

Canada Life Limited

**Scheme Report of the  
Independent Expert of the  
Proposed Transfer of non-profit  
annuity business from Canada  
Life Limited to Irish Life  
Assurance plc under Part VII of  
the Financial Services and  
Markets Act 2000**

28 August 2020

Prepared by Jeremy Nurse FIA



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# Section 1: Introduction

## Introduction

- 1.1 When a scheme for transferring insurance business from one company to another is put to the High Court of Justice in England and Wales ("Court") for approval it has to be accompanied by a report on the terms of the scheme from an independent expert (the "Independent Expert"). The Independent Expert's report (the "Scheme Report") is a requirement under Part VII of the Financial Services and Markets Act 2000 ("FSMA").
- 1.2 I, Jeremy Nurse, have been appointed by Canada Life Limited ("CLL") to provide a Scheme Report for the proposed Part VII transfer of certain policies from CLL to Irish Life Assurance plc ("ILA") (the "Proposed Scheme"). This Scheme Report has been prepared for the Court in order to aid the Court's consideration as to whether the Proposed Scheme should be approved.
- 1.3 CLL is an insurance company domiciled in the UK and is authorised by the Prudential Regulation Authority and regulated by the Prudential Regulation Authority ("PRA") and by the Financial Conduct Authority ("FCA"). ILA is an insurance company domiciled in Ireland and is regulated by the Central Bank of Ireland ("CBI"). Both CLL and ILA are members of the Great-West Life Inc ("GWL"), a company domiciled in Canada) group of companies.
- 1.4 As a result of a previous Part VII transfer of insurance business into CLL, the firm currently carries on cross-border insurance business under the EU Freedom of Services passport in relation to policies that were originally written through authorised branches in Ireland and Germany. Due to the recent departure of the UK from the European Union, these passporting arrangements are due to expire from 31 December 2020 and, in order to ensure a continued ability to service these policies written on a cross-border basis beyond this date, CLL and ILA have agreed that the block of Irish and German policies that had previously been transferred into CLL should, under the terms of the Proposed Scheme and with the approval of the Court, be transferred to ILA.
- 1.5 In addition to this Scheme Report, I have also produced a summary of the Scheme Report (the "Summary") which is based on the Executive Summary of the Scheme Report contained within Section 2. The remainder of the Scheme Report contains detailed information that is not shown in the Summary. In particular, the Scheme Report contains the following sections:
  - The remainder of Section 1 sets out the details of the Proposed Scheme, my statement of independence and the terms of reference of my work;
  - Section 2 provides the Executive Summary of the Scheme Report;
  - Section 3 sets out the general considerations that need to be taken into account by the Independent Expert in setting the scope and undertaking the work;
  - Section 4 sets out background on the UK and Irish Life Insurance market and regulatory environment;

- Sections 5 and 6 provide background to the Proposed Scheme and the companies involved;
  - Sections 7 to 11 contain details of the review I have performed, and my findings, with regards to how policyholders may be affected by the Proposed Scheme;
  - Section 12 contains the reliances and limitations of this Scheme Report; and
  - The Appendices contain the statement of my independence, details of the data and information I have used in forming my conclusions, my Certificate of Compliance, a glossary of terms used throughout this report and details of how this Scheme Report complies with the regulatory requirements of the PRA and the FCA.
- 1.6 The Scheme Report and the Summary have been prepared on the instruction of CLL and ILA for the benefit of the Court solely for the purposes of the FSMA requirements for Part VII transfers. I owe a duty to the Court to help the Court on matters within my expertise. This duty overrides any obligation to any person from whom I have received instructions or by whom I am paid.
- 1.7 This Scheme Report, and the Summary, may be distributed to policyholders, the PRA, the FCA and any other person entitled to receive a copy under applicable law or regulation.
- 1.8 This Scheme Report and the Summary may be relied on by the Court. Neither the Independent Expert nor Willis Towers Watson accepts any responsibility or liability to any third party in relation to the Scheme Report or the Summary. Any reliance placed by such third parties on the Scheme Report or the Summary is entirely at their own risk.

## The Independent Expert, qualifications and disclosures

- 1.9 I am a Fellow of the Institute and Faculty of Actuaries, having qualified in 1989. I have acted as the Chief Actuary (and, previously, the Actuarial Function Holder and the Appointed Actuary) for a number of UK and overseas life insurance companies for almost 20 years, the last 12 of which have been as an employee of Willis Towers Watson. I am a Senior Director in the firm of Towers Watson Limited ("TWL") where I am part of the Insurance Consulting and Technology business line. TWL is part of Willis Towers Watson which is a leading global advisory, broking and solutions firm.
- 1.10 Both CLL and ILA are members of the group of companies headed by GWL, which is domiciled in Canada. CLL is a wholly-owned subsidiary of The Canada Life Group (U.K.) Limited ("CLG") (incorporated in England and Wales), which itself is a subsidiary of The Canada Life Assurance Company, a regulated Canadian insurer and a subsidiary of GWL. Irish Life Group Limited was acquired by GWL in 2013 and is a wholly-owned subsidiary of CLL. ILA is a wholly-owned subsidiary of Irish Life Group Limited.
- 1.11 I consider that I have no conflict of interest or involvement, current or historical, with CLL, ILA or any other GWL group companies which would affect my suitability to act as the Independent Expert for the Proposed Scheme. I confirm that I do not have any direct or indirect interest in GWL, CLL, ILA or other related firms that could compromise my independence.

- 1.12 Willis Towers Watson, globally, has relationships with CLL, ILA and other companies in the GWL group of companies. However, I do not consider that the nature and size of these involvements impact on my ability to act as Independent Expert for the Proposed Scheme. I have provided details of these relationships directly to the PRA and the FCA.
- 1.13 My appointment as the Independent Expert in connection with the Proposed Scheme has been approved by the PRA, in consultation with the FCA. A more detailed statement of independence is included in Appendix A of this Scheme Report.
- 1.14 A certificate of compliance with Part 35 of the Civil Procedure Rules is attached as Appendix C. I confirm that I have understood my duty to the Court.

## The purpose and scope of my report

- 1.15 The purpose of the Scheme Report is to review the proposed transfer of the block of Irish and German policies in CLL to ILA under the Proposed Scheme. These policies had originally been written on a cross-border basis by The Equitable Life Assurance Society ("ELAS") through authorised Irish and German branches respectively. These policies had then been transferred to CLL as part of a wider Part VII transfer of insurance business from ELAS in 2016. In particular, I consider the effects of the proposed transfer on the security of the benefits and on the reasonable benefit expectations, service standards, management and governance of the policyholders of CLL and ILA. I have also considered the implications for the relevant parties if the Proposed Scheme was not to go ahead.
- 1.16 The Scheme Report has been prepared under the terms of the guidance set out in the Policy Statement "The Prudential Regulation Authority's approach to insurance business transfers" issued in April 2015 by the PRA (the "PRA Policy Statement"), in Chapter 18 of the Supervision Manual ("SUP 18") contained in the FCA Handbook and in FG 18/4 "The FCA's approach to the review of Part VII insurance business transfers" (the "FCA Guidance"). CLL and ILA have reviewed this report and both companies have confirmed that it is accurate in its description of all factual elements of the proposed transfer.
- 1.17 The Scheme Report will be presented to the Court and will be made available to policyholders via the CLL website. Holders of transferring policies will be sent a Policyholder Guide, which will include a summary of the Proposed Scheme and a summary of my report (written by me). In the case of German policyholders, this will be a German language equivalent of the English version. These summaries will also be made available on the CLL website, along with other Scheme-related documents.
- 1.18 In assessing the impact of the implementation of the Proposed Scheme on the policyholders of CLL and ILA, and whether those policyholders are being treated fairly as a result of the implementation of the Proposed Scheme, I have had regard to:
- The likely effect of the implementation of the Proposed Scheme on the security of policyholders' contractual benefits and on the benefit expectations of policyholders created by past practices employed, or statements made, by each company; and
  - The reports of the Chief Actuaries of CLL and ILA on the impact of the implementation of the Proposed Scheme.

- 1.19 There are no documents or other items of information that I have requested and have not been provided. Appendix B contains a list of the main sources of data and information upon which I have relied.
- 1.20 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Proposed Scheme, and in preparing my report, which nonetheless should be drawn to the attention of the Court in its consideration of the terms of the Proposed Scheme.
- 1.21 I have only considered the terms of the Proposed Scheme presented to me and am not required to consider possible alternative schemes in forming my opinions.
- 1.22 I have also reviewed and considered the contents of advanced drafts of the Policyholder Guide and the accompanying letter (the "Policyholder Letter") which are intended to be sent to all transferring policyholders of CLL, subject to the expected waivers discussed in paragraph 10.9. CLL does not intend to send information on the transfer to its non-transferring policyholders, while ILA does not intend to send information on the transfer to any of its policyholders, and each has applied to the Court for a waiver to that effect.

