everyone **counts**

2013 Annual Report & Accounts

Homeowners Friendly Society Group annual report
& accounts for the year ended 31 December 2013

engage
Mutual Assurance

society information

Engage Mutual Assurance is a trading name of Homeowners Friendly Society Limited.

registered office
Hornbeam Park Avenue,
Harrogate HG2 8XE
telephone: 01423 855000
email: mail@engagemutual.com
website: **engagemutual.com**
Registered and Incorporated under the Friendly Societies Act 1992
Registered No: 964F
Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulation Authority.
Member of the Association of Financial Mutuals (AFM)

independent service providers

auditor
KPMG Audit plc, Statutory Auditor

solicitors
Addleshaw Goddard LLP

bankers
Barclays Bank Plc

board of directors

The Directors who have served during the year are:
David G Robinson MA FFA
Peter J Burrows BA ACA
Paul G Chandler MA MBA
Caroline E Fawcett BSc DipM MCIM (appointed 28 May 2013)
Andrew T Gosling MA FCA
Karl J D Elliott BA
Peter W Mason BSc FIA (resigned 31 January 2013)
Nigel B Masters BSc FIA
Christina M McComb BA MBA

other society officers

secretary
Andrew J Horsley MCSI FCIS

actuarial function holder and with profits fund 2 actuary
Trevor M Batten FIA

with profits fund 1 actuary
Trevor Batten (until 21 March 2013)
Stephen Turland BA FIA (appointed 21 March 2013)

board committees

audit
Andrew T Gosling (Chairman)
Caroline E Fawcett (from 13 November 2013)
Christina M McComb
Peter W Mason (resigned 31 January 2013)
Nigel B Masters

finance
Nigel B Masters (Chairman)
Peter J Burrows
David G Robinson

corporate governance and nominations
David G Robinson (Chairman)
Peter J Burrows (from 22 February 2013)
Paul G Chandler (until 13 November 2013)
Andrew T Gosling
Christina M McComb
Peter W Mason (resigned 31 January 2013)
Nigel B Masters (until 13 November 2013)

remuneration
Christina M McComb (Chairman)
Paul G Chandler
Caroline E Fawcett (from 13 November 2013)
Peter W Mason (resigned 31 January 2013)
David G Robinson

Risk *(established 13 November 2013)*
Paul G Chandler (Chairman)
Karl J D Elliott
Andrew T Gosling
Nigel B Masters

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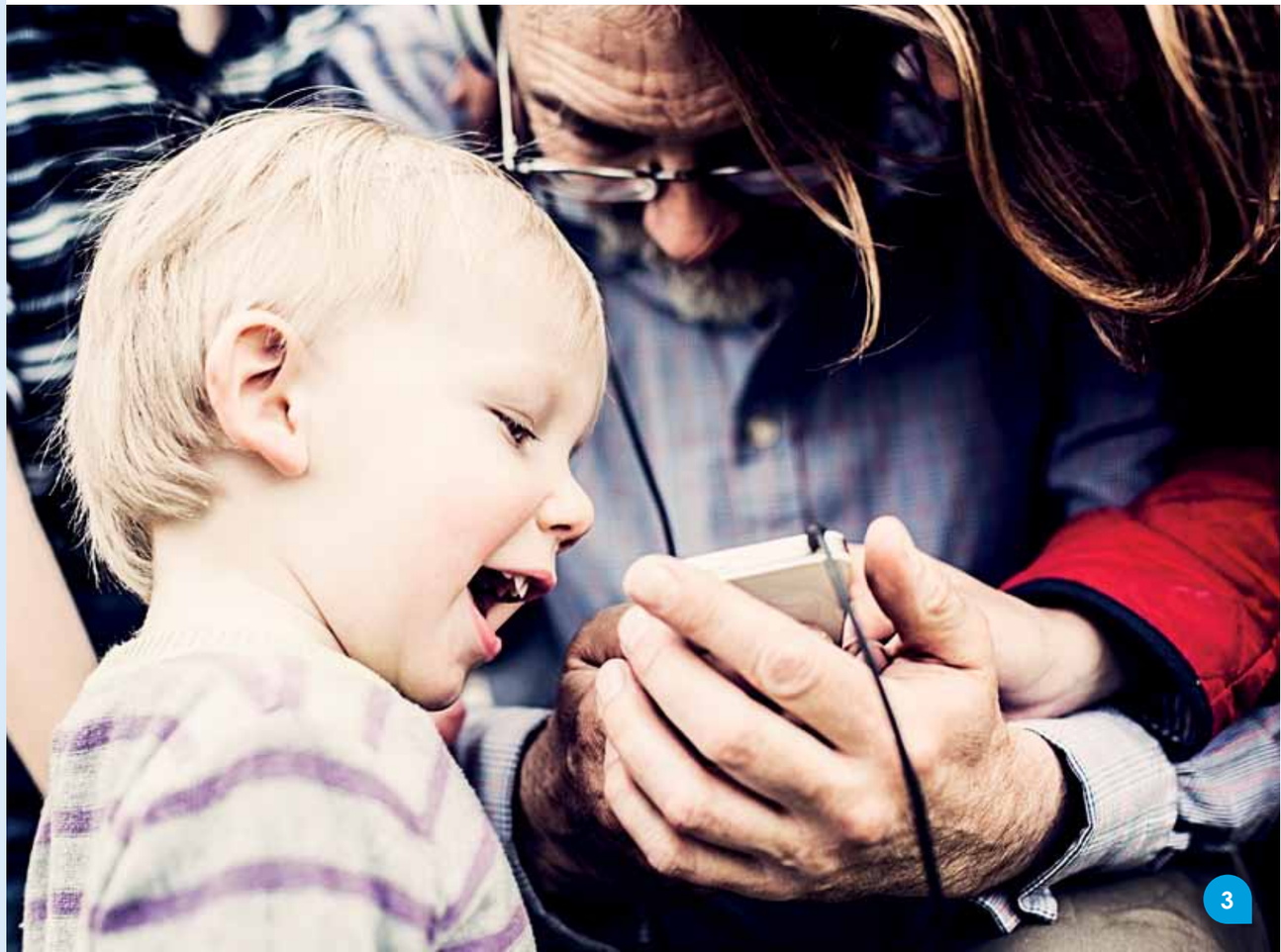


who we are

Engage Mutual Assurance is a trading name of Homeowners Friendly Society Limited. We are a mutual organisation based in Harrogate, North Yorkshire, providing simple, good value life insurance, health and savings products for around 500,000 customers.

Within the Engage Mutual Group there are a number of subsidiary companies:

- Engage Mutual Health offers health insurance products. Engage Health Holdings Limited is the holding company of Engage Mutual Health
- Engage Mutual Funds Limited is the provider of our Child Trust Fund product
- Engage Mutual Services Limited is our marketing services subsidiary
- Engage Mutual Administration Limited is the principal employer, with around 200 staff providing administrative services to the other companies in the Group
- Engage Foundation provides additional benefits to customers and their families beyond their policy terms and conditions

simple, good value life insurance, health and savings products for around **500,000 customers.**

why we exist

our vision:

to build a thriving and enduring mutual – **serving, empowering and representing our customers.**

our values are always to:

Think like a customer

Behave like a mutual

Put the customer first

Remember that our customers are people

Do the right thing in the right way

chairman's introduction

There were some encouraging signs of recovery in the economy during 2013, although your Society is all too aware that sustained low interest rates, together with the Government's austerity measures, have led to continuing pressures on the day-to-day finances of many of our customers. In response, Engage Mutual has continued to work hard to provide a financially strong, safe haven for our customers' savings, health and protection needs.

2013 saw a strong uplift in stock market performance with the FT-SE® All-Share Index growing by 16.7%. This resulted in improved returns for many of our customers with policies invested in our equity linked and with profits Funds.

In contrast, our deposit-based savers continued to be faced with historically low interest rates as the Bank of England base rate remained at an all-time low of one half of one percent, for the fifth year running. We understand the challenges this presents to savers, especially those relying on interest earned to top up their incomes or pensions and our treasury team has again worked hard on their behalf to deliver an average gross return of 1.6% in the year, a good result in current market conditions. We have also continued to limit the charges we apply to a maximum of £50 per year. We will continue to seek the best returns possible in the market, consistent with not exposing our customers' policies to undue risk.

During 2013, your Society made good progress, with a clear articulation of our strategy, further strengthening of our corporate governance arrangements and Board and continued sales growth in our core markets. As a customer-owned business it should come as no surprise that our strategy focuses on working in the best interests of our customers. In fact, unless our customers derive tangible benefits from the fact that they are part of a mutual business, mutuality will simply be a meaningless label. Our aim is to bring mutuality to life in all that we do; in developing helpful, relevant products, priced to provide good value as opposed to high profits; in dealing with our customers' claims fairly and compassionately, especially when they need our help and support; and in the way we communicate and engage with our customers, listening and responding to what they need most from their Society. We were therefore delighted that for the fourth year running, our customers once again recognised our efforts with industry-leading satisfaction scores, of which you can read more on p13.

> As a customer-owned business it should come as no surprise that **our strategy focuses on working in the best interests of our customers.**

In 2013 we further improved our successful 'Engage with your Community' initiative, providing even more financial support to community volunteering projects nominated by our customers across the UK. In line with our strategy which involves providing additional customer benefits, we also took the interpretation of what it is to be a mutual business even further by developing the Engage Foundation.

We held our first two Customer Forum meetings in 2013, at which I was delighted to meet a broad cross section of our customers. These were invaluable sessions at which our ideas and plans for the Engage Foundation were tested out and were met with a very favourable response. Having developed the concept further following this feedback, I'm proud to report that the Engage Foundation was launched in January 2014. You will read more detail in the Chief Executive's report, but I do wish to take this opportunity to say how pleased the Board has been at this latest development.

It is my belief that the effective governance of mutual organisations is just as important as for shareholder-owned businesses, if not more so. Consequently, we have taken steps in 2013 to further strengthen our governance processes, whilst shaping a Board of Directors with a range of relevant and diverse skills and experience.

> Looking to the future, we have a sound strategy **based entirely upon the principles of customer-ownership.**

There have been a number of changes to the Board over the year, the most significant being the appointment of Peter Burrows as Chief Executive Officer in August 2013, following a rigorous search process against strong external applicants. Peter is a firm advocate of a mutual business model that has customer ownership and a sense of collective community and participation at its heart, and Engage Mutual is already developing and carrying these principles forward under his leadership.

Peter has strengthened our executive management team in 2013, especially in the areas of Sales and Operations, and has adapted our structures to ensure an even stronger focus on customer service as well as on commercial effectiveness. These changes will enable the organisation to ensure that delivery of our strategy has the focus and attention it requires in order to succeed.

We also further strengthened the Board in 2013 by appointing Caroline Fawcett as a non-executive director, again after a thorough, externally-assisted recruitment process. Caroline brings a wealth of experience in helping businesses engage and communicate better with their customers and so is ideally placed to contribute to our customer-owned strategy. She is already adding new capabilities and thinking to our Board and like the rest of the Board is strongly committed to our values.

As part of our ongoing development of our governance infrastructure, we also improved the way in which we monitor and mitigate the risks that the organisation faces, by setting up a dedicated Risk Committee under the Chairmanship of non-executive director, Paul Chandler. Whilst the Board remains ultimately responsible for the oversight of the financial and other risks facing the business, the establishment of the Risk Committee is already proving to be an effective way of ensuring that sufficient focus and rigour is applied to this important aspect of our governance.

As your Chairman, I am confident that your Society is well placed to ensure that the interests of our customers will be well provided for today and in the years to come. There is a commitment and enthusiasm throughout the whole organisation to make a positive difference to our customers' lives and this is already being reflected in the quality of our products, standards of service and customer benefits we deliver. In delivering our strategy, your Society will continue to explore opportunities to work more closely with other like-minded organisations, where we see real and tangible benefit to our customers in doing so.

Looking to the future, we have a sound strategy based entirely on the principles of customer-ownership. It is a business with excellent customer service, simple, affordable products and a strong and sustainable financial foundation at its core. We have a highly-capable and dedicated team in place, all of whom share our mutual values and ethos, which gives me great confidence in our ability to deliver a thriving and enduring business in the future.

I would like to thank my fellow Board members, the management and staff of Engage Mutual and our customers for their support throughout the year.

David Robinson
Chairman
20th March 2014

chief executive's review

I was delighted to be appointed as Chief Executive of the Society in August 2013. In parallel, your Board adopted a new vision for the Society: to build a thriving and enduring mutual - serving, empowering and representing our customers.

Engage Mutual has become a successful business by focusing on the fundamentals: we offer simple, good value products, we underpin that with excellent customer service, and we maintain a strong capital position so that our customers can be confident that their policies are secure. None of this will change. But looking to the future, we recognise that in order to continue to flourish we need to build our reputation and enhance our product range, reinvigorating the principles and values of mutuality in a modern framework.

Although the economy is beginning to show more positive signs than a year ago, customers will need no reminder of the austere financial conditions of recent years. Throughout that period your Society has successfully maintained its financial strength, and 2013 was no exception. Our capital position remains enviably strong, and you should therefore be confident that the Society has a bright future with the financial strength to continue to meet its financial commitments to customers. Of course, in parallel with maintaining robust finances, we continue to invest in the future and to explore new opportunities for growth. We have successfully completed a number of acquisitions in recent years, and we remain open to merger and acquisition activity where this is in our customers' best interests.

Our commitment to providing outstanding customer service remains a guiding principle, and in 2013 we again participated in the annual independent 'LAMRA Life and Savings Benchmarking Survey', a benchmark of leading organisations in the industry. The results from 2013, and indeed from prior years, demonstrate that our performance is consistently better than most others in the industry, and in many areas significantly so. We are proud that our customers rate us so highly, but we will not allow ourselves to become complacent.

You will find full details of our performance and results within the Strategic, Operating and Financial Review starting on page 12.

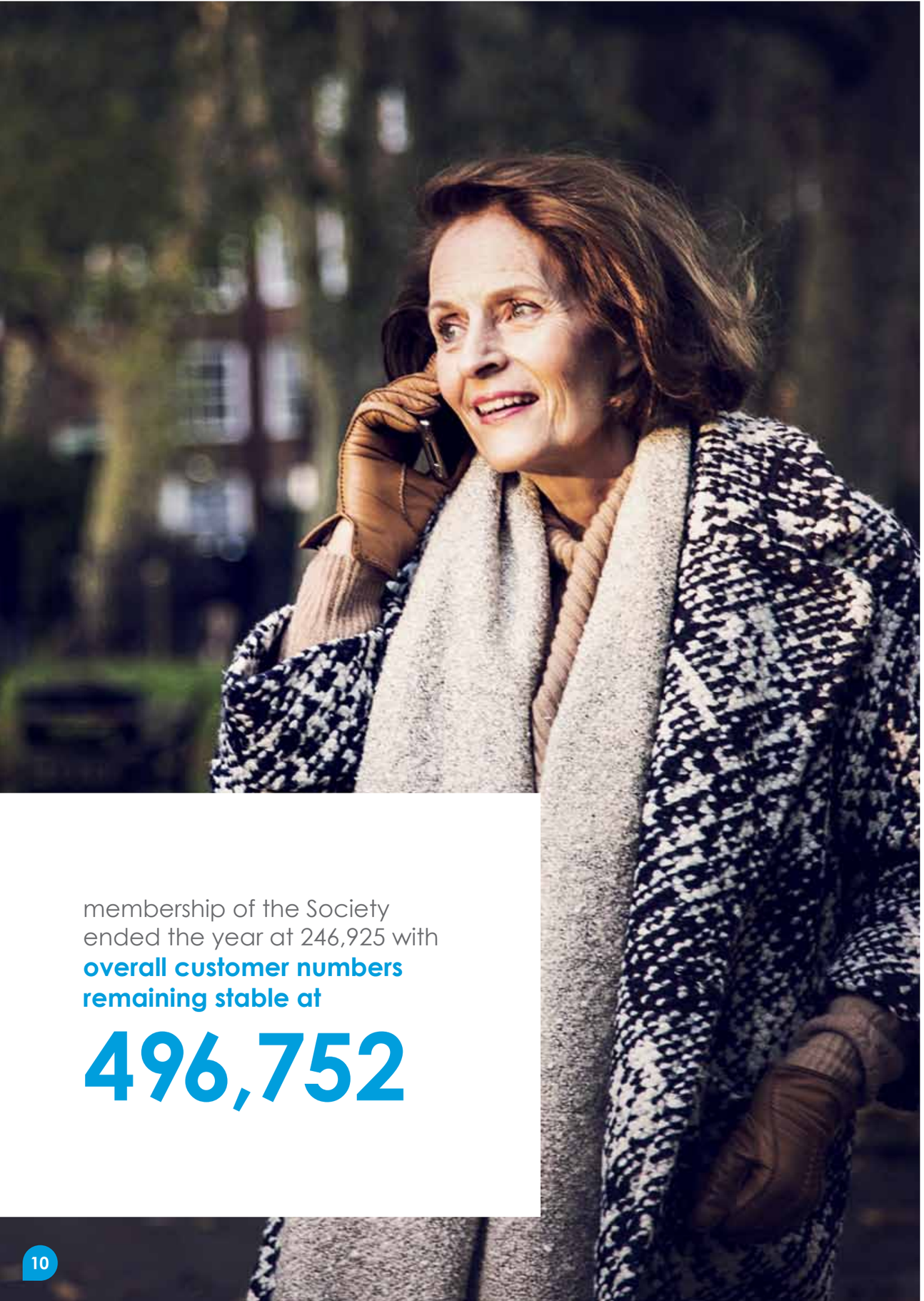
> We offer simple, good value products, we underpin that with excellent customer service, and we maintain a strong capital position so that **our customers can be confident that their policies are secure.**

However, the following are some of the highlights of 2013:

- we continued to grow our Over 50s Life Cover sales, having extended its benefits to give customers the ability to access their sum assured in the event of terminal or critical illness and providing additional support services over the duration of the policy. New Over 50s Life sales were £3.4 million, representing growth of 5% on the prior year
- health cash plan new business sales totalled £0.8 million, growth of 36% on the prior year
- 2013 was another difficult year for deposit savers, but against a backdrop of continued low interest rates we delivered a gross return for customers of 1.6%. We also maintained our charge cap arrangement, whereby charges on deposits are capped at a maximum of £50 per annum
- both of our With Profits Funds continue to use their capital strength to return excess capital to the funds' customers. Typical enhancement rates to payouts are 12.5% in the With Profits I Fund and 9% in the With Profits II Fund
- we continue to make progress in our work to trace customers who, whether due to forgetting or mislaying their policies, have unclaimed money held by the Society. The total amount successfully reunited with its rightful owners now exceeds £3.1 million
- total costs were contained at £20.4m, broadly in line with 2012 levels
- we maintained a strong capital position, with the Group's available capital resources totalling £93.9 million, ahead of our target to hold in excess of three times that which we are required to hold by regulatory requirements
- membership of the Society ended the year at 246,925, with overall customer numbers at 496,752
- in the recent LAMRA Life & Savings Benchmarking Survey, 91% of customers told us that we treat them fairly

We believe that the mutual model of ownership creates a naturally more favourable environment for members, who are both the customers and owners of their business. In 2013, following consultation with customers, we announced our intention to launch the Engage Foundation. This is a significant step for us, embodying our desire to make membership of the society genuinely meaningful, and providing benefits to customers that go beyond their policy terms and conditions.

We formally launched the Engage Foundation in January 2014 with a commitment to make £1 million available to customers over a five year period. Our customers will decide how best they spend this money for their collective benefit, with the bulk of the money being spent on customer community initiatives in line with customer feedback received during the



membership of the Society ended the year at 246,925 with **overall customer numbers remaining stable at**

496,752

Our staff continue to be the bedrock upon which we build the day to day successful running of our business. **In 2013 we were proud to be awarded Investors In People 'Champion' status**, in recognition of our commitment to the development and continued wellbeing of our people.

consultation period. Any Engage Mutual customer is entitled to propose a community scheme, and the most popular schemes – as determined by an open vote on our website – will benefit from funding. In addition, customers can apply for individual grants to support themselves or a loved one in times of hardship.

The Engage Foundation has been established as a genuine customer benefit, with proposals and decisions as to how the money is spent entirely in the hands of customers themselves. But critically, we expect the Foundation to generate commercial benefit commensurate with its cost. In that sense we believe that the Foundation will represent a 'win-win' scenario, providing additional benefit to customers whilst at the same time delivering real commercial benefit in terms of brand awareness and reputation, and attracting new customers to the organisation.

We remain strong advocates of the need for robust regulation of the sector, with a passionate belief in good corporate governance. On 1 April 2013 the Financial Services Authority divided into two successor regulatory bodies, the Prudential Regulation Authority and the Financial Conduct Authority. We welcome this increased focus on the two key regulatory areas of financial strength and the fair treatment of customers. The pace of regulatory change continues, and we continue our preparations in respect of the new risk and capital management regulations known as 'Solvency II' which after a number of delays has now been confirmed as effective from 1 January 2016. This will undoubtedly place new challenges on any insurance business, but our risk processes and capital strength are such that we remain confident of our ability to comply with the new requirements.

Our staff continue to be the bedrock upon which we build the day to day successful running of our business. In 2013 we were proud to be awarded Investors In People 'Champion' status, in recognition of our commitment to the development and continued wellbeing of our people. In receiving this accolade we became the only mutual across Yorkshire and Humberside to be an IIP Champion, and joined a prestigious group of just 10 organisations working to promote and share best practice across the region. The results of our annual independent staff survey were similarly strong, showing that our people benchmark is in line with the global top quartile of businesses.

In conclusion, I would like to extend my thanks to all of our customers and staff for their continued commitment and support. Without you, the Society would not exist; but together, I believe that we can make Engage Mutual a thriving and enduring customer-owned business.

