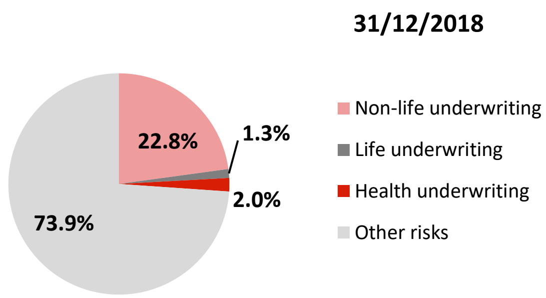
C.1. Underwriting risk

Underwriting Risk is the risk of loss or adverse change in the value of insurance liabilities, due to inadequate pricing and provisioning assumptions.

Exposure

As at 31st December 2019, underwriting risk represents 27.3 percent of all of the risk modules included in the SCR standard formula calculation. The following charts present details by module and any changes when compared to the previous year.





Management and mitigation techniques

MMS minimises underwriting risk through the following measures:

- **The establishment of policies, limits, and exclusions in underwriting risk:**

  The various insurance products sold by MMS outline the cover provided but are all subject to terms, conditions, limitations, and exclusions. These are generally subject to domestic and international market standards and practices, and also reflect the reinsurance agreements entered into. Notwithstanding, MMS's Underwriting Policy establishes the insurance products that can be sold or written by the company. Furthermore, the internal Underwriting Guidelines provide further detail in assisting the Underwriting and Commercial teams on the prudent acceptance or otherwise of a risk, thus controlling and reducing undesired Underwriting Risk.

- **Setting of a sufficient premium:**

  MMS gives importance to premium sufficiency, which is supported by actuarial calculations.

- **Adequate setting of the technical provisions:**

  Claims handling and the adequacy of technical provisions are basic principles of insurance management. IFRS technical provisions are calculated by MMS's Finance Department with the involvement of the Actuarial Unit. These are audited by actuaries forming part of the company's independent auditors. The establishment of technical provisions is regulated by a specific Group Policy, adopted by MMS. The best estimate liabilities calculations are performed by the Actuarial Unit and are reviewed by the Corporate Actuarial Office.

- **Use of Reinsurance:**

  The Technical departments of MMS are responsible for correctly identifying the appropriate level of risk transfer for its previously-defined risk limits, and for defining/designing the types of reinsurance agreements based on its risk profile and appetite, with help from the MAPFRE RE technical advisors.

  Once its reinsurance needs have been defined, MMS communicates them to MAPFRE RE to jointly plan the optimal structure and conditions for ceding contracts.

  As at 31st December 2019, MMS has ceded 18.8 percent of its premiums and 31.7 percent of its technical provisions[2] to reinsurance.

  The appropriateness of the reinsurance management procedures are revised and updated at least annually.

  The Actuarial Area issues an annual report expressing its opinion on the underwriting policy, the sufficiency of the premium rates and the technical provisions, as well as on the adequacy of reinsurance arrangements.

Concentration

MMS's insurance risk is highly diversified through the different products offered. MMS is currently writing insurance business in Malta but also has passporting rights to provide services in several countries outside Malta. However, MMS does not actively write insurance business outside of Malta. It only provides cover to Maltese customers with overseas interests. Hence, MMS is largely exposed to insurance risk in one geographical area.

MMS applies acceptance limits, which allow it to control the degree of concentration of insurance risk. MMS employs reinsurance contracts to reduce insurance risk arising from the concentration or accumulation of guarantees exceeding maximum acceptable limits. This is also facilitated by the purchase of reinsurance on a risk-by-risk basis.

The highest exposures to underwriting risk arise from natural or man-made catastrophes. To mitigate catastrophe risk, specific reinsurance coverage is purchased, to protect MMS's net retained exposure. This is reviewed at least on an annual basis and the level of cover purchased is based on a technical analysis of possible different scenarios, carried out by MAPFRE RE, the Group's reinsurance business unit.

Transfer of risk to special-purpose entities

MMS does not transfer underwriting risk to special-purpose entities.

[2] Solvency II Technical Provisions

C.2. Market Risk

Market Risk is the risk of loss or adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities, and financial instruments.

Exposure

The following is a breakdown of MMS's investments by asset category:

Investments	Investments at 31/12/2019	(%) Investments	Investments at 31/12/2018	(%) Investments
Investment properties	**16,167**	**13.8%**	**15,360**	**12.0%**
Financial investments	**100,896**	**86.2%**	**113,072**	**88.0%**
Strategic participations	90,979	77.7%	96,878	75.4%
Fixed income	7,172	6.1%	13,129	10.2%
Equity	2,745	2.3%	3,065	2.4%
Mutual funds	-	-	-	-
Deposits other than cash equivalents	-	-	-	-
Hedging derivatives	-	-	-	-
Other investments	-	-	-	-
Total	**117,063**	**100%**	**128,432**	**100%**

Figures in thousand euros

As at 31st December 2019, 77.7 percent of total investments relates to strategic participations, listed in Annex I. The main exposure pertains to MMS's investment in MAPFRE MSV Life p.l.c., representing 95.2 percent of the strategic participations. Furthermore, 6.1 percent of the total investments were fixed income securities. Of these, 46.6 percent correspond to the Government of Malta debt exposures.

As at 31st December 2019, Market risk represents 52.4 percent of all of risk modules included in the SCR standard formula calculation. The following charts present details by module and changes when compared to the previous year.

Management and mitigation techniques

MMS mitigates its exposure to market risk by means of a prudent investment policy, characterized by investment-grade fixed-income securities and the establishment of general and specific exposure limits.

These limits are established in the Investment Plan, which is approved by the Board of Directors and is reviewed at least on an annual basis.

The management of the investment portfolio is considered as semi-active management, with internal risk limits in place.

MMS's investment portfolio assumes a degree of Market Risk, in accordance with the following:

- Modified duration is the variable aspect of the management of interest rate risk, and is conditioned by the limits established in MMS's Investment Plan and the Asset and Liability Management (ALM) policy approved by the Board of Directors.

- Spread and concentration risks are mitigated by the high proportion of fixed-income securities with investment-grade ratings and through issuer diversification.

- Equity investments are subject to a maximum limit of the investment portfolio and issuer limits.
- Currency risk is minimised through currency matching with respect to the currencies in which the assets and liabilities are denominated.
- Property risk is monitored and it is ensured that the risks lie within the Investment Policy for property investments.

Concentration

For Market Risk, MMS applies the limits established in the Investment Plan, which ensures sufficient diversification by issuer, country and activity sectors.

Maltese Government bonds represent 33.7 percent of the total financial investments (excluding real estate and strategic investments). MAPFRE MSV Life p.l.c. is the most important strategic investment held by MMS whilst MMS's property investment allocation is mainly concentrated in a single exposure.

C.3. Credit Risk

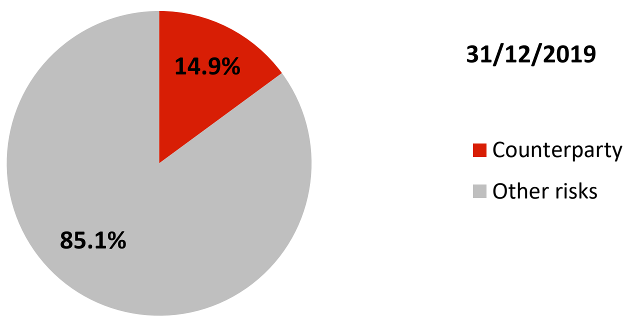
Credit Risk is the risk of loss or adverse change in the financial situation, resulting from fluctuations in the credit standing of issuers of securities, counterparties, and any debtors to which insurance and reinsurance undertakings are exposed to, in the form of counterparty default risk, or spread risk, or market risk concentrations.

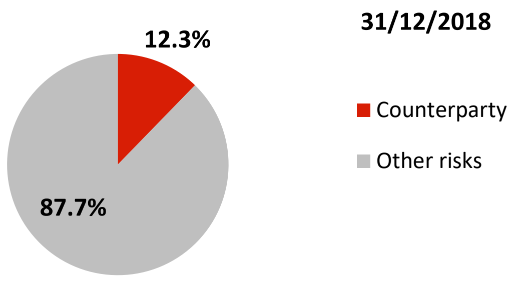
Credit Risk is included under the SCR Standard Formula calculation as:

- Spread and concentration risk under the Market Risk module (Section C.2 of the Report); and
- Counterparty default risk which distinguishes between two types of exposures:
    - Type 1 exposures: which include reinsurance contracts, and cash at bank where a credit rating is usually available for the counterparty.
    - Type 2 exposures: which include intermediaries' receivables and policyholders debtors, among others.