## Reliances and limitations

- 1.23 In preparing the Scheme Report, I have had access to certain documentary evidence provided by CLL and ILA and I have had access to, and discussions with, senior management of CLL and ILA. I have also held discussions on the Proposed Scheme directly with the PRA and the FCA. My conclusions depend on the substantial accuracy of this information without independent verification. The principal documents which I have reviewed in respect of CLL and ILA are listed in Appendix B. I have considered, and am satisfied with, the reasonableness of this information based upon my own experience of life assurance business and understanding of the relevant regulatory requirements.
- 1.24 This report must be considered in its entirety as individual sections, if considered in isolation, may be misleading. Draft versions of this report should not be relied upon for any purpose. I have provided a summary of my report (the Summary) for inclusion in the Policyholder Guide and for publication on the CLL website (and, where relevant, distribution to any persons requesting a copy of it); other than this, no summary of this report may be made without the express consent of Willis Towers Watson.
- 1.25 This report has been prepared on an agreed basis for the Court, CLL and ILA in the context of the Proposed Scheme and must not be relied upon for any other purpose. No liability will be accepted by Willis Towers Watson, or me, for any application of this report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of this report. In particular, no liability will be accepted by Willis Towers Watson or me under the terms of the Contracts (Rights of Third Parties) Act 1999.
- 1.26 This Scheme Report, the Summary described in paragraphs 1.17 and 1.24 and the Supplementary Report described in paragraph 1.33 do not provide financial or other advice to individual policyholders.
- 1.27 Further reliances and limitations are provided in Section 12 below.



## COVID-19

- 1.28 In the course of preparing this Scheme Report, it has become evident that the coronavirus outbreak named as COVID-19 ("COVID-19"), a rapidly developing global pandemic, is having significant short-term effects on economic activity and creating extensive social disruption, both within the UK and globally. Longer term socio-economic implications and the impact on both liabilities and assets remain uncertain. The situation is fast-moving and changing daily, leading to a high degree of uncertainty about the eventual type and scale of impacts and financial losses that may emerge.
- 1.29 The figures and conclusions in this Scheme Report make no explicit allowance for the effects of COVID-19, although I do provide some initial high-level commentary on the likely effects within Section 10. Based on the information I have already been provided with by the management of CLL and ILA giving a preliminary indication of the likely financial effects of COVID-19 on the firms, I do not currently consider that the impact of COVID-19 will affect my conclusions contained within this Scheme Report. Within my Supplementary Report I will consider more fully the expected effects of COVID-19 on the financial positions of both CLL and ILA, and any resulting impacts upon my conclusions.

## Professional guidance

- 1.30 I am required to comply with relevant technical actuarial standards ("TASs") issued or adopted by the Financial Reporting Council ("FRC") in the UK, and relevant actuarial profession standards ("APSS") issued by the Institute and Faculty of Actuaries ("IFoA") in the UK. This Scheme Report complies with all applicable TASs and APSS. In particular, this Scheme Report has been prepared in accordance with:
- TAS 100: Principles for Technical Actuarial Work, issued by the FRC;
  - TAS 200: Insurance, issued by the FRC;
  - The Actuaries' Code, issued by the IFoA; and
  - APS X2: Review of Actuarial Work and APS X3: The Actuary as an Expert in Legal Proceedings, both issued by the IFoA.

## Peer review

- 1.31 APS X2 issued by the IFoA requires members to consider whether their work requires an independent peer review.
- 1.32 In my view this report does require independent peer review, and this has been carried out by Trevor Fannin FIA, a Senior Director in Willis Towers Watson who has not been part of the team working on this assignment.

## My Supplementary Report

- 1.33 As envisaged by paragraph 2.39 of the PRA Policy Statement, I will prepare a further report (the "Supplementary Report") prior to the Final Hearing to provide an update for the Court on my conclusions on the impact of the implementation of the Proposed Scheme on the different

groups of policyholders in the light of any significant events subsequent to the date of the finalisation of this report, in particular in relation to the current COVID-19 situation and the United Kingdom's exit from the European Union ("Brexit"). My Supplementary Report will also be made available to policyholders, as is usual, by its being placed on the relevant website and sent to those persons who have previously requested a copy of this Scheme Report.

## Legal jurisdiction

- 1.34 This Scheme Report is governed by and shall be construed in accordance with English law. Towers Watson Limited, CLL and ILA submit to the exclusive jurisdiction of the English courts in connection with all disputes and differences arising out of, under or in connection with this Scheme Report.

## Section 2: Executive Summary

- 2.1 This section provides a summary of the Proposed Scheme and a summary of my conclusions. Details and background to the information in this section, as well as definitions of some of the terms used in this section, are in the main body of this report.

### Summary of the Proposed Scheme

- 2.2 The intention of the Proposed Scheme is to transfer a small number of Euro-denominated in-payment individual non-profit annuities to ILA from CLL by means of a Part VII transfer (the “Transferring Policies”). These policies were originally written by ELAS on a cross-border freedom of establishment (branch) basis through authorised German and Irish branches to policyholders, the vast majority of whom had their permanent residence in Germany or Ireland (except four policyholders who were resident in either France, Austria or Spain). The policies were previously transferred to CLL from ELAS by way of a previous Part VII transfer in 2016 and have subsequently been serviced by CLL on a freedom of services (cross-border) basis.
- 2.3 The end of the “implementation period” in relation to the United Kingdom’s exit from the European Union is currently scheduled to occur on 31 December 2020. CLL considers that, after expiry of the implementation period, it is likely to lose its legal rights to service cross-border policies originally issued to policyholders who were habitually resident at the time of issue in the European Union (including the ability to pay claims), due to the loss of the “passport” rights applicable to member states of the European Union. The Board of CLL therefore considers that the transfer of the above policies pursuant to the Proposed Scheme is necessary to ensure that the GWL group can continue to meet its legal and regulatory obligations in relation to the Transferring Policies on an ongoing basis.
- 2.4 The Proposed Scheme is expected to be presented to the Court for a Directions Hearing, on 8 September 2020, and for a Final Hearing in December 2020. If approved then it is expected to be implemented by the Court with an Effective Date of 31 December 2020.
- 2.5 If the Proposed Scheme is approved by the Court, then on the Effective Date, the Irish and German non-profit annuity policies of CLL will transfer to the ILA non-profit fund, along with their allocated assets and liabilities (together comprising the “Transferring Business”).
- 2.6 The size of the Transferring Business is small relative to the other business in both CLL and ILA (being around 0.4% and 0.2% of the respective insurance liabilities (net of reinsurance) for each company).

### Impact of the Proposed Scheme on Transferring Policyholders

- 2.7 I have considered the impact of the implementation of the Proposed Scheme on:
- The security of benefits of the Transferring Policies;
  - The reasonable expectations of the holders of those policies (“Transferring Policyholders”), including benefit expectations, service standards, management and governance; and

- Any change to the profile of risks to which the Transferring Policies will be exposed as a result of the implementation of the Proposed Scheme.

2.8 I have also considered the impact of the implementation of the Proposed Scheme on the Transferring Policyholders' eligibility for compensation under the Financial Services Compensation Scheme ("FSCS") and their rights to refer complaints to the Financial Ombudsman Scheme ("FOS").

### ***Security of benefits of the Transferring Policies***

2.9 Following the transfer, the long-term insurance policies will transfer into and become the responsibility of ILA, and ILA will be responsible for meeting the benefits payable under those policies. It is therefore relevant to consider:

- The financial strength required under Solvency II for CLL and ILA;
- The capital policies and risk appetite statements of CLL and ILA, including their relative strengths, the proposed responses to a breach, and the governance surrounding them;
- The change in risk profile to which the Transferring Policies are exposed as a result of the transfer;
- The financial resources available in CLL and ILA to provide security for the guaranteed benefits of the Transferring Policies, and the quality of those resources; and
- The protection available to the Transferring Policyholders in the event that either firm becomes insolvent.

