MAPFRE | MIDDLESEA

Solvency and Financial Condition Report
31st December 2016

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. Activity and results

MAPFRE Middlesea plc (hereinafter, the Company, MAPFRE Middlesea or MMS) is a composite public limited 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

MMS is a subsidiary of MAPFRE S.A and forms part of the MAPFRE GROUP, and other companies with activity in insurance, financial, real estate and service sectors.

The technical account result during 2016 was equal to €1.50 million, which with the non-technical results amounting to €0.98 million resulted in a pre-tax result of €2.48 million.

In 2016, the volume of net premiums written amounted to €49.57 million, with total management expenses representing 34.5% of the net premiums written. Net claims incurred amounted to € 28.19 million.

The net combined ratio of 101.57% mainly resulted from the deterioration in the loss ratio of the motor line of business, with lower favorable run-offs attained compared to previous year.

Total net income from investments during the year amounted to €4.81 million, of which total investment expenses were €0.19 million.

B. Governance system

MMS's governance structure is composed of the following governing bodies:

- General Meeting of Shareholders
- Board of Directors
- Management Committee
- Audit Committee
- Investment Committee
- Remuneration Committee
- Risk and Compliance Committee

These governing bodies ensure the appropriate strategic commercial and operational management enabling MMS to respond to any issues which might arise throughout its different organizational levels, business and corporate environment in a timely and sufficient manner.

MMS's Board of Directors established its Risk Management Policy which encompasses policies and strategies in line with those defined by the MAPFRE, S.A. Board of Directors.

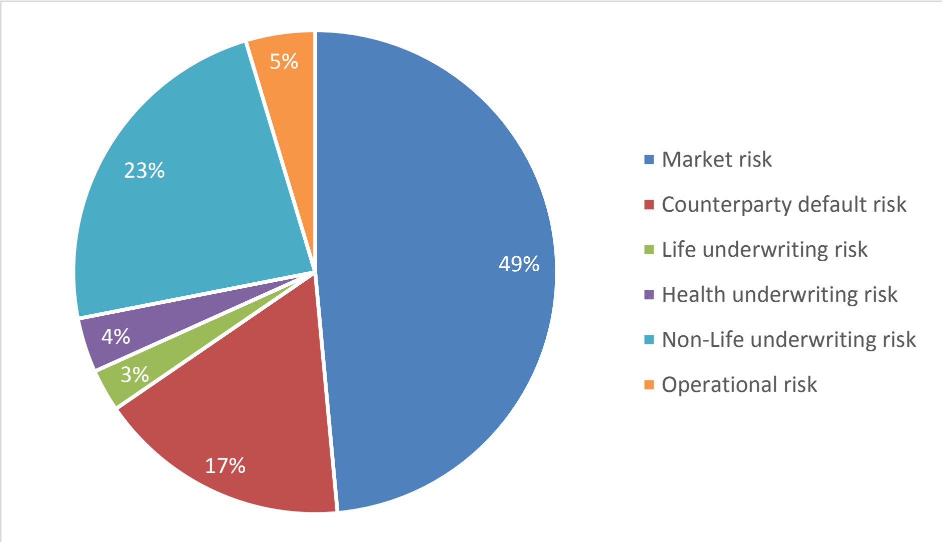
In this regard, MMS has adopted the “three lines of defense” model.

Within this framework, MMS’s structure is comprised of areas which, perform a number of independent supervisory activities aimed at assessing the risk assumed by the first line of defense.

C. Risk profile

After the entry into force of the Solvency II regulations, MMS calculates its 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:



MMS’s risk profile mainly comprises of Market Risk, due to MMS’s strategic investment in MAPFRE MSV Life plc. This risk is followed by Non-Life Underwriting Risk and Counterparty Default Risk.

MMS ensures a high degree of diversification with respect to its underwriting risk as it operates in a number of different lines of business, with a solid market presence. Similarly, its Investment Plan has limits which guarantee sufficient diversification by issuer, country, and activity sector for its market risk.

Apart from the above risks, MMS conducts internal risk-identification procedures to determine the risks which represent a threat to complying with the strategic plan or which might continuously impede the attainment of MMS’s capitilisation levels considered appropriate to its risk profile. As a result of the mitigation measures in place, no other significant risks were identified which would materially affect MMS’s solvency.

MMS also considered a number of stress tests and scenarios to assess its resilience and strength of its business model when facing adverse events during the projected period. The results from these analyses indicate that the MMS will continue to have eligible own funds to comply with the SCR even in stressed scenarios.

D. Valuation for solvency purposes

The Solvency II value of assets amounts to €168.70 million, while the Accounting value (IFRS value) is equal to €145.71 million. The differences between the Solvency II value and the IFRS value 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 €73.03 million, while the IFRS value is equal to €83.61 million. The main difference between Solvency II value and the IFRS value arose due to 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).

The excess of assets over liabilities for Solvency II purposes amounted to €95.67 million, which represented an increase of 54% over the IFRS value of equity.

E. Capital management

MMS has the appropriate structure necessary to manage and oversee its own funds, policies and management plans in place so as to maintain solvency levels within the limits established by legislation and the Company's risk appetite.

MMS's Solvency Capital Requirement (SCR) amounted to €31.42 million, while the Minimum Capital Requirement (MCR) amounted to €8.75 million. The MCR is the minimum level of security below which the amount of financial resources should not fall.

Eligible own funds to cover MMS's SCR represent € 92.15 million, of which € 92.09 million were classified as unrestricted Tier 1 and € 0.06 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.

MMS's ratio of eligible own funds to cover the SCR stood at 293.3% as at end December 2016 whilst the ratio of eligible own funds to cover the MCR was equal to 1052.3%. Thus it can be concluded that MMS is in a position to be able to comfortably meet its future commitments, considering the future Solvency II capital requirements.

As part of its own risk and solvency assessment process, MMS prepared a medium-term capital plan including a projection of the own funds and of its overall solvency needs for the budgeted period. This analysis shows that the company will have a high SCR and MCR coverage during the period considered.

A. Business and performance

A.1 Business

A.1.1 Name and legal form

MAPFRE Middlesea plc is a composite public limited company with primary activities being underwriting of non-life and group life risk.

The registered address is MAPFRE Middlesea P.L.C.

Middle Sea House,

Floriana, Malta

MAPFRE Middlesea underwrites risks which are solely and exclusively situated in the Maltese territory. Legacy business which originated from MMS's previous branches outside the Maltese territory initiatives is in run off. MMS is a subsidiary of MAPFRE S.A, situated at Carretera de Pozuelo-Majadahonda s/n 28222 Majadahonda, Spain forming part of the MAPFRE GROUP, and other companies with activity in insurance, financial, real estate and service sectors.

The ultimate parent is MAPFRE FUNDACIÓN, a non-profit Entity located in Madrid at Paseo de Recoletos # 23.

MAPFRE Middlesea plc is also the parent company of a number of subsidiaries with main activities being insurance, insurance management services, and finance activities. Section A.1.3 provides a breakdown of MMS subsidiaries.

Supervision of the Entity

The Malta Financial Services Authority is the body responsible for the financial supervision of MAPFRE Middlesea as it is based in Malta. The Malta Financial Services Authority is located at Notabile Road, Attard, Malta, with the following website http://www.mfsa.com.mt.

EXTERNAL AUDITORS:

On 8th March 2017, KPMG Malta issued an unqualified opinion in its audit report on MMS's financial statements as at 31st December 2016. KPMG Malta is formed as a Civil Partnership with registered address: KPMG, Portico Building Marina Street, Pieta', Malta.

Holders of qualifying holdings

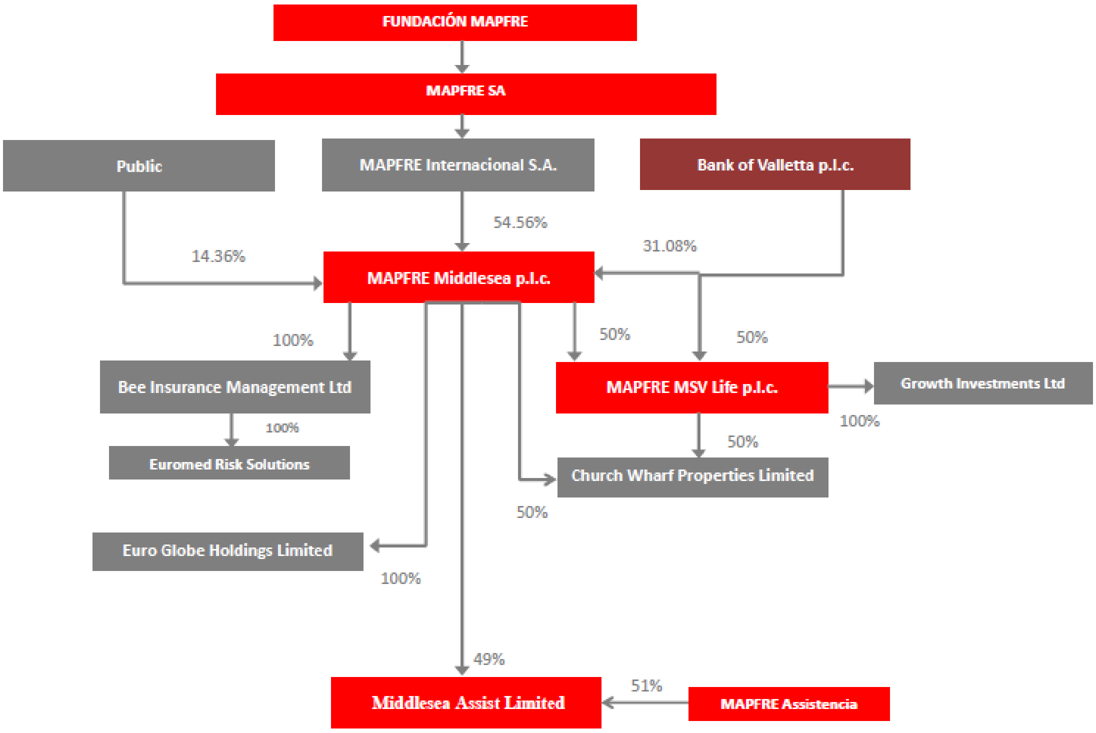
The following table reflects the holders of qualifying holdings which hold qualified investments in the company.

Name	Legal status	Location	Percentage of ownership
MAPFRE Internacional	Limited Liability	Spain	54.56%
Bank of Valletta	Limited Liability	Malta	31.08%

Mr Joseph F.X.Zarha has direct interest of below 1% in the company's share capital. Mr Paul Testaferrata Moroni Viani has an indirect shareholding in the company's shares through his shareholding in other companies.

MMS Position within the Group's legal structure

The following is the organizational structure indicating the company's position within the Group's legal structure:



Lines of business

Though a composite insurer, MAPFRE Middlesea is primarily a general insurer and 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

Geographic areas

MMS does not write any new business outside the Maltese territory. Previous business which was underwritten by the company's branches outside the Maltese territory is in runoff.

A.1.2 Business and/or events that have occurred over the reporting period that have had a material impact on the undertaking

During 2016 MAPFRE Middlesea continued to consolidate its position as the local market leader in the non-life insurance sector.

In 2016, the coming into force of Solvency II represented a very significant and important change in the regulatory landscape. To this effect, it is to be noted that MAPFRE Middlesea's solvency ratio shows that it has the necessary capital resources to execute its long term strategy and a good level of resiliency under challenging business scenarios.

The net combined ratio of 101.57% mainly resulted from the deterioration in the loss ratio of the motor line of business, with lower favorable run-offs attained compared to previous year.

Furthermore, in 2016, MMS made a number of changes at the corporate level with the appointment of new Senior Officers and the establishing of new functions to better align itself with the GROUP structure and to further strengthen the governance aspect.

A.1.3 Information about the subsidiaries

As indicated in section A.1.1. of this report, the below list reflects the companies which belong to MMS, in which a direct or indirect investment is held, to include their legal status, activity, and ownership interest at year-end 2016.

Subsidiary Undertakings

Name of Company	Percentage of Shares
Euro Globe Holdings Limited	100%
Euromed Risk Solutions*	100%
Bee Insurance Management Limited	100%
MAPFRE MSV Life plc	50%
Church Wharf Properties Limited	50%
Middlesea Assist Ltd	49%
*Held indirectly through Bee Insurance Management	

A.2 Underwriting performance

Below is the quantitative information regarding the activity and underwriting results for the year 2016 by line of business:

S.05.01.02.01- Non life insurance and reinsurance obligations (direct business and accepted proportional reinsurance).

