



Independent auditor's report

to the members of Aioi Nissay Dowa Insurance Company of Europe Limited

1. Our opinion is unmodified

We have audited the financial statements of Aioi Nissay Dowa Insurance Company of Europe Limited ("the Group") for the year ended 31 December 2017 which comprise the consolidated statement of comprehensive income, consolidated statement of other comprehensive income, consolidated statement of financial position, company statement of financial position, consolidated statement of changes in equity, company statement of changes in equity, consolidated cash flow statement, company cash flow statement and the related notes, including the accounting policies in note 1.

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2017 and of the Group's loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the Audit Committee.

We were appointed as auditor by the shareholders on 29 June 2016. The period of total uninterrupted engagement is for the two financial years ended 31 December 2017. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview

Materiality:	£3.26m (2016:£3m)
group financial statements as a whole	0.88% (2016:0.93%) of insurance premium revenue

Coverage	97% (2016: 97%) of insurance premium revenue
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Risks of material misstatement	vs 2016
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Recurring risks	Valuation of general insurance claims outstanding	◀▶
	Valuation of Goodwill and Intangible assets	▼

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2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
<p>Valuation of general insurance claims outstanding</p> <p>Group: £332 million gross, £157 million net; 2016: £250 million gross, £128 million net. Company: £325 million gross, £150 million net; 2016: £244 million gross, £122 million net.)</p> <p><i>Refer to page 36 for the accounting policy, note 2a on page 44 for the accounting judgement and note 27 for the financial statement disclosures.</i></p>	<p>Subjective valuation</p> <p>General insurance claims outstanding represents the single largest liability for the Group and the Company. Valuation of these liabilities is highly judgemental because it requires a number of assumptions to be made with high estimation uncertainty such as the initial reserve, loss ratios and estimates of the frequency and severity of claims.</p> <p>The determination and application of key assumptions and methodologies is complex and requires consistency across underwriting years and lines of business and relies on the integrity of underlying data.</p> <p>The allowance made for the Ogden rate change and Periodic Payment Order ("PPO") reserves is impacted by current legislative uncertainty.</p> <p>The management margin needs to be responsive to assessed residual risks</p>	<p>We used our own actuarial specialists to assist us in performing our procedures on the valuation of claims outstanding.</p> <p>Our procedures included:</p> <p>Control design and operation: Updating and documenting our understanding of the systems, processes and methodologies in use. Testing the governance and key controls around the reserving process. This included an assessment of the reserving governance process. Testing the design, implementation and operating effectiveness of the key controls over the completeness and accuracy of the data used in the reserving models.</p> <p>Test of detail: On a sample basis, inspecting case files. For the IBT MGA we focused on large losses being those assessed as having the highest risk. We considered the adequacy of the reserve estimates in the light of evidence in the case files.</p> <p>Expectation vs Outcome: Using data & analytic techniques to identify trends and areas of focus such as movement in large claims, negative case reserves, ageing of claims and review periods for large and attritional (smaller and less complex) claims arising from the ITB MGA book.</p> <p>Expert judgement: assessing the methodology applied by the Group and Company and the reasonableness of key assumptions both against historic experience as well as a broader market context. Given the high levels of uncertainty surrounding the ultimate cost of bodily injury claims, we focused on the large outstanding claims including assessing the application of the Ogden discount rate and the adequacy of provisions for Periodic Payment Orders ("PPOs"). Assessing the reasonableness of the booked reserves inclusive of management margin, and its consistency with previous periods.</p> <p>Independent performance: for the lines of business assessed as being the highest risk, performing our own projections of the reserves and comparing our results against management results to assess and understand any material variances.</p>