Peter Burrows
Chief Executive
20 March 2014

strategic, operating and financial review

strategic and operating review

Our customers matter most, so we want to be there for them when it matters.

Our aim is to build a thriving and enduring business for our customers, balancing their needs as product holders and business owners. To do this we will continue to offer simple good value products, excellent customer service, and maintain a strong balance sheet, but increasingly we will use surplus funds for the benefit of our customers, adding value to them beyond their contractual policy terms.

Within that context, we have made significant progress in 2013 in defining our vision for the organisation and the steps that we intend to take to bring our vision to life.

Our vision is to **build a thriving and enduring mutual - serving, empowering and representing our customers.**

Historically, we've provided security for customers to help them cope with life's challenges. Our customers tell us that they have unmet needs in leading a full, healthy and independent life. This provides the opportunity for us to take a wider and increasingly relevant role in their lives, and our market leading customer sentiment gives us a platform from which to build.

In addition to the security offered by our products, we want to help people to live life to the full. It's not just about security in the tough times; it's also about getting the most out of the good times.

We want to make a positive difference to the lives of people, right across the UK. We will achieve this by:

- providing security, help and support to customers and their families through our products
- providing additional support, practical and financial, to individual customers and their families
- enabling customers to make a significant and lasting impact on their lives and the communities they live in

In the coming twelve months we aim to:

- build a stronger reputation that brings our vision to life for customers in a meaningful way
- develop the Engage Foundation. In January 2014 we announced that we had made £1m available to customers over 5 years, through individual grants and project funding, that will help our customers to make something better in their lives and local communities
- continue to grow our Over 50s and Health product new business, focusing on building a growing and commercially successful organisation
- introduce a wider range of simple, good value products and services that are relevant and helpful to our customers in living their lives and preparing for the future

This strategic intent underpins every decision we take as an organisation.

In building a thriving and enduring mutual, we are committed to listening and engaging with customers; providing simple, affordable products and services, delivering excellent customer service, all underpinned by a strong and secure capital position. We believe in being a socially responsible employer and in making a positive contribution to the communities in which we live and work. Below we outline how we have made real progress on the journey to delivering our strategy during 2013.

operating review

customer engagement

Customer engagement took a significant step forward in 2013 as we launched a number of initiatives which put our customers at the very heart of our thinking.

During the year we undertook our largest ever programme of customer insight. This included a number of focus groups, asking different groups of customers and people in our target audience about their aspirations, hopes and fears and what role, if any, they thought that a mutual organisation could play in their lives.

It also led us to hold our first formal Customer Forums, in Manchester and London, where we invited

customers to come along to meet us and each other and to share their views and help us develop our plans for the future of the organisation.

In April 2013, we added a new section to our web site called Get Involved. This enabled customers to participate in AGM voting and influence our support for customer led community projects and charitable giving. This has proved an excellent starting point to understanding how we can help and support customers over and above the products they hold with us.

Our Engage with your Community initiative saw us provide grants of up to £5,000 for 6 customer led community projects selected from over 100 nominations across the UK.

These insights, events and activities have proved invaluable in helping us shape our thinking and plans for future engagement, something we believe is critical to our long-term success as a meaningful mutual organisation.

It is also as a consequence of the past 12 months' customer engagement activities that we have announced our intention to launch the Engage Foundation. From January 2014 we have made £1 million available to customers over 5 years, and our customers will decide how best they spend this money for their collective benefit. Money will initially be distributed through individual grants and project funding to help customers to make something better in their lives and local communities. These awards and grants are made possible by the financial strength of the organisation. Because of this we are able to share the success of the organisation with its customers, who as a mutual are its owners.

We could have given customers this money directly, but for every customer that would have meant just £2 over 5 years, not enough to make a real difference. By pooling this money we can make things better, and it is with the ringing endorsement of our customers that we have decided to launch the Engage Foundation in this way.

customer feedback

Excellent customer service is a key tenet of our business strategy, and so understanding what our customers think of us and where

strategic, operating and financial review (cont.)

we can do better is of paramount importance. We conduct a variety of research throughout the year to ensure that we keep up-to-date with customers' views. We're also keen to know how we compare to other organisations and that's why we take part in the annual LAMRA Life & Savings Benchmarking Survey (previously the Association of British Insurers Customer Impact Survey).

The LAMRA Life & Savings Benchmarking Survey is a benchmark survey of customer service for the life insurance industry. Conducted annually, the survey measures customers' satisfaction on a wide range of factors including service, product and communications. This year customers of sixteen leading life and investment organisations were surveyed; the most comprehensive survey of its type in our industry.

We were delighted with the key findings of the survey which saw us outperform the industry in 44 of the 46 areas measured. The highlights include:

93% agree that Engage Mutual is a trusted provider

92% of customers rate our service good or higher

91% of our customers agree that we treat them fairly.

A selection of the survey results is shown below.

93%

agree that Engage Mutual is a trusted provider

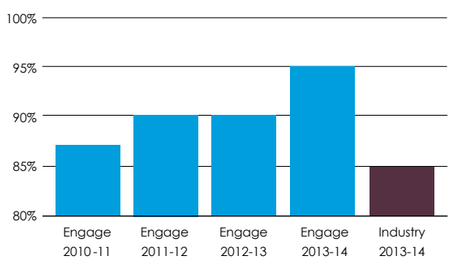
92%

of customers rate our service good or higher

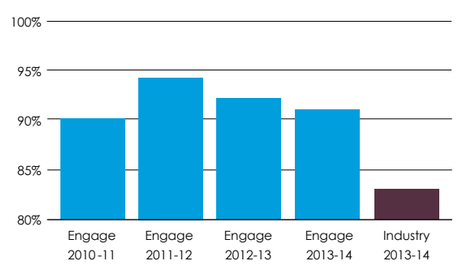
91%

of our customers agree that **we treat them fairly**

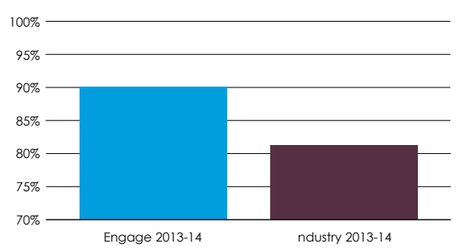
overall customer service satisfaction



treats customers fairly



values its customers



This was introduced as a new measure for the 2013 survey.

These results support the findings of our own regular customer benchmark survey throughout the year, gathering feedback from 2,000 customers on our service, communications, competitiveness and the effectiveness and ease of use of our website. In testing market conditions, customers continue to be very satisfied with the services we offer, recording another excellent year in overall satisfaction.

products and services

In 2013 we continued a process of ensuring that our current range of products is attractive to customers seeking simple, value for money solutions to their health and protection needs.

placed to continue growing sales in the future. We also saw an increase in the take up of our free Funeral Funding Option, which gives customers who hold an over 50s life cover plan a discount on funeral fees for no additional cost to themselves. This continues to be a very attractive additional benefit for customers, with over 30% taking the option when purchasing their product.

Health sales continued to grow in 2013 thanks to a combination of our unique One Fund corporate health cash plan and sales of our retail health cash plan product. We improved our One Fund product during 2013 in order to be more appealing to customers and our

our already competitive rates and excellent customer service mean **we are well placed to continue growing sales in the future.**

Our Over 50s Life Cover product continues to successfully meet our customers' needs with increased sales in 2013. The introduction of terminal and serious illness benefits, which enable customers to draw down some or all of their sum assured during their lifetime, has proved very popular with customers and distributors alike. These features are unique to this product, and together with our already competitive rates and excellent customer service, mean we are well

intent remains to provide a simple and cost efficient alternative to the increasingly expensive Private Medical Insurance policies that many simply cannot afford.

In addition to our core product offering, we maintained the Engage Mutual Annuity Service in partnership with leading broker Key Retirement Solutions. It is vitally important that our pensions customers get the most appropriate and beneficial outcome when selecting whether to purchase an annuity and we believe that offering an open market solution is in their best interest. We also continued to receive additional contributions into over 200,000 Child Trust Funds that we look after on behalf of our younger customers.

In 2013 we undertook significant change programmes to improve and streamline our administration systems and procedures. These projects experienced significant operational challenges in the year, but are positioned to complete in 2014.

We also continued our highly successful campaign to reunite customers with their unclaimed savings and life policy benefits, meaning that we have now reallocated £3.1 million of previously unclaimed assets, over 50% of our unclaimed asset book. Meanwhile our Keep it, Will it, Flag it initiative continues to help reduce the instances of unclaimed assets in the future by raising awareness of the importance of keeping policy documents safe, referencing policies in wills and making next of kin aware of any policies held.

In an environment of continued record low interest rates, 2013 also saw us continue our discretionary cap on the charges made to our Deposit Fund customers, ensuring that we capped the impact that charges had on their returns at a maximum of £50.

sales and distribution

The impacts of the new regulatory regime are still working their way through the market place and we have already seen many of our larger competitors begin to reconsider the products that

strategic, operating and financial review (cont.)

Engage with your Community enabled us to **support six customer-led projects across the UK, from food banks to community gardens, with each receiving funding of up to £5,000 each.**

they provide and the distribution channels that they use. We monitor our product offer and the routes to market in order to ensure that we offer increasingly relevant and competitive products for our customers, and we anticipate introducing further new products to market during 2014 to strengthen our position.

Whilst we have continued to deliver year on year growth in core products, we aspire to growing our new business significantly in the coming years. In response, we have taken steps in the second half of 2013 to strengthen our sales resources with the appointment of a new Executive Sales Director to the executive team, as well as growing our field sales capacity, all designed to support further increased growth in new business in 2014.

In what is now our seventh year of partnership with Clydesdale Bank and Yorkshire Bank, we continued to successfully deliver savings and protection plans to customers across their UK branch network. For the last three years we have worked in partnership with Benenden Health, providing over 15,000 of their customers with health cash plans. However, during 2013 it became clear that the strategies of our two businesses were no longer aligned and it would be in both parties' interests to cease the arrangement. After three years of working together, we have agreed to an amicable parting with Benenden Health and we will cease to manage their health cash plan book, most likely towards the end of 2014.

social, community and people

Engage Mutual has had a very close relationship with The Steve Prescott Foundation charity for a number of years and in September 2013 we sponsored the Steve Prescott Kilimanjaro Challenge, which saw a group of 12 intrepid explorers climb Africa's tallest mountain, raising much needed funds for the Christie Hospital and Try Assist charities in the process.

It was with great sadness that we learnt that Steve passed away on Saturday 9 November 2013. Steve was a close friend of the business and he is sadly missed, but his legacy lives on and we will continue to support the great work of the Steve Prescott Foundation in 2014.

Over the years we've lent considerable support to local and national charities, sports clubs and community projects that really matter to our customers. Engage with your Community – an initiative set up to give our customers' local community groups the chance to receive funding of up to £5,000 for a specific project - enabled us to support six customer-led projects across the UK, from Food Banks to Community gardens, along with practical advice and support from us, all of which delivered real benefits to their local communities. At the same time, Engage with your Club, designed to help amateur rugby league clubs hold action events in their local communities to improve their facilities, helped 56 amateur rugby league clubs during 2013. Those events saw over 1,700 volunteers turn out to support their community clubs, and clocked up over 9,000 volunteer hours.

At Engage we are extremely proud of the customer service our teams provide, which is only possible by listening to customers and investing in the capability of our people. It's an honour therefore to see those efforts recognised again in 2013 for our outstanding commitment to our people with the award of Investors in People (IIP) Champion status, making us one of only a handful of businesses in our region to have received this award.

To help support and encourage our teams in their own fundraising activities, the last Friday of each month is dedicated to a colleague who is fundraising for a charity close to their hearts. Fundraising Fridays began in May 2013 and so far, our Harrogate team has provided much needed support for a variety of local, regional and national charities.

We spend a great deal of time working to ensure that Engage Mutual is a rewarding and enjoyable place to work and our annual staff engagement survey clearly shows that the vast majority of our staff feel the same. Our overall staff engagement score was a highly enviable 74% in 2013, putting us in the top 15% of companies globally, a great achievement of which we are extremely proud.

financial review

In 2013 our priority has been to continue to maintain and enhance the financial stability and capital strength of the Group, whilst both refocusing and investing in our operating processes to support our strategic priorities. We recognise that we need to develop a stronger reputation, increase our market share by developing a broader product offer, and deliver genuine benefits of belonging to a mutual such as the Engage Foundation.

Our focus is designed to ensure that not only are we able to grow, but that in parallel we are able to reshape the Group to reduce and ultimately eliminate our reliance on a number of products that the Group no longer actively offers for sale.

Our financial results for the year are described in more detail below. As always, in managing your business we have endeavoured to strike the right balance between maintaining the Group's long-term financial and capital strength, and maximising the immediate financial benefits for customers through, for example, insurance benefits and the level of bonuses on savings policies.

capital strength

Our capital position continues to be strong and customers can be confident that the Group is well capitalised and adequately funded to meet its financial commitments. Capital as measured by the Group Fund for Future Appropriations (FFA) stands at £95.8 million (2012 – £83.9 million). The capital growth is primarily due to positive market and economic impacts, which has supported our investment in new business growth.

Capital requirements are analysed further in note 1 to the accounts, which shows that at 31 December 2013 the Group held:

- £41.6 million of excess capital over its regulatory requirements for the Non Profit Fund, representing 4.9 times the minimum capital requirement;
- £20.9 million of excess capital over its regulatory requirements for the open Engage Mutual With Profits Fund 1, representing 5.4 times the minimum capital requirement; and
- £11.4 million of excess capital over its regulatory requirements for the closed Engage Mutual With Profits Fund II, representing 3.4 times the minimum capital requirement

with profits

The Group operates two With Profits Funds – With Profits Fund I, that we have operated since 2003, and With Profits Fund II that we have operated since 2010 as part of the acquisition from Ecclesiastical Life Limited. Each fund is separately ring fenced for the exclusive benefit of its own members.

Engage Mutual With Profits Fund (With Profits Fund I)

At 31 December 2013 the fund held assets of £72.8 million. Investment returns for the fund were shared amongst its customers as set out in the fund's Principles and Practices of Financial Management (PPFM), with the majority of customers receiving an asset share growth of 6.5% in the year.

As part of the fund's bonus declaration, regular bonus rates were unchanged at current levels. Across most classes final bonus rates have remained unchanged, or increased, reflecting the positive investment returns of 6.5% in 2013. Currently no market value reduction factors are being applied.

Owing to the strong financial position of the fund, the Board has agreed to continue to use a proportion of the surplus assets in the fund to improve pay outs. Claims arising during 2013 on policies not already benefiting from guarantees received a typical uplift of 12.5%, and as a result, in 2013 we paid over £0.5 million to members in excess of the payments that they would otherwise have received.

We are continuing to enhance payments to members in 2014.

strategic,operating and financial review (cont.)

During 2013, 1,742 new policies were written in the fund, and we continue to write this new business profitably. We therefore have no plans to close the fund to new business.

Engage Mutual (ELL) With Profits Fund (With Profits Fund II)

At 31 December 2013 the fund held assets of £82.4 million and made an overall return of 4.7% during the year. Regular bonus rates remain unchanged for regular premium life and pensions business, but have reduced on single premium bonds. For Deposit Administration contracts, regular bonus rates were increased on some schemes, but reduced on others where the guaranteed benefits are already high.

Final bonus rates and market value reduction factors were set so that pay-outs continue to be consistent with the target ranges set out in the fund's PPFM.

The fund is closed to new business and in October 2011 a formal run-off plan was agreed with the Financial Services Authority (now the Prudential Regulation Authority and Financial Conduct Authority). This governs how, over time, the excess assets in the fund will progressively be distributed to customers via enhanced claims pay outs. The precise level of enhancement depends on both individual customer circumstances and the ongoing investment performance of the fund, but as a guide we expect a typical enhancement to be around 9% for policies not already benefiting from guarantees. As a result, in 2013 we paid over £1.1 million to customers in excess of the payments that they otherwise would have received.

£41.6 million

of excess capital over its regulatory requirements for the Non Profit Fund, representing **4.9 times minimum capital requirement**

life insurance business

Life insurance is a mature part of our business, and we plan to diversify and grow it in the future by increasing sales made through intermediaries and developing new distribution channels. In 2013 we extended our sales capability focusing on developing our existing relationships and initiating a number of new distribution arrangements with independent financial advisers, brokers and sales partners.

We continue to build on the strength of our Over 50s Life Cover offering and during 2013 sales of this product grew by 5%. Sales of other life insurance products in historic markets, most notably with profits policies, declined in 2013 with the result that new life insurance sales generated an annual premium income of £3.9million (2012 £4.3 million).

savings business

Investment market conditions began to stabilise in 2013, with the value of equity stocks improving, albeit interest rates remained consistently low. This was reflected in policy performance.

Customers choosing policies linked to equities in 2013 have generally experienced an improvement in the value of their policy with our main equity fund delivering an investment rise of 15.8%.

Child Trust Fund customers saw a further year of investment gains of 14%. Our customers continued to make contributions to their policies throughout the year and as a result the fund grew 19% over the year to £210.2 million.

We have continued to work on behalf of our customers investing in deposit policies. We aim to maximise returns whilst being conscious of the credit rating of the counterparties with whom we invest, and we ensure that deposits are spread across a number of different providers.

This year the overall gross return of 1.6% represents a premium of 1.1% above base rate.

Given the ongoing low interest rate environment, for the third successive year we continued to cap the charges we make for managing deposit policies at a maximum of £50. Typically, this means that any amounts invested in a deposit policy in excess of £10,000 incur no additional charge. Overall, this benefited members by an additional £45,000, reducing the total charges paid by members in 2013 by 8%. Decisions regarding future charge caps will continue to be made each year, based on affordability and the prevailing rates at the time.

health business

Our health business remains a strategic growth area for us and we continue to invest in developing health products and services. The short-term impact of that investment presents as losses, reflecting the natural profit profile of a general insurance business in development. In 2013 we continued to grow our unique One Fund health cash plan product for corporate customers and our retail health cash plan as we explore new and innovative product opportunities.

premiums and claims

In aggregate, premiums received across all of our business lines fell by 4% to £55.4 million. Within that total, the largest fall was in Investment premiums. Life insurance premiums increased by 2% to £33.8 million and Health insurance premiums reached £7 million, a growth of 1%.

Aggregate claims increased by 10% to £95.0 million due to the run off of With Profits policies and higher health insurance claims expected in relation to higher business volumes.

long-term business

Our long-term business, which includes life insurance and investment business, ended the year with a net credit to the Fund for Future Appropriations (FFA) of £12.8 million, primarily due to positive market and economic impacts offset by strategic and new business investment.

general insurance business

As noted above, our health business is relatively immature and is generating losses in the short-term as it absorbs fixed costs and we establish its market position. We recorded a loss in 2013 of £2.3 million.

other business

Despite the Government's closure of the scheme, our Child Trust Fund business continues to prosper. Funds under management grew to £210.2 million with income up 20% to £2.9 million. Given the closure of the scheme we expect modest but positive growth in income

strategic,operating and financial review (cont.)

going forward.

Our Funeral Funding Option product earned us £1.1 million in commission income from third parties during 2013.

The Society's pension scheme surplus stands at £4.4 million; we continue to adopt an accounting approach consistent with the prior year and do not take credit for that surplus in the Group accounts.

costs and infrastructure

Net operating expenses were £20.4 million, broadly level with the previous year. This reflects the continual drive for efficiency both in administering acquired businesses and simplifying our existing processes. We also increased the cost efficiency of our new business distribution.

risk management

Monitoring and management of risk, and particularly its impact on capital resources, is fundamental to our business. We monitor our capital adequacy on two distinct bases:

statutory reporting

The accounts are presented on the basis of UK GAAP for insurance companies, which require us to reserve for risks and to make provision in line with standard stress tests to ensure that our capital resources are adequate. The statutory reserves contain an in-built margin of prudence to support the various risks that we manage.

A separate return is also prepared and submitted by all Friendly Societies and Insurance Companies to the Prudential Regulation Authority (PRA), our lead regulator, which documents a detailed analysis of our results. We regularly monitor the development of these results and the level of capital coverage noted above in our internal management reporting.

realistic reporting

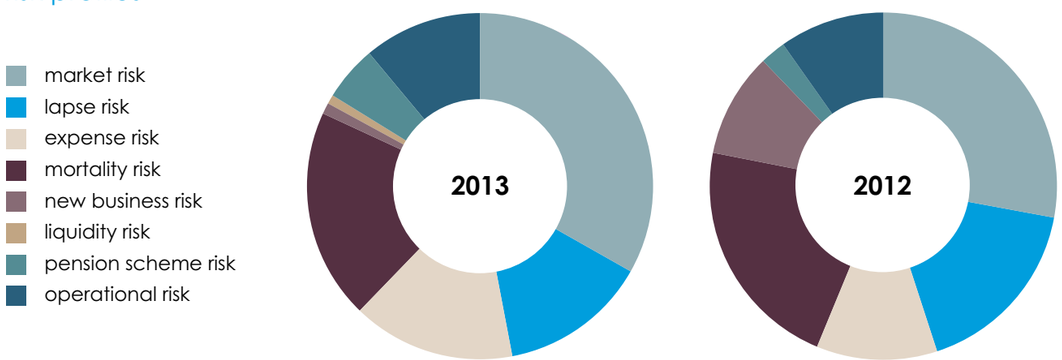
Developments in regulatory reporting have introduced 'realistic reporting', which instead of standard stress tests uses the best estimates of management to value future cash flows. We then apply a range of different stress tests and scenarios to evaluate the amount of additional risk capital that we should hold in the event that any of these risks were to materialise in practice.

This risk evaluation process involves management consideration of the nature of the risks and how they may apply within our business. We further test our evaluation by identifying potential situations which could cause our business model to fail. This provides useful insight into our risk profile and so allows the Board to set appropriate levels of risk appetite and agree appropriate management actions if individual or combinations of risk events were to occur.

