Registered Number 56357

Legal & General Reinsurance Company No.2 Limited
Report and Accounts 2021

Contents

Page

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INDEPENDENT AUDITOR'S REPORT

To the Shareholder and Board of Directors of Legal & General Reinsurance Company No.2 Limited

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Legal & General Reinsurance Company No.2 Limited (the "Company"), which comprise the statement of financial position for the period ended 31 December 2021, the statements of profit or loss and total comprehensive loss, changes in equity and cash flows for the period then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company for the period ended 31 December 2021, and its financial performance and its cash flows for the period then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Company in accordance with International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Bermuda and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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

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

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

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

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 will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

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

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

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

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

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

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

KPMG Audit Limited

Chartered Professional Accountants
Hamilton, Bermuda
29 April 2022

Statement of Profit or Loss and Total Comprehensive Loss

From 11 February to 31 December 2021

	Notes	2021 CA$m
Revenue		
Gross written premiums	1E	**494**
Net premiums earned		**494**
Investment return	1K/3	**1**
Total revenue		**495**
Expenses		
Claims and change in non-participating insurance contract liabilities	1E/4	**536**
Other expenses	1L	**6**
Total expenses		**542**
Loss for the period attributable to equity holders of the Company before tax		**(47)**
Income tax expense attributable to equity holder	1D	**-**
Profit or loss and total comprehensive loss for the period attributable to equity holder of the Company		**(47)**

All of the loss for the period is attributable to continuing activities.

There are no comparatives prepared as the Company was incorporated on 11 February 2021.

Statement of Financial Position

As at 31 December

	Notes	2021 CA$m
Assets		
Funds withheld	1F/7	**15**
Financial investments	1G/8	**561**
Cash and cash equivalents	1H	**23**
Total assets		**599**
Equity		
Share capital	10	**111**
Retained losses		**(47)**
Total shareholders' equity		**64**
Liabilities		
Non-participating insurance contracts liabilities	1E/11/12	**529**
Payables and other financial liabilities	1I/13	**6**
Total liabilities		**535**
Total equity and liabilities		**599**

The Notes on pages 9 to 24 are an integral part of these financial statements.

The financial statements on pages 5 to 8 were approved by the Board of Directors on 28 April 2022 and were signed on their behalf by:

DocuSigned by:
Tim Stedman
BE9AB8CA1DCC401...
T Stedman
Chairperson

DocuSigned by:
Carl Moxley
DF35383126D64E5...
C Moxley
Director

DocuSigned by:
Amy Ellison
9DC16EB325D4406...
A Ellison
Director

Statement of Changes in Equity
From 11 February to 31 December 2021

For the period ended 31 December 2021	Notes	Share capital CA$m	Retained losses CA$m	Total equity CA$m
As at incorporation		-	-	-
Issue of share capital	10	111	-	111
Profit or loss and total comprehensive loss for the period		-	(47)	(47)
As at 31 December 2021		111	(47)	64

Statement of Cash Flows

From 11 February to 31 December 2021

	2021 CA$m
Cash flows from operating activities	
Loss for the period	**(47)**
Adjustments for non-cash movements in profit for the period	
Realised and unrealised gains on financial investments	**(3)**
Accrued dividends and income	**(4)**
Net increase in operating assets	
Funds withheld	**(15)**
Non-profit non-unit linked investments	**(448)**
Net increase in operational liabilities	
Non-participating insurance contract liabilities	**529**
Payables and other financial liabilities	**6**
Interest received	**5**
Net cash flows from operating activities	**23**
Cash flows from investing activities	
Purchases of financial investments	**(111)**
Net cash flows used in investing activities	**(111)**
Cash flows from financing activities	
Proceeds from issue of share capital	**111**
Net cash flows from financing activities	**111**
Net increase in cash and cash equivalents	**23**
Cash and cash equivalents at incorporation	**-**
Cash and cash equivalents at 31 December	**23**

The Company's statement of cash flows includes all cash and cash equivalent flows.

1. Accounting policies

A Basis of preparation

The Company's financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRS') issued by the International Accounting Standards Board ('IASB'). The Company's financial statements also comply with International Financial Reporting Interpretations Committee ('IFRIC') interpretations as issued by the IASB. The financial statements have been prepared under the historical cost convention, with the exception of certain financial assets (including funds withheld and financial investments) and financial liabilities, which are reported at fair value through profit or loss ('FVTPL').

These financial statements contain information about Legal & General Reinsurance Company No.2 Limited as an individual company and do not contain consolidated financial information. The Company is included in the consolidated Group accounts of Legal & General Group Plc ('Group'), a United Kingdom ('UK') domiciled publicly traded company.

The Company presents its Statement of Financial Position in order of increasing liquidity. This is considered to be more relevant than a before and after 12 months presentation, given the long-term nature of the Company's core business. However, for each significant asset and liability line item, which combines amounts expected to be recovered or settled before and after 12 months from the Statement of Financial Position date, disclosure of the split is made by way of a note.

Financial assets and financial liabilities are disclosed gross in the Statement of Financial Position unless a legally enforceable right of offset exists and there is an intention to settle recognised amounts on a net basis. Income and expenses are not offset in the Statement of Profit or Loss and Total Comprehensive Income unless required or permitted by any accounting standard or IFRIC interpretation, as detailed in the applicable accounting policies of the Company.

(i) Going Concern

The Company's business activities, together with the factors likely to affect its future development, performance and position in the current economic climate are set out in the Company's financial statements. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are described in these financial statements. Principal risks and uncertainties are detailed in Note 18.

The Directors have made an assessment of the Company's going concern, considering both the Company's current performance and the Company's outlook for a period of at least, but not limited to, 12 months from the date of approval of these financial statements, which takes account of the current and future impact of the Covid-19 pandemic, using the information available up to the date of issue of these financial statements.

The Company manages and monitors its capital and liquidity, and various stresses are applied to those positions to understand potential impacts from market downturns. The key sensitivities and the impacts on the Company's capital position from a range of stresses are disclosed in Note 18. These stresses do not give rise to any material uncertainties over the ability of the Company to continue as a going concern. Based upon the available information, the Directors consider that the Company has the plans and resources to manage its business risks successfully.

Having reassessed the principal risks and uncertainties (both financial and operational) in light of the current economic environment, the Directors are confident that the Company will have sufficient funds to continue to meet its liabilities as they fall due for a period of, but not limited to, 12 months from the date of approval of the financial statements and therefore have considered it appropriate to adopt the going concern basis of accounting when preparing the financial statements.

(ii) New standards, interpretations and amendments to published standards that have been adopted by the Company

The Company has applied the following standards and amendments for the first time in its annual reporting period commencing 1 January 2021.

Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 – Interest Rate Benchmark Reform Phase 2
These amendments, issued in August 2020, address issues that might affect financial reporting after the reform of an interest rate benchmark, including its replacement with alternative benchmark rates. In particular, they offer practical expedients, under certain conditions, when a financial contract is modified due to a change resulting directly from Interbank Offered Rate ('IBOR') reform. They also allow a series of exemptions from the current rules around hedge accounting. The amendments will be considered as new interest rate benchmarks are introduced.