2.10 I have considered each of these areas in the main body of this report, and in summary:

- CLL calculates its Solvency Capital Requirement ("SCR") under Solvency II using a Partial Internal Model ("PIM"), whereas ILA uses the Solvency II Standard Formula.
- The capital policies of CLL and ILA express minimum levels and target operating ranges of capital as a percentage of SCR. These policies have very similar target ranges of SCR coverage which the firms aim to manage to and hence similar levels at which management actions would be triggered if coverage fell below such levels.
- Both firms have an adequate range of management actions at their disposal to mitigate scenarios in which their solvency position starts to deteriorate.
- The change in risk profile to which the Transferring Policies will be exposed as a result of the implementation of the Proposed Scheme will not have a material adverse effect on the security of benefits for the Transferring Policies.
- Table 2.1 shows the relevant figures as at 31 December 2019 for the financial resources available in CLL and in ILA. The figures for CLL are shown on a pro-forma basis, after allowing for the previous Part VII transfer of MGM Advantage Life Limited ("MGMA") into CLL on 1 January 2020. The figures for ILA are shown both as at 31 December 2019 before the Proposed Scheme takes effect (using the GBP:EUR exchange rate effective as

at that date) and then on a pro-forma basis as at the same date, assuming that the Proposed Scheme had been effective at that date. Although ILA is expected to have a lower absolute amount of excess resources over its SCR following the implementation of the Proposed Scheme than CLL has before its implementation, when viewed as a margin over the SCR, the solvency ratio of ILA is 12% higher than CLL and is comfortably in excess of its target range.

**Table 2.1: CLL and ILA solvency pre and post Scheme as at 31 December 2019**

Solvency II Pillar 1 31 December 2019	CLL (pro-forma, including MGMA) pre-Scheme (£m)	ILA pre-Scheme (converted to £m)	ILA pro-forma post-Scheme (converted to £m)
Own Funds	4,240	1,637	1,641
SCR	2,710	969	974
<b>Excess resources over SCR</b>	<b>1,530</b>	<b>668</b>	<b>667</b>
<b>Solvency coverage ratio</b>	<b>156%</b>	<b>169%</b>	<b>168%</b>

- The ILA pro-forma post-Scheme figures in the table above assume a £79 million payment from CLL to ILA upon the transfer of the liabilities (which amount to £68 million in total Technical Provisions in CLL as at 31 December 2019), which has yet to be agreed between the parties. I will provide an update on this in my Supplementary Report, however, if the payment (in excess of assets backing insurance liabilities required by ILA) was higher or lower by £10 million, this would result in only a small change to the solvency coverage ratio of ILA of around +/- 1%.
- ILA contains two ring-fenced with-profit funds which, in extreme circumstances, may require capital support from the ILA non-profit fund on an informal basis. The with-profit funds are well capitalised with a high surplus above guaranteed benefits and capital requirements. I therefore consider that the risk of capital support being required is a remote possibility and one that would not materially adversely affect the security of the Transferring Policyholders.
- I have taken into account the loss of the FSCS protection from which the Transferring Policyholders currently benefit. The FSCS provides protection to relevant policyholders in the event of insolvency or default of UK based insurers (whether in respect of their UK or EEA business). After the implementation of the Proposed Scheme, the Transferring Policyholders will hold policies with an Irish based insurance company and therefore those that are currently entitled to FSCS protection will lose this entitlement. There is currently no equivalent to the FSCS in Ireland for long-term insurance business. However, the overriding purpose of the Proposed Scheme is to effect the transfer of the Transferring Business from CLL to ILA, in order to enable the continued and lawful servicing (notably, paying regular annuity payments to Transferring Policyholders) of the Transferring Business, regardless of the impacts arising from Brexit. In my opinion, having certainty that the Transferring Policies can continue to be serviced lawfully after Brexit is fundamentally important, and will be of considerable importance to the Transferring Policyholders. The loss of any FSCS protection is a consequence of achieving this certainty. In addition, I have considered that the FSCS only provides protection to covered policyholders following an insolvency or default event of an insurer. Given that ILA will be well capitalised and will

continue to be required to comply with the Solvency II Directive in EU law, the likelihood of default or insolvency of ILA is, in my opinion, sufficiently remote. I have also considered that ILA believe it disproportionate to either maintain or establish a UK branch in order to service the Transferring Policyholders, particularly as ILA will not have any ongoing business with UK policyholders and the regulatory landscape will be much more onerous for a “third country” entity once the UK has exited the European Union. In conclusion, I am satisfied that the loss of the perceived benefit of the FSCS protection as a result of the Proposed Transfer is sufficiently low, so that the Transferring Policyholders are not being materially adversely affected by the loss of the FSCS protection.

- 2.11 Taking all of the above into account, I am satisfied that the implementation of the Proposed Scheme will not have a material adverse impact on the security of benefits of the Transferring Policies.

### *Reasonable expectations of Transferring Policyholders*

- 2.12 The Transferring Policies are all guaranteed non-participating immediate annuities (as defined/described in the Glossary in Appendix D). The reasonable expectations of the holders of such policies are:

- That they receive their benefits as guaranteed under the policy, on the dates specified, from the point of purchase and throughout the life of the policy;
- That the administration, management, and governance of the policies are all in line with legal requirements and with the contractual terms under the policies; and
- That the standards of service received following the transfer are at least as good as those they currently receive.

- 2.13 There are no areas of discretion involved in determining the benefits payable on the Transferring Policies. Therefore, policyholders’ reasonable expectations in respect of their benefits are that they receive the amounts guaranteed under the policy as and when due. As there are no changes in the Transferring Policies’ terms and conditions, and as I have concluded that the transfer will not have a material adverse impact on the security of benefits of the Transferring Policies, the transfer should have no impact on policyholders’ reasonable expectations in respect of their benefits. A significant consideration, in the light of the legal restrictions that would be imposed upon CLL following Brexit if the Proposed Scheme does not go ahead, is that the ongoing annuity payments due under the terms of the Transferring Policies would not legally be payable, which in my opinion would be a materially adverse position for the Transferring Policyholders.

- 2.14 Both ILA and CLL have a similar governance structure in which the Board of Directors of each entity is responsible for the governance and oversight of all operations and risks. Both firms are currently required to comply with the Solvency II rules on systems of governance and have a similar Enterprise Risk Management Framework in place involving the three lines of defence. ILA already has close to €4 billion of annuities (gross of reinsurance) in force and has the necessary expertise in managing these.

- 2.15 CLL currently has two services agreements in place with other group companies in relation to the Transferring Business, which will be transferred unchanged to ILA from CLL on the

Effective Date of the Proposed Scheme. I have been informed by the management of CLL and ILA that there are no current plans to make any changes to these services agreements.

- 2.16 I am therefore satisfied that the implementation of the Proposed Scheme will not materially affect the standards of governance or administration standards applicable to the Transferring Business.

### **Impact of the Proposed Transfer on non-transferring Policyholders of CLL**

- 2.17 The Proposed Scheme comprises all of the remaining long-term insurance business of CLL that was originally written by ELAS in its Irish and German branches and which was transferred into CLL from ELAS under the previous Part VII transfer referenced in paragraph 2.2 above. All other CLL policies and contracts will remain in CLL, including non-profit life, critical illness and permanent health protection policies (on both an individual and a group basis), pension policies, including drawdown and annuities (on both an individual and a group basis), and unit-linked investment bonds. CLL will continue to issue and manage these contracts after the Effective Date of the Proposed Scheme.
- 2.18 I have considered the impact of the implementation of the Proposed Scheme on:
- The financial resources available to provide security for the non-transferring policyholders after implementation of the Proposed Scheme, compared to those currently available.
  - Any change to the profile of risks to which the non-transferring policyholders are exposed as a result of the transfer.
  - The effect of the implementation of the Proposed Scheme on the reasonable expectations of the non-transferring policyholders, including benefit expectations, service standards, management and governance.