	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted 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	
Premiums written										
Gross - Direct Business	8,128	932	13,644	16,735	1,908	10,829	3,657	2,005	62	57,899
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-
Gross - Non-proportional reinsurance accepted										-
Reinsurers' share	27	-	534	655	168	8,524	317	2	27	10,255
Net	8,102	932	13,109	16,080	1,740	2,305	3,340	2,003	34	47,644

	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted 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	
Premiums earned										
Gross - Direct Business	7,919	962	12,182	14,942	1,772	9,974	3,519	1,728	51	53,049
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-
Gross - Non-proportional reinsurance accepted										
Reinsurers' share	27	24	488	599	196	7,883	512	2	23	9,754
Net	7,893	938	11,693	14,343	1,576	2,090	3,007	1,726	27	43,295
Claims incurred										
Gross - Direct Business	4,309	272	11,594	7,918	1,440	4,190	559	889	-	31,171
Gross - Proportional reinsurance accepted	-	-	7	-	22	-	-	-	-	30

	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted 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	
Gross - Non-proportional reinsurance accepted										
Reinsurers' share	173	(14)	(33)	66	559	3,268	(11)	13	-	4,021
Net	4,136	286	11,634	7,852	904	922	570	876	-	27,179
Changes in other technical provisions										
Gross - Direct Business	-	-	-	-	-	-	-	-	-	-
Gross - Proportional reinsurance accepted	-	-	-	-	-	-	-	-	-	-
Gross - Non-proportional reinsurance accepted										-
Reinsurers' share	-	-	-	-	-	-	-	-	-	-

	Line of Business for: non-life insurance and reinsurance obligations (direct business and accepted 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	
Net	-	-	-	-	-	-	-	-	-	-
Expenses incurred	2,663	376	4,081	5,371	579	1,052	1,048	862	42	16,795
Other expenses										-
Total expenses										16,795

S05.01.02.02- Life Insurance Obligations

	Line of Business for: **life insurance obligations**			
	Other life insurance	Annuities stemming from non-life insurance contracts and relating to health insurance obligations	Annuities stemming from non-life insurance contracts and relating to insurance obligations other than health insurance obligations	**Total**
Premiums written				
Gross	2,110	-	-	2,110
Reinsurers' share	181	-	-	181
Net	1,930	-	-	1,930
Premiums earned				
Gross	2,110	-	-	2,110
Reinsurers' share	181	-	-	181
Net	1,930	-	-	1,930
Claims incurred				
Gross	1,668	-	-	1,668
Reinsurers' share	659	-	-	659
Net	1,008	-	-	1,008
Changes in other technical provisions				
Gross	337	-	-	337
Reinsurers' share	(241)	-	-	(241)
Net	578	-	-	578
Expenses incurred	294	-	-	334
Other expenses				-
Total expenses				334

MAPFRE Middlesea closed the year with written premiums totaling €60.1 million. Net profits amounted to €2.6 million, while the combined ratio of premiums charged is 101.6%.

A.3 Investment performance

A.3.1 Information on income and expenses arising from investments by asset class:

The following table reflects quantitative disclosures regarding income from real estate investments, the portfolio to maturity, available for sale portfolio, portfolio held for sale, and realized/unrealized net gains, in thousands of euros.

Total income from investments 2016	Income from investments
Items	
INCOME FROM INTEREST, DIVIDENDS, AND OTHER	
Real estate investments	
Rent	399
Other	-
Income from held-to-maturity investments	
Fixed-income securities	-
Other investments	-
Income from available-for-sale securities	**266**
Income from the fair value through profit or loss portfolio	**283**
Dividend income from Group undertakings	**2,672**
Other finance income	**1**
TOTAL REVENUE	**3,621**
REALIZED AND UNREALIZED GAINS	
Net realized gains	
Real estate investments	-
Held-to-maturity investments	-
Available-for-sale financial investments	-
Trading portfolio financial investments	(24)
Other	-
Net unrealized gains	
Increase in fair value through profit or loss portfolio	1,394
Other	-
TOTAL GAINS	**1,370**

Total income from investments 2016	Income from investments
TOTAL INCOME FROM INVESTMENTS	**4,991**

Figures in thousands of euros

The following table reflects qualitative disclosures regarding expenses generated by real estate investments, the portfolio to maturity, available for sale portfolio, portfolio held for sale, and realized/unrealized net gains, in thousands of euros.

Investment expenses 2016	Investment expenses
Items	
FINANCIAL EXPENSES	
Real estate investments	
Net operating expenses	34
Other expenses	-
Expenses from held-to-maturity investments	
Fixed-income securities	-
Other investments	-
Expenses from available-for-sale portfolio	**9**
Expenses from trading portfolio	**-**
Other finance expense	**59**
TOTAL EXPENSES	**102**
REALIZED AND UNREALIZED LOSSES	
Net realized losses	
Real estate investments	-
Held-to-maturity investments	-
Available-for-sale financial investments	-
Trading portfolio financial investments	-
Other	-
Net unrealized losses	
Decrease in the fair value of the trading portfolio and loss	-

Investment expenses 2016	Investment expenses
from derivatives	
Impairment charges on available for sale portfolio	84
TOTAL LOSSES	**84**
TOTAL EXPENSES ARISING FROM INVESTMENTS	**186**
NET INCOME	**4,805**

Figures in thousands of euros

Total income from investments during the year amounted to €5 million**.** Items contributing the most to revenue were dividends from group undertakings at €2.67 million all allocated to equity. Real estate investments both from income and fair vale gains also have a great weight in total revenue.

Total expenses arising from investments during the year amounted to €0.19 million. This was mainly due to an impairment on available for sale investments.

A.3.2 Information about any gains and losses recognized directly in 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 in thousands of euros during 2016:

Investments	Income recognized in equity	Losses recognized in equity	Net difference
I. Real estate investments	-	-	-
II. Financial investments	125	-	125
1. Held-to-maturity portfolio	-		
Fixed-income securities	-	-	-
Other investments	-	-	-
2. Available-for-sale portfolio			
Shares	83	-	83
Fixed-income securities	42	-	42
Mutual funds	-	-	-
Other	-	-	-
III.- Investment in associates accounted for by the equity method	-	-	-
IV.- Accepted reinsurance deposits	-	-	-
V. Other investments	-	-	-
Overall performance	125	-	125

Figures in thousands of euros

Available for sale investments registered a positive contribution to equity of €0.13 million. An impairment of €0.08 million was recognized in the profit or loss account which loss cannot be transferred back to Equity.

A.3.3 Information about assets securitisation

MMS does not have any securatisation investments.

A.4 Performance of other activities

A.4.1 Other income and expenses

During this year, the company incurred the following "other" income and expenses other than those arising from the underwriting activity and from the return on investment, including:

	2016
Other income	-
Other expenses	1,655

Figures in thousands of euros

Expenses

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

A.4.2 Lease contracts

Financial leases

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

Operational leases

Leases where the lessor substantially retains substantially the risks and rewards incidental to ownership are classified as operating leases.

MMS leased the following items through operating lease agreements (data at 31st December 2016):

Type of asset	Net book value	Maximum duration of contracts (years)	Maximum years elapsed
Property investment	13,717	33	9
Others	-	-	-

Figures in thousands of euros

MMS leases real estate, mainly offices. These leases have an average life of 13 years ranging from 3 years to 33 years. Contracts have renewal and termination options with fixed notification periods.

B. System of Governance

B.1 General information on the system of governance

MAPFRE Middlesea's governing bodies ensure that the company's strategic, commercial and operational management enable it to respond to any issues which might arise throughout its different organizational levels, business and corporate environment in a timely and appropriate manner.

B.1.1 MAPFRE Middlesea's System of Governance

The following outlines the main functions and responsibilities of MAPFRE Middlesea's Governing Bodies:

- **General Meeting of Shareholders**: Is the highest governing body, in that its decisions are applicable to all shareholders. Both ordinary and extraordinary General Shareholders' Meetings are called by the Board of Directors.

- **Board of Directors**: Is the body in charge of managing, administering, and representing the company. It is the top most decision making and supervisory organ. It establishes the roles of the Management Committee and its Delegated Committees, designating its members, where necessary.

- **Management Committee:** This is the governing body delegated by the Board of Directors to coordinate and supervise the company's top-level actions, covering operational and management aspects, as well as making the necessary decisions to ensure its appropriate functioning, using the powers delegated at any given time.

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

- **Investment Committee:** The role of the Investment committee is to advise the Board of Directors on Investment Management policies to be adopted by the company so as to secure the safety, 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 in ensuring 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 the Company's Mission statement. This committee is also responsible for the compliance with the provisions of the Code of Principles of Good Corporate Governance as set out in the listing rules. Further to this, it is also under the committee responsibility to reward executives having regard to the performance of the company and the general pay environment.

- **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, measurement monitoring and management of risk, compliance, prevention of money laundering and other aspects associated with its business.

MAPFRE Middlesea has a management model centered on rigorous control and supervision at all levels. It ensures widespread delegation, execution and performance of the tasks assigned to the teams, as well as their heads, fostering the deep analysis by the management teams at all levels related to the decision-making process, prior and after their execution.

Apart from the abovementioned administration and supervisory bodies, being part of the MAPFRE Group, the company is supervised by the Regional Management Committee, which directly supervises the management of the company, strengthening all the global and regional corporate projects.

B.1.2 Key functions

During 2016, the Board of Directors approved the Actuarial, Compliance, Risk Management, and Internal Audit policies. These policies ensure the operational independence of the key functions and direct access to the governing body. The names of the parties responsible for the key functions were communicated to the Malta Financial Services Authority.

More information may be found on Basic Functions in Sections B.3, B.4, B.5, and B.6.

B.1.3 Relevant General Meeting of Shareholders and Board of Directors agreements

During 2016, there were no significant changes to MMS's governance structure except for the change of one of the Board Directors, who was not reappointed.

B.1.4 Balances and remuneration to the members of the administrative, management or supervisory body

Remuneration paid to the MMS management and employees is determined in accordance with prevailing regulations as well as its remuneration policy, approved by the Board on 20th April 2016**.**

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 which exceed MMS's tolerance level and avoids conflicts of interest. Its main principles are as follows:

- Based on each job/function, it includes measures designed to avoid any conflicts of interest which might arise.
- Consider merit, technical know-how, professional knowledge, and performance.
- Ensure equality, without discrimination based on criteria related to gender, race, or ideology.
- Transparency, as they are shared.
- Flexibility in structure, adaptable to the different market groups and circumstances.
- Aligned with strategy as well as its risk profiles, objectives, risk-management practices, and long-term interests.
- Market competitiveness.

Based on the aforementioned policy, personnel remuneration is comprised of five items:

a) Fixed remuneration: established in all cases in accordance with the position and professional profile, paid in previously agreed-upon installments.

b) Variable compensation/incentives: remuneration the exact amount of which may not be known in advance: it may be annual (short-term), or pluri-annual (medium- and long-term). The weight of variable compensation is determined by rank in the organization, as well as evaluations; it increases in line with the hierarchical level.

c) Recognition programs: Devoted to formally recognize employee contributions to implementing strategies, while also awarding quality contributions, the dissemination of MAPFRE corporate culture, and innovation.

d) Social benefits: Products, services, or assistance which MMS offers its employees, based on collective agreements or individual arrangements with employees.

e) Salary complements: Economic assistance granted to employees based on the position held (i.e., corporate vehicle, housing, etc.).

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 on 20th October 2016, and it establishes the applicable Relevant Personnel[1] and Outsourced Personnel [2] requirements, as follows:

Relevant Personnel, and Outsourced Personnel, where applicable, should have the appropriate qualifications, know-how, and expertise to ensure that MMS is professionally managed and supervised.

The expertise and experience of Relevant Personnel will include academically-acquired knowledge and the experience necessary to carry out 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) Governance systems
d) Financial and actuarial analysis
e) Regulatory framework

Individually: training and experience appropriate to the professional profile, specifically in the insurance and financial services area, with practical experience obtained 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.

To this effect, Relevant Personnel (and Outsourced Personnel, where applicable) must meet the following requirements:

1) Personal, professional, and commercial ethics including:

a) A personal career reflecting the highest respect for company and other laws governing economic activity and business operations, as well as good sales, financial, and insurance practice.
b) No criminal records related to crimes against heritage, money laundering, against the social/economic order and against the tax authorities and social security, and fines related to offences related to infringement against the insurance industry, securities market or consumer protection.
c) Based on research a lack of relevant and solid results in both the criminal and administrative areas on some of the matters mentioned in above section b).
d) They must not be prevented from exercising representation in public or management positions in insurance or financial entities.
e) They must not be disqualified based on the prevailing regulations.

[1] Relevant personnel: The Directors and Officers, Senior Executives (all those persons in senior management positions who directly report to their administrative body, execute committees or managing directors) and Key Function Holders, as well as all other persons who are required to meet the fit and proper requirements at every moment in accordance with applicable laws.

[2] Outsourced personnel: should any of the key functions be outsourced, parties employed by the services provider to this end.

2. Capacity and compatibility:

a) No involvement in legal incompatibility, incapacity, or prohibition proceedings as regards prevailing legislation and internal regulations.
b) Not be involved in an unavoidable situation of conflict of interest pursuant to the provisions of the prevailing legislation and internal regulations.
c) Not have significant shareholdings or provide services to competing entities or any other GROUP entities, or perform tasks related to the role of employee, executive, or administrator, unless prior authorization has been granted by the Board of Directors, and in competent government bodies of the company in question, in the case of subsidiaries.
d) Not involved in circumstances which may cause his or her membership on MMS's Board to place the company's interests at risk.