New disclosure requirements have also been introduced as part of Phase 2, and in line with these the Company has provided the below details around the nature and extent of risks to which it is exposed arising from financial instruments subject to IBOR reform, how such risks are managed and the Company's progress in completing its transition to alternative benchmark rates.

In the UK, GBP London Interbank Offered Rate ('LIBOR') has been replaced by Sterling Overnight Index Average ('SONIA') from the end of 2021. Furthermore, USD LIBOR is expected to be replaced by mid-2023. Euribor will remain but will be administered by EMMI ('Euro Money Markets Institute').

The key challenges for the Company arose in the following areas:

- All financial contracts that reference LIBOR needed to be amended;
- Derivatives and assets on balance sheet that were exposed to changes in market value when the reference rate changes needed to be considered;
- Customers needed to understand the implications for the products and agree the necessary changes.

1. Accounting policies (Continued)

To deal with these risks and to manage the Group wide conversion, the Group initiated a project in 2019 to transition away from LIBOR. Business as usual processes were enhanced to include increased market surveillance on LIBOR trading, added record-keeping specific to LIBOR trades, increased client communications and additional complaints monitoring processes.

The largest shareholder exposures are related to LIBOR-linked derivatives that are used for hedging the annuity business. In 2021, the Group stopped trading assets referenced to LIBOR (except in some very limited circumstances) and initiated a programme of replacing legacy assets denominated in LIBOR with new SONIA based positions.

The Company does not hold any GBP LIBOR exposure.

Trading out of USD LIBOR has been more gradual as a result of the transition date moving to 23 June 2023, however this has now accelerated following Group's guidance that no new USD LIBOR investments should be made from 1 January 2023.

The following table contains details of all of the financial instruments currently subject to the IBOR reform that the Company holds on its balance sheet at 31 December 2021, which have not yet transitioned to SONIA or an alternative interest rate benchmark. The amounts of non-derivative financial assets are shown at their carrying amounts and derivatives are shown at their notional amounts.

	USD LIBOR 2021 CA$m	**Total 2021 CA$m**
Derivatives assets (liabilities)[1]	(10)	**(10)**

1. The company currently holds derivatives within Funds Withheld

(iii) Standards, amendments and interpretations to published standards, which are not yet effective

Certain standards, amendments and interpretations to existing standards have been published which are mandatory for the Company's accounting periods beginning on or after 1 January 2022 or later periods but which the Company has not adopted early, as disclosed below.

IFRS 17 – Insurance Contracts
IFRS 17, 'Insurance Contracts' was originally issued in May 2017 and subsequent amendments were issued in June 2020. The standard is expected to be effective for annual periods beginning on or after 1 January 2023. The standard will be applied retrospectively, subject to the transitional options provided for in the standard and provides a comprehensive approach for accounting for reinsurance contracts including their measurement, income statement presentation and disclosure.

IFRS 17 is an accounting change and therefore while it will have an impact on the timing and profile of profit recognition, we expect the underlying economics and cash generation of the Company's businesses will remain the same. While the Company is still refining its methodology and completing the development of models and operational capabilities, it is not possible to provide a reliable estimate of the impact on adopting IFRS 17, nor of the ongoing impact on the Company's financial results.

In terms of key accounting policies and approaches, the Company is able to set out the following at this time:

- The Company will be applying the General Measurement Model to all business measured under IFRS 17.
- On transition to IFRS 17, the Company will apply the fully retrospective approach unless impracticable. In some instances, this will lead to the modified retrospective and fair value approaches being used for specific groups of reinsurance contracts.
- The selection of a rate at which to discount future cash flows for groups of reinsurance contracts is a key determinant in the valuation of the reinsurance liability. We intend to apply a top down discount rate to such groups, starting from an appropriate asset portfolio with economic deductions.
- IFRS 17 requires an accounting policy decision as to whether to recognise all finance income or expense in the profit and loss or whether to disaggregate the income or expense that relates to changes in financial assumptions into other comprehensive income. All finance income and expense will be included in profit or loss except for protection business where we intend to disaggregate such changes.

The Company participates in Group's programme to implement the standard. Work will continue throughout 2022 to ensure technical compliance as well as to test and embed the required systems and operational capability. Communication and training plans are in place for impacted employees, and the impact on resources across the Finance function is being assessed to ensure the business is ready to implement the new standard.

1. Accounting policies (Continued)

IFRS 9 – Financial Instruments
In July 2014, the IASB issued IFRS 9, 'Financial Instruments' which is effective for annual periods beginning on or after 1 January 2018. The standard replaces IAS 39 'Financial Instruments: Recognition and Measurement'. It includes new principles around classification and measurement of financial instruments, introduces an impairment model based on expected credit losses (replacing the current model based on incurred losses) and new requirements on hedge accounting. The IASB subsequently issued 'Amendments to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts' which allows entities which meet certain requirements to defer their implementation of IFRS 9 until adoption of IFRS 17 'Insurance Contracts' or 1 January 2021, whichever is the earlier. In June 2020, the IASB agreed to extend the temporary exemption in IFRS 4 from applying IFRS 9 to annual reporting periods beginning on or after 1 January 2023.

For an insurer to apply this deferral:
- (i) Total liabilities related to insurance must exceed 90% of total liabilities; or
- (ii) Total liabilities related to insurance are greater than 80% of total liabilities but less than 90% of total liabilities so long as the insurer does not engage in significant activity unconnected to insurance.

Total liabilities connected to insurance within the Company at the initial assessment date 31 December 2021 were 99% of total liabilities. The Company, therefore, qualifies for the deferral of IFRS 9 and is making use of this option.

In December 2021, in order to alleviate operational complexities and potential one-off accounting mismatches in comparative information between insurance contract liabilities and related financial assets on the initial application of IFRS 17, the IASB issued an amendment to IFRS 17 titled 'Initial Application of IFRS 9 and IFRS 17—Comparative Information'. If an entity applies IFRS 17 and IFRS 9 at the same time, this amendment permits it to present comparative information about financial assets derecognised in the comparative period as if the classification and measurement requirements of IFRS 9 had been applied to them. The Company has chosen to restate comparative information and to apply this classification overlay to all financial assets in scope. While the Company is still refining its methodology and completing the development of models and operational capabilities, it is not possible to provide a reliable estimate of the impact on adopting IFRS 9, nor of the ongoing impact on the Company's financial results.

IFRS 9 classifies financial assets into the following three categories: amortised cost, fair value through other comprehensive income ('FVOCI') and FVTPL. The classification of financial assets is based on the entity's business model for managing them, as well as their contractual cash flow characteristics. The Company expects to reclassify a certain amount of financial assets as a result of these assessments, in order to better align the accounting treatment of assets that are backing insurance contract liabilities under IFRS 17.

With the exception of financial assets measured under FVTPL, the Company will apply an expected credit loss impairment model to all financial assets in scope (including lease receivables and contract assets). The new impairment model requires utilising not only past events and current conditions but also reasonable and supportable forward-looking information, in order to assess the credit risk profiles of those financial assets in scope. The Company will recognise either twelve months' or lifetime expected credit losses in the consolidated income statement at each reporting period. The Company intends to use the practical expedient for financial assets with low credit risk at the reporting date, which allows recognising twelve months' expected credit losses. Additionally, for trade receivables, contract assets and lease receivables, the Company plans to use a provision matrix method to calculate and recognise lifetime expected credit losses.

