Changed accounting policy 2016

The Danish Executive Order on Financial Statements for insurance companies and pension funds has been adapted to the new EU solvency rules, Solvency II from 2016. The new rules took effect on 1 January 2016.

Solvency II sets down the basic principles for calculation of insurance provisions:

- Best estimate of the present value of expected future cash flows for underwritten insurance contracts
- A risk margin to cover the risk of deviation between best estimate and final execution of future cash flows
- An interest rate curve laid down for Solvency II. Topdanmark uses the volatility adjusted interest rate curve.

Solvency II incorporates the expected profit in the capital base at the time when the insurance contracts have been underwritten.

In accounting terms, the expected profit on underwritten insurance contracts must be incorporated in the balance sheet in a separate provision item, profit margin, which is taken to profit and loss over the period of cover of the insurance contracts.

Most significant elements in calculation of insurance provisions due to implementation of Solvency II at Topdanmark:

Non-life insurance

Premium provisions

Premium provisions are calculated at present value of best estimate of expected payments of future insurance events, covered by underwritten insurance contracts. At Topdanmark, insurance contracts are primarily written on an annual basis.

Expected payments comprise compensation and expenses on claims handling and administration. Furthermore, unpaid acquisition costs (primarily writing and portfolio commission) as well as bonuses and rebates.

The expected payments are calculated at present value discounted by the volatility-adjusted interest curve.

Best estimate of undue premiums for underwritten insurance contracts is deducted from premium provisions.

Changes in provisions due to changes in the interest rate curve and unwinding until the expected time of payment are transferred to the item Return and value adjustment for non-life insurance provisions.

Profit margin

Profit margin is the expected profit of the remaining period of cover for underwritten insurance contracts.

Profit margin is calculated as the difference between premiums for future periods of cover for insurance contracts underwritten, and the expected payments included in the premium provisions.

The expected payments are calculated at present value, discounted by the volatility-adjusted interest rate curve.

Changes in present value of the expected payments due to changes in the interest rate curve and unwinding of the profit margin over the period of cover of the insurance contracts are transferred to the line Return and value adjustment for non-life insurance provisions.

The share of the risk margin attributed to settlement of premium provisions is offset in the profit margin.

In case the expected present value of future payments for a portfolio of insurance contracts with uniform risks is expected to exceed the premium, the profit margin for this portfolio will be set at zero.

Risk margin

Risk margin is the amount a company would have to pay any acquirer of an insurance portfolio for taking over the risk that the actual payments in connection with settlement of insurance provisions deviate from best estimate.

At Topdanmark Forsikring, the risk margin is calculated using the Solvency II model Cost of Capital. A model developed in-house stressing biometric risks, is used for illness/accident insurance administered by Topdanmark Livsforsikring.

Previously, risk margin has not been a separate provision item in the financial statement.

Life insurance

Life insurance provisions

The life insurance provisions are calculated as the present value of the expected cash flow for policies written using best estimate of all relevant parameters such as life expectancy and frequency of disability. As previously, the life insurance provisions include a risk margin reflecting what an independent acquirer of the insurance portfolio would demand to take on the risk of fluctuations in the expected payments. Accordingly, the life insurance provisions are divided into guaranteed benefits, risk margin and individual and collective bonus potential.

Innovatively, the guaranteed benefits are valued at best estimate of the frequencies of surrenders and termination of payment of premium, while the risk margin is calculated as the increase of the guaranteed benefits by stressing the biometric risks.

As a consequence of the recognition of estimates of the frequencies for surrenders and termination of payment of premium in the guaranteed benefits, the individual bonus potential is no longer split up into bonus potential on future premiums and bonus potential on paid-up benefits.

Forward-looking, the collective bonus potential will be included in the life insurance provisions, but otherwise continue to act as an equalisation of the individual years' payments of bonus in accordance with the contribution rules reported to the DFSA.

Profit margin

The profit margin is the expected future profit for the Company on the contracts concluded, and it is financed, as far as possible, by the individual bonus potential and secondarily by the collective bonus potential. The value is calculated as an interest margin in accordance with the going concern principle, in which the recognised profit on the future premiums complies with the contract limits of Solvency II.