MMS designation procedures

Parties proposed for executing Relevant Personnel roles requiring notification to Supervisory Authorities or, where applicable, those of Outsourced Personnel, must provide prior, truthful, and complete declaration regarding their personal, family, professional, or business endeavors, especially indicating the following:

a) Individuals or entities which are considered related parties, based on prevailing legislation.
b) Any circumstances which might represent lack of compatibility with MMS legislation and bylaws, as well as internal regulations and codes of good governance, or any situations representing conflict of interest.
c) Any other professional obligations, in case they might detract from the necessary dedication to the post.
d) Criminal proceedings in which the party is accused or processed.
e) Any other matters or situations which may affect performance.

The above declaration must be presented on the company's models established for this purpose.

The above mentioned parties must ensure that their declarations are continually updated, and must communicate any relevant changes in their situations, and participate in periodic updates when required to do so by the company's governing body, including the reevaluation of any competence and honorability requirements.

B.3 Risk-management system, including Own Risk and Solvency Assessment

B.3.1 Governance framework

The Board of Directors of MAPFRE Middlesea approved the Risk Management Policy which encompasses policies and strategies in line with those defined by MAPFRE GROUP, and specifically approves its risk management and control mechanisms and supervises its internal information and control systems.

As mentioned previously, the Board of Directors delegates management and permanent supervision of the company's daily strategic and operational aspects to the Management Committee, granting it the power to make any decisions considered necessary for the day to day running of the business.

Complementary to this individual company structure, the Group's Corporate Risk Area handles all significant risk management aspects related to different legal entities, establishing policies to be implemented by the Governing bodies in each individual company, allowing for any necessary local adaptations.

The Risk and Compliance Committee provides support and advice to the Board of Directors in defining and evaluating the risk management policy and in determining the risk tolerance and strategies, as well as the appropriate supervision of the application of internal/external good governance within the company.

The Audit committee is responsible for overseeing the efficiency of MMS's Internal Control System and Risk Management System.

The Investment Committee is responsible for reviewing and approving investment strategies on a periodic basis ensuring that assets are managed efficiently and within approved risk mandates.

The Remuneration Committee is responsible for recommending the remuneration policy for the non-executive directors and senior management, outlining the appropriate packages of their remuneration and monitoring the level and structure of the remuneration on the basis of adequate information provided by management.

MAPFRE Middlesea has adopted the three lines of defense model. This model encompasses:

a) As the first line of defense, operational managers own and manage risks.

b) The internal control system and the areas in the second line of defense contribute to the independent supervision of risk management activities within the framework of the policies and risk limits established by the Board of Directors.

c) Internal Audit is the third line of defense, and independently guarantees the appropriateness and efficacy of the Internal Control system as well as other elements of the Corporate Governance System.

Within this framework, MMS's structure is comprised of functions which, in their respective frameworks, perform a number of independent supervisory activities within the scope of their respective functions with regard to assumed risks.

The functions defined by MMS are:

- Actuarial function: prepares mathematical, actuarial, statistical, and financial calculations enabling it to determine prices and technical provisions. In close collaboration with the Risk Function, it also performs underwriting risk modeling, based on the calculation of the capital requirements of insurance companies, which contributes to achieving targeted technical results and the MMS's desired solvency levels.

- Compliance Function: identifies, evaluates, monitors, and informs regarding any risk exposure involved in the day to day running or the company

- Internal Control Function: ensures that the established Internal Control System performs seamlessly in the Company's environment, and that predetermined procedures are complied with.

- Risk Management Function which is responsible for:
  - Supervision and control of the effectiveness of the Risk Management System in accordance with the policies established by the Board of Directors.
  - Risk identification and measurement.
  - Solvency calculations.
  - Monitoring and notification of risk exposure.

- Internal Audit Function, which provides an independent assessment of:
  - The sufficiency, adequacy, and efficiency of the Internal Control System.
  - The Risk Management System
  - The appropriateness and performance of the Governance Areas included in the Governance System outlined in Solvency II Directives.

B.3.2 Risk management objectives, policies, and processes

The Risk Management System has the following main objectives:

- Promote a solid and efficient risk management culture and system.
- Ensure that all decision-making processes include the analysis of potential risks.
- Preserve MMS financial health and solvency, contributing to the MAPFRE GROUP'S positioning as a trustworthy global insurance company.

The strategies, objectives, and reporting procedures for the key risks to which MMS is exposed, reflected in the Risk Appetite approved by the Board of Directors establishes the degree of risk which MMS is prepared to assume to reach its business objectives with no material deviations, even when facing adverse situations. This policy is reviewed on an annual basis by the Board of Directors in order to assess the effectiveness and sufficiency of the limits established.

Based on the risk management organizational structure, the first line of defense must mitigate the risks to which MMS is exposed. These actions are performed in accordance with the risk limits and policies established to that effect. The Risk function in collaboration with the Actuarial function is in charge of monitoring and measuring the capital required by each risk mitigation alternative.

The Board of Directors receives regular information on credit risk, as well as annual information on complying with limits set by the Risk Appetite.

The Board of Directors must be immediately informed about any risks which:

- Based on evaluations performed, exceed the established risk limits;
- May lead to losses equal to or higher than the established risk limits; or
- Might endanger compliance with solvency requirements or MMS business continuity.

Once the existence of a risk exceeding established limits has been reported, the Board of Directors may take the following actions:

- Authorize the acceptance of the risk exceeding the established limits.
- Cancel the risk, in the most opportune and convenient way possible.
- Contract protection which keeps risk within established limits; in this case, the consequences arising from lack of compliance by the third party providing this protection as well as operational risks should be taken into account.
- Obtain additional capital resources making it possible to assume a higher level of risk.

The ORSA reviews monitor and notify material risks which MMS might face. Section B.3.3 of this report details risk and solvency Own Assessment information.

Herewith follows a breakdown of risk identification, measurement, management, monitoring, and reporting:

Type of Risk	Description	Measurement and management	Monitoring and notification
Underwriting risk	Group Life and Reinsurance risks: - Premium risk - Reserves risk - Catastrophe risk - Reinsurance Mitigation	Standard Formula	Annual
Market risk	Covers the following risks: - Interest rate - Shares - Real estate - Spread - Concentration - Currency	Standard Formula	Annual
Credit risk	Reflects any possible losses arising from unexpected infringement by counterparties and debtors during the following 12months.	Standard Formula	Annual
Operational risk	Includes those which arise due to failed internal processes, people and systems, or from external events.	Standard Formula MMS performs dynamic qualitative processes assessments (RiskM@p). Operational Risk events register and monitoring system	Annual Biennial Continuous

Type of Risk	Description	Measurement and management	Monitoring and notification
Liquidity risk	The risk MMS might not be able to realize its investments and other assets in order to meet its financial commitment deadlines.	Liquidity position Liquidity indicators	Continuous
Safety and environmental risks	Comprise Operational Risk, although this category only includes safety and environmental risk.	Identify, mitigate, and evaluate impact	Quarterly, included in Operational Risk and event Log
Compliance risk	The risk of losses due to legal/regulatory sanctions or reputational losses arising from the infringement of internal/external laws and regulations, as well as applicable administration regulations.	MMS monitors, assesses, and informs the Governing bodies on exposure to risk arising from activities performed. Monitoring and register of significant events.	Continuous Annual
Strategic and Corporate Governance Risks	Includes the following risks: - Business ethics and corporate governance - Organizational structure - Alliances, mergers & acquisitions - Market competition	Through the MAPFRE Group's corporate policies aligned with the Institutional, Business, and Organizational Principles for listed entities.	Continuous

All calculations relating to the standard formula calculation must be updated when a material change in the risk profile is detected.

Generally, as mentioned previously, the Board of Directors must be periodically informed of the risks to which MMS is exposed.

B.3.3 Own Risk and Solvency Assessment (ORSA)

MAPFRE Middlesea's Board of Directors has ultimate responsibility for the risk management framework. As part of this framework, the Board of Directors approved the Own Risk & Solvency Assessment policy on the 10th December 2015

As indicated in this Policy, the ORSA process is integrated and forms part of the Risk Management System, encompassing processes and procedures designed to identify, measure, manage, and report on any short- or long-term risks identified in MMS throughout the period reflected in the strategic plan, as well as the sufficiency of capital resources with regard to its own assessment of solvency needs. Based on this goal, it considers all the significant and potential sources of risk facing MMS, and outlines steps and initiatives designed to manage and mitigate them.

The Risk function coordinates the ORSA preparation, preparing a draft report for submission for approval to the Board of Directors, who must channel the various contributions from the Areas/Departments involved in the process.

The ORSA report is prepared annually, unless certain material events justify the preparation of additional reports during the year (extraordinary ORSA). The approval process is the same.

The ORSA process covers the following stages**:**

1. Identification of risks

The risk identification process is key for the ORSA to achieve its objectives, i.e. in order to prevent and avoid any potential future solvency issues.

The Risk Function assesses MMS's risk profile, considering the Risk Appetite and tolerance limits approved by the Board of Directors. The purpose of this analysis is to identify any (qualitative and quantitative) risks which might be faced during the period covered in the strategic plan, and which might significantly affect company's performance, or regulatory capital.

To identify risks, the Risk function requests opinions of the relevant parties as defined in the Risk Management Policy through which according to their best of knowledge and experience would be able to provide information and relevant opinions.

2. Risk measurement

The ORSA reflects the own assessment of MMS solvency needs with regard to its risk profile, strategic plan, and tolerance limits set forth in its Risk Appetite.

The assessment also covers the following:

- Continuous compliance with capital and technical provision requirements.
- The degree to which MMS's risk profile diverges from the assumptions supporting Solvency Capital Requirements (SCR) where required by prevailing legislation.

To ensure quality data standards throughout the process, information used in the ORSA must be documented, reliable, and coherent in accordance with its purpose. The ORSA is prepared based on realistic assumptions, and aligned with the strategic plan.

Projections reflect MMS's risks and the financial implications of its business plan so that the ORSA is based on an appropriate assessment of the future business profile. The Actuarial function participates throughout the process, verifying that technical provision calculations and projections are correct.

Stress tests on material risks identified during the process based on MMS's risk profile are also considered.

3. Report preparation

The Risk Function prepares the ORSA report.

4. Documentation

The Risk Function maintains the documentation relating to the process.

B.4 Internal control system

B.4.1 Internal control

Since July of 2008, MAPFRE has had a written set of Internal Control policies approved by the MAPFRE S.A. Board of Directors, which sets forth the most relevant activities to be carried out so that the Internal Control System is maintained to optimal standards. Its most recent update was approved by the MAPFRE S.A. Board of Directors on 17th December 2015. MMS Board of Directors has also approved the Internal Control Policy, with its most recent update being approved on the 22nd April 2016

The implementation of the Internal Control System is based on the application of COSO standards; in this regard, there is a direct relationship between MMS's desired objectives and the internal control system components (and organizational structure).

Based on the above, the establishment of goals and plans to meet them is an internal control prerequisite, since goals must first be defined so that Management may identify and evaluate any potential events affecting their achievement.

MAPFRE Middlesea's activities are complemented by the MAPFRE Corporate Areas, integrated by a flexible structure of Areas managing shared services, providing support, supervision, and coordination in aspects falling under common policies.

Due to its very nature, Internal Control involves all personnel, regardless of their role in the organization; overall, they contribute to providing a reasonable assurance that established objectives will be reached.

The following responsibilities and functions have been established so that the Internal Control System may efficiently meet established objectives:

- Within MMS, the Board of Directors is ultimately responsible for overseeing the Internal Control System, to ensure it functions correctly.

- Key management, as the company's executive arm, with the supervision by the governing bodies, is responsible for designing and ensuring that the Internal Control System components function adequately.

- In line with the policies and procedures established by the Board of Directors and Key management, the company's management and governance structures consider the potential changes to the environment and the business model which might affect its ability to meet its goals, with the necessary internal controls established in this regard.

- MMS Internal Control System's correct functioning is the responsibility of all organization personnel.

- Internal Audit supervises the suitability and effectiveness of the Internal Control System and other governance aspects, and evaluates the appropriateness, sufficiency, and effectiveness of the Internal Control System.

- MAPFRE Group's Internal Control area fosters a common internal control framework, coordinating a continuous evaluation on MAPFRE Middlesea's Internal Control System set-up and functionality. Furthermore, in conjunction with MMS area responsible for Internal Control, they oversee its correct implementation in their areas.

MAPFRE Middlesea's Internal Control System involves tasks and actions present in all the organization's areas, and as such, are fully integrated in its organizational structure.

B.4.2 Compliance function

MAPFRE Middlesea's Compliance Function is based on the relevant regulatory requirements, as well as the principle of proportionality related to the company's business size and the nature/complexity of the risks taken.

The Compliance Function policy outlines the responsibilities, information processes and procedure necessary for the identification, measurement, monitoring, management and notification of non-compliance risks. The policy review takes place annually although it is subject to modification at any given time by the Board of Directors, with the current policy in force being approved by the Board of Directors on the 21st July 2016.

