

**Shepherds
Friendly**

Your modern mutual



The Shepherds Friendly Society Limited

Report of the Board and Financial Statements

www.shepherdsfriendly.co.uk

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The Shepherds Friendly Society Limited

Board:

Joanne Hindle	Chairman
Nemone Wynn-Evans	Non-Executive Director and Senior Independent Director
Geoffrey Ross	Non-Executive Director
Barry Bibby	Non-Executive Director (Resigned January 2016)
Simon Pashby	Non-Executive Director (Appointed July 2016)
Roger Turner	Non-Executive Director (Appointed July 2016)
Ann-Marie O'Dea	Chief Executive Officer
Kim Harris	Executive Director
Justine Morrissey	Executive Director

Company Secretary:

Tim Robertson

Registered Office:

Haw Bank House, High Street
Cheadle, Cheshire SK8 1AL

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Email: info@shepherdsfriendly.co.uk

Website: www.shepherdsfriendly.co.uk

Actuarial Function Holder and With Profits Actuary:

Christopher Critchlow BSc FIA of OAC plc

External Auditors:

Moore Stephens
Chartered Accountants, Registered Auditors

Internal Auditors:

Gateway Assure Ltd

Bankers:

The Royal Bank of Scotland Plc

Investment Managers:

Vestra Wealth LLP
Legal and General Investment
Management Ltd

Property Managers:

Matthews and Goodman, Manchester

Authorised and Regulated by the Prudential Regulation Authority and the Financial Conduct Authority - Registration number 109997. Incorporated under the Friendly Societies Act 1992 - number 240F.

Your Board



Joanne Hindle - Chairman

Joanne joined the financial services industry in 1986 and has held a variety of roles. These include being Pensions Development Director for NatWest Life, Corporate Services Director for UNUM and Chair of the trade body ILAG. Joanne currently works as head of legal for part of the AXA Group as well as chairing the Board of the Holmesdale Building Society.



Nemone Wynn-Evans - Non-Executive Director (Senior Independent Director)

Nemone has 20 years' executive and non-executive experience in the financial services sector, across wholesale and retail, including as a former Finance Director on the main board of a stock exchange. Currently she is Chief Operating Officer at a Multi-Family Office providing investment management services, as well as a non-executive director of the commercial arm of a university, and she has recently been appointed as a non-executive director of a regional building society. Nemone is also the Society's Senior Independent Director (SID).



Ann-Marie O'Dea - Chief Executive Director

Ann-Marie brought to the Society a wealth of marketing experience gained from over 20 years in the industry. She has held senior positions in various advertising and marketing agencies working on accounts such as Royal Bank of Scotland, Yorkshire Bank, Parcelforce and the N Brown Group. Since joining she has held several Board roles; Marketing Director and also Managing Director of the Society's subsidiary Financial Advice Network. She was appointed CEO in January 2015.



Kim Harris - Executive Director

Kim has a long history with the Society, initially as a Non-executive Director and most recently as MD of the Society. In his role he carries accountability for the overall strategic and operational direction of the Society. Prior to joining the Shepherds Friendly full time, Kim had a successful career in the building society sector as well as being the owner of a financial services recruitment company.



Justine Morrissey - Executive Director

Justine has worked all her career as an actuary in the life assurance industry. The last 15 years has been in the Friendly Society sector in a variety of roles from product development to regulatory reporting. She joined the Society in 2012 and is the Finance and Risk Director. A prime focus within her role is ensuring the adherence to the Solvency II regulations for the Society.



Geoffrey Ross - Non-Executive Director

Geoffrey spent his entire career as an actuary in the life assurance industry holding Chief Actuary and Finance Director roles in a number of insurance companies/ friendly societies. He set up his own consultancy practice on retiring from the Phoenix Group in 2006 acting as With Profits Actuary for a number of companies in that Group. Currently he is With Profits Actuary of Reliance Mutual.



Simon Pashby - Non-Executive Director

Simon Pashby is a Chartered Accountant with over 30 years' experience working in financial services, 15 years as an audit partner with KPMG. He has experience of advising a wide range of organisations in financial services on risk, regulations and controls. Simon retired from KPMG in 2012 and now works as an independent non-executive director, and maintains his current knowledge as a Fellow of the Institute of Chartered Accountants. He is Vice-Chairman of the Medical Protection Society, a Members' mutual fund which provides indemnity services to the medical profession, where he chairs the Audit and Risk Committee, and is a non-executive director of the Scottish Building Society, where he chairs the Operational Risk Committee.



Roger Turner - Non-Executive Director

Roger Turner has extensive experience in financial services; having been a trader in fixed income and derivatives, a regulator and a consultant with PwC where he was a Partner within the Financial Services Regulatory Practice. He has worked predominantly in the UK but undertaken numerous assignments for overseas organisations most notably in the Far East and the USA. Roger is the CEO of an asset manager in London and a Non-Executive Director of a Building Society in Wales where he is also Chairman of the Remuneration Committee. He holds a B.A. (Hons.) in Business Studies and an M.B.A. in Finance from the City University Business School.

The Strategic Report

Including the Chairman's Statement

Strategic Report

The purpose of the Strategic Report is to provide Members of the Society with information that will enable them to assess how the directors have performed their duties in the interests of the Members. The strategic report reflects the collective view of the Society's Board of Management and includes the Viability Statement.

Information in the report complements the financial statements, enabling the annual report to be a more cohesive document. It provides information about the business and its development, performance or position that is not reported in the financial statements but which is relevant to the Members' evaluation of past results and assessment of future prospects.

This information is provided below under the sub-headings of Chairman's Report, Chief Executive's Business Review and Viability Statement.

Chairman's Report

With the implementation of the European Union's Solvency II Directive, 2016 saw a year of significant change for the United Kingdom insurance industry, with the sector operating under a new prudential regulatory regime.

The Solvency II Directive has led to the implementation by the UK Regulators of a new approach to the approval and control of those responsible for running financial service businesses. This, in our case, is known as the Senior Insurance Managers' Regime (SIMR). The fundamental difference to what has gone before is that Senior Managers and other key function holders will be subject to personal regulatory or legal punishment, should they be found guilty of knowingly behaving irresponsibly in managing the business. All Board Members were successfully transferred into the Senior Insurance Managers' regime.

All of the Society's Board of Management now comply with a defined set of conduct standards, and I am pleased to report that two new Board Members were recruited in 2016 to ensure that the allocation of all the necessary responsibilities has been achieved.

In my last report I reported that following on from threats to global recovery identified in 2015, investment markets would in 2016 continue to have a turbulent year. Market Risk is a material risk the Society faces, and indeed 2016 has been a year of both extraordinary and tragic events. In addition to the two main 'shocks' i.e. the UK vote to leave the EU, and Donald Trump winning the US Presidential election, we have seen:-

- in February, stock markets around the world falling sharply;
- terrorist attacks in France and Germany, which highlighted the continued danger from Islamic extremists;
- in Italy, the oldest bank in the world being rescued by a state bail out, and a failed referendum on political reform;
- concerns at the beginning of 2016 on the slowing Chinese economy;
- falling commodity prices, and fears of a global recession; and
- sterling weakening by 20% in the year.

Despite all the market shocks in 2016, we saw at year end stock markets around the globe at close to new highs, with commodity stocks performing strongly. The FTSE100 ended at 7142.83, compared with 6242.32 at the end of 2015, an increase of 14%.

However, as we look out into 2017, politics looks as if it will continue to dominate. BREXIT negotiations, the forthcoming UK election, European elections in France, Norway and Germany, and a new US President are all likely to complicate the outlook, and we should be prepared for more volatility in the months to come.

Performance

At the end of 2016, the Society's funds under management stood at £77.0m (2015: £74.3m). The Shepherd's long term insurance fund is invested across a range of asset classes. The fund as a whole achieved a return of 9.5% (excluding CTF funds).

The Society's Child Trust Fund is invested on a unit linked basis in a Legal & General managed FTSE 100 Tracker Fund and in 2016 achieved a return of 15.75%.

The Society has continued to make good progress over the past twelve months, and continues to be financially strong. Therefore, it gives me great pleasure to confirm that this has meant that we have been able to award Members an annual bonus for the fourteenth consecutive year.

Investment Policy

One of the key areas of focus for 2016 has been on Market Risk, and whether our current investment policies were aligned with our risk appetite and insurance liabilities. To allow for greater focus there has been a change within the Society's governance framework with the formation of an Investment Committee.

As part of our investment objectives, we have considered how our portfolios are invested, ensuring we try and obtain returns sufficient to enable the Society to meet Members expectations by maintaining bonuses at competitive rates.

Strategy

The Society's Board meets twice a year to review the medium to long-term strategy of the business. Strategy is always set within the context of the Society's Risk Appetite Statement and this in turn is regularly reviewed as part of the continuous process to operate our business within the framework provided by our Own Risk Solvency Assessment (ORSA).

The ORSA is a forward-looking assessment of how we operate the Society in the best interests of its Members. It is a document required to be given to our Regulators by the European Solvency II Directive. As such the content of this Strategic Report will always be a reflection of the content of the Society's ORSA.

Another material risk the Society faces is New Business Risk, and I am pleased to confirm that in 2016 new business increased to a record 6,717 plans (2015: 3,911) and allowances generated from these plans, together with income from investments exceeded the amount required to cover operating expenses by 37%. Allowances being the value released from premiums written to cover all the operating expenses of the Society plus profit.

In terms of generating and preserving value for our Members it is essential that the Society manage the material risks it faces successfully.

So far my report has touched on two of the most material risks the Society faces - Market Risk and New Business Risk. The other material risks the Society faces are identified as insurance risk, business continuity risk and reputational damage risk. These risks are discussed fully later in this Strategic Report.

Also later in this Strategic Report we make a viability statement, and in there we comment on the impact made by implementation of Solvency II.

Since day one, the Society has acted in the best interest of its Members in everything we do, because we belong to them. As we celebrate 190 years since the formation of Shepherds Friendly, this remains the case. Mutuality remains the basis upon which the Society operates and we have a strict set of values that we believe help us to provide our Members with the best products and services we can offer.

In deriving a set of values that form the basis of our society, we listened to the people who matter the most - our members and our staff. These being:-

- To remain mutual acting at all times in our members interests
- To provide products that our members value
- To provide an individual experience for every member

- To be a place where people want to work
- To ask, listen and respond
- To remain focussed on evolving our technology to meet the changing needs of our members

Finally I would like to thank the executive team, senior management and staff for their dedication to our Members throughout 2016, and for their hard work which has been a critical factor in what has been a very successful year.



J Hindle Chairman

Senior Independent Director - Nemone Wynn-Evans

Role of the Senior Independent Director

In publicly listed companies, the role of a Senior Independent Director is to be a voice of the shareholders and to ensure their interests are fully understood by the Board.

At Shepherds Friendly, our members are our owners of the Society, and we seek to place them at the heart of everything we do. Nemone's role is to ensure that this happens, and also to act as a channel of communication for any member who believes they have a problem which cannot be resolved through the usual channels.

Complaints

The Society has in place clearly documented procedures for the handling and recording of complaints. The Compliance Officer investigates all complaints thoroughly and impartially within a reasonable time. A Member who feels dissatisfied with the result of such investigation has the right to raise the matter with our Senior Independent Director and can refer the complaint to the Financial Ombudsman Service.