Accounting effect

The effect on the Group's result for Q1 2015 and the year 2015, plus the Group capital appear from the table below:

Result and equity	Result		Equity		
DKKm	Q1 2015	2015	2014	Q1 2015	2015
Result and equity according to financial statement	310	1,132	5,135	5,055	4,673
Adjustments					
Claims provisions					
Best estimate	0	0	266	266	266
New interst rate curve	4	51	82	86	133
Reinsurance share	(1)	(1)	(1)	(2)	(2)
Risk margin	(30)	7	(320)	(350)	(313)
Premium/profit margin	(2)	6	(55)	(56)	(49)
Others	(3)	3	(4)	(7)	(2)
Pre-tax effect	(32)	66	(32)	(63)	34
Tax	7	(14)	7	14	(7)
Effect of adjustments, post-tax	(25)	51	(25)	(49)	26
Result and equity, new accounting policy	286	1,183	5,111	5,006	4,699

Due to the changed accounting policies, the Group post-tax result for 2015 was uprated by DKK 51m, from DKK 1,132m to 1,183m.

Group equity post-tax end of 2015 was uprated by DKK 26m from DKK 4.673m to DKK 4.699m.

Add to this, a DKK 3m uprate of life insurance provisions, included in the 2016 opening balance, not included in the comparative figures, since it has not been possible to prepare comparative figures for life insurance.

The accounting effect on the key elements of the income statement for Q1 2015 and the year 2015 appears from the table below:

Effect of new accounting policy

Accounts Q1 2015

DKKm	Technical result non-life	Technical result life	Invest-ment-return	Trans-ferred return	Pension return tax	Unwinding and value-adjustment non-life	Other items	Pre-tax profit	Tax	Profit
Accounts Q1 2015	216	(7)	2,428	(1,881)	(353)		(8)	395	(84)	310
Effect of changes in accounting policy										
Unwinding premium provisions	6					(6)				
Unwinding profit margin	1					(1)				
Change strengthening of premium provisions	8					(7)		1	(0)	1
Change in unwinding claims provisions	4					(4)				
Change in risk margin	(28)					(5)		(33)	7	(25)
Change in measurement claims provision on own account(new interest rate curve)						3		3	(1)	2
Change in measurement derivatives (new interest rate curve)	(3)							(3)	1	(2)
Effect of changes in format requirements										
Line item "Technical interest" deleted	2			25		(27)				
Value adjustments technical provisions non-life transferred to new line item			257			(257)				
New line item "Pension return tax" in technical result		0		(353)	353					
Total effect of changes	(9)	0	257	(328)	353	(305)		(32)	7	(25)
Accounts Q1 2015, new policy	207	(7)	2,685	(2,209)	0	(305)	(8)	363	(77)	286

DKKm	Technical result non-life	Technical result life	Invest-ment-return	Trans-ferred return	Pension return tax	Unwinding and value-adjustment non-life	Other items	Pre-tax profit	Tax	Profit
Accounts 2015	1,169	19	1,616	(1,135)	(165)		(22)	1,481	(349)	1,132
Effect of changes in accounting policy										
Unwinding premium provisions	22					(22)				
Unwinding profit margin	5					(5)				
Change strengthening of premium provisions	(7)					7				
Change in unwinding claims provisions	23					(23)				
Change in risk margin	14					(1)		13	(3)	10
Change in measurement claims provision on own account(new interest rate curve)						50		50	(11)	39
Change in measurement derivatives (new interest rate curve)	3							3	(1)	2
Effect of changes in format requirements										
Line item "Technical interest" deleted	2			106		(108)				
Value adjustments technical provisions non-life transferred to new line item			(195)			195				
New line item "Pension return tax" in technical result		0		(165)	165					
Total effect of changes	62	0	(195)	(59)	165	93		66	(14)	51
Accounts Q1 2015, new policy	1,231	19	1,421	(1,194)	0	93	(22)	1,547	(364)	1,183

Non-life insurance

The accounting effect on the technical result for non-life insurance for Q1 2015 and the year 2015 appears from the following table:

Non-life insurance Technical result DKKM	Premiums earned	Technical interest	Claims incurred	Net re-insurance	Expenses	Technical result
Accounts Q1 2015	2,242	(2)	(1,629)	(28)	(367)	216
Eliminated profit owner-occupied properties			(3)		(5)	(9)
Segment non-life Q1 2015 (basis for ratios)	2,242	(2)	(1,632)	(28)	(372)	207
Unwinding premium provisions	7			(0)		6
Unwinding profit margin	2			(0)		1
Change strengthening of premium provisions	8					8
Line item "Technical interest" deleted		2				2
Change in unwinding claims provisions			4			4
Change in measurement derivatives (new interest rate curve)			(3)			(3)
Change in risk margin claims provisions			(28)			(28)
Segment non-life new accounting policy	2,258	0	(1,659)	(29)	(372)	198
Eliminated profit owner-occupied properties			(3)		(5)	(9)
Accounts Q1 2015, new policy	2,258	0	(1,655)	(29)	(367)	207
Accounts 2015	8,956	(2)	(6,210)	(171)	(1,404)	1,169
Eliminated profit owner-occupied properties			(14)		(22)	(36)
Segment non-life 2015 (basis for ratios)	8,956	(2)	(6,224)	(171)	(1,426)	1,133
Unwinding premium provisions	24			(2)		22
Unwinding profit margin	5			(0)		5
Change strengthening of premium provisions	(7)					(7)
Line item "Technical interest" deleted		2				2
Change in unwinding claims provisions			23			23
Change in measurement derivatives (new interest rate curve)			3			3
Change in risk margin claims provisions			14			14
Segment non-life new accounting policy	8,977	0	(6,183)	(173)	(1,426)	1,195
Eliminated profit owner-occupied properties			(14)		(22)	(36)
Accounts 2015, new policy	8,977	0	(6,169)	(173)	(1,404)	1,231

Combined ratio

Combined ratio for Q1 2015 and the year 2015 is adjusted as follows:

Combined ratio	Q1 2015		Full year 2015	
	Accounts	New policy	Accounts	New policy
Gross loss ratio	72.8	73.5	69.5	68.9
Net reinsurance ratio	1.3	1.3	1.9	1.9
Claims trend	74.1	74.7	71.4	70.8
Gross expense ratio	16.6	16.5	15.9	15.9
Combined ratio	90.7	91.2	87.3	86.7
Combined ratio excl. run-off profits	92.7	93.3	91.6	90.9

The key figure statement follows previous practice, with the following elements added as separate items in the income statement:

Change in profit margin and risk margin is included in gross premium income.
Change in risk margin is included in claims expenses.

Operating ratio

Since technical interest, net of reinsurance is omitted; combined ratio and operating ratio are identical. Consequently, operating ratio is only presented in future, when required in accordance with the Danish Executive Order on Financial Statements.

Life insurance

The following changes are made in the technical result for life insurance for Q1 2015 and the year 2015:

Technical result life											
			Pension		Change in provisions						
		Investment	return	Bene-			Unit-		Expen-	Reinsur-	Technical
DKKm	Premiums	income	tax	fits	Claims	Life	linked	Bonus	ses	ance	result
Accounts Q1 2015	1,617	1,856	0	(784)	(17)	(623)	(1,771)	(181)	(107)	2	(7)
Change in format requirements											
New line item "Pension return tax" in technical result		353	(353)								0
Change in claims provision to change in life provisions					17	(17)					0
Bonus to change in life provisions						(181)		181			0
Change in provisions for unit-link to change in life provisions						(1,771)	1,771				0
Accounts Q1 2015, new policy	1,617	2,209	(353)	(784)	0	(2,592)	0	0	(107)	2	(7)
Accoounts 2015	6,320	1,029	0	(3,240)	20	810	(4,471)	(39)	(406)	(3)	19
Change in format requirements											
New line item "Pension return tax" in technical result		165	(165)								0
Change in claims provision to change in life provisions					(20)	20					0
Bonus to change in life provisions						(39)		39			0
Change in provisions for unit-link to change in life provisions						(4,471)	4,471				0
Accounts 2015, new policy	6,320	1,194	(165)	(3,240)	0	(3,680)	0	0	(406)	(3)	19

"Change in profitmargin" will in 2016 be transferred from change in life provision to a separate line item

New rules for handling the shadow account have been implemented. As a result, the balance of the shadow account at the end of 2015 must be booked or written down over the next five financial years.

Insurance provisions for life insurance are uprated by DKK 3m from the end of to 2016. The change is included in the opening balance for 2016, since it has not been possible to prepare new comparative figures for the year 2015 and previous years.