Our risk assessment seeks to ensure that there is adequate capital, calculated on a best estimate basis, to meet the risks, or combinations of risks, faced by our business which have a greater than one in two hundred chance of occurring over the next twelve months.

The key risks to which we are exposed and their current relative impact on our realistic capital are represented below. The chart illustrates how our risk profile has remained relatively stable over the year, which is consistent with our business activity over 2013.

risk profiles



risk framework

The Board is responsible for ensuring that we have an appropriate risk reporting and control framework to manage and develop our business. This is set out in more detail later within the Corporate Governance section of this report. During the year a Board Risk Committee and an Executive Risk and Governance Committee were established. The Board receives a regular risk report from the Risk Committee which tracks the status of current risks and the effect of mitigating management actions.

Management control is delivered through a number of committees which report into the Executive Committee. These sub-committees manage business performance and risk within agreed terms of reference. In this way, they provide a clear and visible internal management framework to ensure that we monitor and manage our risks, operate efficiently and effectively, comply with regulation and treat our customers fairly.

We continue to work on our response to the new Solvency II European Directive which is now due to come into force on 1 January 2016. When these regulations are implemented they will have wide ranging implications for management practice, particularly for risk and financial reporting.

Our plans to manage our business and risk in a way that is not just compliant with Solvency II, but also maximises the commercial benefits that the new regulation brings, are progressing in accordance with our defined timelines. Based on current proposals, we are confident that we will meet the Solvency II capital requirements.

We will also seek to leverage the existing investment we have made in governance and reporting systems to fully embed risk management, evaluation and reporting in line with the new requirements.

executive committee

All Executive sub-committees report into the Executive Committee which is chaired by the Chief Executive. The Executive Committee includes the Group's Executive Directors, the Actuarial Function Holder, the Group Secretary & Compliance Officer, and other Executives with functional responsibility for managing the society. The meeting is attended in part by sub-committee Chairs, the Corporate Risk Officer and the Internal Audit Manager.

The Executive Committee has day-to-day authority for managing the affairs of the Group, including risk management and delivery of business plans and strategy. The Board and committees receive regular management information that takes into account all aspects of our business. The Board formally reviews management plans and capital forecasts twice a year, to ensure that financial projections reflect adequate capital to service our current business and to meet development plans.

financial reporting

Financial reporting standards, particularly for groups such as ourselves who undertake relatively complex insurance and investment activities on behalf of members, continue to change rapidly. Whilst the increased levels of standardisation and enhanced levels of disclosure are generally positive, one unfortunate side effect is that financial statements are becoming increasingly difficult for the lay person to interpret.

We currently present our accounts in line with UK generally accepted accounting practice (UK GAAP) for insurance companies. However, a new suite of UK GAAP standards has been issued which will apply to the Group from 1 January 2015. The Group has the option, at that time, to adopt the new standards, or present accounts in line with International Financial Reporting Standards (IFRS). We remain mindful of the need to make any transition in a way that is both cost effective and as meaningful as possible for members, and are assessing the various options carefully. We do not plan to make any changes in 2014 under the early adoption provisions of the standards.

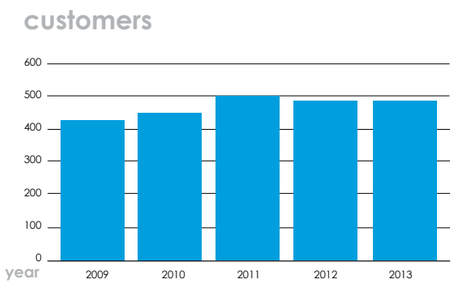
looking ahead

The Group continues to be in a strong financial position. We will continue to invest in strategic developments as we aim to build a business that is increasingly better equipped to meet the insurance needs of members. Our vision is to build a thriving and enduring mutual – serving, empowering & representing our customers.

financial performance for the year ended 31 December 2013

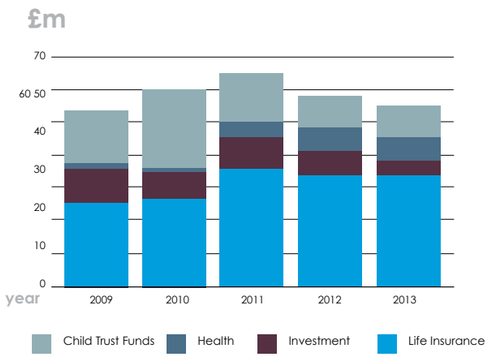
The following graphs are the main key performance indicators used to manage the business.

group customers



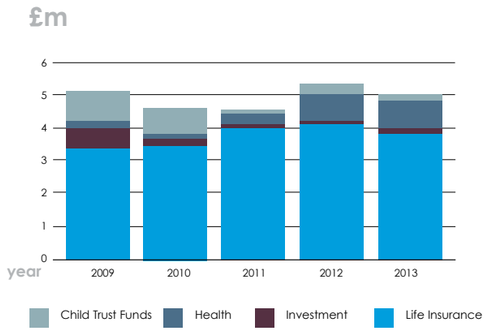
Customer numbers are broadly stable at 496,752.

premiums from customers



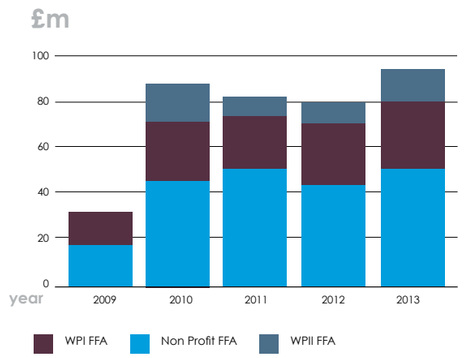
Growth in Over 50s and Health premiums was offset by an expected reduction in investment premiums. Overall premiums of £55.4 million are 4% lower than the prior year.

new business performance



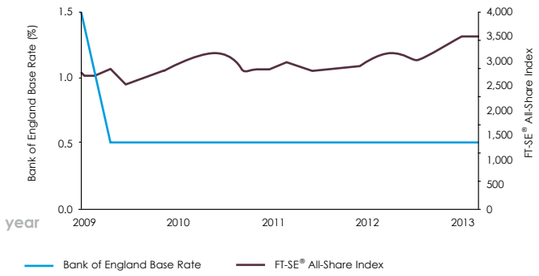
New business sales fell by 6% to £5.0 million overall, due to a decline in historic product markets. Sales of our core Over 50s Life Insurance product grew 5% year on year to £3.4 million, and our health insurance product sales grew 36% to £0.8 million.

group fund for future appropriations



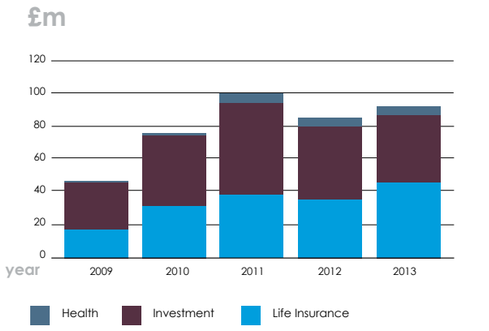
Overall the fund for future appropriations, representing funds not yet allocated to members, grew by 14% to £95.8 million, primarily due to economic factors. We continue to hold excess capital more than three times that required by the regulator.

FT-SE® all-share index and Bank of England Base Rate



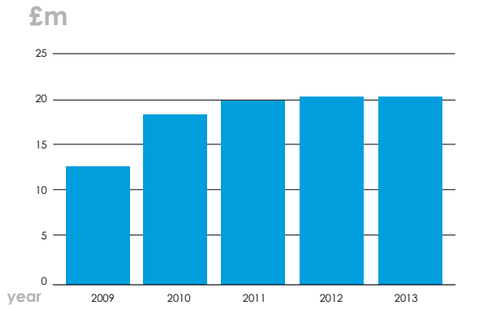
Equity markets were strong in 2013, with the FT-SE® All-Share Index ending the year up 16.7%. The Bank Of England Base Rate was unchanged over the year at 0.5%.

claims paid to customers



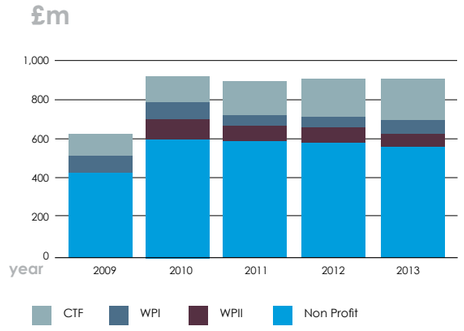
Claims paid to our customers totalled £95.0 million, comprising of £46.5 million of life insurance benefits, £43.0 million of maturing investment policies and £5.5 million of health benefits.

group expenses



Group expenses of £20.4 million were in line with 2012, highlighting our continued focus on controlling expenditure.

group assets



Group assets remained stable at £933 million. This comprises £210 million of CTF assets under management and £723 million assets recorded on the Society balance sheet.

your board of directors

David Robinson – MA FFA (64)
Chairman

David joined the Board in August 2010 and was appointed Chairman in September 2010. He has extensive financial services experience, specifically in the mutual insurance sector. David is convinced that well-governed and well-managed mutual organisations have an important role to play in serving the needs of a wide range of customers. He is passionate about delivering excellent customer experiences and believes that the right people and culture can deliver exceptional results for customers.

A Fellow of the Faculty of Actuaries, David has over 40 years' experience in financial services, which has seen him become founding Chief Executive of insurance business Bright Grey as well as having held senior roles at Scottish Provident and Royal London.

David is a member of the Court of Heriot Watt University, Edinburgh and is also Chair of Trustees of charity, Smalls for All.

Christina McComb – BA MBA (57)
Vice Chairman

Chris joined the Board in May 2005 and was appointed Vice Chairman in 2009. She has wide ranging experience of advising and investing in smaller companies, having spent 14 years at leading venture capital group, 3i.

Chris also has experience of the public sector, having been a Director of the Shareholder Executive from 2003-2006, managing the Government's shareholder interests in a number of public-owned enterprises and latterly as Director and Head of Investment at Partnerships UK Plc.

She is currently Senior Independent Director of the British Business Bank, a non-executive director of C5 Capital Ltd, Baronsmead VCT 2, Nexeon Limited and Standard Life European Private Equity Trust plc, and a Trustee of the Land Restoration Trust.

Peter Burrows – BA ACA (45)
Chief Executive

Peter joined the Board as Finance Director in November 2010 and was appointed as Chief Executive in August 2013. He is a Chartered Accountant with 20 years' experience gained in a combination of executive management and consulting roles, with a passionate belief in the benefits that mutuality brings both to members and wider society.

Prior to joining Engage Mutual, Peter held a number of senior finance positions with Aviva plc, both in the UK and in Europe. Before that he held senior management positions with Ernst & Young, where he advised financial services businesses on financial, risk management and governance matters.

He is a Director of the Association of Financial Mutuals and also a governor of York College, where he chairs the Finance & General Purposes Committee and also serves on the Remuneration and Search & Governance committees.

Paul Chandler – MA MBA (52)

Paul joined the Board in October 2012, bringing 20 years' experience as a Chief Executive and a strong profile as a leading advocate and exponent of fair trade. He is particularly interested in promoting ethical practices and mutuality in the financial services sector.

From 2001 until 2013 Paul was Chief Executive of Traidcraft, the UK's leading fair trade organisation. Prior to that he was Chief Executive of SPCK, the Christian publisher and bookseller, having previously spent some of his early career with Barclays Bank.

Paul is the Chair of the William Leech Foundation, a non-executive director of Shared Interest (the fair trading cooperative lending society), trustee of the County Durham Community Foundation, Chair of Durham Cathedral and a fellow of St Chad's College Durham.

Karl Elliott – BA (41)
Marketing Director

Karl became Marketing Director of the Society in October 2004 and was appointed to the Board in December 2007. Having worked in financial mutuals for over twenty years, Karl believes that a mutual business should put customer benefit, participation and a sense of collective community at the heart of all that it does.

He joined the Society in 1999 and carried out a number of product, marketing and distribution roles within the marketing team, including the launch and development of the Engage Mutual brand.

He represents the Society on a number of industry groups including the Association of Financial Mutuals Communications Group.

Caroline Fawcett – BSc DipM MCIM (55)

Caroline joined the Board in May 2013. She is a recognised customer experience expert, designing and leading customer-driven strategic change programmes that help organisations to increase their customer focus. She is currently Managing Director of consultancy firm Customer Experience First, which provides support for the public and commercial organisations.

Caroline built her career in marketing in the financial services industry in both the UK and the USA. She was Customer Experience Director at Legal & General plc for many years and more recently has held Customer Director roles at the Department for Environment, Food and Rural Affairs and for the international outsource organisation, Serco. Caroline is a non-executive director for a leading mental health and learning disability NHS Foundation Trust.

Andrew Gosling – MA FCA (58)
Senior Independent Director

Andrew joined the Board in March 2011 as a non-executive director. He is a Chartered Accountant with over 35 years' experience in the financial services sector as a Director, auditor and regulator. He is a committed supporter of mutuality and believes that mutuals are vital in providing choice to the consumer.

Until his retirement in 2010, Andrew was Finance Director of Yorkshire Building Society, where he also sat on both the Risk and Asset & Liability Committees. Before that he was a partner in Ernst & Young, leading the firm's financial services practice in the North of England. He also spent two years at the FSA, supervising some 25 building societies through the downturn of the 1990s. Andrew is currently a non-executive director of Darlington Building Society and Vanquis Bank.

Nigel Masters – BSc FIA (61)

Nigel joined the Board in June 2012 as a non-executive director. He is a Fellow of the Institute and Faculty of Actuaries with over 35 years' experience in financial services. Nigel's focus is to promote the enhancement of members' benefits and services while maintaining the Society's strong capital base.

Nigel has held a number of senior actuarial positions, including Group Chief Life Actuary for Zurich Financial Services and partner in the actuarial consulting practice at PricewaterhouseCoopers. He was previously President of the UK actuarial profession and has represented the profession on various European and international bodies.

He is a non-executive director of Wesleyan Assurance Society and Director of NMActuarial Limited.

how we manage the business

The Directors have pleasure in presenting their Annual Report, together with the financial statements for the year ended 31 December 2013.

business objectives

The Board is committed to building a thriving and enduring mutual – serving, empowering and representing our customers.

subsidiary companies

The role of our subsidiary companies play an important role in building an enduring and thriving mutual – serving, empowering and representing our customers :

- Engage Mutual Health is the provider of our health cash plan and medical insurance business
- Engage Health Holdings Limited is the holding company of Engage Mutual Health
- Engage Mutual Funds Limited is the provider of our stakeholder child trust fund product
- Engage Mutual Administration Limited, our administration services subsidiary, provides services to the Society and its operating subsidiaries
- Engage Mutual Services Limited, our marketing services subsidiary, is an introducer of third party products and services and provides marketing services to the Society and its operating subsidiaries
- Engage Foundation (established 17 December 2013) is the provider of additional benefits to customers and their families beyond their contractual policy terms and conditions

The Board is committed to the ongoing development of **Engage Mutual as a leading friendly society.**

The role of the subsidiaries and their impact on the finances of the Society is such that we present consolidated accounts for the Group.

business review

Key business developments and the future outlook for the business of the Society and its subsidiaries are reviewed by the Chairman and Chief Executive on pages 6 to 11 and in the Strategic, Operating and Financial Review on pages 12 to 23. The Strategic, Operating and Financial Review identifies and explains the Group's Key Performance Indicators and sets out how it has performed against each during 2013.

The Directors are of the opinion that all activities performed during the year by the Society and its subsidiaries have been carried out within their respective powers.

principal risks, uncertainties and going concern

The principal risks and uncertainties faced by the Group and our approach to managing them are set out in note 1.

The Board has reviewed the summary of the Guidance for Directors published by the Financial Reporting Council and concluded that in the light of:

- the published year end position on statutory solvency
- available financial resources in liquid form
- the capital projections for the Group within its agreed business plans
- the results of our Individual Capital Assessment

there are no material uncertainties that may cast significant doubt about the Group's ability to continue as a going concern.

staff

The average number of staff (including Executive Directors) employed by the Group totalled 203. The aggregate remuneration paid to Directors and staff employed by the Group, during the year, amounted to £9.4 million including pension and National Insurance contributions (2012 £8.9 million). All of our staff are employed by our Group administration services subsidiary, Engage Mutual Administration Limited.

The Group's management meets employee representatives regularly to discuss a wide range of topics, through its staff forum. Communication with and between all employees is subject to regular review and includes bi-monthly presentations, team briefings and informal meetings with the Chief Executive and senior staff.

Engage Mutual has an equal opportunities policy for recruitment and is committed to the ongoing development of its staff. The Society has been officially recognised as an 'Investor in People' since 2001 and in 2013 was awarded Investor in People Champion status.

Our staff are key to our operations and the Group supports the continued learning and development of its staff through regular analysis of training needs, an annual staff satisfaction survey and by the provision of a broad range of training opportunities.

board of directors

A list of Directors who held office during the year appears within the Society Information section on pages 24 and 25.

Caroline Fawcett was appointed as a Director on 28 May 2013 and being eligible, offers herself for election to the Board of Directors at the 2014 AGM.

Peter Burrows, Karl Elliott, Christina McComb and David Robinson retire in accordance with the Society's rules and the Friendly Societies Act 1992 and, being eligible, offer themselves for re-election.

Christina McComb has now served the Society for nine years, but the Board believes that her skills and experience are such that they wish her to continue as a Director beyond the normal nine year maximum term.

No Director had any interest either in the shares of the Society's subsidiary companies or in any contract of significance, with the Group or any of its subsidiary undertakings, at any time during the financial year.

The Society maintains Directors' and Officers' liability insurance cover in respect of legal action against its Directors and officers. The insurance cover was reviewed and renewed in 2013.

The Directors in office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Group's auditor is unaware.

membership

Membership of the Society as at 31 December 2013 stood at 246,925 (2012: 254,979). The total number of customers as at 31 December 2013 was 496,752 (2012: 498,764).

complaints policy

We aim to deliver a high standard of service to our customers. If any customer believes that we have failed in this aim, they have recourse to our complaints procedures. We have documented procedures for the handling and recording of complaints. We deal with all complaints with due care, ensuring that they are thoroughly investigated.

The Board of Directors regularly reviews the number and type of complaints received in order to monitor that complaints are properly dealt with and corrective action is taken to prevent recurrence.

Senior management deals with serious complaints. In the unlikely event that a complaint cannot be resolved to the customer's satisfaction, the customer will be made aware of the option to appeal to the Financial Ombudsman Service.

diversity

The Board gives consideration to all aspects of diversity, including gender, on the Board although it has adopted the principle that all appointments should be made on merit. For this reason, the Board has not set any measurable objectives although this will be kept under review.

The percentage of females on the Society's Board at the date of this report is 25%. In addition, 37% of the Executive team is female. Within the Management team, who report directly to a member of the Executive team, the percentage of females is 69%.

The Society takes into account diversity at all levels of recruitment and encourages staff through various initiatives, including taking on non-executive roles, to enable staff to gain experience of Board roles.

how we manage the business (cont.)

supplier payment policy

It is the Group's policy and practice to settle invoices within 30 days of receipt, unless specifically agreed otherwise in advance with suppliers.

pensions arrangements

We are committed to assisting our staff to make adequate provision for their retirement.

For all employees, we have a Defined Contribution arrangement in place whereby the Group matches the employee's contributions with a maximum corporate contribution of 10% of salary.

Our Defined Benefit scheme closed to new members in March 2001 and to further accruals from 31 December 2012. Members of the scheme have been offered membership of the Society's Defined Contribution scheme.

The Directors continue to work with the Trustees to manage the Defined Benefit pension scheme investment policy and to maintain the financial strength of the fund. This ensures that the scheme remains in a position to meet its obligations going forward in a manner which should not place a material financial strain on the Group.

environmental, social and community issues

Environmental, social and community issues impacting on the business of the Society and its subsidiaries are detailed in the Strategic, Operating and Financial Review starting on page 12.

We take our role as a socially responsible organisation very seriously, be that in the way we treat our employees or in the role we play helping and protecting the environment in which we work and live.

We were delighted to be recognised as an IIP Champion in 2013, reflecting the importance we place on our colleagues' wellbeing and personal development in the workplace. In 2013 we redoubled our efforts to increase recycling, reduce paper consumption and cut down energy use within the organisation, as well as continuing to support the Cycle to Work scheme. Our community work has seen us support local charities and customer initiatives including community gardens, food banks, school outdoor learning gardens and a wildlife trust, all of which has made a positive contribution to our working environment and wider communities.

In 2013 we donated in excess of £35,000 to charities, which included donations to a local charity, Saint Michael's Hospice as well as to The Steve Prescott Foundation. In addition, we meet all the costs of maintaining the grounds that we share with Saint Michael's Hospice.

Our staff support several charities and have donated to and raised money for, amongst others, Saint Michael's Hospice, Harrogate Homeless Project, Comic Relief and BBC Children in Need during 2013. Total money raised by staff during the year was in excess of £7,000.

appointment of auditors

A resolution to re-appoint KPMG Audit Plc as statutory auditors will be proposed at the forthcoming Annual General Meeting.

Our policy on rotation of auditors is such that audit services are formally reviewed at least every five years. KPMG were appointed in 2012. The existing auditors are permitted to be re-appointed as part of this process.

By Order of the Board
Andrew Horsley
Secretary
20 March 2014

In 2013 we donated in excess of £35,000 to charities, which included donations to local charity, Saint Michael's Hospice as well as to The Steve Prescott Foundation.

corporate governance

The Board is accountable to the Society's members for the operation of the Group and to ensure that **it is run in the best interests of the members.**

The Board is also mindful that the effectiveness of the Board is vital to the financial strength and future success of the Society.

To ensure that the Board manages the Society in a prudent and effective manner and that it manages the risks that the Society faces, it is committed to complying with good practice in corporate governance.