B.5 Internal audit function

As discussed in the Risk Management System section, Internal Audit is the Risk Management Model's third line of defense, designed to provide an independent assurance of the appropriateness and effectiveness of the Internal Control System as well as other elements of the Governance System.

In the structure of the MAPFRE Group, the Internal Audit Department reports to the MAPFRE Middlesea Board of Directors through its Audit Committee (Board Delegated Body) and its chairman. The Chief Internal Audit Officer reports to the Audit Committee. This makes it possible for the company's internal audit function to maintain its independence and objectivity with regard to the activities overseen.

The Internal Audit Charter was updated and approved by the Board of Directors on the 22nd April 2016 and outlines the mission, functions, attributes, and obligations of MMS internal Audit Function, defining its structure, and outlining its framework of relationships between the Internal Audit Department and the CEO, management, and corporate areas, assurance functions, and external auditors. It also includes the rights and obligations of the company's internal auditors as well as their code of ethics. Its main objectives are to spread awareness regarding the Internal Audit Function throughout MMS.

The Internal Audit Policy which was also updated and approved by the Board of Directors on the 22nd April 2016 is designed to formalize and communicate the following aspects: classification of audit engagements, recommendations and deadlines, treatment of audit reports, and any other general circumstances related to internal audit activities. Internal Audit activities are exclusively carried out by MMS's Internal Audit department.

Both documents, the charter and Policy, are reviewed at least on a yearly basis. Any changes made to the documentation must be approved by the Audit Committee and Board of Directors.

MMS's internal auditors avail themselves of the Code of Ethics which is included in the Internal Audit Charter, and defines their rules of conduct:

Integrity and honorability

Internal auditors:

- Shall perform their tasks honestly, diligently, and responsibly.
- Shall observe the law and make disclosures expected by law and the profession. Shall not knowingly be a party to any illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the company.
- Shall respect and contribute to the legitimate and ethical objectives of the organization.

Objectivity

Internal auditors:

- Shall not participate in any activity or relationship that may impair, or be presumed to impair, their unbiased assessment. This participation includes those activities or relationships that may be in conflict with the interest of the company.
- Shall refrain from undertaking any audit that may entail a conflict of interest for them.
- Shall not accept anything that may impair, or be presumed to impair, their professional judgement.
- Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

Confidentiality

Internal auditors:

- Shall ensure strict confidence in the use of information acquired in the course of their duties
- Shall not use information for any personal gain or in a manner that would be contrary to the law or detrimental to the legitimate and ethical objectives of the company.

Competencies:

Internal auditors:

- Shall have collectively the necessary knowledge, skills and experience on at least the insurance and financial markets, business strategy and business model; system of governance; financial and actuarial analysis; regulatory framework; information technology; risk management and fraud.;
- Shall have qualities for dealing with people and communication skills to convey clear and effectively the various aspects of the work
- May outsource those services that require more specific knowledge.
- All internal audit services will be performed in accordance with Internal Audit professional practice regulations.

B.6 Actuarial function

MAPFRE Middlesea's Actuarial function is outsourced to MAPFRE S.A. which is the parent company of MAPFRE Middlesea. This agreement fully respects the company's outsourcing policy as described in section B.7. Although the Actuarial Function Holder is situated in Spain, MMS has established an internal Actuarial team to act as the local reference point.

B.7 Outsourcing

MAPFRE Middlesea has outsourced its Actuarial Function to the Spanish company of the MAPFRE Group called MAPFRE S.A. This outsourced service took place within the terms set forth in the functions and/or outsourcing policies and/or insurance activities approved by the Board of Directors of MAPFRE Middlesea as well as their regulatory policies. The above outsourcing commenced on 1st January 2016, and was duly communicated to the Malta Financial Services Authority.

The existing governance structure ensures that MAPFRE Middlesea has sufficient control over critical functions and/or activities which have been outsourced, in the terms established in the Solvency II Directive and local enacting legislation.

MAPFRE Middlesea's Outsourcing Policy was approved on 21st July 2016, by the Board of Directors, and is in line with the Outsourcing Policies approved by the MAPFRE S.A. Board of Directors for the Group on 24th June 2015. The indicated outsourcing project was carried out in line with the policy.

The key principle upon which the MAPFRE Middlesea's Outsourcing Policy is based establishes that MAPFRE Middlesea retains full responsibility for meeting all obligations arising from the functions or activities susceptible to being outsourced, in much the same manner as if they were performed internally.

B.8 Any other information

MAPFRE Middlesea’s governance system reflects the requirements established in the Solvency II Directive on managing inherent risks.

Its structure is based on the related regulatory requirements, as well as the principle of proportionality related to its business size and the nature, scale and complexity of the risks assumed.

C. Risk profile

After the entry into force of the Solvency II regulations, MMS calculates its Solvency Capital Requirement (SCR) using the standard formula. For the main risk categories, the standard formula is considered an appropriate risk measurement tool for determining the company's risk exposure, as it recognises the capital charge corresponding to the key risks (such as underwriting, market, and counterparty risk). As explained further on, the company's exposure to other risks which are not considered in the standard formula (such as liquidity risk) is not considered significant, as MMS manages and mitigates such risks effectively.

As indicated in Solvency II regulations, the SCR corresponds to the insurance undertaking's equity for limiting the probability of bankruptcy to one case per 200 or that the insurance undertaking is 99.5% able to meet its commitments to insurance beneficiaries and policyholders during the following year.

Table S.25.01.21 in Section E of this report reflects MMS's risk profile, which mainly comprises of Market Risk, due to MMS's strategic investment in MAPFRE MSV Life plc. This risk is followed by Non-Life Underwriting Risk and Counterparty Default risk.

This Section provides detail on the breakdown of the capital requirement under Solvency II by risk module and risk sub-module. It also includes a description of the reduction and mitigation techniques used by MMS to minimise its risks.

C.1 Underwriting risk

Underwriting Risk is the risk arising from insurance obligations in relation to the perils covered and the processes used in the conduct of business.

Underwriting Risk is included under the SCR Standard Formula calculation. The SCR Underwriting Risk represents 51.4% of the total SCR (diversified).

MMS minimises underwriting risk through the implementation of the following measures:

- Establishing policies, limits, and exclusions in underwriting risk:
  MMS establishes authorisation and exclusion limits for reducing undesired Underwriting Risk in its manual and/or policies.

- Setting a sufficient premium:
  MMS gives importance to premium sufficiency, which is supported by specifically-designed IT applications.

  MMS's Underwriting Policy includes reference to:

  a) The type and characteristics of the insurance activity, such as insurance risk type, MMS is prepared to accept.

  b) The consideration of reinsurance and other risk mitigation techniques within the process of designing a new insurance product and when calculating the premium.

  c) Internal underwriting limits for different products or classes of products.

  d) Maximum acceptable exposure to specific risk concentrations.

- Sufficient reserves or technical provisions:

  Claims handling and the sufficiency of technical provisions are basic principles of insurance company management. Technical provisions are calculated by the MMS's Actuarial function and their establishment is regulated by specific policies.

- Using reinsurance as a risk-mitigating technique and having a Reinsurance Policy in place

  At 31st December 2016, MMS ceded 18.0% of its earned premiums and 16.1% of its technical provisions.

  The Technical Underwriting Department of MMS is 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, 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 assignment contracts.

  Annually, MMS's Actuarial Function reviews reinsurance contracts in force, and determines the adequacy of contracted coverage.

C.2 Market Risk

Market Risk is the risk arising from the level or volatility of market prices of financial instruments which have an impact upon the value of the assets and liabilities of the undertaking. It reflects the mismatch between assets and liabilities in particular with respect to the duration thereof.

MMS's investment strategy is based on a prudent investment approach, and the portfolio is mainly characterised[3] by fixed-income securities with investment grade ratings which is aligned with the Investment Plan. The following is a breakdown of MMS's investments by asset category:

Investments *(After performing the look-through of the Investment Funds)*	**Investments at 31/12/2016**	**% Investments**
Real estate investments	**13,713**	**10.3%**
Financial investments	**119,328**	**87.7%**
Strategic participations	97,003	72.9%
Fixed-income securities	17,860	13.4%
Equity securities	4,465	3.4%
Other	-	-
Accepted reinsurance deposits	-	-
Hedging derivatives	-	-
Other investments	-	-
Total	**133,041**	**100.0%**

Figures in thousands of euros

At 31st December 2016, 13% of the total investments were Fixed-income securities. Of these, 46% corresponds to Government of Malta debt exposures.

Market Risk is included under the SCR Standard Formula calculation. The SCR Market Risk represents 83.3% of the total SCR (diversified).

MMS mitigates its exposure to market risk through a prudent investment policy characterised by fixed-income securities, and the establishment of generic and specific exposure limits.

The management of the investment portfolio is considered as a 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 set forth in MMS's Investment Plan established by the Board as well as the modified duration of any liabilities.

- 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 the maximum limit of the investment portfolio, and issuer limits.

[3] Excluding strategic investments

- Interest rate risk exposure is minimised in the case of the company's liabilities which should not exceed a fixed percentage established in the annual Investment Plan for reasons related to investment management.

- 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 that the risks lie within the Investment Policy for Property Investment.

- Risk limits are set in quantitative terms, determined based on easily-observable variables.

C.3 Credit risk

Credit risk is the risk of loss due to unexpected default, or deterioration in the credit standing, of the counterparties and debtors of insurance and reinsurance undertakings over the following 12 months.

MMS's Credit Risk Management policy distinguishes between three types of exposures:

a. Exposure to banks, savings banks, credit cooperatives, financial entities, and other similar entities. Their exposure to Credit Risk is measured according to their economic value. (Financial entities)

b. Exposure to fixed income securities, derivative instruments, and other financial investments different from equities. Their exposure to Credit Risk is measured according to their economic value, once possible mitigating factors have been deducted. (Investments).

c. Exposure to insurance and reinsurance undertakings, captive companies and similar entities. Their exposure is measured by adding the book value of all the asset balances owed to MMS by such entities and, in particular, unearned premium reserves, outstanding claims and cash or current account balances, and then deducting from the figure obtained, if any, the book value of the deposits made in favour of MMS and possible mitigating factors. Additionally, the maximum loss resulting from material off-balance-sheet exposures is considered when required.

Credit Risk is included under the SCR Standard Formula calculation as spread and concentration risk under the Market risk module and as Counterparty default risk under the Counterparty default risk module.

The Counterparty Default risk module distinguishes between two types of exposure:

- Type 1 exposure which includes reinsurance contracts, derivatives, bank balances
- Type 2 exposure which includes intermediaries' receivables and policyholder debtors among others.

The Counterparty Risk SCR represents 29.0% of the total SCR (diversified).

MMS's Credit Risk Management Policy sets limits in line with the counterparty's or investment instrument's risk profile, as well as exposure limits related to the counterparty's rating. A risk exposure monitoring and notification system is also set up.

MMS's Credit Risk Management Policy is based on the application of criteria of prudence based on issuer solvency. Fixed-income investments are subject to limits by the issuer, and seek out geographic similarity between the issuers of assets and commitments.

MMS's approach to reinsurance is to cede business to reinsurers of proven financial capacity. Generally, MMS reinsures with entities with a credit rating of at least BBB, which is equivalent to a Credit quality step of 03. Business can also be ceded to other reinsurers, following an internal analysis that reflects that they have a solvency level equivalent to the aforementioned classification or provide appropriate guarantees.

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

- The principle of optimising capital consumption.
- The principle of optimising conditions.
- Counterparty solvency principle.
- The effective transferability of risk principle.
- The principle for matching risk transfer level.

C.4 Liquidity risk

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

MMS has a Liquidity Risk Management Policy and an Asset and Liability Management Policy which 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 assets to cover commitments arising from MMS's obligations towards its policyholders and creditors at maturity. The balance of cash and cash equivalents amounted to €7.19 million as at 31st December 2016, which is equivalent to 24.4% of total financial investments[4] and cash balances. The majority of fixed-income investments have investment grade ratings and are traded on organized financial markets, which provides comfort to cover any commitments arising from MMS's obligations.

MMS's 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.

[4] Excluding strategic investments

C.5 Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, personnel or systems, or from external events.

Operational Risk is included under the SCR Standard Formula calculation. The Operational Risk model reflects those not previously included in the above modules. It includes legal risks, but not those arising from making strategic decisions, or reputational risk.

The SCR Operational Risk represents 5.8% of the total SCR (diversified).

The qualitative identification and evaluation of operational risks are managed via Riskm@p, a MAPFRE group application designed to analyse the importance and likelihood of occurrence of operational risks within the company. Furthermore, Riskm@p is also used for handling control activities and also for managing the corrective measures established in order to mitigate identified risk. This Operational risk management tool is based on a dynamic analysis of the company's processes so that each department manager identifies and evaluates any potential risk affecting the business process.

C.6 Other material risks

i. Legal risk

Legal risk is defined as an event consistent with regulatory, jurisprudential or administrative changes that may adversely affect MMS.