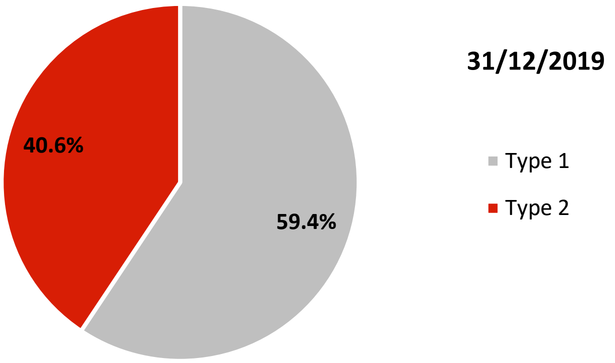
Exposure

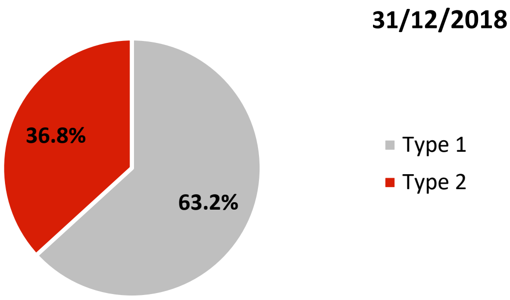
As at 31st December 2019, the counterparty default risk represents 14.9 percent of all the risk modules included in the SCR.





The following charts show the solvency capital requirement results for the two types of exposures:





Management and mitigation techniques

MMS's Credit Risk Management Policy establishes exposure limits according to the counterparty's credit rating. A risk exposure monitoring and notification system is also set up.

MMS's strategy with regards to reinsurance is to cede business to reinsurers of proven financial capacity. Generally, MMS reinsures with entities having a credit rating of at least A (credit quality step of 02). The MAPFRE Group Security Committee monitors exposure to reinsurance counterparties.

The main principles, which are taken into consideration when purchasing reinsurance and/or implementing other risk mitigation techniques within MMS are:

- Optimisation of capital consumption.
- Optimisation of conditions.
- Solvency of the counterparties.
- The effective transferability of risk.
- Suitability of the risk transfer level.

Concentration

The highest concentration in relation to reinsurance is to reinsurers within the MAPFRE Group.

COVID-19

The financial strength of MMS two main counterparties i.e. Bank of Valletta and MAPFRE GROUP means that the credit risk stemming from these positions remains on the low. Exposures to intermediaries is not concentrated in a single exposure but spread across a number of intermediaries. Though this risk might be considered higher due to COVID-19, currently available information does not point towards an increased risk.

C.4. Liquidity Risk

Liquidity risk is the risk that insurance and reinsurance undertakings are unable to realise its investments and other assets in order to settle their financial obligations when they fall due.

Exposure

Liquidity risk is not included in the SCR Standard Formula calculation. Exposure to liquidity risk is considered to be low, taking into account the prudent investment strategy established in the Investment Policy, which is characterised by a relatively high proportion of Government of Malta debt exposures.

In extreme events, liquidity risk is minimised through the use of reinsurance as a risk mitigation technique to reduce the concentration of underwriting risk and also through the selection of highly rated reinsurers.

Management and mitigation techniques

MMS has a Liquidity Risk Management Policy and an Asset and Liability Management Policy, which together represent the framework of reference for handling Liquidity risk. The Liquidity Risk Management Policy is based on maintaining sufficient cash balances and other high-quality liquid assets to comfortably cover commitments arising from MMS's obligations towards its policyholders and creditors at maturity.

As at 31st December 2019, the cash and cash equivalents balance amounted to €27.05 million (2018: €18.44 million), equivalent to 73.2 percent of total financial investments and cash balances[3].

Additionally, the majority of fixed-income investments have investment-grade ratings and are traded on organised financial markets, which provide comfort to cover any commitments arising from MMS's obligations. MMS is confident that its liquidity position will enable it to withstand any liquidity pressures, which may happen over the next months due to COVID-19.

MMS's Liquidity Risk Management Policy requires, on a continuous basis, a sufficient volume of high-quality liquid assets, available credit facilities and estimated cash inflows to cover its expected cash outflows.

Concentration

No liquidity risk concentrations have been identified.

Expected profits included in future premiums

The calculation of best estimate of technical provisions considers the expected profits from future premiums (as a reduction in the best estimate value when positive, or a higher value in the case of expected losses). As at 31st December 2019, the amount of these expected profits totalled €142k net of reinsurance.

[3] excluding strategic investments

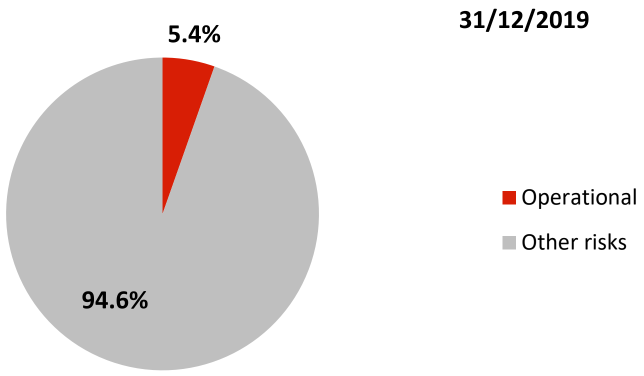
C.5. Operational Risk

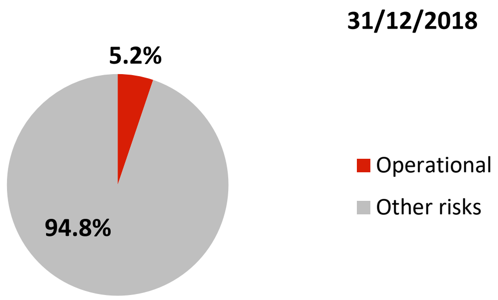
Operational Risk is the risk of loss arising from the inadequate or failed internal processes, personnel or systems, or from external events including legal risks, but excluding risks arising from strategic decisions as well as reputational risks.

Operational risks are both quantitative and qualitative in nature. In this regard, MMS measures the quantitative aspect through the standard formula calculation. On the other hand, the qualitative aspect is assessed through various risk assessments as described further below.

Quantitative Exposure of Operational Risk

As at 31st December 2019, operational risk represents 5.4 percent of all of the risk modules included in the SCR standard formula calculation. The following charts present details by module and changes when compared to the previous year.





Management and mitigation techniques

MMS has systems for monitoring and controlling operational risk, although the possibility of suffering operational losses cannot be excluded given the difficulty of forecasting and quantifying this type of risk.

Operational risks are identified and evaluated through Riskm@p, a software application developed in-house by MAPFRE to control risks, particularly operational risks.

The yearly operational risk and control assessment consists of a process-based dynamic qualitative analysis. This assessment requires the participation of senior employees and managers across all departments to identify and assess potential risks and the effectiveness of the related controls affecting the business and support processes. The assessment is conducted in respect of 12 processes, whilst corresponding risks are divided into 10 Risk Areas, which are sub-divided into 24 Risk Types.

Concentration

MMS relies on its IT systems for the management of insurance policies. A prolonged unavailability of these systems could have a negative impact on its operations. However, MMS has a business continuity plan which mitigates this risk.

COVID-19

Due to COVID-19, the company triggered its business continuity plan. The plan has two main pillars:

- To safeguard the health and safety of the Company's employees, its customers, various stakeholders and the general public;
- Ensuring the continuity of service to the Company's customers having regard to the current extraordinary operational environment.

This plan leverages on the company's investment in information technology and its digital transformation initiatives. This enabled the company to be in a position to have over 85% of its staff to be capable to work remotely. Though the Company's offices are not open for customers' face to face interaction, both internal and external communication has been maintained through the different means available whether telephony, video, on-line portal and e-mail. Customer service has continued. Management is still able to access systems, tools and data thus being able to continue to process, transform, analyze, monitor and report business critical information. Management, Board and Committee meetings, essential in the current situation, continue to be regularly held and decision taken, through virtual meetings facilities.

C.6. Other material risks

C.6.1 Coronavirus pandemic

It is expected that the spread during March 2020 of COVID-19 in western economies will cause uncertain impacts, not foreseen in the business estimates made at the end of 2019.

These impacts can be classified as first-order impacts, stemming both from an increase in claims in certain business lines, and from the increase in spending necessary for the implementation of business continuity plans.

At a later stage, there could be impacts caused by the evolution of financial markets and, in the longer term, by a reduction in growth estimates that, in some markets, could lead to a recession phase.

Throughout the month of March, markets saw increases in volatility to levels not seen since the financial crisis of 2008. There have been significant falls in the valuations of equity accompanied by a drop in interest rates, leading the curve into further negative territory and an increase in some government spreads due to the need to adopt fiscal measures to reactivate the economy and the consequent impact on governments' deficit and debt levels.

It is estimated that these indirect or second-order events will have a greater impact than those of the first order, but their amount cannot be estimated in the current phase of virus containment. It is expected that the longer this phase continues, the greater these impacts will be.

C.6.2. Cybersecurity risk

Cybersecurity risks include all the risks related to the secure use of IT and communication technologies, including intentional acts originating from or in cyberspace that could compromise the confidentiality, integrity, and availability of information and storage, processing, and transfer systems.

The MAPFRE Group has a Corporate Security and Environmental Department, which is responsible for analyzing and managing cybersecurity risks that might harm the Company. In 2019 work has continued on the improvement of protection against cyber risks, on proactive privacy, on the culture of cybersecurity and on cybersecurity from the beginning.

MAPFRE SA has taken out a Cyber Security Insurance Policy covering various Cyber Security Risks for all Group Companies.