### **Security of benefits of the non-transferring CLL policies**

- 2.19 The Transferring Business reflects an immaterial part of the total liabilities in CLL. The Transferring Business represents 0.4% of CLL's insurance liabilities (net of reinsurance) as at 31 December 2019.
- 2.20 Table 2.2 below shows the financial strength of CLL both before the Proposed Scheme and after the Proposed Scheme, on the Solvency II Pillar 1 basis, as at 31 December 2019. These figures all make allowance on a pro-forma basis for the previous Part VII transfer of MGMA into CLL which became effective on 1 January 2020:



**Table 2.2: CLL solvency pre and post Scheme as at 31 December 2019**

Solvency II Pillar 1 31 December 2019	CLL (pro-forma, including MGMA) pre- Scheme (£m)	CLL post-Scheme (£m)
Own Funds	4,240	4,230
SCR	2,710	2,699
<b>Excess resources over SCR</b>	<b>1,530</b>	<b>1,531</b>
<b>Solvency coverage ratio</b>	<b>156%</b>	<b>157%</b>

- 2.21 The figures in the table above show that there is expected to be an immaterial impact on the solvency ratio of CLL following the implementation of the Proposed Scheme, with the solvency ratio increasing by 1% to 157%. I note that the CLL post-Scheme figures in the table above assume a payment of £79 million from CLL to ILA upon the transfer of the liabilities, which has yet to be agreed between the parties. I will provide an update on the financial information in my Supplementary Report, however, if the payment (in excess of assets backing insurance liabilities required by ILA) was higher or lower by £10 million, this would result in an immaterial change to the solvency coverage ratio of less than +/- 1%.
- 2.22 Since 31 December 2019 there have been significant changes in the economic and insurance environment as a result of COVID-19. I comment on the preliminary indications of the likely high-level effects of this global pandemic on the financial position of both firms in Section 10 of this report, although it is still too early to have fully worked through all the financial impacts in this fast-changing situation. Consequently, I expect to provide more detailed information on how COVID-19 has affected the financial position of both firms in my Supplementary Report.
- 2.23 Given the small size of the Transferring Business relative to the overall size of the business of CLL, the Proposed Scheme will have an immaterial impact on the risk exposure of the remaining policyholders in CLL.

### *The reasonable expectations of the non-transferring policyholders in CLL*

- 2.24 The non-transferring policyholders in CLL all hold non-profit policies and their expectations will principally relate to the continued fulfilment of the unchanged contractual terms of their policies, the management and governance of their policies, and the servicing of their policy. Following implementation of the Proposed Scheme, I understand from the management of CLL that there will be no change to any of these items.
- 2.25 I can therefore confirm that I am satisfied that the reasonable expectations of the remaining CLL policyholders will continue to be met to the same levels following implementation of the Proposed Scheme.

### **Impact of the Proposed Transfer on existing policyholders of ILA**

- 2.26 The existing ILA policies can be broken down into policies in the following funds:
- ILA non-profit fund
  - ILA ring fenced with-profit fund 1



- ILA ring fenced with-profit fund 2

2.27 The key points I have considered in respect of the above groups of policyholders are:

- The financial resources available to provide security for the existing ILA policyholders after implementation of the Proposed Scheme, compared to those currently available.
- Any change to the profile of risks to which the existing ILA policyholders are exposed as a result of the transfer.
- The effect of the implementation of the Proposed Scheme on the reasonable expectations of the existing ILA policyholders, including benefit expectations, service standards, management and governance.

### ***Security of benefits of the existing policyholders***

- 2.28 ILA's capital management policy will not change as a result of the Proposed Scheme, and so the security of existing policyholder benefits will only be affected by changes in the ability of ILA to comply with this policy.
- 2.29 Table 2.1 above shows that if the Proposed Scheme had been effective as at 31 December 2019, there would have been a 1% reduction in coverage of the SCR, to 168% within ILA. This represents an immaterial impact on the security of existing ILA policyholders, and, based on the figures in the table, ILA would remain comfortably above its target range of solvency cover.
- 2.30 Under the Proposed Scheme, no assets or liabilities will be transferred into or out of the two ILA with-profit funds. Therefore, the only potential change in the exposure of these funds, as a result of the Proposed Scheme, is due to changes in the financial strength of the ILA non-profit fund, potentially limiting the availability of capital support to the with-profit funds. The solvency coverage ratio of the ILA non-profit fund would slightly reduce as a result of the Proposed Scheme, in a similar way as to ILA overall, as shown in Table 2.1. There will therefore be very limited impact of the Proposed Scheme on the ability of the ILA non-profit fund to be able to support the ILA with-profit funds if required.
- 2.31 Given the small size of the Transferring Business relative to the overall size of the business of ILA, it will have a very limited impact on the risk exposure of the existing non-profit policyholders and with-profit policyholders in ILA.
- 2.32 Taking all of this into account, I am satisfied that the transfer will not have a material adverse impact on the security of benefits of existing ILA policyholders.

### ***Reasonable expectations of the existing ILA policyholders***

- 2.33 As discussed in section 4, ILA's long-term insurance business comprises:
- Protection products (including life cover, income protection and critical illness) for groups and individuals;
  - Retirement income planning products (including retirement saving, annuities, pension bonds and drawdown);

- Other savings and investments products, investment bonds, sovereign annuities and inheritance tax planning products; and
- Two conventional with-profit funds, consisting mainly of endowment business, whole of life business and a small block of deferred annuity business, and one unit-linked with-profit fund. All three of these with-profit funds are closed to new business.

2.34 Policyholders' reasonable expectations in respect of their benefits under such products are:

- For protection products, that the policyholders receive their benefits as guaranteed under the policy;
- For annuity policyholders, that they receive their income as guaranteed under the policy, on the dates specified;
- For unit-linked business, that the policyholders receive their contractual benefits as set out under the policy, and the policies are operated in accordance with their contractual terms, including the level of charges; and
- For with-profit policyholders, that they receive their guaranteed benefits as set out under their policy, in addition to reasonable expectations of future regular and terminal bonuses, as well as their share of the surplus in the relevant with-profit fund.

2.35 There will be no changes to the contractual terms of existing ILA policies under the terms of the Proposed Scheme and there are not expected to be any changes to the benefits which any existing ILA policyholder can expect to receive as a result of the Proposed Scheme. Furthermore:

- There will be no change to how ILA is governed and managed or to its business plans;
- There will be no changes to the administration or investment services in relation to the existing policies (both non-profit and with-profit policyholders); and
- There will be no changes to the types or amounts of charges levied to the unit-linked funds.

2.36 I am satisfied that the implementation of the Proposed Scheme will not have a material effect on the reasonable expectations of the existing ILA policyholders.

### Other considerations arising from the Proposed Scheme

2.37 In section 10 of this report I have also taken into account various other considerations, including:

- The approach to communication with policyholders (also summarised in paragraphs 2.38 and 2.39);
- The costs of the Proposed Scheme;
- Tax;

- Other creditors;
- The loss of protection for Transferring Policyholders under the Financial Services Compensation Scheme following the implementation of the Proposed Scheme;
- The Financial Ombudsman Service (in the UK) and the Financial Services and Pensions Ombudsman (in Ireland);
- The effect of the Proposed Scheme on previous schemes; and
- The future operation of the Proposed Scheme.

## The approach to communication with policyholders

- 2.38 Regulations require that a legal notice in a form approved by the PRA is published in the London, Edinburgh and Belfast Gazettes, as well as two national newspapers in the relevant EEA states in which Transferring Policyholders are resident. CLL and ILA have opted to publish legal notices in *Suddeutsche Zeitung*, *Frankfurter Allgemeine Zeitung*, *The Irish Times* and *The Irish Independent* plus *The Daily Mail* and *the Times* and will make information available on the CLL website. On materiality grounds, the court will be asked to waive the requirement to publish legal notices in Austria, France or Spain given those countries were the state of commitment for only four policyholders in total.
- 2.39 It is proposed that each Transferring Policyholder will receive a policyholder pack that comprises a covering Policyholder Letter and a Policyholder Guide, which will include amongst other things:
- A summary of the terms of the Proposed Scheme;
  - A summary of the report by the Independent Expert; and
  - A questions and answers section.
- 2.40 It is proposed that CLL and ILA will seek waivers from sending communications to, respectively, the non-transferring CLL policyholders and the existing ILA policyholders regarding the Proposed Scheme. In my opinion it is reasonable for the firms to seek these waivers and that the relevant policyholders will not be materially adversely affected by not receiving such communications.

## Overall conclusions

- 2.41 Due to the legal situation following the UK's exit from the European Union, it will become a legal necessity for CLL to transfer the Transferring Business to another insurance entity domiciled within a remaining EEA member state in order to ensure that the Transferring Policies can still legally be serviced, in particular to continue making annuity payments to the Transferring Policyholders. The Proposed Scheme has been prepared in order to meet this legal necessity.
- 2.42 I am satisfied that the implementation of the Proposed Scheme will not have a material adverse effect on:

- The security of benefits of the policyholders of CLL and ILA, including the Transferring Policyholders;
- The reasonable benefit expectations of the policyholders of CLL and ILA, including the Transferring Policyholders; or
- The service standards and governance applicable to the CLL and ILA policies, including the Transferring Policyholders.

