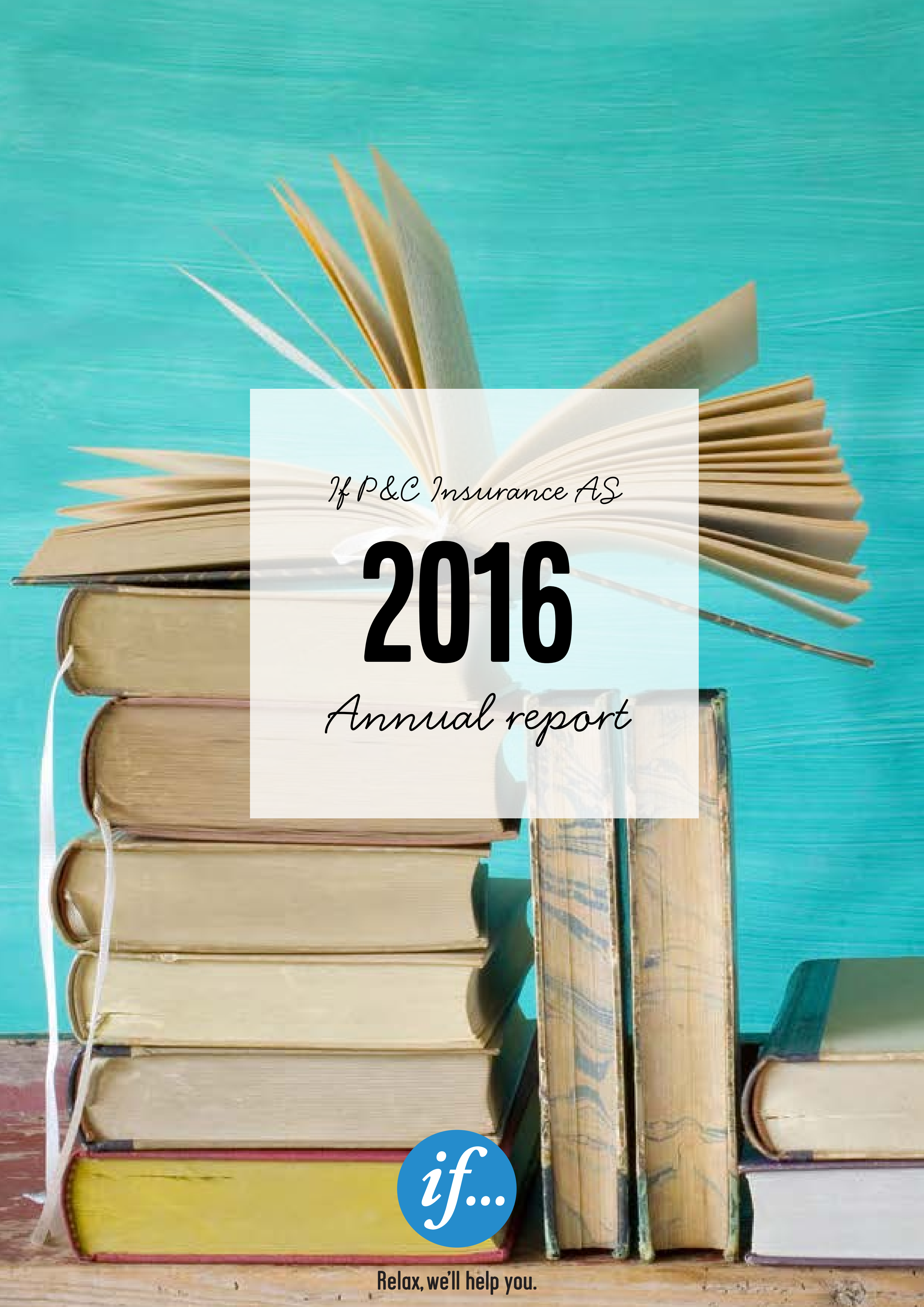
If P&C Insurance AS

2016

Annual report



Relax, we'll help you.

ANNUAL REPORT 2016

Translation from Estonian original

Business name:	If P&C Insurance AS
Registry code:	10100168
Address:	Lõõtsa 8a, 11415 Tallinn
Telephone:	+372 667 1100
E-mail:	info@if.ee
Web page:	www.if.ee
Main field of activity:	non-life insurance services
Beginning of financial year:	1 January 2016
End of financial year:	31 December 2016
Chairman of the Management Board:	Andris Morozovs
Auditor:	Ernst & Young Baltic AS

TABLE OF CONTENTS

MANAGEMENT REPORT

Organization

"If P&C Insurance AS" (the Company, "If") is wholly owned subsidiary of the leading Nordic P&C insurance group "If P&C Insurance Holding Ltd (publ)", which is itself owned by "Sampo Plc", a Finnish company listed on the Helsinki Stock Exchange. Furthermore Sampo Group is also the major shareholder of the Nordea banking group. In addition to the property and casualty insurance operations within If, Sampo Group also provides life insurance via Mandatum Life.

If has been offering property and casualty insurance in the Baltic markets since 1992 both for private individuals and corporate customers. If has approximately 320,000 policyholders across the Baltic countries and is the market leader in Estonia.

The company is Estonian registered operating in Latvia and Lithuania through branches. The current corporate structure enables efficient operations and claims handling across the Baltic region. Some of the business functions are common for all three Baltic countries, however each country has its own independent sales and customer service functions.

Legal structure of the company

If P&C Insurance AS (Estonia)
reg. no. 10100168

Branch in Latvia
If P&C Insurance AS Latvijas filiāle
reg. no. 40103201449

Branch in Lithuania
If P&C Insurance AS filialas
reg. no. 302279548

Five-year summary

€000	2016	2015	2014	2013	2012
Premiums written, gross	130,781	133,200	122,574	116,906	115,166
Premiums earned, net of reinsurance	130,729	126,545	118,647	112,877	110,954
Claims incurred, net of reinsurance	83,716	75,433	66,947	68,248	65,123
Operating expenses[1]	34,041	33,862	36,218	32,165	31,509
Technical result[2]	12,971	17,250	15,482	12,463	14,323
Net profit	13,589	19,926	17,016	13,241	20,675
Combined ratio[3]	90.1%	86.4%	87.0%	89.0%	87.2%
Expense ratio[4]	26.1%	26.8%	30.5%	28.5%	28.5%
Loss ratio[5]	64.0%	59.6%	56.5%	60.5%	58.7%
Financial investments	244,971	235,574	223,279	198,805	184,710
Return on investments[6]	1.4%	1.1%	2.3%	0.5%	3.9%
Total assets	275,508	265,144	245,166	225,376	215,315
Owner's equity	135,528	126,757	113,598	97,163	91,278

FORMULAS

[1]Operating expenses	Insurance contract acquisition costs and administrative expenses (+) reinsurance commissions and other income
[2]Technical result	Premiums earned, net of reinsurance (-) claims incurred, net of reinsurance (-) operating expenses
[3]Combined ratio	Expense ratio + loss ratio
[4]Expense ratio	$\frac{\text{Operating expenses}}{\text{Premiums earned, net of reinsurance}}$
[5]Loss ratio	$\frac{\text{Claims incurred, net of reinsurance}}{\text{Premiums earned, net of reinsurance}}$
[6]Return on investments	$\frac{\text{Investment income (-) investment expenses (+) changes in fair value recognized in other comprehensive income}}{\text{Weighted average volume of financial investments in the period}}$

Results from operations

RESULTS

Despite uncertainties in the global economy, the Baltics have experienced economic growth. If faced a challenging year, largely due to negative claims development and strategic change in sales channel distribution.

In 2016, the technical result decreased by comparison to the year before with €13.0 million recorded as opposed to €17.3 million in 2015. This decrease can be attributed to a decline in premiums that was not fully offset by reduced operating costs. General claims expenditure in 2016 was in line with expectations but higher than the extraordinarily low expenditure recorded in 2015. Large claims expenditure was as expected, however, in Motor lines both the average cost per claim and claims frequency increased.

PREMIUMS WRITTEN

The Company's gross written premiums decreased by €2.4 million from €133.2 million in 2015 to €130.8 million. Premium volumes increased in Lithuania, however, this was offset against a decrease in both Estonia and Latvia. Growth was primarily noted in the large accounts segment, accident and health insurance lines. Overall market profitability worsened throughout the year. Careful risk assessment and targeted price increases, mainly on Motor lines, resulted in decreasing premium volume.

CLAIMS AND OPERATING EXPENSES

Claims expenditure, inclusive of claims handling costs, increased by €8.3 million from €75.4 million to €83.7 million.

The loss ratio, inclusive of claims handling costs, deteriorated during 2016 and amounted to 64.0% as opposed to 59.6% in 2015. Large claim expenditure met with expectations and loss ratios improved in Property, Marine and Transportation lines mainly due to a lower level of large claims, however, motor products deteriorated due to increased claims frequency.

Operating expenses, exclusive of claims handling costs, increased slightly by €0.1 million to €34.0 million against €33.9 million in 2015, yet the company's expense ratio decreased to 26.1% from 26.8%.
The continued focus on efficiency improvements compensated for the relatively high salary expenditure and the general effects of inflation.

The combined ratio worsened to 90.1% from 86.4% in 2015 owed to the increased frequency of claims in the motor sector.

NET PROFIT AND TAX

The overall net profit after tax stood at €13.6 million in 2016, down from €19.9 million in 2015. Current tax accounted for €0.66 million a reduction from €0.81 million in 2015.

INVESTMENT RESULT

The value of financial investments stood at €245.0 million as 31st of December 2016, which is €117.0 million higher than the obligated amount stipulated under insurance contracts net of reinsurance.

Applying the full market valuation, profit from asset management increased to €3.36 million up from €2.52 million in 2015 with a return ratio of 1.4% compared to 1.1% previously. Net investment return amounted to €1.28 million as opposed to 2015's €3.49 million on the income statement, whilst €2.08 million was recorded under other comprehensive income up from €-0.97 million in 2015.

The average weighted credit rating for the holdings of the investment portfolio as 31st of December 2016 was A- using Standard & Poor's scale, down from A as 31st of December 2015. The portfolio running yield remained constant at 0.9%, however, duration rose to 1.6 years as opposed to 1.2 years in 2015.

The prevailing low interest rate environment is a serious challenge for the investment portfolio. The strong involvement of the European Central Bank in the fixed income markets has resulted in a downward spiral for European short and long term rates, which means that it is increasingly difficult to re-invest maturing instruments at attractive levels. However, our investment focus remains unchanged, i.e. we seek to find new opportunities in the European investment grade bond markets and plan to re-invest maturing bonds into medium term instruments.

Solvency capital

Starting from 1st of January 2016, the methodology for calculating the Solvency Capital Requirement has changed. This was due to a new Insurance Activity Act, reflecting Solvency II Directive requirements entering into force. The Company has been using the standard formula approach for regulative Solvency Capital Requirement (SCR)[1] calculations since 1st of January 2016. All regulatory solvency requirements have been met by the Company.

The Company will publish its first yearly solvency and financial condition report ("SFCR") in May 2017.

Risk management

Risk is an essential and inherent element of the Company business activities and operating environment. A high quality Risk Management is a prerequisite for running the business and for assuring a stable result and the delivery of the long term return targets.

The objective of Risk Management is to create value for the company's stakeholders by securing its long-term solvency, minimizing the risk of unexpected financial loss. Risk management provides input for business decision-making by taking into account the effects on risk and capital.

In 2016 the Company has implemented the Solvency II narrative and qualitative reporting to the Financial Supervision Auhtority.

The Company's risks, exposures and risk management are described in Note 2.

---

1 The Solvency Capital Requirement (SCR) takes all quantifiable risks to which the Company is exposed into account. It covers existing business, as well as the new business expected to be written over the following 12 months. SCR corresponds to the Value-at-Risk of the basic own funds of the Company subject to a confidence level of 99,5 % over a one-year horizon.

Personnel

The insurance industry is developing rapidly in light of digitalization and changing customer behavior. As a result, jobs in the insurance industry are evolving and becoming more complex, requiring multifaceted leaders and increasingly competent employees.

Our employees provide the front line for our customers and must be able to offer astute advice on a range of insurance matters. Our first class customer focus can only be achieved with dedicated staff who possess high levels of insurance industry competency.

The HR strategy of If is based on four core areas: employeeship, leadership, competence development and ensuring the right person is utilized in the right place.

A modern and complex service organization like If with competent and highly trained staff increasingly requires individual employees to take full responsibility for their own performance and development. We call this "employeeship". Implementing Employeeship within If and making it a cornerstone of our culture is a key priority.

In contemporary business, the needs for a more holistic leadership approach are increasing. In addition to strong skills in traditional management, today's business leader must also be able to help highly skilled specialists reach their full potential through nurturing their own internal and intrinsic motivation.

We have adapted If's leadership model over the years in light of the increased importance of intrinsic motivation, realizing high levels of performance is rely on an employee's inner drive, motivation and commitment.

The mature insurance industry has long reached maturity, meaning that having the industry's most competent employees is the key source of sustainable competitive advantage. Thus planning and delivery of competence development has been an important focus area.

The war for talent is increasing in the Baltic labor markets and thus the company needs to focus on employer branding activities in order to both attract and retain the best employees. The result of bi-annual employee survey Temper indicates that people enjoy working for If and are happy to recommend If both as employer and as insurance provider.

By 31st of December 2016 the number of full time employees in the company had risen to 572 from 545 in 2015.

The company's expenses for personnel totaled €19.3 million in 2016, an increase of €0.3 million over the year.

Outlook

The outlook for Baltic economic development is relatively good. Private consumption will continue to drive the economic growth, whilst continued wage increases combined with low inflation will fuel the economy. Export volumes are expected to improve gradually, and investments are expected to recover from the currently low level.

Insurance market volumes are expected to grow faster than GDP, partly due to premium rate increases as a result of the poor market profitability. Baltic insurance market consolidation accelerated past years, the market consolidation is expected to result in an improved financial discipline and results.

Operations

If provides a complete range of P&C insurance products to corporate and private customers in the Baltics, working directly via sales points, telephone and the internet. Furthermore, If utilizes a network of brokers and partners. Sales and customer service staff are located in central offices throughout the region and today If has the third largest insurance portfolio among all P&C insurance providers in the Baltic States.

One of the fastest growing sales channels is Internet sales. In 2016, Internet sales amounted to almost 200,000 policies and gross written premium grew by 22% compared to 2015. During 2016, If continued to invest in its online capabilities and is committed to bringing additional customer friendly solutions to the market. In addition, the Partner sales channels were developed further through product launches and system improvements.