The Board is of the view that, to comply with good practice in corporate governance, it should aim to adhere to the principles and provisions of the UK Corporate Governance Code annotated by the Association of Financial Mutuals to cover mutual insurers ('the Code').

It is our policy to observe the Code wherever appropriate for an organisation of our size, status and aspiration or to explain clearly why we feel any deviation from the Code is acceptable or necessary. The Board considers that it complies with all aspects of the Code unless the contrary is stated within this report.

As highlighted last year, the UK Corporate Governance Code introduced a requirement that Directors of larger organisations be subject to annual election by members. The Board has considered this provision in respect of the 2014 AGM and has agreed that this should not be brought in at that time. The Board is concerned that in extreme circumstances this provision could have implications for the stability of the Society which would not be in the best interests of members. The Board applies principles of good governance by adopting the following procedures:

- the Board meets a minimum of six times a year for Board meetings and, in addition, meets at least twice a year for a detailed review of the Group's strategy. The attendance record of each Director at those meetings and at relevant committee meetings is set out on page 31

corporate governance (cont.)

- the non-executive directors are responsible for bringing independent judgement to Board debate and decisions, and for constructively challenging the Executive Team which is made up of the Executive Directors and other Executive Managers
- the non-executive directors meet without the Executive Directors present at least annually
- the Board's principal role is to focus on the Group's strategy and ensure that the necessary resources are in place for the Group to meet its objectives and that financial control and risk management procedures are robust. In particular, its role is to provide general direction to the organisation and to safeguard the interests of members
- the Board maintains a schedule of retained powers relating to approval of the strategic aims of the Group as well as approval of policies and matters which must be approved by the Board under legislation and the Society's rules
- to ensure that the Board functions effectively, all Directors receive accurate, timely and clear information and it is the responsibility of the Chairman to ensure that this is periodically reviewed. As well as circulating papers as hard copies, the Board has access to its own secure website where papers are available together with additional supporting material, which acts as a library of papers for Directors
- there is regular communication between the Directors, the Chairman, the Chief Executive and the Group Secretary between meetings. When a Director is unable to attend Board or committee meetings, issues can be raised with the relevant Chairman
- the Chairman also ensures that, on appointment, non-executive directors receive a comprehensive tailored induction programme on the Group's business and regulatory environment. All non-executive directors update their skills, knowledge and familiarity with the Group through meetings with the Executive and employees and through attending relevant external courses. Individual training requirements for non-executives are discussed during the performance evaluation process
- each Director has access to independent professional advice, where they judge it necessary to discharge their responsibilities as Directors and have the benefit of appropriate liability insurance cover at the Society's expense
- all Directors have access to the advice and services of the Group Secretary, who is professionally qualified and is responsible for ensuring the Board procedures are complied with and advising the Board, through the Chairman, on governance matters. The Society's rules provide that the appointment and removal of the Group Secretary is a matter for the Board
- the Board currently consists of two Executive Directors and six non-executive directors. The Board appointed Peter Burrows as Chief Executive on 19 August 2013, following the resignation of Andrew Haigh at the end of 2012.

non-executive directors

In the opinion of the Board, each non-executive director, including the Chairman, is independent in character and judgement. The Board has adopted a policy that no non-executive director will normally serve the Society for longer than 9 years. The Society has appointed Andrew Gosling as Senior Independent Director. The Senior Independent Director will be available to members, if they have concerns which contact with the Chairman, Chief Executive or Finance Director has failed to resolve or for which such contact is inappropriate.

chairman and chief executive

The roles of the Chairman and Chief Executive are held by different people and are distinct in their purpose. The Chairman is responsible for leadership of the Board and ensuring that the Board acts effectively. The Chief Executive has overall responsibility for managing the Society and its subsidiaries and for implementing the strategies and policies agreed by the Board.

attendance of directors at board and committee meetings

Set out below are details of the Directors during 2013 and their attendance record at Board meetings and relevant committee meetings in the year.

Board Meetings	David Robinson	Christina McComb	Peter Burrows	Paul Chandler	Karl Elliott	Caroline Fawcett	Andrew Gosling	Peter Mason	Nigel Masters
HFSL (14)†	14	14	14	14	13	10 of 10	14	n/a	14
EMFL (1)*	1	1	1	1	0	n/a	1	n/a	1
EMAL (1)**	1	1	1	1	0	n/a	1	n/a	1
EMSL (1)***	1	1	1	1	0	n/a	1	n/a	1
EMH (1)****	1	1	1	1	0	n/a	1	n/a	1
EHHL (1)*****	1	1	1	1	0	n/a	1	n/a	1
Committee Meetings									
Audit (4)	n/a	4	n/a	n/a	n/a	1 of 1	4	n/a	4
Finance (5)	5	n/a	5	n/a	n/a	n/a	n/a	n/a	5
Corporate Governance & Nominations (2)	2	2	1 of 1	2	n/a	n/a	2	1 of 1	2
Remuneration (5)	5	5	n/a	5	n/a	1 of 1	n/a	4	3 of 3
Risk (1)	n/a	n/a	n/a	1	1	n/a	1	n/a	1

* Engage Mutual Funds Limited.
** Engage Mutual Administration Limited.
*** Engage Mutual Services Limited.
**** Engage Mutual Health.
***** Engage Health Holdings Limited.
† Homeowners Friendly Society Limited.

performance evaluation

In 2011 the Board engaged an independent external organisation, Boardroom Review, to conduct a Board effectiveness review. The process produced a number of areas for consideration and improvements have been identified and implemented.

The Group has a formal performance evaluation system for all members of staff including the Executive Directors. The Chief Executive appraises the Executive Directors on their performance and the Chairman undertakes an appraisal of the Chief Executive.

A performance evaluation system for non-executive directors has been established. In 2013, the appraisal of non-executive directors took the format of a formal appraisal of each individual director by the Chairman. This procedure identifies any individual and Board training requirements and provides evidence for the Board to decide whether to recommend to members that a director should be re-elected.

The Senior Independent Director also meets with the Chairman to evaluate the Chairman's performance. A meeting of the non-executive directors is also held, without the Executive Directors present, to discuss collectively the performance of the Executive Directors.

appointments to the Board and re-elections

The appointment of new Directors is considered by the Corporate Governance and Nominations Committee (see page 33) which makes recommendations to the Board. In normal circumstances an external agency is engaged to assist in the recruitment of non-executive directors once a vacancy and the required skills and experience have been identified. Any such vacancy is advertised on the Society's website to enable suitably qualified members to apply.

Under the Society's rules, all Directors are subject to election by members at the AGM following their appointment (or at the AGM in the following year if the Director is appointed by the Board in the period between the beginning of the year and the AGM). In addition, all Directors must receive approval from the Prudential Regulation Authority and the Financial

Conduct Authority as an Approved Person, in order to fulfil their controlled function as a Director.

On 28 May 2013, Caroline Fawcett was appointed to the Board. Caroline will be put forward for election by members at the 2014 AGM.

Under the Society's Rules, Directors have to submit themselves for re-election at least once every three years. Given their particular expertise, experience and performance to date, the Board recommends David Robinson, Christina McComb, Peter Burrows and Karl Elliott be put forward for re-election by members. The Board acknowledges that Christina McComb has served the Society for nine years, but her skills, experience and contribution to the Society to date are such that they wish her to continue as a Director beyond the normal nine year maximum term.

Copies of the letters of appointment of the non-executive directors are available for inspection at our Head Office and can be viewed by contacting the Group Secretary.

board committees

The Board has established a number of committees which have their own terms of reference. Each committee is properly authorised under the rules of the Society to take decisions on behalf of the Board within the guidelines and delegations laid down by the Board. The Board is kept fully informed of the work of the committees. Any issues requiring resolution will be referred to the Board. Details of the Board committees are set out below, and their membership in 2013 is set out on page 2. The Chairman of each committee reports to the subsequent Board meeting on the matters discussed at each committee meeting. The minutes of each committee meeting are circulated to all Directors.

audit committee

The Audit Committee consists of Christina McComb, Nigel Masters and Caroline Fawcett under the Chairmanship of Andrew Gosling. All of the committee members have relevant financial sector experience and Andrew Gosling and Nigel Masters have relevant financial experience. The responsibilities of the committee are in line with the provisions of the FRC Guidance on Audit Committees. The main function of the committee is to assist the Board in fulfilling its oversight responsibilities, specifically the ongoing review, monitoring and assessment of:

- the integrity of the financial statements and reviewing significant financial reporting judgements contained in them
- the effectiveness of systems of internal control
- the internal and external audit processes
- compliance with applicable laws and regulations
- the recommendation to the Board on the appointment, re-appointment and removal of external auditors and the periodic review of their performance and independence and the policy on the use of the external auditor for non-audit work

During 2013 the committee met four times in the execution of its responsibilities.

During the meetings the Committee considered reports on:

- the system of internal control – as well as regular reports from the internal and external auditors on control matters, the committee receives an annual paper from Internal Audit which expresses an opinion on the effectiveness of the system of internal control
- the integrity of financial statements – a Review of Going Concern is prepared for the committee, which considers the impact on capital, liquidity and profitability of the Group
- compliance with laws and regulations, including adherence to money laundering regulations – the committee receives regular reports from the Compliance Officer and Money Laundering Reporting Officer on conduct matters, which express an opinion on the effectiveness of the systems of internal control
- the activities of internal audit and external auditors – the committee receives regular reports from both the external auditor and Internal Audit and closely monitors all issues raised until they have been resolved satisfactorily by management. Both auditors have met privately with the committee during the year
- the level of non-audit fees paid to the external auditor – the committee has reviewed the level of non-audit fees paid to the external auditor throughout the year and believes that these have not impaired the independence and objectivity of the external auditors. The Chairman of the Audit Committee meets regularly with the internal audit manager to discuss issues of internal control. The committee considers that it has met its responsibilities and performed its duties with appropriate levels of care and expertise during 2013

finance committee

The Finance Committee consists of David Robinson and Peter Burrows, under the Chairmanship of Nigel Masters. The committee met five times during 2013 to review key aspects of Group financial management in greater detail than is possible at regular Board meetings. In particular, the Board has charged the committee with providing direction and monitoring of strategic progress in the management of the Group's with profits business, monitoring of the Group's investment strategy, monitoring of the Group's investment performance, reviewing the principles underlying the capital management of the Group, product pricing for all Group products, expense analysis and the Society's returns to the Prudential Regulation Authority (PRA).

corporate governance & nominations committee

The Corporate Governance and Nominations Committee consists of the Vice Chairman, The Senior Independent Director and the Chief Executive, under the Chairmanship of David Robinson. The majority of members of the committee were independent non-executive directors during 2013. The committee meets as appropriate to review the structure, size and composition of the Board and to make recommendations to the Board with regard to any adjustments that are deemed necessary. It is also responsible for identifying and nominating for the approval of the Board, candidates to fill Board vacancies as and when they arise. Nominations for appointment to the Board are considered for approval by the full Board.

Professional recruitment consultants are appointed to ensure that vacancies are brought to the attention of a wide audience. All applicants are independently appraised by the external consultants and a short list is drawn up, prior to interview by the Board.

remuneration committee

The Remuneration Committee consists of David Robinson, Paul Chandler and Caroline Fawcett under the Chairmanship of Christina McComb.

The Board considers that all members of the Committee are independent for the purpose of reviewing remuneration matters.

The Chief Executive and the HR Director also attended meetings during the year at the request of the Chairman, except when their own remuneration was being discussed. The duties of the Committee are:

- to determine the remuneration arrangements and policy for Executive Directors and to submit proposals to the Board for approval;
- to agree service contracts for Executive Directors and to review these regularly;
- to set the parameters for, and keep under review, management bonus schemes;
- to receive details of the review of management remuneration carried out by the Chief Executive;
- to review the impact of any committee decision on remuneration to be disclosed in the Group Annual Financial Statements; and
- to consider other topics as determined by the Committee Chair or the Board

The Committee met five times during the year.

To ensure that the Committee has sufficient independent information and advice on remuneration matters, it retains the use of Towers Watson Limited as its independent advisor.

risk committee

The Risk Committee consists of Karl Elliott, Andrew Gosling, and Nigel Masters, under the Chairmanship of Paul Chandler.

The duties of the Committee are:

- To review the Group's risk appetite, policies and future risk strategy, ensuring these are in alignment, and to make recommendations to the Board on any material changes.

- To review the drivers of any changes in the risk profile, and their implications and to consider regular Risk Reports, reviewing management's view of emerging and potential risks, and any arising management actions, and to feed back to the Board the Committee's observations on significant issues and trends in relation to the Group's risk profile
- To review the risk management framework relative to the Group's activities and the effectiveness of risk reporting
- To support the Risk Director and Group Corporate Risk Officer in developing and implementing workplans and in securing appropriate resources for their work
- To oversee the Own Risk Self-Assessment (ORSA) process and work with the Finance Committee to recommend adoption of the ORSA to the Board
- To ensure that risk assessments are undertaken of strategic or significant transactions and any major business projects; to consider the outputs from such assessments, drawing on independent external advice where appropriate and available, and make observations to the Board on the risk aspects of such proposals prior to the Board taking decisions on whether to proceed
- To ensure that risk is properly considered in the Audit, Finance and Remuneration Committees, as well as the Board, in execution of the individual committee's duties
- To ensure that Committee members are provided with appropriate and timely training and to monitor and encourage the embedding and maintenance throughout the Group of a supportive culture in relation to the management of risk
- To review its own performance and Terms of Reference periodically, recommending any changes it considers necessary to the Board for approval
- To consider other topics, as referred to it from time to time by the Board

The Committee was established and met for the first time on 12 December 2013.

The full terms of reference of the Audit, Finance, Corporate Governance and Nominations, Remuneration and Risk Committees are available on request from the Group Secretary or by viewing our website at **engagemutual.com.**

executive sub committees

The governance structure includes a number of executive sub committees that have responsibility for key risk areas. These committees represent the With Profits funds, Business Performance and Risk and Governance. The sub committees allow the Executive to concentrate on issues at a Group level.

relations with customers

The customers of the Engage Mutual Group are currently made up of the friendly society's life fund members, child trust fund customers and health insurance customers.

Engage Mutual applies the same principles of value and service to all customers and encourages feedback on any aspect of the Group's activities.

The Engage Mutual Group has an established customer panel, consisting of around 1,000 customers, who are invited to comment on a variety of issues.

The customer panel provides us with a number of members who give up their time to provide feedback and insight on product development and customer service. In addition, in 2013 the Society established a process of meeting with different groups of customers, face to face, via customer forums

All members of the friendly society who are eligible to vote are encouraged to exercise their vote at the AGM by voting in person, online or by using the proxy voting form which includes a 'vote withheld' option and prepaid reply envelope. Alternatively, members can exercise their vote through the appointment of a proxy if the member cannot attend and vote at the meeting. An individual resolution is proposed on each separate issue including a resolution on the Annual Report and Accounts.

One of the ways in which we express our mutuality is through the provision of discretionary benefits in times of hardship or need. We continue to provide discretionary benefits from time to time whilst remaining mindful of the need for balance, fairness to all members and affordability. We will continue to operate under these principles in 2014.

system of internal control

The Board has overall responsibility for the Group's system of internal controls, which aims to safeguard the Group's assets and to ensure that proper accounting records and financial reporting processes are maintained and that the financial information used within the business and for publication is accurate, reliable and fairly presents the financial position of the Group and the results of its business operations.

The Board is also responsible for reviewing the effectiveness of the system of internal controls.

This has been in place for the year under review and is regularly reviewed by the Board. The system is designed to provide reasonable assurance of effective operations and compliance with laws and regulations, although any system of internal controls can only provide reasonable, not absolute, assurance against material misstatement or loss, and can only mitigate rather than eliminate the risk of failure to achieve business objectives.

The Directors also review the effectiveness of the Group on non-financial as well as financial controls, including operational controls, risk management and the Group's high level internal control arrangements. The Group has adopted an internal control framework that contains the following key elements.

control environment

The Group's control environment is designed to create an attitude of taking acceptable business risk within clearly defined limits. The control environment includes:

- an organisational structure with clear lines for responsibility, delegation of authority and reporting requirements
- co-ordinated activity across the whole Group through Executive Committee meetings
- clearly defined policies for capital and revenue expenditure. Larger capital and revenue expenditure requires Board authorisation
- comprehensive systems of financial reporting. The annual budget and long term plans of the Group are reviewed and approved by the Board. Results are reported against budget and remedial action is taken where appropriate
- a 'whistle-blowing' policy allows any employee to report, in confidence, suspected serious malpractice. An anti-fraud policy with guidance further supports the Code
- Internal Audit, Risk, Compliance and operational functions that review the system of internal control

risk management

The Board and Executive have the primary responsibility for identifying the key business risks facing the Group.

The Group has a Risk Function which operates a risk management process that identifies the key risks facing the business.

The Society has a risk register that identifies and records risks and the actions being taken to manage them. The information is consolidated for the Board on how the key risks are being managed. The Board has responsibility for establishing a coherent framework for the Group to manage risk in order to carry out its responsibility to ensure effective risk management and control.

During the year a review of current risk procedures and governance commenced which will be progressed further in 2014.

This includes the establishment of a Board Risk Committee and an Executive Risk and Governance Committee. The Board Risk Committee met for the first time on 12 December 2013.

control procedures

The Group's control procedures are designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to loss of assets or fraud.

corporate governance (cont.)

monitoring

The operation of the system of internal control is the responsibility of line management. It is subject to independent audit review and, where appropriate, review by the external auditor and external regulators.

The Audit Committee, on behalf of the Board, reviews the reports of the Group on internal control.

A key part of the process in assessing internal control by the Audit Committee is the quarterly Combined Assurance Map. The Combined Assurance Map is reported to the Audit Committee. The Directors are then able to review the system of internal controls and ensure it complies with appropriate guidance.

external audit

One of the duties of the Audit Committee is to make recommendations to the Board in relation to the appointment of the external auditors. It is intended that a resolution to re-appoint the external auditor be put to the Annual General Meeting on 22 May 2014.

Details of the amounts paid to the external auditors during the year for audit and other services are set out in note 7 to the financial statements. The Committee has put in place safeguards to ensure that the independence of the audit is not compromised, including a policy on the commissioning of non-audit services from the external auditor. The external auditors are permitted to provide some non-audit services that are not, and are not perceived to be, in conflict with their independence. The pre-approval of the Committee is required for services above certain thresholds determined by the Committee.

In addition, the following assignments are prohibited from being performed by the external auditors:

- bookkeeping or other services related to the accounting records of financial services
- financial information systems design and implementation
- internal audit outsourcing services
- management functions or human resources
- any other services that the Audit Committee may determine

The performance of the external auditor is formally monitored annually to ensure it meets the needs of the Group and the results are reported to the Committee.

auditors

The Audit Committee monitors the Group's policy on the use of the external auditors for non-audit work. The purpose of the policy is to ensure the continued independence and objectivity of the external auditors.

The external auditors undertook a number of non-audit assignments during 2013. In the opinion of the Audit Committee these were within the limits set out in the policy and are considered to be consistent with the professional and ethical standards expected of the external auditors.

internal audit

Internal Audit is an independent appraisal function that derives its authority from the Board through to the Chairman of the Audit Committee. Its primary role is to provide reasonable and effective assurance about the adequacy and effectiveness of the Group's financial control framework and risk management.

Internal Audit seeks to discharge the responsibilities set down by reviewing the processes that ensure business risks are effectively managed and reviewing the financial and operational controls that help to ensure compliance with corporate objectives, policies and procedures and external legislation. Internal Audit also acts as a source of constructive advice and best practice, assisting senior management with its responsibility to improve the process by which business risks are identified and managed and to report and advise on the proper and effective use of resources.

The information received and considered by the Audit Committee provided reasonable assurance that during 2013 there were no material breaches of control or regulatory standards and that, overall, the Group maintained an adequate system of internal control.

regulation

We maintain an ongoing dialogue with our Regulator(s) in order to keep up to date with developments and in order to address any necessary changes to business practice and policy required by developments in the comprehensive regulatory framework.

Solvency II

We continue to work on our response to the new Solvency II European Directive which is now due to come into force on 1 January 2016. When these regulations are implemented they will have wide ranging implications for management practice, particularly for risk and financial reporting. We will seek to leverage the existing investment we have made in governance and reporting systems to fully embed risk management, evaluation and reporting in line with the new requirements.

statement of solvency

Throughout 2013 and as at 31 December 2013, the Group's capital resources exceeded the minimum capital resources requirements prescribed by the Prudential Regulation Authority.

annual general meeting (AGM)

At the AGM, the Chairman, Chief Executive and other Executive Directors give presentations on the previous year's performance and on future plans. The meeting also provides an opportunity for members to question the Chairman and Chief Executive on the resolutions to be proposed at the meeting and on any other aspect of the Society's business. All Directors attend the AGM including the Chairmen of all the Board committees.

The results of the proxy votes, and the votes cast at the AGM, are publicised on the Society's website. A separate resolution is proposed on each issue, including a resolution on the Annual Report and Accounts.

statement of compliance with the annotated code

The Society does not seek to comply with the UK Corporate Governance Code, as issued by the Financial Reporting Council. However, to the extent considered appropriate for a friendly society we do comply with the Annotated UK Corporate Governance Code for Mutual Insurers issued by the Association of Financial Mutuals ('the Code'), with the following exceptions.