## Section 3: General considerations of the Independent Expert

### The role of the Independent Expert

- 3.1 As described in Section 1 of this report, the Proposed Scheme concerns two life insurance companies: CLL and ILA. As Independent Expert, I need to consider the terms of the Proposed Scheme generally and how the different groups of policyholders of CLL and ILA are likely to be affected by the implementation of the Proposed Scheme. In particular I need to consider:
- The effect of the implementation of the Proposed Scheme on the security of the policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;
  - The effect of the implementation of the Proposed Scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect:
    - the security of policyholders' contractual rights;
    - levels of service provided to policyholders; or
    - the reasonable expectations of policyholders; and
  - The cost and tax effects of the Proposed Scheme, in so far as they may affect the security of policyholders' contractual rights or their reasonable expectations.
- 3.2 I am only required to comment on the effects of the implementation of the Proposed Scheme on policyholders who enter into contracts with CLL and ILA before the Effective Date of the Proposed Scheme.
- 3.3 In this report I have not restricted my assessment of the Proposed Scheme to consideration of potential adverse effects.
- 3.4 The type of policy held by a policyholder will be a key determinant of the risks to which the policyholder is exposed. Other than this, the key determinants of the policyholder's risk exposure will be the characteristics of the company in which the policy is held, for example:
- The size of the company;
  - The amount and quality of capital resources available, other calls on those capital resources and capital support currently available to the company;
  - The internal capital policy of the company;
  - The investment strategy of the company;
  - The mix of business of the company;

- The company's strategy, e.g. whether the company is open or closed to new business, its acquisitions strategy; and
  - Other factors, such as operational risks faced by the company, reinsurance arrangements of the company, the company's governance framework and its tax position.
- 3.5 Some of these risks are company-specific, for example risks arising from the particular mix of business written or from the company's strategy, and some are common to various different groups of policyholders across the companies subject to the Proposed Scheme.

### Security of policyholder benefits

- 3.6 As part of my role as Independent Expert for the Proposed Scheme, I need to consider the security of policyholder benefits, that is, the effect of the implementation of the Proposed Scheme on the likelihood that policyholders will receive their benefits when these are due.
- 3.7 In considering and commenting upon policyholder security, I shall primarily consider policyholders' guaranteed benefits. The regulations pertaining to insurance companies domiciled both within the UK and within other EU member states (including, in particular, Ireland) require such companies to hold a minimum amount of capital in addition to the assets backing a realistic estimate of their liabilities to policyholders. Insurance companies must also demonstrate that they can fulfil their regulatory requirements and meet policyholder claims as they become due in adverse scenarios.
- 3.8 Therefore, the amount by which the assets available to support the long-term insurance business exceed the long-term liabilities provides security for the guaranteed benefits.

### Treating customers fairly / Policyholders' reasonable expectations

- 3.9 I also need to consider the proposals in the context of the regulatory obligation on both companies to treat their customers in line with local regulatory requirements and, in particular, the effect of the implementation of the Proposed Scheme on policyholders' reasonable expectations.
- 3.10 This involves considering the effect of the implementation of the Proposed Scheme on any areas where discretion is involved on behalf of the relevant insurance company, for example in determining the charges applied to a policy and the benefits granted to the policyholder, as well as consideration of the effect of the implementation of the Proposed Scheme on the management, service and governance standards of the company in question.

### The conclusions of the Independent Expert

- 3.11 As Independent Expert, my assessment of the impact of the Proposed Scheme on the various affected policies is ultimately a matter of actuarial judgement regarding the likelihood and impact of future possible events. Given the inherent uncertainty of the outcome of such future events and that the effects may differ across different groups of policies, it is not possible to be certain in respect of their effect on the policies.
- 3.12 In order to acknowledge this inherent uncertainty, the conclusions of the Independent Expert in respect of Part VII transfers of long-term insurance business are usually framed using a

materiality threshold. If the outcome under consideration is very unlikely to happen and does not have a large impact, or is likely to happen but has a small impact, then it is not considered to have a material effect on the policies.

- 3.13 The setting of my conclusions in this framework is a consequence of the Court's consideration of prior schemes. In particular, principles stated by Mr Justice Evans-Lombe in relation to a transfer involving AXA Equity & Law Life Assurance Society plc and Axa Sun Life plc in 2001 (based on principles outlined by Mr Justice Hoffman in 1989) are often used as the basis for the consideration of insurance business transfers by the Independent Expert and by the Court.
- 3.14 In particular, Mr Justice Evans-Lombe stated that "the court is concerned whether a policyholder, employee or other interested person or any group of them will be adversely affected by the scheme". He additionally stated: "That individual policyholders or groups of policyholders may be adversely affected does not mean that the scheme has to be rejected by the court. The fundamental question is whether the scheme as a whole is fair as between the interests of the different classes of persons affected". The most common interpretation of these (and other relevant) statements has been that a conclusion that "no group of policyholders is materially adversely affected by the Scheme" provides a sufficient condition to conclude that the fairness of the Proposed Scheme as a whole has been demonstrated.
- 3.15 This is therefore the framework within which I undertake my consideration of the Proposed Scheme.

## The Supplementary Report

- 3.16 This Scheme Report is based on:
- Audited financial information in respect of CLL and ILA as at 31 December 2019;
  - Financial projections performed by CLL to the end of 2024, using the management accounts as at 31 December 2019 as the start point; and
  - Financial projections performed by ILA to the end of 2023, using the management accounts as at 31 December 2018 as the start point and reflecting some experience in early 2019.
- 3.17 I expect to produce a further report (the "Supplementary Report") prior to the Final Hearing, to provide an update for the Court on my conclusions in the light of any significant events subsequent to the date of the finalisation of this report.
- 3.18 The Supplementary Report will be based on the unaudited financial position of CLL and ILA as at 30 June 2020 and updated financial projections, which will take into account any significant changes, in particular in relation to the current COVID-19 situation and Brexit.
- 3.19 The Supplementary Report will be made available on the CLL website and sent by post to any person who has requested a hard copy of this report from CLL or ILA.

## Reliance on legal advice

- 3.20 There are some aspects of the Scheme that are legal matters which fall outside my expertise. For these areas, I have considered whether it is appropriate to take independent legal advice and I have decided that it is appropriate for me to rely on the advice provided to CLL by Herbert Smith Freehills.
- 3.21 My reasons for this are:
- The relevant legal matters do not appear to be contentious; and
  - The fair treatment of policyholders is not dependent on the legal advice.
- 3.22 I am therefore satisfied that it is appropriate for me to rely on the conclusions of Herbert Smith Freehills in forming my view on the Proposed Scheme.



## Section 4: The UK and Irish Life Insurance market and regulatory environment

### The current regulatory regime for UK and Irish insurance companies

- 4.1 CLL is an insurance company domiciled in the UK, while ILA is an insurance company domiciled in Ireland. The regulatory regime to which both UK and Irish insurers are subject, and the applicable solvency requirements, are relevant to my considerations as Independent Expert and are summarised in this section.

#### UK

- 4.2 Prior to 1 April 2013, regulation of UK insurance companies was the responsibility of the Financial Services Authority. Since 1 April 2013, responsibility for the regulation of such companies has been split between the PRA and the FCA.
- 4.3 The PRA is a part of the Bank of England and carries out the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.
- 4.4 The PRA has statutory objectives to promote the safety and soundness of the insurers that it regulates, and to contribute to ensuring that policyholders are appropriately protected. More generally, these statutory objectives can be advanced by seeking to ensure that regulated insurers have resilience against failure and that disruption to the stability of the UK financial system from regulated insurers is minimised.
- 4.5 The FCA regulates the conduct of all financial services firms in relation to consumer protection, industry stability and the promotion of healthy competition between providers.

#### Ireland

- 4.6 In Ireland, the CBI is responsible for both the prudential regulation and supervision of insurance companies (and other financial services firms) and for the conduct of such firms in relation to consumer protection, industry stability and the promotion of healthy competition between providers. The CBI has also published a Consumer Protection Code which covers services provided by regulated entities to persons within (but not outside of) Ireland. This therefore means that if the Proposed Scheme takes effect, the consumer protection standards that would continue to apply to Transferring Policyholders who were residing in Germany from inception of their policies, or who have German law governing their policies (in the case of the Austrian, French and Spanish policies), are the local German regulations as overseen by BaFin, the Federal Financial Supervisory Authority in Germany.
- 4.7 In general, all aspects of German insurance law will continue to apply to the policyholders who were resident in Germany at inception. The four policies where the policyholder was based in either Austria, France or Spain at inception will have been written through either the Irish or German branches of ELAS and hence either Irish or German law applies to these policies.
- 4.8 The CBI supervises all regulated entities (including life assurance undertakings) by using a risk-based approach. This classifies financial entities into four groups based on their impact -

High, Medium-High, Medium-Low and Low - and dedicates resources to those entities with the largest impact on consumers and financial stability. The CBI classifies ILA as a High Impact entity, and therefore applies a high degree of monitoring and oversight on the business.