C.6.3. Risk of new distribution channels

The risk of new distribution channels risk is the risk deriving from the failure to adapt MMS's product distribution and service provision channels quickly enough in response to changes to client preferences, the Internet, mobile devices and digitalization in general, giving rise to a severe decline in demand.

MAPFRE Group strategic initiatives relating to Digital Transformation and Client Orientation aim to mitigate this risk. The company is constantly striving to improve the digital interaction with clients and distributors. Improvements and enhancements to the self-service client portal are ongoing with some challenges along the way due to the transition to TRON[4] which is currently in progress.

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[4] TRON is the new non-life business core system being implemented

In 2019 MMS launched the ChatBot on the company website and Facebook page and this is facilitating the client interaction at various client touchpoints. During this year, the ChatBot will be further enhanced to provide clients with a status update on their claims. This will improve MMS's overall response time and efficiency.

An agency portal has been developed to improve communication and provide better support to the Company's Distributor Clients. The development has taken place during 2019 and the portal will be formally launched in 2020.

During 2020 the company will go through a reassessment of its digital strategy to ensure that it is fully aligned to emerging trends in consumer demands.

C.6.4. Reputational risk

Reputational risk is defined as the probability that a negative perception or experience by the various stakeholders (employees, clients, distributors, providers, shareholders, and society in general) could have an adverse effect on MMS.

Reputational risk is managed based on the Corporate Social Responsibility Policy as well as the MAPFRE Group's 2019-2021 Sustainability Plan, approved by MAPFRE S.A.'s Board of Directors.

Specific actions implemented to manage reputational risk include those related to transparency, cybersecurity, diversity, combating fraud and corruption risks, the inclusion of environmental, social and governance factors in the supply chain, in underwriting and during the investment decision-making process, among others.

C.6.5. Non-compliance risk

Non-compliance risk is defined as the possibility of incurring losses as a result of legal or regulatory penalties or reputation losses arising from the failure to comply with laws, regulations and standards (both internal and external), or with applicable administrative requirements.

This risk is managed, primarily, through the identification, assessment, monitoring and mitigation tasks performed by the MMS's Compliance Area. In 2019, MMS put in place the Compliance Risk Management Process as developed by the Corporate Compliance Office.

C.7. Any other information

C.7.1. Sensitivity analysis of significant risks

MMS performs sensitivity analyses of the solvency position involving certain macroeconomic variables, such as:

- An increase/decrease in interest rates
- Appreciation of the euro
- A Decrease in the valuation of equities
- Increase in the spread of corporate and sovereign exposures.

The sensitivity of the solvency ratio[5] to the changes in these variables is shown below:

	31/12/2019	% Change
Solvency Ratio (SR)	278.8%	
SR in the event of a 100 basis point increase in the interest rate	275.7%	-3.2 p.p.
SR in the event of a 100 basis point decrease in the interest rate	274.8%	-4.0 p.p.
SR in the event of a 10% appreciation of the euro	278.4%	-0.4 p.p.
SR In the event of a 25% decrease in equities	273.1%	-5.7 p.p.
SR In the event of a 50 basis point increase in corporate spreads	278.5%	-0.3 p.p.
SR In the event of a 50 basis point increase in corporate and sovereign spreads	276.3%	-2.5 p.p.

p.p. percentage points

C.7.2. Other issues

<u>Off-balance-sheet positions</u>

There are no significant exposures to the above risks arising from off-balance sheet positions.

[5] MMS does not consider the UFR since it does not have a material long term profile. The UFR is the long-term interest rate that is used as a reference to construct the curve of interest rates in the periods in which there are no longer market indicators.

D. Valuation for solvency purposes

D.1. Assets

The following are the main differences between the measurement of assets under Solvency II ("Solvency II Value") and IFRS ("Accounting value") as at 31st December 2019.

It is important to note that the balance sheet presented is in-line with the Solvency II regulations, and therefore it was necessary to re-classify data included under certain headings in the financial statements to different headings as presented under "Accounting value" in the table below:

Assets	Solvency II Value 2019	Accounting Value 2019
Goodwill	-	-
Deferred Acquisition Costs	-	7,775
Intangible assets	-	6,934
Deferred tax assets	709	-
Pension benefit surplus	-	-
Property, plant & equipment held for own use	2,874	2,874
Investments (other than assets held for index-linked and unit-linked contracts)	117,062	83,615
Property (other than for own use)	16,167	16,167
Holdings in related undertakings, including participations	90,979	57,593
Equities	2,454	2,454
Equities – listed	2,454	2,454
Equities - unlisted	-	-
Bonds	7,014	6,952
Government Bonds	6,200	6,141
Corporate Bonds	814	811
Structured notes	-	-
Collateralised securities	-	-
Collective Investments Undertakings	449	449
Derivatives	-	-
Deposits other than cash equivalents	-	-
Other investments	-	-
Assets held for index-linked and unit-linked contracts	-	-
Loans and mortgages	-	-
Loans on policies	-	-
Loans and mortgages to individuals	-	-
Other loans and mortgages	-	-
Reinsurance recoverables from:	23,889	29,953
Non-life and health similar to Non-life	23,836	29,901
Non-life, excluding health	23,916	29,870
Health similar to Non-Life	(80)	31
Life and health similar to life, excluding health and index-linked and unit-linked	52	53
Health similar to life	-	-
Life, excluding health and index-linked and unit-linked	52	53
Life index-linked and unit-linked	-	-
Deposits to cedants/Deposits for Accepted Reinsurance	-	-
Insurance and intermediaries receivables	15,237	15,237
Reinsurance receivables	316	316
Receivables (trade, not insurance)	446	446

Assets	Solvency II Value 2019	Accounting Value 2019
Own shares (held directly)	-	-
Amounts due in respect of own funds items	-	-
Cash and cash equivalents	27,045	27,045
Any other assets, not elsewhere shown	1,291	1,353
TOTAL ASSETS	**188,869**	**175,547**

Figures in thousand euros

Below are the explanations of the key asset valuation differences in the table above.

Deferred acquisition costs

Under IFRS, acquisition costs can be deferred whilst for Solvency II reserving expenses are not deferred but are taken into account fully in the technical provisions.

Intangible assets

Under IFRS, intangible assets are measured at cost less their accumulated amortization and where applicable possible impairment. MMS mainly recognises Value of Business Acquired (VOBA) and computer software as intangible assets. Computer software mainly represents amounts capitalized relating to the development of MMS's IT system by related companies forming part of the MAPFRE Group.

The VOBA is amortised using the straight-line method over a period not exceeding five years. The carrying value is assessed yearly for impairment by projecting the profitability of the portfolio acquired over the life of the asset having considered projected combined ratios and retention patterns.

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use to the specific software. These costs are amortised using the straight-line method over their useful lives, not exceeding a period of seven years.

Under Solvency II, an intangible asset other than goodwill is only recognised at a value not equal to zero if it can be sold separately and the undertaking can demonstrate the existence of a market value for the same or similar assets. MMS considers that both the VOBA and computer software do not meet the conditions established in the Solvency II regulations for market value recognition, and therefore are reported at a zero value.

Deferred tax assets

Deferred taxes are measured under Solvency II as the amounts reported in the audited financial statements as adjusted by the tax impact (at different applicable rates) on the difference between the values assigned to assets and liabilities for solvency purposes, and their carrying values as recognised in the financial statements and valued for tax purposes.

Under IFRS, deferred taxes are calculated on all temporary differences using a principal tax rate of 35% with the exception of investment property and freehold and other property, for which deferred income taxes may be calculated using a principal tax rate of 8% or 10% of the carrying amount.

MMS recognised a net deferred tax liability on its closing IFRS balance sheet at a carrying amount of €0.71 million. The differences between the Solvency II and IFRS value of the deferred tax assets arose due to the different valuation criteria used for the following:

- Deferred acquisition costs

- Intangible assets
- Participations
- Reinsurance recoverables
- Technical provisions

Due to the nature of the deferred tax assets held by MMS, there are no specific expiration dates for them.

Property, plant and equipment held for own use

Property, plant and equipment held for own use includes property and vehicles leased from third parties. These leases have been valued in accordance with IFRS 16 – Leases, which came into effect on the 1 January 2019. The carrying value as at 31 December 2019 was €570k.

Investments (other than assets held for index-linked and unit-linked contracts)

All investments must be measured at fair value on the Solvency II balance sheet, regardless of the accounting portfolio under which they are classified. The determination of fair value is performed by following the same procedures and methodology used for determining fair value based on IFRS 13.

IFRS 13 defines fair value as the price received in exchange for an asset or paid for transferring a liability during an orderly transaction between market participants at the valuation date. In a fair value valuation, the transaction should take place in the asset or liability's main market, and where this does not exist, in the most advantageous market. Valuation techniques appropriate to the circumstances for which there is sufficient information to conduct a fair value measurement must be used, maximising the use of relevant observable variables while minimising the use of variables that cannot be observed.