We will keep our approach to compliance with the Code under review during 2014.

annual election of directors

The UK Corporate Governance Code introduced a requirement that Directors of larger organisations be subject to annual election by members. The Board has considered this provision in respect of the 2014 AGM and has agreed that this should not be brought in at that time. The Board is concerned that in extreme circumstances this provision could have implications for the financial stability of the Society which would not be in the best interests of members. The Board will review the position again over the course of 2014 and conclude on whether to introduce annual election by members for the AGM business in 2015.

diversity

The Board gives consideration to all aspects of diversity, including gender, on the Board although it has adopted the principle that all appointments should be made on merit. For this reason, the Board has not set any measurable objectives although this will be kept under review.

audit committee report

A updated version of the UK Corporate Governance Code, which applies to financial years commencing on or after 1 October 2012, introduced a requirement for the annual report and accounts, taken as a whole, to be fair, balanced and understandable. It also called for a description of the work of the Audit Committee to include:

- The significant issues considered in relation to the financial statements, and how they were addressed;
- How the Audit Committee assessed the effectiveness of the external audit process; and
- The approach to appointing the auditor and how objectivity and independence are safeguarded relative to non-audit services

A description of the work of the Audit Committee is included in the Corporate Governance Report. However, we have not sought to comply fully at this time with all aspects of the new Audit Committee reporting requirements, for example provision of a detailed explanation of the significant issues considered in relation to the financial statements.

how directors are remunerated

As a mutual, we are required to prepare accounts in accordance with the Friendly Societies Act 1992 and applicable accounting standards. However, in the interests of good corporate governance, we go beyond that and use the disclosure requirements contained in the Companies Act 2006 as a basis for the disclosure of Directors' remuneration.

This report provides details of the remuneration of the executive director and the non-executive directors.

policy on remuneration for executive director and other executives

The Remuneration Committee is responsible for the Group's Executive remuneration policy.

The objective of the Committee is to give the executive director encouragement to enhance the Group's performance by ensuring that they are rewarded fairly and responsibly for their individual contributions.

When determining the remuneration policy for executives, the Committee considers a number of factors including:

- the need to recruit and retain good quality and highly motivated people;
- the remuneration practices of competitor businesses, including other mutuals; and
- compliance with the appropriate regulatory code of practice

The remuneration includes a performance related element which is linked to the achievement of business and personal objectives.

Throughout the Group, we aim to ensure that our people are rewarded fairly for their contribution. To achieve this, we obtain independent benchmarking data from Towers Watson Limited and set remuneration for each individual, whether Executive Director or staff member, by reference to a relevant role benchmark. The Remuneration Committee thereby ensures that Executive Director remuneration is determined using processes consistent with those adopted for all employees, and is set at a level designed to reflect similar roles carrying comparable responsibility in other organisations.

components of director remuneration

There are three components of Executive Director remuneration:

- basic salary and associated benefits, including a car allowance and medical insurance;
- performance related pay, which is based on achievement of objectives set annually; the payment of any bonus award is deferred over four years in line with best practice guidance for financial services organisations, and paid subject to continued satisfactory business performance; and
- pension arrangements

Each is dealt with separately below.

Throughout the Group, we aim to **ensure that our people are rewarded fairly for their contribution.**

basic salary

It is the committee's policy to ensure that the basic salary for each Executive Director is appropriate and competitive for the responsibilities involved. Salaries are reviewed annually by the committee in February and any changes are introduced with effect from 1 March. Only basic salary is pensionable. Executive Director salaries are shown in table a.

performance related pay

The Group operates a discretionary performance related pay scheme for executive director. The Committee meets annually to agree objectives and set incentive targets. The measures used to assess performance are taken from the Group's management information and balanced scorecard.

The objectives and weightings applied for 2012 and 2013 were similar. They reflect the continuing need for robust financial management, balanced with progress in the implementation of the Group's strategic direction in terms of customer development, infrastructure maintenance and people management. Hence the framework comprises:

- financial results in the year 50%
- customer community development and service 20%
- infrastructure maintenance and development 20%
- people management and development 10%

Under the combined scheme for 2013, the executive director were eligible for an award of up to 85% of basic salary. 40% of the award is paid in the following year, with the balance deferred over a further three years subject to continued satisfactory business performance.

The Performance Related Pay scheme was reviewed by the Remuneration Committee during 2013. As a result, from 2014 onwards the proportion of Executive Director remuneration represented by performance related pay has been reduced and the appropriateness of salary levels has been reviewed. The maximum award that may be made to the executive director is now 50% of basic salary, with similar deferral arrangements as described above. On target performance will result in an award of 30% of basic salary.

Awards made under the performance related pay scheme are shown in table a and b.

pension arrangements

During 2013 the Society operated a Defined Contribution pension scheme.

Peter Burrows and Karl Elliott each receive an employer contribution of 10% of basic salary paid into

how directors are remunerated (cont.)

a Defined Contribution pension scheme. Karl Elliott was also a member of the Society's Defined Benefit scheme which was closed to further service accruals on 31 December 2012; he became a member of the Defined Contribution scheme from 1st January 2013.

Pension details are set out in tables a and c.

service contracts

Executive directors have service contracts with a one year notice period. No non-executive director has a service contract.

share options

As a mutual, we do not operate a share or share option plan.

non-executive directorships

The Committee believes that non-executive directorships of external organisations represent an important opportunity for personal development. Accordingly, and subject to Board approval, executive directors may take such appointments.

At this time Peter Burrows is a director of the Association of Financial Mutuals, the trade body representing the interests of the mutual insurance sector. He is also a governor of York College, an educational establishment. He does not receive remuneration for either position.

non-executive directors

The remuneration of our non-executive directors is recommended by the Chairman and Chief Executive for the Remuneration Committee to agree annually.

The remuneration is determined on the basis of an agreed minimum number of days committed to Group business and is also benchmarked against non-executive remuneration in other financial services organisations of similar size, including other mutuals.

The remuneration of non-executive directors does not include any incentive element and non-executive directors are not entitled to participate in any of the Group's pension schemes.

non-executive directors are elected for a period of three years. The Board may resolve to reappoint a non-executive director at or before the expiry of their term. It is our policy to allow non-executive directors to serve no more than nine years in aggregate.

Details of the year of appointment and fees of our non-executive directors are shown in table d.

emoluments of directors for the year ending 31 December 2013

table a – executive director's total remuneration

	Date of appointment to the Board	Basic Salary £'000	Benefits £'000	Performance award - earned in year £'000	Performance award - deferred £'000	Other £'000	Pension £'000	Total £'000
2013								
Peter Burrows	10-Nov-10	208	10	47	71	-	20	356
Karl Elliott	4-Dec-07	143	8	31	46	-	104	332
Total		351	18	78	117	-	124	688
2012								
Peter Burrows	10-Nov-10	152	9	36	54	-	15	266
Karl Elliott	4-Dec-07	123	8	29	44	-	148	352
Andrew Haigh	09-Jun-99	204	15	58	88	344	221	930
Total		479	32	123	186	344	384	1,548

notes

(1) Benefits represent car allowance and medical insurance.

(2) Andrew Haigh resigned as a Director on 24 December 2012. In line with his service contract he received remuneration in respect of his twelve month notice period of £285,000. He also received a termination payment of £59,000.

(3) Karl Elliott's salary increased in 2013 reflecting a supplement awarded due to changes in the Defined Benefit scheme.

(4) The Pension total includes Society contributions to a Defined Contribution scheme for Peter Burrows of £20,000 (2012: £15,000) and Karl Elliott of £15,200 (2012: £nil) and an increase in accrued pension for the Defined Benefit scheme for Karl Elliott of £89,000 (2012: £148,000).

emoluments of directors for the year ending 31 December 2013 (cont.)

table b – long-term performance award

	Deferred performance award b/f £'000	Awarded in the year £'000	Earned in the year £'000	Deferred performance award c/f £'000
2013				
Peter Burrows	97	71	(40)	128
Karl Elliott	92	46	(46)	92
Total	189	117	(86)	220
2012				
Peter Burrows	65	54	(22)	97
Karl Elliott	79	44	(31)	92
Andrew Haigh	183	88	(271)	-
Total	327	186	(324)	189

table c – defined benefit pension details of executive directors

	Years of service	Total accrued pension at 31 December 2013 £'000	Increase in accrued pension during the year (net of inflation) £'000	Increase in accrued pension during the year (including inflation) £'000	Transfer value of increase in accrued pension less member contributions £'000	Transfer value of total accrued pension at 31 December 2012 £'000	Transfer value of total accrued pension at 31 December 2013 £'000	Increase in transfer values net of members' contributions £'000
2013								
Karl Elliott	14	31	-	1	16	523	612	89

	Years of service	Total accrued pension at 31 December 2012 £'000	Increase in accrued pension during the year (net of inflation) £'000	Increase in accrued pension during the year (including inflation) £'000	Transfer value of increase in accrued pension less member contributions £'000	Transfer value of total accrued pension at 31 December 2011 £'000	Transfer value of total accrued pension at 31 December 2012 £'000	Increase in transfer values net of members' contributions £'000
2012								
Karl Elliott	13	30	5	5	87	369	523	148
Andrew Haigh (1)	14	47	6	7	126	711	936	214

notes

(1) Andrew Haigh resigned as a Director on 24 December 2012.

(2) Karl Elliott transferred his pension contributions into a Defined Contribution scheme on 1 January 2013 following the closure of the Society's Defined Benefit scheme to future accruals on 31 December 2012.

table d – non-executive directors' remuneration

	Date of appointment to the Board	2013 fees £'000	2012 fees £'000
David Robinson	3-Aug-10	60	60
Paul Chandler (1)	1-Oct-12	35	9
Andrew Gosling	24-Mar-11	35	35
Peter Mason (2)	9-Dec-05	3	35
Nigel Masters (1)	1-Jun-12	35	20
Christina McComb	11-May-05	35	35
Caroline Fawcett (3)	28-May-13	23	-
Total		226	194

notes

(1) Nigel Masters joined the Board in June 2012 and Paul Chandler joined the Board on 1 October 2012.

(2) Until May 2012 the fees paid in respect of Peter Mason were payable to PWM Enterprises Limited. Peter Mason resigned from the Board on 31 January 2013.

(3) Caroline Fawcett joined the Board on 28 May 2013.

statement of responsibilities of the directors

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Friendly Society law requires the Directors to prepare Group and Society financial statements for each financial year. Under that law they have elected to prepare the Group and Society financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

The Group and Society financial statements are required by law to give a true and fair view of the state of affairs of the Group and of the Society as at the end of the financial year and of the income and expenditure of the Group and of the Society for the financial year.

In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and Society and enable them to ensure that its financial statements comply with the Friendly Societies Act 1992 and the regulations made under it.

The Directors are also responsible for preparing a Report of the Directors in accordance with the Friendly Societies Act 1992 and the regulations made under it.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and the Society, and to prevent and detect fraud and other irregularities.

The Directors have decided to prepare voluntarily a Directors' Remuneration Report in accordance with certain aspects of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 made under the Companies Act 2006, as if those requirements were to apply to the Society.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Society's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

independent auditor's report

To the members of Homeowners Friendly Society Limited.

We have audited the financial statements of Homeowners Friendly Society Limited for the year ended 31st December 2013, set out on pages 44-87. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

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

respective responsibilities of the Directors and auditor

As explained more fully in the Statement of Directors' Responsibilities set out on page 42 the Directors are responsible for preparing financial statements which give a true and fair view. Our responsibility is to audit, and express an opinion on, the 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 Board's Ethical Standards for Auditors.

scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at https://www.frc.org.uk/auditscopeukprivate

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 affairs of the Group and of the Society as at 31st December 2013 and of the income and expenditure of the Group and of the Society for the year then ended; and
- have been properly prepared in accordance with the Friendly Societies Act 1992 and the regulations made under it

opinion on other matters prescribed by the Friendly Societies Act 1992

In our opinion the Report of the Directors 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 accounting records and the financial statements for the financial year.

matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Friendly Societies Act 1992 requires us to report to you if, in our opinion:

- proper accounting records have not been kept;
- 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

In addition to our audit of the financial statements, the Directors have engaged us to review whether the Corporate Governance Statement reflects the Society's compliance with the nine provisions of the Annotated Corporate Governance Code for Mutual Insurers (published by the Association of Financial Mutuals) specified for our review.

Jonathan Holt
(Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor

Chartered Accountants
St. James Square
Manchester
M2 6DS
20 March 2014

group income and expenditure accounts
for the year ended 31 December 2013

Technical Account Long-Term Business

The profit and loss account for recording long-term insurance contracts

	Notes	2013 £'000	2012 £'000
Earned premiums, net of reinsurance			
Gross premiums written	2	**33,822**	33,245
Outward reinsurance premiums	2	**(10,282)**	(10,886)
Investment income	3	**25,346**	46,348
Unrealised gains / (losses) on investments	3	**19,757**	(723)
Other technical income	10	**4,234**	5,255
Claims incurred, net of reinsurance			
Gross claims incurred	4	**(46,544)**	(36,236)
Outward claims reinsurance	4	**6,486**	5,589
Change in long-term business provision, net of reinsurance	19	**36,778**	1,345
Change in gross liability for investment contracts	20	**(36,568)**	(25,001)
Other technical charges		**(3,952)**	(3,017)
Goodwill amortisation		**-**	425
Net operating expenses	6	**(14,613)**	(14,167)
Investment expenses and charges	3	**(1,725)**	(776)
Taxation	12	**37**	(307)
Transfer to the fund for future appropriations	23	**(12,776)**	(1,094)
Balance on the long-term business technical account		**-**	-

Share dividends, interest on deposits held and realised gains on investments

Movements in value of investments held

Change in value of linked policyholders' benefits

Fund managers' charges

Group tax cost

group income and expenditure accounts (cont.)
for the year ended 31 December 2013

Technical Account General Business

The profit and loss account for recording general insurance contracts

	Notes	2013 £'000	2012 £'000
Earned premiums			
Gross premiums written		**7,018**	6,908
Change in unearned premiums		**(11)**	9
Claims incurred			
Claims paid		**(5,416)**	(5,211)
Change in provision for claims		**(68)**	54
Other technical charges		**(403)**	(597)
Net operating expenses	6	**(3,442)**	(3,979)
Balance on the general business technical account		**(2,322)**	(2,816)

Premiums collected which relate to cover in the future

Claims which will be settled in the future

The total income and expenditure on the health business

Non-Technical Account

The profit and loss account for recording income and expenditure from non-insurance subsidiaries

	Notes	2013 £'000	2012 £'000
Continuing operations			
Balance on the long-term business technical account		**-**	-
Balance on the general business technical account		**(2,322)**	(2,816)
Other income	11	**4,179**	3,545
Net operating expenses	6	**(2,365)**	(2,175)
Pension finance income	24	**(1)**	172
Taxation	12	**-**	-
Loss on ordinary activities		**(509)**	(1,274)

Income earned in non-insurance subsidiaries

Expenses incurred in non-insurance subsidiaries

group statement of total recognised gains and losses

for the year ended 31 December 2013

Income and expense items which differed to projected amounts on the pension scheme

Surplus in the pension scheme which has not been recognised as an asset

	Notes	2013 £'000	2012 £'000
Loss on ordinary activities		**(509)**	(1,274)
Actuarial gain on pension scheme	24	**(1,083)**	(1,056)
Unrecognised pension scheme asset	24	**755**	579
Total recognised losses in the year		**(837)**	(1,751)

group balance sheet

as at 31 December 2013

Assets

Harrogate head office and Kew Gardens property

Investments held in respect of policyholders' liabilities, and surplus investments

Accumulated sales costs that are associated with acquiring new policies and are spread over several years

	Notes	2013 £'000	2012 £'000
Investments			
Investment in land and buildings	13	**5,075**	5,075
Linked financial investments	15	**364,513**	301,306
Non-linked financial investments	15	**259,563**	343,526
Reinsurers' share of technical provisions			
Long-term business provision	19	**52,828**	61,458
Other assets			
Other debtors	16	**2,731**	3,179
Tangible assets	17	**386**	479
Cash at bank		**34,445**	36,150
Deferred taxation	12	**853**	853
Prepayments and accrued income			
Accrued interest and rent		**1,761**	2,015
Deferred acquisition costs	18	**258**	460
Other prepayments and accrued income		**516**	488
Total assets		**722,929**	754,989
Net pension asset	24	-	-
Total assets including the pension asset		**722,929**	754,989

group balance sheet (cont.)

as at 31 December 2013

Liabilities

	Notes	2013 £'000	2012 £'000
Fund for future appropriations	23	**95,824**	83,885
Technical provisions			
Long-term business provision	19	**244,524**	289,922
Claims outstanding	19	**9,223**	7,661
Gross liability for investment contracts	20	**364,313**	365,443
Creditors			
Creditors arising out of insurance operations	21	**1,115**	1,129
Other creditors including taxation and social security	22	**2,276**	1,669
Accruals and deferred income		**5,654**	5,280
Total liabilities		**722,929**	754,989

Value recognised for regulatory reserves and other surplus funds, including possible future with profit bonuses

The amount that needs to be set aside to meet future liabilities arising from our insurance contracts

Provision for with profits policies, insurance liabilities and other known contingencies

Maturities, surrenders and death claims awaiting processing and payment

Value of linked policyholders' benefits

Expenses incurred in the period yet to be processed

Approved at a meeting of the Board of Directors on 20 March 2014 and signed on its behalf by:

P J Burrows
Chief Executive

D G Robinson
Chairman

A J Horsley
Secretary

society income and expenditure account

for the year ended 31 December 2013

Technical Account Long-Term Business

	Notes	2013 £'000	2012 £'000
Continuing Operations			
Earned premiums, net of reinsurance			
Gross premiums written	2	**33,822**	33,245
Outward reinsurance premiums	2	**(10,282)**	(10,886)
Investment income	3	**25,346**	45,430
Unrealised gains / (losses) on investments	3	**16,757**	(55)
Other technical income	10	**4,624**	5,722
Claims incurred, net of reinsurance			
Gross claims incurred	4	**(46,544)**	(36,236)
Outward claims reinsurance	4	**6,486**	5,589
Change in long-term business provision, net of reinsurance	19	**36,778**	1,345
Change in gross liabilities for investment contracts	20	**(36,568)**	(25,001)
Other technical charges		**(3,950)**	(3,017)
Net operating expenses	6	**(14,613)**	(14,167)
Investment expenses and charges	3	**(1,725)**	(776)
Taxation	12	**37**	(307)
Transfer to the fund for future appropriations	23	**(10,168)**	(886)
Balance on the long-term business technical account		**-**	-

Share dividends, interest on deposits held and realised gains on investments

Movements in value of investments held

Change in value of linked policyholders' benefits

Fund managers' charges

Society tax cost

society balance sheet
as at 31 December 2013

Assets

	Notes	2013 £'000	2012 £'000
Investments			
Investment in land and buildings	13	**5,075**	5,075
Investment in subsidiaries	14	**9,950**	9,950
Linked financial investments	15	**364,513**	301,306
Non-linked financial investments	15	**256,250**	340,509
Reinsurers' share of technical provisions			
Long-term business provision	19	**52,828**	61,458
Other assets			
Other debtors	16	**3,870**	3,748
Cash at bank		**31,197**	35,037
Prepayments and accrued income			
Accrued interest and rent		**1,760**	1,958
Deferred acquisition costs	18	**258**	460
Other prepayments and accrued income		**516**	488
Total assets		**726,217**	**759,989**

Harrogate head office and Kew Gardens property

Investments held in respect of policyholder's liabilities, plus surplus investments

Accumulated sales costs that are associated with acquiring new policies and are spread over several years

society balance sheet (cont.)
as at 31 December 2013

Liabilities

	Notes	2013 £'000	2012 £'000
Fund for future appropriations	23	**104,556**	94,388
Technical provisions			
Long-term business provision	19	**244,010**	289,418
Claims outstanding	19	**8,699**	7,205
Gross liabilities for investment contracts	20	**364,313**	365,443
Creditors			
Creditors arising out of insurance operations	21	**801**	767
Other creditors including taxation and social security	22	**1,730**	1,675
Accruals and deferred income		**2,108**	1,093
Total liabilities		**726,217**	**759,989**

Value recognised for regulatory reserves and other surplus funds, including possible future with profit bonuses

The amount that needs to be set aside to meet future liabilities arising from our insurance contracts

Provision for with profits policies, insurance liabilities and other known contingencies

Maturities, surrenders and death claims awaiting processing and payment

Value of linked policyholders' benefits

Expenses incurred in the period yet to be processed

Approved at a meeting of the Board of Directors on 20 March 2014 and signed on its behalf by:

P J Burrows
Chief Executive

D G Robinson
Chairman

A J Horsley
Secretary

statement of accounting policies

a. Basis of accounting

The Group financial statements have been prepared in compliance with the Friendly Societies (Accounts and Related Provisions) Regulations 1994, the Friendly Societies Act 1992, and in accordance with the Statement of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers ("ABI SORP"), in December 2005 and as amended in December 2006.

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards.

After making appropriate enquiries, the Directors confirm they are satisfied that the Society has adequate financial resources and regulatory capital for the next twelve months from the date of approval of these financial statements. Accordingly, they continue to adopt the going concern basis in the preparation of the financial statements as confirmed in the statement of the responsibilities of the directors on page 42. Further details on the financial resources, regulatory capital and financial and insurance risks are set out in note 1 to the accounts on pages 58 to 66.

b. Basis of consolidation

The consolidated financial statements incorporate the assets, liabilities, and results of the Society and its subsidiary undertakings drawn up to 31 December each year.

The General Insurance results of Engage Mutual Health have been consolidated into the Technical Account – General Business.

The ongoing results of other subsidiary undertakings are included in the Non-Technical Account. The net results are included in the Fund for Future Appropriations for the Group, together with any amounts in the statement of Total Recognised Gains and Losses.

The Group has one Non Profit Fund and two With Profits Funds referred to in our financial statements as follows:

- With Profits Fund I (WP1) (acquired from United Kingdom Civil Service Benefit Society Limited in 2003)
- With Profits Fund II (WP2) (acquired from Ecclesiastical Life Limited in 2010)

c. Classification of contracts

The Group classifies its products in accordance with Financial Reporting Standard 26 'Financial Instruments: Recognition and Measurement' ('FRS 26').

