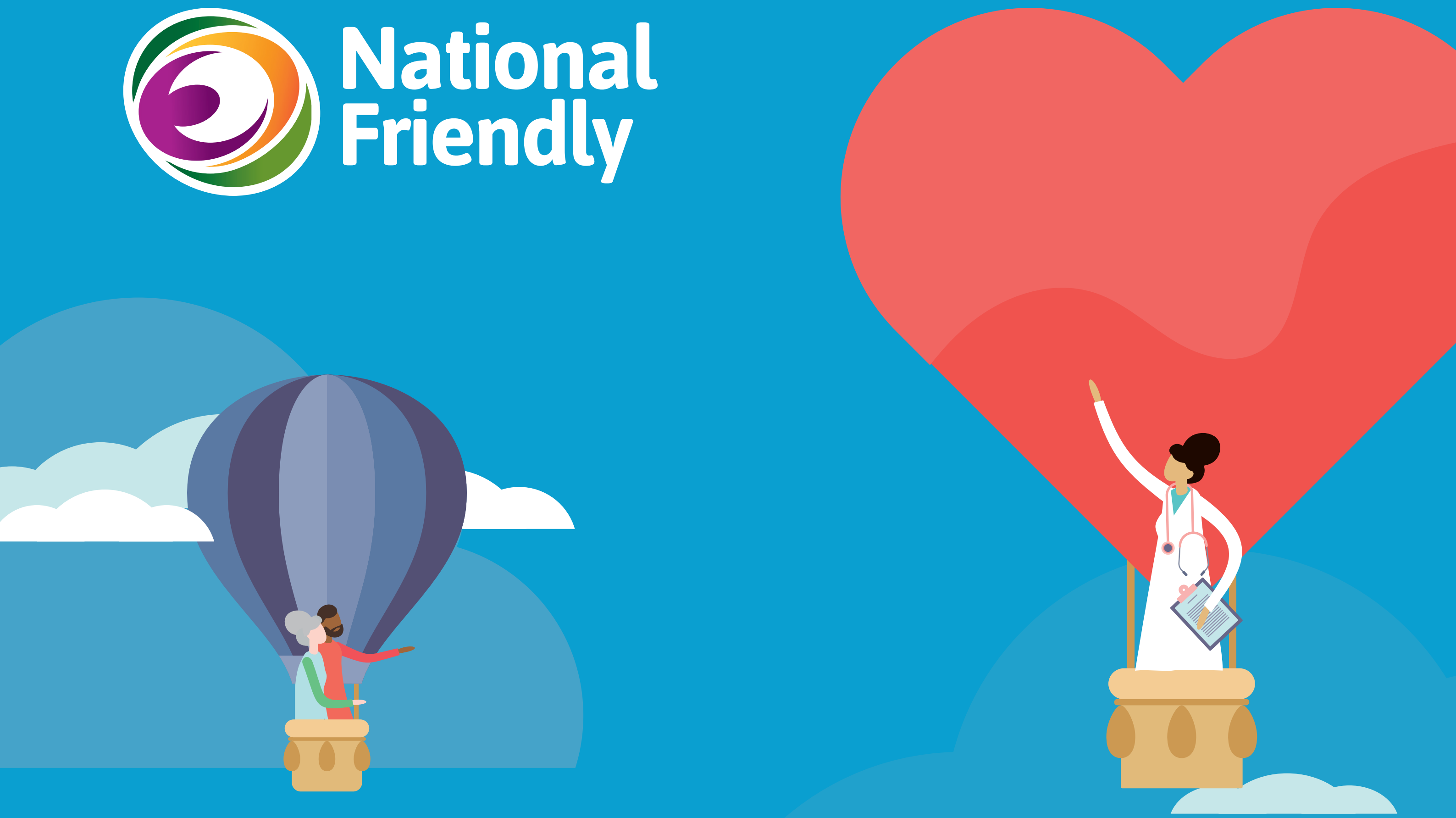
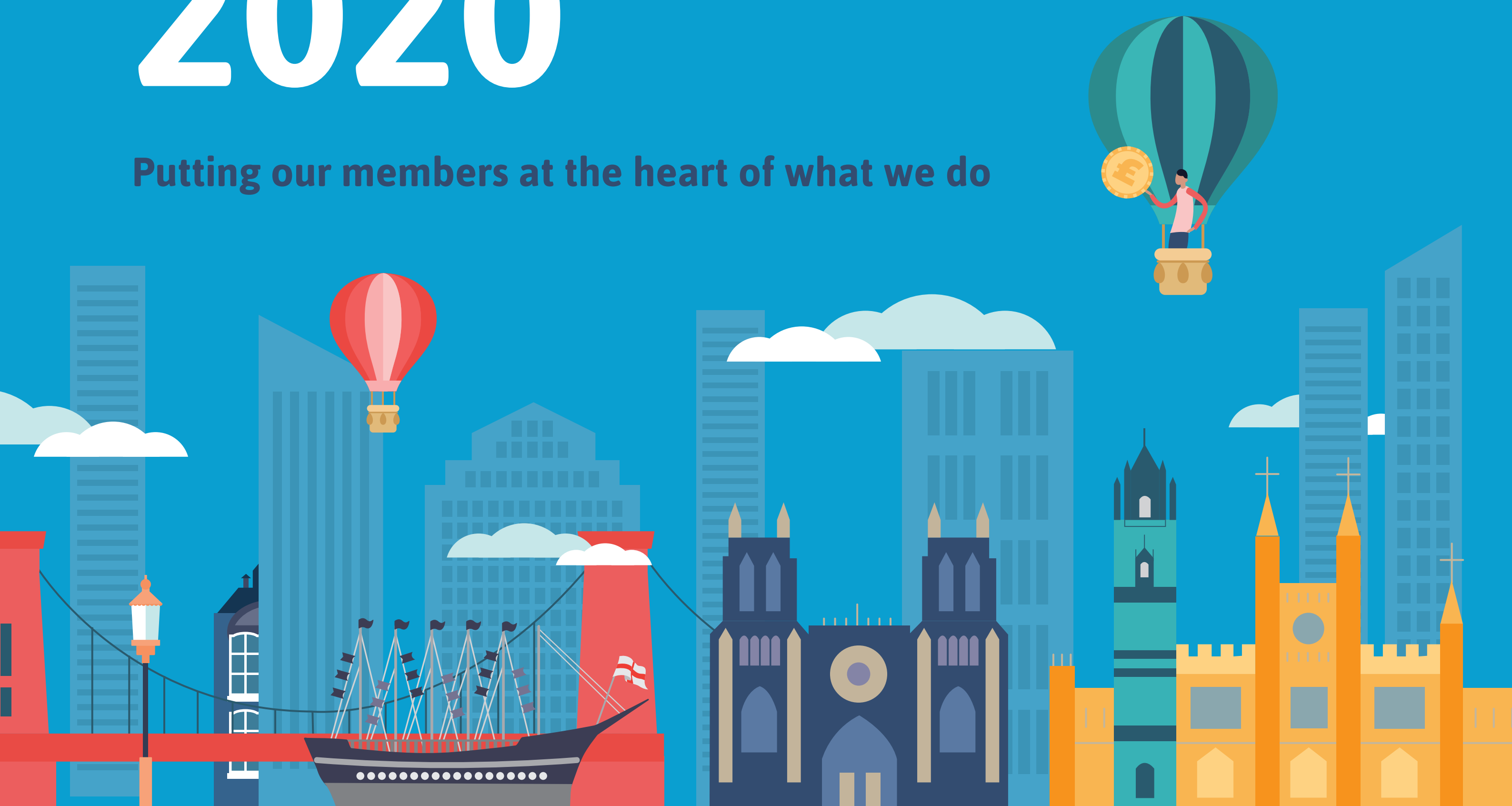
National Friendly



Annual Report & Financial Statements 2020

Putting our members at the heart of what we do



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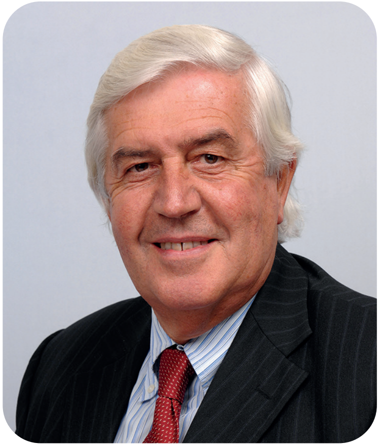
Established 1868
Registered and incorporated Friendly Society no. 369F
Member of the Association of Financial Mutuals.
Authorised by the Prudential Regulation Authority and
regulated by the Financial Conduct Authority and the
Prudential Regulation Authority.
Chief Executive Officer: Graham Singleton
Secretary: Keith Meeres



Chair’s Review

2020 was a challenging year for the Society as it was for many people. The year ended with particular sadness with the sudden passing of our Chief Executive, Jonathan Long. Jonathan made a significant contribution over 14 years with the Society, nine of these as Chief Executive, overseeing the Society as it returned to writing new business and the development of new products and services to meet the health, welfare and protection needs of our members.

COVID-19

The COVID-19 pandemic has affected all of our lives, by not only generating a year of economic uncertainty but also prompting long-term changes to how we live and work. We have had robust business continuity processes in place for many years and these were activated in March 2020. Colleagues across all teams were able to work from home to help meet the needs of both our existing and new members.

The pandemic has been a stark reminder of the importance of protecting our health and welfare needs. National Friendly was founded on the principle of helping people to help themselves. All of our products, services and benefits ensure our members are prepared for life’s uncertainties and we believe this is now more crucial than ever.

Performance

Even during these difficult times, due to the hard work and commitment from my colleagues, we saw growth in both newly issued policies and annualised new business premium income, which grew to £9.5 million, compared to £8.0 million in 2019.

Our Guaranteed Life Assurance product continued to be an important driver for new business in 2020 as was the further advancement for our Immediate Care Plan product. The Immediate Care Plan was launched in 2019 and in 2020 we launched a variant with a deferred period. The innovative nature of our product design led to increased interest with Financial Advisers. Due to this positive feedback, customer demand and its profitability; in early 2021 we expanded the number of Financial Advisers who are able to recommend it to their clients. This has propelled us into the top four national providers for this type of product.

Capital strength

The COVID pandemic seriously disrupted the financial markets in the first half of 2020 causing the Society’s Solvency Capital Requirement (SCR) coverage to fall to 92% of the regulatory prescribed required level as at 31 March 2020, as disclosed in the Society’s 2019 Strategic Report.

The Society immediately took a number of measures to improve its financial strength, restoring 100% coverage of the SCR by 30 June 2020. Additional measures completed in the second half of 2020 (principally some changes to the Society’s and the Society’s pension scheme investment portfolios – investing in less risky assets), coupled with a strong financial markets recovery, restored the Society’s SCR coverage ratio, to 143% at 31 December 2020, and further actions continue to be taken to improve the ratio further.

Award success

I am also proud to report that we have won a national award for the work we do in the local community. We achieved success at the Protection Review Awards 2020, winning the award for ‘Doing it Better’. We were nominated alongside other insurers such as Zurich and Vitality. The award recognises companies with initiatives that have made a genuine difference to the lives of vulnerable people in the local area. The judges were impressed with our support for The Bristol Hippodrome’s social events for the over 60s that help address loneliness in later life. The award also recognised our fundraising partnership with Southmead Hospital Charity.

Your Society

I would like to welcome all the new members to the Society and may I take this opportunity to remind both new and previous members of the value of mutuality. We have no shareholders to answer to, your membership represents a commitment from myself and the Board that every decision we make will always have your best interests at heart. Many of our members have been with us for a long time and I would like to thank you all for your loyalty and trust in us. This organisation would not exist without you and to us, your opinion is the most important. I therefore strongly urge you to vote in our Annual General Meeting (AGM). You can pose questions to the Board at the AGM by sending them through to us before the meeting. You can also have your say by joining our Focus Group. You can find out more about our AGM and Focus Group on page 13.

Looking to the future

At the time of writing, we are approaching the halfway point of the second year of the pandemic. We will continue to ensure we have adequate provision in place to protect us against any potential future financial impacts. With the COVID-19 vaccination programme well underway, I believe we can all be optimistic about a return to some level of normality and look ahead with hope.

As we continue our drive to create innovative new products, in April 2021 we were proud to launch an Accident Only Income Protection policy. The policy is designed to pay out a regular benefit to people who have had an accident and suffered a loss of earnings as a result. Initial interest and sales of the product have been very positive.

Board and Governance

I was invited by the Board to take on the role of the Chair of the Society in May this year following Tracy Morshead's decision to step down from the Board. I welcome the opportunity to lead the Society, and confirm our strategy resolutely remains being a "forward thinking and trusted mutual that meets the health, welfare and protection needs of our members."

I thank my predecessor, Tracy, for all of his hard work, dedication and commitment over the past 12 years, seven of which he served as Chair. Under his stewardship we re-opened to new business and we have firmly established a sustainable and growing stream of new policy sales to provide the financial support and protection that our members need for their health and welfare.

In 2020 the Society started the process of reviewing the composition of the Board to include the appointment of new non-executive directors to replace long-serving non-executives. Non-executive directors Peter McIlwraith, the senior independent director, and Mark Jackson resigned from the Board at the AGM in 2020 after serving for 17 years and 11 years respectively. I thank them on your behalf for their devoted service. New non-executive directors Mark Searles and Mary Gavigan joined the Board in 2020.

Mark Searles has been appointed as senior independent director. Mark will also be assuming the Chair role for our subsidiary company, National Friendly Financial Solutions. He has an extensive background in financial services distribution which will be essential in his new role.

Graham Singleton stepped in as Interim CEO in early 2021 having previously joined the Board in 2019 in a non-executive director capacity. Graham subsequently applied for the permanent role and following a competitive search process, recognising Graham's very extensive industry knowledge and experience, the Board offered him the permanent role.

Julian Ellacott has joined the Board and will be assuming the Society's Chief Actuary role which is currently undertaken by an external actuary. He joined National Friendly last July and has already made an impact, contributing to the improvement of our capital strength and ensuring that our products are priced competitively whilst also being technically sound.

Thank you

I am grateful to you, our Members, who place your trust and welfare with the Society and to the Financial Advisers who recommend the Society to their clients.

Finally, I would like to give a big thank you to the Board and to all my colleagues for their dedication and commitment to transitioning to a new way of working during such difficult circumstances. Their hard work ensured the impact was minimal to the service we provide to you as members and I am grateful for their continued efforts in driving the Society forward and achieving our strategy.

Geoff Brown
Chair Elect
30 June 2021

CHAIR'S REVIEW
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THE DIRECTORS' REPORT
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Strategic Report

The Society's vision is: ***"To be a forward thinking and trusted mutual that meets the health, welfare and protection needs of our customers"***.

Overall Strategy

The Society's aim as an organisation is to provide for its members products and services that look after their health and welfare to give certainty and control over their wellbeing both now and in the future. These are fundamental needs which are as valid today as they were when the Society was first established by Reverend Canon Portal in 1868.

Our service is and will be delivered in a timely, personal and friendly manner using technology wherever appropriate. There will always be someone who you can speak to whatever the query or need.

The Society has two key objectives to achieve net growth in its member base, whilst managing regulatory capital and acting in the best interests of all of the Society's members in protecting and enhancing member value:

» Expanding the current product proposition with further new products delivering benefits and services where there is a clear need and market opportunity.

» Promoting member retention, offering alternatives when products mature or reach trigger points such as a price and benefit review – ensuring that we continue to meet members' needs where we are well placed to do so.

The Society's core proposition remains in the health and welfare market providing both insurance and investment products to help members to insure and / or save towards meeting their long-term needs.

Business Performance

The Society's business plan and key performance indicators ('KPIs') for 2020 established at the start of the year continued to focus on developing and launching new products in line with its strategy. The COVID-19 pandemic however meant that plans to launch an income protection plan had to be deferred until 2021 (an accident only version being launched in April 2021).

As noted in the Chair's statement in March 2020 the Society's Solvency Capital Requirement (SCR) coverage briefly fell below 100% (92% as at 31 March 2020). There are however two regulatory capital thresholds and the Society's coverage of the absolute minimum permitted capital requirement (MCR) remained very strong as noted in the table below.

The main actions to improve the Society's SCR coverage over the balance of the year were an adjustment to the level of property and equity assets the Society was invested in as well as negotiating with the Society's closed final salary pension scheme to similarly reduce its exposure to riskier asset classes.

Despite the challenges introduced by the COVID-19 pandemic new business sales grew by 19% during 2020 – a very credible performance in challenging business development conditions.

The following KPIs are used to measure ongoing success and have been measured throughout the year:

Own Funds – This is an economic Solvency II measure of the Society's net assets after liabilities and represents the long-term value attributable to its members (Embedded Value), and allows the Board to establish the impact of management activity over the long term.

Solvency Coverage Requirement (SCR) coverage ratio – This is a measure of how much surplus capital is available after the solvency capital requirement (a risk-based calculation, based on the actual risks on the balance sheet) that an insurer is required to hold. The regulatory requirement is for this ratio to exceed 100%, and the Society has a Solvency Risk Appetite that targets a higher ratio, in order to provide additional security to our customers.

New Business Premium Income – The target is sustained profitable growth, in parallel increasing membership numbers whilst maintaining strong control over costs.

Key Performance Indicators:

	31st December	
	2020	**2019**
Absolute Level of Own Funds	£16.00m	£18.27m
SCR coverage ratio		
• With Transitional Measures Relief[1]	143%	140%
• Without Transitional Measures Relief[1]	131%	129%
MCR coverage ratio		
• With Transitional Measures Relief[2]	479%	561%
• Without Transitional Measures Relief[2]	442%	515%
New Business Gross Written Premium	£9.47m	£7.95m

Notes

1. As at 31st March 2020 SCR coverage was 92% & 85% with and without transitional measures relief

2. As at 31st March 2020 MCR coverage was 369% & 340% with and without transitional measures relief

Capital Management KPI Commentary

The Society's capital position is assessed in accordance with the Solvency II regulations and the Society manages its business on this basis. This is a risk-based approach to the assessment of capital requirements whereby Technical Provisions are calculated as the sum of the best estimate of liabilities plus a risk margin. The Society is required to hold sufficient Own Funds (assets less technical provisions) to meet the SCR, which represents the amount of risk capital required to withstand a set of events at the 1/200 confidence level which covers market, underwriting, counterparty and operational risks. The SCR is calculated using the prescribed Standard Formula set out in the regulations.

01. Own Funds Movement

Although liabilities reduced (owing mainly to the maturing of with profits policies), asset values fell by a greater amount, as a result of market movements during the year. This was the primary reason for the fall during the year, of £2.3m, as set out in the table above.

02. The Solvency Capital Requirement (SCR)

Actions taken to reduce the asset risk were partially offset by additional SCR resulting from the growth in new business and particularly in respect of mortality and lapse risk attributable to the Guaranteed Life Assurance products.

03. Transitional Measure for Interest rates ('TMIR')

The above SCR & MCR results allow for the transitional measure on interest rates ('TMIR') approved by the regulator to enable the Society to smoothly transition to Solvency II. TMIR allows the gradual move from using Solvency I discount rates to the prescribed Solvency II risk free rates for pre-2016 policies over a period of 16 years, as these policies mature. Before taking account of the transitional measure, the excess assets position was £3.5m (2019: £3.8m).

04. New Business Premium Income

New Business sales are measured by their annualised new business premium income ('API') and deposits to new savings and investment policies. In 2020, the Society's new business API grew by 24%.

For 2021 the aim is to introduce a KPI which measures member engagement and overall advocacy – our aim is to continuously improve how we meet our members' needs both through product design & pricing and service.

Strategic Report (continued)

Business Performance (continued)

New business
Through writing new business, the Society continues to protect and enhance the long-term interests of its members through:

- **i.** Writing profitable new business that strengthens Own Funds, for the benefit of all members;
- **ii.** Providing an affordable option for new and existing members to help fund their later life needs;
- **iii.** Increasing the overall membership numbers and achieving economies of scale for the benefit of all members, ensuring we have the capacity to deliver the personalised service we aspire to; and
- **iv.** Working collaboratively with some of the top reinsurers on both product design and risk mitigation/protection for the Society.

The Society's continued aim is to provide existing and new members with products that address their welfare and care needs at every stage of life including later life care (long-term care) supported by an excellent customer experience at each stage of the member's journey with the Society.

2020 saw further advancement for our annuity product, the Immediate Care Plan, which aims to cover care home fees for people entering into a nursing or care home, guaranteed for life, in exchange for a lump sum premium. Building on the successful 2019 pilot, in 2020 the Society launched a variant which pays out after a deferred period of one or two years. In February 2021 the Society became one of only four insurers in the UK using a common application platform for the immediate care plan, covering the whole UK market.

Our Guaranteed Life Assurance product, available to those aged 50 and over, was again the dominant new business product in 2020 in terms of numbers of policies, with increased emphasis on the partially underwritten version. From April 2021 the Society now only sells the underwritten variant of the product, materially mitigating the risk of anti-selection (i.e. the risk of attracting a disproportionate number of adverse risks).

COVID -19
At the outset of the pandemic we quickly implemented our business continuity plans enabling nearly all staff to work from home, the key priority being ensuring their safety and wellbeing whilst continuing to meet the needs of customers and business partners.

The transition to home working proved far more successful than we could have ever hoped, with the technology providing robust service together with staff demonstrating great adaptability. We were and remain concerned to ensure we support the mental health of our staff, recognising that for some the isolation of working from home was particularly challenging. Teams were encouraged to hold virtual coffee breaks throughout the day using the web conferencing facilities and specific requests for people to return to the office were actioned where and when safe to do so. As 2021 has progressed increasing numbers of our colleagues have requested a minimum time allocation to be back in the office.

We continue to monitor government advice closely to carry on ensuring that we look after the health and wellbeing of our employees and the communities within which we work. Office cleaning protocols have been radically overhauled with daily deep cleans.

Such was the success of virtualising our office premises that in conjunction with our strategic business partners, who similarly had resilient contingency plans, we are able to continue to deliver the standard of service we aspire to for our customers.

Risk Management
Long-term sustainability through capital management remains a priority for the Society and writing new contracts of insurance in sufficient volume is integral to achieving this.

The Board has identified key threats to business strategy and mitigation plans have been put in place so that the Society can remain sustainable and continue to operate in the best interests of its policyholders. These risks are summarised on the next page:

Risk	Impact	Mitigating Activities
Regulatory Capital Requirements The Society is unable to meet its regulatory capital requirements	Regulatory intervention. Transfer of engagements or run off.	Close monitoring of capital management at Board level both with and without the approved transitional measure. This includes scenario analysis and key sensitivities such as morbidity, lapse and expense assumptions. Quarterly evaluation of SCR coverage allowing for updated market conditions, expense assumptions, change in the in-force book and new business written. Monthly "roll forward" estimates of the solvency position showing the latest estimate of the undiversified Solvency II capital against each of the relevant risks.
Insurance Risk ***Morbidity Risk*** Morbidity (claims higher than expected) experience deteriorates over and above expectations.	Increased reserves result in reduced Own Funds	Management of morbidity claims remains a key focus. Morbidity data tracking spreadsheets have been developed for the business administered by the Third Party Administrator so that they can be produced on a monthly basis. This covers all healthcare products. All other product morbidity tracking is done on a twice yearly basis. Any new business will be written on a reinsured basis to mitigate the morbidity risk of new policies. Regular audit and monitoring of claims payments as well as audit review of the claims administrator to confirm that paid claims are valid. Review of premiums on Healthcare policies considers actual claims experience to inform expected future claims and proposed premium changes.
Lapse Risk Lapses are higher or lower than projected.	Lapses exceeding levels of new business result in higher per policy expenses. Lower than predicted lapses in some product lines could result in increased technical provisions.	Lapse rates are regularly monitored and reported so that sufficient reserves are held reflecting up to date lapse assumptions. The reasons for the lapses are examined and action taken as needed.
Pension Scheme Risk Volatility of pension scheme valuation	Any change in valuation is reflected in the Society's UK GAAP and Solvency II balance sheets.	Review the investment strategy of the pension scheme with the objective of reducing volatility (noting that any proposed changes to strategy need to be approved by the pension trustees). Use interest rate swaps to hedge against adverse interest rate movements on the Society's balance sheet. Exploring options of potential scheme buy-out to third party insurer or by the Society.