Chief Executive's Report and 2016 Business Review

It is with great pleasure that for another year running I can report the successes the Society is achieving. Given a backdrop of an even more challenging year than that we faced in 2015, it demonstrates the strength and depth of the Society and its committed employees.

To achieve continued success we realise that we have to constantly adapt our products and distribution strategies, while at the same time ensuring that we interact with our Members and business partners in ways that meet their needs and demands. Such a strategy has led to a remarkable year in terms of new business growth and retention of existing Members.

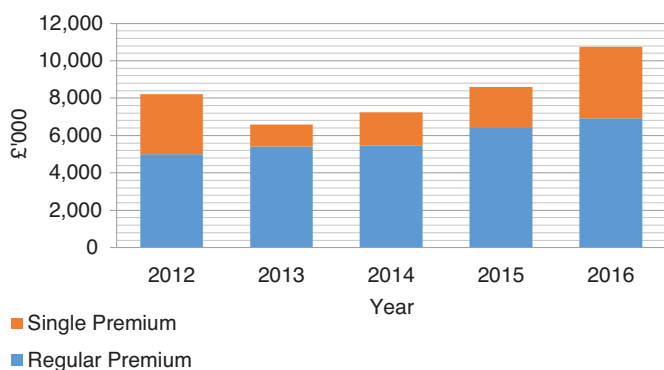
The end of 2015 saw the Society fully re-launch its Income Protection plan, with sales increasing dramatically in 2016. New distribution routes were identified for the Over 50's plan and the affiliate network developed as a route to market for with-profits plans.

All of this activity culminated in the number of new business plans being in excess of 6,700, an increase of 72% over 2015. New annual premium equivalent was 80% higher than 2015 and enabled us to generate sufficient allowances to exceed operational costs comfortably with a total operational surplus 37% higher than budget. The number of members increased to 86,918 (2015: 83,912).

2016 Business Highlights

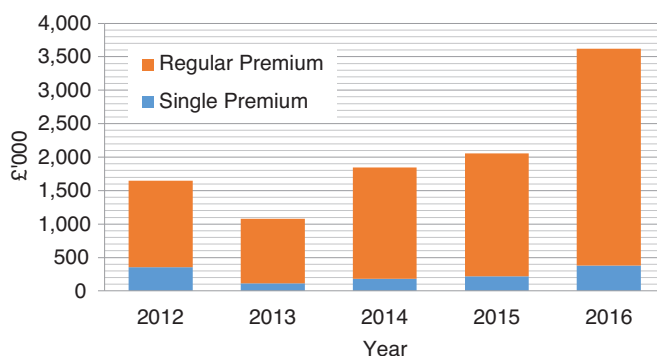
The results for 2016 are set out in detail on pages 27 to 40 and the highlights are as follows:-

Gross Premium Income



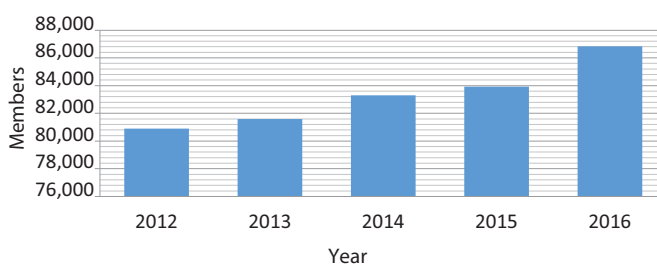
Gross premium income is the total income generated by the Society through both regular and single premiums, new business and additional contributions. Gross long term insurance premium income has increased in 2016 to £10.7m (2015: £8.6m).

Annualised New Business written



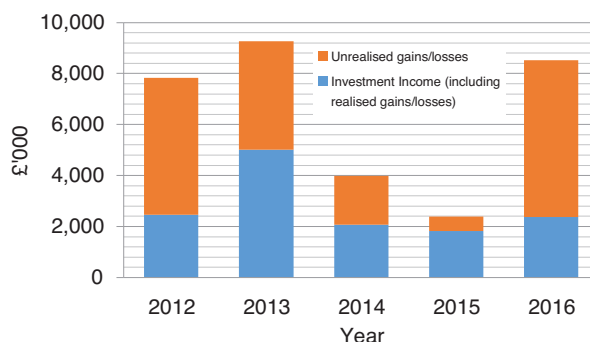
New Business written on an Annual Premium Equivalent (APE) basis increased in 2016 to £3.6m (2015: £2m).

Individual Membership



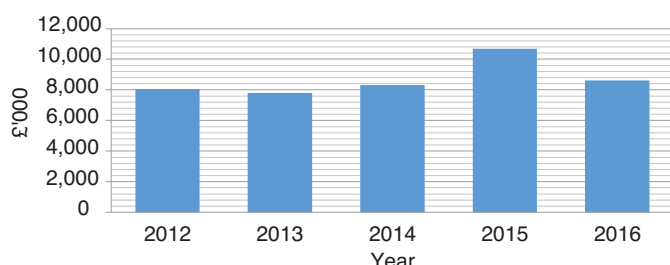
The size of the membership base is an indication of the scale of the Society. As at 31st December 2016, the Society had 86,918 members, which is an increase of 2,919 (+3.5%) (2015: 83,912).

Investment Income



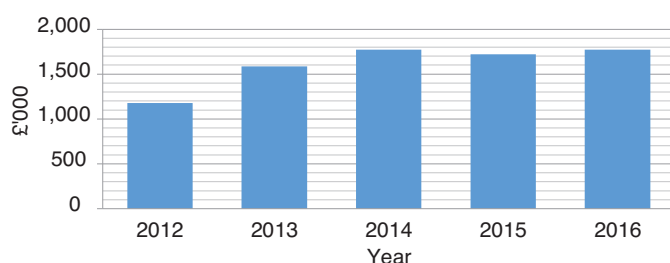
The Society's investment portfolio produced good returns for 2012. The total investment return (including unrealised gains and losses) for 2016 stood at £8.5m (2015: £2.4m).

Claims in Payment



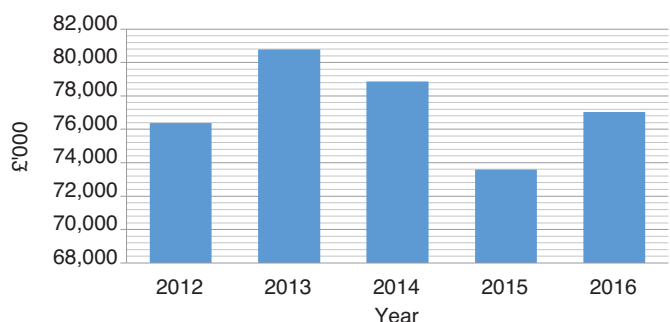
Total claim payments in 2016 were £8.6m (2015: £10.7m)

Society Administration Expenses



Expenses are managed through the setting of budgets within the business planning process and a regular review and challenge process throughout the year. Society administration expenses for 2016 were £1.8m (2015: £1.7m).

Total Assets



At the end of 2016 the Society held total assets of £77.5m (2015: £73.7m). Investments held include a mixture of equities, fixed interest stocks, property and cash. Other assets include debtors, prepayments and accrued income.

In undertaking our business we continue to put our Members at the heart of everything we do, ensuring at each member touch point with the Society that the highest levels of conduct risk are evidenced. Our conduct risk framework enables us to measure our performance. For example we have initiated a 'nursery care' programme for new members. The programme's objective is to assess whether the material used in the sales process was clear and transparent, and how the members' service team dealt with queries. A telling question asked is, 'would they recommend the Society to a family member or friend'. The results from all activities have been very positive with 92% of responders saying they would recommend the Society and an overall satisfaction score of 4.6 out of 5 for the member's service team.

As I mentioned earlier the challenges we faced in achieving such a successful year were considerable, perhaps none more so than those faced in achieving the required regulatory changes. They have been demanding in terms of management time and costs to the Society, with the work surrounding the implementation of SIMR as mentioned in the Chairman's report one of the major projects undertaken. As we look forward I do not see either being reduced. A major project that was due for completion in 2016 was that concerning the PRIIPS (Packaged Retail and Insurance based Investment Product) regulation and the provision of Key Information Documentation, which will be required for all the Society's investment products. This has now been delayed, with the work required to be completed alongside the production of an RSR (Regular Supervisory Report) and an SFCR (Solvency and Financial Condition Report which are major new initiatives of Solvency 11 in 2017).

The Board in 2017 agreed their statement of strategic intent; it recognises that our ability to remain in business does hinge largely upon our ability to sell sufficient new business and therefore this has been identified as the most significant risk faced by the Society. The statement clearly articulates this:-

"To continue to write increasing volumes of profitable new business; this will mitigate our biggest risk and fulfil member expectation by meeting their plans' objectives".

New business risk and other material risks identified are briefly discussed in the Directors Report and Viability Statement overleaf.

A M O'Dea Chief Executive Officer

Director's Report and Viability Statement

Directors Report

The Board of Management in the strategy work they do, and in production of the ORSA, assess on a forward looking basis the prospects for the Society. They do this on a three-year projection having considered the material risks the Society is known to face and, having done their best to identify them, risks which may emerge in the future. Stress tests are then applied to the projections which assume worse than expected events occur.

The following are the material risks the Board have identified as facing the Society -

New Business Risk

This is a high risk faced by the Society. It is the risk of not being able to sell enough new business to generate allowances which enable us to meet operational costs on an on-going basis. Steady growth in new business volumes is essential to build sufficient capital strength to continue in business and deliver the expectations held by policyholders. We mitigate this risk by offering a varied range of products in both investment and protection markets using both With-Profit and Non-Profit plans. We also use a variety of routes to market, which when allied to a varied product range, means we are not over dependent on any one product or route to market and can better weather falls in demand when they occur.

New business volumes are constantly monitored. The Executive compare the volumes to its yearly budget targets and decide if any of the actions mentioned above require amending.

Market Risk

this is a medium risk faced by the Society. Market Risk is the risk that arises from fluctuations in capital values of, or income from, invested assets, or in interest or exchange rates applicable to those assets. Market movements e.g. falling values, have an impact on solvency as it affects the capital resources of the Society. This also affects policyholders through the bonus levels that can be paid annually and the final maturity value of their policies.

At an operational management action level market risk is monitored by keeping track of the 28 day average value of the FTSE 100 index. Final bonuses could be changed if the average value is above the higher trigger point or below the lower trigger. If the lower level figure continued, a decision would then be taken as to the point annual bonuses should also be changed. Such trigger points are set by the Board in conjunction with the Chief Actuary.

There are further management actions, agreed by the Board with the Society's actuary, to monitor the market values of investments. There are defined "trigger points" at which management actions will be taken to defend solvency by reducing volatile investments, and replacing them with assets which may better maintain their capital value.

Insurance Risk

This is a medium risk faced by the Society. Insurance Life Risk is the risk from losses on life insurance business caused by mortality, lapses and expenses being worse than expected.

On a forward looking basis we are not unduly concerned by the threat of a sudden worsening in the level of mortality claims. The Society has a very small historic book of pure term insurance policies and there is re-insurance behind those policies. This type of business is no longer written. The other death benefits are on policies, such as tax exempt Friendly Society with-profits savings plans and the Over 50's whole of life policies, where the sums insured per policyholder are relatively small.

Insurance Health Risk covers the potential losses from income protection insurance business. This covers morbidity, lapses and expenses being worse than expected. This risk needs to be carefully monitored and controlled as it is potentially more volatile than mortality risk. We have experienced a worse than expected claims level on a specific book of income protection business. This book of business is small in numbers of policy and is subject to strong on-going management. The Society ceased writing this book of business in 2014.