The updated Insurance Activity Act, which came into force 1st of January 2016 in Estonia, favors increased transparency and customer protection within the insurance market. Consequently, If changed its co-operation model with its brokers. Going forward cost and payment for broker services will be an engagement directly handled between broker and consumer, making it visible the standalone costs for broker services.

A key goal for If is to create industry leading customer experience across all business lines, particularly when policyholders have need to submit a claim. Each claim case is closely monitored and the reporting claimant is offered the opportunity to provide feedback through submitting a grade and commenting on their experience. These surveys show that customers who have had an insurance claim are even more satisfied with If than those who have never reported a claim.

If constantly considers the importance of safeguarding human rights, preventing corruption and other social and environmental aspects. In accordance, If has established policies and processes including, but not limited to, Ethics Policy, Code of Conduct, Baltic Guideline on Avoidance of Conflicts of Interest, Baltic Guideline for Fit and Proper Assessment, Anti-Money Laundering and Anti-Terrorist Financing Policy and Competition Compliance Instruction and Environment Policy.

As a leading insurance company in the Baltics, If is aware of its social responsibility. Through sponsorships and funding, the Company is making consistent contributions to projects related to claims prevention. If is also raising awareness of insurance products in society, particularly in areas where insurance coverage is low.

In 2016, If Insurance celebrated 150 years of operating in Estonia – the roots of the predecessors of If Insurance reach back to 1866 with the establishment of *Tallinna Alevite Vastastikuse Tulekinnituse Selts* (Mutual Fire Insurance Society of Tallinn Suburbs). Throughout the year, communication and marketing activities were carrying the message of If's anniversary year. The focus was on If being a highly reliable financial enterprise with a long history and extensive experience, and having offered a sense of assurance to Estonians throughout five generations. If has gained its customers' loyalty thanks to excellent claims handling and a better sense of security. Research confirms that regionally, If Insurance is the most widely known insurance company with the highest customer satisfaction level. If Insurance will continue to improve and ensure the company's quality enables us to both retain and build upon this position in the future.

Continued branding activities have helped to maintain If brand awareness in an increasingly competitive environment. New employer branding communication and activity plans have been launched and indeed If received an "Excellent Employer DNS" award from recognized Latvian Human resources professionals. New If safety fund advice videos and donation campaigns have helped to build If attractiveness on social media, promote engagement and increase the number of social media followers by 25%.

In Lithuania nearly all private customers are now served through remote channels, totaling over 90%. The small remaining part of private customers are able to contact sales or claims personnel, based in regional offices, via Skype. This has moved If closer to realizing the goal of having a fully dedicated regional sales force to serve commercial customers.

If has continued in its quest to improve efficiency and benefit from common IT systems. In 2016 defunct local systems were closed and replaced by modern common IT solutions with full online customer support.

Applied accounting principles

The 2016 Financial Statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) adopted by the EU.

The financial statements include the accounts of the Estonian company with its branches.

Heinar Olak
Member of the Management Board

Artur Praun
Member of the Management Board

FINANCIAL STATEMENTS

Statement of comprehensive income

€000	Note	2016	2015
PREMIUMS EARNED, NET OF REINSURANCE			
Premiums earned		133,298	129,531
Premiums ceded		-2,569	-2,986
TOTAL	3	**130,729**	**126,545**
OTHER INCOME			
Return on investments	4	1,282	3,485
Reinsurance commissions and other income		254	276
TOTAL		**1,536**	**3,761**
TOTAL REVENUE		**132,265**	**130,306**
CLAIMS INCURRED, NET OF REINSURANCE			
Claims incurred, gross	5	-84,151	-75,750
Reinsurer's share in claims paid	5	435	316
TOTAL		**-83,716**	**-75,434**
EXPENSES			
Insurance contract acquisition costs	6	-22,480	-22,444
Administrative expenses	6	-11,816	-11,694
TOTAL		**-34,296**	**-34,138**
TOTAL CLAIMS AND EXPENSES		**-118,012**	**-109,572**
NET RESULT BEFORE TAXES		**14,253**	**20,734**
INCOME TAX	14	-664	-809
NET PROFIT FOR THE FINANCIAL YEAR		**13,589**	**19,925**
OTHER COMPREHENSIVE INCOME TO BE RECLASSIFIED TO PROFIT AND LOSS IN SUBSEQUENT PERIODS:			
Change in the value of available-for-sale assets	4	2,082	-966
TOTAL		**2,082**	**-966**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**15,671**	**18,959**

The notes to the financial statements set out on pages 14 to 60 form an integral part to the financial statements.

Statement of financial position

€000	Note	31.12.2016	31.12.2015
ASSETS			
Cash and cash equivalents		12,178	10,115
Financial investments	9	244,971	235,574
Receivables related to insurance activities	7	11,097	12,195
Accrued income and prepaid expenses	8	3,734	3,947
Reinsurance assets	13	2,717	2,308
Deferred tax asset	14	128	152
Investment in subsidiary	15	88	88
Property, plant and equipment	10	595	765
TOTAL ASSETS		**275,508**	**265,144**
LIABILITIES AND OWNER'S EQUITY			
Liabilities related to insurance activities	11	4,878	5,553
Accrued expenses and prepaid revenues	12	4,490	4,517
Liabilities arising from insurance contracts	13	130,612	128,317
TOTAL LIABILITIES		**139,980**	**138,387**
Share capital		6,391	6,391
Share premium		3,679	3,679
Mandatory reserve		2,362	2,362
Revaluation reserve		3,503	1,421
Retained earnings		106,004	92,979
Net profit for the year		13,589	19,925
TOTAL OWNER'S EQUITY	16	**135,528**	**126,757**
TOTAL LIABILITIES AND OWNER'S EQUITY		**275,508**	**265,144**

The notes to the financial statements set out on pages 14 to 60 form an integral part to the financial statements.

Statement of changes in equity

€000	Share capital	Share premium	Mandatory reserve	Fair value reserve	Retained earnings	Net profit for the year	Total equity
EQUITY AT BEGINNING OF 2015	**6,391**	**3,679**	**2,362**	**2,387**	**98,779**	**-**	**113,598**
Paid dividends	-	-	-	-	-5,800	-	**-5,800**
Other comprehensive income	-	-	-	-966	-	-	**-966**
Profit for the year	-	-	-	-	-	19,925	**19,925**
EQUITY AT END OF 2015	**6,391**	**3,679**	**2,362**	**1,421**	**92,979**	**19,925**	**126,757**
EQUITY AT BEGINNING OF 2016	**6,391**	**3,679**	**2,362**	**1,421**	**112,904**	-	**126,757**
Paid dividends	-	-	-	-	-6,900	-	**-6,900**
Other comprehensive income	-	-	-	2,082	-	-	**2,082**
Profit for the year	-	-	-	-	-	13,589	**13,589**
EQUITY AT END OF 2016	**6,391**	**3,679**	**2,362**	**3,503**	**106,004**	**13,589**	**135,528**

The notes to the financial statements set out on pages 14 to 60 form an integral part to the financial statements.

Statement of cash flows

€000	Note	2016	2015
CASH FLOW FROM OPERATING ACTIVITIES			
Premiums received	3, 7, 11	131,062	132,472
Premiums ceded	3, 11	-2,912	-2,867
Claims paid, incl. claims handling expenses	5, 6, 7	-78,888	-73,309
Cash flow from reinsurance		254	1,410
Employee-related and service-related expenses		-33,896	-34,480
Investments in bonds and other interest-bearing securities		-47,839	-131,630
Proceeds from disposals of bonds and other interest-bearing securities		37,376	118,915
Investments in term deposits		-25,000	-36,000
Proceeds from term deposits		27,500	34,700
Dividends received		-	2,000
Interest received		2,563	2,853
Income tax paid	14	-1,053	-1,164
CASH FLOW FROM OPERATING ACTIVITIES		**9,167**	**12,900**
TOTAL CASH FLOW FROM INVESTING ACTIVITIES			
Purchase of property, plant and equipment		-206	-344
Proceeds from disposal of property, plant and equipment		2	6
CASH FLOW FROM INVESTING ACTIVITIES		**-204**	**-338**
CASH FROM FROM FINANCING ACTIVITIES			
Paid dividends	16	-6,900	-5,800
CASH FLOW FROM FINANCING ACTIVITIES		**-6,900**	**-5,800**
CHANGE IN CASH FLOW		**2,063**	**6,762**
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR		**10,115**	**3,353**
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		**12,178**	**10,115**

The notes to the financial statements set out on pages 14 to 60 form an integral part to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

Note 1. Accounting principles and basis of estimations used in the preparation of the financial statements

1. THE COMPANY AND ITS ACTIVITIES

If P&C Insurance AS is an insurance company which has registered address at Lõõtsa 8a, Tallinn (Republic of Estonia) and includes the Estonian company and its branches in Latvia and Lithuania (hereinafter the Company).

The main activity of If P&C Insurance AS is the provision of non-life insurance services. The Company's primary operations are described in the Management report.

The financial statements of the Company for the year ended 31 December 2016 were authorized for issue in accordance with a resolution of the Management Board on 15 February 2017.

2. BASIS OF PREPARATION

The 2016 financial statements of the Company have been prepared in accordance with the International Financial Reporting Standards (IFRS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) as endorsed by the European Union. The financial statements have been prepared on a historical cost basis, except for certain financial investments which have been measured at fair value.

The financial statements values are presented in Euros and all values are rounded to the nearest thousand (€000), except when otherwise indicated.

The Annual Report which is prepared by the Management Board and reviewed by the Supervisory Board and includes the financial statements, is approved by the General Shareholder's Meeting in accordance with the Commercial Code of the Republic of Estonia. Shareholders have the right not to approve the Annual Report prepared by the Management Board and reviewed by the Supervisory Board, and demand preparation of a new Annual Report.

Though the Company forms group together with its subsidiary Support Services AS, the Company has elected in accordance with IFRS 10 paragraph 4 not to present consolidated financial statements and to present only separate financial statements. The Company is a wholly –owned subsidiary of If P&C Insurance Holding Ltd (publ) and the parent produces consolidated financial statements available for public use that comply with International Financial Reporting Standards (IFRS) as adopted by the EU. Consolidated financial statements of the parent are available at website www.sampo.com under section Annual report.

The financial statements include the accounts of the insurance company in Estonia and the accounts of its branch offices in Latvia and Lithuania. Branches use the same accounting principles in all material aspects applied for the Company as a whole. All in-house balances and transactions, unrealised gains and losses resulting from those transactions between the Estonian unit, the branch in Latvia and the branch in Lithuania are eliminated in full.

3. CHANGES IN ACCOUNTING POLICY, ESTIMATES AND DISCLOSURES

The financial statements are composed based on consistency and comparability principles, which means that the Company continually applies same accounting principles and presentation. Changes in accounting policies and presentation take place only if these are required by new or revised IFRS standards and interpretations or if new accounting policy and/or presentation give more objective overview of financial position, financial results and cash flows of the Company.

3.1. Adoption of new and/or changed International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations

The accounting policies and presentation adopted in preparation of the current financial statements are consistent with those of the previous financial year. The Company has not made use of the amendments to IAS 27 Separate Financial Statements, IAS 16 Property, Plant & Equipment and IAS 38 Intangible assets: Clarification of Acceptable methods of Depreciation and Amortization. The Company has made use of the amendment to IAS 1: Disclosure Initiative and chosen not to disclose insignificalt items in the development of claims note. IASB has issued the Annual Improvements to IFRSs 2010-2012 Cycle and 2012-2014 Cycle. None of these had an effect on the Company's financial statements.

3.2. New standards and interpretations issued but not yet effective

Issued, but not yet effective, international accounting standards are assessed not to cause any significant impact on the financial statements when first applied, except IFRS 9 Financial Instruments, and to a certain extent, IFRS 16 Leases.

IFRS 9 has been adopted for use in the EU but in a published, not yet adopted, amendment to IFRS 4 Insurance contracts, the IASB has decided that in certain circumstances insurance companies can delay their first application of IFRS 9. The Company fulfils these conditions and plan to implement the standard later than its ordinary effective date 1 January 2018. Therefore, no significant effects on The Company's accounts from making a transition from IAS 39 to IFRS 9 are expected until 2021, although some expanded disclosures will be added in 2018. Since e.g. the notion of business model will be important and the Financial Instruments standard includes some optionality, The Company believes that there will be significant cross-influences to the new, not yet finalized standard for Insurance Contracts that need to be carefully assessed.

Regarding IFRS 16, a first and preliminary assessment shows an immaterial effect on The Company's profit and loss and a limited effect on the balance sheet.

4. MATERIAL JUDGMENTS, ESTIMATES AND RESOLUTIONS

Preparation of financial statements requires the passing of resolutions on the basis of judgments and estimates. These judgments and estimates have an effect on the assets and liabilities recorded at balance sheet date, and the income and expenses of the financial year. Although the judgments are based on the management's best knowledge as well as concrete facts, the actual results may differ from the estimates.

EVALUATION OF LIABILITIES FROM INSURANCE CONTRACTS

Judgments are made both for establishing technical provisions for the incurred and reported losses as of the balance sheet date, and for accounting for the provisions for not reported losses. The time period during which the final claims are incurred may be extensive. In all insurance categories, the provision for claims consist of incurred but not reported losses. Forecasts regarding provisions for future claims are based on the claims actually incurred in previous periods. Each balance sheet date, estimates on technical provisions for claims in previous periods are revaluated, with any changes reported in the statement of comprehensive income. The provisions for claims are not changed explicitly in accordance with fluctuations in the value of money over time.

As of the end of 2016, gross insurance technical provisions amounted to €130,612 thousand (2015: €128,317 thousand), of which the reinsurer's share amounted to €2,717 thousand (2015: €2,308 thousand). Insurance technical provisions have been described in Note 1 section 5.

5. MAIN ACCOUNTING PRINCIPLES

A) ACCOUNTING FOR THE SUBSIDIARY IN THE COMPANY'S FINANCIAL STATEMENTS

Investments in subsidiary are recognized in the Company's financial statements at cost less impairment (if any). This means that the investment is initially recognized at acquisition cost, consisting of the fair value of the payable amount, adjusted thereafter by the impairment losses arising from the drop in the value of the investment.

Impairment tests are conducted in order to determine whether or not the recoverable amount of the investment (the higher of the fair value less sales expenses, or value-in-use) has dropped below the carrying value, if there is any indication that the carrying amount may not be recoverable.