Strategic Report (continued)

Business Performance (continued)

Risk (continued)	Impact (continued)	Mitigating Activities (continued)
Interest Rate Lower interest rates have an adverse impact on calculation of long-term liabilities.	Increased value of long-term liabilities reduce SCR coverage.	Look to match assets against technical provisions as closely as possible. Use of the transitional measure to recognise the impact of low interest rates under the Solvency II regime when compared with historic Solvency I position. Review investment strategy to achieve the best outcomes from a Solvency II perspective whilst achieving the right return for policyholders. Monitor the 10-year prescribed risk-free rate versus the rate at the last full valuation.
Expense Risk Inability to sell sufficient new policies to reverse the declining book and address the expense overrun.	Ongoing administration costs against continued decline in policies and income result in higher net cost to administer each policy. Increasing per policy costs against declining book.	Expenses are closely monitored and organisational restructuring undertaken to ensure the right cost base. Writing new profitable contracts of insurance to ensure the trend of reduced per policy costs continues. Clear marketing strategy and development of profitable products that meet customer needs and demand against an effective and cost efficient distribution strategy. Close monitoring of ongoing expenses against sales volumes. Models have been developed showing an estimate of the per policy expenses if business volumes continue at current run rates compared to the current per policy expense assumption so that management action can be taken in the event of material variances.
Operational Risk The Society's subsidiary, National Friendly Financial Solutions (NFFS), does not generate a profit.	The subsidiary does not provide a positive financial contribution to the Society, resulting in an increase in expense reserves resulting from lower intercompany recharges.	NFFS has its own business plan with stretch targets to include: - Improvement in performance and productivity - Reducing the dependency on one key lead provider - Acquisition of new client books Performance against plan is closely monitored and action taken as appropriate to control cost.
Governance Loss of key personnel and unable to recruit suitably qualified persons to fulfil key function roles including at Board level.	Loss of knowledge and expertise. Persons unwilling to take roles in highly regulated environment.	Competitive remuneration structure with ongoing development opportunities. Established agreements in place with recruitment agencies should the need for recruitment arise. Some functions may be outsourced. Use of specialist contractors as a short-term solution.

Risk (continued)	Impact (continued)	Mitigating Activities (continued)
Pandemic Risk The Society impacted by a global pandemic (COVID-19) putting increased strain on its systems, staff and investments.	Inability to operate business critical operations at full capacity with potential detriment to customer and suppliers. Brokers/sales channels unable to operate at forecasted levels resulting in fewer new policy sales. Health & Wellbeing of staff. Economic downturn resulting in reduced value of Society assets and / or increase in long-term liabilities resulting in reduced solvency coverage. This potentially has an adverse impact on policyholders Own Funds Unpredictable impacts on demographic risks (mortality, morbidity, longevity and lapses), potentially leading to greater claims pay-outs/reduced future surpluses.	**Operations** The Society has implemented working from home protocols and social isolation in line with Government guidelines whilst maintaining service through homeworking. We will continue to monitor the situation and take further action as necessary. We are able to continue to pay customers, suppliers and staff remotely using electronic means where possible. There has been no material impact on sales performance as both the in-house and broker sales channels continue to operate remotely. Sales performance is monitored against targets on a daily basis Regular communication to staff providing guidance and directing staff to Government and NHS advice. **Market Risk** The Board monitors the impact of changing market conditions on the Society's regulatory solvency position, and actions to manage the risk profile are implemented as required. **Demographic Risk** Experience is analysed regularly, and industry sources are taken into account, in order to detect trends.

Viability Statement

The Directors confirm that they have a reasonable expectation that the Society is well placed to manage its business risks, including those presented by the current pandemic, and will continue to meet its liabilities, as they fall due. Financial projections for the next five years are incorporated into the Society's Own Risk and Solvency Assessment ('ORSA'), and these confirm the Directors' expectation that the Society will continue in operation over this period, Own Funds and financial resilience progressively increasing with the passage of time. The Directors' assessment has been made with reference to the Society's current position and prospects, the Society's strategy, the risk appetite and principal risks and how these are managed, as detailed above.

The strategy and associated principal risks underpin the Society's plans and scenario testing, which the Directors review at least annually and form an integral part of the ORSA process. The central projection, the Directors' best estimate of future experience, makes certain assumptions about the level of new business, economic and demographic risks, insurance risks including morbidity, lapses and future expense assumptions.

The ORSA central projection is stress tested in robust downside scenarios including stresses for worsening economic and demographic experience, lapses and expenses over and above the central assumptions. Under these stress tests, the projections demonstrate that the Society continues to meet all of its liabilities as they fall due. The Board recognises that such future assessments are subject to a level of uncertainty that increases with time and therefore, future outcomes cannot be guaranteed or predicted with absolute certainty.

Strategic Report (continued)

Investment Performance

The Society's investments are held in a number of asset classes in particular fixed income, property and equities. These portfolios are managed by external property and fund managers whose performance is monitored on a regular basis by the Investment Committee.

Property

The commercial property market in 2020 saw a downturn from the positive returns of 2018 and 2019. Values in the fragile retail sector have continued to fall but the major influence on the market has been the effects of COVID-19. The contraction of the economy since March 2020 and the first lockdown has had a detrimental effect on tenant demand and this has put downward pressure on rental levels.

With the exception of the retail sector, prime property yields have remained fairly constant for those investments that provide secure income streams. The number of properties classed as 'prime' has shrunk as many occupiers who were previously deemed to be secure covenants have sought rent concessions and deferments from landlords. The appetite for risk has reduced and more investments are being classed as 'secondary' and being down valued.

From the Society's property investment portfolio there was just one sale during the year; a warehouse in Chesham, Buckinghamshire. Following a successful lease extension, the asset sold at a price reflecting a premium of 29% on its December 2019 valuation. There was one purchase; a fitness/gym investment in Birmingham City Centre entirely let to David Lloyd Leisure on a new 15-year lease. Taking into account the Chesham sale, the Society's property portfolio reduced in capital value by 5.6% during 2020. This compares with a reduction of 7.6% for All UK commercial property. The portfolio was 92% let at the year-end with just two office suites remaining vacant. Total contracted income return was 6.0%.

The uptake of the COVID-19 vaccines will hopefully bring a much-awaited boost to the economy including the property market. Ongoing asset management initiatives coupled with the letting of vacant space and a higher rent collection should achieve a solid rental return from the portfolio during 2021.

Since the year-end, taking advantage of approaches from interested parties, three properties have been sold for a combined sale value of £3.83m, £205,000 above the book value as at the year-end, the sale proceeds being re-invested in fixed income securities rather than replacement properties. The reduced property portfolio however remains a strategic investment backing our with profits policies.

Fixed Income

UK Government Bonds (Gilts) generated positive returns over the year as investors flocked towards 'safe-haven' assets amid the COVID-19 crisis and its associated impact on economic growth. To combat the crisis, the Bank of England (BoE) began to buy £200 billion of assets to support the economy. They increased this by a further £100 billion at its June 2020 meeting. The BoE also cut interest rates from 0.75% to 0.1%, setting borrowing costs at their lowest point in history.

The yield on short-dated Gilts fell below zero, setting new all-time lows amid the uncertainty surrounding Brexit. In contrast, longer-dated Gilt yields did not fall as much as markets reacted to the policy shift by the US Federal Reserve, which said it would be more willing to allow inflation to rise above its 2% target for some time and would worry less about the inflationary implications of very low unemployment. Furthermore, Gilt yields were also underpinned by concerns about a new, more infectious COVID-19 strain in the UK that threatened to derail the optimism over a vaccine-fueled rebound in economic growth.

For bonds issued by companies (also known as 'corporate bonds' or 'credit'), the spread of the COVID-19 pandemic resulted in unprecedented levels of volatility, resulting in credit spreads (the difference between the yields on corporate bonds and on Gilts) widening, to levels last seen during the global financial crisis. However, the significant monetary and fiscal stimulus on a global scale helped reverse the massive volatility witnessed in March 2020.

Later in the year, the risk sentiment was further supported by positive news regarding vaccine trials, Joe Biden's victory in the US presidential elections and as Brexit took full effect. The UK and EU clinched a post Brexit trade deal, with years of talks ending in a settlement allowing tariff-free trade.

The Society's portfolio performed well in absolute terms with returns of 10% for the 12-month period.

UK Equity

UK equities ended the year lower as the COVID-19 outbreak and resulting containment measures caused a sharp deceleration in economic activity and put pressure on company earnings, dividends and share prices. Nevertheless, unprecedented fiscal and monetary policy responses from authorities around the world and the development of viable vaccines lifted equities later in the period. Separately, Joe Biden's victory in the US presidential election (and expectations it could signal a new round of economic stimulus) and the agreement on a post-Brexit trade deal gave markets a significant boost towards the end of the year.

With-profits Review

Following further substantial falls in interest rates and the continued market volatility and uncertainty arising from the ongoing COVID-19 pandemic, the Society made the decision to reduce annual bonus rates across its product range.

Final bonus rates were also reduced, reflecting the market falls seen over the first half of 2020 because of the pandemic. The performance of the fund will continue to be monitored and at the relevant time, if markets have recovered sufficiently and other circumstances permit, bonus rates may increase.

Our Members

Engaging with our members

Being a mutual friendly society it is very important for us to engage with our members and we do this through our Annual General Meeting ('AGM') and Focus Group. Our Member Focus Group is made up of 45 members from across the Society and meets to discuss issues and ideas going forward usually twice a year. Our Focus Group members have a wide range of policies held with us and have diversity in age gender and national coverage.

Our Annual General Meeting (AGM)

In 2020, the AGM took place on 30th September at the Society's office, 11-12 Queen Square, Bristol BS1 4NT. As is the case for many similar organisations and in accordance with Government legislation in light of COVID-19, we made the decision not to invite attendees to the event. This was to prevent unnecessary travel and best protect our members, board and staff.

The Board and the Executive Committee were in attendance at the AGM, with some communicating remotely. The AGM gives the membership the opportunity to ask questions about the position of the Society, the events of the past year and where they would like to see the Society going in the future. All our members were encouraged to contact us and submit questions ahead of the AGM and these were considered at the meeting. A summary of the questions and responses, as well as minutes for the AGM, can be viewed on our website at www.nationalfriendly.co.uk/agm.

Fair customer outcomes

Our members and their best interests are always at the forefront of our thinking which we firmly believe delivers fair member outcomes at every step of the way.

To demonstrate our commitment to providing fair outcomes, we:

» Make sure that fair treatment of members is central to the Society's culture and values.
» Design and market products that meet our members' needs and perform as we have led them to expect.
» Provide members with clear information and keep them appropriately informed before, during and after point of sale.
» Make sure that any advice provided by National Friendly Financial Solutions is suitable and addresses the customer's needs.
» Use incentives for staff that reward behaviours that are consistent with the principles of fair member outcomes.
» Maintain service levels and processes that support members who need to make a claim or complaint.
» Do not create barriers for members to change product or switch provider.
» Have in place internal controls to monitor our achievement of these principles.

Strategic Report (continued)

Corporate Social Responsibility ('CSR')

Our vision
Our approach to CSR is a practical one; we look at ways in which we can make a fundamental difference to our people, the community and environment.

Our CSR Committee meets regularly to discuss new initiatives and drive our strategic vision, which is to:

- Develop two-way community involvement with our business
- Improve the health, safety and wellbeing of our people
- Operate ethical employment practices
- Achieve high standards in the environmental management of our business

Community
We work with local charities to support our CSR strategic vision and in this respect, we continue to work with Ablaze who we first started supporting in 2010 and for 2020 we also supported the Children's Hospice South West as our chosen Charity of the Year.

<u>Ablaze - Reading Buddies Programme</u>
The Society has been a trusted partner of Ablaze for many years, the charity formed and supported by Bristol's business community to connect local firms with education and help improve the opportunities available to Bristol's young people.

In normal times six of our staff members visit a local primary school during their lunch hour every week to read with the children, supporting the Ablaze Reading Buddy programme. The programme is intended to increase the amount of reading out loud opportunities pupils have, inspire them to read more and encourage them to gain a love of books.

With COVID-19 and the current restrictions in place to tackle the spread of the virus, the Ablaze Reading Buddy programme has been unable to operate as normal. At the date of this report schools are not able to welcome volunteers onto their premises and this is likely to be the case until the start of the next academic year (September 2021).

Therefore we supported Ablaze through Stories at Home, a Bristol City Council initiative which has been providing vulnerable families and disadvantaged pupils with access to books in their own homes during the COVID-19 lockdown.

We donated £1,000 to Cabot Primary School under the scheme. We were introduced to the school three years ago to help to raise the literacy attainment levels of pupils struggling with their learning and reading.

Ablaze's Primary Project manager Catherine Correia added:
"Although National Friendly's volunteer reading buddies are unable to read with their pupils at the moment, this generous donation will help to support the attainment and skill levels and make a difference to the lives of local people. It is a wonderful example of a great partnership and strong collaboration."

Bristol City Council teaching & learning consultant Debbie Miles said:
"Books are such a vital tool in every young person's life. They really do unlock doors, inspire and support as well as enhance the learning for children in a fun and effective way. This donation from National Friendly will provide books which will go on giving year after year."

As part of our ethos, we have always been enthusiastic about getting involved in projects which will help shape the future for young people. We will continue to work with Ablaze to develop a safe and successful way to deliver their impact to local schools throughout the city of Bristol.

Queen Square Association
The Society is a member of the Queen Square Association, a registered charity, formed in June 1999 comprising interested residents and occupants of Queen Square, Bristol. Its aims are to protect, maintain, repair, beautify, restore and advance the historical value of Queen Square

for the benefit of its members and those visiting Bristol, and has the responsibility of raising funds along with the help of lottery funding.

The Association also recognises that an improved environment can be highly beneficial to the businesses situated on the Square, and we play an active role in building a positive relationship with our neighbours.

People

We pride ourselves on the quality of our staff and keeping them involved as we develop our strategy. We have committed staff who continue to deliver a high quality of service to our members and contribute to the achievement of our strategic objectives.

The Society recognises the importance of continuing development and supporting our staff to achieve their goals and every member of staff has agreed objectives and annual appraisals to assess performance against these objectives and demonstration of the Society's values.

The Society's values are:

» Customer Orientated
» Fair
» Focused
» Innovative
» United
» Responsive
» Empowered

Environment

We recognise that, like any organisation, the activities we undertake will have an impact on the environment around us. We therefore continually seek initiatives from our staff so that we operate on as much of a carbon neutral basis as is possible. Our strategy is therefore to:

» Reduce our energy consumption and increase energy efficiency through the appropriate use of office equipment, lighting and heating.
» Eliminate waste where practicable.
» Make use of recycled or recyclable material.
» Work with suppliers who adopt similar or higher environmental standards.

The printers we use are sourced from accredited Forest Stewardship Council ('FSC') printing companies, meaning that our choice of paper is produced from well-managed forests and/or recycled materials. They are Bristol based and less than three miles away from our office.

We use both digital and lithoprint technology to print our policy literature, enabling us to select the most economical way of printing. Two types of ink are used. Toner is used for digital printing and vegetable-based ink is used for lithoprint.

We also send policy literature electronically and will increasingly seek to do this wherever possible. If you would prefer to receive your policy documentation via email, please contact our Customer Services team on 0333 014 6244 and they will update your records accordingly.

Our Foundation Fund

The Society's Foundation Fund provides strong support to our approach to CSR albeit under the direction of an independent Foundation Fund Committee.

The Foundation Fund has the general aim of making discretionary grants for the following purposes:

» To provide benevolent support to any member of the Society or their family at a time of need.
» For any activity or undertaking which promotes the engagement of the Society with its membership.
» To provide additional services or benefits to any or all of the Society's members/families.

The objectives of the Foundation Fund are in line with the Society's long standing aims of supporting its members at times of need. The aim is to award grants and disbursements that, regardless of relative value, are meaningful and make a significant difference to the recipients.

Members of the Society or employees can make applications by submitting a completed application form, which can be obtained by contacting the Society via www.nationalfriendly.co.uk/contact-us/. Disbursements are reviewed and agreed by the Foundation Fund Committee.

Strategic Report (continued)

Our Charity of the Year

Our staff choose a 'Charity of the Year' to raise funds for on an annual basis. Firstly, all staff are invited to nominate charities, which they are passionate about. The CSR committee, against pre-agreed selection criteria, then reviews nominations to create a shortlist. All staff then vote from the shortlist for their preferred charity of the year and the charity with the most votes is selected.

2020 has been wrought with challenges for the charity sector, in particular our charity of the year, Children's Hospice South West ('CHSW'), who have been raising awareness about the financial troubles the hospice has been faced with, since the start of the coronavirus pandemic.

CHSW's three hospices have adapted their care for children and their families since the start of the coronavirus pandemic. Now only providing symptom management and end of life care in the hospice, care teams are visiting more families at home as well as providing support virtually for children and their families who have had to continuously self-isolate.

We were given the opportunity to innovate and support CHSW throughout 2020 and strategically reach out and deepen our relationship with them.

We became the sole sponsor of CHSW's very first Virtual Memories by Moonlight event which took place on 26th September 2020, our sponsorship contributed towards the event costs ensuring as much as possible raised from the event can help to provide vital support for children with life-limiting conditions and their families. Together we raised £26,000 for CHSW.

Staff raised further funds by taking part in sponsored runs and walks. All events were carried out virtually or solely completed to ensure safe social distancing.

Kiley Pearce, Fundraiser for CHSW said:

"This year more than ever we felt it was really important to still provide people with the opportunity to join together, albeit virtually, to remember and celebrate the lives of their loved ones. We are so grateful to National Friendly for all of their support in promoting the event and of course raising much needed awareness of CHSW across the region.

We aim to make a fundamental difference to local lives within our community, even with the lingering threat of the coronavirus pandemic. Our sponsorship has contributed massively to the fantastic amount of money that has been raised to help provide vital support for children with life-limiting conditions and their families."

On behalf of the Board

Graham Singleton
Chief Executive Officer
30 June 2021

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Corporate Governance Report

Corporate Governance Review

The Board is of the view that good corporate governance is fundamental to the Society's operations. To comply with best practice in corporate governance it aims to adhere to the principles of the Association of Financial Mutuals Corporate Governance Code published in January 2019 ("AFM Code"). The AFM Code provides a high-level approach to corporate governance, based on six key principles, whilst providing flexibility for the Society to explain the application and relevance of its corporate governance arrangements.

The Society has applied the AFM Code and provided statements to explain how it has followed each key principle in the way that is most appropriate to its business model and objectives.

Principle One - Purpose and Leadership

The Society's long-term objective remains to protect and enhance member value through improved Own Funds and excess assets so that it continues to act in the best interests of its members. It aims to achieve this by providing policyholders with products and services that help to look after their health and welfare and provide certainty and control over their wellbeing both now and in the future.

The Board formally reviews the Society's purpose and goals, at least annually, against the latest circumstances and market factors in order to guide the ongoing strategy, decisions and culture.

The Society's mutual ethos and values are essential to its future success and as an organisation, it will endeavour to work together to embed them and to promote them. The Society's current values are customer orientated and help to define its culture through promoting fairness and innovation whilst empowering colleagues to work together, responding to our customers' needs.

The Board sets key targets and objectives, which it monitors on a regular basis throughout the year. These targets change in line with the Society's objectives and priorities. For 2020, the Board has focused on developing and launching products in line with the Society's strategy whilst managing capital to achieve long-term sustainability.

The principal activities of the Society's subsidiaries are as follows:

- National Friendly Financial Solutions Limited provides telephone based financial services: distribution of National Friendly products and an independent advice and comparison non advised service;
- National Friendly Software Solutions Limited owns the intellectual property rights to a policy administration system. It licences this software to the Society as well as marketing the system to other similar insurers.

Principle Two - Board Composition

Role of the Board

The Board is the main decision making body for National Friendly. It determines the strategic direction and has responsibility for the overall management of the Society's business affairs. The Board sets the Society's values and standards and has overall responsibility for establishing that obligations to members and other stakeholders are understood and met. The Board monitors and oversees the Society's operations with the purpose of maintaining competent management, sound planning, robust and prudent risk and capital management, an effective internal control environment, a culture of risk awareness and ethical behaviour, and compliance with statutory and regulatory obligations.

The Board meets a minimum of six times a year and more often if necessary. Additionally, it meets at least once a year to undertake a detailed review of the Society's strategy.

The Board sets out its responsibilities and the structure of delegation of authority by the Board to management, as required by regulation and the Society's rules.

The Society maintains liability insurance for all officers throughout the year.

Chair and Chief Executive

The role of the Chair and Chief Executive are held by different people and are distinct and separate in their purpose.

The Non-Executive Chair is responsible for leadership of the Board and making sure that the Board acts effectively and has no involvement in the day to day business of the Society. The Chief Executive has overall responsibility for managing the Society and its subsidiaries and for implementing the strategies and policies agreed by the Board.

Appointments to the Board

The appointment and re-election of Directors is considered by the Nominations Committee (see page 25), which makes recommendations to the Board. The Society seeks to have broad experience and diversity on the Board. There is focus to increase Board diversity without compromising on the calibre of directors and therefore, Board appointments are always made on merit as well as the skills, knowledge and experience of the Board as a whole.

All Directors are subject to election by members at the AGM following their appointment and re-election at least every three years. Any Non-Executive Director who has served the Society for longer than nine years or has attained age 70 is subject to annual re-election. In addition, all Executives and Non-Executives performing a Senior Management function are subject to approval from the Prudential Regulation Authority ('PRA') and / or the Financial Conduct Authority ('FCA') under the Senior Managers & Certification Regime ('SM&CR').

Professional Development

The Chair ensures that, on appointment, all Directors receive a comprehensive induction programme. Non-Executive Directors update their skills, knowledge and familiarity with the Society through meetings with the Executive, including access to key functions and through attending external seminars and training.

The Board has access to independent professional advice at the Society's expense where they consider it necessary to discharge their responsibilities. In addition, all Directors have access to the advice and services of the Secretary who is responsible for ensuring the Board procedures are complied with and advising the Board, through the Chair, on governance matters.

Board Balance and Independence

The Board consisted of five Non-Executive Directors and two Executive Directors for the majority of 2020. Two long-standing Non-Executives Directors retired at 30 September 2020, replaced by two new Non-Executive Directors appointed in June 2020 and September 2020.

The Board continues to review its own balance, completeness and appropriateness to meet the complexities of the business end to ensure that there is adequate succession planning. The Board has and will continue to assess the balance of skills, experience and knowledge and as necessary will appoint individuals to meet the Society's business needs.

The Board has appointed Mark Searles as Senior Independent Director ('SID') (to replace Geoff Brown who held the SID role prior to being appointed Chair, after Peter McIlwraith resigned on 30 September 2020). The SID provides a sounding board for the Chair and serves as an intermediary for other directors. The SID is also available to members if they have concerns where contact through the Chair or Chief Executive Officer has failed to resolve a matter or for which such contact is inappropriate.

The Society considers the review of the Board's performance to be an essential part of good corporate governance. The evaluation considers the balance of skills, experience, independence and knowledge of the members of the Board, including its diversity, how the Board works together as a unit, and other factors relevant to its effectiveness.