Financial liabilities are expected to be classified and measured under their current categories (FVTPL or amortised cost) under IFRS 9.

The Company participates in Group's programme to implement the standard. Work will continue throughout 2022 to ensure technical compliance as well as to test and embed the required systems and operational capability. Communication and training plans are in place for impacted employees, and the impact on resources across the Finance function is being assessed to ensure the business is ready to implement the new standard.

(iii) Standards, amendments and interpretations to published standards which are not yet effective (continued)

Annual Improvements to IFRS Standards 2018-2020
These amendments, issued in May 2020, make minor amendments to IFRS 1 'First-time Adoption of IFRS', IFRS 9 'Financial instruments', IAS 41 'Agriculture' and the Illustrative Examples accompanying IFRS 16 'Leases'. The amendments are effective for annual reporting periods beginning on or after 1 January 2022. The Company does not expect the impact to be significant.

Amendments to IAS 37 – Provisions, contingent liabilities and contingent assets
These amendments, issued in May 2020, specify which costs a company includes when assessing whether a contract will be loss making. The amendments are effective for annual reporting periods beginning on or after 1 January 2022. The Company does not expect the impact to be significant.

Amendments to IAS 1 – Presentation of Financial Statements
These amendments, issued in February 2021, intend to help preparers in deciding which accounting policies to disclose in their financial statements on or after 1 January 2023. The Company does not expect the impact to be significant.

Amendments to IAS 8 – Accounting policies, Changes in Accounting Estimates and Errors
These amendments, issued in February 2021, aim to help entities to distinguish between accounting policies and accounting estimates. The amendments are effective for annual reporting periods beginning on or after 1 January 2023. The Company does not expect the impact to be significant.

Amendments to IAS 12 – Income Tax
These amendments, issued in May 2021, clarify how companies account for deferred tax on transactions such as leases and decommissioning obligations. The amendments are effective for annual reporting periods beginning on or after 1 January 2023. The Company does not expect the impact to be significant.

1. Accounting policies (Continued)

B Critical accounting policies and use of estimates

The preparation of the financial statements includes the use of estimates and assumptions, which affect items reported in the Statement of Financial Position and the Statement of Profit or Loss and Total Comprehensive Loss at the date of the financial statements. Although these estimates are based on management's best knowledge of current circumstances and future events and actions, actual results may differ from those estimates, possibly significantly.

The preparation of the financial statements has also considered the impact of climate change, and as at 31 December 2021, management does not consider this to be a significant area of accounting judgement or source of estimation uncertainty. Specific considerations around climate change have been presented in the Company's financial statements in the following sections:

- Financial investments (Note 8)
- IFRS sensitivity analysis (Note 18)

The major areas of judgement on policy application are considered below:

The determination of fair values of unquoted and illiquid financial investments (Notes 1G, 1H, 7, 8)

Determination of fair value of unquoted and illiquid assets, involves judgements, as mark to model valuations, through the incorporation of both observable and unobservable market inputs, inherently include assumptions that lead to the existence of a range of plausible valuations for financial assets. For unquoted financial investments, the Company obtains pricing information from a range of pricing services and brokers. Where there are indications that there is no active market, the Company seeks further evidence of the fair value from alternative pricing sources and market information. Priority is given to publicly available prices from independent sources when available, but overall, the source of pricing and/or the valuation technique is chosen with the objective of arriving at a fair value measurement, which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The valuation techniques include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and, if applicable, enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments.

Non-participating insurance contract liabilities (Notes 1E, 1F, 11, 12) and associated balances

This relates to the assessment of the significance of insurance risk transferred to the Company in determining whether a contract should be accounted for as an insurance or investment contract. Contracts, which transfer significant insurance risk to the Company, are classified as insurance contracts. Contracts that transfer financial risk (e.g. change in interest rate or security price) to the Company but not significant insurance risk are classified as investment contracts.

Judgement is required in order to assess the significance of the transfer of insurance risk within a contract. This assessment is based on whether the occurrence of an insured event could cause the Company to make significant additional payments, i.e. does the occurrence of the event cause significantly higher cash outflow for the Company than its non-occurrence.

The determination of long-term business liabilities can never be definitive as to the timing or the amount of claims and are therefore subject to regular reassessment. The assumptions for the rate of future longevity, and mortality are based on the Company's internal experience and judgements about how experience may vary in the future. This assessment takes into account market benchmarking, internal experience studies and independent industry data.

Determination of the expense assumptions used in the calculation of the insurance liabilities that represent the expected future costs of administering the underlying insurance policies. The expense assumptions are based on management's best estimate of these future costs. The main estimates and assumptions used in calculating insurance liabilities are disclosed in more detail in Note 13.

Determination of valuation interest rates used to discount the liabilities are sensitive to the assumptions made, for example, on credit default of the backing assets. These assumptions take into account consideration of market experience and historic internal data. The valuation interest rate is also sensitive to the selection of assets chosen to back the liabilities.

C Summary of significant accounting policies

The Company has selected accounting policies which state fairly its financial position, financial performance and cash flows for a reporting year. The accounting policies have been consistently applied to all years presented unless otherwise stated. Accounting policies that relate specifically to a balance or transaction are presented above the relevant numerical disclosure.

Financial assets and financial liabilities are disclosed gross in the Statement of Financial Position unless a legally enforceable right of offset exists and there is an intention to settle recognised amounts on a net basis. Income and expenses are not offset in the Income Statement unless required or permitted by any accounting standard, as detailed in the applicable accounting policies of the Company.

The principal accounting policies adopted in preparing these financial statements are set out below.

D Tax balances

Under current Bermuda law, the Company is not required to pay any taxes in Bermuda on either income or capital gains. The Company has received an undertaking from the Minister of Finance in Bermuda that in the event of any such taxes being imposed the Company will be exempted from taxation until the year 2035.

The Company is subject to tax in the UK on the profits that arise by reference to central management and control being undertaken by the Board of Directors in the UK.

1. Accounting policies (Continued)

In 2021, the Organisation for Economic Co-operation and Development ('OECD') agreed a landmark deal to implement a global minimum tax rate, alongside a tax on digital services based on the end user location. Model rules for the global minimum tax rate were published in December, with the intention that these should be effective from 2023. This is an ambitious target for introducing a new global tax regime, and significant effort is required for multi-national groups to achieve compliance with the new rules.

E Non-participating insurance contract liabilities
Non-participating insurance contracts are contracts, which transfer significant insurance risk to the insurer at the inception of the contract. The change in the insurance liability reflects the reduction in liabilities due to the payment of claims in the year, offset by liabilities arising from new business. The movement also reflects assumption changes relating to variables such as claims expectations, expenses and the unwind of the previous period's expectations.

Under current IFRS requirements, insurance contract liabilities are measured using the requirements under former UK Generally Accepted Accounting Principles ('GAAP'), as permitted by IFRS 4, 'Insurance contracts'.