B) TRANSACTIONS IN FOREIGN CURRENCY

The financial statements are presented in Euros, which is the functional and reporting currency of the Company. Foreign currency transactions are translated into Euro on the basis of the exchange rates of the European Central Bank.

C) REVENUE RECOGNITION

Revenue is recognized at the fair value of the received or receivable income. Revenue from sales of services is recorded upon rendering of the service.

Interest income is recorded on an accrual basis, based on the effective interest rate of the asset item. Dividend income is recognized when the respective right of claim arises.

Insurance premiums

The collected insurance premiums are recorded upon entry into force of the insurance policy and adjusted with the changes in prepaid premiums, calculated based on the pro rata method. Premiums written are premiums received and receivable under the insurance contracts or, in case of installment payments, those installment payments with the due date in the accounting period. If the due date of the first installment payment is later than the effective date of the contract, the recognition of insurance premiums will be based on the effective date of the contract. Insurance premiums and installment payments received for contracts whose effective date is later than the balance sheet date, are recognized as a prepayment. There are differences in the recognition of insurance premiums in Estonia comparing to Latvia and Lithuania. The majority of first installments of insurance premium in Estonia are recognized after the cash receipt from the client, but in Latvia and Lithuania first installment of insurance premium is recognized in gross written premium on an accrual basis. This difference has no material impact on the financial results of the Company because the lag between signing the policy and receiving the first installment from the policyholder is in period 1-15 days and significant part of the amount is deferred as unearned premium provision (UPR).

Reinsurance commissions

Reinsurance commission fees consist of the commission fees received from reinsurers under the reinsurance contract.

D) EXPENSES

The Company's expenses are divided according to their function as follows:

- Insurance contract acquisition costs – direct and indirect expenses arising from the acquisition of insurance contracts, incl. direct expenses, such as commission fees for mediators, expenses on preparation of insurance documents as well as indirect expenses, such as advertising expenses, administrative expenses related to the processing of applications and issue of policies.
- Claims handling expenses – consist of administrative expenses indirectly related to claims handling. Claims handling expenses include the respective expenses incurred by the insurer, incl. wages and salaries, social tax and administrative expenses related to claims handling.
- Administrative expenses include insurance-related expenses which do not constitute acquisition costs or claims handling expenses.

Claims handling expenses are included in claims paid in the statement of comprehensive income.

Insurance contract acquisition costs have been adjusted with the changes in the deferred acquisition costs, net of reinsurance.

E) CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents consists of bank balances and overnight deposits.

The cash flow statement is prepared based on the direct method.

F) FINANCIAL ASSETS

Initial recognition and measurement

Financial assets are classified in the following categories upon the initial recognition:

- financial assets measured at fair value through profit or loss (financial assets held for trading or designated upon initial recognition at fair value through profit or loss);
- loans and receivables (deposits, accounts receivable and other receivables);
- investments held-to- maturity (financial assets which are non-derivative instruments and have fixed or determinable payments and fixed terms of redemption, provided that the company is planning to and is capable of holding the assets to maturity);
- available–for-sale financial assets (all other financial assets that are designated as available for sale or not mentioned above into any other category).

Financial assets are recognized initially at fair value plus, in case of investments not at fair value through profit or loss, directly attributable transaction costs.
Financial assets at fair value through profit or loss were assets held for trading except for certificates of deposits which were designated upon initial recognition at fair value through profit or loss.

The Company has classified time deposits as loans and receivables.

The Company has not classified any financial assets as "investments held to maturity" in the reporting or comparative period. The Company had no derivative instruments.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the marketplace (regular way trades) are recognised on the trade date, i.e., the date that the Company commits to purchase or sell the asset.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss are assets which held for trading except for certificates of deposit which are designated upon initial recognition at fair value through profit or loss.
For investments designated as at fair value through profit or loss, the following criteria are met:

- the assets are part of a group of financial assets, which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.

These investments are initially recorded at fair value. Subsequent to initial recognition, they are remeasured at fair value on the balance sheet date. Gains and losses arising from changes in fair value, or realized on disposal, together with the related interest income, are recognized under “Return on investments” in the statement of comprehensive income.
The Company evaluates its financial assets at fair value through profit and loss (held for trading) whether the intent to sell them in the near term is still appropriate.

When the Company is unable to trade these financial assets due to inactive markets and management’s intent to sell them in the foreseeable future significantly changes, the Company may elect not to classify newly purchased financial assets in the fair value through profit or loss category. This evaluation does not affect any financial assets designated at fair value through profit or loss using the fair value option at designation.

The fair value of listed securities is based on the bid price of the security on the balance sheet date. If a market for a financial instrument is not active, or the instrument is not quoted, the fair value is established by using generally accepted valuation techniques.

Available-for-sale financial assets

Debt securities in this category are those that are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale financial assets are subsequently measured at fair value, with unrealised gains or losses recognised in other comprehensive income in the available-for-sale reserve (equity). Where the insurer holds more than one investment in the same security that they are deemed to be disposed of on a first-in first-out basis. Interest earned whilst holding available-for-sale investments is reported as interest income using the effective interest rate (EIR).When the asset is derecognised the cumulative gain or loss is recognised in return of investments, or determined to be impaired, or the cumulative loss is recognised in the statement of comprehensive income and removed from the available-for-sale reserve.

Loans and receivables

Loans and receivables comprise non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Company does not intend to sell immediately or in short term. Loans and receivables are initially recognized at cost which is the fair value of the consideration given, including transaction costs that are directly attributable to the acquisition of the asset. Loans and receivables are subsequently measured at their amortized cost by using the effective interest rate method. Amortized cost is calculated by taking into account any discount or premium on acquisition, as well as expenses directly related to the transaction, over the year to maturity.

Interest income from loans, receivables and deposits is recorded under "Return on investments" in the statement of comprehensive income.

Receivables from customers, reinsurance receivables and other receivables are recognized at nominal value when incurred (on the transaction date), and, subsequent to initial recognition, at cost less applicable impairment. Receivables are measured on an individual basis.

<u>Derecognition of financial assets</u>

A financial asset (or, when applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired

Or

- The Company retains the right to receive cash flows from the asset and has assumed an obligation to pay the received cash flows in full without material delay to a third party under a ‘pass-through’ arrangement;

  and either:

  - The Company has transferred substantially all the risks and rewards of the asset

  Or

  - The Company has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Company has transferred its right to receive cash flows from an asset or has entered into a passthrough arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Company’s continuing involvement in the asset.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

In that case, the Company also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Company has retained.

Impairment of financial assets

The Company assesses at the end of each reporting period whether there is any objective evidence that a financial asset, other than those at fair value through profit and loss, may be impaired.
A financial asset is impaired and impairment losses are incurred, if there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset, and if that event has an impact, that can be reliably estimated, on the estimated future cash flows of the financial asset.

There is objective evidence of impairment, if an issuer or debtor e.g. encounters significant financial difficulties that will lead to insolvency and to estimation that the customer will probably not be able to meet the obligations to the Company.

When there is objective evidence of impairment of a financial asset carried at amortized cost, the amount of the loss is measured as the difference between the receivable's carrying amount and the present value of estimated future cash flows discounted at the receivable's original effective interest rate. The difference is recognized as an impairment loss in profit or loss. The impairment is assessed individually.

Impairment loss of financial assets related to operating activities is charged to expenses in the statement of comprehensive income (under "Administrative expenses") while the impairment loss of financial assets related to investing activities is recognized as a reduction of the "Return on investments" in the statement of comprehensive income.

If, in a subsequent period, the amount of the impairment loss decreases, and the decrease can objectively be related to an event occurring after the impairment was recognized (e.g. default status is removed), the previously recognized impairment loss shall be reversed through profit or loss.

Financial assets carried at amortised cost

For financial assets carried at amortised cost, the Company first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Company determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

Available-for-sale financial investments

For available-for-sale financial investments, the Company assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.
In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of comprehensive income.

Future interest income continues to be accrued based on the reduced carrying amount of the asset and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the statement of comprehensive income.

G) PROPERTY, PLANT AND EQUIPMENT

Assets with a useful life of over one year are recorded as property, plant and equipment (PPE). PPE are initially recorded at acquisition cost, consisting of purchase price (incl. customs duties and other non–refundable taxes) and expenses directly related to the acquisition, incurred upon bringing the assets to their present condition and location.

Following initial recognition, an item of PPE is carried in the balance sheet at its cost, less accumulated depreciation and any accumulated impairment losses. If the recoverable amount of the non-current asset item drops below its carrying amount, the asset will be written down to its recoverable amount (the higher of the fair value, less sales expenses, or the value-in-use). Impairment tests will be conducted to determine whether the recoverable amount has dropped below the carrying amount, if there is any indication that the carrying amount may not be recoverable. Impairment losses are charged to expenses in the statement of comprehensive income, under "Insurance contract acquisition costs", "Claims handling expenses", and "Administrative expenses" in accordance with the functionality.

On each statement of financial position date, the Company assesses whether there is any indication that the previous impairment is no longer justified. If there is any such indication, the Company will assess the recoverable amount and, if necessary, reverse the previous write-down. The reversal of the write-down is recorded as a reduction of the expenses during the period when the reversal occurred.

Depreciation is calculated from the moment the asset can be used for the purposes established by the management, until the assets' classification into non-current assets held for sale or removal from use. If fully amortized assets are still being used, the acquisition cost and the accumulated depreciation of the assets will be recorded in the balance sheet until the assets have been removed from use.

The depreciable amount of the PPE item (i.e. the difference between the acquisition cost and final value) is charged to expenses over the useful life of the item. Land and works of art are not depreciated. Depreciation is calculated on a straight-line basis, in accordance with the useful life of the asset item, as follows:

- Buildings 50 years;
- Computer equipment 3 years;
- Transport vehicles 5 years;
- Machinery and equipment 5-6 years;
- Office furniture and equipment 5-6 years.

If the PPE item consists of distinguishable components with different useful lives, these components are separately recorded under assets, and the depreciation rates specified separately thereof in accordance with their useful lives.

H) FINANCIAL LIABILITIES

Financial liabilities are initially accounted for at their acquisition cost consisting of the fair value of the consideration given. Following initial recognition, financial liabilities are measured at their amortized cost by using the effective interest rate method. Transaction costs are taken into consideration upon calculating the effective interest rate, and charged to expenses over the term of the financial liability. Any expenses related to the financial liability (incl. interest expenses) are charged to the expenses of the period on accrual basis.

The financial liability will be derecognized when the liability is paid, cancelled or expired.

I) INSURANCE CONTRACTS

IFRS 4 requires classification of insurance contracts into insurance and investment contracts, depending on whether the contract involves transfer of a significant insurance risk. An insurance contract is a contract under which one party accepts significant insurance risk from the policyholder by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. The Company concludes short-term insurance contracts with its customers. The main risks covered with these contracts are property damage and property destruction, personal liability, or short-term health damage.

All contracts concluded by the Company are classified as insurance contracts in the scope of IFRS 4.

J) DEFERRED ACQUISITION COSTS

Insurance contracts acquisition costs directly related to premiums that are carried over to the next period are recognized in the statement of financial position as deferred acquisition costs. Direct acquisition costs are deferred on the basis of the ratio of the provision for unearned premiums to premiums written. Deferred acquisition costs include only direct insurance contract acquisition costs, such as commission fees to mediators.

K) PROVISION FOR UNEARNED PREMIUMS

The provision for unearned premiums is set up for future losses and operating expenses that may arise during the term of the insurance contract.

The provision for unearned premiums is calculated separately for each contract, based on the share of the unexpired term of the contract of the total term of the contract.

L) PROVISION FOR CLAIMS OUTSTANDING

The provision for claims outstanding is set up for claims incurred but not yet settled, including claims incurred but not yet reported (IBNR). In order to cover claims handling expenses of incurred unsettled claims, a provision for claims handling expenses is set up under the provision for claims outstanding.

The provision for claims outstanding is calculated using case-by-case valuation method (larger reported claims) as well as statistical methods (small reported claims, IBNR provision). The provision for claims outstanding is not discounted, except the motor third party liability annuities that are discounted to the net present value using discount rate which is 0.75%.

M) REINSURANCE

The main forms of reinsurance contracts are excess-of-loss reinsurance contracts and proportional reinsurance contracts. The contracts are, as a rule, concluded for a term of one year. Reinsurance coverage is purchased in the course of standard insurance in order to minimize the potential net loss by hedging the risks. All reinsurance contracts transfer a significant portion of the insurance risk.

Reinsurance assets consist of reinsured insurance liabilities. The reinsurer's share of the provision for unearned premiums and the provision for claims outstanding has been recorded in accordance with the reinsurance contracts.

Any impairment of reinsurance assets are recorded in the statement of comprehensive income.

N) ACCOUNTING FOR LEASE

Lease transactions, where all material risks and rewards from ownership of an asset are transferred to the lessee, are treated as finance lease. All other lease transactions are treated as operating lease. The Company as the lessee had only operating lease contracts in the reporting period.

Operating lease payments are recorded during the rental period as expenses based on the straight-line method.

The Company had no assets leased out under finance or operating lease in the reporting period or in the comparative period.

O) CORPORATE INCOME TAX

Pursuant to the Estonian Income Tax Act, Estonian companies are not subjected to pay income tax on the profit since 1 January 2000. Rather, they are subjected to income tax on the paid dividends. The established tax rate is 20/80 of the net dividend paid in 2016 (2015: 20/80 of the net dividend paid).

Corporate income tax on the payment of dividends is recorded under income tax expense in the statement of comprehensive income at the moment of announcing the dividends, irrespective of the period for which the dividends were announced or when the dividends are actually paid. The maximum possible income tax liability related to dividend payment is disclosed in Note 16.

The Company tax expense is calculated in accordance with IAS 12 Income taxes. This entails that current as well as deferred tax is calculated and reported. Current taxes are calculated for every unit in accordance with the tax rules in each country. Branch offices are taxed on their results in the country concerned. In Estonia the company is liable for taxation only on the income not taxed in branches and only when dividends will be paid out. For Latvian branch tax rate is 15% (2015: 15%) and for Lithuanian branch 15% (2015: 15%).

Deferred tax attributable to temporary differences between the amounts reported and the equivalent actual taxation is reported in the company’s accounts. For income reported in the income statement for the period but which is not taxed until a later period, a deferred tax cost is charged, which results in a corresponding liability item, deferred tax liabilities. Similarly, costs that will not result in tax deductions until a later period give rise to a deferred tax revenue and a corresponding deferred tax asset. Deferred tax assets and liabilities are not reported net because they pertain to different countries tax authorities.