The composition and effectiveness of the Board was reviewed and refreshed in 2020 and following this, a Governance health check review was completed by the Society's internal auditors, Mazars LLP.

Corporate Governance Report (continued)

Principle Three - Director Responsibilities

Accountability

Board members have a clear understanding of their accountability and responsibilities.

The Directors, Committee members and the wider management team complete annual declarations on Code of Ethics and Conduct, confirming that they have behaved in accordance with the Society's expected behaviours and values.

The SM&CR provides a regulatory framework for the standards of fitness and propriety, conduct and accountability to be applied to individuals in positions of responsibility at insurers. All Directors, including Non-Executive Directors not formally approved by the regulator are subject to the regulators' Conduct Rules.

In addition, each Director has declared any potential conflicts of interest. Appropriate safeguards are implemented where there could be any potential conflicts. These declarations are collated by the Compliance Manager and reported to the Board as appropriate.

Committees

The Board has established sub committees, under its overall authority, and delegated certain governance responsibilities. Further details of the responsibilities and activities of these Committees are provided on pages 24-25. A Non-Executive Director chairs each committee and all members are considered to have appropriate skills and expertise to undertake their role within the committees.

Information

The Chair has responsibility for overseeing that all Directors receive accurate, timely and clear information, which is fundamental to the effective function of the Board. The information covers all key aspects of the business including the strategy, risks and opportunities, operational matters and financial performance and market conditions.

The Society has robust systems and controls in place to ensure the integrity of the information. Key information is collated from the Society's various finance and administration systems and prepared by relevant internal functions, managed by employees that are appropriately qualified. Financial information is externally audited on an annual basis and the internal audit function provides independent assurance on the effectiveness of the system of internal control.

Principle Four - Opportunity and Risk

Opportunity

The Board considers long-term strategy and opportunities each year as part of the annual planning process. Informed decisions on the future strategy and opportunities are based on financial projections for the next five years that make certain assumptions about the level of new business, economic and demographic risks, insurance risks including morbidity, lapses and future expense assumptions. The overall objective remains to achieve a sustainable and growing business in order to enhance member value through improved Own Funds and excess assets.

Risk

Risk management is an integral part of the Society's business activities to ensure that the strategic objectives are met. The integrated approach ensures that value is created by identifying the right balance between risk and reward, whilst making sure that obligations are met and the outcomes remain in the best interest of policyholders.

The extent to which the Society tolerates risks is described by the performance indicators, operational parameters and process controls set out in its 'Risk Appetite'.

The Society's risk appetite includes the level of action/mitigation to be implemented against identified risks. There is direct interaction between the risk appetite and those risks highlighted in the risk assessment. Risks are rated on impact and probability and it has been determined that any risk with a residual risk rating 'high' will require an action plan which will state what action is to be taken and on what timescale.

The management of risk is the responsibility of the Board and staff at all levels of the Society. The Board is supported in its role in this regard by sub-committees, who ensure that inherent and emerging risks are identified and managed appropriately and in a timely manner. The Strategic Report includes key risks that are presented at least quarterly and monitored by the Risk & Compliance Committee.

Principle Five - Remuneration

The Remuneration Committee has clear terms of reference and is responsible for making recommendations to the Board concerning the remuneration strategy, framework and benefits for Executive Directors and key function holders. In doing so, the Committee can take advice from external consultants on best market practices and remuneration benchmarking.

The Board has established a clear remuneration policy that outlines the key remuneration principles and framework for the Society. The Society's approach to remuneration is an integral part of the Business strategy and the policy is designed to attract, retain and motivate competent, experienced and skilled staff. This policy covers all Directors and employees of the Society.

Principle Six - Stakeholders

The Board recognises that good governance and effective communication are essential on a day-to-day basis to deliver purpose and protect the Society's brand, reputation and relationship with stakeholders including its members, intermediaries, suppliers and employees.

The Society's strategy is aligned with long-term aspirations for sustainability and enhancing member value.

The Board is committed to maintaining good communications with members. In order to fulfil this commitment, a Members' Focus Group and Research Community have been established. Engagement with the Focus Group has been positive and feedback valued. The Board also firmly believes in the principles of Treating Customers Fairly and adheres to these in its day-to-day operation.

Communication with staff is undertaken through regular dialogue with staff, as groups, individually and through the organisation's intranet (with upward feedback positively encouraged). Open meetings are also conducted with the Chief Executive and other members of the Executive Committee.

The Society is committed to the ongoing development of its staff and actively engaging with its workplace. Employee engagement surveys are also performed to highlight areas of improvement in communication of the Society's purpose and objectives. The Executive Committee considers the results of these surveys in order to identify initiatives to improve employee engagement and satisfaction. The Society achieved a 1* accreditation for very good levels of workplace engagement by Best Companies in January 2020.

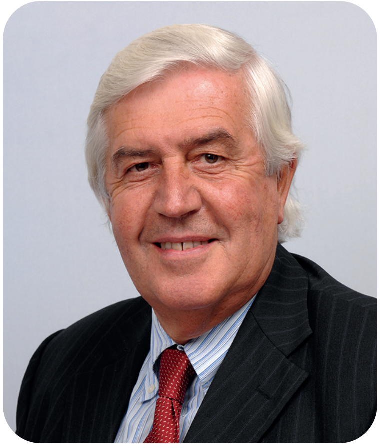
It is important to the business that any malpractice, misconduct or wrongdoing by employees, agency workers and contractors of the Society is reported and properly dealt with. The Society therefore encourages all individuals to raise any concerns that they may have about the conduct of others in the business or the way in which the business operates.

A Whistleblowing Policy is in place, which sets out the way in which individuals may raise any concerns that they have and how those concerns will be dealt with.

Corporate Governance Report (continued)

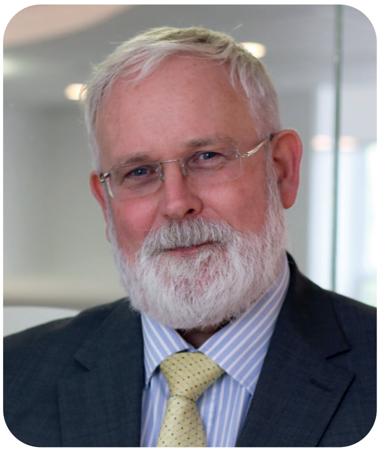
The Board

Geoff Brown
(Chair)



Geoff is a qualified Actuary and had 44 years of experience in the financial services industry before retiring in late 2013. He spent most of his career in the health and care sector including 20 years with international healthcare company BUPA Limited, where he held a variety of roles and responsibilities – most recently as Chief Risk Officer of the BUPA Group and prior to this as Director of Compliance and Chief Actuary of the UK division. Geoff is also currently a Non-Executive Director of Medicover Forsakrings AB (publ.) and Chair of its Compliance and Risk Committee. Medicover is a Swedish insurer that provides healthcare insurance propositions for individuals and companies in Poland, Romania and Hungary. Geoff joined the National Friendly Board as a Non-Executive Director in June 2014, he was appointed Chair in May 2021 subject to regulatory approval.

Graham Singleton
(Chief Executive Officer)



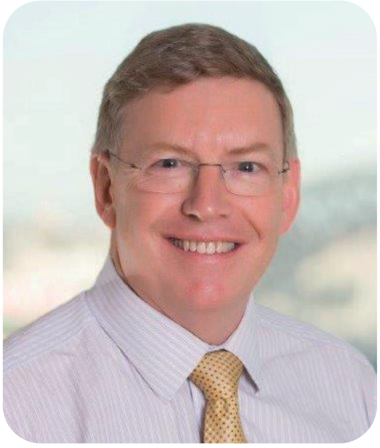
Graham is a qualified Actuary with over 35 years of experience in the financial services industry. He spent most of his career in Life and Pensions. He held Chief Actuary and Chief Financial Officer roles in various companies before latterly becoming CEO of the Phoenix Resolution Life Companies and Swiss Re's UK insurer Reassure Limited, and its Life and Pensions Outsourcing business Admin Re Limited. He has performed non-executive work covering a variety of financial services disciplines including consumer finance as a non-executive of the Very Group Finance Company Limited and general insurance for a niche provider of buildings insurance backed guarantees, Guaranteed Protection Insurance Limited. Graham joined the National Friendly Board as a Non-Executive Director in December 2019 and was appointed as Interim CEO in February 2021. The appointment was made permanent in April 2021.

CHAIR'S REVIEW
STRATEGIC REPORT
CORPORATE GOVERNANCE REPORT
THE DIRECTORS' REPORT
AUDIT COMMITTEE REPORT
RISK AND COMPLIANCE COMMITTEE REPORT
NOMINATIONS COMMITTEE REPORT
DIRECTORS' REMUNERATION REPORT
INDEPENDENT AUDITOR'S REPORT
CONSOLIDATED INCOME STATEMENT
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
CONSOLIDATED BALANCE SHEET
NOTES TO THE FINANCIAL STATEMENTS

Julian Ellacott
(Chief Actuary)

Julian joined the Society in July 2020 to lead the internal Actuarial Function. He qualified as a Fellow of the Institute of Actuaries in 2003, and has over 20 years' experience working in the life insurance sector. He spent nearly 10 years working for the international consultancy Watson Wyatt (now part of Willis Towers Watson), advising all types of insurer, from friendly societies to multinationals. For the 11 years immediately prior to joining the Society he worked for Just Retirement (now Just Group), in a variety of actuarial roles spanning risk and capital management, pricing and corporate development. Julian was appointed to the Board as an Executive Director in May 2021, and also asked to act as Chief Actuary for the Society subject to regulatory approval.

Mark Searles
(Senior Independent Director)



Mark has held senior executive and Board positions within the Financial Services and Technology sectors. He most recently spent 9 years in Australia, as Group CEO & Managing Director of AUB Group Ltd, Australasia's largest, listed, equity-based Risk Management group. Prior to moving to Australia, Mark held senior management positions with Zurich; LloydsTSB; HSBC; Sage and American Express. Returning to the UK in 2019, he is currently a Haberdashers-appointed Governor of an Education Academy Trust (Chairing their Audit Committee) in addition to holding various Advisory roles. Mark joined the National Friendly Board as a Non-Executive Director in June 2020; and was invited to act as Senior Independent Director in May 2021. This is subject to regulatory approval.

Mary Gavigan
(Non-Executive Director)

Mary is a Fellow of the Institute of Chartered Accountants in England & Wales. She has specialised in the Financial Services sector for over 25 years acting as consultant and advisor as a FS (insurance) expert with a focus on restructuring and business transformation. She has also held interim Chief Finance Officer roles during her career. Mary spent most of her career at KPMG and other advisory firms. She is a Non-Executive Director of STM Life Assurance PCC PLC where she is Chair of its Audit Committee as well as a member of its Risk Management Committee. Mary's charity work includes being a Trustee and Non-Executive Director of Epilepsy Research UK. Mary joined the National Friendly Board as a Non-Executive Director in September 2020 and acts as Chair of the Audit Committee, this position is subject to regulatory approval.

Corporate Governance Report (continued)

Committee Information

The Terms of Reference of the Audit, Risk & Compliance, Investment, Nomination and Remuneration Committees are available on the Society's website and on request to the Secretary.

Audit Committee

Current Members

Mary Gavigan (Chair) – Appointed to the committee on 1 October 2020 and to Chair on 5 March 2021

Mark Searles – Appointed 1 October 2020

Other Members

Graham Singleton (Chair) – Appointed 1 October 2020; Resigned 5 March 2021

Peter McIlwraith – Resigned 30 September 2020

Mark Jackson – Resigned 30 September 2020

The Audit Committee meets at least four times a year at appropriate times in the financial reporting and audit cycle. The main function of the Committee is to assist the Board in fulfilling its oversight responsibilities, specifically the ongoing review, monitoring and assessment of:

» The integrity of the financial statements and reviewing significant financial reporting judgements contained in them.

» The effectiveness of internal control and risk management processes.

» The effectiveness of the internal and external audit functions and processes.

» The recommendation to the Board in relation to the appointment, reappointment, remuneration and removal of the external auditors.

» The objectivity and independence of the external auditor in respect of the provision of any non-audit services.

» The arrangements by which staff within the Society may raise concerns, in confidence, about possible improprieties in matters of financial reporting or other matters.

The Executive Directors and internal and external auditors attend meetings of the Committee as appropriate. The internal and external auditors may also meet separately with the Committee without the Executive Directors or any other members of staff present.

Internal audits of the regulated business are conducted by Mazars LLP and reported to the Committee.

Investment Committee

Current Members

Geoff Brown (Chair) – Resigned 30 September 2020; Re-appointed 20 May 2021

Mary Gavigan – Appointed 1 October 2020

Graham Singleton – Appointed 1 October 2020

Mark Searles – Appointed 20 May 2021

Julian Ellacott – Appointed 20 May 2021

Other Members

Tracy Morshead (Chair) – Resigned 20 May 2021

Sandy Richards – Resigned 14 May 2021

Jonathan Long – Deceased 14 December 2020

Peter McIlwraith – Resigned 30 September 2020

The Investment Committee meets as required but at least three times a year to review compliance with the terms of the Principles and Practices of Financial Management in relation to the investment strategy and review its continuing appropriateness in the light of changing circumstances with consideration to the needs of both with-profits and non with-profits policyholders. The Committee also has responsibility for:

» Appointing the Society's Investment Fund Managers.

» Determining the asset allocation and performance benchmarks.

» Monitoring the performance of the Funds and of the Fund Managers.

Nomination Committee

Current Members

Mark Searles (Chair) – Appointed 1 October 2020
Mary Gavigan – Appointed 1 October 2020
Geoff Brown – Resigned 30 September 2020; Reappointed 20 May 2021

Other Members

Graham Singleton – Appointed 1 October 2020; Resigned 1 April 2021
Peter McIlwraith – Resigned 30 September 2020
Tracy Morshead – Resigned 30 September 2020

The Nomination Committee meets as appropriate to review the structure, size and composition of the Board and to make recommendations to the Board with regard to any adjustments that are deemed necessary. Nominations for appointment to the Board are considered for approval by the full Board.

Professional recruitment consultants can be and are consulted to ensure that non-executive vacancies on the Board are considered appropriately.

Membership of the Committee may be altered as appropriate in particular to address circumstances where one of its members is being considered for re-appointment.

Remuneration Committee

Current Members

Mary Gavigan (Chair) – Appointed 1 October 2020
Mark Searles – Appointed 1 October 2020
Geoff Brown – Appointed 20 May 2021

Other Members

Tracy Morshead – Resigned 20 May 2021
Peter McIlwraith – Resigned 30 September 2020
Mark Jackson – Resigned 30 September 2020

The Remuneration Committee meets at least twice a year to establish, implement and maintain a remuneration policy and practices in line with the Society's risk management strategy, risk profile, objectives and risk management practices.

Further details on Directors' remuneration are set out in the Directors' Remuneration Report on pages 36-41.

Risk & Compliance Committee

Current Members

Geoff Brown (Chair)
Mark Searles – Appointed 20 May 2021
Mary Gavigan – Appointed 20 May 2021
Graham Singleton – Appointed 20 May 2021
Julian Ellacott – Appointed 20 May 2021

Other Members

Tracy Morshead – Resigned 20 May 2021
Jonathan Long – Deceased 14 December 2020
Sandy Richards – Resigned 14 May 2021

The Risk Management Committee normally meets at least four times a year. The main function of the Committee is to assist the Board in its leadership and oversight of risk across the Society including the understanding and, where appropriate, optimisation of current and future risk strategy, overall risk appetite and tolerance, risk management framework including risk policies, process and controls, and the promotion of a risk awareness culture throughout the Society. The Committee has the additional responsibility of providing oversight of the Society's governance and regulatory compliance arrangements and their on-going effectiveness.

The Chair of the Committee meets the Head of Finance & Risk at least once a year, without management present, to discuss their remit and any issues arising from the risk and control assessments that have been carried out.

With-Profits Advisory Arrangement

Current Members

Geoff Brown (Chair)
Mark Searles – Appointed 1 October 2020
Mary Gavigan – Appointed 20 May 2021

Other Members

Mark Jackson – Resigned 30 September 2020

The With-Profits Actuary attends meetings of the Advisory Arrangement as appropriate.

The With-Profits Advisory Arrangement meets as required and at least once a year to independently monitor and bring independent judgment on the extent to which procedures, systems and controls are adequate and effective to enable the Society to comply with the requirements of the FCA Handbook over the management and governance of with-profits business.

Executive Committee

The Executive Committee forms part of the Society's corporate governance structure. The Board is the main decision making body and the Executive Committee, whilst not a sub-committee of the Board, is charged (either individually or collectively) with running the Society's business within the delegated authority of the Board.

Corporate Governance Report (continued)

Attendance of Directors at Board and Committee meetings held during the year to 31 December 2020

	Board		Audit Committee		Remuneration Committee		Nominations Committee	
	Meetings attended	Meetings held	Meetings attended	Meetings held	Meetings attended	Meetings held	Meetings attended	Meetings held
Non-Executive								
Geoff Brown	13	13	4	4	1	*	1	1
Mary Gavigan	3	3	2	2	1	1	-	-
Mark Jackson	9	9	2	2	-	-	1	1
Peter McIlwraith	9	9	2	2	-	-	1	1
Tracy Morshead	12	13	3	*	1	1	-	1
Mark Searles	8	8	2	*	1	1	-	-
Graham Singleton	11	13	3	4	1	*	-	-
Executive								
Jonathan Long	12	13	3	*	-	-	1	*
Sandy Richards	13	13	4	*	1	*	1	*

	Investment Committee		Risk & Compliance Committee		With Profit Advisory Arrangement	
	Meetings attended	Meetings held	Meetings attended	Meetings held	Meetings attended	Meetings held
Non-Executive						
Geoff Brown	3	3	3	3	3	3
Mary Gavigan	1	1	2	*	2	*
Mark Jackson	-	-	-	-	1	1
Peter McIlwraith	2	2	-	-	-	-
Tracy Morshead	3	3	3	3	-	-
Mark Searles	1	*	2	*	2	2
Graham Singleton	3	3	3	*	2	*
Executive						
Jonathan Long	3	3	3	3	1	*
Sandy Richards	3	3	3	3	3	*

** Attendance on an invitation basis.*

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Directors' Report

Statement of Responsibilities of the Directors

The Board is required to prepare financial statements for each financial year, which give a true and fair view of the state of affairs of the Society as at the end of the financial year and of the results for that year. In preparing these financial statements the Board is required to:

» Select suitable accounting policies and then apply them consistently.

» Make judgements and estimates that are reasonable and prudent.

» State where applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements.

» Prepare the statements on a going concern basis, unless it is inappropriate to assume that the Society will continue in business.

» Prepare the financial statements in accordance with the Friendly Societies (Accounts and Related Provisions) Regulations 1994 and in accordance with the applicable accounting standards in the United Kingdom.

In following the Friendly Societies (Accounts and Related Provisions) Regulations 1994, this includes the two updates to this regulation: the Friendly Societies (Accounts and Related Provisions) (Amendment) Regulations 2005; and the Friendly Societies (Accounts and Related Provisions) (Amendment) Regulations 2008.

The Directors confirm that the financial statements comply with the above.

The Directors are responsible for keeping appropriate accounting records which disclose with reasonable accuracy, at any time, the financial position of the Society and to enable it to ensure that the financial statements comply with the Friendly Societies Act 1992. They are also responsible for safeguarding the assets of the Society and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for members to assess the performance, business model and strategy of the Society and the Group.

The maintenance and integrity of the National Deposit Friendly Society Limited and Group website is also the responsibility of the Directors.

Disclosure of Information to Auditors

The Directors that held office at the date of approval of this Directors' Report confirm that, so far as they are aware, there is no relevant audit information of which the Society's auditors are unaware, and each Director has taken all the steps they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Society's auditors are aware of that information.

Going Concern

The Society's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report for the year. The financial position of the Society, its cash flows, liquidity position and borrowing facilities have also been considered by the Board. The Society's policies and processes for managing capital are highlighted in Note 2 to the financial statements. The Society has adequate financial resources, supported by long-term relationships with its policyholders and suppliers. Therefore, the Directors believe that the Society is well placed to manage its business risks in respect of liquidity and cash flows. After making enquiries, the Directors have a reasonable expectation that the Society has adequate resources to continue in operational existence for a period to 31 December 2022. Accordingly, the financial statements have been prepared on a going concern basis.

Annual General Meeting

The 2020 Annual General Meeting was held in Bristol on 30th September 2020 and was attended by Board Members and Officers of the Society, although some were communicating remotely. As is the case for many similar organisations and in accordance with Government legislation in light of COVID-19, we made the decision not to invite attendees to the event. This was to prevent unnecessary travel and best protect our members, board and staff.

A number of resolutions were voted on including:

» The Board Report.

» The Directors' Remuneration Report.

» The Auditor's Report and the Annual Report and Financial Statements.

» Re-appointment of Ernst & Young LLP as Auditors.

» Re-election of Tracy Morshead and Geoff Brown as Non-Executive Directors.

» Election of Sandy Richards as Executive Director.

» Election of Graham Singleton, Mark Searles and Mary Gavigan as Non-Executive Directors.

The response from members submitting their postal/proxy forms was 11.1% of members eligible to vote electing to do so.

In 2021, the AGM is planned to be held in Bristol Hotel in September, members will be invited to attend the event. Members will be able to submit questions ahead of the date, in case there is further change in the Covid-19 regulations that would prevent members attending in person.

Employees

The average number of Directors and staff employed by the Group and Society is disclosed in Note 9 on page 77.

The aggregate remuneration paid to Directors and staff employed by the Group during the year amounted to £3.9m million (2019: £3.4 million).

Charitable Donations

The Society made charitable donations of £14,175 (2019: £6,672). There were no political donations (2019: £nil).

Change of Secretary

Dawn Carey resigned as Secretary on 30th September 2020. On 1st October 2020 Sandy Richards was appointed as Secretary. Sandy Richards resigned as Secretary on 14th May 2021. Keith Meeres was appointed as Interim Secretary on 20th May 2021.

Re-appointment of Auditors

A resolution to re-appoint Ernst & Young LLP ('EY') as the Society's external auditors will be proposed at the forthcoming AGM.

Approved by Order of the Board

Graham Singleton

Chief Executive

30 June 2021

Audit Committee Report

The Audit Committee's role is to consider all audit related matters, in particular, to review the Society's financial reporting arrangements, the effectiveness of its internal controls and its risk management systems; as well as the internal and external audit processes. Through the Committee the Board has established formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself regarding the integrity of the financial statements. The Committee met four times during the financial year. The Committee reports its activities to the Board and makes recommendations to the Board.

The key responsibilities of the Committee are noted below with examples of how it discharges its duties.

Audit Committee Key Responsibilities	
Financial Reporting	1. Monitoring the integrity of the Society's financial statements and reviewing critical accounting policies, judgements, and estimates. 2. Reviewing the appropriateness of the going concern basis for preparing the financial statements. 3. Providing advice to the Board on whether the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and it provides the information necessary for members to understand the Society's position and prospects, including performance, business model and strategy.
External Audit	1. Reviewing the continued objectivity and independence of the external auditor, including the level and appropriateness of non-audit services. 2. Considering the appointment, removal, performance and remuneration of the external auditors. 3. Considering the planning, scope and findings of the annual external audit, the receipt of, and responses to, the auditor's management letter and reviewing the degree of liaison with internal audit. 4. Reviewing the effectiveness of the external audit process, considering relevant UK professional and regulatory requirements.
Internal Controls and Risk Management	1. Reviewing the adequacy and effectiveness of the Society's internal financial controls and internal control and risk management systems in conjunction with reviewing reports produced by internal and external audit. 2. Reviewing the statements to be included in the Annual Report concerning internal controls and risk management.
Internal Audit	1. Considering and approving the strategic and annual plans. 2. Considering management responses to recommendations. 3. Monitoring and reviewing the effectiveness of internal audit. 4. Considering the appointment, removal, performance and remuneration of the internal audit firm.