In order to increase the coherence and comparability of the fair value measurements, IFRS 13 establishes a fair value hierarchy making it possible to classify the valuation technique variables used to determine fair value in three different levels:

Level 1 corresponds to unadjusted quoted prices on active markets; Level 2 uses observable data, or listed prices for instruments which are similar to those being appraised; or other valuation techniques in which all the significant variables are based on observable market data; Level 3 uses specific variables for each case.

Although not all assets and liabilities may have available observable market transactions or information, in any case, the objective of a fair value appraisal is always the same: estimate the price for an orderly transaction for selling or transferring the liability between market participants at the valuation date in present market conditions.

Under "Investments", based on the Solvency II Balance sheet, the following investments are included:

- ***<u>Holdings in related undertakings</u>***

In accordance with Article 212 of the Solvency II Directive 2009/138/EC, related parties and subsidiaries are related companies in which there is an investment or over which there is a dominant significant influence.

Wherever possible, investments in related companies are measured at their listed prices on active markets. However, due to the absence of quoted prices on active markets, the assets were valued using the adjusted equity method, considering the solvency valuation specifics indicated for each investment or subsidiary.

Under IFRS, investments in subsidiaries are valued at cost less impairment, which differs from Solvency II criteria.

Due to the difference in valuation criteria, an increase of €33.39 million was recorded for these investments on the Solvency II balance sheet when compared to the IFRS balance sheet.

- ***Bonds***

Under IFRS, accrued interest for bonds is accounted for as "Any other assets, not elsewhere shown", whilst the Solvency II value of the bonds is equal to the market value.

Reinsurance recoverables

The calculation of the Reinsurance recoverables is in line with the calculation of technical provisions for direct insurance, which means that these amounts must be recognised at their best estimate, also considering the timing difference between collection and direct payments, as well as the expected losses from the counterparty default.

When determining the recoverable value of the amounts of reinsurance arising from amounts considered in technical provisions, MMS takes into account the following:

- The expected value of potential reinsurance default based on creditworthiness and the time horizon of expected payment patterns.
- Expected reinsurance collection patterns based on past experience.

For reinsurance recoverables extending beyond the established payment period outlined in reinsurance contracts in force, a renewal of current contractual terms is considered, with no substantial modification in contracted cost or coverage.

The classification among the different lines of business and the development of reinsurance claims are based on the assumptions made for gross technical provisions.

The value of the potential recovery of reinsurance arising as a result of technical provisions for direct insurance is directly linked to estimates and projections for future cash flows which might be subject to a number of factors of uncertainly, which are mainly the following:

- Direct insurance and reinsurance claims, which are linked to reinsurance contracts.
- The ability to meet the reinsurer's future payment commitments.
- Reinsurance payment pattern.

Under IFRS, technical reserves for cessions to reinsurers are calculated in accordance with the reinsurance contracts entered into as applied to the gross technical provisions.

Insurance and intermediaries receivables

Balances included under insurance and intermediaries receivables mainly relate to premiums due net of commissions that are either not past their payment date or past their payment date net of any impairment provision against them. The collection of such amounts has not been included in the cash flows for the calculation of technical provisions.

Reinsurance receivables

Reinsurance receivables mainly include amount receivable from reinsurers by way of claim recoveries on claims paid by the Company. The collection of such amounts has not been included in the cash flows for the calculation of technical provisions.

Any other assets, not elsewhere shown

The difference between the IFRS value and the Solvency II value of €62k relates to the accrued interest of bonds, which under IFRS s accounted for under “Any other assets, not elsewhere shown”.

D.2. Technical provisions

Following are the main differences between the valuation of technical provisions under Solvency II and IFRS:

Technical provisions	Solvency II Value 2019	Accounting Value 2019
Technical provisions - Non-Life	74,583	87,129
Technical provisions - Non-Life (excluding health)	69,707	80,441
Technical provisions calculated as a whole	-	
Best Estimate (BE)	67,074	
Risk margin (RM)	2,633	
Technical provisions - health (similar to Non-Life)	4,876	6,688
Technical provisions calculated as a whole	-	
Best Estimate (BE)	4,541	
Risk margin (RM)	335	
Technical provisions - Life (excluding index-linked and unit-linked)	761	1,037
Technical provisions - health (similar to Life)	-	-
Technical provisions calculated as a whole	-	
Best Estimate (BE)	-	
Risk margin (RM)	-	
Technical provisions - Life (excluding health and index-linked and unit-linked)	761	1,037
Technical provisions calculated as a whole	-	
Best Estimate (BE)	647	
Risk margin (RM)	114	
Technical provisions - index-linked and unit-linked	-	-
Technical provisions calculated as a whole	-	
Best Estimate (BE)	-	
Risk margin (RM)	-	
Other technical provisions	-	-
TOTAL TECHNICAL PROVISIONS	**75,344**	**88,166**

Figures in thousand euros

As has been previously mentioned, MMS is an insurance entity specialising in the Non-Life segment, which covers the legally-assigned risks in this segment, although it also operates in the Life segment with a fairly insignificant portfolio (1 percent of the total technical provisions).

In general terms, the main difference between both valuations is the criteria framework under which each regulation falls. While under Solvency II, technical provisions are measured using market economic criteria, for financial statements, technical provisions are calculated based on accounting standards. The Solvency II Directive stipulates that the value of technical provisions shall be equal to the sum of the best estimate and the risk margin.

The following are the qualitative explanations of the valuation differences when using Solvency II criteria and those used during the preparation of the financial statements.

D.2.1. Best estimate and risk margin

Best estimate

The Best Estimate Liabilities (BEL) of the Non-life and Health similar to Non-Life businesses are calculated separately from provisions for claims outstanding and premium provisions.

a) <u>Best estimate of the provision for claims outstanding</u>

The best estimate for the provision for claims outstanding is based on the following principles:

- Taking into account all claims, which have been incurred prior to the valuation date, regardless of whether they have been reported or not.
- It is calculated as the present value of expected future cash flows associated with the incurred claim. Projected cash flows include payments for services and related expenses (claims and investment management).
- Should there be any liabilities transferred to a counterparty, the recoverable amounts are adjusted to factor in the expected losses arising from default of the counterparty.
- The best estimate considers the time value of money based on the consideration of the claim inflows and outflows.
- From a methodological point of view, it is determined as the ultimate cost of claims and effective payments made, net of their potential recovery or collection.

The claims provisions in the financial statements include: the provision for claims outstanding and the provision for claims settlement expenses. The provisions for claims outstanding are largely based on case-by-case estimates supplemented with additional provisions for IBNR and unexpired risks in those instances where the ultimate cost determined by estimation techniques is higher. Motor claims occurring between 2016 and 2019 have been determined on an ultimate cost basis. Certain losses involving fatalities or serious bodily injury are reserved at the case-by-case reserve estimate.

The best estimate of claim provisions calculated based on Solvency II criteria present the following differences with respect to those calculated based on financial statement requirements:

- While under Solvency II, technical provisions are measured using market economic criteria, for financial statements, annual technical provisions are calculated based on accounting standards.
- The consideration of all cash flow sources.
- The counterparty default risk adjustment to reinsurance recoverable amounts.
- The financial discount of cash flows.

b) <u>Best estimate of the Provision for premiums</u>

The best estimate for the Provision for premiums is based on the following principles:

- It relates to future claims, or those which take place subsequent to the valuation date, within the remaining claim coverage period.
- It is calculated as the present value of expected cash flows associated with the current portfolio, in accordance with contract boundaries.

- Projected cash flows will include payments for services and related expenses (administration, acquisition, claims management, and investment management).

- Should there be any liabilities transferred to a counterparty, the recoverable amounts are adjusted to contemplate the expected losses due to default of the counterparty.

- The best estimate takes into account the time value of money based on an analysis of claim inflows and outflows.

The calculation of this provision is comprised of the cash flows corresponding to two portfolios:

- Current portfolio, which includes the following:

  - Expected claims. Two different methods may be used to calculate the present value of benefit payments:

    - The frequency and average cost method: claims are calculated as the result of exposure based on frequency assumptions and ultimate average costs.

    - Loss ratio method: the expected claims arising from applying an Ultimate loss ratio to Unearned Premium Reserve (UPR), gross of acquisition expenses. In this method, moreover, Events Not in Data (ENIDs) have been considered. ENIDs are events that the Company has never registered, and therefore no experience of their likely impact, but which may happen in the future. The Company has identified such possible losses estimated the cover limits and the probability of such events happening. The estimated impact was seen both from a gross basis and net of potential reinsurance recovery. It has been included as an assumption based on the earned premium.

  - Expenses attributable to the current portfolio: acquisition (no commissions), administration, chargeable to benefits, investment expenses, as well as other technical expenses.

- Future business, which includes the following:

  - Premiums for policies, which have not yet been renewed but include company commitments to renew. This calculation includes the future behaviour by policyholders based on the application of an estimated lapse ratio.

  - Expected loss ratio relating to future premiums, using the same methods indicated for the current portfolio.

  - Expenses attributable to future premiums (charged expense-to-premium ratio applied to future premiums): acquisition expenses (including fees), administration, chargeable to benefits, investment expenses, as well as other technical expenses.