The liabilities are calculated on the basis of current information using the gross premium valuation method. This brings into account the full premiums receivable under contracts written, having prudent regard to expected lapses and surrenders, estimated renewal and maintenance costs and contractually guaranteed benefits.

Gross written premiums represent the total premiums written by the Company before deductions for reinsurance. Premiums are recognised as revenue when due for payment. Claims and surrenders are accounted for when payment is due. Claims payable include the direct costs of settlement. Acquisition costs comprise direct costs, such as initial commission, and the indirect costs of obtaining and processing new business. These costs are charged to the Statement of Profit or Loss and Total Comprehensive Loss when incurred.

F Funds withheld
Funds withheld include assets contractually withheld by ceding companies in accordance with each respective reinsurance agreement. The value of the assets withheld and interest income are recorded in accordance with each specific treaty terms.

The funds withheld back the Company's non-participating policyholder liabilities and on initial recognition are designated at FVTPL. The funds withheld are measured at a value equal to the fair value of the underlying assets held by the withholding companies, with fair value gains and losses reflected in the Statement of Profit or Loss and Total Comprehensive Loss. The funds withheld are measured on the basis of current information relating to the assets withheld and are designated as FVTPL to avoid an accounting mismatch in the Statement of Profit or Loss and Total Comprehensive Loss.

G Financial investments
The Company classifies its financial investments on initial recognition as held for trading ('HFT') or designated at FVTPL. Initial recognition of financial investments is on the trade date. The Company's policy is to measure financial investments at FVTPL. All derivatives are classified as HFT.

Financial investments classified as HFT and FVTPL are measured at fair value with gains and losses reflected in the Statement of Profit or Loss and Total Comprehensive Loss. Transaction costs are expensed as incurred.

Certain financial investments held by the Company are designated as FVTPL as their performance is evaluated on a total return basis, consistent with asset performance reporting to the Company's Investment Committee and the Company's investment strategy. Assets designated as FVTPL include debt securities. Assets backing non-participating policyholder liabilities are designated as FVTPL. The Company's investments backing non-participating insurance contract liabilities are measured on the basis of current information and are designated as FVTPL to avoid an accounting mismatch in the Statement of Profit or Loss and Total Comprehensive Loss.

The fair values of quoted financial investments are based on current bid prices. If the market for a financial investment is not active, the Company establishes fair value by using valuation techniques such as recent arm's length transactions, consensus market pricing, reference to similar listed investments, discounted cash flow models or option pricing models.

Receivables are initially measured at fair value plus acquisition costs, and subsequently measured at amortised cost using the effective interest method.

H Cash and cash equivalents
Cash and cash equivalents include deposits held at call with banks, treasury bills and other short-term highly liquid investments with original maturities of three months or less from the date of acquisition.

I Payables and other financial liabilities
Payables and other financial liabilities comprise of management fees payable and are measured at amortised cost. The carrying value of these liabilities approximates their fair value.

J Foreign currency transactions
Foreign currency transactions are translated into the functional currency ('Canadian Dollar' or "CA$") using the exchange rate prevailing at the date of the transactions. Foreign currency monetary assets and liabilities are translated at the spot rate at period end. Foreign exchange gains and losses are recognised in the Statement of Profit or Loss and Total Comprehensive Loss, except when recognised in equity as qualifying cash flow or net investment hedges.

1. Accounting policies (Continued)

K Investment return
The reporting of investment return comprises investment income, unrealised gains and losses from financial investments held at FVTPL, and realised gains and losses from all financial assets and liabilities.

Investment income includes dividends and interest. Dividends are accrued on an ex-dividend basis. Interest is included on an accruals basis. Interest income for financial assets, which is not classified as FVTPL, is recognised using the effective interest method. Investment income is presented net of investment management fees.

L Other expenses
Other expenses comprise administrative expenses, management fees payable, corporate expenses and other charges. Other costs are accounted for as they arise. The Company does not have direct employees since they are employed by Legal & General Resources Bermuda Limited ('LGRB').

M Derivative financial instruments
The Company's activities expose it to the financial risks of changes in foreign exchange rates and interest rates. The Company uses a variety of exchange traded and over-the-counter derivative financial instruments, including, futures, options, forward currency contracts and swaps, such as interest rate swaps and cross currency basis swaps measured at fair value to hedge these exposures.

Changes in the fair value of any derivative instruments are recognised immediately in the Statement of Profit or Loss and Total Comprehensive Loss.

Where the risks and characteristics of derivatives embedded in other contracts are not closely related to those of the host contract and the whole contract is not carried at fair value, the derivative is separated from that host contract and measured at fair value, with fair value movements reflected within investment return, unless the embedded derivative itself meets the definition of an insurance contract.

2. Company information

The Company was incorporated on 11 February 2021 as a long-term Class E reinsurer in Bermuda under Bermuda's Insurance Act of 1978. The principal activity of the Company is the provision of life reinsurance solutions globally, focussing on pensions risk transfer ('PRT') in selected international markets. The Company currently has long-term PRT business in Canada.

The Company was capitalised with CA$111m. Legal & General Re Holdings Limited ('Re Holdings') is the direct parent and Legal & General Group Plc is the ultimate parent.

The Company is domiciled in Bermuda and its registered office and principal place of business is 19 Par-la-Ville Road, Hamilton HM 11 Bermuda. Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The financial statements are presented in Canadian Dollars ('CA$), which is also the Company's functional currency.

The Company has appointed KPMG Audit Limited as independent auditors.

3. Investment return

Total investment return for the period was a gain of CA$1m:

- Gross gain (including interest and dividend income) of CA$123k arose in the period on the funds withheld (See Note 7).
- Net gain of CA$2m arose on financial investments designated as FVTPL.
- Net loss of CA$1m arose from foreign exchange revaluation.

4. Claims and change in non-participating insurance contract liabilities

From continuing operations	2021 CA$m
Claims paid	7
Change in non-participating insurance contract liabilities	529
Total claims and change in non-participating insurance contract liabilities	**536**

5. Foreign exchange and exchange rates

Investment return for the period includes a foreign exchange loss of CA$1m arising on conversion of foreign currency monetary assets and liabilities to functional currency. During the period, losses arising from foreign currency financial investments amount to CA$ Nil.

Principal rates of exchange used for translation are:

	2021 Average	2021 Year-End
United States Dollar	**1.279**	**1.265**
Sterling	**1.704**	**1.711**
Euro	**1.447**	**1.439**

6. Dividends

The Company did not declare or pay a dividend to Re Holdings during the period.

7. Funds withheld

On 24 August 2021, the Company entered into a Business Transfer Agreement with Legal & General Reinsurance Company Limited (‘L&G Re’). L&G Re transferred to the Company its rights and obligations, including the associated investment and collateral arrangements, related to its Canadian PRT business. The agreement includes the transfer of the Canadian Funds Withheld (‘CFWH’) from L&G Re to the Company. Balance as of 31 December 2021 amounts to CA$15m.

Income accrued and return on the withheld assets, according to the terms defined in each reinsurance treaties, was a gain of 0.80% for the year ended 31 December 2021. The ratings of the assets underlying the funds withheld are shown in Note 18 Table 1.