2. Key audit matters: our assessment of risks of material misstatement

	The risk	Our response
<p>Valuation of general insurance claims outstanding (continued)</p> <p>Group: £332 million gross, £157 million net; 2016: £250 million gross, £128 million net. Company: £325 million gross, £150 million net; 2016: £244 million gross, £122 million net.)</p> <p><i>Refer to page 36 for the accounting policy, note 2a on page 44 for the accounting judgement and note 27 for the financial statement disclosures.</i></p>	<p>Subjective valuation</p> <p>The acquisition of Box Innovation Group Limited ("BIGL") in 2015 generated a significant amount of goodwill and acquired intangible assets.</p> <p>Due to the inherent subjectivity of management's long term business plan for the business and other estimates/judgements within the discounted cash flow model used for the value in use calculation, there is a risk that the goodwill arising from the BIGL acquisition may require an impairment. On impairment, consideration is required of the appropriateness of the impairment and the impact on the consolidated statement of comprehensive income and consolidated statement of financial position.</p> <p>Performance in the period may provide indicators of impairment of acquired intangible assets. Booked impairments may be subjective as they rely on estimates, judgements and assumptions within the business plan.</p>	<p>Benchmarking assumptions: Assessing the movements in gross ultimate loss ratios across accident years through benchmarking to market data.</p> <p>Analytical procedures: Assessing the methodology in use for determining the net of reinsurance reserves and testing the calculation.</p> <p>Our results</p> <p>We found the Company's assessment of the valuation of general insurance claims outstanding to be acceptable (2016 acceptable)</p>
<p>Valuation of goodwill and intangible assets</p> <p>Goodwill: (£0 million; 2016: £48 million)</p> <p>Intangible assets: (£30 million; 2016: £72 million)</p> <p><i>Refer to page 37 for the accounting policy, note 2c and d on page 46 for the accounting judgement and notes 14 and 15 for the financial statement disclosures.</i></p>	<p>Forecast-based valuation</p> <p>Due to the inherent subjectivity of management's long term business plan for the business and other estimates/judgements within the discounted cash flow model used for the value in use calculation, there is a risk that the goodwill arising from the BIGL acquisition may require an impairment. On impairment, consideration is required of the appropriateness of the impairment and the impact on the consolidated statement of comprehensive income and consolidated statement of financial position.</p> <p>Performance in the period may provide indicators of impairment of acquired intangible assets. Booked impairments may be subjective as they rely on estimates, judgements and assumptions within the business plan.</p>	<p>As a result of management's decision to fully impair goodwill and to write down certain intangible assets, our procedures included:</p> <p>Control design: We evaluated the design and implementation of controls over the annual assessment of impairment of goodwill and in considering impairment triggers for the acquired intangible assets including the Board's assessment in light of performance in the year.</p> <p>Comparing cash flows: Comparing the cashflows used for the impairment testing of the goodwill and intangible assets to the Group's business plan and past performance to assess the reasonableness of the cash flows used and the sensitivity of those cash flows for forecast based valuation. Testing if the cash flows used met the criteria within IAS36-<i>Impairment of Assets</i>. Considering whether management's decision to impair the goodwill and certain intangible assets was appropriate and whether the quantum of that impairment was within an acceptable range</p> <p>Benchmarking assumptions: Comparing the Group's assumptions to externally or independently derived data in relation to key inputs such as the projected economic growth and discount rates.</p> <p>Reperformance: For the intangible assets, recalculating the amortisation charge having assessed the remaining useful economic lives of the assets.</p> <p>Assessing transparency: Assessing the impact of the impairment reviews on the reported results and financial position of the Group and assessing whether the Group's disclosures in respect of the outcome of the goodwill and intangibles review were consistent with the business performance and Strategic Report.</p> <p>Our results</p> <p>We found the valuation of the goodwill and intangible assets to be acceptable (2016: acceptable).</p>

3. Our application of materiality and an overview of the scope of our audit

Materiality for the Group financial statements as a whole was set at £3.26m (2016: £3m), determined with reference to a benchmark of Insurance premium revenue, (of which it represents 0.88% (2016: 0.93%)). We consider Insurance premium revenue to be the most appropriate benchmark as it provides a more stable measure year on year than Group profit before tax. We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.16m in addition to other identified misstatements that warranted reporting on qualitative grounds.

Materiality for the Parent Company financial statements as a whole was set at £2.9m (2016: £3m), determined with reference to a benchmark of parent Company Insurance premium revenue, of which it represents 0.82% (2016: 0.97%). We consider insurance premium revenue to be the most appropriate benchmark as the principal objectives of the parent entity is to write insurance policies. We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.15m in addition to other identified misstatements that warranted reporting on qualitative grounds.