Membership, skills and experience

The Audit Committee acts independently of the Executive to ensure that the interests of members are properly protected in relation to financial reporting and internal control.

All members of the Audit Committee are Non-Executive Directors. The external and internal auditors regularly attend Committee meetings. The Chair of the Audit Committee is a Chartered Accountant who specialises in financial services with significant relevant accounting and audit competence. The Committee has competence relevant to the life and health insurance sector. The Committee has reviewed the collective skills of members and concluded that the balance of skills, knowledge and experience of the Committee is appropriate.

Internal Control and Risk Management

Details of the risk management systems in place are provided within the Risk and Compliance Committee report on page 33. The Audit Committee was satisfied that internal controls over year-end financial reporting were appropriately designed and operating effectively with one exception as described in note 30 on page 97.

The Audit Committee and Risk and Compliance Committee work together effectively to cover all relevant issues and ensure that any pertinent areas of overlap are appropriately addressed.

Whistleblowing

The Committee is responsible for reviewing the adequacy and security of the Society's whistleblowing arrangements for its employees and contractors to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. As part of this responsibility the Audit Committee ensured that whistleblowing arrangements allow proportionate and independent investigation of such matters.

Internal Audit

Internal Audit is outsourced to Mazars. During 2020, the Audit Committee monitored the effectiveness of Internal Audit and the Internal Audit programme, approving the audit plan and budget, and confirming that appropriate resources were in place to execute the plan effectively.

In the year ended 31 December 2020, Internal Audit carried out a significant number of audits of varying size and complexity. The findings from each individual review are presented to the Audit Committee including management responses. The Audit Committee considers the adequacy of management responses and the implications of significant findings on the effectiveness of the overall internal control system and the Risk Management Framework.

During the year internal audit reports were received on a wide range of subjects, including:

» Revenue Recognition
» Product Development and Governance
» Payroll
» Operational Resilience
» Outsourced Health Claims Processing (to Axa)
» Governance Health check

Independent External Auditor

The Audit Committee is responsible for assessing the effectiveness of the annual audit process, for monitoring the independence and objectivity of the external auditor and for making recommendations to the Board in relation to the appointment of the external auditor.

EY has been the Society's external auditor since September 2017 and they have carried out the external audit work for each financial year since the year end 31 December 2017. A resolution proposing the re-appointment of EY as the Society's external auditor was put to the members at the 2020 AGM and approval gained.

The Committee continues to assess the independence, the objectivity of the external audit and the effectiveness of the audit process on an ongoing basis. The external auditor is required to rotate the audit partner responsible for the Society audit every five years.

The Society has policies in place, which aim to safeguard and support the independence and objectivity of the external independent auditors. One such policy requires the prior approval of the Audit Committee for the engagement of the independent auditors for non-audit work. The external auditor (EY) did not undertake any non-audit assignments during 2020.

Audit Committee Report (continued)

Financial Reporting - Areas of particular focus

The Audit Committee considered the following significant judgments and estimates, in light of the reports received from external auditors and discussions with external auditors and management.

Significant Issue	How it was addressed
Assessment of actuarial demographic assumptions for morbidity, mortality, longevity and persistency	The Society has in place procedures to analyse experience on its insurance contracts. Sophisticated valuation methodology is used whereby statistical analyses are used alongside available industry data to assess the best estimate demographic assumptions. The general process for setting assumptions has not changed for 2020 year-end (although some changes were made to methodology for some individual assumptions). Valuation assumptions are set with regard to the Society's own experience (given the uniqueness of the healthcare policies) taking into account trends in the actual versus expected experience. As much relevant data as possible is used to improve the reliability of any estimates of future experience. Lapse experience is monitored on a monthly basis throughout the year. Allowance is made for significant non-recurring events in experience, but which are unlikely to influence subsequent experience.
Assessment of assumptions relating to expenses	Renewal expenses are determined using per policy expenses equal to the level of expected administration costs in 5 years' time divided by the expected volume of business in force at that time. An Additional Expense Reserve is held on top of this, to cover the shortfall in expense margins over a 5 year period, until the volume of business reaches scale. The projection of the expected volume of business is based on the most recent sales projections, as well as demographic and lapse assumptions. The Audit Committee is satisfied that, considering all material factors, the approach is reasonable and one that reflects its best estimate of future experience.
Impact of COVID-19 on going concern and viability	The COVID-19 pandemic has had significant impact on the Society (see note 2 Capital Management on page 60) none of which have had an impact on the going concern and viability to the Society since the Society has been able to manage the circumstances that COVID19 has presented. The primary issues faced are: » The initial negative impact on financial markets, which has largely now reversed. » The reduction in claims on health policies, which the Society has made allowance for reversing once pandemic related restrictions are relaxed. Longer term impacts of COVID-19 on mortality, morbidity, lapses and financial markets are unclear. The Society does not expect there to be further impacts on its viability. After taking into account emerging industry opinion and practice, long term assumptions have not changed in response to the impacts of COVID-19.
Internal control breach and follow up Investigation in relation to this	Following a review of one of its subsidiaries, during quarter one of 2021, the board became aware on an internal control breakdown. In the circumstances advice was sought and the matter is being investigated (see note 30).

Furthermore, it is the role of the Audit Committee and the Board to consider key assumptions in the preparation of the financial statements including the valuation of property and determination of pension deficit.

Mary Gavigan
Chair of the Audit Committee
30 June 2021

Risk and Compliance Committee Report

Embedding a strong risk management culture is a strategic priority across the Society supported by robust risk management and controls.

The Risk and Compliance Committee assists the Board in its leadership and oversight of risk including the understanding and, where appropriate, optimisation of current and future risk strategy, overall risk appetite and tolerance, risk management including risk policies, process and controls, and the promotion of a risk awareness culture throughout the Society.

Risk is integrated into the culture of the Society with an effective policy and a programme led by the Board, delegated through this Committee and to the Society's Operational and Conduct Risk Forum.

Key responsibilities of the Risk and Compliance Committee
Review and recommend the approval of the risk management, compliance and governance framework across the Society
Keep under review the Society's compliance with statutory and regulatory requirements
Make recommendations to the Board concerning the Society's overall risk appetite, tolerances and strategy
Monitor and review the Society's management of the financial risks of climate change
Advise the Board on proposed strategic transactions including significant acquisitions or disposals
Review, update, and test business continuity plans on a regular basis
Review the Society's procedures for the prevention and detection of bribery and corruption; and money laundering
Review and monitor management's responsiveness to the findings and recommendations of the Operational and Conduct Risk Forum

The Risk and Compliance Committee and the Audit Committee work together to cover all relevant issues and to avoid duplication.

Membership

The Committee consists of at least four members, with at least two being independent Non-Executive Directors of which one is the Chair.

The Committee met four times during the financial year, one of these being integrated into a Board meeting to consider Risk Appetite.

At each meeting we receive a comprehensive risk management report and a risk appetite dashboard report, which contributes to a Key Risk Indicator dashboard presented to the Board on a quarterly basis.

During 2020 we also received the Society's:

» Annual Risk Management Report

» Annual Operational Compliance Report

» Annual Money Laundering/Financial Crime Report

» Annual Business Continuity/Disaster Recovery Report

Progress in 2020

The Society continued to refresh and strengthen its approach to risk management during the year and will further embed this capability within the business.

While the Society placed significant risk management focus on the pandemic, with a particular emphasis on the safety and resilience of our people and members, we have continued to focus on our wider risk management agenda, including:

» reviewing the approach of setting the Society's risk appetites, including the articulation of the associated measures and triggers for action

» reviewing specific aspects of risk as they arise in the external environment and focusing on specific areas of risk for our health and protection businesses

» reviewing our strategic and emerging risk profiles

Risk and Compliance Committee Report (continued)

- reviewing our climate change risk profile and evaluating our approach to enhancing climate change risk management and disclosures
- reviewing our approach to the calibration of our solvency risk appetite statement to update for changes in our risk profile
- improving our regular risk reporting to the Board to assist in its effective oversight
- continuing to improve our wider information technology capabilities and IT operational resilience controls.

Risk management

The Society's risk management framework seeks to ensure that there is an effective process in place to manage risks. Risk management is integral to all aspects of the Society's activities and is the responsibility of all staff. Managers have a particular responsibility to evaluate their risk environment, to put in place appropriate controls and to monitor the effectiveness of those controls. The risk management culture emphasises careful analysis and management of risk in all business processes.

We review the risk management framework at least annually and receive regular reports from the Operational and Conduct Risk Forum.

Risk is assessed and managed under the following risk categories:

Risk	Definition
Market Risk	The risk that the Society's solvency coverage is adversely affected by changes to financial market conditions, which impact the fair value of assets held.
Credit Risk	The risk that a counterparty is unable to fulfil its obligations to the Society, thereby leading to a loss of financial assets.
Insurance Risk	The risk that the actual demographic (mortality, morbidity, lapse) experience and/or expenses of administering policies is worse than assumed in the calculation of best estimate liabilities
Liquidity Risk	The risk that the Society is not able to meet its financial obligations to policyholders and other creditors when they become due and payable.
Operational Risk	The risk of direct or indirect loss (actual or potential) resulting from inadequate or failed internal processes, people and systems or from external events. This includes risks relating to compliance, business processes, information technology, outsourcing and financial reporting
Conduct Risk	The risk that the Society's behaviour results in poor outcomes for customers and the market as a whole.
Other Material including Pension	Any other risks that may cause loss or harm to the Society and/or its members.
Emerging Risk	Potential emerging risks to which the Society may be exposed

The Board has identified key threats to business strategy and mitigation plans have been put in place so that the Society can remain sustainable and continue to operate in the best interests of its members. These risks are summarised on pages 8-11.

Geoff Brown
Chair of the Risk and Compliance Committee
30 June 2021

Nominations Committee Report

The Nomination Committee meets as appropriate to review the structure, size and composition of the Board and to make recommendations to the Board with regard to any adjustments that are deemed necessary. Nominations for appointment to the Board are considered for approval by the full Board.

Professional recruitment consultants can be and are consulted to ensure that non-executive vacancies on the Board are considered appropriately.

Membership of the Committee may be altered as appropriate in particular to address circumstances where one of its members is being considered for re-appointment.

The unfortunate circumstances within the year relating to the untimely death of Jonathan, our CEO, meant that the Nomination Committee was required to undertake a greater number of assignments than the norm. The most important of these was to manage the search and selection process of a new CEO for the Society culminating in a recommendation to the Board. The committee appointed an external executive search firm to undertake a broad market search and a shortlist of quality candidates was prepared who were then subject to interviews by the committee and Board members. At an early stage, Graham Singleton indicated his desire to become a candidate and he stepped away from involvement in the assessment process to ensure there was no conflict of interest. Having undertaken a comprehensive interview and review process the committee was unanimous in its' recommending to the Board that Graham be appointed as the new CEO. The Committee was also active post the resignation of Sandy Richards as Executive Director and recommended to the Board the appointment of Julian Ellacott as an Executive Director.

Other activities of the Committee during the year included the recommendation to the Board relating to the appointment of Mary Gavigan and myself as Non-Executive Directors replacing Peter McIlwraith and Mark Jackson who stepped down from the Board in mid-2020.

At all times, the Committee has ensured best practice has been followed in the recommendation of new Board Director appointments and has taken responsibility for managing the processes necessary in ensuring the relevant outcomes have been achieved on behalf of our members.

Mark Searles
Chair of the Nomination Committee
30 June 2021

Directors' Remuneration Report

Introduction

The Society is committed to a framework which recognises and rewards contribution that individuals make. This Report of the Directors on remuneration explains how the Society applies the principles in the Annotated Code of Corporate Governance relating to remuneration.

The Remuneration Committee keeps itself informed of relevant developments and best practice and is authorised at its discretion to obtain advice from external advisers.

Remuneration Committee

The Remuneration Committee is appointed by the Board and all members of the Committee are Non-Executive Directors. The CEO and / or other relevant Executive Officers attend meetings as appropriate. Mary Gavigan and Mark Searles were appointed to the Committee on 1 October 2020 after Peter McIlwraith and Mark Jackson resigned on 30 September 2020. On 20 May 2021 Tracy Morshead also resigned and was replaced by Geoff Brown.

The Committee, within the terms of the Remuneration policy agreed by the Board, sets the level of remuneration for the Chief Executive and other Executive Directors. The Committee also sets the proposed level of fees for the Chair, having taken advice from the Executive Directors. The Chair takes no part in the setting of his own remuneration.

Policy

The Society's approach to remuneration is an integral part of the Business strategy and the policy is designed to attract, retain and motivate competent, experienced and skilled staff. The policy is based on the following principles:

a. Reward and remuneration will be clear and up to date with the market so that individuals are motivated and the Society is able to attract and retain key talent.

b. Remuneration package will be competitive and recognise the relative remuneration in comparable markets through benchmarking.

c. Remuneration will be determined fairly and objectively across the Society.

d. Variable reward for the Directors and key function holders will be linked to strategic objectives as well as considering current and future risks.

e. Total remuneration will include a fixed base salary as well as a variable discretionary bonus and other financial and non-financial employee benefits.

f. The remuneration policy will be transparent and accessible to all staff across the Society.

Remuneration for Executive Directors consists of a fixed salary, variable incentive pay, pension and other benefits including company car allowance. All benefits (other than variable pay), including pension arrangements, are on the same terms as employees.

For each Executive Director, the Remuneration Committee determines an appropriate level of remuneration, taking account of the specific role and responsibilities. The Committee has access to external advisers, for guidance and benchmarking. Each year the Committee reviews the level of Directors' remuneration so that it continues to be competitive and provides proper and risk-based incentives to the Executive.

The Society requires that the Directors do not use personal hedging strategies or insurance that could be used to undermine the risk alignment effects embedded in their remuneration arrangements.

Remuneration for Non-Executive Directors comprises a basic fee plus a supplement for the Chair of the Board and for the Senior Independent Non-Executive Director, both based primarily upon the time commitment required for the roles.

Summary

This report, together with the disclosures below, is provided to give members a full explanation of the policy and application of directors' remuneration. A resolution will be put to the Annual General Meeting inviting members to vote on the Directors' Remuneration Report. This vote is advisory and the Board will consider any action that may be required following the outcome of the vote.

Mary Gavigan
Chair of the
Remuneration Committee
30 June 2021

Directors' Remuneration Report (continued)

Directors' emoluments for the year ended 31 December 2020	Salaries & Fees	Performance Related Pay	Other Benefits[1]	Total 2020	Total 2019
	£	£	£	£	£
Chair					
Tracy Morshead[2]	51,200	-	-	51,200	49,950
Executive Directors					
Jonathan Long[3]	169,760	-	30,222	199,982	243,904
Sandy Richards[4]	133,250	-	25,750	159,000	88,713
Non-Executive Directors					
Geoff Brown	34,085	-	-	34,085	30,690
Mary Gavigan[5]	10,487	-	-	10,487	-
Mark Jackson[6]	23,595	-	-	23,595	30,690
Peter McIlwraith[6]	31,725	-	-	31,725	41,260
Mark Searles[7]	18,352	-	-	18,352	-
Graham Singleton[8]	31,460	-	-	31,460	2,558
Total				**559,886**	**487,764**

[1] Other benefits include pension scheme contributions, car benefits and allowances, medical and other benefits in kind or equivalent monetary value.

[2] The Chair also provides Non-Executive support and chairs the Board of National Friendly's subsidiary company, National Friendly Financial Solutions Limited.

[3] Jonathan Long deceased on 14 December 2020.

[4] Sandy Richards resigned as Executive Director on 5 April 2019. She was re-appointed as Executive Director on 1 December 2019.

[5] Mary Gavigan was appointed as a Non-Executive Director on 1 September 2020.

[6] Mark Jackson and Peter McIlwraith resigned as Non-Executive Directors on 30 September 2020.

[7] Mark Searles was appointed as a Non-Executive Director on 1 June 2020.

[8] Graham Singleton was appointed as a Non-Executive Director on 1 December 2019.

One of the Executive Directors is a member of the National Deposit Staff Superannuation Scheme. This is a defined benefit retirement plan that closed to future accrual on 31 May 2009.

Pension Entitlement - Defined benefit retirement plan							
	Years of Service	Pension accrued during 2020	Accrued pension as at 14/12/2020	Accrued pension as at 31/12/2019	Closing value at 14/12/2020	Opening value at 31/12/2019	Pension input amount over 2019
	£	£	£	£	£	£	£
Jonathan Long	14	130	5,305	5,175	106,100	105,266	834

At the AGM, members voted on the resolution to approve the 2019 Directors' Remuneration Report. The Group is committed to on-going shareholder dialogue and takes an active interest in voting outcomes. Where there are substantial votes against the resolutions in relation to Directors' remuneration, the reasons for any such vote will be sought, and any actions in response will be detailed in the next Directors' Remuneration Report.

The following table sets out the actual voting in respect of the approval of the 2019 Directors' Remuneration Report:

Number of votes cast for	Percentage of votes cast for	Number of votes cast against	Percentage of votes cast against	Total votes cast	Number of votes withheld
2703	91.81%	83	2.82%	2944	158

Directors’ Remuneration Report (continued)

Executive Directors

Base Salaries
Base pay will normally be reviewed annually in January taking into consideration RPI and CPI as a guide in any cost of living uplift.

Pay reviews may take place at other times of the year to reflect a change in role and / or significant change in responsibilities. The Committee may consult with external advisors as appropriate for such pay reviews, who can undertake a job evaluation to provide a guide salary range relevant to the role. The evaluation considers the demands of the role and then applying factors derived from salary research data, takes account of the Society’s size, sector and location.

Performance Related Pay
The Executive Directors are eligible for an annual Performance Related Pay currently representing up to a maximum of 30% of base salaries. All Executive Directors participate on the same basis and this comprises two elements: the first is assessed on a collective basis against identified corporate objectives and the second element is an individual performance related programme where the Executive Directors are assessed against personal goals and objectives.

LTIP
There is currently no Long Term Incentive Plan (‘LTIP’) scheme in operation. The Remuneration Committee may give consideration to the terms of such a scheme in the future, considering the Society’s medium and long term objectives over an extended time horizon, whilst taking account of the Society’s risk profile.

Retirement and Related Benefits
The Executive Directors are members of a defined contribution pension scheme which is available to all employees. The Society contributes up to a maximum of 12% of base salary per Director, dependent upon personal contribution levels.

Other Benefits
Executive Directors are entitled to private medical insurance, death in service benefit of four times basic salary and a company car or car cash allowance. Other benefits available to all staff are also available to Executive Directors such as salary sacrifice schemes for pension contributions, child care voucher scheme and the cycle to work initiatives and for season ticket loans.

Directors’ Contract
The Executive Directors have service agreements which incorporate their terms and conditions of employment. Executive Directors are employed on contracts subject to no more than twelve months’ notice in accordance with corporate governance best practice.

Non-Executive Directors

All Non-Executive Directors including the Chair have letters of appointment which set out their duties and responsibilities. The appointment of Non-Executive Directors is usually for a period of three years and is subject to election and re-election at the Society's AGM. After nine years of service re-election becomes an annual process.

Fees are benchmarked against similar roles in comparable organisations. Fees are calculated on an annual rather than a daily basis. However, it is assumed that to fulfil the basic role of a Non-Executive Director, sufficient time and commitment is required each month for review work and attendance at regular Board meetings, the Society's AGM, Special General Meetings where appropriate, other ad hoc meetings with regulators and advisers as may be required and training courses.

Non-Executive Directors remuneration is not performance related nor pensionable and Non-Executive Directors do not participate in any incentive plans. However, a formal annual appraisal process is undertaken where the views of all Directors are taken into consideration and the outcome of this is ratified by the Board.

Fees for Non-Executive Directors are determined by the Executive Directors and subject to approval of the Board as a whole. They are designed to recognise the responsibilities of Non-Executive Directors and to attract individuals with the necessary skills and experience to contribute to the objectives of the Society.

Independent Auditor's Report

Independent Auditor's Report to the members of National Deposit Friendly Society Limited

Opinion

In our opinion:

» National Deposit Friendly Society Limited's Group and Society's financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the Society's affairs as at 31 December 2020 and of the Group's and the Society's income and expenditure for the year then ended;

» the Group and Society's financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and

» the financial statements have been prepared in accordance with the requirements of the Friendly Societies Act 1992.

We have audited the financial statements of National Deposit Friendly Society Limited (the 'Society') and its subsidiaries (the 'Group') for the year ended 31 December 2020 which comprise:

Group	Society
Consolidated balance sheet as at 31 December 2020	Balance sheet as at 31 December 2020
Consolidated income statement for the year then ended	Income statement for the year then ended
Consolidated statement of comprehensive income for the year then ended	Statement of comprehensive income for the year then ended.
Related notes 1 to 30 to the financial statements, including a summary of significant accounting policies	Related notes 1 to 30 to the financial statements including a summary of significant accounting policies

The financial reporting framework that has been applied in the preparation of the Group and Society financial statements is applicable law and United Kingdom Accounting Standards, including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" and FRS 103 "Insurance Contracts" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. 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 Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

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

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the group and Society's ability to continue to adopt the going concern basis of accounting included:

» confirming our understanding of management's going concern assessment process and obtaining management's assessment which covers the period through to 31 December 2022;

» assessing the accuracy of management's analysis by agreeing figures to audited or publicly available information where applicable;

» evaluating the liquidity and solvency position of the Group and Society by reviewing base case liquidity and solvency projections;

» obtaining and reviewing the latest Board approved Own Risk and Solvency Assessment (ORSA), assessing whether the stress testing included in the ORSA were reasonable stress tests and considering the solvency position under each stress scenario;

» evaluating management's forecast analysis to understand how severe the downside scenarios would have to be to result in the elimination of liquidity headroom;

» reading the Society's capital recovery plan and reviewing all correspondence with the Prudential Regulation Authority in relation to the plan;

» assessing the plausibility of available management actions to mitigate the impact of the key risks by comparing them to our understanding of the Group and Society;

» performing enquiries of management and those charged with governance to identify risks or events that may impact the Group and Society's ability to continue as a going concern. We also reviewed management's assessment approved by the Board, minutes of meetings of the Board and its committees, and made enquiries as to the impact of COVID-19 on the business; and

» assessing the appropriateness of the going concern disclosures by comparing the consistency with management's assessment and for compliance with the relevant reporting requirements.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Group and Society's ability to continue as a going concern for the period to 31 December 2022.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's or Society's ability to continue as a going concern.

Overview of our audit approach	
Audit scope	• We performed an audit of the complete financial information of the Society and audit procedures on specific balances for a further two components. • The components where we performed full or specific audit procedures accounted for 100% of the Long Term Business Provision 100% of Gross Written Premiums and 100% of Total assets.
Key audit matters	• Inappropriate actuarial demographic assumptions for morbidity, longevity and persistency. • Inappropriate actuarial expense assumptions. • Potential contingent liability in respect of internal control breakdown.
Materiality	• Overall group materiality of £400k which represents 0.5% of the Long Term Business Provision.

An overview of the scope of the Society and Group audits

Tailoring the scope

Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for each entity within the Group. Taken together, this enables us to form an opinion on the consolidated financial statements. We take into account size, risk profile, the organisation of the group and effectiveness of group-wide controls, changes in the business environment and other factors when assessing the level of work to be performed at each entity.

In assessing the risk of material misstatement to the Group financial statements, and to ensure we had adequate quantitative coverage of significant accounts in the financial statements, we selected all three reporting components within the Group.

The audits of the three components were performed by the group audit team. These audits covered 100% of the material line items within the Group's income statement and balance sheet accounts.