FRS 26 requires companies to categorise the policies they issue as 'investment' contracts or 'insurance' contracts. Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event could cause an insurer to pay the significant additional benefits in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights or obligations are extinguished or expire. Contracts initially classified as investment contracts can be reclassified as insurance contracts after inception, if insurance risk becomes significant.

Amounts received from and paid to policyholders of investment contracts are accounted for as deposits received (or repaid) and are not included in the premiums and claims in the Technical Account – Long-term Business. For unit-linked contracts the related liability is established on the due date for payment. Fees for investment management and other services are recognised in the Technical Account – Long-term Business in the period in which the services are provided. The liability for the unit-linked business is disclosed in the Balance Sheets as 'Gross liability for investment contracts'.

statement of accounting policies (cont.)

d. Long-term business

Premiums

Long-term insurance business premiums, relating to insurance contracts, including reinsurance premiums, are recognised when they become due for payment. New business premiums, including single premiums, are recognised when they are received.

Claims

For insurance contracts death claims are accounted for when notified to the Group. Annuity payments are recorded when due. Maturities and surrenders are recorded on the earlier of the date when paid or when the policy ceases to be included within the Long-Term Business Provision. Reinsurance recoveries are credited to match the relevant gross amounts.

Deferred acquisition costs

Certain directly attributable costs of acquiring new insurance contracts are deferred. Such costs are disclosed as an asset in the balance sheet. The deferred acquisition costs are amortised in line with the expected life of the policies.

Policyholder liabilities

See accounting policy J - 'Valuation of insurance liabilities' and policy K – 'Linked investment contracts'.

Reinsurance

Long-term insurance business is ceded to reinsurers under contracts to transfer part or all of one or more of the following risks: mortality, morbidity and lapse.

Amounts recoverable from reinsurers are estimated based upon the related gross insurance provisions, having due regard for collectability. The recoverability of reinsurance assets is assessed having regard to market data on the financial strength of each of the reinsurance companies. The reinsurers' share of claims incurred, disclosed in note 4, reflects the amounts received and receivable from reinsurers in respect of claims incurred during the period. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised in the Technical Account – Long-term Business when payable, offset against any premium income.

e. General business

Premiums

General business premiums comprise the total premiums due for the whole period of cover excluding insurance premium tax. Unearned premiums are calculated as the unexpired element of risk spread on a straight line basis across the period of the policy.

Claims

General business claims incurred comprise claims paid during the financial year together with the movement in the provision for outstanding claims, including an estimate of claims incurred but not reported (IBNR) at the year end. Claims outstanding comprise provisions for the estimated cost of settling all claims incurred but unpaid at the balance sheet date whether reported or not.

Provision is made at the year end for the estimated cost of claims incurred but not settled at the balance sheet date, including the cost of claims incurred but not yet reported to the company at the year end. The cost of notified but not settled claims is estimated on an individual case by case basis by the claims handlers using their experience of settling previous claims. The estimation of claims incurred but not reported is generally subject to a greater degree of uncertainty. IBNR claims are estimated using techniques which use past trends to forecast the expected cost of these claims.

f. Investment income and unrealised gains and losses on investments ('Investment return')

Investment return comprises all investment income, realised gains and losses and movements in unrealised gains and losses, net of investment expenses.

Dividends on equity holdings are included as investment income on the date the equity shares are quoted ex dividend and are stated net of the dividend withholding tax. Interest, including mortgage interest, rent and expenses are accounted for on an accruals basis or using the effective interest method where the impact of doing so is material.

Dividends on accumulation share holdings in open ended investment companies (OEICs) and accumulation unit holdings in unit trusts are included as investment income on the date the dividend voucher is received.

Realised gains and losses on investments are calculated as the difference between sale proceeds and purchase price. Movements in unrealised gains and losses on investments represent the difference between the fair value at the balance sheet date and their purchase price or their fair value at the last balance sheet date, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

g. Investments

Land and buildings

Land and buildings are held at open market value. Full valuations are made by independent professionally qualified valuers every three years. In the intervening years these valuations are updated by the Directors with assistance of independent professional advice as required. Full valuations may be made in the intervening periods where economic conditions in the property market would suggest it is necessary.

Land and buildings occupied by the Group are valued in accordance with generally recognised methods of valuation. The aggregate unrealised surplus or deficit is included in the Technical Account – Long-term Business. It is the Group's practice to maintain these assets in a continual state of repair and to extend and make improvement thereto from time to time; accordingly, the Directors consider that the lives of these assets are sufficiently long and residual values, based on prices prevailing at the time of acquisition or subsequent valuation, are sufficiently high that any depreciation would be immaterial.

Investments in Group undertakings and participating interests

In the balance sheet of the Society, investments in Group undertakings are stated at current value which is equal to cost less any provision for the impairment.

Recognition and derecognition of financial instruments

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or substantially all the risks and rewards of the asset. Purchases and sales of financial assets are accounted for at the trade date; that is the date that the Group commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

g. Investments (cont.)

Financial Investments

The Group classifies its financial investments as either financial assets at fair value through profit or loss or loans and receivables.

Financial assets at fair value through profit or loss are initially recognised and subsequently measured at fair value in the balance sheet with transaction costs taken directly to the income and expenditure accounts. All changes in fair value are recognised in profit or loss as described in accounting policy F - 'Investment income and unrealised gains and losses on investments'.

The methodology for determining the fair value for financial assets is as follows:

- listed and other quoted investments are carried at stock exchange bid values at the balance sheet date;
- linked investments, including redeemable debt and other fixed income securities, and listed and other quoted investments, are stated at bid prices; and
- unlisted investments are carried at fair value as determined by the Directors.

Loans and receivables, comprising mortgages and other loans, are recognised when cash is advanced to borrowers. These are carried at amortised cost using the effective interest method. To the extent that the loan is uncollectable, it is written off as impaired in the long-term business account. Subsequent recoveries are credited back to the long-term business technical account.

Derivative financial instruments

Derivative financial instruments include financial instruments that derive their value from underlying equity instruments. All derivatives clarified as held for trading on initial recognition in the balance sheet are recognised at their fair value, which usually represents their cost, including any premium paid. They are subsequently re-measured at their fair value with changes in the fair value recognised immediately in UPR gains and losses on investments. All derivatives are carried as assets when the fair values are positive and as liabilities when the fair values are negative. None of the derivative financial instruments used by the Group are used for hedge accounting.

The notional or contractual amounts associated with derivative financial instruments are not recorded as assets or liabilities on the balance sheet as they do not represent the fair value of these transactions. Collateral pledged by way of cash margins on futures contracts is recognised as an asset on the balance sheet within cash and cash equivalents.

h. Non-Technical Account

Revenue is recognised as follows:

Fee income paid to Engage Mutual Administration Limited in relation to the provision of administration services is recognised when the services are provided, to the extent the amounts are considered recoverable.

Rebates payable to Engage Mutual Funds Limited by external fund managers are recognised when they are receivable.

Introductory and referral fees earned by Engage Mutual Services Limited are recognised on inception of the underlying arrangement. Where necessary, provisions for cancellations are made at the time the fees are recognised, and are deducted from the revenue. To the extent that the provision for cancellations differs to actual experience, the difference is netted from introductory and referral fees.

i. Fixed assets

Depreciation is provided on the cost of assets in annual instalments over their estimated lives. The cost of new computer software is depreciated in full in the year in which it is incurred and eliminated from the accounts after five years. The rates of depreciation applied per annum are as follows:

Fixtures, fittings and office equipment	20% straight line
Computer equipment	25% straight line
Motor Vehicles	25% straight line

statement of accounting policies (cont.)

j. Valuation of insurance liabilities

The Long-Term Business Provision is determined by the Society's Actuarial Function Holder following his annual investigation of the long-term business, which is based on methods and assumptions that have been approved by the Board of Directors. It is calculated initially to comply with the reporting requirements under the Prudential Sourcebook for Insurers ('Inspru'). This statutory solvency basis of valuation is then adjusted by eliminating certain reserves required under Friendly Society Regulations. This adjusted basis is referred to as the modified statutory solvency basis.

No explicit provision is made for future final (terminal) bonuses under this basis. Implicit provision for part of future yearly (reversionary) bonuses is included in the long-term business provision.

k. Linked investment contracts

Linked investment contract liabilities are measured at fair value as their value is directly linked to the market value of the underlying portfolio of assets. The fair value of a unit-linked contract is equal to the market value of the units held (i.e. the unit reserve).

In 2013, linked financial investments include pension linked assets. In 2012, these assets were presented as non-linked financial investments. Had the 2012 linked and non-linked financial investments been presented on the same basis as 2013, the linked financial investments would have been £63,091,000 higher at £364,397,000 (formerly £301,306,000) and the non-linked financial investments would have been £63,091,000 lower at £280,435,000 (formerly £343,526,000).

l. Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws enacted or substantially enacted at the balance sheet date.

Deferred tax assets and liabilities are recognised in accordance with the provisions of Financial Reporting Standard 19 'Deferred Taxation' ('FRS 19'). The Society has chosen not to apply the option available under FRS 19 of discounting such assets and liabilities to reflect the time value of money. Except as set out in FRS 19, deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date. Deferred tax assets are recognised only to the extent that it is regarded as more likely than not that they will be recovered.

m. Pension costs

The Group operates a defined benefit pension scheme for staff whose employment commenced before 6 April 2001; the scheme was closed to future accruals on 31 December 2012. The financial statements reflect the changes in value of the scheme's assets less the present value of the scheme's liabilities. A pension asset is only recognised in the consolidated balance sheet to the extent that the pension surplus is recoverable through either a refund or reduced future contributions.

The pension cost for the scheme is analysed between the current service cost, past service cost and net return on pension scheme. Current service cost is the actuarially calculated present value of the benefits earned by the active employees in each period. Past service costs, relating to employee service in prior periods arising in the current period as a result of the introduction of, or improvement to, retirement benefits, are recognised in the profit and loss account in the period in which they are vested. The current and past service costs are included in net operating expenses in the Non-Technical Account.

Net expected return on the pension asset comprises the expected return on the pension assets less interest on scheme liabilities and is included in pension finance income in the Non-Technical Account.

Actuarial gains and losses (changes in the surpluses or deficits due to experience of gains and losses) are charged to the statement of total recognised gains and losses.

The Group operates a defined contribution scheme for staff whose employment commenced after 6 April 2001. Payments to this scheme are treated as an expense when due. They are included in net operating expenses in the Non-Technical Account.

statement of accounting policies (cont.)

n. Foreign currency

Assets and liabilities held in foreign currencies are translated to sterling at rates of exchange ruling at the end of the year. Income and expenditure denominated in foreign currencies are translated at the appropriate rates prevailing during the year.

o. Operating leases

Operating lease payments are accounted for on a straight line basis over the term of the lease. There are no lease incentives.

p. Cash flow statement

The Society, being a mutual life assurance company, is exempt from the requirement under Financial Reporting Standard 1 'Cash Flow Statements' ('FRS 1') to produce a cash flow statement.

q. Fund for future appropriations

The fund for future appropriations represents all funds, the allocation of which has not yet been determined by the end of the financial year. Any surplus or deficit arising on the Technical Account – Long-term Business is transferred to or from the fund on an annual basis. Gains or losses arising on the Technical Account – General Business and Non-Technical Account are also transferred to or from the fund each year.

r. Contingent reinsurance financing

The Group receives reinsurance financing on sales of its Over 50s Life Cover from reinsurers. The financing repayment is contingent upon margins emerging on the business in future years. The advances are receivable at the inception of a policy and are included as income within Other Technical Income in the Technical Account - Long-term Business. The repayment of the financing advance is repayable as the margins emerge and is included in Other Technical Charges. Provision for future repayments is included in the calculations of the long-term business provision.

1. management of financial and insurance risk

a. Market risk – interest rate and equity

Interest rate risk

The Group seeks to match future benefit payments with future income from premiums and investments period by period. This is referred to as asset and liability matching or ALM. When the income and payments in a period do not exactly match, the excess cash inflow must be invested or the cash shortfall must be funded at the interest rates prevailing at the time. The Group sets its reserves based on prudent assumptions about these future interest rates. As market views of future interest rates change, the reserves change. Interest rate risk is the risk that adverse interest rate changes will require reserves to be increased.

A separate interest rate risk arises from the impact of interest rate changes on unit-linked funds invested in fixed interest rate assets. Changes in current interest rates directly affect the market values of the fixed interest assets, which in turn affect unit values. A significant element of the Group's income is directly related to the value of the unit funds through annual management charges. The interest rate risk in this case is that adverse interest rate movements will reduce the value of these unit-linked funds and hence the Group's income.

Equity price risk

The Group has exposure to equity securities both directly through equity securities held and indirectly through holdings in Open Ended Investment Companies (OEICs) and Authorised Unit Trusts which in turn invest, partially and wholly, in equity securities. Exposure to individual companies is managed to ensure compliance with regulatory limits for solvency purposes.

The Group has in place a number of agreements with investment managers to ensure that investment transactions are managed within agreed mandates and benchmarks and which limit the exposure in aggregate terms to equity investments, as well as between specific sectors and asset classes.

On the unit-linked and OEIC funds which the Group manages the equity price risk is borne by our policyholders, since the value of the policyholders' liabilities relate directly to the value of the underlying assets held on their behalf. However, a significant element of income for the Group is derived as a fixed percentage of the market value of unit-linked and OEIC assets and as such any changes in the value of assets impacts future income.

1. management of financial and insurance risk (cont.)

b. Market risk - credit

Credit risk is the risk that counterparties will be unable to pay amounts in full when they fall due. The Group is primarily exposed to credit risk in relation to its reinsurance arrangements, both in relation to the reinsurers' share of the long-term business provision and in relation to amounts they owe on claims which the Group has already paid, and on corporate bonds and bank deposits.

Reinsurance is used to manage insurance risk. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim, the Group remains liable for the payment to the policyholder. The Group monitors the financial strength of its reinsurance counterparties by reviewing credit ratings provided by rating agencies and other publicly available financial information.

Other credit risk arises from exposure to various business counterparties, including insurance intermediaries. The Group conducts appraisals of the level of risk associated with business counterparties at the inception of an agreement, as well as on an on going basis. The Group does not have significant credit risk relating to amounts due from contract holders since policy benefits are directly related to the payment of outstanding premiums.

The assets bearing credit risk, together with an analysis by credit rating are shown below:

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Debt securities and other fixed income securities	210.9	209.8	210.9	206.8
Loans secured by mortgage	3.3	4.9	3.3	4.9
Assets arising from reinsurance contracts held	52.8	61.5	52.8	61.5
Pooled money market instruments	16.9	2.4	13.6	2.4
Cash at Bank and in hand	34.4	36.2	31.2	35.0
Total assets bearing credit risk	**318.3**	314.8	**311.8**	310.6

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Debt and other assets rated as:				
UK Government	162.6	147.2	162.6	147.2
A Rated and above	129.1	144.2	122.6	140.0
B rated - BBB	21.3	17.3	21.3	17.3
Below BBB or not rated	5.3	6.1	5.3	6.1
Total assets bearing credit risk	**318.3**	314.8	**311.8**	310.6

Credit risk on unit-linked assets is borne by the policyholder, since policy benefits are linked directly to assets. These assets are therefore not disclosed in the above credit risk exposures.

1. management of financial and insurance risk (cont.)

c. Liquidity risk

Liquidity risk is the risk that the Society will encounter difficulty in raising funds to meet its cash commitments as they fall due. Liquidity risk may result from either the inability to sell financial assets quickly at their fair values; or from a counterparty defaulting on repayment of a contractual obligation; or from an insurance liability falling due for payment earlier than expected; or from the inability to generate cash inflows as anticipated.

The Group manages a significant value of tax-exempt savings plans based on wholesale cash deposits and maintains a prudent liquidity profile in relation to such deposits. Amounts payable on linked contracts are generally payable on demand and the Group is responsible for ensuring there is sufficient liquidity in the investment portfolio to ensure payments can be made as they fall due. However, the Group policy on the linked funds is such that in certain circumstances it may defer the payments until such time liquid assets can be realised.

With profits contracts can be surrendered before maturity for a cash surrender value. The Group has the discretion to impose market value reductions (MVRs) on early surrender which reduce the amount payable. MVRs contribute to managing the liquidity risk in the With Profits Funds as well as ensuring an equitable treatment between policyholders surrendering and those remaining in the With Profits Funds.

An analysis of the expected maturity periods of the policyholder insurance liabilities, on a discounted basis, net of reinsurance, is set out below.

At 31 December 2013	Total £m	Within 1 year £m	1 - 5 years £m	5 - 15 years £m	More than 15 years £m
Long-term business:					
Non Profit Fund	79.5	2.3	12.4	26.5	38.3
With Profit I	45.7	6.2	19.1	19.6	0.8
With Profit II	66.0	5.5	19.8	30.9	9.8
Total	**191.2**	**14.0**	**51.3**	**77.0**	**48.9**

At 31 December 2012	Total £m	Within 1 year £m	1 - 5 years £m	5 - 15 years £m	More than 15 years £m
Long-term business:					
Non Profit Fund	94.4	2.8	14.9	31.3	45.4
With Profit I	49.7	10.0	18.6	20.1	1.0
With Profit II	83.9	6.9	21.6	44.1	11.3
Total	**228.0**	**19.7**	**55.1**	**95.5**	**57.7**

Due to the long-term nature of the insurance liabilities and the requirement of the Group's investment policies to hold a significant proportion of liquid assets, there is sufficient liquidity to meet claims as they arise.

Investment liabilities are classed as repayable on demand and there is considered to be sufficient liquidity to meet claims as they arise, and the Society has the right to defer repayments in order to realise the corresponding linked assets. As such an analysis of expected maturity periods of the investment liabilities has not been completed.

1. management of financial and insurance risk (cont.)

d. Lapse risk

Lapse rate is a measure of the proportion of long-term policies that leave the Society over a period of time, excluding deaths and maturities. Lapse risk arises where the value of policies remaining in force is lower than anticipated.

The methodology for calculating the long-term business provision for the majority of whole of life business allows the utilisation of PRA Policy Statement 06/14 (PS06/14). Under PS06/14 negative reserves, which are assets sat within the overall long–term business provision, are permitted subject to an allowance for lapses. Higher lapses will lead to the negative reserves being lower.

e. Expense risk

When calculating the value of the policyholder liabilities a prudent allowance is made for future expenses. To the extent that future expenses differ from this allowance the Group is exposed to Expense risk.

The Group has internal management information and governance activity in order to ensure that the levels of ongoing management and acquisition expenses remain within expected levels.

f. Mortality and longevity risk

Mortality risk arises in relation to whole of life business, term assurance and group life business, if the mortality of the lives assured is different to that assumed. The Group manages mortality risk at a portfolio level by using reinsurance arrangements which transfer a large percentage of the mortality risk to our reinsurance partners in return for an agreed reinsurance premium.

Longevity risk in relation to the annuity business would arise if annuitants lived longer than anticipated. The Group manages annuitant longevity risk by setting a prudent valuation assumption and monitoring actual experience. The Group also monitors the need for reinsurance as a tool for managing longevity risk. An increase in longevity would expect to be offset, to an extent, by a decrease in mortality on the whole of life business, and vice versa.

g. Unit-linked investment contracts

For unit-linked investment contracts the Group matches all the policyholder liabilities with assets on which the unit prices or value of the policies are based. There is therefore minimal interest, market or credit risk for the Group on these contracts.

Amounts payable on linked contracts are generally payable on demand and the Group is responsible for ensuring there is sufficient liquidity in the investment portfolio to ensure payments can be made as they fall due. However, the Group policy on the linked funds is such that in certain circumstances it may defer the payments until such time as liquid assets can be realised.

h. Capital management

The Society and its regulated subsidiaries maintain sufficient capital, consistent with the Group's risk profile and the relevant regulatory requirements. Further information about the risk management framework can be found in the Corporate Governance Report on pages 29 to 37.

The Society is a mutual organisation and there are no shareholders. As at 31 December 2013 the available capital resources consisted of the Fund for Future Appropriations (FFA). The FFA is the accumulated surplus that has not yet been allocated to policies. It forms the working capital of the Group and is available to meet risk and capital requirements, as well as any uncertain additional liabilities that may arise in the future.

1. management of financial and insurance risk (cont.)

h. Capital management (cont.)

The Group is subject to regulation by the Prudential Regulation Authority (PRA). In reporting financial strength, capital resources and solvency are measured following the regulations provided by the PRA.

Modified statutory solvency, as determined by the PRA rules, and reported in these financial statements sets liabilities on a prudent basis so that the margins of prudence are expected to be sufficient to withstand shocks or stresses. Stresses are also covered by the resilience component of the capital requirements as reported in the PRA Return. The resulting statutory reserves are tested to ensure that we do not breach our minimum capital requirements on a number of tests including one-off falls in the price of equities, change in yields on fixed income securities, as well as one-off reductions in income. Additional reserves are also held to ensure that the Group can be expected to discharge its responsibilities to policyholders at all times up until their policies mature.

The PRA requires companies to undertake capital tests using a number of market consistent approaches and to report privately to the PRA on the results. The PRA is currently developing the future incentives of the capital requirement rules for insurers – Solvency II. The Solvency II rules are expected to apply from 1st Jan 2016. The Group (including the Society and its regulated subsidiaries) is monitoring the development of the Solvency II requirements, which it currently expects to meet.

Capital management objectives

The Group's objectives in managing capital are that:

- obligations to customers across the Group are met in full when due;
- risks are subject to structured analysis in accordance with the risk appetite agreed by the Board;
- sufficient capital resources are available to fund the growth of the Society;
- the aggregate risk exposure of the Group is to be managed to ensure that the capital resources available always meet the minimum capital requirements set out by the PRA.

notes to the financial statements (cont.)
for the year ended 31 December 2013

1. management of financial and insurance risk (cont.)