## The Solvency II regulatory regime

### Introduction

- 4.9 The current regulatory solvency framework for the European Economic Area (“EEA”) insurance and reinsurance industry came into effect on 1 January 2016. This regime is known as Solvency II, and it imposes solvency requirements that reflect the specific risks faced by each insurer and reinsurer and aims to achieve consistency across the EEA. All but the smallest EEA insurance companies are required to adhere to a set of risk-based capital requirements, and to disclose their solvency position in a public document.
- 4.10 Solvency II is based on three pillars:
- Under Pillar 1, quantitative requirements define a market-consistent framework for valuing the company’s assets and liabilities, the results of which are publicly disclosed.
  - Under Pillar 2, insurers must meet minimum standards for their corporate governance and their risk and capital management. There is a requirement for permanent internal audit and actuarial functions. Insurers must regularly undertake a forward-looking assessment of risks, solvency needs and adequacy of capital resources, called the Own Risk and Solvency Assessment (“ORSA”), and senior management must demonstrate that the ORSA actively informs business planning, management actions and risk mitigation.
  - Under Pillar 3, there are explicit requirements governing disclosures to supervisors and to the public. Firms produce private reports to supervisors and a publicly available solvency and financial condition report.

### The Pillar 1 requirements

- 4.11 The determination of a market consistent value of liabilities under Solvency II requires the insurer to calculate the best estimate liability (“BEL”). The expected future obligations of the insurer are projected over the lifetime of the contracts using the most up-to-date financial information and using best estimate actuarial assumptions, and the BEL represents the present value of these projected cash-flows.
- 4.12 Under Solvency II, a company’s Pillar 1 liabilities are called the “Technical Provisions” which consist of the sum of the BEL and the “risk margin”. The risk margin is an adjustment designed to bring the Technical Provisions up to the amount that another insurance or reinsurance undertaking would be expected to require in order to take over and meet the insurance obligations in an arm’s length transaction.
- 4.13 The Pillar 1 assets are, broadly speaking, held at market value.
- 4.14 The Solvency Capital Requirement (“SCR”) under Solvency II is the capital requirement under Pillar 1 and is intended to be the amount required to ensure that the firm’s assets continue to exceed its Technical Provisions over a one year time frame with a probability of 99.5%.

- 4.15 The Minimum Capital Requirement (“MCR”), which is lower than the SCR, defines the point of intensive regulatory intervention. The MCR calculation is simpler, more formulaic and less risk-sensitive than the SCR calculation.
- 4.16 In calculating the SCR, it is expected that most firms will use the “Standard Formula”, as prescribed by the European Insurance and Occupational Pensions Authority (“EIOPA”). However, Solvency II also permits firms to use their own Internal Models (or a combination of a “Partial Internal Model” and the Standard Formula) to derive the SCR. These Internal Models and Partial Internal Models are subject to approval by the relevant regulator: in the UK this is the PRA, while in Ireland this is the CBI.
- 4.17 Under the Solvency II regulations, an Internal Model has to be calibrated such that the SCR provides a probability of at least 99.5% of remaining able to cover Technical Provisions over a one year time horizon, and the calibration of the Standard Formula stresses targets the same confidence level.
- 4.18 A firm may opt to develop a Partial Internal Model where a full Internal Model is not required. This may be a requirement of holding assets such as restructured Equity Release Mortgages, or if the firm’s profile of a particular risk is significantly different from the calibration of the Standard Formula. Such firms may still use the Standard Formula for those risks not covered by the Internal Model.
- 4.19 Under the Solvency II regime, the excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds, which can be thought of as the capital available in the company to cover the solvency capital requirements.
- 4.20 Under Solvency II, companies are required to classify their Own Funds into three tiers, which broadly represent the quality of the Own Funds in relation to their ability to absorb losses. The Own Funds of the highest quality are classified as Tier 1. In order to be classified as Tier 1, Own Funds must exhibit both of the following:
- Permanent availability, i.e. the item is available, or can be called up on demand, to fully absorb losses on a going concern basis, as well as in the case of winding up; and
  - Subordination, i.e. in the case of winding up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations towards policyholders and beneficiaries of insurance and reinsurance contracts, have been met.
- 4.21 Own Funds that are classified as Tier 2 or Tier 3 are of a lower quality, with less ability to fully absorb losses.
- 4.22 Any firms intending to use an Internal Model, or any of the adjustments to the Technical Provisions discussed in paragraphs 4.23 to 4.32, must formally apply to their relevant regulator (i.e. the PRA for UK firms, the CBI for Irish firms) for approval.

### *The Matching Adjustment*

- 4.23 In calculating the BEL for certain types of business, the Solvency II rules permit firms to apply to their regulator to make use of the “matching adjustment” (“MA”). The MA is an increase to

the discount rate used in the calculation of the BEL that allows firms to take credit for the additional investment return in excess of the risk-free rate that they expect to earn from a “hold to maturity” investment strategy for their less liquid assets, which are used to back their most stable and predictable liabilities, typically non-profit in-payment annuity liabilities.

- 4.24 Firms using the MA are subject to various restrictions around the types of asset that are permitted to back the relevant liabilities, the circumstances in which the assets may be traded, and the extent to which mismatching of asset and liability cash flows is permitted.

### *The Volatility Adjustment*

- 4.25 For liabilities that are not subject to the MA, the Solvency II rules permit firms to apply to their regulator to make use of the “volatility adjustment” (“VA”). The VA is an increase to the discount rate used in the calculation of the BEL (other than for liabilities that are subject to the MA) which aims to prevent forced sales of assets in the event of extreme bond spread movements.
- 4.26 The VA is based on the spreads on a representative portfolio of assets for each relevant currency, and risk-free discount curves which include the VA are published regularly by EIOPA.

### *The Transitional Measures*

- 4.27 Insurers are also permitted to apply to their regulator to make use of transitional measures. Transitional measures allow firms to phase in the balance sheet impact of moving from the previous Solvency I regulatory regime to the Solvency II regulatory regime. The transitional measures can be applied in one of two ways:
- The Transitional Measure on Technical Provisions (“TMTP”) allows firms to phase in the increase in Technical Provisions that resulted from the change in regulations from Solvency I to Solvency II (only in relation to business written prior to 1 January 2016) over a sixteen-year period. In the UK, the increase in Technical Provisions is measured relative to the firm’s Solvency I Pillar II liabilities. I am not aware of firms making widespread use of this transitional measure in Ireland.
  - The Transitional Measure on the Risk-Free Interest Rate allows firms to phase in any reduction in the discount rate used to calculate their liabilities under Solvency II relative to the previous solvency regime over a sixteen-year period.
- 4.28 The TMTP is widely used by UK insurers, including CLL, but infrequently by Irish insurers (and is not used by ILA). The Transitional Measure on the Risk-Free Interest Rate is not widely used by either UK or Irish insurers, and in particular is not used by either party subject to the Scheme.
- 4.29 For a given firm, the TMTP is calculated as at the implementation date of Solvency II, i.e. 1 January 2016. The TMTP is calculated as the excess, if positive, of the firm’s Technical Provisions under Solvency II over the firm’s insurance liabilities under the previous Solvency I regime.

- 4.30 A further test is then carried out to determine whether deducting the calculated TMTP from the firm's Solvency II Technical Provisions at 31 December 2015 would result in a Financial Resources Requirement ("FRR") under Solvency II that is lower than the firm's FRR under the previous Solvency I regime at the same valuation date. The FRR for a given solvency regime is calculated as the firm's total liabilities plus the firm's capital requirement under that regime. If the Solvency II FRR after deduction of the TMTP is lower than the FRR under Solvency I, the calculated TMTP must be reduced to a level that ensures that this is no longer the case.
- 4.31 The final calculated TMTP is deducted from the firm's Technical Provisions in its Solvency II balance sheet at 1 January 2016. For valuation dates after 1 January 2016, the TMTP that was calculated at 1 January 2016 is reduced linearly to zero over a sixteen-year period.
- 4.32 A firm's TMTP is expected to be subject to recalculation every two years, subject to approval from the relevant regulator (e.g. the PRA in the UK). Regulatory guidance in the UK states that firms will be able to apply to the regulator to recalculate their TMTP if they believe that their risk profile has changed materially since the previous recalculation, due to events such as business transfers, changing use of the MA or VA, or material changes in market conditions.