Independent Auditor's Report (continued)

Independent Auditor's Report to the members of National Deposit Friendly Society Limited (continued)

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included 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. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
Inappropriate actuarial demographic assumptions for morbidity, longevity and persistency (2020 Long Term Business Provision: £80,977k, 2019 Long Term Business Provision: £83,145k) Refer to the Audit Committee Report (page 32); Accounting policies (page 55); and Note 20 of the Financial Statements (page 88) The assumptions underpinning the valuation of the long-term business provision as at 31 December 2020 are disclosed in note 20 to the financial statements. The valuation of the long–term liabilities the Society holds is inherently uncertain due to the dependency on a number of key assumptions, including morbidity, longevity and persistency and the risk resides around these assumptions being incorrect. Each of these assumptions presents different capital requirements across the Society's life and health business. In addition, these assumptions have different sensitivities, and for some assumptions small changes will have a material impact on the Group's reported result. Demographic assumptions are set based on internal and market experience, overlaid with the application of judgement in particular around expectations of future trends and external factors.	To obtain sufficient audit evidence to conclude on the appropriateness of actuarial assumptions, we engaged our actuarial specialists as part of our audit team and performed the following procedures: We obtained an understanding and tested the design and operating effectiveness of key controls over management's process for setting and updating the demographic actuarial assumptions. We tested that the policy records data used in the process for setting and updating demographic and expense assumptions was complete and accurate by agreeing back to the policy administration system. We audited the results of management's experience analysis to assess whether this justified the adopted assumptions, checked that the assumptions used are consistent with the experience analysis and reviewed the judgements made (such as the weight put on recent years' experience), and explanations provided by management as to why experience had changed, to ensure they were reasonable. In respect of longevity improvements, we have evaluated the use of the chosen industry standard Continuous Mortality Investigation ('CMI') model and the parameters used to validate that it was appropriate relative to the industry and Society experience. We concluded on whether the final assumptions were within a reasonable range based on our expert judgement, management's internal experience analysis and benchmarking to peers. We audited the additional judgements made in respect of the COVID-19 pandemic. This consisted of considering the appropriateness of any adjustments, or lack of adjustments, to long term assumptions or short term provisions via manual reserves. We reviewed the disclosures that have been made regarding the sensitivity of the valuation of the Long Term Business Provision to changes in the key actuarial assumptions.	Based on the analysis of experience, industry practice and the financial and regulatory requirements, we determined that: The persistency assumptions used by management are in the middle of a reasonable range; The longevity assumptions are towards the optimistic end of a reasonable range; and The morbidity assumptions are outside of the lower end of a reasonable range by an amount that is not material. On an aggregate basis, the demographic assumptions were outside the lower end of a reasonable range by an amount that is not material.

Risk (continued)	Our response to the risk (continued)	Key observations communicated to the Audit Committee (continued)
Inappropriate actuarial expense assumptions (2020 Long Term Business Provision: £80,977k, 2019 Long Term Business Provision: £83,145k) Refer to the Audit Committee Report (page 32); Accounting policies (page 55); and Note 20 of the Financial Statements (page 88) The assumptions underpinning the valuation of the long term business provision as at 31 December 2020 are disclosed in note 20 to the financial statements. Whilst less significant than the demographic assumptions referred to as part of the key audit matter above, we consider expense assumptions to be a key part of the actuarial valuation. Expense assumptions are set based on the anticipated costs associated with administering the business, including expenses inflation as well as the split between acquisition / maintenance and between different classes of business.	To obtain sufficient audit evidence to conclude on the appropriateness of actuarial assumptions, we engaged our actuarial specialists as part of our audit team and performed the following procedures: We obtained an understanding and tested the design and operating effectiveness of key controls over management's process and governance for setting expense assumptions. We compared the methodology and assumptions with market practice. We tested that the expense inputs into the model including the future expected costs savings agreed to the forecast expense paper approved by the Board. We tested whether the split between maintenance and acquisition expenses and whether the allocation of expenses between various product types and between new business and in–force business was reasonable by agreeing to actual data as well as future business plans. We assessed the business planning decisions which affect the expense assumptions for example new business growth and sales force expansion in response to Covid-19 risk. We reviewed the disclosures that have been made regarding the sensitivity of the valuation of the Long Term Business Provision to changes in the key actuarial assumptions.	We determined that the expense assumptions used by management are towards the optimistic end of a reasonable range based on industry practice and the financial and regulatory requirements.
Potential contingent liability in respect of internal control breakdown Refer to the Audit Committee Report (page 32) and Note 30 of the Financial Statements (page 97) Following a review of one of its subsidiaries (NFFS), during quarter one of 2021, the board became aware of an internal control breakdown that resulted in certain transactions being entered into that otherwise may not have been. In the circumstances members of the board sought advice and the matter is being investigated. The investigation is at an advanced stage and relevant regulatory parties have been informed as appropriate. There is a risk that appropriate disclosure of the matter is not included in the financial statements.	Our procedures included: Engaging EY specialists to provide support to the audit team in understanding the fact pattern of the matter and in assessing the potential impact on the financial statements. Obtaining an understanding of management's response, including the scope and findings from management's investigation. Considering the impact on the Group's entity level controls to identify the impacts on the audit work, considering the potential for management override of controls. Discussing with management and those charged with governance the status of work performed and reviewing all correspondence on the matter with regulators to determine if the criteria under FRS 102 for recording a provision or disclosing a contingent liability had been met. Validating whether appropriate disclosure on the matter was included in the financial statements.	We have gained reasonable assurance that at the date of signing the financial statements, the disclosure in the financial statements is a fair reflection of the status of management's investigation and response to the matter.

Independent Auditor's Report (continued)

Independent Auditor's Report to the members of National Deposit Friendly Society Limited (continued)

In the prior year, our auditor's report included a key audit matter in relation to data migrations to the new policy administration system (Odyssey) in the year. This risk is non-recurring in nature and therefore is not included in the current year.

In the prior year, our auditor's report also included a key audit matter in relation to the impact of COVID-19 on going concern and viability. In the current year, the work performed in this area is included in the 'conclusions relating to going concern' section of this report.

Our application of materiality
We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality
The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Group and Society to be £400,000 (2019: £540,000), which is 0.5% of Long term Business Provision (2019: 3% of the Fund for Future Appropriations). This has been a change from Fund for Future Appropriations used in the previous years due to the solvency coverage ratio breach at the end of March 2020 and our conclusion that the long term business provision was the key driver of own funds which are then used to calculate the solvency coverage ratio. As a result, we determined that the long term business provision would be a more critical concern for stakeholders.

Performance materiality
The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Group and Society's overall control environment, our judgement was that performance materiality was 50% (2019: 50%) of our planning materiality, namely £200k (2019: £270k). We have set performance materiality at this percentage based on our assessment of the risk of misstatement.

Audit work of the components for the purpose of obtaining audit coverage over significant financial statement accounts is undertaken based on a percentage of total performance materiality. The performance materiality set for each component is based on the relative scale and risk of the component to the Group as a whole and our assessment of the risk of misstatement at that component. In the current year, the range of performance materiality allocated to components was £40k to £200k (2019: £54k to £270k).

Reporting threshold
An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £20k (2019: £27k), which is set at 5% of planning materiality, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report set out on pages 4 to 41, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained in the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

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 course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinion on matters prescribed by the Friendly Societies Act 1992

The Group and Society complies with Friendly Societies Act 1992 and the regulations made under it. In our opinion the Report of the Board of Management has been prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it, and the information given in the Report of the Board of Management is consistent with the accounting records and consolidated financial statements for the financial year.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the Group and the Society and its environment obtained in the course of the audit, we are required by the Friendly Societies Act 1992 to state in our report whether by exception the following:

» If we are of the opinion that proper accounting records have not been kept; or

» If we fail to obtain all the information and explanations and the access to documents which, to the best of our knowledge and belief, are necessary for the purposes of our audit; or

» The annual accounts are not in agreement with the accounting records.

We have no exceptions to report arising from this responsibility.

Voluntary reporting relating to the AFM Corporate Governance Code

In accordance with the terms of engagement from the Society, our responsibility is to report on the extent of the Society's compliance with the AFM Corporate Governance Code dated January 2019 as disclosed in the Annual Report and on whether the disclosure is consistent with the requirements of the Code.

Based on the work undertaken as part of our audit, we have concluded that the Society has complied with the provisions of the AFM Corporate Governance Code dated January 2019 and that the disclosure in the Annual Report is consistent with the requirements of the Code.

Responsibilities of directors

As explained more fully in the statement of responsibilities of the directors set out on page 28, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine 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, the directors are responsible for assessing the group and Society'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 the directors either intend to liquidate the group or the Society or to cease operations, or have no realistic alternative but to do so.

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 ISAs (UK) will always detect a material misstatement when it exists.

Independent Auditor's Report (continued)

Independent Auditor's Report to the members of National Deposit Friendly Society Limited (continued)

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.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Society and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Group and Society and determined that the most significant are direct laws and regulations related to elements of the Friendly Societies Act 1992 and tax legislation, and the financial reporting framework. Our considerations of other laws and regulations that may have a material effect on the financial statements included permissions and supervisory requirements of the Prudential Regulation Authority ('PRA') and the Financial Conduct Authority ('FCA').
- We understood how the Group and Society complies with these legal and regulatory frameworks by making enquiries of senior management and those charged with governance for their awareness of any non-compliance of laws or regulations. We also reviewed correspondence between the Society and its subsidiaries and UK regulatory bodies; reviewed minutes of the Board and its committees; and gained an understanding of the Group's approach to governance.
- We assessed the susceptibility of the Group and Society's financial statements to material misstatement, including how fraud might occur by considering the controls that the Group and Society has established to address risks identified by the Group and Society, or that otherwise seek to prevent, deter or detect fraud. We also considered areas of significant judgement, performance targets, economic or external pressures and the impact these have on the control environment. Where this risk was considered to be higher, we performed audit procedures to address each identified fraud risk, including the procedures over the demographic and expense assumptions noted under the Key audit matters section above. With regard to revenue recognition fraud risk we tied back all but an immaterial amount of the gross premium income to cash received during the year and additional procedures included testing a sample of manual journals. In addition we tested controls and reconciliations performed by the Customer Services and Finance Teams with regards to generation and collection of gross premium income via direct debit. We have also tested the monthly journal upload of investment income into the general ledger to investment managers reports. These procedures were designed to provide reasonable assurance that the financial statements were free from fraud or error.
- Based on this understanding we designed our audit procedures to identify non-compliance with such laws and regulations. For direct laws and regulations, we considered the extent of compliance with those laws and regulations as part of our

procedures on the related financial statement items. For both direct and other laws and regulations, our procedures involved: making enquiry of senior management and the Audit Committee for their awareness of any non-compliance of laws or regulations, inquiring about the policies that have been established to prevent non-compliance with laws and regulations by officers and employees, inquiring about the Group and Society's methods of enforcing and monitoring compliance with such policies, inspecting significant correspondence with the FCA and PRA and reviewing minutes of the Board and its committees and the complaints log. We also performed the specific procedures over the internal controls issue noted under the Key audit matters section above.

» The Group and Society operates in the insurance industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at:
https://www.frc.org.uk/auditorsresponsibilities.
This description forms part of our auditor's report.

Other matters we are required to address
Following the recommendation from the audit committee, we were appointed by the Society on 6 September 2017 to audit the financial statements for the year ending 31 December 2017 and subsequent financial periods.

The period of total uninterrupted engagement including previous renewals and reappointments is 4 years, covering the years ending 31 December 2017 to 31 December 2020.

The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Society and we remain independent of the Group and the Society in conducting the audit.

The audit opinion is consistent with the additional report to the audit committee.

Use of our report
This report is made solely to the Society's members, as a body, in accordance with Section 73 of the Friendly Societies Act 1992. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

Andy Blackmore
(Senior statutory auditor)
for and on behalf of
Ernst & Young LLP
Statutory Auditor
Bristol
30 June 2021

Consolidated Income Statement

For the year ended 31 December 2020

		Group				Society			
		2020		2019		2020		2019	
	Note	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Gross premiums written and payments to deposit	4	16,333		14,371		16,333		14,371	
Outward reinsurance premiums		(2,446)		(861)		(2,446)		(861)	
Earned premiums net of reinsurance			13,887		13,510		13,887		13,510
Investment income	5		8,564		3,608		8,564		3,608
Unrealised gains on investments	5		-		7,855		-		7,855
Other technical income	6		631		439		93		29
			23,082		**25,412**		**22,544**		**25,002**
Gross claims paid		13,843		19,158		13,843		19,158	
Reinsurers' share		(2,057)		(266)		(2,057)		(266)	
Net claims paid			11,786		18,892		11,786		18,892
Change in provision for claims			(55)		318		(55)		318
Change in long term funds Long term business provision – gross amount		(2,168)		(4,989)		(2,168)		(4,989)	
Movement in reinsurers' share		559		1,401		559		1,401	
Long term business provision – net of reinsurance amount			(1,609)		(3,588)		(1,609)		(3,588)
Investment contract liabilities			(1)		(14)		(1)		(14)
Provision for linked liabilities – insurance contracts	22		48		160		48		160
Provision for linked liabilities – investment contracts	22		(15)		48		(15)		48
Bonuses and rebates			(55)		(35)		(55)		(35)
Net operating expenses	7a								
Acquisition costs		6,015		4,319		5,603		4,137	
Administrative expenses		3,955		3,647		3,318		3,176	
			9,970		**7,966**		**8,921**		**7,313**
Other technical charges – project costs	7b		1,646		1,479		1,582		1,465
- other			39		43		39		51
Investment expenses	8		750		830		750		830
Unrealised losses on investments	5		3,781		-		3,781		-
Loss on investment in subsidiary	26		-		-		563		119
Tax attributable to long term business	11a		(3)		(20)		-		(21)
Transfer to/(from) the fund for future appropriations			(3,200)		(667)		(3,191)		(536)
			23,082		**25,412**		**22,544**		**25,002**
Balance after transfer to/(from) the fund for future appropriations			-		-		-		-

The information on pages 54 to 97 form an integral part of these financial statements.

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2020

		Group		Society	
		2020	2019	2020	2019
	Note	£'000	£'000	£'000	£'000
Balance transferred from income statement		-	-	-	-
Actuarial gain/(loss) on pension scheme	21	806	(1,169)	806	(1,169)
Revaluation of occupied land and buildings		240	241	240	241
Total comprehensive income		**1,046**	**(928)**	**1,046**	**(928)**
Transfer to/(from) the fund for future appropriations		1,046	(928)	1,046	(928)
Total comprehensive income after transfer		-	-	-	-

The information on pages 54 to 97 form an integral part of these financial statements.

Consolidated Balance Sheet

As at 31 December 2020

		Group				Society			
		2020		2019		2020		2019	
ASSETS	Note	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Intangible assets	17		2,951		3,087		203		-
Investments Land and buildings	12	19,925		22,390		19,925		22,390	
Investment in subsidiaries	26	-		-		593		551	
Other financial investments	13	69,850		76,259		69,850		76,259	
			89,775		**98,649**		**90,368**		**99,200**
Assets held to cover linked liabilities	16		1,603		1,684		1,603		1,684
Debtors – Loans and receivables Debtors arising from direct insurance operations	3	160		117		118		112	
Other debtors	3	417		689		412		689	
			577		**806**		**530**		**801**
Other assets Tangible assets	18	3,137		2,891		3,137		2,891	
Cash at bank and in hand	14	4,357		614		4,328		548	
Deferred tax asset	11c	13		10		-		-	
			7,507		**3,515**		**7,465**		**3,439**
Prepayments and accrued income – Loans and Receivables Accrued interest and rent		1,505		1,401		1,505		1,401	
Other prepayments and accrued income		261		235		2,633		2,925	
			1,766		**1,636**		**4,138**		**4,326**
			104,179		**109,377**		**104,307**		**109,450**

The information on pages 64 to 97 form an integral part of these financial statements.

As at 31 December 2020

LIABILITIES	Note	Group 2020 £'000	Group 2020 £'000	Group 2019 £'000	Group 2019 £'000	Society 2020 £'000	Society 2020 £'000	Society 2019 £'000	Society 2019 £'000
Fund for future appropriations	27		15,419		17,573		15,439		17,584
Technical provisions Long term business provision	20	80,977		83,145		80,977		83,145	
Investment contract liabilities		3		4		3		4	
Claims outstanding		2,477		2,532		2,477		2,532	
Provision for bonuses and rebates		30		85		30		85	
			83,487		**85,766**		**83,487**		**85,766**
Technical provision for linked liabilities – insurance contracts	22		1,244		1,196		1,244		1,196
Technical provision for linked liabilities – investment contracts	22		360		375		360		375
Reinsurers' share of technical provisions			1,859		1,300		1,859		1,300
Provision for other risks and charges									
Derivatives	28		74		199		74		199
Creditors Arising out of direct insurance operations		-		49		-		49	
Other creditors including taxation and social security		472		607		358		393	
Accruals and deferred income		1,032		981		1,254		1,257	
			1,504		**1,637**		**1,612**		**1,699**
Net pension liability	21	232		1,331		232		1,331	
			232		1,331		232		1,331
			104,179		**109,377**		**104,307**		**109,450**

The information on pages 54 to 97 form an integral part of these financial statements.

These financial statements were approved by the Board on 30 June 2021.

Graham Singleton
Chief Executive

Geoff Brown
Chair Elect

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

01. Accounting Policies

These accounting policies have been applied consistently in the preparation of the financial statements.

General information

The Society is a registered friendly society incorporated and domiciled in the United Kingdom. The address of its registered office is 11-12 Queen Square, Bristol. BS1 4NT

Statement of compliance

The Group and Society financial statements of National Deposit Friendly Society Limited have been prepared in compliance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, "The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland" ("FRS 102"), Financial Reporting Standard 103, "Insurance Contracts" ("FRS 103") and the Friendly Societies Act 1992.

Basis of preparation

The financial statements have been prepared on a going concern basis. The Society's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report for the year. The Board has also considered the Society's financial position, its cash flows and liquidity position. The Society's policies and processes for managing capital are highlighted in Note 2 to the financial statements. The Society has adequate financial resources, supported by long-term relationships with its policyholders and suppliers.

In addition, the Directors have considered the management actions set out in the capital recovery plan submitted to the PRA during 2020, the wide range of stress scenarios considered as part of the ORSA process and the outcomes of the completed management actions. Together these demonstrate that the Society's capital is projected to remain above the Minimum Capital Requirement and the Solvency Capital Requirement, with sufficient liquidity to meet liabilities for a period to 31 December 2022. Over 70% of the Society's investments are held in cash, fixed income and equities, which can be liquidated at short notice and therefore, the Society is confident that it can continue to meet its cash outflows, including claims and supplier payments, during this uncertain period.

Therefore, the Directors believe that the Society is well placed to manage its business risks in respect of liquidity and cash flows. The Directors have a reasonable expectation that the Society has adequate resources to continue in operational existence for a period to 31 December 2022. Accordingly, the Society continues to adopt the going concern basis in preparing the annual report and financial statements.

The financial statements have been prepared under the historical cost convention modified for fair value and in accordance with The Friendly Societies (Accounts and Related Provisions) Regulations 1994, and United Kingdom Generally Accepted Accounting Practice, specifically FRS 102 and FRS 103.

Basis of consolidation

The Group financial statements comprise the assets, liabilities and income and expenditure account transactions of the Society and its subsidiaries National Friendly Financial Solutions Limited and National Friendly Software Solutions Limited. The net results are included in the fund for future appropriations for the Group. The activities of the Society and Group are accounted for in the income statement and statement of comprehensive income.

Premiums

Premiums are accounted for when due for payment.

Insurance commission

Insurance commission represents the value of commission receivable, recognised on the effective commencement or renewal date of the policy. All commission received relates to insurance business transacted in the United Kingdom.

Reinsurance
The Society cedes reinsurance in the normal course of business. The cost of reinsurance is recognised in the income statement at the date of purchase. Premiums ceded and claims reimbursed are presented on a gross basis in the income statement and balance sheet as appropriate.

Reinsurance assets primarily include balances due from reinsurance companies for ceded insurance contract liabilities. Reinsurance assets are measured as the fair value of the technical provisions of the policies subject to the reinsurance treaty.

If the technical provisions on policies with a quota share reinsurance treaty are negative then the reinsurer's share of these provisions can be a liability. Reinsurance liabilities represent future premiums and/or fees which will be ceded to reinsurers, in excess of future receipts from the reinsurer.

Realised and unrealised gains and losses
Realised investment gains and losses represent the difference between the sale proceeds and original cost. Unrealised investment gains and losses represent the net movement in the market value of investments during the year after allowing for realised gains and losses recognised in the income statement.

Investment return
Investment return comprises the investment income and fair value gains and losses derived from assets held at fair value through profit and loss, rental income and fair value gains and losses derived from investment property and interest income derived from cash and cash equivalents.

Investment income derived from assets held at fair value through profit and loss includes dividends and interest income. Dividends are accounted for on the date the shares become quoted ex-dividend. UK dividends are shown excluding their irrecoverable associated tax credit. Interest income is recognised on the effective interest rate basis. Income from rents and securities is taken into account on an accruals basis. Bank interest is accrued in the period in which it arises.

Claims
Maturity claims and annuities are charged against income when due for payment. Claim payments whose beneficiaries cannot be traced are held in a suspense liability for an appropriate period of time, depending on the age of the customer and the nature of the policy, and then released if still unclaimed. Surrenders are accounted for when paid or, if earlier, on the date when the policy ceases to be included within the calculation of the long-term business provision. Death claims and all other claims including Healthcare are accounted for when notified.

Long term business provision
The long-term business provision is determined by the Society's Board and is calculated on a Solvency II basis. It is calculated to be consistent with the PRA Rulebook: Solvency II Firms Technical Provisions Instrument 2015.

The Solvency II provisions, on which the long-term business provision is based, are defined as the sum of the Best Estimate of Liabilities and the Risk Margin. The best estimate and risk margin are calculated separately. The best estimate of liabilities is calculated on a policy by policy basis for all contracts accepted on risk at the valuation date using a cash flow approach and generally accepted actuarial practices. The calculations generate probability weighted cashflows for each monthly time period within a policy's contract boundary. The cash flows are discounted using the PRA's risk-free yield curve and thus make allowance for the time value of money.

The total risk margin is calculated as the sum of the present values of the cost of capital rate applied to the Solvency Capital Requirement (SCR) of a reference undertaking, willing to take on the Society's insurance portfolio, in each future year until the obligations are extinguished and there is no remaining SCR.

The Long Term Business Provision reported in the Financial Statements does not take account of any transitional measures approved by the PRA in respect of the transition from Solvency I to Solvency II.

Bonuses
Bonuses charged to the long-term business technical account in a given year comprise new reversionary bonuses declared in respect of that year which are provided within the calculation of the long term business provision.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

01. Accounting Policies (continued)

Claims outstanding

The outstanding claims reserve provides for all the estimated (based on actuarial calculations) Healthcare, Healthguard, Optimum and Heathcover claims payable as at 31 December and represents the estimated ultimate cost of settling all claims which have occurred up to the balance sheet date.

The methodology used to calculate this reserve has been modified at this year-end to allow for greater deferral of claims as a result of COVID related disruption to healthcare providers.

Depreciation

Properties

No depreciation has been provided on investment properties in accordance with Section 16 "Investment Property" of FRS 102.

Intangible assets

Intangible assets represent the intellectual property rights for computer software and a customer book acquired from a third party from which future revenue is expected. Intangible assets are held at cost less accumulated amortisation.

Computer Software is amortised on the straight line basis over its useful economic life, which is 10 years.

Software under Construction is not amortised until completed, but is reviewed for impairment at least annually. The Customer Book is amortised on the straight line basis over its useful economic life, which is 10 years.