Over the last years, the regulatory framework to which the insurance sector is subject is being extended with new regulations both at international and local level. Additionally, it must be borne in mind that MMS operates in a complex environment under an increasing regulatory pressure, not only in the insurance side but also in the technological, corporate governance or criminal corporate responsibility fields, among others.

ii. Compliance risk

Compliance risk is defined as the risk of incurring in losses as a consequence of legal and/or regulatory sanctions or loss to reputation which MMS may suffer as a result of not complying with laws and all other regulations, internal and external rules and standards or administrative requirements which should be applied to its activities.

iii. Reputational risk

Reputational risk is defined as the possibility of a decrease in the value of MMS due to its negative perception by consumers, shareholders, distributors, employees etc.

Reputational risk is created by behavior or work in the organization that is below expectations or negative experiences of key groups MMS deals with directly, but also of other groups that MMS can affect while carrying out its activity.

iv. Cyber risk

Cyber risk shall be understood as those risks that refer to security in the use of information and communication technologies (ICT), cyberspace and the transfer, processing and storage of electronic data. The manifestation of these cyber risks can compromise:

- The confidentiality, integrity and availability of the information handled by MMS, as well as that of the systems which store, process and/or transmit it.
- The continuity of MMS's business activity and the services it provides to its clients.
- In extreme cases, the fiscal security both of the facilities and of the people.

v. Business continuity

Business Continuity (BC) is defined as the capability of the organization to continue with the delivery of products or services at acceptable predefined levels following a disruptive incident.

Through the years, MMS has been taking a number of initiatives to improve its resilience should such incidents occur. These efforts have now been further consolidated under the remit of the Chief Security Officer.

C.7 Any other information

C.7.1 The most significant concentrations of risk

MMS's insurance risk is highly diversified through the different products offered. MMS is currently writing insurance business in Malta but it also has passporting rights to provide services in several countries outside Malta.

MMS applies a system of procedures and limits enabling it to control the degree of concentration of insurance risk. It also employs reinsurance contracts to reduce insurance risk arising from the concentration or accumulation of guarantees well over maximum acceptance limits.

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 36.6% of the total financial investments (excluding real estate and strategic investments). MAPFRE MSV plc Life is the most important strategic investment held by MMS whilst MMS's property investment allocation is concentrated in a single exposure.

There are no other concentrations of risk expected during the activity planning period.

C.7.2 Sensitivity analysis of significant risks

MMS uses the actual economic balance sheet, SCR, and solvency position at a determined date. Based on this cut-off point, a number of asset and liability variables are chosen which may affect MMS's solvency position.

The process includes a projection of the MMS's situation during the subsequent four years based on its Capital Management Plan, to determine any effects on the solvency position.

The projection is made using a base scenario considered by MMS to be probable, and a series of additional scenarios including the risk factors identified as relevant.

Based on the outcome of the stress tests and sensitivity analyses performed, MMS will continue to have eligible Own Funds to comply with the SCR even in stressed scenarios. The solvency ratio is kept at acceptable values and MMS's solvency is not placed at risk at any time.

C.7.3 Other matters

Off-balance-sheet positions

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

Transfer of risk to special-purpose entities

MMS does not transfer risk to special-purpose entities

D. Valuation for solvency purposes

D.1 Assets

Following are the asset valuation differences using Solvency II criterion, including qualitative explanations for the main differences arising from their valuations using Solvency II and those used in preparing the financial statements (Accounting value) at 31st December 2016.

For a better understanding, it is important to consider that the model balance sheet presented is adjusted to Solvency II regulations, and therefore it was necessary to reclassify the data included under "Accounting value" since each model structures its balance sheet differently. Thus, differences in classification arose under certain headings between the data included in the financial statements and those reflected under "Accounting value." Following are the main differences between the measurement of assets under Solvency II and IFRS:

Assets	Solvency II Value	Accounting Value
Goodwill		-
Deferred acquisition costs		6,049
Intangible assets	-	4,319
Deferred tax assets	57	1,224
Pension benefit surplus	-	-
Property, plant & equipment held for own use	1,841	1,841
Investments (other than assets held for index-linked and unit-linked contracts)	133,041	93,350
Property (other than for own use)	13,713	13,713
Holdings in related undertakings, including participations	97,003	57,506
Equities	4,114	4,114
Equities – listed	4,114	4,114
Equities – unlisted	-	-
Bonds	17,700	17,505
Government Bonds	14,504	14,336
Corporate Bonds	3,196	3,169
Structured notes	-	-
Collateralised securities	-	-
Collective Investments Undertakings	512	512
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:	9,882	14,854
Non-life and health similar to non-life	9,678	14,650

Assets	Solvency II Value	Accounting Value
Non-life, excluding health	9,581	14,570
Health similar to non-life	97	80
Life and health similar to life, excluding health and index-linked and unit-linked	204	204
Health similar to life	-	-
Life excluding health and index-linked and unit-linked	204	204
Life index-linked and unit-linked	-	-
Deposits to cedants	-	-
Insurance and intermediaries receivables	13,836	13,836
Reinsurance receivables	845	845
Receivables (trade, not insurance)	909	909
Own shares (held directly)	-	-
Amounts due in respect of own fund items or initial fund called up but not yet paid in	-	-
Cash and cash equivalents	7,191	7,191
Any other assets, not elsewhere shown	1,093	1,288
TOTAL ASSETS	**168,696**	**145,707**

Figures in thousands of euros

It is important to note that certain re-classifications have been done in the "Accounting value" column as presented in the table above from the classification in the Audited Financial Statements. This has been done to align such classification with the Solvency II classification of amounts.

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

D.1.1 Deferred acquisition costs

Assets	Solvency II Value	Accounting Value
Deferred acquisition costs		6,049

Figures in thousands of euros

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

D.1.2 Intangible assets

Assets	Solvency II Value	Accounting Value
Intangible assets	-	4,319

Figures in thousands of euros

Under IFRS, intangible assets are measured at cost less their accumulated amortization and where applicable, possible impairment. MMS mainly recognizes value of business acquired (VOBA) and computer software as intangible assets. 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 licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised using the straight-line method over their useful lives, not exceeding a period of five years.

Under Solvency II, an intangible asset other than goodwill is only recognized 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 value of business acquired (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.

D.1.3 Deferred tax assets

Assets	Solvency II Value	Accounting Value
Deferred tax assets	57	1,224

Figures in thousands of euros

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 recognized 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 if appropriate. MMS recognized deferred tax assets on its closing balance sheet at a carrying amount of €1.22 million.

MMS recognized deferred tax assets on the Solvency II balance sheet of €0.06 million, resulting from the offsetting of deferred tax assets and liabilities since taxes are paid to the same tax authority.

The differences between the Solvency II and the IFRS value arose due to the different valuation criteria used for the following:

- Deferred acquisition costs
- Intangible assets
- Investments
- Reinsurance recoverables
- Technical provisions

D.1.4 Property, plant & equipment held for own use

Assets	Solvency II Value	Accounting Value
Property, plant & equipment held for own use	1,841	1,841

Figures in thousands of euros

In accordance with Solvency II criteria, property, plant & equipment held for own use must be measured at fair value. Whilst no valuation is carried out on such assets, including the freehold land and building element, their fair value is not significantly different as compared to their carrying amounts.

Under IFRS, properties are valued at its appraisal value, determined by external, independent and qualified valuers. This appraisal value has been considered as its fair value under Solvency II and therefore no adjustment to the valuation was needed.

D.1.5 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 standard 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 main asset or liability's market, and where this does not exist, in the most advantageous market. Valuation techniques appropriate to the circumstances for which there is sufficient data to conduct a fair value measurement must be used, maximizing the use of relevant observable variables while minimizing the use of variables which 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 purpose 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:

D.1.5.1 ***Property (other than for own use)***

Assets	Solvency II Value	Accounting Value
Property (other than for own use)	13,713	13,713

Figures in thousands of euros

In accordance with Solvency II criteria properties which are not considered for own use and are devoted to earning rental fees, capital gains or both must be measured at fair value.

Under IFRS, such properties are valued at its appraisal value, determined by external, independent and qualified architect.

An independent valuation of the investment property of MMS comprising mainly of office buildings was performed by an independent architect to determine the fair value of the land and buildings as at 31st December 2016. The investment property of MMS have been determined to fall within Level 3 of the fair valuation hierarchy mentioned in Section D.1.5.

This appraisal value has been considered as its fair value under Solvency II and therefore no adjustment to the valuation was needed.

D.1.5.2 ***Holdings in related undertakings, including participations***

Assets	Solvency II Value	Accounting Value
Holdings in related undertakings, including participations	97,003	57,506

Figures in thousands of euros

In accordance with the text of Article 212 of Directive 2009/138, related parties and subsidiaries are related companies which are subsidiaries or companies in which there an investment is or which can be considered to have a dominant or significant influence.

Wherever possible, investments in related entities are measured at their listed prices on active markets as regards the Solvency II balance sheet. However, due to the absence of quoted prices on active markets, the investments and subsidiaries were valued using the adjusted equity method, considering the solvency valuation specifics indicated for each investment or subsidiary.

Under IFRS and in accordance with the accounting policies of MMS, investments in subsidiaries are valued at cost less impairment, which differs from Solvency II criteria. Due to the difference in valuation criteria, a higher value was recorded for the investments on the Solvency II balance sheet.

D.1.5.3 ***Equities, bonds and collective investment entities***

- *Equities and collective investment undertakings*

Equities and collective investment undertakings are recognized at fair value on the financial statements and therefore do not reflect valuation differences in comparison with the Solvency II values.

- ***Bonds***

Assets	Solvency II Value	Accounting Value
Government Bonds	14,504	14,336
Corporate Bonds	3,196	3,169

Figures in thousands of euros

Bonds are classified as follows:

A) Government bonds:

This sub-category includes those issued by central governments or organsations forming part of the government structure. This includes instruments issued by autonomous or local administrations in European Union member states, which are considered similar to the debt instruments issued by their central governments.

B) Corporate bonds:

This sub-category includes those issued by institutions which cannot be included within the category of governmental issuers.

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.

D.1.6 Reinsurance recoverables

Assets	Solvency II Value	Accounting Value
Reinsurance recoverables	9,882	14,854
Non-life and health similar to non-life	9,678	14,650
Life and health similar to life, excluding health and index-linked and unit-linked	204	204

Figures in thousands of euros

The calculation of the recoverable amounts of reinsurance is in line with that for gross technical insurance provisions, which means that these amounts must be recognised at their best estimate, also considering the cash flow patterns as well as the expected losses from the counterparty's default.

The following aspects were taken into account when determining the recoverable value of the amounts of reinsurance arising from amounts considered in technical provisions:

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

The classification along the different lines of business and the development of reinsurance claims are based on the assumptions made for gross technical provisions. 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 as explained in section D.2.

D.1.7 Insurance and intermediaries receivables

Assets	Solvency II Value	Accounting Value
Insurance and intermediaries receivables	13,836	13,836

Figures in thousands of euros

For purposes of Solvency II balance sheet, when determining the value of loans with policyholders and intermediaries, the time effect implicit in the loans is irrelevant. The obligatory estimates of possible loan default with insurers related to bills pending payment are considered to correctly reflect their economic value and therefore no adjustment to the valuation was required.

D.1.8 Reinsurance receivables

Assets	Solvency II Value	Accounting Value
Reinsurance receivables	845	845

Figures in thousands of euros

For purposes of the Solvency II balance sheet, when determining the value of amounts receivable from reinsurance transactions, the expected value of potential default by the reinsurer is considered, based on its creditworthiness and the time horizon of the recoveries.

The value of potential reinsurance collections 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 related to the possibility of meeting the counterparty's future payment commitments. Hence, no adjustment to the valuation was required.

D.1.9 Receivables (trade, not insurance)

Assets	Solvency II Value	Accounting Value
Receivables (trade, not insurance)	909	909

Figures in thousands of euros

For the purpose of the Solvency II balance sheet, receivables which do not relate to insurance transactions have been valued in accordance with IFRS based on their face value.

D.1.10 Cash and cash equivalents

Assets	Solvency II Value	Accounting Value
Cash and cash equivalents	7,191	7,191

Figures in thousands of euros

Cash and cash equivalents includes cash in hand and deposits in current accounts, whose value is subject to fairly insignificant risk of change.

For the purposes of Solvency II valuations, cash and cash equivalents have been valued in accordance with IFRS.

D.1.11 Any other assets, not elsewhere shown

Assets	Solvency II Value	Accounting Value
Any other assets, not elsewhere shown	1,093	1,288

Figures in thousands of euros

The difference between the IFRS value and the Solvency II Value of €0.20 million relates to the accrued interest of Bonds which under IFRS, is 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	Accounting Value
Technical provisions - non-life	59,700	67,842
Technical provisions - non-life (excluding health)	56,253	64,124
Technical provisions calculated as a whole	-	
Best Estimate	53,443	
Risk margin	2,810	
Technical provisions - health (similar to non-life)	3,447	3,718
Technical provisions calculated as a whole	-	
Best Estimate	3,171	
Risk margin	276	
Technical provisions - Life (excluding index-linked and unit-linked)	1,553	1,660
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)	1,553	1,660
Technical provisions calculated as a whole	0	
Best Estimate	1,452	
Risk margin	101	
Technical provisions - index-linked and unit-linked	-	-
Technical provisions calculated as a whole	-	
Best Estimate	-	
Risk margin	-	
Other technical provisions		-
TOTAL TECHNICAL PROVISIONS	**61,253**	**69.502**

Figures in thousands of euros

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 (2.5% of the total technical provisions).