Current and deferred tax disclosure is made in Note 14.

P) EVENTS AFTER THE BALANCE SHEET DATE

Material circumstances that have an effect on the valuation of assets and liabilities and became evident between the balance sheet date (31 December 2016) and the date of approving the financial statements (15 February 2017), but are related to transactions that took place in the reporting period or earlier periods, are recorded in the financial statements.

Note 2. Risks and risk management

A) OVERVIEW OF COMPANY'S RISK MANAGEMENT

Risk is an essential and inherent element of the Company´s business activities and operating environment. A high quality risk management is a prerequisite for running the business and for assuring stable earnings while delivering on the long term return requirements.

Risk Strategy

Company's risk strategy forms part of the governing principles for the operations.
The risk management strategy is to:

- Ensure that risks affecting the profit and loss account and the balance sheet are identified, assessed, managed and monitored;
- Ensure that the riskiness of the insurance business is reflected in the pricing;
- Ensure adequate long term investment returns within set risk levels;
- Ensure that risk buffers, in the form of capital and foreseeable profitability, are adequate in relation to the current risks inherent in business activities and existing market environment;
- Limit fluctuations in the economic values;
- Ensure the overall efficiency, security and continuity of operations.

The Company's Risk Strategy is set by the Supervisory Board and is in line with the If Group Risk Strategy.

Risk Appetite Framework

The risk appetite framework sets the level of risk that the Company is willing to accept in the pursuit of its objectives. The framework includes the risk appetite statement, capital adequacy, policies, processes, controls, and systems through which the risk appetite is established, communicated, and monitored. Risk appetite and tolerance levels for different risk categories are implemented by the relevant Policies adopted by the Company´s Supervisory Board.

The link between the risk strategy, the risk profile and the capital is ensured through the risk appetite statement, the financial planning process, regular risk monitoring and reporting and the Own Risk and Solvency Assessment (ORSA) process.

Risk Management System

The Risk Management System within the Company forms a part of the Internal Control System and covers Estonian, Latvian and Lithuanian operations thereby giving an integrated approach to risk management throughout the Company. The Company's Risk Management System is linked with the If Group Risk Management System to enable managing the risks on the Company level and supporting the risk management on If Group level.

The objectives of the Risk Management System are to create value for the Company's stakeholders by securing long-term solvency, minimising the risk of unexpected financial loss and giving input to business decisions by continuously taking into account the effects on risk and capital.

The key to fulfilling these objectives is to:

- Identify and, in accordance with internal and external requirements, aggregate the quantifiable risks and have effective processes for management of both quantified and non-quantified risks affecting the Company and;
- Formalize and set up reporting routines to meet regulatory requirements as well as Company's internal risk reporting requirements.

Key risks affecting the Company are subject to dedicated risk management processes. The Risk Management function is responsible for coordinating the risk management activities on behalf of the Management Board.

Risk Governance and Reporting Structure

The Management Board of the Company has the ultimate responsibility for the effective implementation of the Risk Management System by ensuring appropriate risk management set-up and promoting the sound risk culture within the Company. The Management Board and the Supervisory Board, receive risk reports from the Risk Manager, take active part in the forward looking risk and solvency assessment (ORSA) process and ensure that the management and follow-up of risks are satisfactory and effective.The risk Management Function supports the implementation of the Risk Management System.
The Risk Management function set-up and reporting lines are showed in Figure 1.

For effective implementation of the Risk Management System within the Company, the three lines of defence concept is used.

First line of defence

The Heads of Unit own the risk and implement the risk mitigation actions in their day to day operations. This is regarded as the first line of defence in the Risk Management System. In each risk category the Business Risk Coordinators are appointed by the Heads of Unit to support the risk management activities including reporting to the Risk Manager.

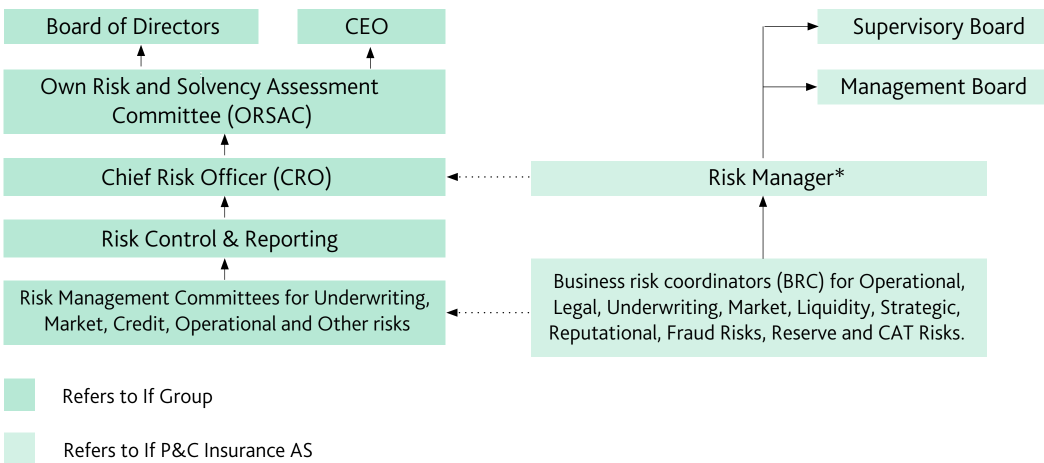
Second line of defence

The Risk Manager performs second line of defence duties by assessing, analysing and monitoring the Company level risks independently from the business operations. Additionally, the second line of defence supports the business in risk assessment, gives advice on risk mitigation actions, promotes a sound risk culture and reports regularly risk exposures to the Management Board, Supervisory Board and to the Chief Risk Officer of If Group.

Third line of defence

The Internal Audit performs third line of defence duties by giving assurance to the Supervisory Board on the effective implementation of the Risk Management System within the Company.

Figure 1. Risk management function set-up and reporting structure

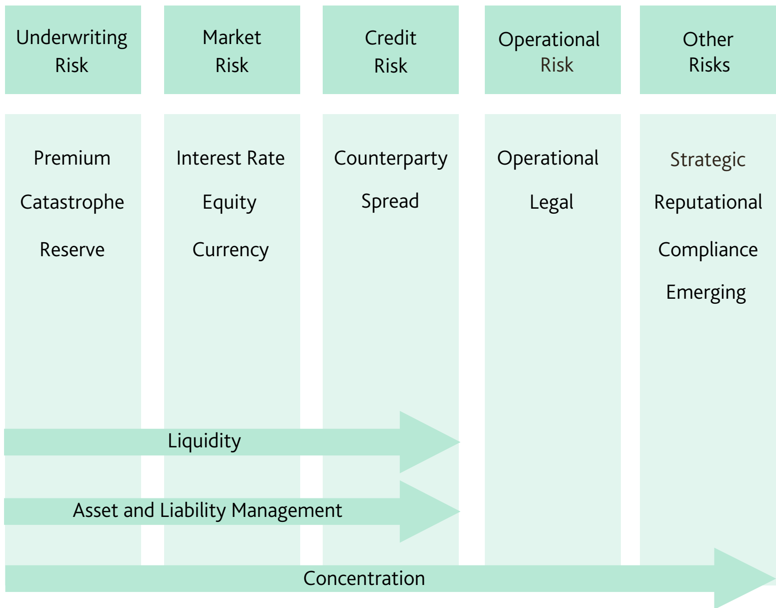


*Responsible person for Risk Management is the Risk Manager

Policies adopted by the Supervisory Board are in place for each risk area specifying restrictions and limits chosen to reflect and ensure that the risk level at all times complies with Company's overall risk appetite and capital constraints.

The main risk categories the Company is exposed are: Underwriting; Market; Credit and Operational Risks which are covered by the Risk Management System along with the Other Risks (Figure 2).

Figure 2. Categorization of risks



B) CAPITAL MANAGEMENT

The Company focuses on both capital efficiency and sound risk management by keeping its capital resources at an appropriate level in relation to the risks taken over the business planning horizon. This means ensuring that available capital exceeds the internal and regulatory capital requirements.

The company's risk profile, required capital and available capital are measured, analysed and reported to the Management Board and to the Supervisory Board on quarterly bases, or more often when deemed necessary.

Capital position

The capital position is the relationship between available capital and required capital. To fulfill requirements from supervisory authority, regulatory capital measures are used to describe the capital position.

Regulatory measures

Insurance is a regulated business with formal national rules for the capital requirement and available capital. When the Solvency II regulation entered into force on January 1, 2016, the Company started to use the Solvency II standard formula for calculating their solvency capital requirements.
The company fulfilled regulatory capital requirements during 2016.

C) UNDERWRITING RISKS

Underwriting risk is the risk of loss or of adverse changes in the value of insurance liabilities, due to inadequate pricing and provisioning assumptions.
The underwriting risk of the company is exposure to premium, catastrophe and reserve risks.

PREMIUM RISK AND CATASTROPHE RISK

Premium risk is the risk of loss or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing, frequency and severity of insured events which have not occurred at the balance date.

Catastrophe risk is the risk of loss or of adverse change in the value of insurance liabilities, resulting from significant uncertainty of pricing and provisioning assumptions related to extreme or exceptional events.

Risk Management and Control

The Company manages the underwriting risk on a day-to-day basis based on internal Underwriting policies and guidelines, which set the principles for risk selection, pricing and insurance cover.
A crucial factor affecting the profitability and risk of P&C insurance operations is the ability to accurately estimate future claims and administrative costs and thereby correctly price insurance contracts. The pricing of private segment risks and smaller corporate segment risks are set through tariffs and detailed risk selection rules. The underwriting of bigger and more complex corporate segment risks is based to a greater extent on general principles and individual underwriting. In general, pricing is based on statistical analyses of historical claims data and assessments of the future development of claims frequency and claims inflation.

The insurance portfolio is well diversified, given the fact that the Company has a large customer base and its business is underwritten in different geographical areas and across several lines of business.

Despite this diversified portfolio, risk concentrations and consequently severe claims may arise through, for example, exposures to natural catastrophes such as storms and floods. Also single large claims can potentially have a significant impact on the result. The economic impact of natural disasters and single large claims is mitigated using reinsurance.

A Nordic-wide reinsurance program has been in place in If Group and is applicable for the Company since 2003. In 2016, retention levels for the Company were €3.5 million per risk and €3.5 million per event.

Risk profile

There is a risk, given the inherent uncertainty of property and casualty insurance, that losses due to claims may be higher than expected. Examples of such events include large fires, natural catastrophes such as severe storms, floods or unforeseen increases in the frequency or the average size of small and medium-sized claims.

A sensitivity analysis of how changes in the combined ratio, premium volume and claims level affect the results before tax is presented in Table 1.

Table 1. Sensitivity analysis of premium risk, December 31, 2016

€000

Parameter	Current level, 2016	Change	Effect on pretax profit	
			2016	2015
Combined ratio	90.1%	+/-2% points	+/-2,615	+/-2,531
Premium volume	130,729	+/-2%	+/-259	+/-344
Claims level	83,716	+/-2%	+/-1,674	+/-1,509

RESERVE RISK

Reserve risk is the risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing and amount of claim settlements for events which have occurred at or prior to the balance date.

Reserve risk includes revision risk, which is defined as the risk of loss, or of adverse change in the value of insurance and reinsurance liabilities, resulting from fluctuations in the level, trend or volatility of revision rates applied to annuities, due to changes in the legal environment or in the state of health of the person insured. Technical provisions always include a certain degree of uncertainty since the provisions are based on estimates of the size and the frequency of future claim payments.

The uncertainty of technical provisions is normally greater for new portfolios for which complete run-off statistics are not yet available, and for portfolios including claims that take a long time to settle. Motor Third Party Liability (MTPL) and Liability insurance are products of the Company with the latter characteristics.

Risk Management and Control

The Management Board of the Company decides on the guidelines governing the calculation of technical provisions (Baltic Reserving Guidelines). The Company's Appointed Actuary is responsible for developing and presenting guidelines on how the technical provisions are to be calculated and for assessing whether the level of the total provisions is sufficient. The Appointed Actuary is responsible for providing relevant details on planned reserve methods' or assumptions' changes to the management as well as be able to explain the basis of existing methods or assumptions. This is done on purpose to secure a comprehensive view and additional control over reserve risk, as part of the risk management system.

The Company's reserving actuaries analyze the uncertainty of technical provisions. The actuaries continuously monitor the level of provisions to ensure that they are adequate or find out the segments where reserves' deficit or surplus is present. The actuaries also develop methods and systems to support these processes.

The actuarial estimates are based on historical claims data and exposures that are available at the closing date. Factors that are monitored include claims development trends, the level of unpaid claims, legislative amendments, case law, economic conditions and product cover specific changes. When setting provisions, the Chain Ladder and Bornhuetter-Fergusson methods are generally used, combined with projections of risk ratio in areas where claims development data is not sufficient.

The anticipated inflation trend is implicitly taken into account when calculating all provisions and is of the utmost importance for claims settled over a long period of time, such as MTPL and Liability. Inflation risk in the technical provisions is an important consideration taken into account in the investment strategy.

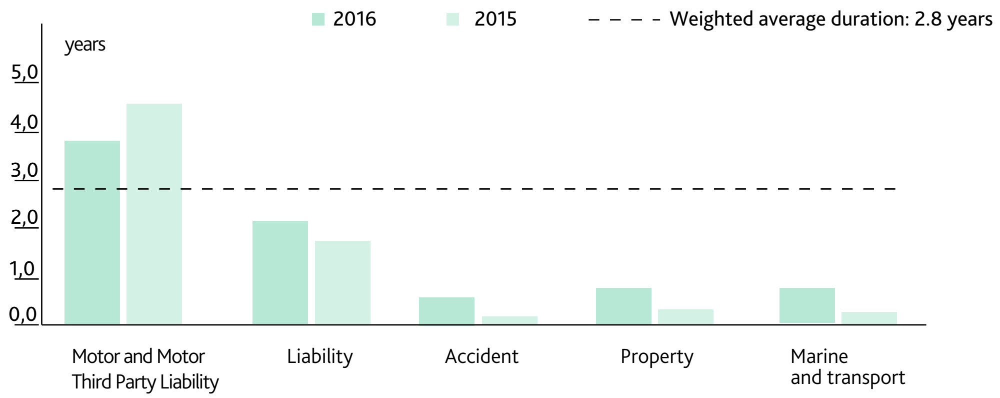
Risk profile

Table 2. Technical provisions by line of business, 31 December

€000 Line on business	Gross liabilities related to insurance contracts		Reinsurers' share of liabilities		Net liabilities	
	2016	2015	2016	2015	2016	2015
Compulsory Motor TPL	57,713	50,201	357	262	57,356	49,939
Motor Own Damage	19,442	19,884	-	-	19,442	19,884
Private Property	8,853	7,678	-	-	8,853	7,678
Corporate Property	13,722	15,151	203	193	13,519	14,958
Liability	20,440	22,969	1,960	1,759	18,480	21,210
Personal Accident	1,894	1,976	-	-	1,894	1,976
Health	3,618	4,399	-	-	3,618	4,399
Other	4,930	6,059	197	94	4,733	5,965
TOTAL	**130,612**	**128,317**	**2,717**	**2,308**	**127,895**	**126,009**

The durations of technical provisions for various products are shown in Figure 3.