Under IFRS, this provision is recognised under the unearned premium reserve, which is calculated on a policy-by-policy basis, reflecting the premium rate on a pro-rata temporary basis for the unearned period of such policies and complemented by the unexpired risk provision calculated segment-by-segment where applicable. This provision supplements the unearned premiums reserve with an amount by which the future contractual cash flows arising from such reserve exceed the same reserve.

Contract boundaries

When calculating the best estimate for Solvency II purposes, the contract boundaries must be taken into account. Depending on the margins on product premiums, the inclusion of the limits of the contract will generate an increase in the best estimate (if the contracts are not profitable) or a reduction in the same (if they are profitable).

The obligations arising from the contract, including those which relate to the insurance/reinsurance company's unilateral right to renew or increase its limits and the corresponding premiums are included in its text, except for:

- Commitments provided by the Company after the date on which it has the unilateral right to:
    - Cancel the contract.
    - Reject premiums payable under the contract.
    - Modify the premiums or benefits to which it is bound by virtue of the contract, so that the premiums clearly reflect the risks.
- All obligations which do not correspond to premiums which have already been paid, unless the policyholder may be forced to pay future premiums, provided that the contract:
    - does not establish an indemnity for a specified uncertain event which may adversely affect the reinsured party.
    - does not include a financial guarantee for the benefits.

The conclusion is that the premium provisions calculated based on Solvency II criteria present the following differences with respect to those calculated based on IFRS requirements:

- The application of the concept of contractual limits, which involves the consideration of future business including the reinsurance ceded attached thereto. Under IFRS, future premiums must be taken into account only if included in the corresponding technical note.
- The consideration of all cash flow sources. In general, under Solvency II, the premium provision for profitable products included in a portfolio in force is less than the unearned premiums reserve reflected in the financial statements. In cases of premium insufficiency, the premium provision is comparable to the unearned premium reserve plus the unexpired risk provision (without taking the discount effect into account). For future business, the Solvency II premium provision for profitable products will be negative.
- The counterparty default risk adjustment to recoverable reinsurance amounts.
- The financial discount of cash flows.

Risk margin

The risk margin is conceptually equivalent to the cost of supplying eligible own funds and the SCR necessary to support insurance commitments during their entire period of validity and until they are definitively settled. The interest rate used in determining the cost of supplying the amount of eligible own funds is known as the cost-of-capital rate. MMS uses the 6 percent rate set by Commission Delegated Regulation (EU) 2015/35.

The method for calculating risk margin may be expressed as follows:

$$RM = CoC * \sum \frac{SCR_t}{(1 + r_{t+1})^{t+1}}$$

where:

- RM: Risk Margin
- CoC: the cost-of-capital rate which is taken as 6%
- SCR_t: Solvency capital requirement after t years. This solvency capital requirement will be that capital necessary to meet insurance and reinsurance obligations for their effective period, with said capital reflecting underwriting risk, residual market risk, counterparty default risk with regards to reinsurance treaties, and operational risk.
- r_{t+1}: basic risk-free interest rate for the maturity of t+1 years.

There are a number of simplified methods to calculate risk margin:

- Level 1: explains how to approximate underwriting, counterparty default, and market risks.
- Level 2: this is based on the assumption that the future solvency capital requirement will be proportional to the "best estimate" of technical provisions during the year in question.
- Level 3: this consists of using the modified duration of liabilities to calculate the current and future solvency capital requirement in a single step.
- Level 4: calculates the risk margin as a percentage of the best estimate of technical provisions net of reinsurance.

MMS calculates the risk margin using Level 2 simplification method.

Actuarial methods and assumptions used when calculating technical provisions

The following are the main actuarial techniques used by MMS when calculating technical provisions under Solvency II:

- A combination of generally-accepted deterministic methods used for calculating the ultimate loss ratio based on a selection of factors to develop frequencies and average costs.
- Stochastic methods for determining claims assuming a probability distribution function.

MMS considers the methodologies used to be appropriate.

The following two key assumptions were used:

- Economic assumptions, which are compared against available financial and macroeconomic indicators which mainly include:
  - Interest rate structure.
  - Exchange rates.
  - Market trends and financial variables.
- Non-economic assumptions, which are mainly obtained from generally-available data based on MMS's and/or the MAPFRE Group's past experience, or external sector/market sources:
  - Realistic administration, investment, acquisition, etc. expenses that will be incurred throughout the duration of the contracts in the portfolio.

- Portfolio losses and lapse rates.
- The frequency and severity of claims based on past data.
- Legislative changes.

Also, it is worth noting that under IFRS, management actions and policyholder behaviour are not included when calculating technical provisions, while under Solvency II, companies can establish a comprehensive plan covering future decisions considering the necessary time frame to calculate their best estimates, including a probability analysis of when policyholders might exercise certain rights included in their insurance policies.

MMS employs an effective actuarial method, which guarantees the appropriateness and consistency of the underlying methods and models used, as well as the assumptions used in these calculations.

For Life insurance:

The following two key assumptions were used:

- Economic assumptions, which are compared against available financial and macroeconomic indicators which mainly include:
  - Interest rate structure broken down by the currencies in which the commitments are denominated.
  - Exchange rates.
  - Market trends and financial variables.
- Non-economic assumptions, which are mainly obtained from generally-available data based on MMS's and/or the MAPFRE Group's past experience, or external sector/market sources:
  - Realistic administration, investment, acquisition, etc. expenses that will be incurred throughout the duration of the contracts in the portfolio.
  - Portfolio losses and policy surrenders.
  - Mortality and longevity.
  - Disability and other risks.

Also, it is worth noting that under IFRS, management actions and policyholder behaviour are not included when calculating technical provisions, while under Solvency II, companies may establish a comprehensive plan covering future decisions considering the necessary time frame to calculate their best estimates, including a probability analysis of when policyholders might exercise certain rights included in their insurance policies.

MMS employs an effective actuarial method, which guarantees the appropriateness and consistency of the underlying methods and models used, as well as the assumptions used in these calculations.

Degree of uncertainty associated with the amount of technical provisions

The value of the technical provisions is directly linked to estimates and projections for future cash flows, which might be subject to a number of factors of uncertainly, mainly:

- The probability that the obligation will materialise with regard to future cash flows.
- The timing of the claim.
- Potential amount of the future cash flows.
- The risk-free interest rate.

These factors are generally estimated based on expert opinions within the area or market data, and their calculation and impact on the technical provisions are duly documented and processed.

D.2.2. Measures designed for managing long-term guarantees

MMS does not make use of any long-term guarantee measures.

D.2.2.a. Matching adjustment

MMS does not make use of any matching adjustments.

D.2.2.b. Volatility adjustment

MMS does not make use of any volatility adjustments.

D.2.2.c. Transitional measure on the risk-free interest rates

MMS does not make use of any transitional measures on the risk-free interest rates

D.2.2.d. Transitional measure on technical provisions

MMS does not make use of any transitional measures on technical provisions.

D.2.3. Significant changes in the assumptions used when calculating technical provisions

MMS did not make any changes with respect to the assumptions used in the calculation of the technical provisions, as a result of the implementation of the Solvency II rules.

D.3. Other Liabilities

Following are the main differences between the measurement of other liabilities under Solvency II and IFRS:

Other Liabilities	Solvency II Value 2019	Accounting Value 2019
Total technical provisions	**75,344**	**88,166**
Contingent liabilities	-	-
Provisions other than technical provisions	-	-
Pension benefit obligations	1,101	1,101
Deposits from reinsurers	-	-
Deferred tax liabilities	-	857
Derivatives	-	-
Debts owed to credit institutions	-	-
Financial liabilities other than debt owed to credit institutions	717	717
Insurance & intermediaries payables	195	195
Reinsurance payables	3,961	3,961
Payables (trade, not insurance)	2,605	2,605
Subordinated liabilities	-	-
Subordinated liabilities not in basic own funds	-	-
Subordinated liabilities included in basic own funds	-	-
Any other liabilities, not elsewhere shown	3,553	5,142
TOTAL LIABILITIES	**87,476**	**102,744**
EXCESS OF ASSETS OVER LIABILITIES	**101,392**	**72,803**

Figures in thousand euros

Deferred tax liabilities

As mentioned earlier, MMS recognized a net deferred tax liability on its closing IFRS balance sheet at a carrying amount of €0.86 million. MMS recognised a net deferred tax asset on the Solvency II balance sheet at €0.71 million, resulting from the offsetting of deferred tax assets and liabilities since taxes are paid to the same tax authority.

Insurance and intermediaries payables

Balances included under insurance and intermediaries payables include amounts that are due to policyholders or intermediaries as a result of transactions made. The payment of such amounts has not been included in the cash flows for the calculation of technical provisions.

Reinsurance payables

Reinsurance receivables mainly include amounts payable to reinsurers by way of ceded premiums less commission and claim recoveries on claims paid by the Company. The payment of such amounts has not been included in the cash flows for the calculation of technical provisions.

Any other liabilities, not elsewhere shown

“Accounting value” mainly includes deferred reinsurance commissions together with other accruals with an accounting value of €5.14 million. For Solvency II purposes, deferred reinsurance commissions are taken into consideration during the valuation of technical provisions, as they include the entirety of the associated expense, and therefore do not appear under this heading.