Following are the qualitative explanations of the key technical provision valuation differences using Solvency II criteria and those used during the preparation of the financial statements. In general terms, the main difference between the two valuation methods is the criteria framework under which each regulation falls. 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 Solvency II Directive 2009/138/CE stipulates that the value of technical provisions shall be equal to the sum of a best estimate and a risk margin.

D.2.1 TECHNICAL PROVISIONS – NON-LIFE BUSINESS

Technical provisions	Solvency II Value	Accounting Value
Technical provisions - non-life	59,700	67,842

Figures in thousands of euros

D.2.1.1 Best estimate

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

a) Best estimate of the provision for outstanding claims

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

- Taking into account all claims occurring prior to the valuation date, regardless of whether they have been reported or not.

- It is calculated by the present value of expected future cash flows associated to the incurred claim. Projected cash flows will indicate payments for benefits and related expenses.

- Should there be any liabilities transferred to counterparty, the recoverable amounts are adjusted to factor in the expected losses due to 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 claim cost less payments made. The calculation of the ultimate cost takes place using proven deterministic statistical methods outlined in Section D.2.4.

The Claims provision in the financial statements include: the provision for outstanding claims and the provision for claim settlement expenses. The provision for outstanding claims consists of the individual case-by-case valuation of claims with the exception of accident year 2016 Motor Claims which have been determined on an ultimate cost basis having regards to estimation techniques establishing the average ultimate cost per claim, which average was applied to the estimated number of IBNR claims. Certain losses involving fatalities or serious bodily injury have been reserved at the case-by-case reserve estimate.

We conclude that the claims provisions calculated based on Solvency II criteria present the following differences with respect to those calculated based on financial statement requirements:

- The elimination of prudence margins. Using financial statement criteria, a certain prudence margin is generally applied to provisions to cover possible unfavorable deviations of outstanding claims. However, under Solvency II, the calculation of the claims provision must be made without including any prudence margins.

- The consideration all cash flow sources.

- The counterparty default adjustment to recoverable reinsurance amounts.

- The financial discount of cash flows.

b) Best estimate of the provision for premiums

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

- It corresponds to future claims, or those which take place subsequent to the valuation date, corresponding to the remaining claim coverage period.

- This is calculated as the present value of expected cash flows associated to the portfolio in force, in accordance with contract boundaries.

- Projected cash flows will include payments for benefits and related expenses: administration, acquisition, claim management, and investment management.

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

- The best estimate considers the time value of money based on the consideration of the claim inflows and outflows.

As indicated previously, the calculation of this provision is comprised of the cash-flows corresponding to two portfolios:

- Portfolio in force: This includes the following:

    - Expected claims: Two methodologies may be used to calculate the current value of service payments:
        - The frequency and average cost method: claims are calculated as the result of exposure based on frequency assumptions and final average costs.

        - Loss ratio method: the expected claims arising from applying the ultimate loss ratio to Unearned Premium Reserve (UPR), gross of acquisition expenses.

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

- Future business: This includes the following:

    - Premiums corresponding to policies which have not yet been renewed but include company commitments to renew. This calculation includes the future performance of policyholders based on the applications of an estimated lapse ratio.

    - Expected claims corresponding to future premiums. The same methodologies for portfolio in force may be used.

    - Expenses attributable to future premiums (charged expense-to-premium ratio applying future premiums): acquisition expenses (including commissions), administration, chargeable to services, 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 tariff premium 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. The provision supplements the unearned premium reserve with an amount by which the future contractual cash-flows arising from such reserve exceed the same reserve.

Boundary of insurance contracts

As outlined in the Solvency II Directive, when calculating the best estimate, it is necessary to consider the contractual limits. In certain cases, this implies the inclusion of future premiums arising from commitments in force. If the contracts are profitable, cash inflows corresponding to these premiums will be higher than the outflows (payments and expenses); thereby generating a negative BEL. Depending on the product's profitability, the inclusion of contractual limits generates a decrease in the best estimate (if the contracts are profitable) or an increase (if they are not).

Contractual limits must meet a series of requirements. The obligations arising from the contract, including those which correspond to the insurance/reinsurance company's unilateral right to renew or increase its limits and corresponding premiums, will be included in its text, except for:

- Obligations provided by the company after the date during which:
    - The Company has unilateral cancellation rights over the contract
    - The Company reserves the right to reject premiums payable related to the contract
    - The Company reserves the unilateral right to modify its premiums or services 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, except for the following conditions:
    - The contract does not establish an indemnity for a specific undetermined event which may adversely affect the insured party.
    - The contract does not include a financial guarantee for coverage provided.

We conclude that claim provisions calculated based on Solvency II criteria present the following differences with respect to those calculated based on financial statement requirements:

- The application of the concept of contractual limits, which involves the consideration of future business. Conversely, under IFRS future premiums must be taken into account if they contemplate 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 UPR reflected on financial statements. In cases of premium inadequacy, the premium provision is comparable to the UPR 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 credit risk adjustment to recoverable reinsurance amounts.

- The financial discount of cash flows.

D.2.2 TECHNICAL PROVISIONS – LIFE BUSINESS

Technical provisions	Solvency II Value	Accounting Value
Technical provisions - life	1,553	1,660

Figures in thousands of euros

D.2.2.1 Best estimate

The Group Life technical provisions are calculated similarly to the Non-Life technical provisions due to the nature of the business written by MMS. MMS does not consider future business in the calculation of the life provision as there is no commitment in the annual renewal.

D.2.3 Risk margin

The Risk Margin is conceptually equivalent to the cost of supplying eligible own funds, and the Solvency Capital Requirement (SCR) necessary to support insurance commitments during their entire period of validity and until they are definitively settled. The interest rate used in determining cost of supplying the amount of eligible own funds is known as the cost-of-capital rate. MMS used the 6% rate set by the 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:

- CoC: cost-of-capital rate which is taken as 6%
- SCR_t: Solvency Capital Requirement after t years
- 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 obligatory future solvency capital requirements are proportional to the best estimate of technical provisions during the year in question.
- Level 3: this consists in using the modified duration of liabilities to approximate obligatory current and future solvency capital in a single step.
- Level 4: calculates the risk margin as a percentage of the best estimate technical provisions net of reinsurance.

There is not always a clear line separating the above Levels. For example, this is the case for the difference between Level 1 and 2 simplifications. Since MMS applies a proportional method to each relevant module or sub-module for calculating future obligatory solvency capital, the risk margin calculations may be considered to be prepared using simplifications belonging to Levels 1 or 2.

D.2.4 Actuarial methods and assumptions used when calculating technical provisions

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

For Non-Life insurance:

A combination of generally-accepted deterministic methods used for calculating ultimate claims based on Development Factors Methods on paid and incurred triangles and large losses case by case. MMS considers the methodologies used to be appropriate.

The following two key assumptions were used during the calculation of the technical provisions:

- Economic assumptions, which are compared to available financial and macroeconomic indicators which mainly include:

  - Interest rate structure split by the commitment currencies.
  - 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 historic experience, or external sector/market sources:

  - Realistic administration, investment, acquisition, etc. expenses which are incurred throughout the duration of the contracts.
  - Customer losses and policy surrenders.
  - The frequency and severity of claims based on historical 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, as indicated in the Directive, 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 methodologies and models used, as well as the hypotheses used in these calculations.

For Life insurance:

- Economic assumption, which are compared to available financial and macroeconomic indicators which mainly include:

  - Interest rate structure split by the commitment currencies.
  - 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 historic experience, or external sector/market sources:

  - Realistic administration, investment, acquisition, etc. expenses which are incurred throughout the duration of the contracts.
  - Loss ratio based on historical data.
  - Legislative changes.

D.2.5 Degree of uncertainty regarding to 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, which are mainly the following:

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

The first three factors are generally estimated based on expert opinions, or using market data.

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	Accounting Value
Total technical provisions	**61,253**	**69,502**
Contingent liabilities	-	-
Provisions other than technical provisions	-	-
Pension benefit obligations	1,186	1,186
Deposits from reinsurers	-	-
Deferred tax liabilities	-	1,030
Derivatives	-	-
Debts owed to credit institutions	-	-
Financial liabilities other than debts owed to credit institutions	-	-
Insurance & intermediaries payables	160	160
Reinsurance payables	2,762	2,762
Payables (trade, not insurance)	7,669	7,669
Subordinated liabilities	-	-
Subordinated liabilities not in Basic Own Funds	-	-
Subordinated liabilities in Basic Own Funds	-	-
Any other liabilities, not elsewhere shown	-	1,301
TOTAL LIABILITIES	73,029	83,610
SURPLUS OF ASSETS VS. LIABILITIES	**95,666**	**62,097**

Figures in thousands of euros

Below are the explanations of the key valuation differences for other liabilities in the table above:

D.3.1 Pension benefit obligations

Other liabilities	Solvency II Value	Accounting Value
Pension benefit obligations	1,186	1,186

Figures in thousands of euros

MMS operates a defined benefit plan in favour of a former Executive Chairman. The pension plan defines an amount of pension benefit that he receives on retirement. The valuation of the obligation is the same under IFRS and Solvency II and is equal to the present value determined by discounting estimated future cash outflows.

D.3.2 Deferred tax liabilities

Other liabilities	Solvency II Value	Accounting Value
Deferred tax liabilities	-	1,030

Figures in thousands of euros

Deferred taxes are measured under Solvency II as the difference between the values assigned to assets and liabilities for solvency purposes, and their assigned values as recognized and valued for tax purposes.

Under IFRS, deferred taxes are calculated on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts. MMS recognised deferred tax liabilities on its closing balance sheet at a carrying amount of €1.03 million. The accounting value of the deferred tax liability arises mainly from tax that the Company will be liable to pay on the selling price on the disposal of investment property.

MMS recognised deferred tax liabilities on the Solvency II balance sheet at zero, resulting from the offsetting of deferred tax assets and liabilities since taxes are paid to the same tax authority.

The differences between the Solvency II and accounting value arose due to the different valuation criteria:

- Deferred acquisition costs
- Intangible assets
- Investments
- Reinsurance recoverables
- Technical provisions

D.3.3 Insurance & intermediaries payables

Other liabilities	Solvency II Value	Accounting Value
Insurance & intermediaries payables	160	160

Figures in thousands of euros

For the purposes of the Solvency II balance sheet, the valuation is considered consistent with that under IFRS, valued at the amount at which they may be transferred or settled between duly-informed interested parties carrying out transactions in mutually-independent conditions.

D.3.4 Reinsurance payables

Other liabilities	Solvency II Value	Accounting Value
Reinsurance payables	2,762	2,762

Figures in thousands of euros

This includes reinsurance debts on the current account established for ceded and receded reinsurance transactions. For the purposes of the Solvency II balance sheet, the valuation is considered consistent with that under IFRS, valued at the amount at which they may be transferred or settled between duly-informed interested parties carrying out transactions in mutually-independent conditions.

D.3.5 Payables (trade, not insurance)

Other liabilities	Solvency II Value	Accounting Value
Payables (trade, not insurance)	7,669	7,669

Figures in thousands of euros

This section includes other payables unrelated to the insurance activity. For the purposes of the Solvency II balance sheet, the valuation is considered consistent with that under IFRS, valued at the amount at which they may be transferred or settled between duly-informed interested parties carrying out transactions in mutually-independent conditions.

D.3.6 Any other liabilities, not elsewhere shown

Other liabilities	Solvency II Value	Accounting Value
Any other liabilities, not elsewhere shown	-	1,301

Figures in thousands of euros

“Accounting value” mainly includes commissions and other accrued granted insurance acquisition expenses with an accounting value of €1.30 million.

For Solvency II purposes, commissions and other granted accrued reinsurance acquisition expenses are taken into consideration during the valuation of technical provisions, as they include the entirety of the associated expenses, and therefore do not appear under this heading.

D.4 Appendices

The following includes the obligatory quantitative information foreseen by Article 75 of Directive 2009/138/EC, based on the instruction in Section S.02.01 of the Appendix II to Commission Implementing Regulation (EU) 2015/2452 regarding balance sheets under Solvency II guidelines.