Funds withheld that are expected to be settled within 12 months and after 12 months are in line with the expected settlement of the backed liabilities as per Note 11(ii).

8. Financial investments

(i) Financial investments at fair value

	Notes	2021 CA$m
Financial investments at fair value designated as:		
Fair value through profit or loss		**561**
Total financial investments	8(ii)	**561**
Expected to be received within 12 months		**39**
Expected to be received after 12 months		**522**

The financial investments are comprised of Canadian Shareholder Fund and Canadian Long-term Fund. The risks associated with financial investments are outlined in Note 18.

Financial investments have been allocated between those expected to be settled within 12 months and after 12 months in line with the expected settlement of the backed liabilities.

Financial investments within the Canadian Shareholder Fund include CA$4m of a Canadian treasury bill having a residual maturity of less than a year. The Company is entitled to receive all of the cash flows from the assets during the period when they are pledged as collateral and has the economic benefit on assets. The Company can decide to substitute an asset, which is designated as collateral at any time, provided the relevant terms, and conditions of the Security Deed are met.

Financial investments within the Canadian Long-term Fund include CA$463m of debt securities pledged as collateral in the course of writing treaties with the Company’s counterparties. The assets used as collateral are AAA, AA, A, BBB Corporate Bonds and Government Bonds having a residual maturity of up to 41 years. The Company is entitled to receive all of the cash flows from the assets during the period when they are pledged as collateral and has the economic benefit on assets. The Company can decide to substitute an asset, which is designated as collateral at any time, provided the relevant terms and conditions of the Security Deed are met.

8. Financial investments (Continued)

(ii) Fair value hierarchy of financial investments and funds withheld

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value measurements are based on observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's view of market assumptions in the absence of observable market information. The Company utilises techniques that maximise the use of observable inputs and minimise the use of unobservable inputs.

The levels of fair value measurement basis are defined as follows:

Level 1: fair values measured using quoted prices (unadjusted) in active markets for identical assets or liabilities.
Level 2: fair values measured using valuation techniques for all inputs significant to the measurement other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
Level 3: fair values measured using valuation techniques for any input for the asset or liability significant to the measurement that is not based on observable market data (unobservable inputs).

(ii) Fair value hierarchy of financial investments and funds withheld (Continued)

The following table presents the Company's assets by IFRS 13 hierarchy levels:

As at 31 December 2021	Total CA$m	Level 1 CA$m	Level 2 CA$m	Level 3 CA$m
Debt securities	557	-	557	-
Accrued interest	4	-	4	-
Total financial investments	**561**	**-**	**561**	**-**
Funds withheld	**15**	**4**	**11**	**-**

The Company's financial assets are valued, where possible, using standard market pricing sources, such as FT Interactive Date, Standard & Poor's, Bloomberg or Lehman. Each uses mathematical modelling and multiple source validation in order to determine consensus prices, with the exception of Over-the-Counter ('OTC') Derivative holdings; OTCs are marked to market using Reuters. In normal market conditions, the Company would consider these market prices to be observable and therefore classify them as Level 1. Where inputs to the valuation have been sourced from a market that is not suitably active, the prices have been classified as Level 2. Refer to Level 3 assets section for methodology.

The Company's policy is to re-assess categorisation of financial assets at the end of each reporting period and to recognise transfers between levels at that point in time.

The Company holds regular discussion with pricing providers to determine whether transfers or classifications between levels of the fair value hierarchy have occurred.

The Company does not have any financial assets classified as Level 3 as of year-end.

The Company's asset portfolio can be exposed to climate change through both:
- Transition risks from the move to a low-carbon economy and the impact this has on asset valuation and the economy; and
- Physical risks from the impact on asset holdings as a result of severe weather events and longer-term shifts in climate.

Exposure to the physical risks of climate change are minimised in the direct investment portfolios through rigorous assessment of potential investments, particularly in ensuring there is low susceptibility to extreme weather events. The Group monitors the carbon intensity of the investments held at a portfolio level to help understand the environmental impact and reduce high carbon intensive investments in the future.

9. IFRS 9 'Financial Instruments' deferral

(i) Fair value of financial assets with contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest ('SPPI') on the principal amount outstanding (i.e. passing the 'SPPI' test):

	Financial assets passing the SPPI test[1,2]	All other financial assets[3]
	2021 CA$m	2021 CA$m
Debt securities	-	557
Accrued interest	-	4
Funds withheld	-	15
Total financial investments at fair value	-	576
Total financial assets (excluding cash and cash equivalents)	-	576

1. Financial assets classified as FVTPL or that are managed and whose performance is evaluated on a fair value basis do not require an SPPI test to be performed. These assets are reported in 'All other financial assets'.
2. For financial assets which pass the SPPI test held at 31 December 2021, there was a change in the fair value in the period of CA$Nil.
3. For all other financial assets held at 31 December 2021, there was a decrease of fair value movement in the period of CA$2m.

10. Share capital

	2021 Number of shares	2021 CA$
Authorised share capital: Ordinary shares of US$1 each	**99,000,000**	**127,963,571**
Issued share capital: Fully paid ordinary shares of US$1 each	**88,732,000**	**111,434,800**

During the period, 88,732,000 authorised and issued ordinary shares of US$1 have been subscribed to by Legal & General Re Holdings Inc. There is one class of ordinary shares. All shares issued carry equal voting rights.

The holder of the Company's ordinary shares is entitled to receive dividends as declared and is entitled to one vote per share at shareholder meetings of the Company.

11. Non-participating insurance contract liabilities

(i) Analysis of non-participating insurance contract liabilities

	Note	Gross 2021 CA$m	Reinsurance 2021 CA$m
Non-participating insurance contracts liabilities	11(iii)	**529**	-
Total non-participating insurance contract liabilities		**529**	-

(ii) Expected non-participating insurance contract liability cash flows

As at 31 December 2021	0-5 years CA$m	5-15 years CA$m	15-25 years CA$m	Over 25 years CA$m	Total CA$m	Carrying Value CA$m
Non-participating insurance contracts liabilities	**196**	**270**	**154**	**71**	**692**	**529**
Non-participating insurance contract liabilities	**106**	**270**	**154**	**71**	**692**	**529**

Insurance contract undiscounted cash flows are based on the expected date of settlement. The weighted average discount rate applied for the carrying value is 2.49%.

11. Non-participating insurance contract liabilities (Continued)

(iii) Movement in non-participating insurance contract liabilities

	Note	Gross 2021 CA$m
As at 1 January		**-**
New liabilities in the period		**509**
Liabilities discharged in the year		**(21)**
Unwinding of discount rates		**5**
Effect of change in non-economic assumptions	12	**(5)**
Effect of change in economic assumptions	12	**16**
Other		**25**
As at 31 December		**529**
Expected to be settled within 12 months		**48**
Expected to be settled after 12 months		**481**

12. Long term insurance valuation assumptions

Non-participating business

The Company writes only non-participating business and it seeks to make prudent assumptions about its future experience based on current market conditions and recent experience. The assumptions incorporate prudent margins in excess of our best estimate assumptions to minimise the possibility of actual experience being less favourable than assumed.