Figure 3. Duration of technical provisions by line of business, 31 December



For several lines of business, technical provisions are sensitive to changes in inflation. The sensitivity of the inflation assumptions differs between countries due to different national rules. A sensitivity analysis of the reserve risk on 31 December is presented in Table 3.

Table 3. Sensitivity analysis, reserve risk, 31 December 2016

€000 Portfolio	Risk	Change in risk parameter	Country	Effect on liabilities/pretax profit 2016	2015
Nominal reserves	Inflation increase	Increase by 1%-point	Estonia	1,202	1,015
			Latvia	178	179
			Lithuania	415	401
			TOTAL	**1,795**	**1,595**
Discounted reserves (annuities)	Decrease in discount rate	Decrease by 1%-point	Estonia	1,226	1,216
			Latvia	182	128
			Lithuania	105	109
			TOTAL	**1,513**	**1,453**
Annuities	Decrease in mortality	Mortality rates decrease by 20%	Estonia	118	111
			Latvia	15	13
			Lithuania	4	4
			TOTAL	**137**	**128**

D) FINANCIAL ASSETS AND LIABILITIES

The recognition of financial assets and liabilities depend on their classification. The classification of assets and liabilities categorized in accordance with IAS 39 is shown in Table 4.

Table 4. Financial assets and financial liabilities

€000	31.12.2016	31.12.2015
Financial assets measured at fair value through profit and loss:		
Classified as held for trading		
Bonds and other interest-bearing securities	35,722	41,621
Available-for-sale financial assets		
Bonds and other interest-bearing securities	187,247	169,438
TOTAL FINANCIAL ASSETS AT FAIR VALUE	**222,969**	**211,059**
Financial assets measured at amortised cost:		
Loans and receivables		
Term deposits	22,002	24,515
Other assets		
Cash and cash equivalents	12,178	10,115
Receivables related to direct insurance activities	10,778	12,015
Accrued income	1,090	786
Receivables related to reinsurance	164	69
Other receivables	155	111
TOTAL FINANCIAL ASSETS	**269,336**	**258,670**
Financial liabilities valued at amortised cost:		
Accrued expenses	4,490	4,517
Liabilities related to direct insurance activities	3,499	4,056
Liabilities related to reinsurance	974	1,198
Other liabilities	405	299
TOTAL FINANCIAL LIABILITIES	**9,368**	**10,070**

A careful process is followed and controls are performed in order to ensure correct fair values of financial assets and liabilities. For example, controls are made by several different external sources and assessments of abnormal price changes are performed when necessary.

Different valuation methods are used to determine the fair value depending on the type of financial instruments and to what extent they are traded on active markets. The valuation of bonds is usually based on prices from Bloomberg. For a limited portion of assets, the value is determined using other techniques. The fair value of unlisted financial assets is determined on the basis of similar market transactions or, if no such transactions have been made, on the basis of the value determined by using the generally accepted valuation techniques.

Financial instruments measured at fair value have been classified into three hierarchy levels depending on their liquidity and valuation methods. The control of hierarchy levels is done quarterly and if conditions have changed for the existing level, the holding in question is moved to the correct hierarchy level. The valuation of financial assets is shown in Table 5.

Table 5. Determination of hierarchy of fair value

€000

31.12.2016	Level 1	Level 2	Total fair value
Financial assets at fair value through profit or loss			
Debt securities	35,722	-	**35,722**
Available-for-sale financial assets			
Debt securities	173,380	13,866	**187,246**
TOTAL	**209,102**	**13,866**	**222,968**

31.12.2015	Level 1	Level 2	Total fair value
Financial assets at fair value through profit or loss			
Debt securities	41,621	-	**41,621**
Available-for-sale financial assets			
Debt securities	145,329	24,109	**169,438**
TOTAL	**186,950**	**24,109**	**211,059**

Level 1 – Financial assets and liabilities with values based on quoted prices in active markets for identical assets or liabilities.
Quoted prices in active markets are considered the best estimate of an asset's fair value. An active market is typically characterized by quoted prices that are easily and regularly available and that represent actual and regularly occurring transactions at arm's length distance. In order to evaluate the activity in an market with respect to frequency and volume the Company uses information compiled and published by Bloomberg.

Assets in the category include interest-bearing assets (including government guaranteed bonds) that have noted prices on an active market at the time of valuation.

Level 2 – Financial assets and liabilities with values based on quoted prices or valuation based on directly or indirectly observable market data.
In the level 2 hierarchy all essential inputs are observable either directly or indirectly. The large majority of the instruments in level 2 are traded in a market with daily quoted prices and regularly occurring market transactions but where the market in not considered to be active enough regarding frequency and volume. A very limited part of the instruments are model valued with the help of market data that is indirectly observable, meaning that prices can be derived from observable markets where market interest rates and underlying rates normally are updated daily or, in exceptional cases, at least on a monthly basis.

Instruments which are valued at level 2 include interest-bearing assets where the market is not active enough like corporate bonds and certificates of deposit.

Level 3 - Financial assets and liabilities which are traded on an illiquid market, with non-observable market data or indications of trading levels without any actual trade.
When neither quoted prices in active markets nor observable market data is available, the fair value of financial instruments is based on valuation techniques which are based on non-observable market data.

Level 3 comprises unquoted instruments and distressed assets encountering financial difficulties.

There were no movements in Level 3 financial instruments measured at fair value in 2016.

E) MARKET RISKS

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

Risk Management and Control
The investment strategy of the Company, given the financial market environment, is to maximize long term investment returns within the levels of risk appetite and the capital allocation while meeting solvency requirements. The Investment Policy and Baltic Investment Policy adopted by the Supervisory Board annually defines the limits for asset allocation. The structure of the Company's technical provisions, risk-bearing capacities, regulatory requirements is taken into account when deciding limits and when setting return and liquidity targets. The Investment Policies also define mandates and authorizations.

Risk profile
The Company's investments operations generated a return of 1.4% in 2016 (2015: 1.1%). The investment assets amounted as at the end of the reporting period to €244,971 thousand (2015: €235,574 thousand).

The major market risk comprises interest rate risk. The Company's exposure to equity and currency risks is not material. The exposure towards market risk can be described through the allocation of investment assets and the sensitivity of values to changes in key risk factors.

Table 6. Allocation of investment assets

€000	31.12.2016	%	31.12.2015	%
Bonds and other interest-bearing securities	222,968	91%	211,059	90%
Loans and receivables (term deposits)	22,002	9%	24,515	10%
TOTAL	**244,971**	**100%**	**235,574**	**100%**

INTEREST RATE RISK
Interest rate risk refers to the sensitivity of the values of assets, liabilities and financial instruments to changes in the term structure of interest rates, or in the volatility of interest rates.

Risk Management and Control
In accordance with the If Group Investment Policy and Baltic Investment Policy, the nature of the insurance commitments with respect to interest rate risk and inflation risk, is taken into account in the composition of investment assets. The interest rate risk is managed by sensitivity limits for instruments sensitive to interest rate changes.

Since the technical provisions are predominantly stated in nominal terms in the balance sheet, the Company is mainly exposed to changes in future inflation. However, the economic value of these provisions, meaning the present value of future claims payments, is exposed to changes in interest rates. Furthermore, the provisions for annuities in Estonia, Lithuania and Latvia are discounted and potential changes in the discount rates will to some extent affect the level of technical provisions in the Company's balance sheet.

The discount rates vary between countries mainly due to legislative differences, but also due to the prevailing interest rate environment.

The company measures and monitors interest risk using the interest sensitive assets and liabilities difference method, while also applying different interest risk scenarios for the evaluation of possible losses arising from changes in the interest rates. Interest risk is defined as potential loss arising from a parallel shift in the interest curve by 1%.

Sensitivity analysis
The below table brings out some of the key assumptions indicating the effect of potential changes, other factors remaining constant. The analysis is based on the investment portfolio as of 31.12.2016 with comparative as of 31.12.2015 and is calculated before taxes.

Table 7. Sensitivity analysis of the fair value of financial assets

Company's investment portfolio on 31 December 2016

€000	**1 % Parallel shift in the interest curve**	
Market risk sensitivity analysis	Up	Down
Effect on financial results	- 3,851	4,035

Company's investment portfolio on 31 December 2015

€000	**1 % Parallel shift in the interest curve**	
Market risk sensitivity analysis	Up	Down
Effect on financial results	-2,848	2,968

Risk profile

The duration of technical provisions and thus sensitivity to changes in interest rates are analyzed in greater detail in Table 3 and Figure 3 in the section concerning reserve risk. The cash flows of financial assets and liabilities are presented by maturities in Table 11, in the section concerning liquidity risks.

The duration of bonds and other interest-bearing investments was 1.6 years at year end 2016 (1.2 years in 2015). The duration of those investments is shown in Table 8.

Table 8. Duration and breakdown of bonds and other interest-bearing investments per instrument type, 31 December

	2016			**2015**		
€000	**Carrying amount**	**%**	**Duration years**	**Carrying amount**	**%**	**Duration years**
Euro credit (excl. Scandinavian)	90,619	37.0%	2.4	89,180	37.9%	2.1
Scandinavian credit	70,856	28.9%	1.1	78,133	33.2%	1.1
US credit	58,989	24.1%	1.3	31,341	13.3%	0.2
Short-term fixed income (incl.Scandinavian short)	22,002	9.0%	0.8	36,920	15.7%	0.4
Euro governments	2,505	1.0%	9.0	-	-	-
TOTAL	**244,971**	**100%**	**1.6**	**235,574**	**100%**	**1.2**

The duration of newly bought bonds and other interest-bearing investments is shorter than the duration of instruments consisted in the portfolio a year before.

EQUITY RISK

Equity risk refers to the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of market prices of equities.

There is no exposure to equity price risk because there are no equity instruments in the portfolio. According to the Investment Policy and Baltic Investment Policy, it is not allowed to invest in equity instruments. The only Equity risk exposure relates to fully owned subsidiary (Support Services AS) and not subject to market movements in equities.

CURRENCY RISK
Currency risk refers to the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of currency exchange rates.

Exposure to currency risk is insignificant. The majority of the insurance liabilities and all financial investments of the Company are in euro.

F) CREDIT RISK

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

Spread risk refers to the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of credit spreads over the risk-free interest rate term structure.

In general, credit risk refers to losses arising from occurred defaults of debtors or other counterparties or from increases in assumed probability of defaults. In the case of default the final loss depends on the value of the asset less any collateral and recoveries at the time of default.

Credit Risk in Investments Operations
The main credit risk for the company is stemming from the investments. Credit risk in the investment operations can be measured as counterparty default risk and spread risk. In most cases part of the credit risk is already reflected by higher spread and thereby the asset has a lower market value, even in the case of no default. Therefore, the spread is in essence the market price of credit risk.

The additional risk, stemming either from lack of diversification in the asset portfolio or from large exposure to default risk by (i) a single issuer of securities or (ii) a group of related issuers not captured by the spread risk or counterparty default risk, is measured as concentration risk.

Risk Management and Control
Credit risk in the investment operation is managed by specific limits stipulated in the Company's Investment Policy and If Group (Holding) Investment Policy. In these documents, limits are set for maximum exposures towards single issuers, type of debt category and per rating class. The spread risk is further limited by sensitivity restrictions for instruments sensitive to spread changes.

Before investing, potential investments are analyzed thoroughly. The creditworthiness and future outlook of the issuer are assessed together with any security or collateral as well as structural details of the potential investment. Internal risk indicators are critical factors in the assessment, however, macroeconomic environment, current market trends and external opinions of analysts and credit ratings by rating agencies are also taken into account. In addition, portfolio performance and the counterparties' credit standings are monitored continuously.

The development of the portfolios with respect to credit risk is monitored at the Company level and reported to the Management Board and to the Supervisory Board on a regular basis. Credit exposures are reported by ratings, instruments and the industry sectors.

Risk profile
The Table 9 below shows the maximum exposure to credit risk for the components of the statement of financial position.

Table 9. Assets exposure to credit risk

€000	31.12.2016	31.12.2015
Financial investments	244,971	235,574
Cash and cash equivalents	12,178	10,115
Receivables related to insurance activities	11,097	12,195
Reinsurance assets	2,717	2,308
Total credit risk exposure	**270,963**	**260,192**

The exposures are shown by sectors, asset classes and rating category in Table 10.