Sensitivities

The regulatory capital position is sensitive to changes in market conditions, due to both changes in the value of the assets as well as the effect these changes in market conditions would have on the value of the liabilities. It is also sensitive to the expense and lapse experience and to changes in mortality.

The timing of any impact on capital would depend on the interaction of past experience and assumptions about future experience. In general, if experience had deteriorated or was expected to deteriorate, and management actions were not expected to reduce future impact, then assumptions relating to future experience would be changed. In this way, liabilities would be increased to anticipate the future impact of the worse experience with immediate impact on the capital position.

In managing the capital position the Board has quantified the impacts of the principal risks faced. The tables below show the impact of the main sensitivities on the Group's long-term liabilities in both the current and prior year.

Long-Term Business Provision (LTBP) Sensitivities (£m) - 2013

	Mortality		Lapse	Expenses		Fixed Interest Yields		Equities/Property	
Fund	**5%**	**(5)%**	**10%**	**10%**	**(10)%**	**20%**	**(20)%**	**10%**	**(10)%**
Non Profit Fund	1.4	1.9	0.0	3.4	(3.4)	(5.9)	8.1	n/a	n/a
With Profit I	0.0	(0.0)	n/a	0.2	(0.2)	(0.3)	0.5	0.1	(0.1)
With Profit II	(0.1)	0.1	n/a	n/a	n/a	(0.7)	0.7	0.1	(0.1)
Change in LTBP	**1.3**	**2.0**	**0.0**	**3.6**	**(3.6)**	**(6.9)**	**9.3**	**0.2**	**(0.2)**

Long-Term Business Provision (LTBP) Sensitivities (£m) - 2012

	Mortality		Lapse	Expenses		Gilt Yields		Equities/Property	
Fund	**5%**	**(5)%**	**10%**	**10%**	**(10)%**	**20%**	**(20)%**	**10%**	**(10)%**
Non Profit Fund	1.2	2.3	(0.1)	4.1	(4.0)	(6.5)	7.4	n/a	n/a
With Profit I	0.0	(0.0)	n/a	0.4	(0.4)	(0.9)	1.2	(0.0)	0.0
With Profit II	(0.1)	0.1	n/a	n/a	n/a	(1.8)	2.2	0.1	(0.1)
Change in LTBP	**1.1**	**2.4**	**(0.1)**	**4.5**	**(4.4)**	**(9.2)**	**10.8**	**0.1**	**(0.1)**

The Non Profit mortality assumptions include the annuity business. The 5% increase in mortality shows the impact of increasing mortality rates on non-annuity business to 105% at the expected rate. The 5% fall in mortality sensitivity shows the impact of reducing mortality rates on annuity business to 95% of the expected rate. A decrease in mortality on annuities would expect to be offset, to an extent, by a decrease in mortality on the whole of life business, and vice versa, but this sensitivity is not included above.

Further details of how the capital objectives and related risks are managed are included in the Operating and Financial Review starting on page 12.

1. management of financial and insurance risk (cont.)

Operational risk – key suppliers / business partners

As part of our risk and capital management we consider all aspects of the operational risks relating to our internal processes and business model. Within the evaluation we consider our resilience and protections against financial or operational failure of key suppliers.

Our strategic suppliers and the services they provide to us are as follows:

Strategic Supplier	Services provided
Munich Re	Risk transfer and financial reinsurance services
Hannover Re	Risk transfer and financial reinsurance services
National Australia Banking Group	Savings and protection distribution
Santander Asset Management	Investment management services
Insight Investments	Investment management services
Ecclesiastical Investment Managers	Investment management services
The Bank of New York Mellon	Custody services
The Bank of New York Mellon (International) Limited	Accounting and administration services
Oracle	Database management for policy administration
Microsoft	Software and operating systems for end user computing
Barclays	Principal banker

Funding of subsidiary undertakings

Engage Mutual Funds Limited (EMFL) is a wholly owned subsidiary of Homeowners Friendly Society Limited (the Society) and is a company regulated by the PRA. EMFL is required to hold sufficient capital to meet regulatory capital requirements in its own right and is funded by share capital issued to the Society.

The Society wholly owns Engage Mutual Health (EMH), a company regulated by the PRA, through a holding company, Engage Health Holdings Limited (EHHL). EMH is required to hold sufficient capital to meet regulatory capital requirements in its own right and is funded by share capital issued indirectly to the Society.

The value of assets held to meet the liabilities of the Society and its regulated subsidiaries' capital requirements is determined in accordance with PRA regulations. The value of the subsidiaries is restricted to amounts which are likely to be recovered.

Engage Mutual Administration Limited (EMAL) and Engage Mutual Services Limited (EMSL) are funded by intercompany loans for ongoing financing purposes.

Restrictions on available capital resources

The Society and its regulated subsidiaries are required to hold capital sufficient to meet the PRA's minimum capital requirements. Account is also taken of the Individual Capital Assessment which considers some of the risks the business faces not covered by the statutory basis.

The available capital resources held in the with profits funds are normally only available to meet the capital requirements or be allocated to policyholders of those funds. There are no restrictions on the available capital held in the non profit fund.

The Society's total available capital resources are £93.9m (2012: £79.9m) of which £41.7m (2012: £39.9m) is held in the with profits funds and £52.2m (2012: £40.1m) is held in the Non Profit Fund..

1. management of financial and insurance risk (cont.)

Available capital resources

	Non Profit £'000	With Profits I £'000	With Profits II £'000	Total £'000
Available capital resources as at 31 December 2013:				
Fund for future appropriations	**61,293**	**27,159**	**16,104**	**104,556**
Adjustments in respect of subsidiary undertakings	(4,186)			(4,186)
Adjustment to assets onto regulatory basis	(2,219)	(121)	(22)	(2,362)
Adjustment to liabilities onto regulatory basis	(2,722)	(1,400)		(4,122)
Total available capital resources	**52,166**	**25,638**	**16,082**	**93,886**
Society capital requirements	(8,090)	(4,784)	(4,657)	(17,531)
Subsidiary capital requirements	(2,476)			(2,476)
Excess capital over regulatory requirements	**41,600**	**20,854**	**11,425**	**73,879**

	Non Profit £'000	With Profits I £'000	With Profits II £'000	Total £'000
Available capital resources as at 31 December 2012:				
Fund for future appropriations	**53,874**	**26,109**	**14,405**	**94,388**
Adjustments in respect of subsidiary undertakings	(6,303)	-	-	(6,303)
Adjustment to assets onto regulatory basis	(3,031)	(139)	(9)	(3,179)
Adjustment to liabilities onto regulatory basis	(4,467)	(500)	-	(4,967)
Total available capital resources	**40,073**	**25,470**	**14,396**	**79,939**
Society capital requirements	(8,369)	(4,537)	(5,137)	(18,043)
Subsidiary capital requirements	(2,251)	-	-	(2,251)
Excess capital over regulatory requirements	**29,453**	**20,933**	**9,259**	**59,645**

1. management of financial and insurance risk (cont.)

Analysis of movement

The table below shows how the total available capital resources changed during 2013:

	Non Profit 2013 £'000	With profits I 2013 £'000	With profits II 2013 £'000	Total 2013 £'000
Opening excess capital at 1 January	29,453	20,933	9,259	59,645
Non-linked investment returns	14,976	1,940	4,379	21,295
Life assurance new business costs	(5,448)	(199)		(5,647)
Reinsurance commissions on new business	418			418
Subsidiary Health new business costs	(1,098)			(1,098)
Other*	3,299	(1,819)	(2,213)	(733)
Closing excess capital at 31 December	**41,600**	**20,855**	**11,425**	**73,880**

* this comprises of anything which is excluded from the other lines, capital (excluding new business) and reinsurance commissions.

Surplus capital has increased by £14.2m primarily due to positive market and economic impacts, reduced by our investment in new business in both life and health.

The technical provisions as set out in the Society's regulatory returns and financial statements, which are used to determine capital resources, are analysed in the following table and comprise of the net LTBP, claims outstanding and gross liabilities for investment contracts which are detailed in the balance sheet.

Technical provisions	2013 £'000	2012 £'000
Linked Life	**294,868**	301,326
Linked Pensions	**68,447**	62,546
Non-Linked Life	**252**	298
Non-Linked Pensions	**3,358**	2,278
With Profit Contracts	**109,352**	129,906
Non-participating life insurance contracts	**624**	2,964
Non-participating pension contracts	**85,989**	99,072
Total technical provisions	**562,890**	598,390
Adjustment to regulatory basis of technical provisions	**1,304**	**3,178**
Total net technical provisions in the financial statements	**564,194**	**601,568**

The following guarantees which would have a material value to policyholders are:

- Maturity values – on conventional and unitised with profits policies there is a guarantee that on the maturity date there will be a minimum payout of the sum assured plus any declared bonuses.
- Return of premium guarantees – on certain unitised with profits policies there is a guarantee that an amount not less than the initial premium will be paid out on the policies' 5th, 10th and each subsequent 10th anniversary. An explicit charge is made for this guarantee.

Whilst not specifically a guarantee or option, payouts on conventional and unitised with profits policies are smoothed over time to reduce the effect of short-term fluctuations in investment returns. This primarily applies to payouts on maturities; however, it can apply to a lesser extent on early surrender of certain policies.

The Society has With Profits Funds with policyholder liabilities of less than £500m. As such it is not within the PRA realistic external reporting regime which requires life insurers to measure liabilities on a market consistent basis, valuing options and guarantees at fair value. However, we use realistic techniques in our internal management reporting for the management of the With Profits Funds. Realistic reporting is based on management best estimates and fair value as evidenced by established market prices wherever possible. It therefore represents a better view of the economic risk faced by the Group, which may or may not be more prudent than the statutory solvency tests.

2. segmental analysis

a. Gross premiums

	2013 £'000	2012 £'000
Gross premium income is made up of:		
Society and Group Life Assurance and Pension Business		
Non profit non-linked contracts:		
- periodic premium	**24,780**	23,190
- single premium	**458**	948
With profits contracts:		
- periodic premium	**8,401**	8,997
- single premium	**183**	110
Total gross premiums written - continuing operations	**33,822**	**33,245**
Reinsurance ceded	**(10,282)**	(10,886)
Total earned premiums, net of reinsurance	**23,540**	**22,359**

As described in Accounting Policy D – 'Long term contracts', in accordance with FRS 26, policies are defined as investment rather than insurance contracts and are accounted for on a deposit basis. The premium analysis above excludes £5,249,000 (2012: £7,744,000) which would otherwise be included.

b. Gross new premiums

	2013 £'000	2012 £'000
Society and Group Life Assurance and Pension Business		
Non profit non-linked contracts:		
- periodic premium	**3,358**	3,205
- single premium	**46**	95
With profits contracts:		
- periodic premium	**496**	992
- single premium	**18**	10
Total new annualised periodic premiums	**3,918**	4,302

As described in Accounting Policy D – 'Long-term contracts', in accordance with FRS 26, policies are defined as investment rather than insurance contracts and are accounted for on a deposit basis. The premium analysis above excludes £33,000 (2012: £63,000) which would otherwise be included.

Where regular premiums are received other than annually, the regular new business premiums are included on an annualised basis.

2. segmental analysis (cont.)

c. Contributions received from Child Trust Fund investment business

	2013 £'000	2012 £'000
Regular contributions	**7,724**	8,005
Government allocated contributions	**-**	290
Other single contributions	**1,635**	1,274
Total contributions	**9,359**	**9,569**

Contributions relate to business conducted by Engage Mutual Funds Limited (EMFL), a regulated subsidiary of the Society. The contributions received are invested, by EMFL, into a range of collective investment schemes. As such the contributions received are not included in the income and expenditure accounts, nor are the assets included in the balance sheet.

The value of assets held within the range of collective investment schemes by EMFL, as at the 31 December 2013 is £210.2m (31 December 2012: £176.1m).

3. investment return

	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Income from investments - listed	**18,033**	20,778	**18,033**	20,778
Realised gains on investments	**7,313**	25,570	**7,313**	24,652
Total investment income	**25,346**	46,348	**25,346**	45,430
Unrealised losses / gains on investments	**19,757**	(723)	**16,757**	(55)
Investment management expenses	**(1,725)**	(776)	**(1,725)**	(776)
Total net investment return	**43,378**	44,849	**40,378**	44,599

Total net investment return includes £163,000 (2012: £11,000) of interest income on assets not held at fair value through profit and loss. Mortgage interest is included in note 10, other technical income.

4. claims incurred, net of reinsurance

	2013 £'000	2012 £'000
Society and Group - Technical Account - long-term business		
Gross claims paid	**45,050**	33,856
Change in provision for claims outstanding at year end	**1,494**	2,380
Gross claims incurred	**46,544**	36,236
Outward claims reinsurance	**(6,486)**	(5,589)
Total claims incurred, net of reinsurance	**40,058**	30,647

As described in Accounting Policy D – 'Long-term contracts', in accordance with FRS 26 policies defined as investment rather than insurance contracts are accounted for on a deposit basis. The claims analysis above excludes £42,947,000 (2012: £45,073,000) which would otherwise be included.

5. bonuses

The value of terminal bonuses paid to With Profit policyholders in the year was £3.2m (2012: £2.1m).

6 net operating expenses

Technical Account - long-term business	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Acquisition costs	**5,648**	5,540	**5,648**	5,540
Change in deferred acquisition costs	**202**	304	**202**	304
Administrative expenses	**8,763**	8,316	**8,763**	8,316
Reinsurance commissions and profit participation	**-**	7	**-**	7
Net operating expenses	**14,613**	14,167	**14,613**	14,167

Technical Account – General Business	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Net operating expenses	**3,442**	3,979	**-**	-

Non-Technical Account	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Net operating expenses	**2,365**	2,175	**-**	-
Total net operating expenses	**20,420**	20,321	**14,613**	14,167

Total commission paid by the Society on new business was £32,300 (2012: £88,000). Total commission paid by the Group was £3,337,900 (2012: £3,203,000).

Expenses incurred in the subsidiary companies are included in net operating expenses in the Technical Account – General Business and the Non-Technical Account.

7. auditor's remuneration

During the year the Group obtained the following services from KPMG Audit Plc and KPMG LLP, at costs as detailed below:

	2013 £'000	2012 £'000
Audit services		
Fees payable to the company's auditor for the audit of the company's annual accounts;	**103**	90
Audit of the accounts of subsidiaries	**32**	32
Audit-related assurance services	**51**	28
Non-audit services		
Tax compliance services	**6**	-
Other assurance services	**26**	5
Other non audit services	**46**	50
Total	**264**	205

8. operating lease rentals

Annual commitments under non-cancellable leases are as follows:

	2013 £'000	2012 £'000
Group		
Operating leases which expire:		
- within one year	**56**	56
- between two and five years	**21**	59
Total	**77**	115

Payments made under operating leases were:

	2013 £'000	2012 £'000
Hire of fixtures and fittings - rental under operating leases	**40**	86
Hire of other assets - rental under operating leases	**37**	36
Total	**77**	122

9. staff costs

	2013 £'000	2012 £'000
Wages and salaries	**7,837**	7,483
Social security costs	**758**	716
Other pension costs	**463**	670
Total staff costs	**9,058**	8,869

The average number of full time equivalent (FTE) employees in the Group during the year, including Directors, is as follows:

	2013 £'000	2012 £'000
Administration	**137**	140
Management	**27**	26
Marketing	**39**	33
Total number of staff	**203**	199

All staff are employed and remunerated by Engage Mutual Administration Limited, the Group administration company. As such no staff are employed directly by the Society. For details of the Directors' remuneration, please refer to the report of the Directors on remuneration, on pages 38 to 41.

10. other technical income, net of reinsurance

Other technical income comprises:

Technical Account - long-term business	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Property rental	**12**	19	**402**	486
Annual Management Rebates	**(679)**	-	**(679)**	-
Mortgage interest	**332**	405	**332**	405
Reassurance Financing Advance	**4,569**	4,831	**4,569**	4,831
Total other technical income	**4,234**	5,255	**4,624**	5,722

Other technical income in the Society includes rental charged to its subsidiary Engage Mutual Administration Limited, for the use of Gardner House. It also includes interest on bank deposits, mortgages and reinsurance financing advances receivable in relation to the sale of new Over 50s Life Cover policies. Property rental in the Group is in relation to the investment property in Kew Gardens.

11. other income

Other income comprises:

	2013 £'000	2012 £'000
Annual management charges from CTF business	**2,937**	2,445
Other operating income	**1,242**	1,100
Total other income	**4,179**	3,545

Other operating income principally relates to amounts receivable from third party insurance intermediary commissions.

12. taxation

Analysis of the tax charge for the period is:

	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Corporation tax				
Policyholder tax charge / (credit)	**37**	(307)	**37**	**(307)**
Deferred tax				
Timing differences, origination and reversal	**-**	-	**-**	**-**
Total tax charge / (credit)	**37**	(307)	**37**	(307)

The tax charge for the Group is included in the Technical Account – Long-term Business (£37,000 [2012: £307,000 credit]) and the Non-Technical Account (nil [2012: £ nil credit]). The charge in respect of policyholder tax relates to a tax credit in 2012 allowed for in the linked investment business pricing.

12. taxation (cont.)

The weighted average applicable UK corporation tax rate is 23.25% for the subsidiaries (2012: 24.5%), due to the reduction of the UK corporation tax rate from 24% to 23%, which was effective from 1 April 2013.

The Finance Act 2013, substantively enacted on 17 July 2013, included legislation reducing the UK corporation tax rate from 24% to 23% with effect from 1 April 2013, and to 21% on 1 April 2014.

A further reduction to the UK tax rate has been announced. The change, which is expected to be enacted next year, proposes to reduce the rate by a further 1% to 20% on 1 April 2015. The change has not been substantively enacted at the balance sheet date and, therefore, is not recognised in these financial statements.

The UK rate of income tax is 20% for the Society (2012: 20%).

The current year tax charge differs from the standard rates for the reasons set out in the following reconciliation.

Reconcilliation of current year tax charge	**Group 2013 £'000**	Group 2012 £'000	**Society 2013 £'000**	Society 2012 £'000
Loss on ordinary activities	**(509)**	(1,274)	**-**	-
Tax included in Non-Technical Account	**-**	-	**-**	-
Result for year after tax	**(509)**	(1,274)	**-**	-
Tax on result	**(118)**	(312)	**-**	-
Factors affecting tax charge:				
Accelerated capital allowances	**7**	(11)	**-**	-
Items disallowable in tax computation	**59**	6	**-**	-
Timing differences	**(69)**	(71)	**-**	-
Group consolidation adjustments	**(91)**	(116)	**-**	-
Prior year adjustment	**-**	-	**-**	-
Movement in unprovided deferred tax asset	**212**	504	**-**	-
Current corporation tax credit for the year	**-**	-	**-**	-

Analysis of deferred tax asset:

	Group 2013 £'000	Group 2012 £'000	**Society 2013 £'000**	Society 2012 £'000
Timing differences	**853**	853	**-**	-
Deferred tax provision on unrealised gains	**-**	-	**-**	-
Total recognised deferred tax asset / (provision)	**853**	853	**-**	-
Unrecognised deferred tax assets	**15,889**	15,646	**9,997**	9,397
Total	**16,742**	16,499	**9,997**	9,397

Deferred tax expected to reverse in the year ended 31 December 2014 has been remeasured using the effective rate that is expected to apply in the period (21.5%) and at 21% for reversals expected after that date.

Deferred tax assets are included in the Balance Sheet – Assets and deferred tax liabilities are included in the Balance Sheet – Liabilities. The net amount is shown below.

12. taxation (cont.)

Analysis of movement in recognised deferred tax asset / (provision)

	Group 2013 £'000	Group 2012 £'000	**Society 2013 £'000**	Society 2012 £'000
Provision at start of the period	**853**	853	**-**	-
Deferred tax credit to Technical Account - Long-term business	**-**	-	-	-
Deferred tax credit to Non-Technical Account	**-**	-	-	-
Provision at end of the period	**853**	853	**-**	-

13. land and buildings

Group and Society	**Current Value 2013 £'000**	Current Value 2012 £'000	**Historical cost 2013 £'000**	Historical cost 2012 £'000
Land and buildings				
- Property occupied by the Group and Society	**4,000**	4,000	**8,147**	8,147
- Investment property	**1,075**	1,075	**816**	625
Balance at 31 December	**5,075**	5,075	**8,963**	8,772

Land and buildings are all freehold. The full external professional valuation of the property occupied by the Group was carried out by King Sturge, Chartered Surveyors at 31 December 2012, and has been reviewed by the Directors at 31 December 2013.

The full external professional valuation of the investment property was carried out by W Hallett & Co., Chartered Surveyors at 31 December 2011, and has been reviewed by the Directors at 31 December 2013.

14. investments in group undertakings

The Society investment in subsidiaries can be analysed as follows:

	2013 £'000	2012 £'000
Cost at 1 January	**13,500**	15,850
Additions	**3,000**	1,000
Disposals	-	(3,350)
Cost at 31 December	**16,500**	13,500
Provision at 1 January	**(3,550)**	(3,550)
Provided in the year	**(3,000)**	(1,000)
Released in the year	**-**	1,000
Provision at 31 December	**(6,550)**	(3,550)
Carrying value at 31 December	**9,950**	9,950

On 1 January 2011, the general insurance business previously underwritten by Engage Mutual Insurance Limited was renewed with EMH. Following the run off of the general insurance liabilities, the regulatory permissions were rescinded by the Gibraltar Financial Services Commission and the Directors voluntarily liquidated the company on 12 April 2012.

On 24 December 2012, the Society subscribed for 1,000,000 ordinary £1 shares in Engage Health Holdings Limited for a consideration of £1,000,000. On 24 December 2012, Engage Health Holdings Limited subscribed for 1,000,000 ordinary £1 shares in Engage Mutual Health for a consideration of £1,000,000.