Valuation rates of interest and discount rates

The valuation interest rate for the underlying annuity business is based on the internal rate of return on the portfolio of assets backing the liabilities.

For the valuation interest rate assumption, asset yields are adjusted to reflect the risk of default associated with the investments held. The Company applies a prudent c36bps per annum reduction to asset yield to allow for the risk of default for all business, overall this leads to a total default provision including additional default provision of cCA$18.8m.

The Company believes the total default allowance is prudent to cover all reasonably foreseeable circumstances.

Annuitant Mortality

Mortality assumptions are set with reference to standard tables drawn up by Club Vita Canada. These tables are based on industry wide mortality experience for pension schemes. Mortality improvement rates are based on the mortality projections model of the Continuous Mortality Investigation Bureau ('CMIB'), a subsidiary of the Institute and Faculty of Actuaries, and reflect expected improvements in longevity in the future.

The majority of internal statistical investigations are carried out at least annually to determine the extent to which the Company's experience differs from that of the industry and suggest appropriate adjustments which need to be made to derive the valuation assumptions. A prudent margin of 10% is applied to the base mortality assumption for valuation assumptions.

Expenses

The Company monitors its expense experience and carries out detailed investigations regularly to determine the expenses incurred in writing and administering the different products and classes of business. An allowance for expense inflation in the future is also made, taking account of both salary and price information. The expense assumptions also includes an appropriate allowance for prudence.

The principal assumptions are:

2021	**Canada**
(i) Rate of interest / discount rate	
Annuities in deferment	**2.49% pa**
Vested annuities	**2.49% pa**
(ii) Mortality tables	
Annuities in deferment [1]	**Vita Curves Mortality model**
Vested annuities [1]	
- Bulk purchase annuities	**Vita Curves Mortality model**

1. For vested and deferred annuities, mortality rates are assumed to reduce according to an adjusted CMI's mortality improvement model. The model reflects population experience and projects current rates of mortality improvements to a user defined Long Term Rate. The Long Term Rate has been determined using a combination of Group's internal Cause of Death model and expert judgment. With the following parameters:
- Males (Canadian): Long Term Rate of 1.5% p.a. up to age 85 tapering to 0% at 110 with a constant addition of 0.30%.
- Females (Canadian): Long Term Rate of 1.0% p.a. up to age 85 tapering to 0% at 110 with a constant addition of 0.30%.

13. Payables and other financial liabilities

	Notes	2021 CA$m
Other balances due	16	**6**
Payables and other financial liabilities		**6**
Settled within 12 months		**6**
Settled after 12 months		**-**

Fair value hierarchy

As at 31 December 2021	Total CA$m	Level 1 CA$m	Level 2 CA$m	Level 3 CA$m	Amortised cost CA$m
Other balances due [1]	**6**	**-**	**-**	**-**	**6**
Payables and other financial liabilities	**6**	**-**	**-**	**-**	**6**

1. See Note 16(i) Related party transactions.

There have been no significant transfers between levels.

14. Contingent liabilities, guarantees and indemnities

Provisions for the liabilities arising under contracts with policyholders is based on certain assumptions. The variance between actual experiences from that assumed may result in those liabilities differing from the provisions made for them. Liabilities may also arise in respect of claims relating to the interpretation of policyholder contracts, or the circumstances in which policyholders have entered into them. The extent of these liabilities is influenced by a number of factors including the actions and requirements of the regulators.

The Company has entered into various Letters of Credit Contracts (‘LOC’).

As at 31 December 2021 Issuer bank	Currency	Facility type	Facility Term[1]	Facility amount in CA$m
Citibank Europe Plc, Ireland	CAD	Committed	August 2026	53
HSBC Bank Canada	CAD	Committed	October 2025	30

1. The Facility Term includes two years extension at the discretion of the issuer bank.

The Company does not have any other contingent liabilities, guarantees or indemnities arising as part of its normal course of business.

15. Parent companies

The immediate parent company of Legal & General Reinsurance Company No.2 Limited is Legal & General Re Holdings Limited, a company incorporated in England and Wales. The ultimate holding company for both of those entities is Legal & General Group Plc. These accounts provide information about Legal & General Reinsurance Company No.2 Limited as an individual undertaking. Copies of the accounts of the ultimate holding company, Legal & General Group Plc, are available, at the Registered Office, One Coleman Street, London, EC2R 5AA, on Legal & General Group Plc website at www.legalandgeneral.com, or from the Company Secretary.

16. Related party transactions

(i) Payables and other financial liabilities

As at 31 December	2021 CA$m
Due to other related party:	
- Resources management charges due[1]	6
Total	**6**

1. The management charges due relate to expenses owed by the Company to affiliates within the group, namely Legal & General Resources Bermuda Limited ('LGRB') and Legal & General Resources Limited. These charges have accrued over the year and relate to the operation costs including employee benefits. Legal & General Resources Limited, which employs all UK staff, charges all of its costs pertaining to secondees to LGRB from the UK offices. LGRB employs Bermuda based staff and incurs all costs of operation, which is recharged to the Company.

(ii) Other charges

For the year ended 31 December	2021 CA$m
Management charges [1]	6
Finance costs	1
Total charges	**7**

1. See note under table 16(i) CA$4m of management charges are staff related costs.

(iii) Other loans

The Company entered into a loan agreement with the related party Legal & General Finance Plc amounting to CA$250m. The Company incurred CA$1m of interest for the loan and the loan balance at the end of the year was CA$Nil.

(iv) Novation agreement

On 24 August 2021, the Company entered into a Business Transfer Agreement with L&G Re, a related party. L&G Re transferred to the Company its rights and obligations, including the associated investment and collateral arrangements, related to its Canadian PRT business. At the inception of the agreement, the Company recognised CA$244m of premiums and CA$241m of non-participating insurance liability.

17. Management of capital resources

Capital management policies and objectives

The Company aims to manage its capital resources to maintain financial strength, ensure policyholder security and meet local capital requirements.

Capital measures

The Company measures its capital on a number of different bases, including those which comply with the regulatory framework within which the Company operates, and those which the Directors consider most appropriate for managing the business, this includes Bermuda Economic Balance Sheet ('EBS') regulatory capital.

Accounting bases

Management use the primary financial statements prepared on an IFRS basis to manage capital and cash flow usage and to determine dividend-paying capacity.

Bermuda statutory requirements

The Company is licensed as a long-term Class E reinsurer under the Bermuda's Insurance Act 1978. Under the Act, the Company is required to maintain a minimum capital and surplus. There are no statutory restrictions on the payment of dividends from retained earnings of the Company as the minimum statutory capital and surplus requirements are satisfied by the share capital. However, approval from the Bermuda Monetary Authority must be obtained before the statutory capital is reduced in excess of 15% of the previous year's statutory filing. In all cases, the Approved Actuary needs to provide support for any proposed dividends.

Capital resources

The financial strength of the Company is measured by reference to its Bermudian statutory accounts, which are a requirement of all Class E reinsurers. The Company's total capital resources of CA$64m comprise CA$111m of issued share capital to the ultimate parent in 2021 and CA$47m in respect of a retained loss.