The Website is amortised on the straight line basis over its useful economic life, which is 3 years.

Tangible fixed assets and depreciation

Land and buildings

The owner occupied floors of 11-12 Queen Square, Bristol used by the Group and Society as a head office are held as land and buildings in tangible fixed assets in accordance with Section 17 "Property, Plant and Equipment" of FRS 102. The property is held at fair value at the balance sheet date with revaluation gains recognised through other comprehensive income.

Land and buildings are not depreciated as the opinion of the directors is that the depreciation is not material and the property is revalued annually on a fair value basis.

Other tangible fixed assets

Tangible fixed assets other than land and buildings are held at cost less accumulated depreciation.

Depreciation has been provided at the following rates calculated to write off each asset over its estimated useful life:

» Computer equipment is depreciated at 25% per annum on a straight line basis;

» Office equipment is depreciated at 12.5% per annum on a straight line basis.

» Motor vehicles are depreciated at 33.33% per annum on a straight line basis.

Acquisition costs

Acquisition costs represent commission payable and other related expense of acquiring insurance policies written during the financial year.

Operating leases

The Group leases office machinery and equipment under contracts of operating leases. The lease expenses are accounted for as an operating expense as incurred.

Project costs

Project costs comprise expenditure on business process improvements which are intended to deliver future financial benefits to the Group through reducing operating costs and/or creating operational efficiencies.

Projects costs are charged to the income statement with the exception of major projects where the outcome is assessed to be reasonably certain as regards viability and feasibility.

These costs are capitalised if they meet the criteria laid out in Section 17 "Property, Plant and Equipment" or Section 18 "Intangible Assets other than Goodwill" of FRS 102. Amortisation is charged once the economic benefits of the project start to be realised.

Pension costs

The Society operates a defined benefit pension scheme. This scheme closed to new entrants and future accrual on 31 May 2009. A pension asset or liability is calculated as the recoverable amount of the scheme's assets less the present value of the scheme's liabilities in accordance with the principles set out in the Section 28 "Employee Benefits" of FRS 102. The Society is currently making contributions to the scheme at the level agreed with the trustees with the objective of having sufficient assets to meet its liabilities.

The pension cost for the scheme is analysed between current service cost, past service cost and net return on pension scheme. Current service cost is the actuarially calculated present value of the benefits earned by the active employees in each year. Past service costs relating to employee service in prior years arising in the current year as a result of the introduction of, or improvement to, retirement benefits, are recognised in the profit and loss account on a straight-line basis over the year in which the increase in benefits vest.

The actuarial gains and losses which arise from a valuation and from updating the latest actuarial valuation to reflect conditions at the balance sheet date are taken to the statement of comprehensive income for the year to the extent they are attributable to members. The attributable deferred taxation is shown separately in the statement of comprehensive income.

Payments made to the defined contribution scheme for current employees are charged as an expense as they fall due.

Taxation

Deferred tax is provided using the full provision method. Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date. It is calculated at rates expected to be applicable when the asset or liability crystallises on a non-discounted basis. Deferred tax assets are recognised only to the extent that there will be sufficient foreseeable future taxable profits from which the future reversal of timing differences can be deducted.

Investment in subsidiaries

Investments in subsidiary companies are held at fair value. The change in fair value through the year is recognised through "gain or loss on investment in subsidiary" in the income statement.

Fund for future appropriations

The fund for future appropriations incorporates amounts which have yet to be allocated to participating policyholders. Any surplus or deficit arising in the income statement or statement of comprehensive income is transferred to or from the fund on an annual basis. Surpluses are allocated by the directors to participating policyholders by way of bonuses. Any unallocated surplus is carried forward in the fund for future appropriations.

Contract classification

The Society classifies its products for accounting purposes as insurance, investment or investment with discretionary participation features. Insurance contracts are those contracts that transfer significant insurance risk. Contracts that do not transfer significant insurance risk are investment contracts.

A discretionary participation feature is a contractual right held by a policyholder to receive additional payments as a supplement to guaranteed benefits:

» that are likely to be a significant proportion of the total contractual payments; and
» whose amount or timing is contractually at the discretion of the issuer and that are contractually based on:
  - the performance of a specified pool of contracts, or a specified type of contract, or
  - realised and/or unrealised investment returns on a specified type of contract, or
  - the profit or loss of the company that issues the contracts.

Such contracts are more commonly known as "with-profits" or as "participating contracts".

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

01. Accounting Policies (continued)

Insurance contracts and participating investment contracts

The insurance and participating investment contract liabilities are determined annually in accordance with regulatory requirements.

The participating liabilities include an assessment of any future options and guarantees included in this business and are measured on a fair value basis.

The estimation techniques and assumptions are periodically reviewed, with any changes in estimates reflected in the income statement as they occur.
The long term business provision is calculated by the Society's Chief Actuary, having due regard to the actuarial principles laid down in the PRA Rulebook, and is approved by the Board.

Investment contracts

Investment contracts are those contracts that transfer financial risk with no significant insurance risk. These contracts are accounted for using deposit accounting. Premiums and claims are not recognised in the income statement in respect of these policies. The investment gain or loss on these policies is shown through the movement in the investment contract liabilities on the income statement and measured on a fair value basis.

Financial assets

The Society classifies its financial assets as fair value through the profit and loss or as loans and receivables. Assets held at fair value through the profit and loss are measured at fair value based on the active market price with gains and losses recognised in the Income Statement, whilst loans and receivables are held at amortised cost. This is in line with International Accounting Standard 39 “Financial Instruments” as allowed under Section 11 “Basic Financial Instruments” in FRS102. Financial assets are derecognised when the rights to receive future cash flows from the investments have expired or have been transferred and the Society has transferred substantially all risks and rewards of ownership. All financial assets are held at fair value through profit and loss other than mortgages, debtors arising from insurance operations, other debtors and accrued interest and rent which are held at amortised cost.

Investments

Listed securities are shown in the financial statements at bid price. Properties are shown in the financial statements at fair value.

Mortgages and loans are valued at amortised cost which is not materially different from the fair value of its future cash flows.

Derivatives

The Society holds some forward contracts for foreign currency exchange. The Society also holds some bond future and swap contracts to better match the duration of the fixed interest portfolio to its liabilities. Depending on whether the contract is in a favourable or adverse position they are classified as financial assets or financial liabilities respectively and are classified as fair value through the profit and loss. They are initially recognised and are subsequently re-measured at their fair value. Changes in fair value are recognised through unrealised or realised gains and losses on the income statement.

All derivatives are carried as assets when fair value is positive and as liabilities when the fair value is negative.

Foreign currencies

Some fixed interest investments are held in foreign currencies. The assets are held on the balance sheet in sterling using the year-end exchange rate, whilst the book cost is calculated using the exchange rate on the day of purchase. Any gains or losses on the exchange rates are recognised through unrealised or realised gains and losses in the income statement.

Cash flow statement

The Society, being a mutual life assurance company, is exempt from the requirement under Section 7 "Statement of Cash Flows" of FRS102 to produce a cash flow statement.

Key estimates and judgements

a) Classification of contracts

A key issue for the Society under FRS103 is that a distinction is made between insurance contracts, investment contracts and investment contracts with discretionary participation features. The Society issues contracts that transfer insurance risk, financial risk or both. Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk.

Investment contracts are those that transfer financial risk with no significant insurance risk. Three products are categorised in this way, namely temporary annuities, CABF Unit-linked Whole of Life Flexiplan and CABF Unit Linked Whole Life Bond.

All with-profits contracts have been classified as participating contracts as these contracts entitle the holder to receive, as a supplement, guaranteed benefits, additional benefits or bonuses that are likely to be a significant portion of the total contractual benefits whose amount or timing is contractually at the discretion of the Society.

b) Technical Provisions - Valuation of investment and long-term insurance contracts

Technical provisions are calculated using policy data held on the Society's administration systems and assumptions set using internal and external data as inputs to actuarial valuation models. The assessment of the appropriate value of the technical provisions requires the Society to make significant judgements when determining the underlying assumptions. The principal economic assumption is the inflation rate for future expenses, while the principal non-economic assumption relates to future lapses. The non-economic assumptions are based on the Society's own experience. The valuation interest rates used to discount projected cash flows are a duration-specific risk-free yield curve specified by the PRA under Solvency II regulations. Due to the long-term nature of these obligations, the estimates are subject to significant uncertainty. Further details on specific assumptions are provided in note 20 to these Financial Statements.

c) Valuation of Investment Properties

The Society owns a portfolio of Investment Properties which are held for long-term rental yield and capital growth. This portfolio is valued on a fair value basis on an annual basis by Society appointed Chartered Surveyors. The valuations have been prepared in accordance with the Royal Institution of Chartered Surveyors' Valuation – Professional Standards effective from 6th January 2014. In preparing these valuations, data and information available concerning rental yields, lease terms, voids and floor areas and enquiries within local market places have been used as contributing factors to each individual property's valuation. The most significant inputs into this valuations are the rental income and yield assumptions. Further information is provided in note 12.

d) Valuation of Financial Assets

The Society holds a number of financial assets such as equities, fixed income securities, derivatives, cash, mortgages and debtors. The Society has no financial assets held for trading, all investment are classified and valued at fair value. Equities, fixed income securities and derivatives are measured at market prices, or prices consistent with market ratings should no price be available. Mortgages and debtors are measured at amortised cost which is not materially different from the valuation of its future cash flows. Any unrealised or realised gains or losses are recognised in the Income Statement. Further detail are provided in note 13.

e) Defined Benefit Pension Schemes

In determining the pension cost and the defined benefit obligation of the Society's defined benefit pension schemes, a number of assumptions are used. These assumptions include an appropriate discount rate, the level of salary escalation, price inflation and mortality rates. Further details are contained in note 21.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

01. Accounting Policies (continued)

Key estimates and judgements (continued)

f) Valuation of Investment in Subsidiaries

Investment subsidiaries are held at fair value. The change in fair value through the year is recognised through the income statement. Judgement is required in assessing the fair value of the subsidiary companies which are not considered to be materially different from the net asset values in the respective subsidiary accounts.

g) Valuation of Intangible Assets

The Group holds intangible assets at cost less accumulated amortisation. The value of these assets are reviewed annually and impaired through the income statement if the carrying value is greater than the fair value of the expected future cashflows.

02. Capital Management

The regulatory capital requirement for the Society is determined by the Solvency II regime. This is a risk-based approach to the assessment of capital requirements whereby Technical Provisions are calculated as the sum of the best estimate liabilities plus a risk margin. The Solvency Capital Requirement ("SCR") is the additional capital the Society is required to hold to withstand a set of adverse events (covering market, underwriting, counterparty and operational risks) with a 99.5% level of confidence. The Society aims to manage its capital to ensure that there is an appropriate level of surplus over the SCR, in line with its Solvency Risk Appetite. This is monitored formally through the Board and Risk & Compliance Committee on a bi-annual basis and more regularly by the Actuarial Function.

The Society calculates its SCR in accordance with the Solvency II standard formula. The liabilities are discounted using risk free discount rates prescribed by the PRA. These rates do not necessarily reflect the rates earned on the financial assets held by the Society. The Society fell below full coverage of the SCR as at 31 March 2020, with an SCR coverage ratio of 92% (the MCR coverage ratio was 369%). The Society notified the PRA accordingly, and submitted a Capital Recovery Plan in July 2020. A number of management actions were taken, immediately following the identification of SCR coverage being below 100% through to the end of the year, in order to restore the solvency position to materially in excess of 100% by the end of 2020.

The Society maintains a single long term business fund. The available capital for the fund is represented by the fund for future appropriations which represents the difference between the assets and liabilities of the Society and Group. For Solvency II regulatory purposes certain assets are deemed inadmissible for meeting the capital requirements. At the balance sheet date £0.7m (2019: £0.5m) of assets could not be included for regulatory capital purposes.

In addition, for statutory purposes under FRS 102 / 103, the Society calculates its FRS 102 / 103 liabilities on the same basis as Solvency II, with the exception that the Society has adopted a Transitional Measure on the risk-free Interest Rate (TMIR) for its regulatory reporting to the PRA under Solvency II. The TMIR applies only to policies in force prior to the Solvency II regime and is released over a 16 year period.

The Capital Statement overleaf outlines the Society's Capital available for regulatory requirements. This is the Solvency II Own Funds. The impact of the TMIR is shown.

Capital Statement

	Society	
	(Unaudited) 2020	(Unaudited) 2019
	£'000	£'000
Fund for future appropriations	**15,439**	**17,584**
Regulatory valuation adjustment	(678)	(522)
Transitional measures adjustment	1,241	1,203
Own Funds available to meet Solvency Capital Requirements	**16,002**	**18,265**

A reconciliation of the movements in the capital available to meet capital requirements at the start and end of the year is set out below:

	Society
	(Unaudited) 2020
	£'000
Available Own Funds at the start of the year	**18,265**
Model and methodology changes	(2)
Assumption changes	(4,731)
Actual versus expected* investment income and gains	3,661
Actual versus expected* inflows	283
Actual versus expected* outflows	(2,587)
Actual versus expected in force data at end 2020	268
New business**	664
Change in Additional Expense Reserve (AER)***	(937)
Change in the Risk Margin (other than due to new business)	332
Impact of Staff Superannuation Fund****	1,098
Other adjustments	(350)
Change in TMIR	38
Available Own Funds at the end of the year	**16,002**

* *Other than for actual investment income, the actual versus expected are only in respect of business in force at 31/12/2019. New business is covered separately.*

** *New business is the total of premiums, claims, commission, acquisition expenses, the change in the BEL and the change in the Risk Margin due to new business.*

*** *Relating to 2021 cash-flows onwards. 2020 cash-flows are picked up in the expected outflows line.*

**** *Impact of Staff Superannuation Fund reflects the change in the assets, the change in the liabilities and the contributions the Society has made over 2020.*

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

02. Capital Management (continued)

- The Society's assets yielded an investment gain over 2020 of £4.5m. Expected investment returns (at the risk-free rate) over 2020 on assets held to back the liabilities were £0.8m. This has resulted in an actual versus expected impact of investment returns of £3.7m.
- Actual outflows were higher than expected by £2.6m. A key driver of this is the spend of £1.8m on strategic expenses over the year.
- New business written over 2020 has increased the available Own Funds by £0.7m.
- The Additional Expense Reserve (AER) has reduced by £0.8m. However, some of the 2019 AER related to expected expenses during 2020 and so are included in the actual versus expected outflows in the table. The change in the AER relating only to expenses from 2021 onwards, reduces Own Funds by £0.9m.
- The change in the Risk Margin (other than due to model changes and new business) has increased available Own Funds by £0.3m.

Options and guarantees

The Society has some With Profit retirement annuity contracts that have valuable Guaranteed Annuity Rates attached to them in a low interest rate environment. In addition, there are some guarantees on mortgage endowments and With Profit bonds, although these are not material.

The net cost of guarantees is particularly sensitive to market risk and to longevity risk.

Assumptions used in the valuation of the Technical Provisions

The assumptions used in the valuation of the Technical Provisions, including those used to value options and guarantees, are determined by conducting an analysis of the Society's past experience and overlaying this with expert judgement.

Capital resource sensitivities

The Society's capital position is sensitive to changes in economic conditions and demographic assumptions, due to both changes in the value of the assets and the value of the liabilities. The main sensitivities arise from:

Market risk: The Society is exposed to reductions in the value of its assets.

The risk is reduced by matching fixed interest assets to the expected profile of the liabilities so that the assets and liabilities move in the same way under a fixed interest market stress scenario.

For With Profit business, the risk to available capital is further reduced by the fact that asset shares will reduce in a market risk scenario. This reduces exposure under the equity and property stresses in particular.

Lapse risk: The Society is exposed to the risk that lapses are higher or lower than expected. Whether this increases or reduces available capital varies by product. The highest impact Standard Formula lapse risk is the risk of a mass lapse scenario.

In the event of an adverse lapse scenario, management actions can be taken on some legacy Health contracts to increase the available capital. These are premium increases, increases to "own share" percentages (the proportion of claims that are paid by the members deposit account) and reductions in "premium surplus" (a discretionary proportion of each premium that is paid into the member's deposit account) and reduction to asset shares under market stresses.

New Health contracts have annually reviewable premiums to reduce exposure to underwriting risks.

Longevity risk: The Society is exposed to the risk that mortality rates reduce, particularly on annuity business. This risk is largely mitigated using reinsurance for the Immediate Needs Annuity business, but the Society is exposed to residual longevity risk on this product, and on other products.

Expense risk: The Society is exposed to the risk that expenses are higher than expected. This could materialise by lower than expected volumes of new business meaning the per policy expenses are increased.

The management actions as described under the lapse risk section can equally be applied in an expense risk scenario to increase the available capital.

In addition, an expense stress in relation to With Profit business can be charged to asset shares, further reducing the impact.

Morbidity risk: The Society is exposed to the risk that there are more morbidity claims than expected, or that they are of higher value.

The management actions as described under the lapse risk section can equally be applied in a morbidity risk scenario to increase the available capital.

Mortality risk: The Society is exposed to the risk that mortality is increased. The risk has increased over 2020 with further variants of the Guaranteed Life Assurance product being sold. The Society's exposure to mortality risk is expected to increase as we continue to sell these products.

The following table shows the sensitivity of the Society's available Own Funds to changes in assumptions. The assumption changes shown are those as per the Solvency II standard formula. The sensitivities do not allow for the TMIR adjustment.

	Society
	Impact (Unaudited)
	£'000
Property risk *Decrease in property values of 25%*	**(2,205)**
Interest rate risk *Increase in risk free yield curve as specified by the PRA (+1%)* *Decrease in risk free yield curve as specified by the PRA (c.-0.1%**)*	 (1,794) 172
Equity risk *Decrease in equity values of 38.5%*	(475)
Credit spread risk *Decrease in corporate bond values of 9.7%*	(3,164)
Lapse risk *** *Increase in lapse rates of 50%* *Decrease in lapse rates of 50%* *Mass lapse of 40%*	 (429) (2,988) (4,061)
Longevity risk *Decrease in mortality rates of 20%*	(2,209)
Expense risk *Increase in per policy expenses of 10% and expense inflation of 1% p.a.*	(2,867)
Morbidity risk *Increase in morbidity rates of 5% and claim inflation of 1% p.a.*	(1,098)
Mortality risk *Increase in mortality rates of 15%*	(1,737)

*** For a 10 year term which is the approximate average duration of the Society's liabilities*

**** Article 142 of the Solvency II Delegated Act requires that the lapse stresses are applied only to lines of business where the stress would result in a decrease in Own Funds. As such, all of the lapse stresses reduce the available Own Funds.*

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

03. Risk Management

The key risks that the Society and Group are exposed to and the way the Society and Group manage them is set out as follows:

Insurance risk

Insurance risk is the risk that arises from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities. Long term insurance risk arises from morbidity, persistency, mortality and expense variances. Systems are in place to measure, monitor and mitigate exposure to all these risks.

The valuation assumptions have been recommended by the Chief Actuary and approved by the Board. See note 20 for details of assumptions used in the calculation of the long term business provision.

Financial risk

The Society is exposed to a range of financial risks through its financial assets, financial liabilities, reinsurance assets and insurance liabilities. The most important components of this financial risk are market risk (including interest rate risk, exchange rate risk and equity price risk), credit risk and liquidity risk. The Society also faces financial risks in respect of property valuations, concentration of investments and counter-party exposures.

Each of the exposures to risk are analysed regularly to assess their likely impact and probability.

i. Market risk

Market risk is the risk that as a result of market movements the Society may be exposed to fluctuations in the value of its assets, the amount of its liabilities, or the income from its assets. Sources of general market risk include movements in interest rates, equities, exchange rates and real estate prices.

The Society has a low appetite for market risks and this is reflected in its investment strategy. The investment strategy is kept under regular review as part of the capital management plan.

a) Interest rate risk

Changes in interest rates impact the value of the Society's assets and liabilities. The risk to Own Funds from changes in interest rates is reduced by close matching of assets to liabilities.

b) Exchange rate risk

The Society has a number of fixed interest investments in foreign currencies which present an exchange rate risk that is mitigated by holding Forward Contracts for foreign exchange as a natural hedge against the exchange rate risk. The Society's holdings shown by currencies are listed below:

	Group & Society	
	2020	2019
Market Value - Equities	**£'000**	**£'000**
UK pound	6,440	10,338
	6,440	**10,338**

	Group & Society	
	2020	2019
Market Value - Fixed Interest	**£'000**	**£'000**
UK pound	59,336	49,969
Euro	-	572
USA dollar	1,006	11,161
	60,342	**61,702**

Exchange rate risk is hedged so a small change in the exchange rate will lead to a negligible change in the value of assets. All liabilities are denominated in sterling so a change in exchange rate will have no effect on the value of liabilities.

c) Equity price risk

Holdings in equities are by their nature subject to market movement. In order to mitigate this risk the Society employs an external investment portfolio manager and the Investment Committee regularly review the level of equities notionally allocated to with profit life business to ensure the level of risk remains appropriate.

ii. Credit risk

Credit risk is the risk of loss incurred whenever a counterparty fails to perform its contractual obligations including failure to perform them in a timely manner.

The Society has a low appetite for credit risk on cash and cash is spread over a number of high rated banks with the maximum limit on the exposure to any one financial institution.

The terms of the investment funds require an appropriate spread of holdings within specified parameters, with the majority of assets being 'A' rated bonds or higher. There are also limits on the maximum exposure to any single counterparty and on the level of exposure to lower rated bonds.

This results in a relatively modest exposure to lower rated and possibly more risky assets within the investment funds. However, the Society considers regular reviews from the fund manager so that the risk within the funds remains appropriate relative to the Society's appetite for credit risk.

The Society currently has a low level of exposure to re-assurer security which will decline as the portfolio matures. Therefore, there are no specific actions envisaged to manage the risks in this section.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

03. Risk Management (continued)

	Group	
	2020	2019
The assets bearing credit risk are summarised and analysed by credit rating below:	**£'000**	**£'000**
Derivative financial instruments	1,589	685
Listed fixed interest securities	60,341	61,702
Loans and receivables (Note 14)	2,195	2,322
Deposits with credit institutions	1,367	3,419
Cash at bank and in hand	4,357	614
	69,849	**68,742**
AAA	2,933	5,925
AA	26,157	25,693
A	29,678	25,305
BBB	7,868	10,172
Below BBB	490	-
Not rated	2,723	1,647
	69,849	**68,742**

	Society	
	2020	2019
The assets bearing credit risk are summarised and analysed by credit rating below:	**£'000**	**£'000**
Derivative financial instruments	1,589	685
Listed fixed interest securities	60,341	61,702
Loans and receivables (Note 14)	2,148	2,317
Deposits with credit institutions	1,367	3,419
Cash at bank and in hand	4,328	548
	69,773	**68,671**
AAA	2,933	5,925
AA	26,127	25,626
A	29,678	25,305
BBB	7,868	10,172
Below BBB	490	-
Not rated	2,677	1,643
	69,773	**68,671**

Our limit for "Below BBB" was exceeded during the year, as a result of the downgrade of two bonds from the same issuer, whose business was significantly impacted by the COVID pandemic. Following discussion with our fund managers a decision was taken to retain these bonds, on the basis of an expectation of future recovery. No financial assets are past due or impaired at the reporting date and management expects no significant losses from non-performance by these counterparties.

iii. Liquidity risk

Liquidity risk is the risk that the Society, although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure such resources only at excessive cost. For example, liquidity risk can arise from mismatching between expected asset and liability cash flows or from the inability to sell assets quickly.

The Society has a low appetite for liquidity risk and the risk is controlled by primarily investing in liquid assets.

The Society also holds some bond futures and swaps to manage the duration of the fixed interest portfolio. This strategy is intended to be maintained and the Society will also continue to monitor its emerging cash flow requirements.