D.4. Alternative methods for valuation

MMS's Investment property is valued at its appraisal value, determined by an external, independent and qualified architect.

D.5. Any other information

There have been no significant changes in valuation criteria for assets and liabilities during the year.

Finance and operating leases

Finance and operating leases are described in Section A.4.2 of this report.

D.6. Annexes

A) Assets

Template **S.02.01.02** detailing quantitative asset disclosures at 31st December 2019:

Assets(*)	Solvency II Value 2019
Intangible assets	-
Deferred tax assets	709
Pension benefit surplus	-
Property, plant & equipment held for own use	2,874
Investments (other than assets held for index-linked and unit-linked contracts)	117,062
Property (other than for own use)	16,167
Holdings in related undertakings, including participations	90,979
Equities	2,454
Equities — listed	2,454
Equities — unlisted	-
Bonds	7,014
Government Bonds	6,200
Corporate Bonds	814
Structured notes	-
-Collateralised securities	-
Collective Investments Undertakings	449
Derivatives	-
Deposits other than cash equivalents	-
Other investments	-
Assets held for index-linked and unit-linked contracts	-
Loans and mortgages	-
Loans on policies	-
Loans and mortgages to individuals	-
Other loans and mortgages	-
Reinsurance recoverables from:	23,889
Non-Life and health similar to Non-life	23,836
Non-Life excluding health	23,916
Health similar to Non-life	(80)
Life and health similar to life, excluding health and index-linked and unit-linked	52
Health similar to Life	-
Life excluding health and index-linked and unit-linked	52
Life index-linked and unit-linked	-
Deposits to cedants	-
Insurance and intermediaries receivables	15,237
Reinsurance receivables	316
Receivables (trade, not insurance)	446
Own shares (held directly)	-
Amounts due in respect of own fund items or initial fund called but not yet paid in	-
Cash and cash equivalents	27,045
Any other assets, not elsewhere shown	1,291

Assets(*)	Solvency II Value 2019
Total assets	**188,869**

Figures in thousand euros

B) Technical provisions

B.1. Template **S.02.01.02** detailing quantitative technical provisions disclosures at 31st December 2019:

Liabilities (*)	Solvency II Value 2019
Technical provisions — non-life	**74,583**
Technical provisions — non-life (excluding health)	69,707
Technical provisions calculated as a whole	-
Best Estimate	67,074
Risk margin	2,633
Technical provisions — health (similar to non-life)	4,876
Technical provisions calculated as a whole	-
Best Estimate	4,541
Risk margin	335
Technical provisions — life (excluding index-linked and unit-linked)	**761**
Technical provisions — health (similar to life)	-
Technical provisions calculated as a whole	-
Best Estimate	-
Risk margin	-
Technical provisions — life (excluding health and index-linked and unit-linked)	761
Technical provisions calculated as a whole	-
Best Estimate	647
Risk margin	114
Technical provisions — index-linked and unit-linked	**-**
Technical provisions calculated as a whole	-
Best Estimate	-
Risk margin	-

Figures in thousand euros

B.2. Templates S.12.01.02 and S.17.01.02 detailing Life and Non-Life technical provisions by line of business at 31st December 2019.

B.2.1 Template S.12.01.02 – Life and Health SLT Technical Provisions as at 31st December 2019

	Other life insurance		Total (life insurance, excluding health but including index-linked and unit-linked)
		Contracts without options or guarantees	
Technical provisions calculated as a whole	-		-
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to technical provisions calculated as a whole.	-		-
Technical provisions calculated as a sum of the Best Estimate and the Risk Margin			
Best Estimate			
Gross Best Estimate		647	647
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default		52	52
Best estimate minus recoverables from reinsurance/SPV and Finite Re — total		594	594
Risk Margin	114		114
Amount of the transitional on Technical Provisions			
Technical Provisions calculated as a whole	-		-
Best Estimate			-
Risk Margin	-		-
Technical provisions — total	761		761

Figures in thousand euro

B.2.2 Template S.17.01.02 – Non-Life Technical Provisions as at 31st December 2019

	Direct business and accepted proportional reinsurance									Accepted non-proportional reinsurance	Total Non-Life obligation
	Medical expense insurance	Income protection insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Assistance	Miscellaneous financial loss	Non-proportional property reinsurance	
Technical provisions calculated as a whole	-	-	-	-	-	-	-	-	-	-	-
Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default associated to TP as a whole	-	-	-	-	-	-	-	-	-	-	-
Technical provisions calculated as a sum of BE and RM											
Best estimate											
Premium provisions											
Gross	3,177	304	6,766	7,976	759	3,373	1,005	141	64	-	23,565
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	(103)	(7)	(653)	147	(72)	1,324	(32)	(18)	-	-	586
Net Best Estimate of Premium Provisions	3,281	311	7,419	7,828	831	2,049	1,037	159	64	-	22,979
Claims provisions											
Gross	576	483	24,600	5,325	1,861	7,021	7,723	254	-	206	48,050
Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	-	31	11,923	53	1,339	5,722	4,155	0	-	28	23,250
Net Best Estimate of Claims Provisions	576	452	12,678	5,272	522	1,300	3,568	254	-	179	24,799
Total Best estimate – gross	3,754	787	31,366	13,301	2,620	10,395	8,728	395	64	206	71,615
Total Best estimate – net	3,857	763	20,096	13,100	1,353	3,349	4,605	413	64	179	47,779
Risk margin	279	56	1,047	671	139	324	348	79	3	23	2,968
Amount of the transitional on Technical Provisions											

	Direct business and accepted proportional reinsurance									Accepted non-proportional reinsurance	Total Non-Life obligation
	Medical expense insurance	Income protection insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance	Fire and other damage to property insurance	General liability insurance	Assistance	Miscellaneous financial loss	Non-proportional property reinsurance	
Technical Provisions calculated as a whole	-	-	-	-	-	-	-	-	-	-	-
Best estimate	-	-	-	-	-	-	-	-	-	-	-
Risk margin	-	-	-	-	-	-	-	-	-	-	-
Technical provisions - total											
Technical provisions – total	4,033	843	32,413	13,972	2,759	10,719	9,075	474	67	229	74,583
Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total	(103)	23	11,270	201	1,267	7,046	4,123	(17)	-	28	23,836
Technical provisions minus recoverables from reinsurance/SPV and Finite Re – total	4,137	819	21,144	13,772	1,492	3,673	4,952	491	67	201	50,747

Figures in thousand euro

B.3 Template **S.19.01.21** – Non-life insurance claims

The following templates reflect the estimate made by MMS of the cost of claims (those paid and provisions for claims in accordance with the Solvency II valuation principles), as well as how the estimate evolves over time.

Gross Claims Paid (non-cumulative)													
Development year													
Year	0	1	2	3	4	5	6	7	8	9	10 & +	In Current Year	Sum of years (cumulative)
Prior											(459)	(459)	(501)
N - 9	10,324	4,089	410	336	164	22	49	49	202	(21)		(21)	15,623
N - 8	9,768	4,476	985	563	363	53	38	89	40			40	16,375
N - 7	10,016	4,260	816	357	129	69	44	44				44	15,735
N - 6	10,620	4,388	620	380	472	1,010	173					173	17,663
N - 5	10,293	4,465	1,756	(444)	423	61						61	16,555
N - 4	11,611	8,709	419	1,109	250							250	22,097
N - 3	15,121	10,181	1,918	627								627	27,847
N - 2	17,885	9,426	2,460									2,460	29,771
N - 1	18,707	9,787										9,787	28,495
N	21,555											21,555	21,555
											Total	**34,519**	**211,215**

Figures in thousand euro

The above table reflects payments made each year for claims arising during non-accumulated years of occurrence.

Gross undiscounted Best Estimate Claims Provisions													
Development year													
Year	0	1	2	3	4	5	6	7	8	9	10 & +		Year end (discounted data)
Prior											1,381		1,388
N - 9	-	-	-	-	-	-	1,503	973	420	158			159
N - 8	-	-	-	-	-	506	410	332	1,543				1,549
N - 7	-	-	-	-	2,459	1,398	1,594	1,500					1,503
N - 6	-	-	-	2,268	1,141	405	188						180
N - 5	-	-	1,464	1,478	815	855							843
N - 4	-	3,656	4,957	3,583	3,265								3,275
N - 3	17,270	6,218	3,373	2,440									2,487
N - 2	18,926	8,310	6,333										6,367
N - 1	21,329	11,865											11,898
N	18,382												18,402
												Total	**48,050**

Figures in thousand euro

C) Other liabilities

Template **S.02.01.02** detailing quantitative disclosures of other liabilities at 31st December 2019:

Liabilities (*)	Solvency II Value
	2019
Contingent liabilities	-
Provisions other than technical provisions	-
Pension benefit obligations	1,101
Deposits from reinsurers	-
Deferred tax liabilities	-
Derivatives	-
Debts owed to credit institutions	-
Financial liabilities other than debts owed to credit institutions	717
Insurance & intermediaries payables	195
Reinsurance payables	3,961
Payables (trade, not insurance)	2,605
Subordinated liabilities	-
Subordinated liabilities not in basic own funds	-
Subordinated liabilities included in basic own funds	-
Any other liabilities, not elsewhere shown	3,553
Total liabilities[6]	**87,476**
Excess of assets over liabilities	**101,392**

Figures in thousand euros

[6] The amount of Total liabilities includes the total of Technical Provisions in Annex D.6.B and not only the sum of the Other liabilities of this table.