A) Assets

Template detailing quantitative asset disclosures at 31st December 2016:

	Assets	Solvency II value
		C0010
R0030	Intangible assets	-
R0040	Deferred tax assets	57
R0050	Pension benefit surplus	-
R0060	Property, plant & equipment held for own use	1,841
R0070	Investments (other than assets held for index-linked and unit-linked contracts)	133,041
R0080	Property (other than for own use)	13,713
R0090	Holdings in related undertakings, including participations	97,003
R0100	Equities	4,114
R0110	Equities - listed	4,114
R0120	Equities - unlisted	-
R0130	Bonds	17,700
R0140	Government Bonds	14,504
R0150	Corporate Bonds	3,196
R0160	Structured notes	-
R0170	Collateralised securities	-
R0180	Collective Investments Undertakings	512
R0190	Derivatives	-
R0200	Deposits other than cash equivalents	-
R0210	Other investments	-
R0220	Assets held for index-linked and unit-linked contracts	-
R0230	Loans and mortgages	-
R0240	Loans on policies	-
R0250	Loans and mortgages to individuals	-
R0260	Other loans and mortgages	-
R0270	Reinsurance recoverables from:	9,882
R0280	Non-life and health similar to non-life	9,678
R0290	Non-life excluding health	9,581
R0300	Health similar to non-life	97
R0310	Life and health similar to life, excluding health and index-linked and unit-linked	204
R0320	Health similar to life	-
R0330	Life excluding health and index-linked and unit-linked	204

	Assets	Solvency II value
		C0010
R0340	Life index-linked and unit-linked	-
R0350	Deposits to cedants	-
R0360	Insurance and intermediaries receivables	13,836
R0370	Reinsurance receivables	845
R0380	Receivables (trade, not insurance)	909
R0390	Own shares (held directly)	-
R0400	Amounts due in respect of own fund items or initial fund called up but not yet paid in	-
R0410	Cash and cash equivalents	7,191
R0420	Any other assets, not elsewhere shown	1,093
R0500	**Total assets**	**168,696**

Source: Template S.02.01.02

B) Technical provisions

B.1 Template detailing quantitative asset disclosures at 31st December 2016:

	Liabilities	Solvency II value
		C0010
R0510	Technical provisions – non-life	59,700
R0520	Technical provisions – non-life (excluding health)	56,253
R0530	TP calculated as a whole	-
R0540	Best Estimate	53,443
R0550	Risk margin	2,810
R0560	Technical provisions - health (similar to non-life)	3,447
R0570	TP calculated as a whole	-
R0580	Best Estimate	3,171
R0590	Risk margin	276
R0600	Technical provisions - life (excluding index-linked and unit-linked)	1,553
R0610	Technical provisions - health (similar to life)	-
R0620	TP calculated as a whole	-
R0630	Best Estimate	-
R0640	Risk margin	-
R0650	Technical provisions – life (excluding health and index-linked and unit-linked)	1,553
R0660	TP calculated as a whole	-
R0670	Best Estimate	1,452
R0680	Risk margin	101
R0690	Technical provisions – index-linked and unit-linked	-
R0700	TP calculated as a whole	-
R0710	Best Estimate	-
R0720	Risk margin	-

Source: Template S.02.01.02

B.2.1 Template detailing non-life technical provisions by business lines at December 31st December 2016:

		Direct business and accepted proportional reinsurance				
		Medical expense insurance	Income protection insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance
		C0020	C0030	C0050	C0060	C0070
R0010	**Technical provisions calculated as a whole**	-	-	-	-	-
R0050	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					
R0060	Gross	1,961	246	8,388	6,045	402
R0140	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	14	(3)	(18)	62	(1)
R0150	Net Best Estimate of Premium Provisions	1,947	249	8,407	5,983	403
	Claims provisions					
R0160	Gross	697	267	14,161	6,908	1,228
R0240	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	75	11	2,798	1	669
R0250	Net Best Estimate of Claims Provisions	622	256	11,364	6,907	560
R0260	**Total Best estimate - gross**	2,658	514	22,550	12,953	1,630

		Direct business and accepted proportional reinsurance				
		Medical expense insurance	Income protection insurance	Motor vehicle liability insurance	Other motor insurance	Marine, aviation and transport insurance
R0270	**Total Best estimate - net**	2,569	506	19,770	12,889	962
R0280	**Risk margin**	226	50	920	648	169
	Amount of the transitional on Technical Provisions					
R0290	Technical Provisions calculated as a whole	-	-	-	-	-
R0300	Best estimate	-	-	-	-	-
R0310	Risk margin	-	-	-	-	-
	Technical provisions - total					
R0320	Technical provisions - total	2,883	563	23,470	13,601	1,799
R0330	Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total	89	8	2,779	63	668
R0340	Technical provisions minus recoverables from reinsurance/SPV and Finite Re - total	2,795	556	20,690	13,538	1,131

		Direct business and accepted proportional reinsurance				Accepted non-proportional reinsurance	Total Non-Life obligation
		Fire and other damage to property insurance	General liability insurance	Assistance	Miscellaneous financial loss	Non-proportional property reinsurance	
		C0080	C0090	C0120	C0130	C0170	C0180
R0010	**Technical provisions calculated as a whole**	-	-	-	-	-	-
R0050	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						
R0060	Gross	2,545	559	915	159	-	21,220
R0140	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	1,199	32	39	10	-	1,333
R0150	Net Best Estimate of Premium Provisions	1,346	527	876	149	-	19,887
	Claims provisions						
R0160	Gross	5,095	6,224	366	-	447	35,394
R0240	Total recoverable from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default	3,270	1,351	117	-	52	8,345

		Direct business and accepted proportional reinsurance				Accepted non-proportional reinsurance	Total Non-Life obligation
		Fire and other damage to property insurance	General liability insurance	Assistance	Miscellaneous financial loss	Non-proportional property reinsurance	
R0250	Net Best Estimate of Claims Provisions	1,825	4,874	248	-	395	27,049
R0260	**Total Best estimate - gross**	7,640	6,784	1,281	159	447	56,614
R0270	**Total Best estimate - net**	3,171	5,401	1,125	149	395	46,937
R0280	**Risk margin**	544	397	97	3	32	3,086
	Amount of the transitional on Technical Provisions						
R0290	Technical Provisions calculated as a whole	-	-	-	-	-	-
R0300	Best estimate	-	-	-	-	-	-
R0310	Risk margin	-	-	-	-	-	-
	Technical provisions - total						
R0320	Technical provisions - total	8,184	7,180	1,377	162	479	59,700
R0330	Recoverable from reinsurance contract/SPV and Finite Re after the adjustment for expected losses due to counterparty default - total	4,469	1,383	156	10	52	9,678
R0340	Technical provisions minus recoverables from reinsurance/SPV and Finite Re - total	3,715	5,798	1,221	152	427	50,023

Source: Template S.17.01.02

B.2.2 Template detailing life technical provisions by business lines at December 31st December 2016:

		Other life insurance			Total (Life other than health insurance, including Unit-Linked)
			Contracts without options and guarantees	Contracts with options or guarantees	
		C0060	C0070	C0080	C0150
R0010	**Technical provisions calculated as a whole**	-			-
R0020	**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				
R0030	**Gross Best Estimate**		1,452	-	1,452
R0080	Total Recoverables from reinsurance/SPV and Finite Re after the adjustment for expected losses due to counterparty default		204	-	-
R0090	Best estimate minus recoverables from reinsurance/SPV and Finite Re - total		1,248	-	1,248
R0100	**Risk Margin**	101			-
	Amount of the transitional on Technical Provisions				

		Other life insurance			Total (Life other than health insurance, including Unit-Linked)
			Contracts without options and guarantees	Contracts with options or guarantees	
		C0060	C0070	C0080	C0150
R0110	Technical Provisions calculated as a whole	-			-
R0120	Best estimate		-	-	-
R0130	Risk margin	-			-
R0200	**Technical provisions - total**	1,553			1,553

Source: Template S.12.01.02

B.3 Template detailing non-life claim performance at 31st December 2016

The following templates reflect the estimate made by MMS of the cost of claims (claims paid and claims provisions under Solvency II valuation principle) and how this estimate develops over time.

Gross Claims Paid (non-cumulative)

(absolute amount)

Development year

Year		0	1	2	3	4	5	6	7	8	9	10 & +		In Current year	Sum of years (cumulative)
		C0010	C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090	C0100	C0110		C0170	C0180
Prior	R0100											335,401		335,401	335,401
N-9	R0160	8,933,635	4,159,469	700,960	469,258	201,021	71,801	104,722	16,835	63,495	8,893			8,893	14,730,089
N-8	R0170	9,503,026	4,431,863	972,499	301,412	251,094	184,422	616,756	78,959	77				77	16,340,107
N-7	R0180	9,608,920	4,736,185	629,719	539,264	422,656	95,646	977,242	144,567					144,567	17,154,200
N-6	R0190	10,320,650	4,092,401	409,746	335,612	163,510	22,084	49,213						49,213	15,393,216
N-5	R0200	9,768,017	4,476,122	985,281	563,179	363,106	53,145							53,145	16,208,849
N-4	R0210	10,011,899	4,264,605	815,866	356,998	128,686								128,686	15,578,054
N-3	R0220	10,611,230	4,396,926	619,814	269,084									269,084	15,897,054
N-2	R0230	10,292,754	4,465,444	1,061,742										1,061,742	15,819,940
N-1	R0240	11,610,748	8,232,441											8,232,441	19,843,189
N	R0250	15,121,182												15,121,182	15,121,182
													Total	25,404,432	162,421,281

Source: Template S.19.01.21

The above template reflects the payments made each year in course for claims arising during non-accumulated years of occurrence.

Gross undiscounted Best Estimate Claims Provisions

(absolute amount)

		Development year											
Year		**0**	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10 & +**	**Year end (discounted data)**
		C0200	C0210	C0220	C0230	C0240	C0250	C0260	C0270	C0280	C0290	C0300	C0360
Prior	**R0100**											4,671,523	4,632,164
N-9	**R0160**										210,689		202,117
N-8	**R0170**									701,714			704,477
N-7	**R0180**								892,223				893,757
N-6	**R0190**							1,503,423					1,501,020
N-5	**R0200**						505,992						502,303
N-4	**R0210**					2,458,771							2,437,615
N-3	**R0220**				2,268,028								2,246,094
N-2	**R0230**			1,463,940									1,436,195
N-1	**R0240**		3,656,410										3,621,012
N	**R0250**	17,270,259											17,221,072
												Total	35,397,826

Source: Template S.19.01.21

C) Other liabilities

Form detailing quantitative liabilities disclosures at December 31st December 2016:

	Liabilities	Solvency II value
		C0010
R0740	Contingent liabilities	-
R0750	Provisions other than technical provisions	-
R0760	Pension benefit obligations	1,186
R0770	Deposits from reinsurers	-
R0780	Deferred tax liabilities	-
R0790	Derivatives	-
R0800	Debts owed to credit institutions	-
R0810	Financial liabilities other than debts owed to credit institutions	-
R0820	Insurance & intermediaries payables	160
R0830	Reinsurance payables	2,762
R0840	Payables (trade, not insurance)	7,669
R0850	Subordinated liabilities	-
R0860	Subordinated liabilities not in Basic Own Funds	-
R0870	Subordinated liabilities in Basic Own Funds	-
R0880	Any other liabilities, not elsewhere shown	-
R0900	**Total liabilities**	**73,029**
R1000	**Excess of assets over liabilities**	**95,666**

Source: Template S.02.01.02

E. Capital management

E.1 Equity

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

To manage and monitor its own funds and capital, MMS has approved a Capital Management Policy covering the following objectives:

- Provide the GROUP and MMS with a procedure to verify that MMS has a sufficient amount of eligible capital to cover the Solvency Capital Requirement as well as the levels established in the Risk Appetite on a continuous basis.
- Ensure that projected eligible capital continuously meet the applicable requirements throughout the period covered.
- Ensure that MMS has a Medium-Term Capital Management Plan.
- Capital management shall take into account the results of the ORSA and the conclusions drawn during said process.
- Within the framework of the medium and long-term capital management plan, should the need for new resources be anticipated, it will be necessary to verify that the new capital instruments issued meet the requirements to be included in the desired level of quality for eligible capital.

Should the eligible capital be insufficient at any moment during the period covered in the projections, the Risk Management Area must propose future management measures to remedy said insufficiency and maintain the solvency levels within the levels established in the applicable regulations and the Risk Appetite.

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

a) compliance with the Solvency regulation which must be applied throughout the projection period concerned, paying special attention to known future regulatory changes, while maintaining solvency levels aligned with the provisions in the Risk Appetite;

b) every expected issuing of eligible capital instruments;

c) reimbursements, both contractual at maturity and those which are discretionary before maturity, in relation to eligible capital instruments;

d) the results of the projections in the own risk and solvency assessment (“ORSA”)

e) foreseeable dividends and their impact on eligible capital.

The Risk Management Area must submit the medium-term Capital Management Plan to the Board of Directors or equivalent Governing Body for approval. The plan is part of the ORSA report. The projection period covers 4 years, and is aligned with the MAPFRE Group’s budget preparation approach.