Business Continuity

This is a low risk faced by the Society. The Society has a range of management actions to ensure it does not suffer a prolonged interruption to its ability to trade. A business continuity and disaster recovery plan are in place and tested regularly. There are two main ways a prolonged business interruption could occur and these are, a loss of premises to operate from, and a loss of Information technology systems and the data contained within them.

The Society occupies rented premises, and therefore loss of the premises would not be a financial loss to the firm. The business is situated within Greater Manchester where there is a considerable amount of unlet office space, and finding new premises in a short time frame is entirely feasible.

The information technology systems are operated on a “cloud” basis supported by a well-established and major provider of out-sourced information technology solutions. Data and systems capability can be delivered from two independent centres. In 2016 the IT infrastructure has been reviewed in line with FCA guidance in this area.

The Society relies on third parties for many parts of its operation from system support to its investment management. If its investment managers suffered a catastrophic failure this would have huge ramifications for its ability to continue to operate. There are controls in place for this relationship to reduce this risk to an acceptable level i.e. custodian arrangement in place.

The Society looks to keep policies, processes and procedures up to date to ensure the operational impact of any change to the business is kept to a minimum.

Wherever possible the firm utilises insurance as a further mitigation to lessen any financial loss arising from operational risks.

Reputational Damage

This is a low risk faced by the Society. This risk is managed and mitigated within the firm by the operation of a Conduct Risk Framework, overseen by the Board with its independent non -executive directors.

The Society has strong controls to ensure its zero appetite for this risk is achieved. Staff are trained on IT security, fraud protection, anti-money laundering and data protection. The cultural values are included in job descriptions and the appraisal process works in tandem with this.

Customer behaviour is analysed to ensure anything that might be an issue can be identified as early as possible for all products and all of the different ways they are sold.

An emerging risk that has been identified that could cause reputational damage is that caused by a Cyber attack.

The Society takes known and generally practised steps to prevent its systems and data being accessed by third parties, whether malevolent or not. A greater level of protection is achieved by using the services of a major data centre provider than maintaining the data on in house servers.

In addition, the Society maintains an independent copy of its data, stored on a hard drive and kept entirely separate from that stored in the two independent data centres provided by the out-sourced service provider. This would enable a re-start to be achieved on new systems if the firm was being held to ransom in terms of accessing its existing systems and data.

A final mitigation is provided by an insurance policy to cover the risk of financial loss as a result of cyber-attack.

Viability Statement

From the projections carried out in conjunction with the Chief Actuary, the Board is satisfied that the Society should remain viable on a forward-looking 3-year basis. The Board believes that 3 years is the longest forward looking projection it can make as beyond that any assumptions would increasingly be pure guesswork. The Society measures its future solvency by reference to a Capital Resources Ratio (CRR) which is defined as assets less liabilities, expressed as a percentage of the capital requirements as currently calculated by the regulatory Individual Capital Assessment (ICA).

The Board has decided that the solvency range of the Society will be contained within a range of 150% to 250% of capital required. When the CRR globally, or for individual risks, is on a path which would breach the lower of these tolerances then management actions will be taken to contain solvency within the range. Similarly, if the material risks are mitigated successfully, no new material risks emerge and the 3-year business plan targets are achieved the then CRR figure would increase steadily.

The Society has a ten-year history of increasing its business volumes and successfully managing its assets. The directors have no reason to believe this cannot be maintained and on this basis the Board is pleased to confirm that the Society is currently viable and is expected to remain so over the coming years and will be able to meet its liabilities as they fall due.

Corporate Governance Review

The Board

The Board meets a minimum of six times a year to conduct the normal business of the Society and in addition meets to discuss the future strategy of the business. 2016 was an especially busy year due to implementation of both the European Solvency II Directive from 1st January 2016 and the Senior Insurance Managers Regime. Accordingly, there were extra Board meetings in 2016 with a total of eight held.

Direction of the day-to-day management of the Society is delegated to the Executive Directors who operate within defined authority limits.

Board Meeting Attendance

The table below shows attendance at the Board and at the sub-committees -

Name	AGM	Board Meetings	With Profits	Audit	Risk	Investment	Nominations	Remuneration
Joanne Hindle - Chairman and NED	1/1	8/8	-	-	-	-	5/5	6/6
Nemone Wynn-Evans - NED	1/1	8/8	-	-	4/4	2/2	5/5	6/6
Geoff Ross - NED	1/1	7/8	4/4	5/5	-	2/2	-	-
Simon Pashby NED (appointed July 2016)	-	3/3	2/2	2/2	-	-	1/1	-
Roger Turner NED (appointed July 2016)	-	3/3	-	-	2/2	2/2	-	3/3
Ann-Marie O'Dea - CEO	1/1	8/8	-	-	-	2/2	-	-
Kim Harris - Executive Director	1/1	7/8	4/4	-	-	-	-	-
Justine Morrissey - Executive Director	1/1	8/8	-	-	4/4	-	-	-
Tim Robertson - Company Secretary	1/1	8/8	-	-	-	2/2	-	-

Financial Responsibilities of the Board Directors

Friendly Society law and the Rules of the Society require the Board of Management to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Society and its subsidiary as at the end of each financial year and the income and expenditure of the Society and its subsidiary for that period. In preparing these financial statements the Board is required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements, and,
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Society will continue in business.

The Board is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Society and its subsidiary and for ensuring that the Society and its subsidiary establishes and maintains systems of control of its business and records and of inspection and report in accordance with the Friendly Societies Act 1992.

It is also responsible for establishing satisfactory systems of control of the Society's business and records, and of inspection and report, to enable the Board and the Society to comply with the Friendly Societies Act 1992 and other financial services legislation, both European and United Kingdom.

The Board of Management has a general responsibility for taking such steps as are reasonably open to it to safeguard the assets of the Society and to prevent and detect fraud and other irregularities.

The directors confirm that they have complied with the above requirements.

The Role of the Board is to operate effectively and assume responsibility for the success of the Society, and the Directors must be able to demonstrate the measures undertaken to achieve this. In doing so, they have the following collective and personal responsibilities.

Collective Responsibilities of the Board Directors

All Directors share responsibility for:

- Maintaining an understanding of the views of the membership and acting in their best interests
- Setting the Society's mission and customer focussed values
- Setting the strategy of the Society and any subsidiary company
- Approving corporate plans to achieve the strategy
- Approving and monitoring budgets necessary to achieve the strategy
- Monitoring the Society's and any subsidiary companies' performance in relation to agreed annual plans, budgets and objectives and thereby assessing the performance of the Executive Directors
- Approving key decisions in respect of all significant counterparty relationships and all significant new business ventures
- Establishing, maintaining and reviewing the Society's system of internal financial, management and operational systems and controls (including risk management)
- Approving the Society's annual financial statements and presenting a balanced and understandable assessment of both the Society's current position and its forecast position in the Board's annual report
- Ensuring that the affairs of the Society and any subsidiary company are conducted solvently, lawfully and in accordance with the Annotated Combined Governance Code and the rules of the regulator
- Establishing and overseeing the framework of delegation to the Chief Executive and delivering to her supportive and entrepreneurial leadership
- To ratify and agree the decisions of the Board Committees
- To monitor composition and performance of the Board/Committees and to conduct succession planning on a continuous basis
- To agree appointments to the Board of people who are fit, proper and competent for the roles and to set appropriate remuneration levels for them.

Personal Responsibilities of Board Directors

Each Director accepts a personal responsibility to:

- Maintain an understanding of the views of the membership
- Support the mission and values of the Society
- Support the regulator's Principles
- Support all Society policies
- Work effectively with other Directors
- Be a member of one or more Committees of the Board, when required
- Contribute to the decisions of any Committee of which they are a member, from their skills and experience, and share the responsibilities for all their decisions
- Attend at least 75% of all Board meetings in a rolling 24-month period to which they are invited, having previously read all relevant papers
- Not to be absent from two consecutive Board meetings other than for reasons of serious ill health
- Attend any training sessions provided for Directors
- Register any interest that may have a bearing on the Society's work and declare any potential or actual conflicts of interest as and when they arise
- Represent the Society positively to all external audiences
- Maintain constructive relationships with Society staff
- Directors may be called on to contribute from their specific skills by liaison informally with any appropriate member of staff
- Undertake a formal evaluation process of the Board's performance.

The directors confirm that they have complied with the above responsibilities.

In addition to the Board of Management which has over-arching responsibility for management of the Society a number of Board Sub-committees operate to provide detailed governance of a range of issues. The work of these committees is described overleaf.

Committee Reports

Nominations Committee

The purpose of the committee is to ensure that nominations to the Board and other senior positions are appropriately managed and in the interest of Members and customers.

Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Joanne Hindle - (Committee Chairman and non-executive director)

Nemone Wynn-Evans - (non-executive director)

Simon Pashby - (non-executive director)

Supported by -

Nasrin Hossain - (invited senior management attendee)

During the year the Committee met five times. There was full member attendance at all meetings. As a result of its work the Committee is able to confirm the following -

- The Chairman meets the definition of an Independent Director contained in the Combined Code, an annotated version for Mutual Insurers;
- There is a clear division of responsibilities between the roles of Chairman and Chief Executive and they are conducted by different individuals. The respective roles are documented in the Board Manual;
- The Board has maintained a sound balance of different skill sets amongst its non-executive directors;
- All non-executive directors meet the definitions of independent directors;
- The non-executive directors have other business interests and all have been assessed as not giving rise to conflicts of interest. It has also been established that they have sufficient time availability to fulfil their Shepherd's Friendly roles properly;
- The Society is successfully fulfilling its diversity policy and has comfortably exceeded its target of at least 25% female directors;
- A Board Effectiveness Appraisal process, based on peer group assessment, was carried out. Immediately after every Board meeting all Directors independently assess the effectiveness of the meeting. The data is analysed and reported back at the next Board meeting by the Chairman of the Nominations Committee along with any proposed improvement actions;
- Once a year a 360-degree personal assessment of all Board Directors is conducted on a peer group basis. The Society employs a professionally qualified HR Manager who plays a key role in analysing and presenting the outcomes which are then fed-back to individuals and form the basis for identifying what knowledge or skills gaps may exist and determines how they will be overcome by planned CPD activities;

- Each Sub Committee assessed performance against their objectives and reported the results for assessment to the whole Board;
- In 2016 the Board used the services of Lintstock Ltd to carry out an independent Board assessment. The outcome of the assessment was highly positive with Board composition, expertise and dynamics all being rated highly overall. (Lintstock had no other connection with the Society);
- In respect of the appointment of non-executive directors (and executive director positions which cannot be filled by internal promotion) the Society recruits on an open market basis;
- As part of the Board's awareness of succession planning, and the need to refresh itself, the Society recruited two new non-executive directors in 2016. One was appointed on an open market basis, and one appointed using the services of Fletcher-Jones Executives Search Ltd. (Fletcher-Jones had no other connection with the Society).

Remuneration Committee

The purpose of the committee is to take responsibility for ensuring that Remuneration matters are appropriately managed and in the interests of Members and customers.

Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Nemone Wynn-Evans - (Committee Chairman and non-executive director)

Joanne Hindle - (non-executive director)

Roger Turner - (non-executive director)

Supported by -

Nasrin Hossain - (invited senior management attendee)

During the year the Committee met six times. There was full member attendance at all meetings. As a result of its work the Committee is able to confirm the following -

- The Committee was satisfied that the remuneration package for executive directors is set at an appropriate level to attract and motivate directors of the right calibre without paying more than is necessary. Independent sources are used to benchmark the executive's level of pay;
- No director is responsible for setting their own remuneration.
- The remuneration level for non - executive directors is set at a level which reflects the time commitment and responsibility of the role. There is no remuneration for Non-executive directors related to performance related measures;
- The percentage level of executive director's pay which is linked to financial and sales performance targets has been reduced as the committee recommended that this better reflects financial services regulatory guidance on remuneration and incentive packages;
- All directors have notice periods that do not exceed one year.

Audit Committee

The purpose of the Committee is to assist the Board and the subsidiary company Board in exercising their responsibilities for compliance with statutory requirements and the integrity of the annual report and accounts. The Audit Committee provides a forum for independent oversight of the Audit matters for the Society and any of its subsidiary companies to ensure the interests of Members and customers are always considered.

Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Geoff Ross - (Chairman and non-executive director)

Simon Pashby - (non-executive director)

Supported by -

Ann Marie O'Dea - (invited executive director attendee)

Justine Morrissey - (invited executive director attendee)

Tim Robertson - (invited senior management attendee)

In addition to the above, representatives from Moore Stephens the External Auditor and Gateway Assure the Internal Auditor, attended meetings by invitation.

During the year the Committee met five times. As a result of its work the Committee is able to confirm the following -

- The membership of the Committee consisted wholly of independent non-executive directors;
- The Committee was satisfied with the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements. The external auditors do not provide other consultancy service to the organisation thereby preserving their independence as auditors;
- By meeting with the external auditors to assess the conduct of the audit the Committee is able to understand any matters raised by the auditors which need improvement actions to be taken. The 2016 review of the Auditors Management Letter with the auditors raised no material concerns;
- The Auditors Management Letter confirmed that there were no significant issues to be considered in relation to the financial statements;
- The Committee recommended to the Board that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for Members to assess the company's performance;

- The Committee is responsible for periodically assessing whether the external auditor's performance is fully satisfactory and whether there should be a re-tendering exercise. In 2016, the Committee were satisfied from conversations with the audit firm, and from the effectiveness of the audit process itself, that the external auditors performed to the required standard. Therefore, at the AGM the Board nominated the auditors to continue in their role;
- The Committee was responsible for reviewing and managing the relationship with the Internal Auditors. In 2016, the Committee were satisfied that the performance of Gateway Assure was deemed satisfactory;
- All of the reports from the internal auditors in 2016 were satisfactory, and no material shortcomings were identified;
- The Committee received the annual report from the Society's Money Laundering Reporting Officer and confirm there were no material concerns raised;
- The Committee also confirms that there were no whistle blowing incidents in the Society.

Risk Committee

The purpose of the committee is to assist and advise the Board in exercising its responsibilities for all aspects of the current and future risk strategy including the determination of risk appetite and tolerance, risk measurement, management and mitigation procedures throughout the Society.

Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Nemone Wynn-Evans - (Chairman and non-executive director)

Roger Turner - (non-executive director)

Graeme Charters - (external expert advisor)

Justine Morrissey - (executive director)

Supported by -

Ann Marie O'Dea - (invited executive director attendee)

Tim Robertson - (invited senior management attendee)

Sam Chivers - (invited senior management attendee)

During the year the Committee met four times. As a result of its work the Committee is able to confirm the following -

- The Committee provided oversight and advice to the Board in relation to current and potential future risk exposures, as well as on the principles and practice of the Society's current and future risk policy, risk measurement and management, including determination of risk appetite and tolerance within the capital constraints of the Society;

- The Committee played a leading role in ensuring the Society develops a sound risk culture where staff throughout the organisation understand the importance of recognising risks and have an embedded risk culture;
- During the year the Committee played a leading role in the production of the 2016 version of the Society's Own Risk and Solvency Assessment (ORSA);
- The Committee continues to monitor the Society's processes to identify, assess, manage and mitigate risks. The Committee looks primarily at the most significant risks facing the businesses, but maintains awareness of all risks by accessing the computerised Risk Database.

With Profits Committee

The purpose of the committee is to advise the Board on the exercise of discretion in the financial management of the Society's business and to support the Board in discharging its corporate governance responsibilities in relation to compliance with the Society's Principles and Practices of Financial Management.

Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Geoffrey Ross - (Chairman and non-executive director)

Simon Pashby - (non-executive director)

Kim Harris - (executive director)

Supported by -

Tim Robertson - (Company Secretary)

Christopher Critchlow - (Chief Actuary and With Profits Actuary)

During the year the Committee met 4 times. As a result of its work the Committee is able to confirm the following -

- There has been independent challenge to the With Profit Actuary's recommendations to ensure that the interests of with-profit policyholders are properly taken into account.
- The Committee is satisfied that the Society has operated in accordance with its Principles and Practices of Financial Management and has made recommendations to the Board which are appropriate.
- Reviews of various activities and events in the context of the regulator's Conduct of Business Rules confirmed that the Society is operating appropriately within the Rules.
- The Committee is satisfied that it has properly advised the Board on the exercise of discretion in the financial management of the business.
- Discretion has been exercised in the management of With-Profit policyholder funds which has resulted in fair treatment of With-Profits policyholders.

Investment Committee

2016 saw the formation of the Investment Committee (IC). The Committee is authorised by the Board, in conjunction with Chief Actuary, to recommend to the Board the investment strategy, including asset allocation, for the Society. The Committee will make asset allocation decisions in line with agreed policy and strategy. The policy and strategy are to be reviewed and approved by the Board on an annual basis. Its full Terms of Reference are published on the Society's website.

Committee Members (31st December 2016)

Geoffrey Ross - (Chairman and non-executive director)

Roger Turner - (non-executive director)

Nemone Wynn-Evans - (non-executive director)

Ann-Marie O'Dea - (executive director)

Tim Robertson - (Company Secretary)

Supported by -

Joanne Hindle - (invited non-executive director attendee)

Following its formation on the 1st August, the IC met twice in 2016. As a result of its work the Committee is able to confirm the following -

- The Committee has worked with the Executive to support effective communication on investment matters between the Actuary of the Society, the Board, the IC and the Investment managers;
- An appropriate strategic asset allocation for the Society's business was considered and compared to the actual investments held, policyholder expectations, risk appetite and desired spread of risk. Recommendations for adjusting the asset allocations were discussed and approved by the Board;
- The Committee have reviewed the performance of the Investment Managers, including performance compared with agreed benchmarks, and compliance with investment objectives and mandates.

Report on compliance with the UK Corporate Governance Code - An Annotated Version for Mutual Insurers

The UK Corporate Governance Code (the Code) requires firms to comply with 26 main principles. The Board confirmed that with the exception of the following, the Society had complied with the Code for 2016:-

Are the terms and conditions of appointment of non-executive Directors made available for inspection by any person at the Society's registered office during normal business hours and at the AGM (for 15 minutes prior to the meeting and during the meeting)?

- Terms and conditions of appointment are available for inspection but have not historically been provided at the AGM.

Report of the Independent Auditor

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SHEPHERDS FRIENDLY SOCIETY LIMITED

We have audited the consolidated financial statements of The Shepherds Friendly Society Limited for the year ended 31 December 2016 which comprise the Group and Society Income and Expenditure Accounts, the Group and Society Balance sheets and the related notes 1 to 17. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 and 103 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'.

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

Respective responsibilities of the Board of Management and auditor

As explained more fully in the Board of Management's Responsibilities Statement set out on page 15, the Board of Management is responsible for preparing consolidated financial statements which give a true and fair view. Our responsibility is to audit and express an opinion on the consolidated financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Boards (APB's) Ethical Standards for Auditors.

Our assessment of risks of material misstatement

We identified the following risks that we believe to have had the greatest impact on our audit strategy and scope:

- the operation and effectiveness of the Society's Member's system during the year and specifically the operation of the system over premium income and claims paid to Members;
- the valuation and ownership of the Society's investments at the year end and the recording of transactions throughout the year;
- the Society's compliance with applicable regulations;
- the recoverability of balances owed to the Society by its subsidiary;
- the Application of revenue recognition accounting;
- the risk of fraud arising from management override of internal controls: and the calculation, methodology and assumptions behind the technical provision.

Our application of materiality

We apply the concept of materiality both in planning and performing our audit, and in evaluating the effect of misstatements on our audit and on the consolidated financial statements. For the purpose of determining whether the consolidated financial statements are free from material misstatement we define materiality as the magnitude of misstatement that makes it probable that the economic decisions of a reasonably knowledgeable person, relying on the consolidated financial statements, would be changed or influenced.

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the consolidated financial statements. We determined materiality for the Society to be £200,000 for items impacting the Income and Expenditure account, which is approximately 1.5% of income. We determined materiality of £1,150,000 for items which require reclassification on the balance sheet, which is approximately 1.5% of gross assets.

We agreed with the Audit & Risk Committee that we would report to the Committee all audit differences in excess of £1,000, as well as differences below that threshold that in our view warranted reporting on qualitative grounds.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the consolidated financial statements sufficient to give reasonable assurance that the consolidated financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Society's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Board of Management; and the overall presentation of the consolidated financial statements. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited consolidated financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

The way in which we formed our response to the risks identified above was as follows:

- In order to address risk around the operation of the Society's Member's system during the year we have tested the operation of the controls over membership records, premium income and claims paid to Members.
- In order to address risk around ownership of the Society's investments held at the period end, we confirmed the holdings to independent third party confirmations provided by the Society's Custodian.
- In order to address the risk around the valuation of the Society's investment we obtained from independent third parties confirmations of the prices for the purpose of subscription or redemption of interest in the underlying investments in investee funds as at 31 December 2016 and vouched these on a sample basis.
- In order to address the risk associated with the recording of investment transactions through the year ended 31 December 2016 we have tested a sample of transactions to independent documentation.
- In order to address the risk over the Society's compliance with it regulatory environment we updated our understanding of the regulatory requirements and reviewed the Society's correspondence with its regulators and statutory filings.
- As part of our testing of the member's system we performed testing relating to controls over the recognition of premium income and the process for the ensuring the accuracy of changes to member's records, including new Members. We also performed substantive testing on a sample of premium income and analytical procedures to validate whether revenue recognition procedures complied with UK Generally Accepted Accounting Practice.
- In order to address the risk relating to management override of controls we have reviewed all significant or unusual entries to ensure they are appropriate and reasonable. We have also reviewed key estimates and judgements for bias.
- In order to address the risk in relation to the technical provision we engaged with a suitably qualified third party reviewing actuary to review and challenge the methodology, assumptions and calculations in relation to the technical provision. We have reviewed and tested the data process system and the controls within it. We checked the process and controls around the experience investigations. We examined the method used to determine best estimate and the cost of risk capital margin and checked that the method used is in line with Solvency II.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view, in accordance with UK Generally Accepted Accounting Practice of the state of the Group's and the Society's affairs as at 31 December 2016 and of the income and expenditure of the Group and Society for the year then ended; and
- have been properly prepared in accordance with the Friendly Societies Act 1992.

Opinion on other matters prescribed by the Friendly Societies Act 1992

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

Opinion on corporate governance statement

In accordance with our instructions from the Society we review whether the Corporate Governance Statement reflects the Society's compliance with the ten provisions of the Annotated UK Corporate Governance Code specified by the Association of Financial Mutuals. We have nothing to report in respect of this review.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the ISAs (UK and Ireland), we are required to report to you if, in our opinion, information in the annual report is:

- materially inconsistent with the information in the audited financial statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- otherwise misleading.