E. Capital Management

E.1. Own funds

E.1.1. Own funds objectives, policies and management processes

The main objectives to manage and monitor MMS's own funds and capital are:

- Ensure that the eligible capital continuously meets the applicable regulatory requirements and the levels established in the Risk Appetite.
- Ensure that the projected eligible capital continuously meets the applicable requirements throughout the period covered.
- Ensure that MMS has a medium-term Capital Management Plan in place.
- Capital management will take into account the results from the Own Risk and Solvency Assessment (ORSA), as well as the conclusions reached during that process.
- Within the framework of the medium-term Capital Management Plan, should it be deemed necessary to obtain new resources, the newly-issued capital instruments should be assessed to determine that they meet the requirements to be included in the desired level of quality for eligible capital.

Should the eligible capital be insufficient at any time during the period under consideration in the three-year projections, the Risk Management Office should propose future management measures to be taken into account in order to rectify this shortfall and maintain solvency margins within the levels established by the applicable regulations and Risk Appetite.

The medium-term Capital Management Plan prepared by the Risk Management Office must at least take into account the following:

– Compliance with the applicable Solvency II regulations throughout the projection period, taking into consideration any known future changes to regulations while maintaining solvency margins aligned with those established in the Risk Appetite.
– All eligible capital instruments envisaged.
– Refunds, both contractual on the due date and those, which it is possible to make on request before maturity, relating to elements of eligible capital.
– The results of the ORSA projections.
– Foreseeable dividends and their impact on eligible capital.

MMS has not used the transitional measures on technical provisions.

During 2019, there were not any significant changes in the objectives, policies and processes used to manage MMS's own funds.

E.1.2 Structure, amount, and quality of own funds

The following reflects the structure, amount and quality of own funds, as well as MMS's coverage ratios i.e. the ratio of eligible own funds to SCR and MCR.

	Total		Tier 1 - unrestricted		Tier 1 – restricted		Tier 2		Tier 3	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
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)	19,320	19,320	19,320	19,320			-	-		
Share premium account related to ordinary share capital	688	688	688	688			-	-		
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	67,675	64,866	67,675	64,866						
Subordinated liabilities	-	-			-	-	-	-	-	-
An amount equal to the value of net deferred tax assets	709	734							709	734
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	**88,392**	**85,608**	**87,683**	**84,874**	**-**		**-**	**-**	**709**	**734**
Ancillary own funds										
Unpaid and uncalled ordinary share capital callable on demand	-	-					-	-		

	Total		Tier 1 - unrestricted		Tier 1 – restricted		Tier 2		Tier 3	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
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	88,392	85,608	87,683	84,874	-	-	-	-	709	734
Total available own funds to meet the MCR	87,683	84,874	87,683	84,874	-	-	-	-		
Total eligible own funds to meet the SCR	88,392	85,608	87,683	85,608	-	-	-	-	709	734
Total eligible own funds to meet the MCR	87,683	84,874	87,683	84,874	-	-	-	-		
SCR	31,702	31,660								
MCR	9,641	9,497								
Ratio of Eligible own funds to SCR	278.8%	270.4%								
Ratio of Eligible own funds to MCR	909.5%	893.7%								

	Amount	
	2019	2018
Reconciliation reserve		
Excess of assets over liabilities	101,392	102,608
Own shares (held directly and indirectly)	-	-
Foreseeable dividends, distributions and charges	13,000	17,000
Other basic own fund items	20,717	20,742
Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	-	-
Reconciliation reserve	67,675	64,866
Expected profits		
Expected profits included in future premiums (EPIFP) - Life business	-	-
Expected profits included in future premiums (EPIFP) - Non- life business	142	137
Total Expected profits included in future premiums (EPIFP)	**142**	**137**

Figures in thousand euros

Amount of eligible own funds to meet the SCR, classified by tiers

MMS has €88.39 million of Eligible own funds as at 31st December 2019 (€85.61 million as at 31st December 2018).

As stipulated in the Solvency II regulations, own funds are classified as either basic or ancillary. They are also classified by Tiers (1,2 or 3) depending on the characteristics determining their availability to absorb losses.

As at 31st December 2019, the unrestricted basic Tier 1 own funds of MMS totaled €87.68 million (2018: €84.87 million).

MMS's Tier 1 own funds consist of:

- Ordinary share capital
- Share premium account related to ordinary share capital
- Reconciliation reserve.

In addition, MMS also has basic Tier 3 own funds, totaling to €0.71 million as at 31st December 2019 (2018: €0.73 million), corresponding to the net deferred tax asset.

All of the own funds of MMS are basic own funds. There are no limitations on their eligibility to cover the Solvency Capital Requirements and Minimum Capital Requirements and have the maximum availability for absorbing losses.

None of the Own Fund items required supervisory approval.

The tables included at the beginning of the section indicate the structure, amount and quality of the own funds and includes the items considered to determine the Reconciliation Reserve based on the excess of assets for absorbing losses.

Solvency Capital Requirement (SCR)

The SCR corresponds to the own funds that MMS must hold to limit the probability of bankruptcy to one per 200-year event, or that MMS is 99.5% confident to be able to meet its commitments to insurance beneficiaries or policyholders during the following year.

As stipulated in the Solvency II Directive, all the unrestricted basic Tier 1 own funds and Tier 3 own funds are eligible to cover the SCR.

The Solvency Ratio is equal to 278.8% (2018: 270.4%) and determines the relationship between Eligible own funds and the Solvency capital requirement calculated using the standard formula.

Minimum Capital Requirement (MCR)

The MCR is the minimum level under which financial resources should never fall. When the amount of eligible own funds falls below the MCR, the policyholders and beneficiaries are exposed to an unacceptable level of risk, should MMS continue with its business.

All the basic unrestricted Tier 1 own funds are eligible to cover the MCR. Since Tier 3 own funds do not have adequate availability in order to absorb losses in case it is necessary, these are not available and eligible to cover the MCR. MMS therefore has €0.71 million in available own funds that are not eligible to cover the MCR.

The ratio of eligible own funds to the MCR is equal to 909.5% (2018: 893.7%)

Difference between the equity in the financial statements and the excess of assets over liabilities for Solvency II purposes

When valuing assets and liabilities for the purposes of Solvency II, different criteria are used from those applied when preparing the financial statements. The above criteria differences lead to differences between the equity stated in the financial statements and excess of assets over liabilities for Solvency II purposes.

As at 31st December 2019, the excess of assets over liabilities for Solvency II purposes amounted to €101.39 million, while equity in the financial statements totaled €72.80 million.

The main adjustments that arise from the reconciliation of equity in the financial statements and own funds under Solvency II may be observed below:

	2019	2018
Equity (IFRS value)	72,804	68,307
Difference in valuation of assets	**20,266**	**27,713**
Deferred acquisition costs (DAC)	(6,186)	(5,451)
Intangible Assets	(6,934)	(6,170)
Participations	33,386	39,334
Difference in valuation of liabilities	**8,323**	**6,588**
Technical provisions	6,757	5,059
Deferred Taxes	1,566	1,529
Excess of assets over liabilities (Solvency II Value)	**101,392**	**102,608**

Figures in thousand euro

The quantitative and qualitative explanations are provided in Sections D.1 Assets, D.2 Technical Provisions and D.3 Other liabilities, in this report.

E.1.3. Other information

Essential items in the reconciliation reserve

In the tables included at the beginning of the section, the structure, amount and quality of the own funds are indicated, together with the items that have been considered in determining the reconciliation reserve. This is based on the amount of the Excess of assets over liabilities for the purpose of Solvency II, with the amount of this excess reaching €101.39 million.

To determine the Reconciliation reserve the following items have been deducted**:**

- Foreseeable dividends, distributions and charges amounting to €13 million.
- Other items of basic own funds for an amount of €20.70 million, which are considered as independent items from own funds (ordinary share capital and share premium account and an amount equal to the value of net deferred tax asset).

The reconciliation reserve includes the most potentially volatile component of eligible own funds, the variations of which are determined by MMS's asset and liability management.

Items deducted from own funds

MMS did not deduct any items from the Own Funds.

Own Funds issued and instruments surrendered

MMS did not issue or surrender any own fund instruments during 2019.

Transitional measures

MMS did not consider any basic own-fund items subject to the transitional arrangements referred to in Article 308b(9) and 308b(10) of Directive 2009/138/EC to be applicable.

Distribution to shareholders

To calculate the own funds at 31st December 2019, both the distributed dividends and the foreseeable dividends were taken into consideration.

On the 2nd April 2020, EIOPA issued a statement on dividends distribution in the context of COVID-19. Given the prevailing uncertainty, EIOPA urges that at the current juncture insurers temporarily suspend all discretionary dividend distributions. This suspension should be reviewed as the financial and economic impact of the COVID-19 starts to become clearer.