These resources are in excess of the required minimum capital and solvency requirements.

17. Management of capital resources (Continued)

Available regulatory capital resource risks
The Company's capital resources are sensitive to changes in market conditions, due to both changes in the value of the assets and to the effect that changes in investment conditions may have on the value of the liabilities. Capital resources are also sensitive to assumptions and experience relating to longevity, new business strain and, to a lesser extent, expenses.

The most significant risks arise from:

- Credit risk: this materialises if the default and downgrade experience of the assets backing the liabilities exceed the reserving assumptions, and
- Longevity risk: losses occur if the mortality of annuitants was lower than the assumptions used for reserving.

18. Risk management and control

This section describes the Company's approach to risk management. It covers the overall approach that applies to all risks and includes a detailed review of risks within the Company's business.

Insurance risk
Exposure to loss arising from claims experience being different to that anticipated.

Insurance risk is implicit in the Company's insurance business and arises as a consequence of the type and volume of business written and the concentration of risk in particular policies or groups of policies subject to the same risks. Insurance risk is managed with policies for underwriting, pricing and reinsurance. The Company's insurance risk policy sets out the overall framework for the management of insurance risk. Areas where the Company is primarily exposed to insurance risk are longevity, rates of longevity improvement and mortality. Insurance risk also arises from incomplete scheme demographic data.

Pricing is based on a fixed set of assumptions, such as mortality, which consider past experience, recent trends, and expert opinion. Actual experience may vary from the pricing assumptions, leading to profits or losses. Overall, the Company seeks to be conservative in its acceptance of insurance risks by establishing strict underwriting criteria and limits.

Operational risk
Exposure to loss arising from inadequate or failed internal processes, people, systems or external events.

Potential for exposure to operational risk extends to all aspects of the business. The Company has constructed a framework of internal controls to minimise material loss from operational risk events recognising that no system of internal control can completely eliminate the risk of error, financial loss, fraudulent action or reputational damage.

Concentration risk
Exposure to loss arising from a specific geographic location or type of loss event.

As part of the ongoing risk assessment processes the Company considers the concentration of risk. The Company seeks to manage concentrations by setting limits around the maximum exposure to loss that it can tolerate from a series of related events. Limit set includes financial instruments. Insurance risk may be concentrated in geographic regions, altering the risk profile of the Company.

Market risk
Exposure to loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets.

The Company's exposure to market risk is influenced by one or more external factors, including changes to interest rates, inflation, financial instrument prices, foreign exchange rates and indices of prices or rates.

Significant areas where the Company is exposed to these risks are:
- assets backing insurance contracts;
- assets and liabilities denominated in foreign currencies; and
- other financial assets and liabilities.

The Company's market risk policy sets out the overall framework for the management of market risk. The policy is reinforced by more granular investment policies for long term and other business, which have due regard to the nature of liabilities and guarantees and other embedded options given to policyholders.

The Company is ultimately responsible for the management of market risk. The Company manages market risk using the following methods:

<u>Asset liability matching</u>
The Company manages its assets and liabilities in accordance with relevant regulatory requirements, reflecting the differing types of liabilities it has on the Company's Statement of Financial Position.

For business such as immediate annuities, which is sensitive to interest rate risk, analysis of the liabilities is undertaken to create a portfolio of securities, the value of which changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. Interest rate risk cannot be completely eliminated, due to the nature of the liabilities and early redemption options contained in the assets.

18. Risk management and control (Continued)

Market risk (Continued)

Derivatives
The Company uses derivatives to reduce the market risk arising in the funds. The most widely used derivatives are over the counter and exchange-traded swaps. The Company may also use futures and other derivatives to facilitate efficient asset allocation within the long-term funds. In addition, derivatives within the long-term fund are used to improve asset liability matching and to manage interest rate and foreign exchange risks. It is the Company's policy that amounts at risk through derivative transactions are covered by cash or corresponding assets and that swaps are collateralised as appropriate to reduce counterparty risk. Derivatives may be either be held directly on the balance sheet or in Funds Withheld or similar reinsurance collateral structures.

The most significant risks arise from:

Interest rate risk
Interest rate risk is the risk that the Company is exposed to lower returns or loss as a direct or indirect result of fluctuations in the value of, or income from, specific assets and liabilities arising from changes in underlying interest rates.

The Company is exposed to interest rate risk on the investment portfolio it maintains to meet the obligations and commitments under its insurance contracts, in that the proceeds from the assets may not be sufficient to meet the Company's obligations to policyholders.

To mitigate the risk that guarantees and commitments are not met, the Company purchases financial instruments, which broadly match the expected policy benefits payable, by their nature and term. The composition of the investment portfolio is governed by the nature of the insurance liabilities, the expected risk-adjusted rate of return and the expected impact on the capital requirement.

Asset liability matching significantly reduces the Company's exposure to interest rate risk. Sensitivity to interest rate changes is included in Table 2 of Note 18.

Currency risk
The Company operates internationally and as a result is exposed to foreign currency exchange risk arising from fluctuations in exchange rates of various currencies. The Company has exposure to currency risk from financial instruments held in currencies other than their functional currencies. The exchange risks inherent in these exposures are mitigated through the use of derivatives, for example forward currency contracts, cross currency basis swaps and futures.

The Company aims to maintain sufficient assets in local currency to meet local currency liabilities however movements may impact the value of the Company's shareholder's equity, which is expressed in CA$. This aspect of foreign exchange risk is monitored and managed, against pre-determined limits. These exposures are managed by aligning the deployment of regulatory capital by currency with the Company's regulatory capital requirements by currency. Currency borrowings and derivatives are used to manage exposures within the limits that have been set.

As at 31 December 2021, the Company held a net liability of CA$30m in US dollars. The Company mitigates exchange rate risk through the use of derivatives, mainly forward currency contracts.

The Company's management of currency risk reduces the shareholder's exposure to exchange rate fluctuations. The Company's exposure to a 10% exchange movement in the US dollar on an IFRS basis, where the values of economic hedging instruments are reflected at their carrying value as opposed to their notional amounts, is: A 10% appreciation in the US dollar to Canadian dollar period-end foreign exchange rate would have a CA$2.4m impact on shareholder equity.

Other price risk
Other price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices, other than those arising from interest rate risk or currency risk. These changes may be as a result of features of the individual instrument, its issuer, or factors affecting all similar financial instruments traded in the market.

The Company controls its exposure to geographical price risks by using internal country credit ratings. These ratings are based on macroeconomic data and key qualitative indicators. The latter take into account economic, social and political environments.

The Company does not hold any equity securities as of 31 December 2021.

Credit risk
Exposure to loss if another party fails to perform its financial obligations to the Company.

The Company's credit risk policy defines the overall framework for the management of credit risk. Credit risk exposures primarily arise in relation to corporate bonds held by the Company and those in relation to the CFWH.

The Company holds fixed and variable rate securities within the financial investments and funds withheld to back part of its insurance liabilities. Significant exposures are managed by the application and regular review of concentration limits, with allowance being made in the actuarial valuation of the insurance liabilities for possible defaults.