In particular, we are required to consider whether we have identified any inconsistencies between our knowledge acquired during the audit and the Board of Management's statement that they consider the annual report is fair, balanced and understandable and whether the annual report appropriately discloses those matters that we communicated to the audit committee which we consider should have been disclosed.

Under the Friendly Societies Act 1992, we are required to report to you if, in our opinion:

- proper accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations and access to documents that we require for our audit.

M P Burnett
Senior Statutory Auditor
For and on behalf of Moore Stephens
Chartered Accountants & Statutory Auditor
31st March 2015

Society Statement Of Comprehensive Income for the year ended 31 December 2016

INCOME	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Technical account - Long term business					
Earned premiums					
Gross premiums written	5	10,749,918		8,590,558	
Outward reinsurance premiums		<u>(4,551)</u>		<u>(5,539)</u>	
Net premiums			10,745,367		8,585,019
Investment income					
Land and buildings		239,040		200,073	
Other investments		1,266,338		1,383,551	
Gains/Losses on the realisation of investments		<u>876,456</u>		<u>262,141</u>	
			2,381,834		1,845,765
Unrealised gains/losses on investments			6,144,420		564,706
Total technical income			<u>19,271,621</u>		<u>10,995,490</u>

EXPENDITURE	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Claims incurred					
Claims paid - gross amount		8,587,979		10,641,292	
Change in the provision for claims		<u>22,516</u>		<u>54,489</u>	
			8,610,495		10,695,781
Changes in other technical provisions					
Technical provisions transfer	13		1,426,559		(5,158,272)
Other expenditure					
Net operating expenses					
Other operating expenses	6	6,943,233		5,057,884	
Investment expenses		<u>41,564</u>		<u>22,106</u>	
			6,984,797		5,079,990
Actuarial (gain)/loss on pension scheme	17		548,000		(411,000)
Transfer: Fund for Future Appropriations			<u>1,701,770</u>		<u>788,991</u>
Total technical expenditure			<u>19,271,621</u>		<u>10,995,490</u>
Balance on technical account - long term business			-		-

The attached notes form part of these accounts. All income and expenditure relates to continuing operations of the Society. There were no recognised gains and losses in 2016 or 2015 other than those shown in the accounts.

Group Statement of Comprehensive Income for year ended 31 December 2016

INCOME	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Technical account - long term business					
Earned premiums					
Gross premiums written	5	10,749,918		8,590,558	
Outward reinsurance premiums		<u>(4,551)</u>		<u>(5,539)</u>	
Net Premiums			10,745,367		8,585,019
Investment income					
Land and buildings		239,040		200,073	
Other investments		1,255,667		1,363,547	
Gains/losses on the realisation of investments		<u>876,456</u>		<u>262,141</u>	
			2,371,163		1,825,761
Unrealised gains/losses on investments			6,144,420		564,706
Other technical income	1		343,025		1,377,607
Total technical income			<u>19,603,975</u>		<u>12,353,093</u>

EXPENDITURE	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Claims incurred					
Claims paid - gross amount		8,587,979		10,641,292	
Change in the provision for claims		<u>22,516</u>		<u>54,489</u>	
			8,610,495		10,695,781
Changes in other technical provisions					
Technical provisions transfer	13		1,426,559		(5,158,272)
Other expenditure / Net operating costs					
Other operating expenses	6	6,818,214		4,259,972	
Investment expenses		<u>41,564</u>		<u>22,104</u>	
			6,859,778		4,282,076
Other technical charges	1		417,258		2,078,558
Actuarial (gain)/loss on pension scheme	17		548,000		(411,000)
Transfer: Fund for Future Appropriations	13		1,741,885		865,950
Total technical expenditure			<u>19,603,975</u>		<u>12,353,093</u>
Balance on technical account					
- long term business			<u>-</u>		<u>-</u>

The attached notes form part of these accounts. All income and expenditure relates to continuing operations of the Society. There were no recognised gains and losses in 2016 or 2015 other than those shown in the accounts.

Society Statement of Financial Position as at 31 December 2016

ASSETS	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Investments					
Land and buildings	11	1,800,000		1,510,000	
Other financial investments	11	<u>74,013,282</u>		<u>71,602,654</u>	
			75,813,282		73,112,654
Debtors					
Debtors arising out of direct insurance operations with members		83		66,970	
Other debtors		<u>172,342</u>		<u>0</u>	
			172,425		66,970
Other assets					
Tangible assets	14	136,443		140,323	
Intangible assets	14	206,853		250,503	
Cash at bank and in hand		<u>791,386</u>		-	
			1,134,682		390,826
Prepayments and accrued income					
Other prepayments and accrued income		<u>371,508</u>		<u>403,405</u>	
Total prepayments and accrued income			371,508		403,405
Total assets excluding pensions asset			<u>77,491,897</u>		<u>73,973,855</u>
Pension scheme surplus/liability	17		-		26,000
Total Assets			<u>77,491,897</u>		<u>73,999,855</u>


LIABILITIES	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Fund for future appropriations		<u>20,332,318</u>	20,332,318	<u>18,630,548</u>	18,630,548
Technical provisions					
Technical provisions	13	55,582,233		54,155,674	
Claims outstanding		<u>242,062</u>	55,824,295	<u>219,546</u>	54,375,220
Provisions for other risks and charges					
Creditors					
Creditors arising from direct insurance operations		61,693		13,034	
Other creditors, including taxation & social security		<u>399,253</u>	460,946	<u>549,412</u>	562,446
Accruals and deferred income			432,338		274,856
Cash at bank and in hand			-		156,785
Pension scheme asset / liability	17		442,000		-
Total Liabilities excluding pension liability			<u>77,491,897</u>		<u>73,999,855</u>

The attached notes form part of these accounts

Approved by the Board on 9th May 2017



J Hindle Chairman



A M O'Dea Chief Executive Officer

Group Statement of Financial Position as at 31 December 2016

ASSETS	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Investments					
Land and buildings	11	1,800,000		1,510,000	
Other financial investments	11	<u>73,513,282</u>		<u>71,102,654</u>	
			75,313,282		72,612,654
Debtors					
Debtors arising out of direct insurance operations with members		83		66,970	
Other debtors	12	<u>190,641</u>		<u>11,347</u>	
			190,724		78,317
Other assets					
Tangible assets	14	136,712		141,319	
Intangible assets	14	312,497		393,263	
Cash at bank and in hand		<u>1,099,108</u>		-	
			1,548,317		534,582
Prepayments and accrued income					
Other prepayments and accrued income		<u>415,482</u>		<u>419,503</u>	
Total prepayments and accrued income			415,482		419,503
Total assets excluding pensions asset			<u>77,467,805</u>		<u>73,645,056</u>
Pension scheme surplus/liability	17		-		26,000
Total Assets			<u>77,467,805</u>		<u>73,671,056</u>

LIABILITIES	Notes	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Fund for future appropriations	13	<u>20,271,441</u>	20,271,441	<u>18,529,556</u>	18,529,556
Technical provisions					
Technical provisions	13	55,582,233		54,155,674	
Claims outstanding		<u>242,062</u>	55,824,295	<u>219,546</u>	54,375,220
Provisions for other risks and charges					
Creditors					
Creditors arising from direct insurance operations		61,693		13,034	
Other creditors, including taxation and social security		<u>436,038</u>	497,731	<u>393,761</u>	406,795
Accruals and deferred income			432,338		274,856
Cash at bank and in hand			-		84,629
Pension scheme asset / liability	17		442,000		-
Total Liabilities excluding pension liability			<u>77,467,805</u>		<u>73,671,056</u>

The attached notes form part of these accounts

Approved by the Board on 9th May 2017



J Hindle Chairman



A M O'Dea Director

Notes to the Financial Statements

For the year ended 31 December 2016

1 Significant Accounting Policies

Basis of Preparation

The financial statements have been prepared in accordance with Financial Reporting Standard 102 and Financial Reporting Standard 103 as issued by the Financial Reporting Council and the Friendly Societies (Accounts and Related Provisions) Regulations 1994 ('the Regulations'). As a mutual Friendly Society, under FRS102, the Society is exempt from the requirement to prepare a Statement of Cash Flow.

In accordance with FRS 103 on Insurance contracts, the Society has applied existing accounting practices for insurance for insurance contracts, modified as appropriate to comply applicable standards.

Following the introduction of Solvency II regulatory reporting requirements applicable from 1 January 2016, the Society changed its accounting policy for the basis of accounting for technical provisions. In accordance with UK Gaap, comparative numbers have been restated to apply the same valuation basis. Details of the change and effect of restatement are shown in note 13.

The financial statements have been prepared on the historical cost basis, except for the revaluation of certain properties and financial instruments.

The preparation of financial statements in conformity with FRS 102 requires the use of certain critical accounting estimates. It also requires the management to exercise its judgement in the process of applying the accounting policies selected for use by the Society. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 2. Use of available information and application of judgement are inherent in the formation of estimates. Actual outcomes in the future could differ from such estimates.

After making enquiries, the directors have a reasonable expectation that the Society has adequate resources to continue in operational existence for the foreseeable future. The Society therefore continues to adopt the going concern basis in preparing its financial statements.

Basis of Consolidation

The Group Accounts comprise the assets, liabilities, and income and expenditure account transactions of the Society and its subsidiary. The on-going results of the subsidiary are included with Other Technical Income and Other Technical Charges. The net results are included in the Fund for Future Appropriations for the Group. The activities of the Society and Group are accounted for in the Statement of Comprehensive Income.

Accounting for Net Earned Premiums

Regular premiums on long-term insurance and participating investment contracts are recognised as income when due for payment. For single premium business, recognition occurs on the date from which the policy is effective. Reinsurance premiums payable are accounted from when due for payment.

Accounting for Investment Income

Investment Income includes dividends, interest, rents and realised gains and losses on investments. They are all included on an accruals basis except for the realised gains and losses, which are included as the difference between the net sale proceeds and the original cost of purchase. Unrealised gains and losses are calculated as the difference between the valuation of the investments at the Statement of Financial Position date and the valuation at the last Statement of Financial Position date.

Accounting for Claims and Benefits

Maturity claims and regular annuity payments are accounted for when due for payment. Surrenders are accounted for on the earlier of the date when paid or when the policy ceases to be included within the long-term business provision.

Death claims and claims for sickness are accounted for when the Society is notified. The value of claims on participating contracts includes bonuses paid or payable. Claims values include related internal and external claims handling costs. Reinsurance recoveries are accounted for in the same period as the related claim.

The estimated cost of claims includes expenses to be incurred in settling claims and a deduction for expected value of recoveries. However it is likely that the final outcome will prove to be different from the original liability established.

Provisions are adjusted at the Statement of Financial Position date to represent an estimate of the expected outcome.

Accounting for Long Term Insurance Liabilities

The Technical provision is determined by the Board on the advice of the Chief Actuary as part of the annual actuarial valuation of the Society's long-term business. The provision is initially determined in accordance with the requirements of the Prudential Sourcebook for Insurers. In accordance with normal insurance practice, certain reserves required for statutory valuation returns are not required to be included in these accounts that are designed to present a true and fair view. This makes sufficient provision for future expenses of fulfilling the long-term contracts and includes a provision for existing reversionary bonuses and current reversionary bonuses declared as a result of the valuation. Future reversionary bonuses are implicitly provided for by use of valuation rates

of interest below those expected. No provision is made for terminal bonuses, which can be varied at any time depending on investment conditions. These liabilities are calculated using historic Society experience and include reserves for claims which have occurred but not reported, a reserve for unexpired risks and a reserve for claims already in payment.