Financial assets held over five years are long-term assets aiming to match the duration of liabilities. It is not possible to invest in fixed income investments with no maturity date. However the Society carries out regular checks so that assets and liabilities are well matched by duration.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

03. Risk Management (continued)

Financial and insurance liabilities at 31/12/20	Group				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
	£'000	£'000	£'000	£'000	£'000
Fund for future appropriation	15,419	-	-	-	**15,419**
Long term business provision	-	2,089	1,225	77,663	**80,977**
Investment contract liabilities	-	1	2	-	**3**
Claims outstanding	-	2,477	-	-	**2,477**
Provision for bonuses and rebates	-	8	16	6	**30**
Technical provision for linked liabilities – insurance contracts	-	1,244	-	-	**1,244**
Technical provision for linked liabilities – investment contracts	-	360	-	-	**360**
Reinsurers' share of technical provisions	-	-	1,859	-	**1,859**
Derivatives	-	74	-	-	**74**
Defined benefit pension liability	-	-	-	232	**232**
Creditors arising out of direct insurance operations	-	-	-	-	**-**
Other creditors including taxation and social security	-	472	-	-	**472**
Accruals and deferred income	-	1,032	-	-	**1,032**
Total financial and insurance liabilities	**15,419**	**7,757**	**3,102**	**77,901**	**104,179**

Financial and insurance liabilities at 31/12/19	Group				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
	£'000	£'000	£'000	£'000	£'000
Fund for future appropriation	17,573	-	-	-	**17,573**
Long term business provision	-	2,325	4,090	76,730	**83,145**
Investment contract liabilities	-	1	3	-	**4**
Claims outstanding	-	2,532	-	-	**2,532**
Provision for bonuses and rebates	-	19	41	25	**85**
Technical provision for linked liabilities – insurance contracts	-	1,196	-	-	**1,196**
Technical provision for linked liabilities – investment contracts	-	375	-	-	**375**
Reinsurers' share of technical provisions	-	-	1,230	70	**1,300**
Derivatives	-	199	-	-	**199**
Defined benefit pension liability	-	-	-	1,331	**1,331**
Creditors arising out of direct insurance operations	-	49	-	-	**49**
Other creditors including taxation and social security	-	607	-	-	**607**
Accruals and deferred income	-	981	-	-	**981**
Total financial and insurance liabilities	**17,573**	**8,284**	**5,364**	**78,156**	**109,377**

	Group				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial assets at 31/12/20	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Equity investments	6,440	-	-	-	**6,440**
Fixed interest securities	-	-	5,852	54,489	**60,341**
Derivatives	-	1,589	-	-	**1,589**
Deposits with credit institutions	-	1,367	-	-	**1,367**
Mortgages	107	2	4	-	**113**
Assets held to cover linked liabilities	1,603	-	-	-	**1,603**
Debtors arising from direct insurance operations	-	160	-	-	**160**
Other debtors	-	417	-	-	**417**
Cash at bank and in hand	4,357	-	-	-	**4,357**
Accrued interest and rent	-	1,505	-	-	**1,505**
Total financial assets	**12,507**	**5,040**	**5,856**	**54,489**	**77,892**

	Group				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial assets at 31/12/19	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Equity investments	10,338	-	-	-	**10,338**
Fixed interest securities	-	158	6,801	54,743	**61,702**
Derivatives	-	685	-	-	**685**
Deposits with credit institutions	-	3,419	-	-	**3,419**
Mortgages	107	2	6	-	**115**
Assets held to cover linked liabilities	1,684	-	-	-	**1,684**
Debtors arising from direct insurance operations	-	117	-	-	**117**
Other debtors	-	689	-	-	**689**
Cash at bank and in hand	614	-	-	-	**614**
Accrued interest and rent	-	1,401	-	-	**1,401**
Total financial assets	**12,743**	**6,471**	**6,807**	**54,743**	**80,764**

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

03. Risk Management (continued)

	Society				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial and insurance liabilities at 31/12/20	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Fund for future appropriation	15,439	-	-	-	**15,439**
Long term business provision	-	2,089	1,225	77,663	**80,977**
Investment contract liabilities	-	1	2	-	**3**
Claims outstanding	-	2,477	-	-	**2,477**
Provision for bonuses and rebates	-	8	16	6	**30**
Technical provision for linked liabilities – insurance contracts	-	1,244	-	-	**1,244**
Technical provision for linked liabilities – investment contracts	-	360	-	-	**360**
Reinsurers' share of technical provisions	-	-	1,859	-	**1,859**
Derivatives	-	74	-	-	**74**
Defined benefit pension liability	-	-	-	232	**232**
Other creditors including taxation and social security	-	358	-	-	**358**
Accruals and deferred income	-	1,254	-	-	**1,254**
Total financial and insurance liabilities	**15,439**	**7,865**	**3,102**	**77,901**	**104,307**

	Society				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial and insurance liabilities at 31/12/19	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Fund for future appropriation	17,584	-	-	-	**17,584**
Long term business provision	-	2,325	4,090	76,730	**83,145**
Investment contract liabilities	-	1	3	-	**4**
Claims outstanding	-	2,532	-	-	**2,532**
Provision for bonuses and rebates	-	19	41	25	**85**
Technical provision for linked liabilities – insurance contracts	-	1,196	-	-	**1,196**
Technical provision for linked liabilities – investment contracts	-	375	-	-	**375**
Reinsurers' share of technical provisions	-	-	1,230	70	**1,300**
Derivatives	-	199	-	-	**199**
Defined benefit pension liability	-	-	-	1,331	**1,331**
Creditors arising out of direct insurance operations	-	49	-	-	**49**
Other creditors including taxation and social security	-	393	-	-	**393**
Accruals and deferred income	-	1,257	-	-	**1,257**
Total financial and insurance liabilities	**17,584**	**8,346**	**5,364**	**78,156**	**109,450**

	Society				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial assets at 31/12/20	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Equity investments	6,440	-	-	-	**6,440**
Fixed interest securities	-	-	5,852	54,489	**60,341**
Derivatives	-	1,589	-	-	**1,589**
Deposits with credit institutions	-	1,367	-	-	**1,367**
Mortgages	107	2	4	-	**113**
Assets held to cover linked liabilities	1,603	-	-	-	**1,603**
Debtors arising from direct insurance operations	-	118	-	-	**118**
Other debtors	-	412	-	-	**412**
Cash at bank and in hand	4,328	-	-	-	**4,328**
Accrued interest and rent	-	1,505	-	-	**1,505**
Total financial assets	**12,478**	**4,993**	**5,856**	**54,489**	**77,816**

	Society				
	No maturity date	Within 1 year	1 - 5 years	Over 5 years	Total
Financial assets at 31/12/19	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Equity investments	10,338	-	-	-	**10,338**
Fixed interest securities	-	158	6,801	54,743	**61,702**
Derivatives	-	685	-	-	**685**
Deposits with credit institutions	-	3,419	-	-	**3,419**
Mortgages	107	2	6	-	**115**
Assets held to cover linked liabilities	1,684	-	-	-	**1,684**
Debtors arising from direct insurance operations	-	112	-	-	**112**
Other debtors	-	689	-	-	**689**
Cash at bank and in hand	548	-	-	-	**548**
Accrued interest and rent	-	1,401	-	-	**1,401**
Total financial assets	**12,677**	**6,466**	**6,807**	**54,743**	**80,693**

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

03. Risk Management (continued)

iv. Fair value estimation

The principal financial assets held at 31 December 2020, analysed by their fair value hierarchies are:

	Level 1	Level 2	Level 3	Total
Assets 2020 Financial assets at fair value through the profit and loss	**£'000**	**£'000**	**£'000**	**£'000**
- Equity investments	6,440	-	-	**6,440**
- Fixed interest securities	20,195	40,146	-	**60,341**
- Derivatives	16	1,573	-	**1,589**
- Assets held to cover linked liabilities	-	1,603	-	**1,603**
Total assets	**26,651**	**43,322**	**-**	**69,973**

The principal financial assets held at 31 December 2019, analysed by their fair value hierarchies were:

	Level 1	Level 2	Level 3	Total
Assets 2019 Financial assets at fair value through the profit and loss	**£'000**	**£'000**	**£'000**	**£'000**
- Equity investments	10,338	-	-	**10,338**
- Fixed interest securities	19,448	42,254	-	**61,702**
- Derivatives	231	454	-	**685**
- Assets held to cover linked liabilities	-	1,684	-	**1,684**
Total assets	**30,017**	**44,392**	**-**	**74,409**

The principal financial liabilities held at 31 December 2020, analysed by their fair value hierarchies are:

	Level 1	Level 2	Level 3	Total
Liabilities 2020 Financial liabilities at fair value through the profit and loss	**£'000**	**£'000**	**£'000**	**£'000**
- Investment contract liabilities	-	3	-	**3**
- Investment contracts on linked liability fund	-	360	-	**360**
- Derivatives	-	74	-	**74**
Total liabilities	**-**	**437**	**-**	**437**

The principal financial liabilities held at 31 December 2019, analysed by their fair value hierarchies are:

	Level 1	Level 2	Level 3	Total
Liabilities 2019 Financial liabilities at fair value through the profit and loss	£'000	£'000	£'000	£'000
- Investment contract liabilities	-	4	-	4
- Investment contracts on linked liability fund	-	375	-	375
- Derivatives	122	77	-	199
Total liabilities	**122**	**456**	**-**	**578**

The basis for determining the fair value hierarchy is as follows:

Level 1 – Valued using unadjusted quoted price in active markets for identical financial instruments.
Level 2 – Valued using techniques based significantly on observed market data.
Level 3 – Valued using techniques incorporating information other than observable market data.

Equity Investments

The Society invests in equity instruments which are actively traded on public stock exchanges with readily available active prices on a regular basis. Such instruments are classified as Level 1. The value is determined with reference to the latest available market price prevailing at the valuation point.

Fixed Interest Securities

Fixed interest securities is made up of debt securities issued by sovereign governments ("gilts") and debt securities issued by corporate entities ("corporate bonds"). Gilts are highly liquid and traded in active markets resulting in a Level 1 classification. Their value is determined with reference to the latest available market price prevailing at the valuation point. Corporate bonds are Level 2 instruments as there is not sufficient third party trading data to justify Level 1 classification. Their value is determined with reference, where possible, to at least two external third party price quotations. This ensures the price used is independent and verifiable.

Derivatives

The Society holds the following derivatives: bond futures, forward currency contracts; and interest rate swaps. Bond futures values are derived from active market quotes and exchange statements and classified as Level 1 using the latest available market price at the valuation point. Forward currency contracts and interest rate swaps are traded Over-The-Counter ("OTC") and calculated both in-house and using dual OTC Vendors, on a mid-market basis, using appropriate up-to-date market prices of underlying instruments applied to industry standard valuation models. Forward currency contracts are valued by either observable foreign exchange rates, observable or calculated forward points and option valuation models. They are classified as Level 2. For Interest rate swaps the most frequently applied valuation techniques include forward pricing and swap models, using present value calculations by estimating future cash flows and discounting them with the appropriate yield curves incorporating funding costs relevant for the position. These contracts are generally Level 2.

Assets held to cover linked liabilities

Assets held to cover linked liabilities consist of equity instruments held in funds which are measured based on their published net asset value they are classified as Level 2.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

04. Gross premiums written and payments to deposit

	Group & Society					
	2020 Periodic	2020 Single	2020 Total	2019 Periodic	2019 Single	2019 Total
	£'000	£'000	£'000	£'000	£'000	£'000
Assurance	3,929	-	3,929	2,658	-	2,658
Immediate needs annuities	-	4,209	4,209	-	3,610	3,610
Bonds and other single premiums	-	319	319	-	228	228
Healthcare policies	7,396	-	7,396	7,393	-	7,393
Payments to deposit	451	-	451	451	-	451
Unit linked	29	-	29	31	-	31
	11,805	4,528	16,333	10,533	3,838	14,371

All business is direct insurance

The gross new premiums written in the year are detailed below:

	Group & Society					
	2020 Periodic	2020 Single	2020 Total	2019 Periodic	2019 Single	2019 Total
Gross new premiums written	£'000	£'000	£'000	£'000	£'000	£'000
Assurance	3,145	-	3,145	2,544	-	2,544
Immediate needs annuities	-	4,209	4,209	-	3,610	3,610
Bonds and other single premiums	-	319	319	-	228	228
Healthcare policies	1,801	-	1,801	1,570	-	1,570
	4,946	4,528	9,474	4,114	3,838	7,952

Gross new business premiums consist of the annual amount due for regular premium policies, regardless of whether such amounts relate in part or in whole to the next financial year, and the total amount due for single premium policies.

The Society only transacts long term business within the United Kingdom.

05. Investment Income

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
Income from land and buildings	**1,514**	**1,524**	**1,514**	**1,524**
Fixed interest stocks	2,059	2,331	2,059	2,331
Ordinary shares	263	428	263	428
Income from investments at fair value through profit and loss	**2,322**	**2,759**	**2,322**	**2,759**
Bank interest	10	19	10	19
Mortgages	3	3	3	3
Income from other investments	**13**	**22**	**13**	**22**
Income from investments	**3,849**	**4,305**	**3,849**	**4,305**
Net (losses)/gains on realisation of land and buildings	308	(370)	308	(370)
Net (losses)/gains on realisation of investments at fair value through profit and loss	4,407	(327)	4,407	(327)
Net (losses)/gains on realisation of investments	**4,715**	**(697)**	**4,715**	**(697)**
Investment income	**8,564**	**3,608**	**8,564**	**3,608**
Net unrealised gains/(losses) on investments				
- Land and buildings	(2,238)	1,040	(2,238)	1,040
- Investments at fair value through profit and loss	(1,511)	6,647	(1,511)	6,647
- Assets held to cover linked liabilities at fair value through profit and loss	(32)	168	(32)	168
	(3,781)	**7,855**	**(3,781)**	**7,855**
Total investment return	**4,783**	**11,463**	**4,783**	**11,463**

There is no interest expense in respect of financial liabilities not at fair value through profit and loss.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

06. Other technical income

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
Insurance commission	539	412	1	2
Other income	92	27	92	27
	631	**439**	**93**	**29**

07. Net operating expenses

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
a) Included in operating expenses are:				
Fees payable to external auditors:				
Audit of the Group and Society financial statements	211	194	205	188
Fees payable to internal auditors in respect of:				
Internal audit	48	51	48	51
Actuarial fees	23	17	23	17
Depreciation of tangible assets	68	62	68	62
(b) Other technical charges – project costs:				
Capital management	810	629	810	629
Distribution	105	40	41	26
Systems and processing	447	587	447	587
Risk management	284	223	284	223
Total project costs	**1,646**	**1,479**	**1,582**	**1,465**

08. Investment expenses

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
Investment management expenses	253	255	253	255
Investment property direct costs	497	575	497	575
	750	**830**	**750**	**830**

09. Staff costs

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
Average monthly number of employees:				
Administration	43	38	43	38
Distribution	36	25	23	20
	79	**63**	**66**	**58**

The average full-time equivalent is 77 (2019: 60) for the Group and 64 (2019: 55) for the Society. Excludes Non-Executive Directors of 5 (2019: 4).

	Group		Society	
	2020	2019	2020	2019
	£'000	£'000	£'000	£'000
Wages and salaries (inc commission)	3,350	2,903	2,947	2,694
Social security costs	353	310	316	290
Pension costs	239	199	218	183
	3,942	**3,412**	**3,481**	**3,167**

This includes Directors' emoluments totalling £559,886 (2019: £487,764). Details of Directors' remuneration are set out on page 38.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

10. Directors' Emoluments

	Group & Society	
	2020	2019
	£'000	£'000
Aggregate emoluments	560	488

There are no retirement benefits accruing for Executive Directors as at 31 December 2020 (2019: one) under a defined benefit scheme. The aggregate amount of pension contribution made by the Society to a defined contribution scheme was £15,990 (2019: £5,274).

	Group & Society	
	2020	2019
Highest paid Director	**£'000**	**£'000**
Total emoluments	200	244
Defined benefit scheme: Pension accrued during the year	1	-
Defined contribution scheme: Contributions made by the Society	-	-

11. Taxation

	Group		Society	
	2020	2019	2020	2019
(a) Tax attributable to long term business	£'000	£'000	£'000	£'000
Tax (credited)/charged in the long-term business technical account comprises: **Current tax** UK corporation tax	-	-	-	-
Prior year adjustments	-	(21)	-	(21)
Total current tax	**-**	**(21)**	**-**	**(21)**
Deferred tax				
Origination and reversal of timing differences	(3)		-	-
Total deferred tax	**(3)**	**1**	**-**	**-**
Total tax credited in the long-term business technical account	**(3)**	**(20)**	**-**	**(21)**

	Group		Society	
	2020	2019	2020	2019
(b) Factors that may affect future tax charges	£'000	£'000	£'000	£'000
The deferred tax assets which have not been recognised due to the uncertainty of their recoverability in the foreseeable future comprise: Realised and unrealised capital losses	218	112	218	112
Expenses deductible in future years	173	233	173	233
Trade losses	999	816	-	-
Short term timing differences	3	4	-	-
Deferred tax asset not recognised	**1,393**	**1,165**	**391**	**345**

The tax charge for the Society which pays BLAGAB tax is provided at a rate of 20% (2019: 20%) computed in accordance with the rates applicable to life assurance companies whereby no tax is charged on pension business profits or permanent health insurance business profits.

For subsidiaries of the Group, tax is provided at a rate of 19% (2019: 19%). In March 2021, the UK Government announced its intention to introduce legislation to increase the main rate of corporation tax from 19% to 25% from 1 April 2023. This change was substantively enacted on 24 May 2021. This announcement was not substantively enacted at the balance sheet date and therefore deferred taxes at the balance sheet date continue to be measured at the enacted rate of 19%.

The tax expense for the subsidiaries is affected by current tax and the non-recognition of current year tax losses, as well as other timing differences. A reconciliation of the total tax expense can be found in the individual statutory accounts in each of National Deposit Friendly Societies' subsidiaries where material differences between accounting and taxable profits arise.

These deferred tax assets may be realised, and therefore reduce future tax payable, when net gains chargeable to corporation tax are realised or when there is sufficient taxable income with which to offset carried forward expenses and/or losses. This will therefore depend substantially upon future movements in the stock market and on future taxable income which cannot be predicted with certainty. There are unused gross capital losses of £1,195,248 (2019: £1,772,340).

Expenses deductible in the Society in future periods are primarily driven by excess management expenses carried forward of £660,803 (2019: £928,526), along with expenses for which tax relief is spread over 7 years of £10,303 (2019: £44,927). Future pension contributions and fixed asset timing differences make up a further £195,674 (2019: £192,108) of future tax deductions. Trade losses not recognised are made up of £5,261,661 (2019: £4,797,294) of trading losses incurred in the subsidiaries.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

11. Taxation (continued)

	Group		Society	
	2020	2019	2020	2019
(c) Balance sheet The deferred tax balance included within other assets comprises:	£'000	£'000	£'000	£'000
Realised capital losses	22	243	22	243
Unrealised capital gains	(22)	(243)	(22)	(243)
Trade losses	13	10	-	-
Undiscounted deferred tax asset balance	**13**	**10**	**-**	**-**
(d) Reconciliation of deferred taxation balances				
Opening deferred tax asset	10	11	-	-
(Charge)/credit to income statement	3	(1)	-	-
Credit/(charge) to statement of comprehensive income	-	-	-	-
	13	**10**	**-**	**-**

12. Investments
Land and buildings

	Group		Society	
	2020	2019	2020	2019
Freehold investment properties	**£'000**	**£'000**	**£'000**	**£'000**
At 1 January	15,283	17,280	15,283	17,280
Disposals	(2,058)	(1,875)	(2,058)	(1,875)
Net gains on revaluation	-	(1,190)	-	(1,190)
At 31 December	**13,225**	**14,215**	**13,225**	**14,215**
Long leasehold properties				
At 1 January	4,435	5,050	4,435	5,050
Additions	1,831	1,831	1,831	1,831
Net gains on revaluation	-	(1,231)	-	(1,231)
At 31 December	**6,266**	**5,650**	**6,266**	**5,650**
Freehold ground rents				
At 1 January	4	60	4	60
Disposals	-	-	-	-
Net gains on revaluation	-	-	-	-
At 31 December	**4**	**60**	**4**	**60**
Freehold and long leasehold investment properties: At 31 December	**19,495**	**19,925**	**19,495**	**19,925**

The Society's properties are included at Fair Value. The Properties are valued by Mellersh and Harding LLP as at 31st December 2020 in accordance with the requirements of the Royal Institution of Chartered Surveyors' Valuation - Professional Standards effective from 6th January 2014.

Under the fair value measurement hierarchy, investment properties are classed as level 3 as they are valued using techniques incorporating information other than observable data.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

13. Other financial investments

	Group & Society			
	2020 £'000 Cost	2020 £'000 Valuation	2019 £'000 Cost	2019 £'000 Valuation
Listed fixed interest securities	53,322	60,341	53,130	61,702
Listed shares	7,034	6,440	9,939	10,338
Derivatives	-	1,589	-	685
Deposits with credit institutions	1,367	1,367	3,419	3,419
Mortgages	113	113	115	115
	61,836	**69,850**	**66,603**	**76,259**

Of the listed fixed interest securities £21,212,932 (2019: £15,694,110) relates to overseas fixed interest securities, with the remainder relating to UK fixed interest securities.

Of the listed shares £nil (2019: £nil) relates to overseas investments, with the remainder relating to UK investments.

Derivatives consist of: forward contracts for foreign currency exchange to mitigate the risk of a change in foreign currency exchange rates; futures to manage the duration of the fixed interest portfolio; and held to hedge against the change in value of the liabilities of the Society and the Staff Superannuation Fund (SSF) which would result from a change in bond yields. The gain in the value of these contracts has been recognised through the income statement. The forward contracts and futures will mature in 2021, the interest rate swaps will mature by 2060.

Included within deposits with credit institutions is £204,556 (2019: £593,536) which relates to cash in a cash margin account which enables the Society to enter into the forward contracts. This amount is held with the clearing house for the life of the contracts and is refunded if market movements mean that the contract is favourable and used to pay for the liability if it is adverse.