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

As stipulated in 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 2016, all the available own funds correspond to Tier 1 unrestricted except for a net deferred tax asset of €0.06 million corresponding to Tier 3. 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. MMS's own funds consist of:

- Ordinary share capital
- Share premium account related to ordinary share capital
- Reconciliation reserve
- An amount equal to the value of net deferred tax assets

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

		Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
	Basic own funds before deduction for participations in other financial sector as foreseen in article 68 of Delegated Regulation 2015/35					
R0010	Ordinary share capital (gross of own shares)	19,320	19,320		-	
R0030	Share premium account related to ordinary share capital	688	688		-	
R0040	Iinitial funds, members' contributions or the equivalent basic own - fund item for mutual and mutual-type undertakings	-	-		-	
R0050	Subordinated mutual member accounts	-		-	-	-
R0070	Surplus funds	-	-			
R0090	Preference shares	-		-	-	-
R0110	Share premium account related to preference shares	-		-	-	-
R0130	Reconciliation reserve	72,082	72,082			
R0140	Subordinated liabilities	-		-	-	-
R0160	An amount equal to the value of net deferred tax assets	57				57
R0180	Other own fund items approved by the supervisory authority as basic own funds not specified above	-	-	-	-	-

		Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
	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					
R0220	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					
R0230	Deductions for participations in financial and credit institutions	-	-	-	-	
R0290	**Total basic own funds after deductions**	92,146	92,089	-	-	57
	Ancillary own funds					
R0300	Unpaid and uncalled ordinary share capital callable on demand	-			-	
R0310	Unpaid and uncalled initial funds, members' contributions or the equivalent basic own fund item for mutual and mutual - type undertakings, callable on demand	-			-	
R0320	Unpaid and uncalled preference shares callable on demand	-			-	-
R0330	A legally binding commitment to subscribe and pay for subordinated liabilities on demand	-			-	-

		Total	Tier 1 - unrestricted	Tier 1 - restricted	Tier 2	Tier 3
		C0010	C0020	C0030	C0040	C0050
R0340	Letters of credit and guarantees under Article 96(2) of the Directive 2009/138/EC	-			-	
R0350	Letters of credit and guarantees other than under Article 96(2) of the Directive 2009/138/EC	-			-	-
R0360	Supplementary members calls under first subparagraph of Article 96(3) of the Directive 2009/138/EC	-			-	
R0370	Supplementary members calls - other than under first subparagraph of Article 96(3) of the Directive 2009/138/EC	-			-	-
R0390	Other ancillary own funds	-			-	-
R0400	**Total ancillary own funds**	-			-	-
	Available and eligible own funds					
R0500	Total available own funds to meet the SCR	92,146	92,089	-	-	57
R0510	Total available own funds to meet the MCR	92,089	92,089	-	-	
R0540	Total eligible own funds to meet the SCR	92,146	92,089	-	-	57
R0550	Total eligible own funds to meet the MCR	92,089	92,089	-	-	
R0580	**SCR**	31,420				
R0600	**MCR**	8,751				
R0620	**Ratio of Eligible own funds to SCR**	2.9327				
R0640	**Ratio of Eligible own funds to MCR**	10.5232				

	Reconciliation reserve	C0060
R0700	Excess of assets over liabilities	95,666
R0710	Own shares (held directly and indirectly)	-
R0720	Foreseeable dividends, distributions and charges	3,520
R0730	Other basic own fund items	20,065
R0740	Adjustment for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds	-
R0760	**Reconciliation reserve**	72,082
	Expected profits	
R0770	Expected profits included in future premiums (EPIFP) - Life business	-
R0780	Expected profits included in future premiums (EPIFP) - Non- life business	469
R0790	**Total Expected profits included in future premiums (EPIFP)**	469

Source: Template S.23.01.01

None of the Own Fund Items required supervisory approval.

MMS's SCR Ratio is equal to 293.3%. This ratio measures the relationship between the eligible own funds and the solvency capital requirements, and was calculated using the Standard Formula. This ratio falls within the Risk Appetite established for MMS and approved by the Board of Directors.

It reflects MMS's significant capital buffer to meet the obligations to its policyholders and beneficiaries in the next twelve months, with a minimum probability of 99.5%.

Availability, subordination and duration of significant Own Fund items used to evaluate their quality

MMS's restricted 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.

However, Tier 3 own funds are not fully eligible for the regulatory capital coverage and do not have adequate availability in order to absorb losses in case it was necessary.

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 used for the preparation of the financial statements. These criteria differences lead to differences between the equity in the financial statements and the excess of assets over liabilities for Solvency II purposes.

As at 31st December 2016, equity in the financial statements totaled €62.1 million, whilst the excess of assets over liabilities for Solvency II purposes amounted to €95.7 million.

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

Items deducted from own funds and restrictions on transferability

MMS does not have participations in financial and credit institutions, so no deductions from the own funds were necessary.

An amount of €3.52 million was deducted from the own funds relating to the approximate amount of dividends which will be distributed to shareholders in 2017.

Adjustments for restricted own fund items in respect of matching adjustment portfolios and ring fenced funds are not applicable to MMS.

Own Funds issued and instruments redeemed

No Own Funds were issued and no instruments were redeemed.

Essential items on the Reconciliation Reserve

S.23.01.01 includes 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 over liabilities for Solvency II purposes.

This surplus amounted to €95.7 million. To determine the reconciliation reserve the following were deducted:

- Foreseeable dividends, distributions, and charges amounting to €3.52 million.

- Other basic own fund items amounting to €20.1 million.

E.1.3 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.

E.1.4 Ancillary own funds

MMS did not consider any ancillary own-fund items.

E.1.5 Items deducted from Own Funds

MMS did not deduct any items from own funds.

E.1.6 Other information

Other ratios apart from those included on template S.23.01

MMS does not use other ratios apart from those included in template S.23.01 in relation to the solvency position.

Subordinated liabilities

MMS does not have subordinated liabilities.

Main loss absorption mechanisms.

MMS does not have basic own fund items which possess loss absorbency mechanisms complying with Article 71 (1) (e) of the Commission Delegated Regulation (EU) 2015/35.

E.2 Solvency Capital Requirement and Minimum Capital Requirement

E.2.1 Amount of the Solvency Capital Requirement

SCR and MCR amounts

Following are the Solvency Capital Requirements (SCR) at module level, calculated using the standard formula:

		Gross solvency capital requirement	USP	Simplifications
		C0110	C0090	C0100
R0010	Market risk	26,182	-	Counterparty default risk (Risk-mitigating effect)
R0020	Counterparty default risk	9,123		
R0030	Life underwriting risk	1,530	-	Life mortality risk, Life expense risk, Life catastrophe risk
R0040	Health underwriting risk	1,966	-	
R0050	Non-life underwriting risk	12,644	-	
R0060	Diversification	(14,051)		
R0070	Intangible asset risk	-		
R0100	**Basic Solvency Capital Requirement**	37,394		

	Calculation of Solvency Capital Requirement	C0100
R0130	Operational risk	1,822
R0140	Loss-absorbing capacity of technical provisions	-
R0150	Loss-absorbing capacity of deferred taxes	(7,797)
R0160	Capital requirement for business operated in accordance with Art. 4 of Directive 2003/41/EC	-
R0200	**Solvency capital requirement excluding capital add-on**	31,420
R0210	Capital add-on already set	-
R0220	**Solvency capital requirement**	31,420
	Other information on SCR	-
R0400	Capital requirement for duration-based equity risk sub-module	-
R0410	Total amount of Notional Solvency Capital Requirement for remaining part	-
R0420	Total amount of Notional Solvency Capital Requirements for ring fenced funds	-
R0430	Total amount of Notional Solvency Capital Requirement for matching adjustment portfolios	-
R0440	Diversification effects due to RFF nSCR aggregation for article 304	-

Source: Template S.25.01.21

To calculate its SCR, MMS used the following simplifications:

For Life Underwriting Risk, MMS makes use of the simplified calculation for the solvency capital requirement for its life business for life mortality risk, life expense risk and life catastrophe risk in accordance with Articles 91, 94 and 96 of the Commission Delegated Regulation 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 risk mitigating effect in accordance with Article 107 of the Commission Delegated Regulation.

The use of these simplifications are considered appropriate to the nature, volume, and complexity of the associated risks.

The total SCR amount was €31.4 million. As indicated in Solvency II regulations, the SCR corresponds to the insurance undertaking's equity for limiting the probability of bankruptcy to one case per 200, or that the insurance undertaking is still 99.5% able to meet its commitments to insurance beneficiaries and policyholders during the following year.

The risk modules with the highest capital requirements are Market risk and Non-Life underwriting risk.

The Minimum Capital Requirement (MCR) is the minimum level of security below which the amount of financial resources should not fall. When the amount of eligible basic own funds falls below the MCR, the policyholders and beneficiaries will be exposed to an unacceptable level of risk, should MMS continue its activity. The MCR amounts to €8.8 million.

The following table shows MMS's MCR, and the different information used in the calculation, which include:

- Net (of reinsurance/ SPV) best estimate
- Net (of reinsurance) written premiums in the last 12 months
- Total capital at risk, net of (reinsurance/SPV)

		Non-life activities	Life activities
		MCR(NL,NL) Result	MCR(NL,L)Result
		C0010	C0020
R0010	**Linear formula component for non-life insurance and reinsurance obligations**	8,025	-

		Non-life activities		Life activities	
		Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0030	C0040	C0050	C0060
R0020	Medical expenses insurance and proportional reinsurance	2,569	8,102	-	-
R0030	Income protection insurance and proportional reinsurance	506	932	-	-
R0040	Workers' compensation insurance and proportional reinsurance	-	-	-	-

		Non-life activities		Life activities	
		Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0030	C0040	C0050	C0060
R0050	Motor vehicle liability insurance and proportional reinsurance	19,770	13,109	-	-
R0060	Other motor insurance and proportional reinsurance	12,889	16,080	-	-
R0070	Marine, aviation and transport insurance and proportional reinsurance	962	1,740	-	-
R0080	Fire and other damage to property insurance and proportional reinsurance	3,171	2,305	-	-
R0090	General liability insurance and proportional reinsurance	5,401	3,340	-	-
R0100	Credit and suretyship insurance and proportional reinsurance	-	-	-	-
R0110	Legal expenses insurance and proportional reinsurance	-	-	-	-
R0120	Assistance and proportional reinsurance	1,125	2,003	-	-

		Non-life activities		Life activities	
		Net (of reinsurance/ SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months	Net (of reinsurance/SPV) best estimate and TP calculated as a whole	Net (of reinsurance) written premiums in the last 12 months
		C0030	C0040	C0050	C0060
R0130	Miscellaneous financial loss insurance and proportional reinsurance	149	34	-	-
R0140	Non-proportional health reinsurance	-	-	-	-
R0150	Non-proportional casualty reinsurance	-	-	-	-
R0160	Non-proportional marine, aviation and transport reinsurance	-	-	-	-
R0170	Non-proportional property reinsurance	395	-	-	-

		Non-life activities	Life activities
		MCR(L,NL) Result	MCR(L,L) Result
		C0070	C0080
R0200	**Linear formula component for life insurance and reinsurance obligations**	-	727

		Non-life activities		Life activities	
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole provisions	Net (of reinsurance/SPV) total capital at risk	Net (of reinsurance/SPV) best estimate and TP calculated as a whole provisions	Net (of reinsurance/SPV) total capital at risk
		C0090	C0100	C0110	C0120
R0210	Obligations with profit participation - guaranteed benefits	-		-	
R0220	Obligations with profit participation - future discretionary benefits	-		-	
R0230	Index-linked and unit-linked insurance obligations	-		-	

		Non-life activities		Life activities	
		Net (of reinsurance/SPV) best estimate and TP calculated as a whole provisions	Net (of reinsurance/SPV) total capital at risk	Net (of reinsurance/SPV) best estimate and TP calculated as a whole provisions	Net (of reinsurance/SPV) total capital at risk
		C0090	C0100	C0110	C0120
R0240	Other life (re)insurance and health (re)insurance obligations	-		1,248	
R0250	Total capital at risk for all life (re)insurance obligations		-		1,000,504
			-		-
			-		-

	Overall MCR calculation	C0130
R0300	Linear MCR	8,751
R0310	SCR	31,428
R0320	MCR cap	14,143
R0330	MCR floor	7,857
R0340	Combined MCR	8,751
R0350	Absolute floor of the MCR	7,400

		C0130
R0400	**Minimum Capital Requirement**	8,751

	Notional non-life and life MCR calculation	Non-life activities	Life activities
		C0140	C0150
R0500	Notional linear MCR	8,025	727
R0510	Notional SCR excluding add-on (annual or latest calculation)	28,819	2,609
R0520	Notional MCR cap	12,968	1,174
R0530	Notional MCR floor	7,205	652
R0540	Notional Combined MCR	8,025	727
R0550	Absolute floor of the notional MCR	3,700	3,700
R0560	Notional MCR	8,025	3,700

Source: Template S.28.02.01

The total net (of reinsurance) written premiums in the last 12 months in Non-life activities amounted to €47.64 million while the total capital at risk for all life (re)insurance obligations amounted to €1,000.50 million.

The MCR which is the level of capital that guarantees a minimum level of security below which the amount financial resources should not fall, has a value of €8.03 million in activities of non-life and €0.73 million for life activities.

The maximum and minimum levels of MCR are €14.14 and €7.86 million, respectively. The combined notional MCR reaches a value of €8.75 million.

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

MMS did 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 any internal model used

MMS does not make use of internal models in its Solvency calculations, but follows the Standard Solvency II Formula**.**

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

At 31st December 2016, MMS had a good solvency position and therefore, it was considered unnecessary to adopt any other action or corrective measure.