Tangible and Intangible Fixed Assets

Tangible and Intangible assets are capitalised and depreciated/amortised by equal annual instalments over their estimated useful life. The principal rates used for this purpose are as follows:

- Equipment is depreciated between two and ten years
- Intangible Assets are amortised over five to ten years
- Property Improvements associated with rental leases are amortised over the length of the lease.

Accounting for Investment Property

Investment property, which is property held to earn rentals and/or capital appreciation, is stated at its fair value at the reporting date. Gains or losses arising from changes in the fair value of the investment property are included in profit or loss for the period in which they arise.

An external independent valuer, having appropriate recognised professional qualifications and current experience of the location and type of property being valued, values the Society's investment property every 3-5 years. Fair values are based on market values. Market values are the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing.

Where current prices cannot be established by reference to an active market, valuations are prepared by considering the aggregate of the estimated net cash flows to be received from renting the property. A yield that recognises the specific risks inherent in the net cash flows is then applied to the net annual rental cash flows to determine the value.

Accounting for Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, balances with banks, uncleared cheques, and investments in money market instruments which are readily convertible, being those with original maturities of three months or less.

Accounting for Leases

Rentals payable on operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Tax Attributable to Long Term Business

Taxes are provided for at the current rates in respect of the taxable element in the Society's business. As a registered Friendly Society, the Society is only subject to tax on part of its life and endowment business.

Other Technical Income and Technical Charges

Other technical income and charges in the Group refers to income and expenditure incurred by the subsidiary.

Foreign Currencies

Transactions in Foreign Currencies are recorded at the average rate for each month. Assets and liabilities held in foreign currencies are translated at the rate ruling at the balance sheet date. All differences are recognised in the technical account.

Pensions

The Society operates a defined contribution scheme for the majority of employees. Employer's contributions are based on a fixed percentage of basic salary charged to the technical account.

A defined benefit scheme is also in operation, although now closed to new entrants. The pension scheme surplus or liability recognised in the balance sheet is the value of the scheme's assets less the present value of the scheme's liabilities. The liabilities are valued on an actuarial basis using the Projected Unit Method, requiring estimates of future cash-flows to be made, discounting them to present value using the discount rate based on AA rated corporate bonds. The overall expected return assumption is calculated as the weighted average of the individual expected return assumptions for each of the major asset classes.

Accounting for the Fund for Future Appropriations

The Fund of Future Appropriations represents the excess of assets over and above the long-term insurance contract liabilities and other liabilities. It represents amounts that have yet to be formally declared as bonuses for the participating contract policyholders together with the free assets of the Society. Any profit or loss for the year arising through the Statement of Comprehensive Income is transferred to or from the Unallocated divisible surplus.

2 Critical Accounting Judgements and Estimates

In preparing the financial statements, management is required to make estimates and assumptions which affect reported income, expenses, assets, liabilities and disclosure of contingent assets and liabilities. Use of available information and application of judgement are inherent in the formation of estimates, together with past experience and expectations of future events that are believed to be reasonable under the circumstances. Actual results in the future could differ from such estimates.

Fair Value of Financial Assets

Market observable inputs are used wherever possible. In the absence of an active market, estimation of fair values is achieved using valuation techniques such as recent arm's length transaction, discounted cash flow analysis and option pricing models. For discounted cash flow analysis, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics. This valuation will also take into account the marketability of the assets being valued.

Technical provisions

The valuation of participating contract liabilities is based upon assumptions reflecting the best estimate at the time.

A separate calculation is also performed to assess the non-participating value of in-force business which is based on best estimate assumptions allowing for a margin of risk and adverse deviation. All contracts are subject to a liability adequacy test, which reflects management's best current estimate of future cash flows.

The assumptions used for mortality, morbidity and longevity are based on standard industry or reinsurers' tables, adjusted where appropriate to reflect the Society's own experience. The assumptions used for expenses, lapse and surrender rates are based on product characteristics and relevant claims experience.

The assumptions used for discount rates are based on current EIOPA specific risk-free rates, adjusted for the Society's own risk exposure. Due to the long-term nature of these obligations, the estimates are subject to significant uncertainty.

The main assumption underlying these techniques is that past claims development experience is used to project ultimate claims costs. Allowance for one-off occurrences or changes in legislation, policy conditions or portfolio mix are also made in arriving at the estimated ultimate cost of claims in order that it represents the most likely outcome, taking account of all the uncertainties involved. To the extent that the ultimate cost is different from the estimate, where experience is better or worse than that assumed, the surplus or deficit will be credited or charged to gross benefits and claims within the Statement of Comprehensive Income in future years.

Taxation

The board has considered its attitude to taxation and the strategies in place in this respect.

This is a mutual society and there is no corporation tax charged on any surpluses generated from the main business of the society due to the special exemption granted under section 461C(1) of the Income and Corporation Taxes Act of 1970. All such amounts are either allocated to members or reinvested in the development of the business.

The society's main activity is writing insurance business: either the sale of insurance contracts with an investment element or sickness insurance products.

These principle activities mean the society makes exempt supplies for the purposes of Value Added Taxation and hence VAT is not levied on the premiums written whilst input VAT cannot be recovered on expenses incurred. The society does pay employment taxes and in the year under review these amounted to £173,280 in respect of PAYE and national insurance payments.

The board's overall attitude to taxation is that whilst the society is duty bound to act in the interests of its members, we do not see this as being inconsistent with making full disclosures and paying over the correct amounts to, HMRC in all instances.

3 Capital Management

This section deals with the capital and risk management approach of the Society. The Society seeks to create value for its members by investing in the development of the business whilst maintaining an appropriate level of capital available.

The risk appetite for each type of principal risk is set based on the amount necessary to meet the PRA's capital requirements.

Policies and Objectives

The Society's key management objectives are:

- To ensure the Society's strategy can be implemented and is sustainable;
- To ensure the Society's financial strength and to support the risks it takes on as part of its business;
- To give confidence to the policyholders and other stakeholders who have relationships with the Society; and
- To comply with the capital requirements imposed by its UK regulator, the PRA.

Details of the Society's objectives and its strategy to achieve them are provided in the Strategic Report - Business Review on page 6.

These objectives are reviewed at least annually and benchmarks are set by which to judge the adequacy of the Society's capital. The capital position is monitored against those benchmarks to ensure sufficient capital is available to the Society.

The assessment depends on various actuarial and other assumptions about potential changes in market prices, future operating experience and the actions management would take in the event of particular adverse changes in the market conditions.

The capital requirement in the annual PRA return is the statutory capital requirement based on EU directives. Management intends to maintain capital in excess of the PRA's total requirements and to hold an appropriate additional margin over this to absorb changes in both capital and capital requirements. The Society complied with all externally imposed capital requirements to which it was subject throughout the reporting period.

Capital Statement

The following summarises the capital resources and the requirements of The Shepherds Friendly Society Limited as determined for UK regulatory purposes. The capital statement below covers all the Society's life assurance business. There are no specific constraints on the capital of the Society. As the Society has no shareholders, all capital belongs to its members.

	2016 £000s	2015 £000s
Fund for Future Appropriations	20,332	18,631
Regulatory Solvency Adjustments	(61)	-
Total available capital resources	20,271	18,631

Measurement and Monitoring of Capital

The Society's solvency position is regularly reviewed to ensure it maintains an acceptable level of solvency. The Society is able to change the rates of future annual and final bonuses it pays to its with-profit policyholders in the event that there is a large change in its available capital resource.

Long Term Insurance Liability Valuation Assumptions

The following sets out the assumptions underlying the valuation of the Society's long term insurance liabilities. The section also details the analysis of change in the Society's capital resources over the year. The liability calculations are based on assumptions reflecting best estimates at the time of calculation, and a margin for adverse deviation. The realistic liabilities are based on the aggregate value of the policy "asset share" reflecting the premiums, investment return, expenses and charges applied to each policy. Allowance is made for policy-related liabilities, such as guarantees and future bonuses. Certain insurance contracts supporting savings plans are valued by their investment unit value.

Methodology for Calculating the Society's Long Term Contracts of Insurance

The key aspects of the methods recommended for this investigation are set out in the following table:

Business Type	Valuation Method
Life Business	
Regular premium life	Net premium with a Zilmer adjustment of 3% of the sum assured
Unitised With-Profits pension	Reserves equal to the value of the units
With-profits Bond (series I and II)	Reserves equal to the amount of the benefit payable on death excluding any final bonus entitlement
Individual Saving Accounts (ISAs), including Junior ISAs	Reserves equal to the amount of the benefit payable on death excluding any final benefit entitlement
Child Trust Fund (CTF)	Reserves equal to the bid unit value of the units held against CTF accounts
Income Protection Business	
Adult Holloway, Young Holloway, University Savings, SIPP and other IP contracts	Gross premium with members' accounts (where relevant) valued as discounted face value and sickness benefits valued using an inception/recovery average weeks claim approach. Premier reserves are calculated using individual case estimates.

Discount Rate of Interest

Discount rates are set having regard to risk free rates of return specified by EIOPA as at 31 December 2016.

Expenses

The Society's expenses were analysed between acquisition and maintenance expenses and allow an allowance for future years as a percentage of future premiums.

Mortality

Mortality rates are set by reference to standard actuarial tables by class of business. Mortality is assumed to follow rates as set out in the following table.

	2016	2015
Life Business excl. Over 50's	65%	65%
Over 50's	200%	200%
Income Protection	40%	100%

Morbidity

The following table sets out the sickness assumptions for each class of income protection business at the end of 2016 and those used at the end of 2015. Rates are set by reference to 100% inceptions and recoveries of CMIR12 tables.

	2016	2015
Adult Holloway	25%	25%
Young Holloway	10%	10%
SIPP Holloway	100%	65%
Non-profit Income Protection	35%	35%

Persistency

The following table sets out the annual rates of lapse assumed for each class of business at the end of 2016 and those used at the end of 2015.

Life	2016	2015
With-profits regular premium	2.00%	2.00%
Non-profit regular premium (exc. Over 50's)	0.50%	2.00%
Over 50's**	7.50%	10.00%
Single Premium bonds (Series I and II)	5.00%	5.00%
Adult ISAs*	10.00%	10.00%
JISAs	2.50%	2.50%

Income Protection	2015	2014
Holloway	2.50%	2.50%
Non-profit Income protection (post-2015 business)***	6.00%	7.50%
Non-profit Income protection pre-2015 business)	See below**	n/a

*Rates for Adult ISAs are duration dependent. Rates are 25% in year 1, 20% in year 2, 15% in year 3, 10% in year 4 and later.

**Rates for Over 50's are duration dependent. Rate are 15% in year 1, 12.5% in year 2, 10% in year 3, 7.5% in year 4 and later.

***Rates for IP business after 2015 are duration dependent. Rate are 15% in year 1, 14% in year 2, 13% in year 3, 12% in year 4 and later.

Options and Guarantees

Society is not exposed to implicit option or guarantee other than those within the Society's with-profits contracts.