### Ring-Fenced Funds

- 4.33 The Solvency II regulatory regime includes the concept of a ring-fenced fund. This refers to any arrangement where an identified set of assets and liabilities are managed as though they were a separate undertaking, meaning that there are restrictions on the extent to which surplus in the ring-fenced fund may be transferred to shareholders or used to cover losses outside the ring-fenced fund. In the UK and Ireland, firms have generally set up ring-fenced funds in order to reflect the arrangements applicable to their with-profit funds (as defined under the previous regulatory regime) and the with-profit and non-profit business within the with-profit fund.
- 4.34 In the UK, specific rules and guidance covering with-profit funds were put in place in 2005 and can be found in chapter 20 of the FCA's Conduct of Business Sourcebook (COBS). This covers areas such as treating with-profit policyholders fairly, principles and practices of financial management, communication and governance.
- 4.35 In Ireland, the CBI's "Domestic Actuarial Regime and Related Governance Requirements Under Solvency II" sets out specific requirements for the management of with-profits funds, including the requirement to establish and maintain a publicly available "With-Profits Operating Principles" document, setting out the management of the funds, for which the Board is responsible.

### Governance of UK and Irish long-term insurers

- 4.36 For most long-term insurers in the UK and Ireland the Board of Directors is the firm's governing body and is ultimately responsible for setting the strategic direction of the firm, overseeing the activities of the firm's day-to-day management and approving the firm's financial statements.
- 4.37 Under Solvency II, all UK and Irish insurers are required to comply with the Solvency II system of governance requirements, covering areas such as risk management, internal control, fit and proper requirements and the actuarial function. The actuarial function is responsible for, amongst other things, coordinating the calculation of the Technical Provisions and providing an opinion on the firm's underwriting policy and the adequacy of the firm's reinsurance

arrangements. The person having responsibility for the actuarial function under Solvency II is known as the Chief Actuary in the UK and the Head of Actuarial Function in Ireland.

## UK

4.38 Since 10 December 2018, UK insurers have been subject to the Senior Managers and Certification Regime ("SM&CR"), operated jointly by the PRA and the FCA. This replaced the separate Senior Insurance Managers Regime, and has brought insurers under the same governance regime as other UK financial institutions. The SM&CR defines a set of senior management functions ("SMF"), which includes:

- Chief Executive Officer;
- Chief Financial Officer;
- Chief Risk Officer;
- Chief Actuary;
- With-Profits Actuary, relevant to firms with With-Profits insurance business;
- Head of Internal Audit; and
- Head of Key Business Area.

4.39 The individuals responsible for these functions are subject to PRA approval.

## Ireland

4.40 In Ireland, the CBI's Fitness and Probity Standards (Code issued under Section 50 of the Central Bank Reform Act 2010) outlines Pre-Approval Controlled Function ("PCF") positions in regulated entities other than Credit Unions, where appointment is subject to the CBI's approval, and includes details of their obligations in relation to the code. The PCFs relevant to a life assurance undertaking include:

- PCF1 Executive Director
- PCF 2 Non-Executive Director
- PCF 3 Chairman of the board
- PCF 4 Chairman of the audit committee
- PCF 5 Chairman of the risk committee
- PCF 8 Chief Executive
- PCF 11 Head of Finance
- PCF 12 Head of Compliance

- PCF 13 Head of Internal Audit
  - PCF 14 Chief Risk Officer
  - PCF 18 Head of Underwriting
  - PCF 19 Head of Investment
  - PCF 42 Chief Operating Officer
  - PCF 43 Head of Claims
  - PCF 48 Head of Actuarial Function
- 4.41 With effect from 1 December 2012 the Standards also apply to all staff in less senior Controlled Function roles.
- 4.42 As well as complying with all the requirements for the Actuarial Function under Solvency II, life insurers are required to comply with any additional requirements as specified by the CBI's "Domestic Actuarial Regime and Related Governance Requirements Under Solvency II", which include:
- the appointment of a Head of Actuarial Function;
  - responsibility for the actuarial function to be held by one person and in the case of a High Impact undertaking, this person must be an employee of the undertaking;
  - the provision of the actuarial opinion to the CBI on an annual basis;
  - the preparation and submission of an actuarial opinion to Board in respect of each ORSA;
  - the preparation and submission of an actuarial opinion on technical provisions;
  - the preparation and submission of an actuarial report on technical provisions;
  - the establishment of Reserving policy;
  - all High, Medium High and Medium Low impact undertakings (including ILA) are required to engage a reviewing actuary to conduct peer review of the TPs of the undertaking and related actuarial opinions.

### A firm's risk appetite and internal capital policy

- 4.43 The Board of a firm is responsible for the management of the company and its exposure to risk. The Board will typically set out its appetite for risk in a form which references the probability (that the Board is willing to accept) of not being able to pay policyholder liabilities as they fall due and/or meet regulatory requirements.
- 4.44 In order to ensure that day-to-day fluctuations in markets and other experience do not lead to a breach of their risk appetite and regulatory capital requirements, insurers usually aim to hold



more capital than strictly required to meet the regulatory minimum. The details of the target level of capital buffer are typically set out in the firm's capital management policy.

- 4.45 The capital management policy of a firm is set by and owned by the Board and describes the capital that the Board has determined should be held in the company. Changes to this policy usually require Board approval and appropriate consultation with the relevant regulator (e.g. the PRA in the UK and the CBI in Ireland).
- 4.46 The capital management policy is typically stated in terms of the capital requirements set down by the relevant regulations. The regulatory capital requirements typically target a particular probability of remaining solvent over a certain time horizon: for example for the Solvency II regulatory regime it is a 99.5% probability of remaining solvent over a one year time horizon. By requiring additional capital to be held on top of the regulatory requirements, the capital management policy increases the probability of remaining solvent over a particular timeframe and therefore increases the security of the benefits provided under the policies subject to that policy.
- 4.47 The level of capital required may also be driven by the desire of the Board to maintain a certain credit rating with external credit rating agencies.

## The products and long-term business relevant to this report

- 4.48 The Proposed Scheme provides for the transfer of all of the remaining long-term insurance business of CLL that was originally written by ELAS in its Irish and German branches and which was transferred into CLL from ELAS under the previous Part VII transfer referenced in paragraph 2.2 above. This consists of guaranteed non-participating immediate annuities (as defined/described in the Glossary in Appendix D).
- 4.49 ILA's existing business comprises:
- Protection products (including life cover, income protection and critical illness) for groups and individuals;
  - Retirement income planning products (including retirement saving, annuities, pension bonds and drawdown) for individuals and groups;
  - Other savings and investments products, investment bonds, sovereign annuities and inheritance tax planning products; and
  - Two conventional with-profit funds, consisting mainly of endowment business, whole of life business and a small block of deferred annuity business, and one unit-linked with-profit fund. All three of these with-profit funds are closed to new business.

## Annuities

- 4.50 Individual annuities are policies within which the policyholder receives a guaranteed regular income until their death, although the amount of that income can vary for some types of annuity. Further variations to the benefits that might be payable under this type of product, that the customer typically selects at the start of the policy, include:



- An increasing benefit, typically annually, with reference to a fixed rate or a defined index;
- Second life benefits, with the payment stream passing to a spouse or defined beneficiary upon the death of the primary policyholder; and
- Death benefits that may return a portion of the initial capital invested upon death within a guaranteed period.

## The financial information in this report

- 4.51 The PRA has granted approval for CLL to use a Partial Internal Model, the MA, the VA, and the TMTP for Solvency II reporting. However, the Transferring Business is not included within the MA fund operated by CLL.
- 4.52 The CBI has granted approval for ILA to use the VA for Solvency II reporting.
- 4.53 CLL's reported Solvency II financial information and its financial position in this report are based on a pro-forma of the company's PIM and, unless stated to the contrary, includes the effects of the previous Part VII transfer into CLL of the business of MGMA, which became effective from 1 January 2020, but which is shown in the 31 December 2019 figures on a pro-forma basis.
- 4.54 ILA's reported Solvency II financial position and its financial position in this report are based on the Solvency II Standard Formula.
- 4.55 The financial information used in the analysis of the effects of the Proposed Scheme is set out in Sections 7, 8 and 9 of this report.
- 4.56 I have not carried out a full independent review of these Solvency II results as at 31 December 2019, but:
- The CLL and MGMA Solvency II results as at 31 December 2019 have been reviewed by CLL's external auditors (Deloitte LLP);
  - The estimated pro-forma Solvency II position of CLL as at 31 December 2019 including MGMA has been prepared by CLL's actuarial function and reviewed by CLL's Chief Actuary;
  - The ILA Solvency II results as at 31 December 2019 have been reviewed by ILA's external auditors (Deloitte LLP); and
  - The estimated ILA post-Scheme pro-forma Solvency II figures as at 31 December 2019 have been prepared by ILA's actuarial function and reviewed by ILA's Head of Actuarial Function.
- 4.57 I am satisfied that it is reasonable to rely upon these Solvency II results for the purpose of this report.
- 4.58 My Supplementary Report will contain unaudited Solvency II financial information as at 30 June 2020 and will provide an update on the effect of the implementation of the Proposed Scheme based upon these figures.