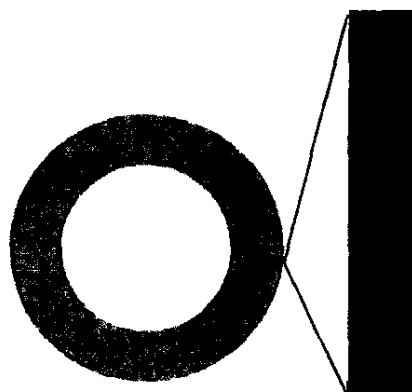
Of the Group's ten (2016: ten) reporting components, we subjected eight (2016: seven) to full scope audits for group purposes.

The work on three of the eight components (2016: three of the seven components) was performed by component auditors and the rest, including the audit of the Parent company, was performed by the Group audit team. The Group audit team performed all the work on the key audit matters. The components within the scope of our work accounted for the percentages illustrated opposite.

The Group audit team instructed component auditors as to the significant areas to be covered, including the relevant risks and the information to be reported back. The Group audit team approved the component materialities, which ranged from £0.2m to £2.45m, having regard to the mix of size and risk profile of the Group across the components.

The Group team visited two of the component locations to assess the audit risks and strategy. The third component team joined the Group team on-site for part of the audit and the Group partner attended the component Audit Committee. Telephone conference meetings were also held with these component auditors during the audit. During these visits and meetings, the findings reported to the Group audit team were discussed in more detail, and any further work required by the Group audit team was then performed by the component auditor. Onsite and offsite reviews were performed by the Group audit team.

Insurance premium revenue
£373m (2016: £323m)



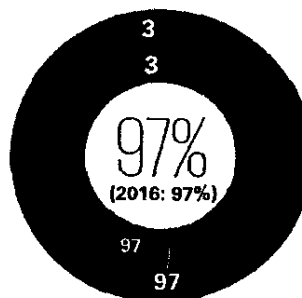
■ Insurance Premium Revenue
■ Group Materiality

Group Materiality
£3.26m (2016: £3m)

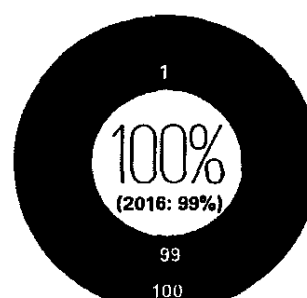
£3.26m
Whole financial statements materiality (2016: £3m)
£2.45m
Range of materiality at 8 components (£0.2m-£2.45m) (2016: £0.15m to £3m)

£0.16m
Misstatements reported to the audit committee (2016: £0.15m)

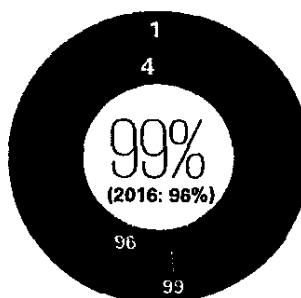
Total Revenue



Total Assets



Loss Before Tax



■ Full scope for group audit purposes 2017
■ Residual components 2017
■ Full scope for group audit purposes 2016
■ Residual components 2016

4. We have nothing to report on going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

5. We have nothing to report on the strategic report and the directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in those reports;
- in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 15, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent 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 they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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 other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our sector experience, through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory and legal correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related company legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related financial statements items.

In addition we considered the impact of laws and regulations in the specific areas of regulatory capital and regulatory conduct. With the exception of any known or possible non-compliance, and as required by auditing standards, our work in respect of these was limited to enquiry of the directors and other management and inspection of regulatory and legal correspondence. We considered the effect of any known or possible non-compliance in these areas as part of our procedures on the related financial statements items.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. This included communication from the group to component audit teams of relevant laws and regulations identified at group level, with a request to report on any indications of potential existence of non-compliance with relevant laws and regulations (irregularities) in these areas, or other areas directly identified by the component team

As with any audit, there remained a higher risk of non-detection of non-compliance with relevant laws and regulations, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.