On 15 March 2013, the Society subscribed for 3,000,000 ordinary shares in Engage Health Holdings Limited for a consideration of £3,000,000. On 15 March 2013, Engage Health Holdings Limited subscribed for 3,000,000 ordinary shares in Engage Mutual Health for a consideration of £3,000,000.

Engage Mutual Health made losses in prior years, as investment into health insurance was made, and this investment is expected to continue in the short-term, accordingly a provision of £4,000,000 has been provided in relation to the Society's investment.

On 17 December 2013, Engage Foundation was incorporated as a company limited by guarantee.

On 7 March 2014, the Society subscribed for 1,000,000 ordinary shares in Engage Health Holdings Limited for a consideration of £1,000,000. On 7 March 2014, Engage Health Holdings Limited subscribed for 1,000,000 ordinary shares in Engage Mutual Health for a consideration of £1,000,000.

Set out below are the Society's investments in subsidiary undertakings as at 31 December 2013, all of which are included in the consolidation; the carrying value of these subsidiaries cancel out on consolidation. All companies are incorporated in England and Wales.

Name of Subsidiary Undertaking	Nature of Business
Engage Mutual Funds Limited	Child Trust Fund management
Engage Mutual Administration Limited	Administration Services
Engage Mutual Services Limited	Insurance and non-regulated financial product intermediary
Engage Health Holdings Limited	Holding company for Engage Mutual Health
Engage Mutual Health	General insurance
Engage Foundation	Funding for community projects

The subsidiaries are wholly-owned by the Society, except for Engage Mutual Health which is wholly-owned by Engage Health Holdings Limited.

15. financial instruments

FRS 29 Financial Instruments: Disclosures, requires disclosure of the fair value measurement basis for valuing financial instruments. Management consider that the carrying amounts of all Financial Assets and Liabilities recorded at amortised cost in the financial statements are approximate to their fair value.

In 2013, linked financial investments include pension linked assets. Had the 2012 linked and non-linked financial investments been presented on the same basis as 2013, the linked financial investments would have been £63,091,000 higher at £364,397,000 (formerly £301,306,000) and the non-linked financial investments would have been £63,091,000 lower at £280,435,000 (formerly £343,526,000).

The financial investments held by the Group are valued as:

Group	2013 £'000	2012 £'000
Linked financial investments	**364,513**	301,306
Non-linked financial investments	**259,563**	343,526
Total financial investments	**624,076**	**644,832**

These can then be further analysed out into the following categories;

Group	Fair value 2013 £'000	Fair value 2012 £'000	Cost 2013 £'000	Cost 2012 £'000
Financial assets held at fair value through profit and loss				
Shares, other variable yield securities and holdings in collective investment schemes	**258,746**	216,986	**196,990**	193,562
Debt securities and other fixed income securities	**257,024**	289,883	**254,787**	268,692
Derivatives held at fair value through profit and loss	**218**	144	**-**	-
Financial assets held at fair value through profit and loss	**515,988**	507,013	**451,777**	462,254
Loans and receivables				
Loans secured by mortgage	**3,380**	4,865	**3,380**	-
Deposits with credit institutions	**98,081**	120,156	**98,081**	120,156
Accrued income and receivables	**6,627**	12,798	**6,627**	12,798
Loans and receivables	**108,088**	137,819	**108,088**	132,954
Total Group financial assets	**624,076**	644,832	**559,865**	595,208
Financial liabilities				
Financial liabilities at fair value through profit and loss	**364,313**	365,443	**364,313**	365,443
Financial liabilities held at amortised cost	**3,391**	2,798	**3,391**	2,798
Total Group financial liabilities	**367,704**	368,241	**367,704**	368,241

15. financial instruments (cont.)

The financial investments held by the Society are valued as:

Society	2013 £'000	2012 £'000
Linked financial investments	**364,513**	301,306
Non-linked financial investments	**256,250**	340,509
Total financial investments	**620,763**	**641,815**

These can then be further analysed out into the following categories;

Society	Fair value 2013 £'000	Fair value 2012 £'000	Cost 2013 £'000	Cost 2012 £'000
Financial assets held at fair value through profit and loss				
Shares, other variable yield securities and holdings in collective investment schemes	**255,434**	216,970	**193,679**	193,544
Debt securities and other fixed income securities	**257,024**	289,883	**254,787**	268,692
Derivatives held at fair value through profit and loss	**217**	144	**-**	-
Financial assets held at fair value through profit and loss	**512,675**	506,997	**448,466**	462,236
Loans and receivables				
Loans secured by mortgage	**3,380**	4,865	**3,380**	-
Deposits with credit institutions	**98,081**	117,155	**98,081**	120,156
Accrued income and receivables	**6,627**	12,798	**6,627**	12,798
Loans and receivables	**108,088**	134,318	**108,088**	132,954
Total Group financial assets	**620,763**	641,815	**556,554**	595,208
Financial liabilities				
Financial liabilities at fair value through profit and loss	**364,313**	365,443	**364,313**	365,443
Financial liabilities held at amortised cost	**2,531**	2,798	**2,531**	2,441
Total Society financial liabilities	**366,844**	367,885	**366,844**	367,885

The valuation method for each category of financial instrument must be disclosed by reference to three 'levels'.

Level 1 – The unadjusted quoted price where there is an active market for buying and selling the financial instrument.

Level 2 – Valuation techniques based on observable inputs, either directly (as prices) or indirectly (derived by prices). This includes financial instruments with a quoted market price but no active market.

Level 3 – Valuation techniques using significant unobservable inputs, which have a significant impact on the instrument's valuation.

notes to the financial statements (cont.)
for the year ended 31 December 201

15. financial instruments (cont.)

Group	Level 1 Active quoted prices £'000	Level 2 Other observable inputs £'000	Total £'000
Financial assets held at fair value through profit and loss			
Shares, other variable yield securities and holdings in collective investment schemes	281,880	94,851	**376,731**
Debt securities and other fixed income securities	106,224	32,815	**139,039**
Derivatives held at fair value through profit and loss	218	-	**218**
Financial assets held at fair value through profit and loss	**388,322**	**127,666**	**515,988**
Financial liabilities held at fair value through profit and loss	**-**	364,313	**364,313**
Financial liabilities held at fair value through profit and loss	**-**	**364,313**	**364,313**

Society	Level 1 Active quoted prices £'000	Level 2 Other observable inputs £'000	Total £'000
Financial assets held at fair value through profit and loss			
Shares, other variable yield securities and holdings in collective investment schemes	278,568	94,851	**373,419**
Debt securities and other fixed income securities	106,224	32,815	**139,039**
Derivatives held at fair value through profit and loss	217	-	**217**
Financial assets held at fair value through profit and loss	**385,009**	**127,666**	**512,675**
Financial liabilities held at fair value through profit and loss	**-**	364,313	**364,313**
Financial liabilities held at fair value through profit and loss	**-**	**364,313**	**364,313**

16. other debtors

	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Amounts owed from Group undertakings	-	-	2,149	1,363
Amounts owed from policyholders	424	706	351	706
Amounts owed from intermediaries	997	1,564	997	1,184
Debtors arising out of reinsurance operations	218	344	218	344
Other debtors	1,092	565	155	151
Total debtors	**2,731**	3,179	**3,870**	3,748

17. tangible assets

Group	Motor Vehicles equipment £'000	Computer equipment £'000	Fixtures, fittings and office equipment £'000	Total £'000
Cost				
At 1 January 2013	7	1,050	1,004	2,061
Additions	-	77	29	106
At 31 December 2013	7	1,127	1,033	2,167
Depreciation				
At 1 January 2012	7	828	747	1,582
Provided in the year	-	128	71	199
At 31 December 2013	7	956	818	1,781
Net book value at 31 December 2013	-	**171**	**215**	**386**
Net book value at 31 December 2012	-	222	257	479

The charge for depreciation for the Group in the year ended 31 December 2012 was £171,000.

18. deferred acquisition costs

	2013 £'000	2012 £'000
On With Profits contracts	**121**	139
On Non Profit contracts	**137**	321
Total deferred acquisition costs	**258**	460

The direct costs of acquiring certain policies are capitalised and are amortised in line with the expected life of the policies.

19. technical provisions

Group	Long-term business provision (LTBP) £'000	Reinsurers' share of LTBP £'000	Provision for outstanding claims £'000
At 1 January 2013	**289,932**	**(61,458)**	**7,661**
Movement in provision for outstanding claims			1,562
Change in Long-Term Business Provision	(45,408)	8,630	
Balance at 31 December 2013	**244,524**	**(52,828)**	**9,223**

Society	Long-term business provision (LTBP) £'000	Reinsurers' share of LTBP £'000	Provision for outstanding claims £'000
At 1 January 2013	**289,418**	**(61,458)**	**7,205**
Movement in provision for outstanding claims			1,494
Change in Long-Term Business Provision	(45,408)	8,630	
Balance at 31 December 2013	**244,010**	**(52,828)**	**8,699**

The above tables disclose the technical provisions for the Group and the Society. Included in the Group disclosure is a long-term business provision of £514,000 and a provision for outstanding claims of £523,000, both in respect of Engage Mutual Health.

Uncertainties and estimation techniques

One of the purposes of insurance is to enable policyholders to protect themselves against uncertain future events. Insurance companies accept the transfer of uncertainty from policyholders and seek to add value through the aggregation and management of these risks. The uncertainty inherent in insurance is inevitably reflected in the financial statements of insurance companies and principally arises in respect of the technical provisions of the company. As a consequence of this uncertainty, the insurance company needs to apply sophisticated estimation techniques to determine the appropriate provisions.

Long-term business provisions (LTBP) are computed using statistical and other mathematical techniques, which are expected to give approximately the same results as if an individual liability were calculated for each long-term contract. The computations are made by suitably qualified personnel employed by the Group on the basis of recognised actuarial methods. This methodology takes into account the risks and uncertainties of the particular classes of long-term business written and the results are certified by the professionals undertaking the valuations.

Process for determining assumptions

The process used to determine any assumptions is intended to result in conservative estimates of the most likely, or expected, outcome. The assumptions are checked to ensure they are consistent with observed market practice or other published information.

For insurance contracts the Group regularly considers whether the current liabilities are adequate. The assumptions that are considered include the expected number and timing of deaths, other claims and investment returns, over the period of risk exposure. A reasonable allowance is made for the uncertainty within the contracts.

The principle assumptions underlying the calculation of the long-term business provision are:

Mortality – a base mortality table is selected which is most appropriate for each type of contract taking into account rates charged to the Society by reinsurers.

Valuation Rates of Interest – these are set in relation to the risk adjusted yields on the underlying assets as per the regulations and guidance from the PRA.

Expenses – these assumptions are determined from the results of an internal expenses investigation with additional margins for prudence.

The LTBP has been calculated on the basis of the following principal interest assumptions for 2013:

Class of business	Interest
Non-linked Annuities tax exempt / taxable	3.21% gross / 3.59% net
Index-linked Annuities tax exempt / taxable	3.08% gross / 3.08% net
Term Assurance / whole of life	3.21%
With Profits I unitised with profits tax exempt / taxable	2.49% gross / 1.89% net
With Profits I conventional with profits tax exempt / taxable	2.19% gross / 2.15% net
With Profits II with profits bond taxable	2.89% net
With Profits II conventional with profits tax exempt / taxable	2.22% gross / 1.19% net

19. technical provisions (cont.)

The mortality assumptions have been based on actual experience with the addition of prudent margins.

With profits bonuses

The LTBP includes £0.5m (2012: £0.9m) for reversionary bonuses to be declared. The cost of any bonuses is included in "Change in Long-term Business Provision" in the Long-Term Business – Technical Account. The cost of terminal bonuses on with profits policies is included in "Gross claims incurred" in the Long-Term Business – Technical Account.

20. gross liabilities for investment contracts

	2013 £'000	2012 £'000
At 1 January	**365,443**	377,771
Deposits from policyholders in respect of investment contracts	**5,249**	7,744
Withdrawals to policyholders in respect of investment contracts	**(42,947)**	(45,073)
Annual management charges on investment contracts	**(2,314)**	(3,039)
Change in fair value of gross liabilities for investment contracts	**38,882**	28,040
At 31 December	**364,313**	**365,443**

As described in the Accounting Policy C – 'Classification of Contracts', in accordance with FRS 26, policies defined as investment, rather than insurance contracts are accounted for on a deposit basis.

21. creditors arising out of insurance operations

Creditors are in relation to reinsurance contracts and health insurance business. Creditors also includes £240,000 (2012: £300,000) for an unexpired risk provision relating to certain classes of private medical insurance written by Engage Mutual Health. All creditors are payable within five years.

22. other creditors, including social security and taxation

	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Amounts owed to Group undertakings	**-**	-	**330**	782
Other taxes and social security costs	**305**	311	**-**	-
Other creditors	**1,971**	1,358	**1,400**	893
Total	**2,276**	1,669	**1,730**	1,675

All other creditors are payable within five years.

23. fund for future appropriations

	Group 2013 £'000	Group 2012 £'000	Society 2013 £'000	Society 2012 £'000
Balance at 1 January	**83,885**	84,542	**94,388**	93,502
Transfer from Long-Term Business - Technical Account	**12,776**	1,094	**10,168**	886
Total recognised gains and (losses)	**(837)**	(1,751)	**-**	-
Balance at 31 December	**95,824**	**83,885**	**104,556**	**94,388**

The surplus in the pension scheme has not been recognised in 2013 and was not recognised in the prior year. Further information is included in Note 24.

24. pension commitments

Defined contribution scheme

The Society operates a defined contribution stakeholder pension scheme for all employees joining the Group after 29 March 2001. A number of employees have their own defined contribution pension arrangements to which the Group is equally happy to contribute. The pension cost charge for the period represents contributions payable by the Society and amounted to £493,477 (2012: £339,275).

Contributions amounting to £45,649 (2012: £64,838) were payable at the end of 2013 to the scheme and are included in creditors.

Defined benefit scheme

The Society operates a defined benefit pension scheme for its staff whose employment commenced before 29 March 2001. During 2011 the Directors reviewed the pension arrangements and took the decision to close the defined benefit pension scheme and offer the defined contribution scheme as a replacement, to any service accruals after 31 December 2012. Compensation, which comprises additional service accruals between 1 January 2011 and 31 December 2012, has been awarded to affected members and the cost of this is shown as past service cost when it was awarded.

The pension scheme is accounted for under FRS 17 'Retirement Benefits'. During 2013 the company contributed into the scheme at a rate of nil (2012: £559,400), per the agreed funding schedule. An additional special contribution of £96,000 was made during 2013 (2012: £75,000). As the scheme is closed to new entrants and was closed to future accruals in 2013, under the Projected Unit Method, the service cost will increase as the remaining members reach retirement.

The contributions are determined by the Scheme Actuary on the basis of triennial valuations. A full actuarial valuation is performed every three years by the Scheme Actuary, and is updated annually to calculate the present value of scheme liabilities. A full actuarial valuation of the Homeowners Friendly Society Pension Scheme was carried out as at 31 December 2010.

The assets of the defined benefit scheme are held separately from those of the company in an independently administered fund.

The funding level of the defined benefit pension scheme is set out in the full triennial valuation and is not based on the FRS 17 methodology which is used for financial reporting purposes. The Directors have agreed a schedule of normal contributions with the Scheme Actuary and the trustees and the company is also making additional special contributions. The Directors have reviewed the recoverability of the FRS 17 pension surplus through either a refund or reduced future contributions and have restricted the surplus to zero in line with the accounting policy as there is no restricted rights to the surplus.

24. pension commitments (cont.)

The other major assumptions used by the Actuary to calculate Scheme liabilities were:

	2013 % per annum	2012 % per annum	2011 % per annum
Long-term salary progression	**-**	2.40	-
Rate of increase in pension payments guaranteed	**3.30**	3.00	3.05
Rate of price inflation and deferred pension revaluation	**2.45**	2.40	2.15
Discount rate	**4.45**	4.60	4.75

The Government recently proposed changes to pension legislation relating to the measure of inflation being linked to increases in deferred pensions. As the scheme is closed to additional service accruals, active members have become deferred members. At the balance sheet date a gain on curtailment of nil (2012: £nil) has been recognised.

The company employs a building block approach in determining the long-term rate of return on pension plan assets. Historical markets are studied and assets with higher volatility are assumed to generate higher returns consistent with widely accepted capital market principles. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation for the Scheme at the 31 December 2013.

The total assets and liabilities in the scheme and the expected rates of return were:

	Long-term rate of return expected at 31 December			Value at 31 December		
	2013 % per annum	2012 % per annum	2011 % per annum	**2013 £'000**	2012 £'000	2011 £'000
Equities	**7.70**	8.00	8.00	**4,397**	3,456	3,046
Gilts	**3.60**	2.70	2.80	**9,274**	8,844	9,315
Bonds	**4.45**	4.60	4.75	**8,998**	8,946	7,992
Other	**0.80**	0.90	1.80	**659**	1,367	1,098
Total market value of schemes assets				**23,328**	22,613	21,451
Present value of scheme liabilities				**(18,911)**	(17,441)	(15,700)
Gross surplus in scheme				**4,417**	5,172	5,751
Unrecognised surplus in scheme				**(4,417)**	(5,172)	(5,751)
Net surplus in scheme				**-**	-	-
Related deferred tax liability				**-**	-	-
Recognised pension asset				**-**	-	-

In the prior years, a composite rate of return has been calculated for corporate bonds and gilts.

24. pension commitments (cont.)

The mortality assumptions used are based on standard mortality tables which allow for future mortality improvements. Under these assumptions the average life expectancies for males and females currently aged 60 are 28.1 years (2012: 28.0 years) and 30.4 years (2012: 30.3 years) respectively.

a. Reconciliation of present value of scheme liabilities

	2013 £'000	2012 £'000
At 1 January	**(17,441)**	(15,700)
Current service cost	-	(254)
Past service cost	-	(75)
Interest cost	**(792)**	(737)
Contibutions by scheme participants	-	(52)
Benefits paid	**455**	428
Net actuarial loss	**(1,133)**	(1,051)
At 31 December	**(18,911)**	(17,441)

b. Reconciliation of market value of scheme assets

	2013 £'000	2012 £'000
At 1 January	**22,613**	21,451
Expected return on plan assets	**792**	909
Contributions paid by employer	**328**	634
Contibutions by scheme participants	**-**	52
Benefits paid	**(455)**	(428)
Acuarial gains	**50**	(5)
At 31 December	**23,328**	22,613

c. Analysis of charges to Non-Technical Account (included in net operating expenses)

	2013 £'000	2012 £'000
Current service cost	**-**	254
Past service cost	**-**	75
Total charge	**-**	329

24. pension commitments (cont.)

d. Analysis of amounts credited to Non-Technical Account (pension finance income)

	2013 £'000	2012 £'000
Expected return on pension scheme assets	**(792)**	(909)
Interest on pension scheme liabilities	**793**	737
Net return	**1**	(172)

e. Analysis of recognised gains and losses

	2013 £'000	2012 £'000
Actual return less expected return on pension scheme assets	**50**	(5)
Experience gains and losses arising on the scheme liabilities	**(1,133)**	(1,051)
Changes in assumptions underlying the present value of the scheme liabilities	**0**	0
Actuarial profit in pension scheme	**(1,083)**	(1,056)
Unrecognised pension asset	**755**	579
Total amount recognised in Non-Technical Account	**(328)**	(477)

f. History of experience gains and losses

	2013	2012	2011	2010	2009
Present value of scheme liabilities (£'000)	**(18,911)**	(17,441)	(15,700)	(15,005)	(13,924)
Fair value of scheme assets (£'000)	**23,328**	22,613	21,451	18,323	16,525
Surplus in scheme	**4,417**	5,172	5,751	3,318	2,601
Difference between the expected and actual return on scheme assets (£'000)	**50**	(5)	1,604	924	385
Percentage of scheme assets (%)	**0.2**	(0.0)	7.5	5.0	2.3
Experience (losses) / gains on scheme liabilities (£'000)	**(97)**	(348)	(104)	92	71
Percentage of present value of scheme liabilities (%)	**0.5**	2.0	(0.7)	0.6	0.5
Total amount recognised in STRGL (£'000)	**328**	477	933	194	3,246
Percentage of present value of scheme liabilities (%)	**1.7**	2.7	5.9	1.3	23.3

25. guarantees and financial commitments

Homeowners Friendly Society has made a commitment to its subsidiaries to provide ongoing funding through purchasing shares and providing loans.

26. statement of information relating to the Actuarial Function Holder

The Actuarial Function Holder of the Society is Mr T M Batten, an employee of the Society. The following information has been provided, in accordance with Section 77 of the Friendly Societies Act 1992:

- Mr T M Batten was not a member of the Society at any time during 2013;
- no other member of his family was a member of the Society during 2013;
- Mr T M Batten is a member of the Homeowners Friendly Society Pension Scheme; and
- the aggregate rate of the remuneration and benefits (excluding pension contributions) of Mr T M Batten for 2013 amounted to £120,563.

27. related party transactions

Transactions or balances between Group entities
Homeowners Friendly Society and its subsidiaries (collectively the Group) have a number of transactions between themselves all of which are undertaken in the normal course of business. As these accounts cover the Society and the Group, no transactions or balances between Group entities, which eliminate on consolidation, require disclosure in accordance with the exemption given in FRS 8 'Related Party Disclosures'.

Transactions involving Directors
During 2013, two Directors together with their connected parties held insurance policies on an arms-length basis with the Society. There were no other transactions during the year.

28. post balance sheet event

On 7 March 2014, the Society subscribed for 1,000,000 ordinary shares in Engage Health Holdings Limited for a consideration of £1,000,000. On 7 March 2014, Engage Health Holdings Limited subscribed for 1,000,000 ordinary shares in Engage Mutual Health for a consideration of £1,000,000.

On 23 January 2014, the Engage Foundation was launched with a commitment to make £1,000,000 available to customers over a five year period.

any questions

call free on **0800 028 1045***

*Calls are free from UK landlines only.

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