The credit profile of the Company's financial investments and funds withheld exposed to credit risk is shown in Table 1. The credit rating bands are provided by independent rating agencies. Credit risk bands are defined using qualitative and quantitative factors that are indicative of the risk of default and are aligned to external credit rating definitions from agencies Standard & Poor's, Moody's, and Fitch. For unrated assets, such as cash and derivatives, not exposed to credit risk, the Company maintains internal ratings, which are used to manage exposure to these counterparties.

18. Risk management and control (Continued)

Credit risk (Continued)

The carrying amount of assets included in the Statement of Financial Position represents the maximum credit exposure. No impairment provisions have been made.

Table 1 – Exposure to credit risk including funds withheld

As at 31 December 2021	AAA CA$m	AA CA$m	A CA$m	BBB CA$m	BB and below CA$m	Unrated Other CA$m	Total CA$m
Government securities	122	35	-	-	-	-	**157**
Other fixed rate securities	-	31	200	176	3	-	**410**
Total debt securities	**122**	**66**	**200**	**176**	**3**	**-**	**567**
Accrued interest	-	-	2	2	-	-	**4**
Cash and cash equivalents	19	-	9	-	-	-	**28**
Total[1]	**141**	**66**	**211**	**178**	**3**	**-**	**599**

1. Total includes the underlying assets within the funds withheld balance.

There are no impaired or past due financial assets within the portfolios in 2021.

Liquidity risk
The risk that the Company, though solvent, either does not have sufficient financial resources available to enable it to meet its obligations as they fall due, or can secure them only at excessive cost.

The Company's liquidity risk policy defines the overall framework for the management of liquidity risk. The Company does not seek exposure to liquidity risk in its own right, but recognises that exposure to liquidity risk can arise as a consequence of the markets in which it operates, the products that it writes and through the execution of investment management strategies.

The liquidity risks, to which the Company's business may be exposed, primarily stem from low probability events that if not adequately planned for, may result in unanticipated liquidity requirements.

A limited level of contingent liquidity risk is an accepted element of writing contracts of insurance. However, the Company's insurance business seeks to maintain sufficient liquid assets and standby facilities to meet a prudent estimate of the cash outflows that may arise from contingent events. The level of required liquidity to be maintained by insurance funds is identified using techniques including cash flow analysis for ranges of extreme scenarios and stress tests for shock events.

To ensure an appropriate pool of liquid assets are maintained in line with a prudent estimate of cash outflows, the profile of investment assets held to meet future liabilities from writing insurance business are structured to include an appropriate proportion of cash and other readily realisable assets. The required profile is formally defined as part of asset benchmarks provided to the investment managers, with regular management information provided by the investment manager on the actual holding relative to the fund benchmark.

Specific liquidity risks associated with the Company’s core product lines and the risk mitigation techniques are as follows:

Annuities: Potential for liquidity risk arises within two specific aspects of the Company’s annuity business (i) changes in future pension commitments and (ii) collateral requirements risk for hedging strategies.

(i) Changes in future pension commitments - once business has been written, cash outflows for pensions in payment are generally predictable, enabling the Company to structure the liquidity, income and maturity profile of investment assets backing long-term liabilities to meet projected cash outflows. Although variations in longevity can alter the duration of outflows over the long term, trends are gradual, providing opportunity to respond with appropriate risk mitigation strategies.

(ii) Collateral requirements for risk hedging strategies - as part of the investment asset management strategy for the Company's annuity business, financial instruments are utilised to manage exposure to fluctuations in interest rates and foreign currency, which may otherwise result in long term liabilities being unmatched. The use of such financial instruments can require the posting of liquid collateral with counterparties, and as such an appropriate pool of the asset types specified by counterparties must either be held or readily available.

The Company manages its banking relationships, capital raising activities, overall cash and liquidity position and the payment of dividends, with support from its ultimate holding company, Legal & General Group Plc’s treasury function. The Company seeks to manage its corporate funds and liquidity requirements on a pooled basis and to ensure the Company maintains sufficient liquid assets and standby facilities to meet a prudent estimate of its net cash outflows. In addition, it ensures that, even under adverse conditions, the Company has access to the funds necessary.

18. Risk management and control (Continued)

Sensitivity analysis
Table 2 shows the impact on pre-tax profit and equity, net of reinsurance, under each sensitivity scenario for the business.

	Impact on pre-tax profit net of reinsurance 2021 CA$m	Impact on equity net of reinsurance 2021 CA$m
Sensitivity test		
1% increase in interest rates	3	3
0.5% decrease in interest rates	(2)	(2)
Credit spread widens by 100 bps with no change in expected defaults	2	2
Annuity: +10bps in credit default assumption	(4)	(4)
Annuity: -10bps in credit default assumption	4	4
1% decrease in annuitant mortality	(1)	(1)
1% Increase in Annuitant Mortality	1	1

- In calculating the alternative values, all other assumptions are left unchanged. In practice, items of the Company's experience may be correlated.
- The Company seeks to actively manage its asset and liability position. A change in market conditions may lead to changes in the asset allocation or charging structure, which may have a more, or less, significant impact on the value of the liabilities. The analysis also ignores any second order effects of the assumption change, including the potential impact on the Company asset and liability position.
- The sensitivity of the profit to changes in assumptions may not be linear. They should not be extrapolated to changes of a much larger order.
- The change in interest rate test assumes a 100/-50 basis point change in the gross redemption yield on fixed interest securities together with a 100/-50 basis point change in the real yields on variable securities. Valuation interest rates are assumed to move in line with market yields.
- In the sensitivity for credit spreads, corporate bond yields have increased by 100bps and there has been no adjustment to the default assumptions.
- The inflation stress adopted is a 0.5% pa increase in inflation resulting in a 0.5% pa reduction in real yield and no change to the nominal yield. In addition, the expense inflation rate is increased by 0.5% pa.
- The annuitant mortality stress is a 1% reduction (proportional) in the mortality rates for immediate and deferred annuitants with no change to the mortality improvement rates (so for example, if the base table multiplier was 95%, this would become 94.05% (95% * 99%) under this stress).

The sensitivity analyses do not take into account management actions that could be taken to reduce the impacts. The Company seeks to actively manage its asset and liability position. A change in market conditions may lead to changes in the asset allocation or charging structure, which may have a more, or less, significant impact on the value of the liabilities. The analysis also ignores any second order effects of the assumption change, including the potential impact on the Company asset and liability position. In calculating the alternative values, all other assumptions are left unchanged, though in practice, items may be correlated. The sensitivity of the profit to changes in assumptions may not be linear. They should not be extrapolated to changes of a much larger order.

Climate change
The Company is exposed to climate change through two broad categories:

- Transition risks from the move to a low-carbon economy and the impact this has on asset valuation and the economy; and
- Physical risks from the impact on asset holdings as a result of severe weather events and longer-term shifts in climate.

Climate change impacts will emerge through risks that we are already exposed to, with the key existing risk exposures covered by the economic and non-economic sensitivities shown in this section. In addition, given the uncertain nature of the risks from climate change, and the lack of historical data to support decision making, a specific scenario testing approach over a longer term time horizon has been developed by the Group to manage the risks from climate change.