14. Financial assets

	Group			
	2020 £'000	2020 £'000	2019 £'000	2019 £'000
Financial assets at fair value through profit and loss	**Cost**	**Valuation**	**Cost**	**Valuation**
Designated upon initial recognition	66,988	75,697	68,033	78,442
	66,988	**75,697**	**68,033**	**78,442**
Loans and receivables	2,195	2,195	2,322	2,322
Total financial assets	**69,183**	**77,892**	**70,355**	**80,764**
Included in the balance sheet as:				
Listed fixed interest securities	53,322	60,341	53,130	61,702
Listed shares	7,034	6,440	9,939	10,338
Derivatives	-	1,589	-	685
Deposits with credit institutions	1,367	1,367	3,419	3,419
Mortgages	113	113	115	115
Other financial investments (Note 13)	**61,836**	**69,850**	**66,603**	**76,259**
Assets held to cover linked liabilities (Note 16)	908	1,603	931	1,684
Debtors arising from direct insurance operations	160	160	117	117
Other debtors	417	417	689	689
Cash at bank and in hand	4,357	4,357	614	614
Accrued interest and rent	1,505	1,505	1,401	1,401
Total financial assets	**69,183**	**77,892**	**70,355**	**80,764**

	Society			
	2020 £'000	2020 £'000	2019 £'000	2019 £'000
Financial assets at fair value through profit and loss	**Cost**	**Valuation**	**Cost**	**Valuation**
Designated upon initial recognition	66,959	75,668	67,967	78,376
	66,959	**75,668**	**67,967**	**78,376**
Loans and receivables	2,148	2,148	2,317	2,317
Total financial assets	**69,107**	**77,816**	**70,284**	**80,693**
Included in the balance sheet as:				
Listed fixed interest securities	53,322	60,341	53,130	61,702
Listed shares	7,034	6,440	9,939	10,338
Derivatives	-	1,589	-	685
Deposits with credit institutions	1,367	1,367	3,419	3,419
Mortgages	113	113	115	115
Other financial investments (Note 13)	**61,836**	**69,850**	**66,603**	**76,259**
Assets held to cover linked liabilities (Note 16)	908	1,603	931	1,684
Debtors arising from direct insurance operations	118	118	112	112
Other debtors	412	412	689	689
Cash at bank and in hand	4,328	4,328	548	548
Accrued interest and rent	1,505	1,505	1,401	1,401
Total financial assets	**69,107**	**77,816**	**70,284**	**80,693**

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

15. Financial Liabilities

	Group			
	2020 £'000	2020 £'000	2019 £'000	2019 £'000
Financial liabilities at fair value through profit and loss	**Cost**	**Valuation**	**Cost**	**Valuation**
Designated upon initial recognition	-	74	-	199
Other financial liabilities at amortised cost	1,867	1,867	2,016	2,016
Total financial liabilities	**1,867**	**1,941**	**2,016**	**2,215**
Included in the balance sheet as:				
Derivatives	-	74	-	199
Investment contract liabilities	3	3	4	4
Investment contract liabilities on linked liability fund	360	360	375	375
Arising out of direct insurance operations	-	-	49	49
Other creditors including taxation and social security	472	472	607	607
Accruals and deferred income	1,032	1,032	981	981
Total financial liabilities	**1,867**	**1,941**	**2,016**	**2,215**

	Society			
	2020 £'000	2020 £'000	2019 £'000	2019 £'000
Financial liabilities at fair value through profit and loss	**Cost**	**Valuation**	**Cost**	**Valuation**
Designated upon initial recognition	-	74	-	199
Other financial liabilities at amortised cost	1,975	1,975	2,078	2,078
Total financial liabilities	**1,975**	**2,049**	**2,078**	**2,277**
Included in the balance sheet as:				
Derivatives	-	74	-	199
Investment contract liabilities	3	3	4	4
Investment contract liabilities on linked liability fund	360	360	375	375
Arising out of direct insurance operations	-	-	49	49
Other creditors including taxation and social security	358	358	393	393
Accruals and deferred income	1,254	1,254	1,257	1,257
Total financial liabilities	**1,975**	**2,049**	**2,078**	**2,277**

Derivatives consist of forward contracts for foreign currency exchange to mitigate the risk of a change in foreign currency exchange rates. The loss in the value of these contracts has been recognised through the income statement forming a natural hedge. Other financial liabilities are carried in the balance sheet at amortised cost. Their fair values are not materially different from the values shown above.

16. Assets held to cover linked liabilities

	Group & Society			
	2020 £'000	2020 £'000	2019 £'000	2019 £'000
	Cost	Valuation	Cost	Valuation
Assets held to cover unit linked insurance contracts	704	1,244	709	1,282
Assets held to cover unit linked investment contracts	204	359	222	402
	908	**1,603**	**931**	**1,684**

Included within assets held to cover linked liabilities is -£1,402 (2019: £112,562) representing units not yet purchased by policyholders.

An analysis of total financial assets, including assets held to cover linked liabilities is provided in Note 14 'Financial assets'.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

17. Intangible assets

	Group				
	Software under Construction	Customer Book	Website	Computer Software	Total
At 31 December 2019	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Cost/Valuation	-	429	-	3,550	3,979
Accumulated depreciation and impairment	-	(42)	-	(850)	(892)
Carrying amount	**-**	**387**	**-**	**2,700**	**3,087**
Year ended 31 December 2020					
Opening net book value	-	387	-	2,700	3,087
Additions	203	-	4	-	207
Amortisation	-	(42)	(1)	(300)	(343)
Carrying amount	**203**	**345**	**3**	**2,400**	**2,951**
At 31 December 2020					
Cost/Valuation	203	429	4	3,550	4,186
Accumulated depreciation and impairment	-	(84)	(1)	(1,150)	(1,235)
Carrying amount	**203**	**345**	**3**	**2,400**	**2,951**

	Society	
	Software under Construction	Total
At 31 December 2019	**£'000**	**£'000**
Cost/Valuation	-	-
Accumulated depreciation and impairment	-	-
Carrying amount	**-**	**-**
Year ended 31 December 2020		
Opening net book value	-	-
Additions	203	203
Carrying amount	**203**	**203**
At 31 December 2020		
Cost/Valuation	203	203
Accumulated depreciation and impairment	-	-
Carrying amount	**203**	**203**

18. Tangible assets

	Group				
	Land & Buildings	Computer Equipment	Office Equipment	Motor Vehicle	Total
At 31 December 2019	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Cost/Valuation	2,740	496	187	121	**3,544**
Accumulated depreciation and impairment	-	(484)	(112)	(57)	**(653)**
Net book amount	**2,740**	**12**	**75**	**64**	**2,891**
Year ended 31 December 2020					
Opening net book value	2,740	12	75	64	**2,891**
Additions	-	34	7	47	**88**
Disposals – cost	-	-	-	(67)	**(67)**
Disposals – accumulated depreciation	-	-	-	53	**53**
Depreciation	-	(12)	(21)	(35)	**(68)**
Revaluation	240	-	-	-	**240**
Closing net book amount	**2,980**	**34**	**61**	**62**	**3,137**
At 31 December 2020					
Cost/Valuation	2,980	530	194	101	**3,805**
Accumulated depreciation and impairment	-	(496)	(133)	(39)	**(668)**
Net book amount	**2,980**	**34**	**61**	**62**	**3,137**

	Society				
	Land & Buildings	Computer Equipment	Office Equipment	Motor Vehicle	Total
At 31 December 2019	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Cost/Valuation	2,740	496	187	121	**3,544**
Accumulated depreciation and impairment	-	(484)	(112)	(57)	**(653)**
Net book amount	**2,740**	**12**	**75**	**64**	**2,891**
Year ended 31 December 2020					
Opening net book value	2,740	12	75	64	**2,891**
Additions	-	34	7	47	**88**
Disposals – cost	-	-	-	(67)	**(67)**
Disposals – accumulated depreciation	-	-	-	53	**53**
Depreciation	-	(12)	(21)	(35)	**(68)**
Revaluation	240	-	-	-	**240**
Closing net book amount	**2,980**	**34**	**61**	**62**	**3,137**
At 31 December 2020					
Cost/Valuation	2,980	530	194	101	**3,805**
Accumulated depreciation and impairment	-	(496)	(133)	(39)	**(668)**
Net book amount	**2,980**	**34**	**61**	**62**	**3,137**

The net book value of land and buildings consists of the proportion of 11-12 Queen Square, Bristol utilised by the Society and Group as a head office, which is valued on a Fair Value basis.

The valuation was performed by Mellersh and Harding LLP as at 31st December 2020 in accordance with the requirements of the Royal Institution of Chartered Surveyors' Valuation - Professional Standards effective from 6th January 2014. Under the amortised cost model the land and buildings have a cost of £1,538,000 (2019: £1,538,000), a useful life of 100 years and a net book value of £1,430,000 (2019: £1,446,000).

Under the fair value measurement hierarchy, tangible fixed assets are classed as level 3 as they are valued using techniques incorporating information other than observable data.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

19. Capital commitments

Amounts authorised and contracted for at 31 December 2020 are £nil (2019: £1,831,364).

20. Long term business provision

The long term business provision has been calculated on the basis of the following principal assumptions:

Rates of interest	Solvency II Best Estimate Assumptions
All contracts	Based on prescribed Solvency II rates

Rates of mortality	Solvency II Best Estimate Assumptions
Health contracts	Ranges from 39.0% to 71.0% (2019: 69.0% to 78.2%) of the AMN00 and AFN00 ultimate tables for assured lives depending on the contract.
Life contracts	Ranges from 29.7% to 1,280% (2019: 29.7% to 400%) of the AMN00, AFN00 and AMS00 ultimate table for assured lives depending on the contract, and for Guaranteed Life Assurance contracts CMI 2018 for future mortality improvements with a long term improvement of 1.25% per annum.
Pension and Annuity contracts	Ranges from 50.6% to 113.1% (2019: 50.6% to 113.1%) of the PNMA00 and PNFA00 mortality tables, and for annuities CMI 2018 for future mortality improvements with a long term improvement of 1.25% per annum.

Rates of lapse	Solvency II Best Estimate Assumptions
All contracts	Lapse assumptions are based upon the Society's actual experience.

Rates of morbidity	Solvency II Best Estimate Assumptions
Health contracts	Morbidity assumptions are based upon the Society's actual experience.

Future morbidity claims cost inflation	Solvency II Best Estimate Assumptions
Health contracts	Morbidity claims cost inflation assumptions are based upon the Society's actual experience and expert judgement.

Expenses	Solvency II Best Estimate Assumptions
Death Benefits Only (DBO) contracts	£3.17 (2019: £3.10) per annum
Non-DBO Old Deposit contracts	£42.74 (2019: £43.02) per annum
Health contracts excluding Optimum combined	£65.19 (2019: £70.79) per annum
Optimum combined contracts	£79.44 (2019: £85.13) per annum
All life assurance and pension policies	£28.49 (2019: £28.68) per annum
Immediate Needs Annuity contracts	£42.74 (2019: £43.02) per annum
Income Protection contracts	£44.85 (2019: £73.63) per annum
All life assurance and pension policies	£28.49 (2019: £28.68) per annum
Per policy Expense Inflation	2.5% (2019: 2.5%) per annum
Tax relief on per policy expenses for taxable business	15%
Offset for with profits life assurance policies	The value of expenses detailed in the terms and conditions for that particular policy

Full details of the method and assumptions used in calculating the long-term business provision are given in the Society's Solvency and Financial Condition Report.

21. Pensions

National Deposit Staff Superannuation Fund

Nature of the Fund

The NDFS Staff Superannuation Fund operated by the Society is a funded defined benefit arrangement which provides retirement benefits based on final pensionable salary.

The Fund is closed to the future accrual of benefits with effect from 31 May 2009. All remaining active members were treated as having left Pensionable Service with effect from that date. These members receive increases in deferment equal to the higher of the increase in their pensionable salary and statutory deferred revaluation while they remain in employment with the Society.

The most recent actuarial valuation of the Fund indicated that the Fund had a deficit. The Society and the Trustees of the Fund have put in place a Schedule of Contributions and a Recovery Plan which detail the contributions that will be made to fund this deficit, which are monthly payments of £15,925 over the period from April 2015 to March 2018, £25,000 from April 2018 to March 2019, £30,000 from April 2019 to March 2020, £35,000 from April 2020 to March 2021 and £40,000 from April 2021 to November 2022 inclusive. Along with one-off contributions of £500,000 in April 2018 and £250,000 in April 2019 and April 2021.

The most recent formal actuarial valuation of the Fund was carried out as at 31 December 2016. The calculations for the FRS102 disclosures have been carried out by running full actuarial calculations as at 31 December 2020.

Funding Policy

Following the cessation of accrual of benefits with effect from 31 May 2009, regular contributions to the Fund are no longer required. However, additional contributions are still made to cover any shortfalls that arise following each valuation. The funding method employed to calculate the value of previously accrued benefits is the Projected Unit Method. The Trustees determine the level of contributions payable to the Fund following agreement from the Society and advice of the Fund's Actuary.

Fund Amendments

There have been no amendments to the Fund during the year and no special events have occurred.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

21. Pensions (continued)

Employee benefit obligations for National Deposit Friendly Society Limited in respect of the National Deposit Friendly Society Staff Superannuation Fund

The amounts recognised in the balance sheet are as follows:

	Group & Society	
	2020 £'000	2019 £'000
Fair value of fund assets	20,774	20,044
Present value of funded obligations	(21,006)	(21,375)
Net (under) / overfunding in Fund	**(232)**	**(1,331)**
Liability recognised on the balance sheet	(232)	(1,331)
Net Defined Benefit Liability	**(232)**	**(1,331)**

The amounts recognised in income statement are as follows:

	Group & Society	
	2020 £'000	2019 £'000
Net Interest expense	20	10
Expense recognised in the Income Statement	**20**	**10**

	Group & Society	
	2020 £'000	2019 £'000
Interest on obligation	376	519
Interest on assets	(356)	(509)
Net Interest expense	**20**	**10**

The amounts recognised as Remeasurements in the Statement of Comprehensive Income are as follows:

	Group & Society	
	2020 £'000	**2019 £'000**
Return on assets (not included in interest)	979	926
Actuarial (Losses)/Gains on obligation	(173)	(2,095)
Total Remeasurements recognised in Other Comprehensive Income	**806**	**(1,169)**
Cumulative amount of Remeasurements recognised in Other Comprehensive Income	**(2,099)**	**(2,905)**
Actual return on Fund assets	**(169)**	**1,435**

The following other costs are included in the relevant sections of the accounts.

	Group & Society	
	2020 £'000	**2019 £'000**
Administration expenses paid from Fund	92	68
Other Items	**92**	**68**

The Society contributed £405,000 to the Fund over the year from 1 January 2020 to 31 December 2020 (2019: £595,000). No contributions were paid by members of the Fund over the period.

The Society expects to contribute £715,000 to the Fund over the year from 1 January 2021 to 31 December 2021. No contributions are expected by members of the Fund over the next year.

Changes in the present value of the Fund's Defined Benefit Obligation are as follows:

	Group & Society	
	2020 £'000	**2019 £'000**
Opening defined benefit obligation	21,375	19,664
Benefits paid	(918)	(903)
Interest on obligation	376	519
Experience (gains)/losses	(404)	33
Losses from changes in assumptions	577	2,062
Closing defined benefit obligation	**21,006**	**21,375**

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

21. Pensions (continued)

The weighted average duration of the liabilities of the Fund was 15 years as at 31 December 2020.

Changes in the fair value of the Fund assets are as follows:

	Group & Society	
	2020 £'000	2019 £'000
Opening fair value of fund assets	20,044	18,985
Interest on assets	356	509
Return on assets (not included in interest)	979	926
Contributions by employer	405	595
Benefits paid	(918)	(903)
Administration expenses	(92)	(68)
Closing fair value of fund assets	**20,774**	**20,044**

The major categories of fund assets as a percentage of the total are as follows:

	%	%
Equities	-	32
Gilts	**69**	13
Corporate bonds	**12**	27
Property	**18**	19
Cash	**1**	9

All of the Fund's assets are classed as level 2 under the fair value hierarchy, as they are valued using techniques based on observed market data. The Fund holds no financial instruments issued by the Company (other than incidentally through investment in pooled funds), nor does it hold any property or other assets used by the Company.

Principal actuarial assumptions at the balance sheet date (expressed as weighted averages (where applicable)).

	Group & Society	
	2020 %pa	2019 %pa
Discount rate at 31 December	1.3	1.8
Discount rate at 1 January	1.8	2.7
Inflation (Retail Price Index)	2.4	2.8
Rate of increase in pensionable salaries	2.8	2.8
Rate of increase in deferred pensions	2.0	2.0
Rate of increase in pensions in payment – service pre 06/04/2005	2.4	2.8
Rate of increase in pensions in payment – service post 06/04/2005	1.9	2.2

Mortality assumptions

The mortality assumptions are based on standard mortality tables, which allow for future mortality improvements. The assumptions are that a member aged 65 will live on average until age 87 if they are male and until age 89 if female.

For a member currently aged 50 the assumptions are that if they attain age 65 they will live on average until age 88 if they are male and until age 90 if female.

Defined contribution scheme

The contributions to the defined contribution scheme made by the Society in the year amounted to £218,250 (2019: £183,372), and contributions made by the Group amounted to £239,154 (2019: £198,869).

22. Technical provisions for linked liabilities

	Group & Society					
	Insurance contracts		Investment contracts		Total	
	2020 £'000	2019 £'000	2020 £'000	2019 £'000	2020 £'000	2019 £'000
At 1 January	1,196	1,036	375	327	1,571	1,363
Payments made to policy holders of investment contracts	-	-	(34)	(28)	(34)	(28)
Change in technical provision as shown in the income statement	48	160	19	76	67	236
At 31 December	**1,244**	**1,196**	**360**	**375**	**1,604**	**1,571**

All movements in unit-linked insurance contracts including premium receipts and claims payments, are recorded in the Income Statement.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

23. Assets attributable to the long term business fund

All assets shown on the Balance Sheet on page 52 are attributable to the long term business fund.

24. Operating lease commitments

The Society leases various office equipment under cancellable operating lease agreements. The lease terms are for up to five years, with penalty for early cancellation.

Total future minimum lease payments: plant & machinery	Group & Society	
	2020 £'000	2019 £'000
Within one year	-	-
Between one and five years	-	-
After five years	20	20
Total	**20**	**20**

25. Related party transactions

National Friendly Financial Solutions Limited was charged £458,526 (2019: £471,270) by the Society in respect of service charges.

The Society paid National Friendly Financial Solutions Limited commission of £656,619 (2019: £333,348) for the sale of National Friendly products.

Contributions of £405,000 (2019: £595,000) were made to the National Deposit Friendly Society Staff Superannuation Fund, of which Jonathan Long is a Trustee, as agreed with the trustees with the objective of having sufficient assets to meet its liabilities.

During the year the Society paid National Friendly Software Solutions Limited £300,000 (2019: £300,000) in licence fees for the policy administration system.

As at 31 December 2020, the Society owed National Friendly Financial Solutions Limited £160,484 (2019: £193,953) and the Society owed National Friendly Software Solutions Limited £101,464 (2019: £110,114).

Key management personnel

All directors and certain senior employees who have authority and responsibility for planning, directing and controlling the activities of the Group are considered to be key management personnel. Total key management personnel compensation is £358,982 (2019: £322,617). Director's remuneration is disclosed in the directors' remuneration report on page 38.

In addition, the directors of the Society may from time to time purchase insurance or investment products marketed by the Society in the ordinary course of business on the same terms as those prevailing at the time for comparable transactions with other persons. In 2020 and 2019, other transactions with the Society's directors' were not deemed to be significant both by virtue of their size and in context with the directors' financial position. All of these transactions are on normal commercial terms.

26. Subsidiary undertakings

The Society has two wholly owned subsidiary companies incorporated in the United Kingdom: National Friendly Financial Solutions Limited and National Friendly Software Solutions Limited.

National Friendly Financial Solutions Limited operates a call centre giving financial advice. National Friendly Financial Solutions Limited is held by the Society at a fair value of £475,000 (2019: £426,000) after a revaluation loss of £556,000 (2019: £244,000). During the year additional capital of £605,000 (2019: £650,000) was provided to National Friendly Financial Solutions Limited.

National Friendly Software Solutions Limited licences a policy administration system to its customers and is held by the Society at a fair value of £118,000 (2019: £125,000) after a revaluation loss of £7,000 (2019: gain of £125,000).

The results of all subsidiaries for the year ended 31 December 2020 have been consolidated into the Group financial statements.

	Group & Society	
	2020 £'000	2019 £'000
Fair value of investment in subsidiaries at 1 January	551	20
Additional share capital provided in the year	605	650
Unrealised loss in value of subsidiaries	(563)	(119)
Fair value of investment in subsidiaries at 31 December	**593**	**551**

27. Fund for Future Appropriations

	Group		Society	
	2020 £'000	2019 £'000	2020 £'000	2019 £'000
As at 1 January	17,573	19,168	17,584	19,048
Transfer to/(from) the fund for future appropriations from income statement	(3,200)	(667)	(3,191)	(536)
Transfer to/(from) the fund for future appropriations from statement of comprehensive income	1,046	(928)	1,046	(928)
As at 31 December	**15,419**	**17,573**	**15,439**	**17,584**

The Fund for Future Appropriations represents the estimated surplus in the funds that has not been allocated and is available to meet regulatory and other solvency requirements.

Notes to the Financial Statements (continued)

For the year ended 31 December 2020

28. Derivatives

Included within assets are forward currency contracts with a fair value of £169,000 (2019: £395,000) and a fair value within liabilities of £74,000 (2019: £12,000). The nominal contract value of these contracts is £6,588,000 (2019: £13,792,000). These are used to manage the exchange rate risk arising from investments in non-sterling denominated bonds. Cash flows under these contracts are dependent on exchange rates at the dates on which the contracts mature. Movements in fair value arise due to variations in exchange rate and are reflected in the income statement. Fair value losses included in the income statement for 2020 in relation to the forward currency contracts amounted to £288,000 (2019: gains of £733,000).

Bond future contracts with a fair value of £16,000 (2019: £231,000) are held within assets and a fair value of £nil (2019: £122,000) within liabilities. The nominal contract value of these contracts is £1,272,000 (2019: £23,734,000) which are held to manage the duration of the fixed interest portfolio. Fair value losses for the year of £93,000 (2019: gains of £428,000) are included in the income statement in respect of bond future contracts.

Interest rate swaps with a fair value of £1,404,000 (2019: £59,000) are held within assets and a fair value of £nil (2019: £65,000) within liabilities. The nominal contract value of these contracts is £30,975,000 (2019: £24,375,000), they are held to hedge against the change in value of the liabilities of the Society and the Staff Superannuation Fund (SSF) which would result from a change in bond yields. The SSF liabilities are determined as projected member benefits discounted at an interest rate determined from bond yields. Fair value gains for the year of £1,409,000 (2019: losses of £5,000) are included in the income statement in respect of interest rate swaps.

The asset position of the forward currency contracts at 31 December 2020 has primarily been driven by the increase in value of sterling against the US dollar by $0.05 in November and December 2020, the US dollar investments have decreased in value, but the derivative contracts held to protect against this risk have increased into an asset position.

The asset position of the Bond futures at 31 December 2020 has primarily been driven by the increase in US treasury 10 year gilt yield of 0.05% in December 2020. Whilst this decreases the value of the US dollar bonds, the derivative contracts held to protect against this risk have increased into an asset position.

The main driver of whether the interest rate swaps are in an asset or liability position is the LIBOR rate. At 31 December 2020 the LIBOR rate on which the floating leg of the interest rate swap is based was higher than the fixed rate for all the contracts held. As a result these derivative contracts are all in an asset position.

Derivatives held at 31 December 2020	Group & Society		
	Contract value £'000	Fair value assets £'000	Fair value liabilities £'000
Forward currency contracts	6,588	169	74
Bond futures	1,272	16	-
Interest rate swaps	30,975	1,404	-
Total derivatives	**38,835**	**1,589**	**74**

Derivatives held at 31 December 2019	Group & Society		
	Contract value £'000	Fair value assets £'000	Fair value liabilities £'000
Forward currency contracts	13,792	395	12
Bond futures	23,734	231	122
Interest rate swaps	24,375	59	65
Total derivatives	**61,901**	**685**	**199**

29. Contingent liabilities

In the course of conducting business, from time to time, the Group companies receive liability claims, and become involved in actual or threatened related litigation in relation to issues from past selling practices, taxation and other regulatory matters. Potential liabilities are influenced by a number of factors including the actions and requirements of the external bodies including regulators and tax authorities as well as ombudsman rulings, industry compensation schemes and court judgments. The directors consider the need for provisions as the circumstances arise. The Group does not currently require a provision but has adequate reserves to meet all reasonably foreseeable eventualities.

30. Events after the end of the reporting period

Following a review of one of its subsidiaries (NFFS), during quarter one of 2021, the board became aware of an internal control breakdown that resulted in certain transactions being entered into that otherwise may not have been. In the circumstances members of the board sought advice and the matter is being investigated. The investigation is at an advanced stage and relevant regulatory parties have been informed as appropriate.

Steps have been taken to review and develop the internal control environment in relation to the internal control breakdown.

Your notes

Your notes

National Friendly

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