Analysis of Change

There has been an increase in the available capital resources from 31 December 2015 to 31 December 2016. This is mainly a result of favourable new business volumes over the year. An analysis of the change is set out below:

	Change in available capital £000s	Available capital £000s
Capital resources 31 December 2015		18,631
Methodology and assumption changes	(3,190)	
Investment gains	509	
New business	7,328	
Trading surplus	(375)	
Change in risk margin	(2,022)	
Change in pension scheme	(468)	
Other	(142)	
Capital resources 31 December 2016		20,271

4 Risk Management and Control

This note provides information on the main risks to which the Society is exposed and how the Society manages these risks.

Underlying Approach to Risk Management

The following key principles outline the Society's approach to risk management and internal control:

- The Board has responsibility for overseeing risk management
- The Risk Committee handles a number of delegated functions on behalf of the Board
- An open and receptive approach to solving risk problems is adopted by the Board
- The Society makes conservative and prudent recognition and disclosure of the financial and non-financial implications of risks
- Managers are responsible for encouraging good risk management practice
- Identified key risk indicators are regularly reviewed and are closely monitored.

Overview of Risk Identification, Assessment, Management & Mitigation Process

The Society operates a technology based risk register which enables the Board, via its Risk Committee, to manage the risks faced by the business in a highly proactive manner. The system is used by staff at all levels in the organisation to ensure an enterprise wide approach to risk identification, assessment, management and mitigation is in operation. Risks are continuously assessed as they change and develop.

The following are the material risks identified by the Society:-

New Business Risks

The Society must write a sufficient volume of new business each year to maintain a flow of emerging surplus to meet its operating expenses. Therefore, it must compete in the open market to win business and in so doing faces a range of risks including the insurance risks described below plus others such as over paying to generate sales and the risk associated with miss-sold or misrepresented products. Accepting these risks is a result of being open to new business. Low new business levels may result in an inability to cover the costs of writing that new business. The Society has continued to monitor new business levels. A stagnation in demand and increasing competition raise the risk of writing too little business. The Society's strategy is to maintain its diversified product range, selling to existing members and developing new routes to market to mitigate this risk.

Insurance Risk

- Mortality risk is the risk that death claims are significantly more than expected in terms of numbers and values
- Morbidity risk is the risk that sickness claims are significantly more than expected in terms of numbers and values
- Lapse risk is the risk the policies cease and therefore contributions from future premiums are not as high as anticipated
- Expense risk is the risk that the future costs of administering claims are higher than anticipated.

Issuing new policies is the business of the Society and therefore it will always have to accept insurance risks if it is to remain open to new business. The inherent major risks within insurance books of business relate to policyholders having a different (worse) risk profile than was thought when they were sold a policy. When such risks appear the Society manages them in a manner of ways, such as in depth claims management, negotiated early settlements, product withdrawal and revised pricing for replacement products.

The product range of the Society generates surplus to be distributed to our members, and an additional risk which is given careful management is the lapse rate. If this is higher than planned, then a lower level of surplus will emerge from a book of business. The Society strives to deliver great service to its policyholders, to encourage high levels of policy retention.

Note 13 sets out the Long Term Business Provisions and the changes over the year.

Financial risks (market risk, credit risk, liquidity risk)

Financial risks vary in nature:

- Market risk is the risk of losses due to changes in the investment assets or the income from those assets.
- Credit risk is the risk of loss due to default by debtors and the Society's counterparties in meeting their financial obligations.
- Liquidity risk is the risk that the Society is unable to meet its own commitments to pay its liabilities when they become due.

The Investment Committee oversees investment activity, monitors investment managers and ensures that the investment policy and asset allocations are adhered to. The policy and investment strategy are reviewed and approved the Board on an annual basis. The Society manages its assets for the benefit of its members. The asset allocation policy, counterparty limits and other controls balance the risks against the rewards. Investment managers are used to manage much of the Society's investment portfolio with the Chief Actuary being asked to review the Investment Policy. Investment policy statements are used to assist in the portfolio management with investment managers.

Sensitivity of the Society's results to changes in key assumptions

Variable	Change in variable %	Change in available capital £000s
Change in mortality	+ 10%	(635)
Change in morbidity (%CMIR12)	+ 25% inceptions and -20% recoveries	(6,462)
Expenses	+ 10%	(3,017)
Change in fixed interest yields	EIOPA interest rate up	(3,403)
Change in fixed interest yields	EIOPA interest rate down	1,220
Fall in equity values	-10%	(1,136)
Fall in property values	-10%	(60)

Subsidiary Risk

The Society has a subsidiary - Financial Advice Network which acts as a distributor of some of the Society's insurance contracts. At the end of 2016 the Network is trading profitably. the Board is managing this business with a view to continued growth but it is exposed to market and regulatory pressures and risks.

5 Earned Premium Analysis

All premiums are written in the United Kingdom on a direct basis and relate to individual business. The following note refers to the Society and not the group.

Long Term Life Business	2016 £	2016 £	2015 £	2015 £
Non Profit Policies				
Periodic premiums	2,468,558		1,938,282	
Reinsurance	<u>(4,551)</u>	2,464,007	<u>(5,539)</u>	1,932,743
With Profit Policies				
Periodic premiums	4,460,800		4,451,311	
Reinsurance	=	4,460,800	=	4,451,311
Single premium	<u>3,820,560</u>	<u>3,820,560</u>	<u>2,200,965</u>	<u>2,200,965</u>
		10,745,367		8,585,019
Annualised new business written: Society and Group			2016 £	2015 £
Single Premium			382,056	220,097
Regular Premium			<u>3,239,300</u>	<u>1,837,763</u>
			<u>3,621,356</u>	<u>2,057,860</u>

Regular premiums are those where there is a contractual obligation or reasonable expectation to pay on a regular basis.

Single premiums are those relating to products issued by the Society which provide for the payment of one premium only.

6 Society and Group Net Operating Expenses

	Society 2016 £	Group 2016 £	Restated Society 2015 £	Restated Group 2015 £
Acquisition costs	5,171,546	5,178,482	3,336,390	3,349,392
Changes in deferred acquisition cost	-	-	(158,586)	(158,586)
Administration expenses	<u>1,771,687</u>	<u>1,639,732</u>	<u>1,721,494</u>	<u>910,580</u>
			<u>4,899,298</u>	<u>4,101,386</u>
Solvency II restatement adjustment	-	-	<u>158,586</u>	<u>158,586</u>
	<u>6,943,233</u>	<u>6,818,214</u>	<u>5,057,884</u>	<u>4,259,972</u>

Also included in the operating expenses are:

	Society 2016 £	Group 2016 £	Society 2015 £	Group 2015 £
Auditor's remuneration and expenses for audit services:	46,812	52,182	34,661	38,616
Non-audit services	-	-	-	-
	<u>46,812</u>	<u>52,182</u>	<u>34,661</u>	<u>38,616</u>

Notes to the Accounts

7 Staff Costs

The average monthly number of persons employed by the Society in the year was as follows:

	2016 £	2015 £
Board Members	8	7
Staff - Administration	29	27
Staff - Acquisition	8	7
	45	41

The aggregate remuneration of key management personnel, being those persons having authority and responsibility for planning, directing and controlling the activities of the entity are as follows:

	2016 £	2015 £
Wages and salaries	572,257	486,868
Social security costs	68,163	58,072
Pension costs	59,311	58,371
	699,731	603,311

The aggregate staff payroll costs were as follows:

	2016 £	2015 £
Wages and salaries	1,822,095	1,780,981
Social security costs	173,280	217,265
Pension costs	272,765	242,325
	2,268,140	2,240,571

Bands: (£5k) Salary & Pensions

	2016 £	2015 £
£0 - £5,000	1	-
£5,001 - £10,000	-	1
£10,001 - £15,000	2	-
£15,001 - £20,000	-	1
£20,001 - £25,000	- 1	-
£25,001 - £30,000	-	1
£30,001 - £35,000	1	-
£35,001 - £40,000	1	1
£45,001 - £50,000	1	-

8 Board Remuneration

	Salary £	Bonus £	Other Benefits £	Total 2015 £	Total 2014 £
A M O'Dea	148,298	52,500	19,364	220,162	204,564
K Harris	97,884	-	48,538	146,422	145,734
J Morrissey	80,120	25,200	12,410	117,730	82,180
J Hindle	45,000	-	3,329	48,329	36,425
G Ross	32,400	-	2,777	35,177	24,430
N Wynn-Evans	32,400	-	2,449	34,849	25,789
Simon Pashby (Appointed July 2016)	10,970	-	853	11,823	-
Roger Turner (Appointed July 2016)	10,970	-	1,540	12,510	-
B Bibby (Resigned January 2016)	4,567	-	-	4,567	16,219
M Howard (Resigned June 2015)	-	-	-	-	9,899
Total	462,609	77,700	91,260	631,569	545,240

Other benefits include contributions to pension money purchase schemes of £59,311. Non-executive directors receive expenses for travel to and from Board meetings at Head Office. These are taxed through PAYE and are included under 'Other Benefits'.

9 Related Party Transactions

Advantage has been taken of the exemption under FRS 102 not to disclose transactions with entities that are part of the Shepherds Friendly group. A number of the Society's directors are also members of the Society and pay annual premiums, all such transactions involving directors are conducted at arm's length.

10 Taxation

The Society has tax losses to carry forward and as such there is no tax liability for the current year. These losses would normally create a deferred tax asset but they cannot be recognised on the basis that foreseeable recovery cannot be determined with reasonable certainty.

11 Society Investments (Group)

Land and buildings*

	Cost 2016 £	Market Valuation 2016 £	Cost 2015 £	Market Valuation 2015 £
Investment properties	1,597,425	1,800,000	1,597,425	1,510,000
Long leasehold	-	-	-	-
	1,597,425	1,800,000	1,597,425	1,510,000

*Property is fully valued at least once every five years on an open market, existing use basis, measured at fair value under FRS 102 requirements. In between the full valuations a 'desktop' valuation is undertaken. Properties were not valued in 2015. In 2016 valuations were undertaken by Matthews and Goodman, Chartered Surveyors.

Other financial investments

	Cost 2016 £	Market Valuation 2016 £	Cost 2015 £	Market Valuation 2015 £
UK and overseas listed shares	41,244,155	51,760,426	44,232,007	49,585,829
UK and overseas listed fixed interest securities	17,477,254	17,807,226	17,760,080	17,948,528
UK and overseas listed Property Investment Fund	3,298,019	3,945,630	2,991,624	3,586,297
	62,019,428	3,513,282	64,983,711	71,120,654

Investment in subsidiary.

The Society owns 100% of the ordinary share capital of Financial Advice Network Limited.