Table 10. Exposures by sectors, asset classes and rating, 31 December

2016

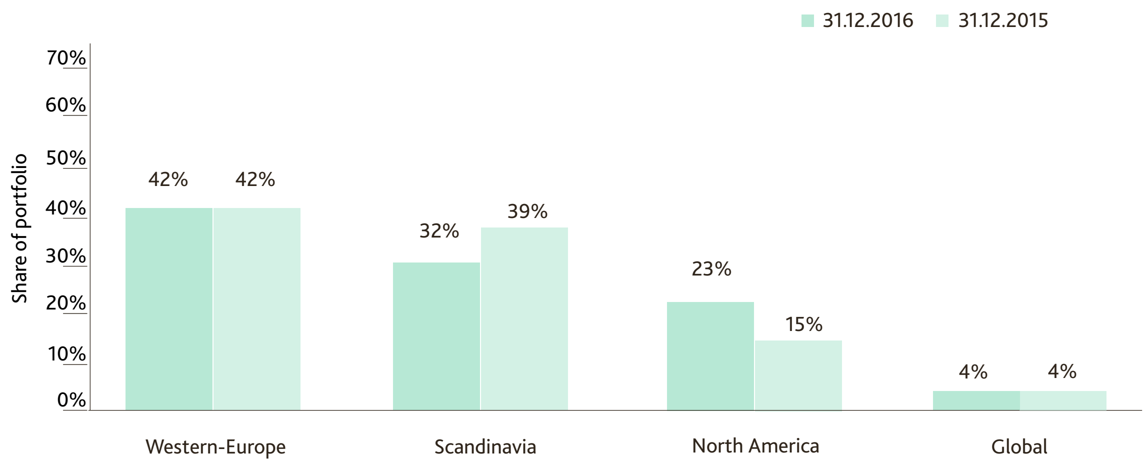
€000	AAA	AA+- AA-	A+ - A-	BBB+- BBB-	BB+ - C	Non-rated	Fixed income total
Basic Industry	-	-	5,009	-	1,152	2,045	**8,206**
Capital Goods	-	10,019	5,138	6,336	-	-	**21,493**
Consumer Products	-	6,010	8,571	10,637	-	-	**25,218**
Covered Bonds	10,313	-	-	-	-	-	**10,313**
Financial Institutions	-	69,685	43,620	5,576	-	-	**118,881**
Governments	-	2,505	-	-	-	-	**2,505**
Health Care	-	-	-	4,598	-	5,360	**9,958**
Real Estate	-	-	-	-	-	1,005	**1,005**
Services	-	-	-	12,639	-	4,146	**16,785**
Telecommunications	-	-	5,207	2,661	-	2,181	**10,049**
Transportation	-	-	2,681	2,535	-	-	**5,216**
Utilities	-	-	-	15,342	-	-	**15,342**
TOTAL	**10,313**	**88,219**	**70,226**	**60,324**	**1,152**	**14,737**	**244,971**

2015

€000	AAA	AA+- AA-	A+ - A-	BBB+- BBB-	BB+ - C	Non-rated	Fixed income total
Basic Industry	-	4,973	-	-	1,163	2,044	**8,180**
Capital Goods	-	-	9,924	6,248	-	-	**16,172**
Consumer Products	-	5,984	3,789	4,491	-	-	**14,264**
Covered Bonds	15,600	-	-	-	-	-	**15,600**
Energy	-	-	-	4,406	-	-	**4,406**
Financial Institutions	-	83,573	41,342	4,486	-	-	**129,401**
Health Care	-	-	-	1,991	-	5,288	**7,279**
Services	-	-	-	12,683	-	4,065	**16,748**
Telecommunications	-	-	5,183	2,646	-	2,108	**9,937**
Transportation	-	-	2,649	-	-	-	**2,649**
Utilities	-	-	-	10,938	-	-	**10,938**
TOTAL	**15,600**	**94,530**	**62,887**	**47,889**	**1,163**	**13,505**	**235,574**

The distribution of bonds and other interest bearing securities related to credit risks according to geographic region is presented in detail in the Figure 4 below.

Figure 4. Division of fixed income securities by geographical areas.



The credit risk in the Company´s investment portfolio is mainly associated with banks in the Nordic region.

Credit Risk in Insurance Operations
In addition to the credit risk associated with investment assets, credit risk arises from insurance operations through ceded reinsurance. Credit risk related to reinsurers arises through reinsurance receivables and through the reinsurers' portion of claims outstanding.

The company's credit risk exposure towards policyholders is very limited, because non-payment of premiums generally results in the cancellation of insurance policies.

Risk Management and Control
To limit and control credit risk associated with ceded reinsurance, the company has a Reinsurance Policy that sets requirements for the reinsurers' minimum credit ratings and the maximum exposure to individual reinsurers. Credit ratings from rating agencies are used to determine the creditworthiness of reinsurance companies. The Company's Reinsurance contracts for lower layers are concluded mainly with If P&C Insurance Ltd. (Sweden), which is rated by Standard & Poor's as A. Additionally, a Nordic-wide reinsurance program has been in place in If Group and is applicable for the Company since 2003. Every individual reinsurance contract is concluded on the basis of an analysis of the reinsurer's solvency and credibility and according to the list of allowed counterparties approved by the Supervisory Board of the Company.

The company has operational debtors handling regulations and is actively dealing with managing credit risk. The terms and conditions for the validity of insurance cover are set forth in the general insurance terms and conditions. Contracts concluded with insurance intermediaries specify payment terms and compliance with these is systematically monitored.

G) LIQUIDITY RISK

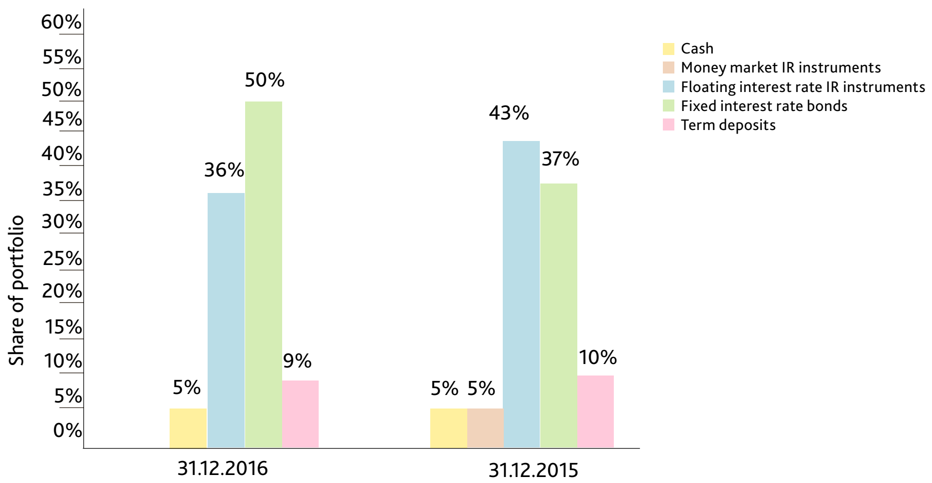
Liquidity risk is the risk that an insurance undertaking is unable to realize investments and other assets in order to settle its financial obligations when they fall due.

Risk Management and Control
In property and casualty insurance, the premiums are collected in advance and large claims payments are usually known long before they fall due, thus limiting the liquidity risk. Additionally, the investment portfolio duration is kept short.

The main objective in liquidity management is to ensure the company's ability to fulfil all its obligations arising from insurance contracts and insurance activities in a timely manner. To identify liquidity risk, expected cash flows from investment assets and technical provisions are analyzed regularly, taking both normal market conditions and stressed conditions into consideration. Liquidity risk is reduced by having investments that are readily marketable in liquid markets.

A more detailed classification of financial assets is presented in Figure 5 below.

Figure 5. Cash and financial investments



Risk profile
The maturities of cash flows for technical provisions, financial assets and liabilities are presented in Table 11. In the table, financial assets and liabilities are divided into contracts with an exact contractual maturity profile. In addition, the table shows expected cash flows for net technical provisions, which are inherently associated with a degree of uncertainty.

Table 11. Maturities of cash flows for financial assets, liabilities and net technical provisions

31.12.2016	Carrying amount			Cash flows						
€000	Carrying amount	Without maturity	With contractual maturity	2017	2018	2019	2020	2021	2022-2031	2032-
Financial assets	**269,336**	**13,268**	**256,068**	73,328	9,337	64,739	79,144	22,373	11,846	-
Financial liabilities	**9,368**	**-**	**9,368**	9,368	-	-	-	-	-	-
Net technical provisions	**127,895**	**-**	**127,895**	71,009	16,121	9,988	6,955	4,960	14,322	4,540

31.12.2015	Carrying amount			Cash flows						
€000	Carrying amount	Without maturity	With contractual maturity	2016	2017	2018	2019	2020	2021-2030	2031-
Financial assets	**258,670**	**10,901**	**247,769**	59,618	45,556	9,043	51,051	71,527	6,741	-
Financial liabilities	**10,070**	**-**	**10,070**	10,070	-	-	-	-	-	-
Net technical provisions	**126,009**	**-**	**126,009**	71,862	15,627	9,806	6,750	4,730	13,285	3,949

H) CONCENTRATION RISK

Concentration risk is all risk concentrations towards a single counterparty, industry sector or geographic region with a material loss potential that is not captured by any other risk type.

Risk Management and Control
In the Company's Underwriting Policy, Investment Policy and Reinsurance Policy limits are set for maximum exposures towards single issuers and per rating class.
Concentration risks for the Company is stemming mainly from the investments as credit risks related to the individual counterparties' investment in the portfolio.

Risk profile
Investments are mainly concentrated to the financial sector in the Scandinavian countries.
Concentrations are illustrated in table 10 Credit exposures by sectors, asset classes and rating, 31 December 2016 which are shown in Credit Risk section (f).

The largest credit risk concentrations related to individual counterparties are shown in Table 12.

Table 12. Concentration of market and credit risks in individual counterparties and asset classes, 31 December

2016 €000	Deposits	FRN and bonds	Total
Nordea Bank AB	22,002	-	**22,002**
DnB ASA	-	17,201	**17,201**
Raiffeisen-Boerenleenbank BA/Netherlands	-	16,366	**16,366**
General Electric Co	-	10,019	**10,019**
Swedbank AB	-	9,923	**9,923**
TOTAL	**22,002**	**53,509**	**75,511**

2015 €000	Deposits and Certificates of Deposit (CD)	FRN and bonds	**Total**
Nordea Bank AB	24,515	10,017	**34,532**
Raiffeisen-Boerenleenbank BA/Netherlands	-	16,307	**16,307**
Danske Bank A/S and branches	5,903	4,518	**10,421**
Swedbank AB	-	10,050	**10,050**
General Electric Co	-	9,924	**9,924**
TOTAL	**30,418**	**50,816**	**81,234**

I) OPERATIONAL RISK

Operational risk is the risk of loss arising from inadequate or failed processes or systems, from personnel, or from external events (expected or unexpected).

The definition includes legal risk that can be described as the risk of loss due to unpredictable or unknown legal development or uncertain interpretations of regulations and defective documentation.

Risk Management and Control
The Company identifies operational risks through different processes:

- Operational and Compliance Risk Assessment process. A Self-assessments, identifying operational risks are performed at least twice a year by each unit. Based on this assessment the second line is assessing the operational risks from the company perspective. The risk levels are monitored on continuous basis and reported regularly to the Management and Supervisory Board of the Company.
- Business and strategic risks are assessed at least twice a year to identify trends and their impact to the Company.
- Operational incidents are reported via a web-based system. The incidents are analysed by the risk function to determine the areas needing improvements. Information on the incidents trend and the severe impacts are part of the regular risk report.
- In order to secure the sustainable business operations, the business continuity management is implemented. To increase the awareness and preparedness for limiting the potential negative impact the crises situations continuity tests are carried out.

The main internal guidelines to manage the operational risks are Baltic Risk Management Guideline, Operational Risk Policy, Security Policy, Baltic Business Continuity Management Guideline, Outsourcing Policy, Complaints Handling Policy and Claims Handling Policy.

The Legal Unit is responsible for identifying legal risks within the Company. In addition, the Legal Unit is responsible for being updated on legislation, case law and products in relation to the insurance business.

J) OTHER RISK

COMPLIANCE RISK
Compliance risk is the risk of legal or regulatory sanctions, material financial losses or loss to reputation as a result of not complying with applicable rules.

Risk Management and Control
The Company aims to achieve an integrated compliance culture. The first line of defence owns and manages their compliance risks in the daily activities and reports to the second line of defence.

Practical compliance risks in the business are identified within the Operational and Compliance Risk Assessment process and incidents are reported through the incident reporting process similarly with the operational risks and incidents. Additionally, compliance monitoring activities in particular field of compliance topics are carried out when deemed necessary.

Identified risks are assessed from a severity perspective, encompassing likelihood and impact and reported quarterly to the Management Board and the Supervisory Board as well as to the If Group Chief Risk Officer.

REPUTATIONAL RISK

A reputational risk is often a consequence of a materialized operational or compliance risk and is defined as potential damage to the company through deterioration of its reputation amongst customer and other stakeholders.

A good reputation is vital for an insurance company, which means that trust is an important factor in the Company's relationship with its customers, employees and other stakeholders. The Company's reputation is determined by how stakeholders perceive our performance in each and every aspect of the Company's performance.

Risk Management and Control

When assessing the operational and compliance risks, the reputational consequence of a materialized risk is taken into account. Additionally, media incidents are reported by the Head of Communication Units in Estonia, Latvia and Lithuania at least twice per year to the Risk Manager. The reputational risk is analysed and reported at least twice per year to the Management Board and to the Supervisory Board along with the regular risk reporting.

Since operational and other risks may evolve into reputational risks if not handled correctly, the Communication department continuously work to ensure that all employees are aware of the importance of maintaining a good reputation and understand how to deal with potential reputational risks. Information about If in media, traditional as well as social, is followed closely as are possible customer complaints in order to act appropriately.

STRATEGIC RISK

Strategic risk is defined as the risk of losses due to changes in the competitive environment, changes in the overall economic climate or internal inflexibility.

Risk Management and Control

In the assessment of strategic risk, internal characteristics are evaluated against the potential impact of competitive economic, regulatory, and other external factors. The Company`s position is compared with peers, business partners and customers, and opportunities of entry for new competitors, products or technologies. The Company´s strategy process includes setting strategic high-level objectives and translating these into detailed short-term business plans. The strategy process also includes a risk assessment update whenever larger changes occur. The strategic risk is analysed and reported at least twice per year to the Management Board and to the Supervisory Board along with the regular risk reporting.

EMERGING RISK

Emerging risks are newly developing or changing risks that are difficult to quantify and which may have a major impact on the undertaking. The risks that are under extra observations are nano-technology, climate change and electric magnetics fields.

Risk Management and Control

Due to the large accumulation of potential emerging risks and thus the risk to the long-term solvency of the company, If Group Risk Management has established a forum with representatives from business with the aim of adopting a Group level perspective on emerging risk exposures.

K) SOLVENCY II

The entry into force of Solvency II on January 1, 2016 has led to a number of changes in the way the solvency capital requirements and the eligible own funds are calculated compared to earlier regulations (Solvency I). On January 1, 2016 the Company used the Solvency II standard formula for calculating the solvency capital requirement (SCR).