MMS is currently considering EIOPA's statement vis-à-vis the foreseeable dividend considered in the solvency calculation. The reported solvency ratio reported at year-end would increase to 319.8% should this foreseeable dividend not be included in the calculation.

E.2. Solvency Capital Requirement and Minimum Capital Requirement

E.2.1. Amounts and valuation methodologies of the Solvency Capital Requirement

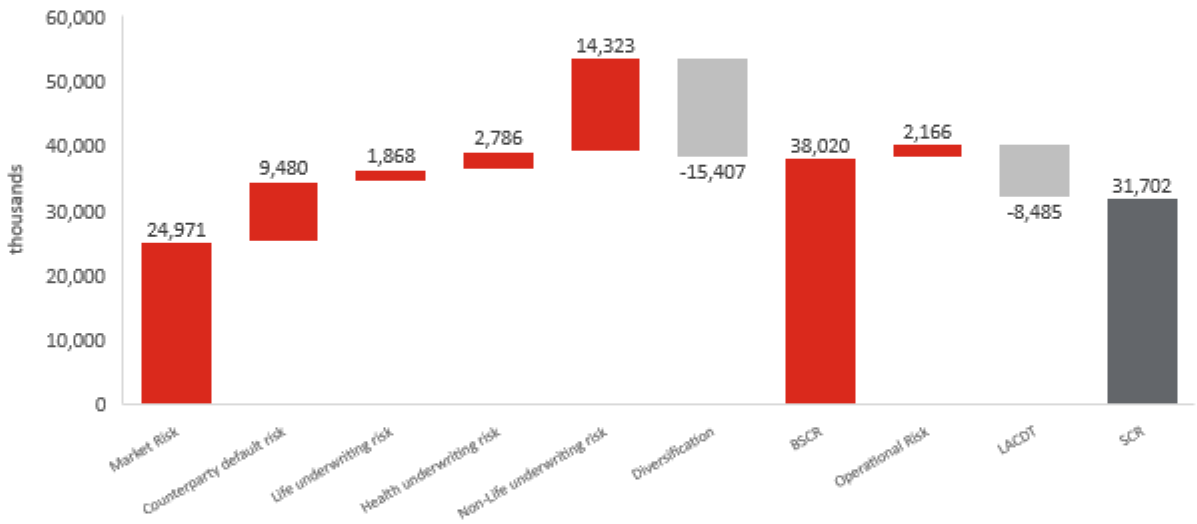
The Solvency Capital Requirement (SCR) at risk module level and calculated using the Standard Formula is set out below:

	Gross solvency capital requirement	Undertaking-specific parameters	Simplifications
Market risk	24,971		-
Counterparty default risk	9,480		
Life underwriting risk	1,868	-	Life mortality risk, Life expense risk, Life catastrophe risk
Health underwriting risk	2,786	-	-
Non-Life underwriting risk	14,323	-	-
Diversification	(15,407)		
Intangible asset risk	-		
Basic Solvency Capital Requirement	**38,020**		

Calculation of the Solvency Capital Requirement	Amount
Operational Risk	2,166
Loss-absorbing capacity of technical provisions	-
Loss-absorbing capacity of deferred taxes	(8,485)
Capital requirement for businesses operated in accordance with Article 4 of Directive 2003/41/EC	-
Solvency Capital Requirement excluding additional capital	31,702
Additional capital already set	-
Solvency capital requirement	**31,702**
Other information regarding the SCR	
Capital requirement for duration-based equity risk sub-module	-
Total amount of the notional solvency capital requirement for the remaining part	-
Total amount of the notional solvency capital requirement for ring-fenced funds	-
Total amount of notional solvency capital requirement for portfolios subject to matching adjustments	-
Diversification effects due to the aggregation of the notional SCR for ring-fenced funds for the purposes of Article 304	-

Figures in thousand euro

The composition of the SCR is set out below; more descriptive information is provided in Section C of this report:



As at 31st December 2019, MMS's total SCR amount was €31.70 million. As at 31st December 2018, it was €31.66 million and the slight increase is mainly due to an increase in Counterparty and Underwriting risks.

To calculate the SCR, MMS used the following simplifications:

- For Life Underwriting risk, MMS uses the simplified calculation for the solvency capital requirement for its life business for life mortality risk, life mortality risk, life expense risk and life catastrophe risk in accordance with Articles 91, 94 and 96 of the Commission Delegated Regulation 2015/35 respectively.

- For Counterparty Default Risk, to calculate the risk-mitigating effect on underwriting risk of a reinsurance arrangement, MMS makes use of the simplified calculation of the mitigating effect in accordance with Article 107 of the Commission Delegated Regulation 2015/35.

These simplifications are considered appropriate to the nature, volume and complexity of the associated risks.

There is no capacity to absorb losses through technical provisions. The loss-absorbing capacity of deferred taxes totalled €8.48 million as at 31st December 2019 (€8.03 million as at 31st December 2018). The loss-absorbing capacity has been calculated using appropriate tax rates for the respective risk modules.

MMS does not make use of capital add-ons or undertaking specific parameters.

As at 31st December 2019, MMS's total MCR amount was €9.64 million. As at 31st December 2018, it was €9.50 million and the increase is mainly due to an overall increase in business.

The following table shows MMS's MCR and the different components of its calculation, which include:

- Net (of reinsurance/SPV) best estimate, for life and non-life insurance obligations.

- Net (of reinsurance) written premiums in the last 12 months, for non-life insurance obligations.

- Total capital at risk, net of (reinsurance/SPV) for life insurance obligations.

Linear formula component for non-life insurance and reinsurance obligations (*)	8,774	
	Non-life activities	
	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	**Net (of reinsurance) written premiums in the last 12 months**
Medical expense insurance and proportional reinsurance	3,857	10,912
Income protection insurance and proportional reinsurance	763	939
Workers' compensation insurance and proportional reinsurance	-	-
Motor vehicle liability insurance and proportional reinsurance	20,096	14,605
Other motor insurance and proportional reinsurance	13,100	20,563
Marine, aviation and transport insurance and proportional reinsurance	1,353	1,855
Fire and other damage to property insurance and proportional reinsurance	3,349	2,963
General liability insurance and proportional reinsurance	4,605	4,336
Credit and suretyship insurance and proportional reinsurance	-	-
Legal expenses insurance and proportional reinsurance	-	-
Assistance and proportional reinsurance	413	2,247
Miscellaneous financial loss insurance and proportional reinsurance	64	28
Non-proportional health reinsurance	-	-
Non-proportional casualty reinsurance	-	-
Non-proportional marine, aviation and transport reinsurance	-	-
Non-proportional property reinsurance	179	-

Linear formula component for life insurance and reinsurance obligations	866	
	Life activities	
	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	**Net (of reinsurance/SPV) total capital at risk**
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	594	
Total capital at risk for all life (re)insurance obligations		1,219,341

Overall MCR calculation	
Linear MCR	9,641
SCR	31,702
MCR cap	14,266
MCR floor	7,925
Combined MCR	9,641

Absolute floor of the MCR	7,400

Minimum Capital Requirement	**9,641**

Notional non-life and life MCR calculaton	Non-Life activities	Life activities
Notional linear MCR	8,774	866
Notional SCR excluding add-on (annual or latest calculation)	28,854	2,848
Notional MCR cap	12,984	1,282
Notional MCR floor	7,214	712
Notional Combined MCR	8,774	866
Absolute floor of the notional MCR	3,700	3,700
Notional MCR	8,774	3,700

Figures in thousand euro

The MCR is the level of capital that guarantees a minimum level of security below which the amount of financial resources should never fall and has a value of €9.64 million. The notional linear MCR is equal to €8.77 million for non-life activities and €0.87 million for life activities. The linear MCR was obtained by applying the factors relating to the data used in the calculation, which are included in the above tables. The combined MCR is equal to €9.64 million and is the result of applying maximum and minimum limits to the linear MCR.

Since the combined MCR is higher than the MCR's absolute limit, the amount of the combined MCR is considered to be the Minimum Capital Requirement, i.e. the amount of €9.64 million.

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

MMS does not use the duration-based equity risk sub-module set out in Article 304 of the Directive 2009/138/EC for the calculation of its Solvency Capital Requirement.

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

MMS does not make use of internal models in its Solvency calculations, but follows the Solvency II standard formula.

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

As at 31st December 2019, MMS had a good solvency position. Therefore, it was considered unnecessary to adopt any other action or corrective measure.

COVID-19 is expected to result in a reduction in the regulatory reported solvency ratio. However, although, at time of writing, it is not possible to have a full impact assessment, given the continuously evolving situation, as things stand, the Company is confident, that given its year-end solvency position, its risk profile and the sensitivities and stress test considered on year-end 2019 balance sheet, that its solvency ratio remains above the regulatory required amounts.

E.6. Any other information

There is no other information regarding the management of capital that has not been included in the preceding sections.

Annex I

The following table presents MMS's subsidiaries at year-end 2019:

Name of Company	Percentage of shares
Euro Globe Holdings Limited	100%
Euromed Risk Solutions Limited*	100%
Bee Insurance Management Limited	100%
MAPFRE MSV Life plc	50%
Church Wharf Properties Limited	50%

** Held indirectly through BEE Insurance Management Ltd*