	Shares in subsidiary £	Loans to subsidiary £
As 31 December 2016	500,000	0

12 Other Debtors (Group)

	2016 £	2015 £
Other debtors	190,641	11,347
	190,641	11,347

13 Movements in Provisions and Appropriations

Prior Year Adjustment

From 1st January 2016 the Society fell within the scope of Solvency II regulations. Due to this certain accounting policies previously adopted have been changed to comply with the new regulations. The changes in accounting policies are:

Changes in the actuarial calculation of the Technical provisions. This moves to a probability-weighted average of future cash flows, discounted at risk free rate, and also includes a risk free margin, that provides for the cost of supporting the capital required for non-hedgable risks over the remaining life of the contract. The adjustments to the reserves are shown below:

Fund for future appropriations (Society)

	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Balance at 1 January		18,630,548		9,780,128
Solvency II restatement adjustment				8,061,429
Balance at 1 January restated				17,841,557
Transfer from/to income and expenditure account	1,701,770		1,093,547	
Solvency II restatement	-		(304,556)	
		1,701,770		788,991
Balance at 31 December (Society)		20,332,318		18,630,548

Fund for future appropriations (Group)

	2016 £	2016 £	Restated 2015 £	Restated 2015 £
Balance at 1 January		18,529,556		9,602,177
Solvency II restatement adjustment				8,061,429
Balance at 1 January restated				17,663,606
Transfer from/to income and expenditure account	1,741,885		1,170,506	
Solvency II restatement	-		(304,556)	
		1,741,885		865,950
Balance at 31 December (Group)		20,271,441		18,529,556

Technical provisions (Group)

	2016 £	Restated 2015 £	Restated 2015 £
Balance at 1 January	54,155,674		67,976,278
Solvency II restatement adjustment			(8,662,332)
Balance at 1 January restated			59,313,946
Transfer from income and expenditure account	1,426,559	(5,304,253)	
Solvency II restatement		145,981	
			(5,158,272)
Balance at 31 December (Group)	55,582,233		54,155,674

The technical provisions were calculated by the Society's Actuarial Function Holder, using assumptions detailed in Note 3 Capital Management.

14 Tangible and Intangible Assets

Tangible assets cost	Property Improvement £	Equipment and Furniture £	Total £	Group £
At 1 January 2016	90,528	170,773	261,301	274,168
Additions	-	22,941	22,941	22,941
Disposals	-	-	-	-
At 31 December 2016	90,528	193,714	284,242	297,109
Depreciation				
At 1 January 2016	1,339	119,639	120,978	132,849
Provided in year	8,230	18,591	26,821	27,548
Disposals	-	-	-	<u>12,598</u>
At 31 December 2016	9,569	138,230	147,799	172,995
Net book value				
31 December 2016	80,959	55,484	136,443	124,114
31 December 2015	89,189	51,134	140,323	141,319

Intangible assets (Restated)	Software £	Total £	Group £
At 1 January 2016	612,258	612,258	878,924
Additions	121,763	121,763	121,763
Disposals	-	-	-
At 31 December 2016	734,021	734,021	1,000,687
Depreciation			
At 1 January 2016	361,755	361,755	485,661
Provided in year	165,413	165,413	202,529
Disposals	-	-	-
At 31 December 2016	527,168	527,168	688,190
Net book value			
31 December 2016	206,853	206,853	312,497
31 December 2015	250,503	250,503	393,263

Previously reported Tangible assets have been reclassified to Intangible assets this year to comply with provisions under FRS 102.

15 Statement in accordance with Section 77 of the Friendly Societies Act 1992

The following information has been approved in accordance with Section 77 of the Friendly Societies Act 1992:

- 1 The Chief Actuary & With Profits Actuary during the year was Mr C Critchlow BSc FIA, an employee of OAC plc. Neither Mr Critchlow, his wife or his children were members of the Society at any time during 2016.
- 2 Neither Mr Critchlow, his wife or children had any financial interest in any transaction with the Society at any time during 2016, other than as an employee of OAC plc.
- 3 The only remuneration was the fee for professional services paid to OAC plc. for the services provided by Mr Critchlow and his support team. The amount payable in this respect amounted to £296,650 inclusive of VAT (2015: £220,508). No other benefits, emoluments, pensions or compensation were paid.
- 4 Mr Critchlow did not receive, and will not receive, any other financial benefit.

16 Operating Rent & Lease Commitments

Annual leases under non-cancellable operating leases are as follows:

	2016 £	2015 £
Annual commitments under rent agreements and operating leases which expire:		
Amounts falling due < 1 year	70,037	68,892
Amounts falling due 2 - 5 years	185,610	252,880
Amounts falling due 5 years +	345,288	248,059
	600,935	569,831

17 Staff Pension Scheme: Society and Group

The Society operates a Final Salary defined benefit pension scheme. Pension benefits are linked to the members' final pensionable salaries and service at their retirement (or date of leaving if earlier). The Scheme has been closed to new entrants since 1 May 2005. The most recent formal actuarial valuation was carried out as at 5 April 2015. The results have been updated to 31 December 2016 by a qualified independent actuary. The assumptions used were as follows:

Final Assumptions Description	Year ending 31 December 2016	Year ending 31 December 2015
Discount Rate	2.80% pa	3.90% pa
Retail price inflation	3.20% pa	3.10% pa
Consumer price inflation	2.20% pa	2.10% pa
Salary Increases	2.00% pa	3.00% pa
Rate of increases of pensions in payment		
-CPI max 3%	2.00% pa	1.90% pa
-RPI 5%	3.10% pa	3.00% pa
-RPI 2.5%	2.30% pa	2.30% pa
Rate of increase for deferred pensioners	2.20% pa	2.10% pa

Demographic Assumptions Description	Year ending 31 December 2016	Year ending 31 December 2015
Mortality (Pre retirement)	As per post retirement	As per post retirement
Mortality (Post retirement)	SP2PA CMI_2015_M/F [1.00%] (yob)	SP2PA CMI_2014_M/F [1.00%] (yob)

Life Expectations	Year ending 31 December 2016 Male	Year ending 31 December 2016 Female	Year ending 31 December 2015 Male	Year ending 31 December 2015 Female
Life expectancy for an individual aged 65 in 2016	21.9 years	23.9 years	21.9 years	23.9 years
Life expectancy at age 65 for an individual aged 45 in 2016	23.2 years	25.4 years	23.2 years	25.4 years

17 Assets

The assets of the Scheme are invested in a diversified portfolio.

Asset Class	Year ending 31/12/2016		Year ending 31/12/2015	
	Market Value £'000	% of total Scheme assets	Market Value £'000	% of total Scheme assets
Equities	-	0%	-	0%
Bonds	1,799	45%	1,562	40%
Gilts	-	0%	-	0%
Property	-	0%	-	0%
Cash	19	0%	98	2%
Diversified growth Funds	2,211	55%	2,327	58%
Annuities	-	0%	-	0%
Total	<u>4,029</u>	<u>100%</u>	<u>3,987</u>	<u>100%</u>
Actual return on assets over period is	241		14	

Reconciliation to the Balance Sheet Description	Year ending 31 December 2016 £'000	Year ending 31 December 2015 £'000
Market Value of assets	4,029	3,987
Present Value of liabilities	4,471	3,961
Surplus/(Deficit) in the scheme	(442)	26
Irrecoverable Surplus	-	-
Pension asset/(liability) recognised in the balance sheet before allowance for deferred tax	(442)	26

Reconciliation of Scheme Assets and Defined Benefit Obligation Description	Assets £'000	DBO £'000	Total £'000
As at 31/12/15	3,987	(3,961)	26
Benefits paid	(351)	351	-
Employer contributions	147	-	147
Member contributions	5	(5)	-
Current service cost	-	(23)	(23)
Administration expenses	-	-	-
Past Service cost	-	(48)	(48)
Settlements	-	-	-
Business combination/ bulk transfers	-	-	-
Interest income/(cost)	152	(148)	4
Remeasurement gains/(losses)	-	-	-
-Actuarial gains/(losses)	-	(637)	(637)
-Return on plan assets excluding interest income	89	- 8	9
As at 31st December 2016	4,029	(4,471)	(442)

Analysis of Amounts Charged (Credited) to Profit or Loss	Year ending 31 December 2016 £'000	Year ending 31 December 2015 £'000
Service Cost:		
Current service cost:	23	24
Administration expenses	-	-
Past service cost	48	-
(Gain)/Loss on business combinations	-	-
(Gain)/Loss on settlements	-	-
Total Service Cost	71	24
Net Interest	(4)	14
Amount Charged/(Credited) to Profit & Loss	67	38
Amounts Recognised In Other Comprehensive Income	Year ending 31 December 2016 £'000	Year ending 31 December 2015 £'000
Remeasurement of the Net Defined Benefit Liability (asset)		
Actuarial gains/(losses) on liabilities	(637)	539
Return on assets excluding amount included in net interest	89	(128)
Limit on recognition of assets excluding amounts included in net interest	-	-
Amount recognised in Other Comprehensive Income	(548)	411

Future Funding Obligation

The last actuarial valuation of the Scheme was performed by the previous Actuary for the trustees as at 5 April 2015. The Society agreed to pay annual contributions of 21.5% of pensionable salaries and £75,000 pa until 31 October 2018. The Society expects to pay £94,000 to the Scheme during the accounting year beginning 1 January 2017.

Glossary

Asset Share

In relation to a policy, the accumulated value of premiums paid with deductions for expenses, mortality costs and any tax, where the accumulation rate is the rate of return achieved by the assets assumed to back the asset shares in question. Adjustments may be made for the cost of guarantees, capital and miscellaneous profits or losses if deemed appropriate.

Corporate Governance

An internal system encompassing processes, policies and people by directing management activities with objectivity, accountability and integrity.

EIOPA

The European Insurance and Occupational Pension Authority is a European regulatory institution.

FRS102 FRS103

A Financial Reporting Standards issued by the the Accounting Standards Board.

Fund for Future Appropriation, FFA

The balance sheet item required by Schedule 3 to the Regulations to comprise all the funds the allocation of which to policyholders has not been determined by the end of the reporting period.

Technical provisions

An actuarial calculation of the amounts due to policy holders. It is also known as technical provisions.

ORSA Own Risk and Solvency Assessment

The ORSA is the Society's Own Risk and Solvency Assessment. It is a forward looking assessment of the Society's solvency position taking into account the specific risks to which it is exposed.

Realised and unrealised gains or losses

A realised gain or loss occurs when an asset is sold and is the difference between the sale proceeds and the cost. Insurance companies are required to revalue their assets every year, and the increase or decrease in value since the previous year is classed as an unrealised gain or loss.

Reinsurance

The Society pays a premium to a larger insurer to share the risks for larger sums assured.

Solvency II

Solvency II Directive is a fundamental review of the capital adequacy regime for the European insurance industry. It aims to establish a revised set of EU-wide capital requirements and risk management standards with the aim of increasing protection for policyholders.

Smoothing

The principal of reducing bonuses in good years to prevent lower bonuses in poor years.

Valuation methods

Note 3 of the Report and Accounts refers to the assumption that the actuary uses in calculating the Technical provisions. The references are to standard actuarial tables for calculating death and sickness rates.

With-Profits Fund

All members/policyholders participate in the profit and losses of the fund

Notes

[illegible]



to make members
feel valued

to remain mutual
when in our
members interests

to provide simple,
value for money
financial solutions

to be a place
where people
want to work

We believe that mutuality is the best way of providing maximum benefit to our members and at the heart of the Society we have the mutual core values of trust, mutual benefit and ownership. We ensure that the money you invest with us is treated in a responsible and sensible manner to give as good a return on your investment as possible.

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SHEPHERDS FRIENDLY IS A TRADING NAME OF THE SHEPHERDS FRIENDLY SOCIETY LIMITED WHICH IS AN INCORPORATED FRIENDLY SOCIETY UNDER THE FRIENDLY SOCIETIES ACT. REGISTERED NO 240F. AUTHORISED BY THE PRUDENTIAL REGULATION AUTHORITY AND REGULATED BY THE FINANCIAL CONDUCT AUTHORITY AND THE PRUDENTIAL REGULATION AUTHORITY, FINANCIAL SERVICES REGISTER NO 109997.

The Head office and Registered office of The Shepherds Friendly Society is based in the United Kingdom.