Note 3. Premiums earned, net of reinsurance

€000	2016	2015
Premiums written, gross	130,781	133,200
Change in the provision for unearned premiums	2,517	-3,669
Premiums earned, gross of reinsurance	**133,298**	**129,531**
Reinsurance premiums	-2,687	-3,040
Change in the provision for unearned premiums	118	54
Premiums earned, ceded	**-2,569**	**-2,986**
TOTAL	**130,729**	**126,545**

Note 4. Return on investments

€000	2016	2015
INTEREST INCOME/EXPENSE		
Financial assets at fair value through profit and loss		
Classified as held for trading		
From bonds and other interest-bearing securities	1,292	1,306
Available-for-sale financial assets		
From bonds and other interest-bearing securities	1,475	1,366
Loans and receivables		
From term deposits	20	31
From cash and cash equivalents	1	1
TOTAL	**2,788**	**2, 704**

PROFIT FROM DISPOSALS		
Financial assets at fair value through profit and loss		
Classified as held for trading		
From bonds and other interest-bearing securities	-	215
Available -for-sale financial financial assets		
From bonds and other interest-bearing securities	14	154
TOTAL	**14**	**369**

LOSS FROM DISPOSALS		
Financial assets at fair value through profit and loss		
Classified as held for trading		
From bonds and other interest-bearing securities	-	-1
TOTAL	**-**	**-1**

€000	2016	2015
PROFIT/LOSS FROM CHANGE IN FAIR VALUE		
Financial assets at fair value through profit and loss		
Classified as held for trading		
From bonds and other interest-bearing securities	-886	-975
TOTAL	**-886**	**-975**
Dividend from shares in subsidiary (Note 15)	**-**	**2,000**
Investment expenses	**-634**	**-612**
TOTAL RETURN ON INVESTMENTS	**1,282**	**3,485**

Reconciliation of fair value reserve of available-for-sale financial assets	**2016**	**2015**
Opening balance, available-for-sale financial assets	1,421	2,387
Changes in fair value during the year, recognized in comprehensive income	2,096	-813
Recognized in income statement	-14	-153
CLOSING BALANCE, AVAILABLE-FOR-SALE FINANCIAL ASSETS	**3,503**	**1,421**

Note 5. Claims incurred, net of reinsurance

€000	2016	2015
Gross		
Claims paid during the year related to that year	-66,566	-59,474
Claims paid related to previous years	-17,995	-17,615
Amounts recovered from salvage and recourses	9,167	8,443
Change in the provision for claims outstanding	-4,812	-3,159
Claims handling costs	-3,945	-3,945
TOTAL	**-84,151**	**-75,750**
Reinsurer's share		
Claims paid during the year related to that year	114	2
Claims paid related to previous years	28	1,104
Change in the provision for claims outstanding	293	-790
TOTAL	**435**	**316**
Net		
Claims paid during the year related to that year	-66,452	-59,472
Claims paid related to previous years	-17,967	-16,511
Amounts recovered from salvage and regresses	9,167	8,443
Change in the provision for claims outstanding	-4,519	-3,949
Claims handling costs	-3,945	-3,945
TOTAL	**-83,716**	**-75,434**

Note 6. Expenses

€000	2016	2015
Personnel expenses	-19,272	-19,016
Commissions to intermediaries	-8,948	-10,279
Data processing	-2,596	-2,563
Expenses on premises	-2,071	-2,083
Office expenses (incl. communication expenses)	-977	-1,030
Other operating expenses	-4,377	-3,112
TOTAL	**-38,241**	**-38,083**
Division of costs on the basis of functions		
Insurance contract acquisition costs	-22,480	-22,444
Administrative expenses	-11,816	-11,694
Claims handling expenses	-3,945	-3,945
TOTAL	**-38,241**	**-38,083**

Note 7. Receivables related to insurance activities and specification of bad debts

€000	31.12.2016	31.12.2015
Receivables related to direct insurance activities, incl.	10,778	12,015
- policyholders	7,704	7,485
- intermediaries	1,750	2,685
- recourses with significant recoverability	987	1,310
- salvages	277	412
- other	60	123
Receivables related to reinsurance	164	69
- incl. from related parties (Note 18)	-	1
Other receivables	155	111
- incl. from related parties (Note 18)	79	85
TOTAL	**11,097**	**12,195**
Term of the receivables		
Neither past-due nor impaired:		
- not due yet (due within 1 year)	10,447	11,431
Past-due but not impaired:		
- due for 0-3 months	519	642
- due for 3-6 months	22	43
- due for 6-12 months	55	32
- due for over 1 year	54	47
TOTAL	**11,097**	**12,195**

SPECIFICATION OF CHANGE IN BAD DEBT PROVISION

€000	Individually impaired	Collectively impaired	Total
At 1 January 2015	**-257**	**-155**	**-412**
Realized losses during the year	125	-	125
Unused amounts reversed during the year	325	-	325
Additions	-418	-	-418
Change in general provisions	-	57	57
At 31 December 2015	**-225**	**-98**	**-323**
Realized losses during the year	109	-	109
Unused amounts reversed during the year	403	-	403
Additions	-559	-	-559
Change in general provisions	-	4	4
At 31 December 2016	**-272**	**-94**	**-366**

Note 8. Accrued income and prepaid expenses

€000	31.12.2016	31.12.2015
Net deferred acquisition costs	2,772	3,313
Prepaid expenses	595	634
Corporate income tax	367	-
TOTAL	**3,734**	**3,947**

DEFERRED ACQUISITION COSTS 2016

€000	Share of acquisition costs (gross)	Reinsurer's share of acquisition costs	Share of acquisition costs (net)
Balance as of January 1	**3,364**	**-51**	**3,313**
Acquisition costs deferred during the year	8,832	-209	8,623
Reversal of previously deferred acquisition costs	-9,352	188	-9,164
Balance as of December 31	**2,844**	**-72**	**2,772**

DEFERRED ACQUISITION COSTS 2015

€000	Share of acquisition costs (gross)	Reinsurer's share of acquisition costs	Share of acquisition costs (net)
Balance as of January 1	**3,092**	**-43**	**3,049**
Acquisition costs deferred during the year	10,125	-209	9,916
Reversal of previously deferred acquisition costs	-9,853	201	-9,652
Balance as of December 31	**3,364**	**-51**	**3,313**

Note 9. Financial investments

€000	31.12.2016	31.12.2015
Financial assets measured at fair value through profit and loss		
Classified as held for trading		
Bonds and other interest-bearing securities		
- listed, with a fixed interest rate (2.375-5.5%)	35,722	41,621
Available-for-sale financial assets		
Bonds and other interest-bearing securities		
- listed	180,499	150,438
- unlisted	6,748	19,000
incl. with a floating interest rate	93,405	106,638
incl. with a fixed interest rate (0.0-3.75%, 31.12.15:0.03-3.75%)	93,842	62,800
TOTAL	**187,247**	**169,438**
Loans and receivables		
Term deposits	22,002	24,515
FINANCIAL INVESTMENTS TOTAL	**244,971**	**235,574**

Term deposits earn an annual interest 0.05% (as of 31.12.2015: 0.18-0.25%).

FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH PROFIT AND LOSS

€000	2016	2015
Balance at Jan.1	**41,621**	**42,631**
Classified as held for trading		
Bonds and other interest-bearing securities		
Sale	-4,977	-
Change in fair value through profit and loss	-887	-975
Change in accrued interest	-35	-35
Balance at Dec. 31	**35,722**	**41,621**

AVAILABLE-FOR-SALE FINANCIAL ASSETS

€000	2016	2015
Balance at Jan.1	**169,438**	**157,441**
Bonds and other interest-bearing securities		
Purchase	47,839	131,630
Sale	-32,384	-118,545
Change in fair value recorded in other comprehensive income	2,082	-966
Change in accrued interest	272	-122
Balance at Dec. 31	**187,247**	**169,438**

LOANS AND RECEIVABLES

€000	2016	2015
Balance at Jan.1	**24,515**	**23,207**
Term deposits		
Purchase	25,000	36,000
Maturity	-27,500	-34,700
Change in accrued interest	-13	8
Balance at Dec. 31	**22,002**	**24,515**

DIVISION OF BONDS AND OTHER INTEREST-BEARING SECURITIES BY MATURITY TERMS

€000	31.12.2016	31.12.2015
Up to 1 year	38,170	32,546
1-2 years	6,818	43,843
2-5 years	166,162	122,602
5-10 years	11,818	12,068
TOTAL	**222,969**	**211,059**

DEPOSITS BY MATURITY TERMS

€000	31.12.2016	31.12.2015
Up to 6 months	-	13,015
6-12 months	22,002	11,500
TOTAL	**22,002**	**24,515**

	31.12.2016		31.12.2015	
€000	**Fair value**	**Acquisition cost**	**Fair value**	**Acquisition cost**
Financial assets measured at fair value through profit or loss				
Classified as held for trading				
Bonds and other interest-bearing securities	35,722	33,918	41,621	38,895
Available-for-sale financial assets				
Bonds and other interest-bearing securities	187,247	182,894	169,438	167,440
TOTAL	**222,969**	**216,812**	**211,059**	**206,335**
Loans and receivables				
Term deposits	22,002	22,000	24,515	24,500
FINANCIAL ASSETS TOTAL	**244,971**	**238,812**	**235,574**	**230,835**

BONDS WITH A FIXED INTEREST RATE, BY INTEREST RATES

Interest rate €000	31.12.2016	31.12.2015
Interest rate: 0.0-0.9%	37,445	16,195
Interest rate: 1.0-1.9%	29,752	20,365
Interest rate: 2.0-2.9%	36,397	41,371
Interest rate: 3.0-3.9%	14,891	15,303
Interest rate: 4.0-4.9%	9,927	10,024
Interest rate: 5.0-6.0%	1,152	1,163
TOTAL	**129,564**	**104,421**

Note 10. Property, plant and equipment

€000	Other PPE
Net book value 31.12.2014	**788**
Acquisition	347
Write-off	-411
Disposal	-75
Acquisition cost 31.12.2015	2,906
-incl. fully depreciated	1,639
Depreciation charge for the year	-340
Depreciation charge of sales and disposals	455
Accumulated depreciation 31.12.2015	-2,141
Net book value 31.12.2015	**765**
Acquisition	206
Write-off	-1,343
Disposal	-88
Acquisition cost 31.12.2016	1,681
-incl. fully depreciated	514
Depreciation charge for the year	-335
Depreciation charge of sales and disposals	1,390
Accumulated depreciation 31.12.2016	-1,086
Net book value 31.12.2016	**595**

Note 11. Liabilities related to insurance activities

€000	31.12.2016	31.12.2015
Liabilities related to direct insurance activities, incl.	**3,499**	**4,056**
-policyholders	2,507	2,961
-intermediaries	869	978
-others	123	117
Liabilities related to reinsurance	974	1,198
- incl. from related parties (Note 18)	536	682
Other liabilities	405	299
- incl. from related parties (Note 18)	155	141
TOTAL	**4,878**	**5,553**

All above mentioned liabilities are current liabilities.

Note 12. Accrued expenses and deferred income

€000	31.12.2016	31.12.2015
Variable compensation reserve (incl. taxes)	1,676	2,154
Unused vacation liability (incl. taxes)	1,004	919
Employee-related liabilities	585	545
Taxes payable	400	433
Other accrued expenses	825	466
TOTAL	**4,490**	**4,517**
Terms of liabilities		
Up to 12 months	4,490	4,517

Note 13. Liabilities related to insurance contracts and reinsurance assets

€000	31.12.2016	31.12.2015
Gross		
Provision for incurred and reported claims and claims handling expenses	62,165	58,488
Provision for incurred but not reported claims	27,222	26,087
Provision for unearned premiums	41,225	43,742
TOTAL	**130,612**	**128,317**
Reinsurer's share		
Provision for incurred and reported claims and claims handling expenses	1,780	1,448
Provision for incurred but not reported claims	235	274
Provision for unearned premiums	702	586
TOTAL	**2,717**	**2,308**
Net		
Provision for incurred and reported claims and claims handling expenses	60,385	57,040
Provision for incurred but not reported claims	26,987	25,813
Provision for unearned premiums	40,523	43,156
TOTAL	**127,895**	**126,009**

€000	2016		
Provision for incurred and reported claims,claims incurred but not yet reported (IBNR)and provision for claims handling expenses	**Liabilities arising from insurance contracts**	**Reinsurer's share of liabilities**	**Net**
Balance as of January 1	**84,575**	**-1,722**	**82,853**
Change in the provision for claims incurred but not yet settled, related to current year	17,946	-2	17,944
Change in the provision for claims incurred but not yet settled, related to previous years	-13,769	-330	-14,099
Change in the provision for claims incurred but not reported, related to current year	9,332	-32	9,300
Change in the provision for claims incurred but not reported, related to previous years	-8,197	71	-8,126
Change in the provision for claims handling expenses	-500	-	-500
Balance as of December 31	**89,387**	**-2,015**	**87,372**

€000	2015		
Provision for incurred and reported claims,claims incurred but not yet reported (IBNR)and provision for claims handling expenses	**Liabilities arising from insurance contracts**	**Reinsurer's share of liabilities**	**Net**
Balance as of January 1	**81,416**	**-2,512**	**78,904**
Change in the provision for claims incurred but not yet settled, related to current year	14,909	-29	14,880
Change in the provision for claims incurred but not yet settled, related to previous years	-12,654	833	-11,821
Change in the provision for claims incurred but not reported, related to current year	8,774	-28	8,746
Change in the provision for claims incurred but not reported, related to previous years	-7,783	14	-7,769
Change in the provision for claims handling expenses	-87	-	-87
Balance as of December 31	**84,575**	**-1,722**	**82,853**

€000	2016		
Provision for unearned premiums	**Liabilities arising from insurance contracts**	**Reinsurer's share of liabilities**	**Net**
Balance as of January 1	**43,742**	**-586**	**43 156**
Premiums written in the year	130,781	-2,687	128,094
Premiums earned during the year	-133,298	2,569	-130,729
Translation difference	-	2	2
Balance as of December 31	**41,225**	**-702**	**40,523**

€000	2015		
Provision for unearned premiums	**Liabilities arising from insurance contracts**	**Reinsurer's share of liabilities**	**Net**
Balance as of January 1	**40,072**	**-532**	**39,540**
Premiums written in the year	133,200	-3,040	130,160
Premiums earned during the year	-129,530	2,986	-126,544
Balance as of December 31	**43,742**	**-586**	**43,156**

The development of claims: 2010 - 2016

The overview of claims 2010-2016 has been provided in the below tables. The claims have been presented separately for each year. The tables provide an overview of the accumulated estimates of claims development (claims paid, incl. recourses and salvages, provision for incurred and reported loss, and IBNR provision) on the gross basis. The information on the claims paid is presented in the last table of claims development disclosure. The tables do not include information on actual claims handling expenses and the provision for claims handling expenses.

At 31 December 2016, the gross provision for claims outstanding for earlier accident years amounted to €8,843 thousand (at 31 December 2015 €12,358 thousand).

Various factors affect claims estimates changing over time, and it more often happens for lines with longer tail. While the information in the table discloses historical perspective of the adequacy of claims outstanding estimates, it alone would not be sufficient basis to conclude on the adequacy of estimates of claims outstanding as at the end of 2016. The company believes that the estimate of provision for outstanding claims as at the end of 2016 is adequate to cover claims incurred till the 31.12.2016 (irrespective of whether these claims have been reported or not). It is clear, however, that final amounts paid by the company will differ from the estimates due to inherent uncertainty, though company targets having those differences as little as possible.

Development of claims, gross

€000	2010	2011	2012	2013	2014	2015	2016
At 31 December							
Accident year	71,683	66,946	68,357	72,737	69,821	76,735	87,509
1 year later	71,690	69,644	67,616	75,086	70,326	77,744	
2 years later	70,102	69,248	67,390	75,405	71,256		
3 years later	69,012	66,545	65,884	74,116			
4 years later	69,259	65,645	62,815				
5 years later	68,905	65,333					
6 years later	68,295						
Provision for outstanding claims (incl. IBNR) as of 31.12.2016	5,742	4,769	6,848	10,987	10,623	11,293	27,278

Claims paid, recourses and salvages (accumulated), gross

€000	2010	2011	2012	2013	2014	2015	2016
At 31 December							
Accident year	46,732	47,296	43,432	46,648	46,600	53,052	60,231
1 year later	60,916	57,908	54,967	59,474	59,494	66,451	
2 years later	60,951	59,997	56,077	60,675	60,633		
3 years later	61,871	60,355	56,727	61,269			
4 years later	62,660	60,533	56,983				
5 years later	63,098	60,631					
6 years later	62,719						

Note 14. Corporate income tax

(A) INCOME TAX EXPENSE

€000	2016	2015
Current tax	-639	-791
Deferred tax	-25	-18
TOTAL INCOME TAX EXPENSE	**-664**	**-809**
Specification of income tax expense		
Latvia	-209	-103
Lithuania	-455	-706
TOTAL	**-664**	**-809**

(B) RECONCILIATION OF TAX CHARGE

€000	2016	2015
Profit of Branches	**4,390**	**5,797**
Tax at 15%	**-659**	**-870**
Permanent differences	10	24
Temporary differences	2	3
Prior year tax adjustment	-24	29
Donation	7	5
TOTAL TAX CHARGE FOR THE YEAR	**-664**	**-809**

(C) DEFERRED TAX

€000	31.12.2016	31.12.2015
Deferred tax liability		
Accelerated capital allowances	16	22
Provision for amounts recoverable by subrogation	37	43
TOTAL DEFERRED TAX LIABILITY	**53**	**65**
Deferred tax asset		
Vacation reserve and other accruals	144	167
Doubtful debts	37	48
Asset valuation allowance for doubtful receivables	-6	-7
Software amortization	6	9
TOTAL DEFERRED TAX ASSET	**181**	**217**
NET DEFERRED TAX ASSET	**128**	**152**

SPECIFICATION OF DEFERRED TAXES

€000	2016	2015
Deferred tax liability		
Latvia	16	22
Lithuania	37	43
TOTAL	**53**	**65**
Deferred tax asset		
Latvia	115	158
Lithuania	66	59
TOTAL	**181**	**217**
Net deferred tax asset		
Latvia	99	136
Lithuania	29	16
TOTAL	**128**	**152**

(D) CURRENT CORPORATE INCOME TAX LIABILITY (-)/RECEIVABLE

€000	31.12.2016	31.12.2015
At 1 January	**-47**	**-421**
Calculated	-639	-790
Paid	1,053	1,164
At 31 December	**367**	**-47**

Note 15. Investment into subsidiary

Support Services AS
Field of activity: sales and claims handling back-office services to If Group companies in Finland, Norway, Denmark and Sweden.
Legal address: Lõõtsa 8a, Tallinn 11415

€000	31.12.2016	31.12.2015
Acquisition cost of shares	**88**	**88**
Number of shares	25,000	25,000
Participation	**100%**	**100%**
Total owner's equity	**371**	**254**
Share capital	25	25
Share premium	63	63
Mandatory reserve	3	3
Retained earnings	163	565
Profit for the period	117	-402
Investment in the company's statement of financial position	**88**	**88**

As of 31 December 2016 the number of issued shares was 25,000 shares with nominal value 1 EUR.

Note 16. Owner's equity

Share capital
As of 31 December 2016 the number of issued shares was of 6,391,165 with nominal value 1 EUR.

Share premium
Share premium is the difference between the nominal value and the issue price of shares. Share premium may be used for covering accumulated loss, if loss cannot be covered from retained earnings, mandatory reserve or other reserves stipulated in the Articles of Association, as well as for increasing the share capital via a bonus issue.

As of 31.12.2016, share premium amounted to €3,679 thousand (31.12.2015: €3,679 thousand).

Mandatory reserve
The mandatory reserve is set up, in accordance with the Commercial Code of Estonia. The mandatory reserve must amount to no less than 1/10 of the share capital.

As of 31.12.2016, mandatory reserve amounted to €2,362 thousand (31.12.2015: €2,362 thousand).

Retained earnings
On 29 March 2016, the sole shareholder resolved the dividend to be paid out in amount of €6,900 thousand and earnings after dividend's payment in amount of €106,004 thousand to be carried forward.

Dividends paid and proposed

€000	2016	2015
Declared and paid during the year	6,900	5,800
Final equity dividend per ordinary share	€1.0796	€0.9075

The company's potential income tax liability
As of 31.12.2016 the company's retained earnings amounted to €119,593 thousand (2015: €112,904 thousand). Undistributed profit from Estonian activities amounts to €115,244 thousand (2015: €106,402 thousand).

The maximum possible income tax liability in Estonia related to the payment of the company's retained earnings, excluding retained earnings of Latvian and Lithuanian branches, as dividends is €23,155 thousand (2015: €21,183 thousand). The company could thus pay total €96,437 thousand (2015: €91,721 thousand) in net dividends including profits of branches in amount of €3,726 thousand (2015: €4,988 thousand) taxed already in Latvia and Lithuania.

The maximum possible income tax liability has been calculated based on the assumption that the net dividends to be paid, and the related total income tax expenses to be recorded in the statement of comprehensive income in 2017, would not exceed the retained earnings as of 31.12.2016.

The profit available for distribution may be further limited by the solvency capital requirement (SCR).

Note 17. Operating lease

The Company leases office space and passenger cars under operating lease terms. Total rental expenses carried in the Company's income statement amount to €1,636 thousand (2015: €1,664 thousand).

As of 31.12.2016, the Company had the following deferred liabilities arising from operating lease contracts:

- up to 1 years	€1,321 thousand	(as of 31.12.2015 €1,439 thousand)
- 1 to 5 years	€1,720 thousand	(as of 31.12.2015 €1,472 thousand)

Note 18. Related party transactions

1. Information about related companies

Subsidiary

The subsidiary Support Services AS, located in Tallinn, Estonia, has been providing sales and claims handling back-office services to the group companies If Finland, If Norway, If Denmark and If Sweden.

Parent company and other group companies

If P&C Insurance Holding Ltd (publ) is located in Stockholm, Sweden and is the parent company of If Group. It is a holding company and owns and administers the shares of If Group companies. The holding company owns the Swedish If P&C Insurance Ltd and life insurance If Livförsäkring AB, the Finnish company If P&C Insurance Company Ltd and the Estonian company If P&C Insurance AS. If's operations in Denmark, Norway, Latvia and partly in Finland are conducted via branches. In addition to the Nordic branches, If P&C Insurance Ltd has established branches in Germany, France, the Netherlands and the United Kingdom.

The holding company owns also If IT Services A/S which is located in Copenhagen, Denmark, and its line of business is to purchase IT operation services for the If Group's companies in the Nordic and Baltic area.

If P&C Insurance Holding Ltd (publ) is a wholly owned subsidiary of Sampo plc., a Finnish listed company.

Relations with Sampo

Sampo Plc is located in Helsinki, Finland. The Company's field of activity is to own and administer shares, other stocks and real estate, to trade in securities, and carry on other investment activities. Sampo Plc manages the Company's investments assets. Compensation for these services is based on a fixed commission calculated in accordance with the market value of the managed investments assets.

The Company concluded agreement with Sampo Plc subsidiary Mandatum Life Insurance Baltic SE regarding the marketing and sales of products. The compensation takes the form of commission.

Relations with Nordea
Nordea is a company associated with Sampo, so is a company related to If. Nordea distributes If' P&C insurance services in Sweden, Finland and the Baltics. The compensation takes the form of commission. Nordea is a banking partner of the Company and agreements have been concluded covering the management of bank accounts and related services. In asset management, investments are made by the Company in floating rate notes and deposits issued by companies in the Nordea Group.

Other related parties
The Company's shareholders, staff, Management Board and Supervisory Board members, their close relatives and other individuals with whom the above persons have significant influence are considered related parties.

2. Transactions with members of the Management Board and members of the Supervisory Board

The Management Board members received a total of €1,523 thousand in remuneration in 2016, including social tax (2015: €1,294 thousand). No termination benefits were paid to members of the Management Board during 2016 (2015:0). According to the conditions of the contract concluded with the members of the Management Board, termination benefit up to 12 months shall be paid if the contract is terminated. No remuneration was paid to members of the Supervisory Board in 2016 and 2015.

Insurance contracts with total premiums of €11 thousand were concluded with the Management Board members in the financial period (2015: €12 thousand).

The remuneration of the Chairman and other members of the Management Board consists of a fixed remuneration, variable compensation, and participation in long-term incentive programs. The proportion of the variable compensation does not exceed 30% of the fixed remuneration. Variable compensation is based on the performance of the Company and If Group (measured by combined ratio, volume of gross written premiums, net profit targets) and the reaching of personal work goals.

3. Transactions with other group or related companies

3.1. The Company has concluded reinsurance contracts with If P&C Insurance Ltd (Sweden) and If P&C Insurance Company Ltd (Finland).

	Calculated reinsurance premiums		Indemnifications and commissions received	
€000	**2016**	**2015**	**2016**	**2015**
If P&C Insurance Ltd (Sweden)	1,514	1,994	11	1,099
If P&C Insurance Company Ltd (Finland)	204	37	16	3
Total	**1,718**	**2,031**	**27**	**1,102**

Receivables and payables related to the above transactions as of 31.12.2016 and 31.12.2015:

€000	31.12.2016	31.12.2015
Receivables		
If P&C Insurance Ltd (Sweden)	-	1
Payables		
If P&C Insurance Ltd (Sweden)	498	682
If P&C Insurance Company Ltd (Finland)	38	-
Total	**536**	**682**

3.2. The Company rendered services to and purchased services from the following group and related companies:

	Services purchased		Services rendered	
€000	2016	2015	2016	2015
Mandatum Life Insurance Baltic SE	-	-	18	16
Nordea Group companies	262	455	578	559
If P&C Insurance Ltd (Sweden)	11	-	140	144
Sampo Plc	493	463	-	-
If IT Services A/S	394	97	7	24
Support Services AS	-	1	45	36
Total	**1,160**	**1,016**	**788**	**779**

Receivables and payables related to the above transactions as of 31.12.2016 and 31.12.2015:

€000	31.12.2016	31.12.2015
Receivables		
Nordea Group companies	65	48
If P&C Insurance Ltd (Sweden)	13	36
Support Services AS	1	1
Total	**79**	**85**
Payables		
Mandatum Life Insurance Baltic SE	2	-
Nordea Group companies	20	21
Sampo Plc	126	120
If P&C Insurance Ltd (Sweden)	7	-
Total	**155**	**141**

3.3. The Company has acquired financial assets and has earned investment income from the following related companies:

€000	31.12.2016	31.12.2015
Financial assets		
Nordea Group companies	22,002	34,532

€000	2016	2015
Investment income/expense		
Nordea Group companies	12	32

Building a better working world

Ernst & Young Baltic AS
Rävala 4
10143 Tallinn
Eesti

Tel: +372 611 4610
Faks: +372 611 4611
Tallinn@ee.ey.com
www.ey.com

Äriregistri kood: 10877299
KMKR: EE 100770654

Ernst & Young Baltic AS
Rävala 4
10143 Tallinn
Estonia

Phone: +372 611 4610
Fax: +372 611 4611
Tallinn@ee.ey.com
www.ey.com

Code of legal entity: 10877299
VAT payer code: EE 100770654

Translation of the Estonian Original

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of If P&C Insurance AS

Opinion

We have audited the financial statements of If P&C Insurance AS, which comprise the statement of financial position as at 31 December 2016, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of If P&C Insurance AS as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (Estonia). Our responsibilities under those standards are further described in the *"Auditor's responsibilities for the audit of the financial statements"* section of our report. We are independent of the Company in accordance with the Code of Ethics for Professional Accountants (Estonia), and we have fulfilled our other ethical responsibilities in accordance with the requirements of code of ethics.

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

Other information

Management is responsible for the other information. Other information consists of management report, but does not consist of the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

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

Building a better
working world

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (Estonia) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with International Standards on Auditing (Estonia), we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.

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

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

Tallinn, 23 February 2017

Olesia Abramova
Authorised Auditor's number 561
Ernst & Young Baltic AS
Audit Company's Registration number 58

Tiina Leif
Authorised Auditor's number 441

PROPOSAL FOR THE DISTRIBUTION OF THE PROFIT

Profit available for distribution in accordance with the statement of financial position amount to:

Profit carried forward	€106,003,719
Net profit for the financial year 2016	€13,588,788
Total profit available for distribution as of 31.12.2016:	**€119,592,507**

The Management Board proposes:

to distribute as dividends to the sole shareholder	€3,800,000
to carry forward	€115,792,507

Andris Morozovs
Chairman of the Management Board

Dace Ivaska
Member of the Management Board

Sanita Ķēniņa
Member of the Management Board

Žaneta Stankevičienė
Member of the Management Board

Heimar Olak
Member of the Management Board

Artur Praun
Member of the Management Board

Jukka Tapani Laitinen
Member of the Management Board

Ville Valtteri Haapalinna
Member of the Management Board

Tiit Kolde
Member of the Management Board

SIGNATURES TO THE ANNUAL REPORT 2016

The Management Board of If P&C Insurance AS has prepared the management report and financial statements for 2016.

Signatures:

Heinar Olak	Member of the Management Board		15.02.2017
Artur Praun	Member of the Management Board		15.02.2017