## Section 5: Background on the companies concerned in the Proposed Scheme

### Canada Life Limited

#### Background

- 5.1 Canada Life Limited (“CLL”) is a member of the Great-West Life group of companies, a major international life assurance organisation that is domiciled in Canada.
- 5.2 CLL is a wholly owned subsidiary of The Canada Life Group (U.K.) Limited (“CLG”) (incorporated in England and Wales). CLG is the parent of a group of companies, whose principal activity is the transacting of ordinary long-term life assurance business. As a holding company, CLG does not write insurance or reinsurance business. CLG is itself a wholly-owned subsidiary of The Canada Life Assurance Company, a regulated Canadian insurer with interests in life insurance, health insurance, investment, retirement savings and reinsurance business, primarily in Canada, the US and Europe, and a wholly-owned subsidiary of GWL.
- 5.3 GWL and its subsidiaries, including The Canada Life Assurance Company (“CLA”), have approximately \$1.6 trillion Canadian dollars as at 31 December 2019 in consolidated assets under administration and are members of the Power Financial Corporation Group of companies.
- 5.4 Irish Life Group Limited, which was acquired by GWL in 2013, forms part of this wider group, and is held as a wholly owned subsidiary of CLL. Irish Life Assurance plc is a wholly-owned subsidiary of Irish Life Group Limited and is a regulated Irish insurer.
- 5.5 A simplified organisational structure is as follows:



- 5.6 CLL has been providing financial solutions for UK customers since 1903, to meet the retirement, investment and protection needs of both individuals and companies in the UK. CLL sells exclusively through third party advisors.

### CLL's long-term business

- 5.7 CLL is authorised by the PRA to undertake long-term insurance business in classes I, II, III, IV, VI and VII as set out in Part 4A of the Financial Services and Markets Act 2000 and is open to new business, predominantly writing individual single premium and group insurance contracts. The single premium business is dominated by pension annuities (individual and bulk) and CLL also offers other products such as drawdown and unit-linked investment bonds. The group insurance business written by CLL provides life, income protection and critical illness cover to employees covered by the schemes.
- 5.8 CLL currently writes long term insurance business only in the UK and has no plans to write business in the EEA. Historically, some business that was transferred into CLL from ELAS through a previous Part VII transfer had been written in Guernsey, Ireland and Germany.
- 5.9 A breakdown of the existing business in CLL, including details of the Transferring Policyholders, can be seen in Table 5.1 below. This table excludes the MGMA business, which was transferred to CLL in January 2020. The MGMA insurance liabilities (net of reinsurance) represent around 9% of CLL's insurance liabilities (net of reinsurance) pre-MGMA transfer. The "Insurance liabilities" are equal to the Solvency II Technical provisions as at 31 December 2019.

**Table 5.1: Breakdown of CLL business in-force as at 31 December 2019**

CLL In-force business 31 December 2019	Number of Policies*	Insurance liabilities (net of reinsurance) (£m)
Annuities in Matching Adjustment fund	152,850	7,375
Annuities not in Matching Adjustment fund:	288,092	6,811
<i>Transferring Policyholders</i>	741	68
<i>Non-Transferring Policyholders</i>	287,351	6,743
Group Health	366,420	852
Group Life	2,467,444	100
Individual Life	21,431	-3
Unit linked	25,171	2,267
<b>Total</b>	<b>3,321,408</b>	<b>17,403</b>

\*In the case of group contracts, policy counts included are number of lives not number of schemes.

- 5.10 CLL has only one fund; the Long Term Business Fund. Within this fund as at 31 December 2019, there is a ring-fenced "Matching Adjustment" fund, which is used to segregate assets backing part of the annuity liabilities, in line with regulatory requirements (as can be seen in the table above). Historically, there was also a with-profit fund (the Manulife Fund), although this was transferred to Scottish Friendly Assurance Society Limited ("Scottish Friendly") in

November 2019 through a Part VII transfer. The transfer of insurance business from MGMA which took effect on 1 January 2020 introduced a second Matching Adjustment fund, although CLL has since applied to the PRA to combine the two Matching Adjustment funds into one. The Transferring Business does not form part of either of CLL's Matching Adjustment funds.

## Recent relevant events

### *The transfer of ELAS non-profit annuities to CLL in 2016*

- 5.11 In 2016, ELAS transferred all its non-profit annuity business to CLL (including unit linked annuities), except those which were a continuation of non-profit deferred annuities reinsured by ELAS in March 2001. The policies to be transferred in this Proposed Scheme to ILA were originally transferred to CLL as part of this transaction.

### *Transfer of legacy life and pensions business to Scottish Friendly in 2019*

- 5.12 In November 2019, CLL transferred approximately 134,000 policies, including all remaining with-profit policies, to Scottish Friendly through a Part VII transfer. This block of business consisted of a mixture of Life and Pensions business.

### *Transfer of MGM Advantage Life Limited ("MGMA") to CLL in January 2020*

- 5.13 On 1 January 2020, the entire insurance business of MGMA was transferred to CLL under a Part VII transfer. This insurance business comprised a mix of pension, savings and retirement policies, including the funding and provision of equity release mortgages. The risk profile is similar to CLL's annuity portfolio though the scale of the business is smaller, with the MGMA insurance liabilities (net of reinsurance) being around 9% of CLL's insurance liabilities (net of reinsurance) pre-MGMA transfer.

### *Partial Internal Model approval*

- 5.14 CLL was granted approval from the PRA to use a PIM in respect of longevity, credit and catastrophe risks in December 2019. This means that CLL holds a level of capital which more appropriately reflects the risk profile of the business than would otherwise be the case under the Standard Formula. The main changes in the PIM compared to the Standard Formula are as follows:

- **Longevity risk:** the PIM applies stresses to both the base mortality tables and to the longevity improvement assumptions, which vary by line of business. The Standard Formula, on the other hand, applies only a single stress to the base mortality tables.
- **Credit risk:** the PIM has more granular stresses than the Standard Formula and specific calibrations for asset types that are not included in the Standard Formula, such as commercial mortgages and equity release mortgages. The PIM also makes allowance for gilt-swap spread risk which is not allowed for under the Standard Formula.
- **Catastrophe risk (life and health):** The PIM models both pandemic and terrorism risk for the life and health catastrophe stresses, calibrated to CLL's portfolio rather than a general portfolio.

### Financial condition

5.15 The published Solvency II Pillar 1 position for CLL as at 31 December 2018 and 31 December 2019 can be seen in Table 5.2 below. This table excludes the business transferred from MGMA on 1 January 2020.

**Table 5.2: Solvency II Pillar 1 position of CLL as at 31 December 2018 and 31 December 2019**

£m	31/12/2019	31/12/2018
<b>Total Assets</b>	<b>29,639</b>	<b>30,947</b>
Best estimate liabilities (gross of reinsurance)	21,700	22,857
TMTF	(1,329)	(1,521)
Risk margin	819	793
<b>Technical provisions*</b>	<b>21,190</b>	<b>22,130</b>
Other liabilities	4,897	5,035
<b>Total Liabilities</b>	<b>26,087</b>	<b>27,165</b>
<b>Excess of assets over liabilities</b>	<b>3,552</b>	<b>3,783</b>
<b>Eligible Own Funds to meet SCR**</b>	<b>4,003</b>	<b>4,146</b>
<b>Eligible Own Funds to meet MCR</b>	<b>3,680</b>	<b>3,913</b>
Solvency Capital Requirement	2,551	2,608
Minimum Capital Requirement	638	652
<b>Excess resources over SCR</b>	<b>1,452</b>	<b>1,538</b>
<b>Excess resources over MCR</b>	<b>3,042</b>	<b>3,262</b>
<b>SCR coverage ratio (%)</b>	<b>157%</b>	<b>159%</b>
<b>MCR coverage ratio (%)</b>	<b>577%</b>	<b>600%</b>

\*The technical provisions net of reinsurance at 31 December 2019 were £17,403 million and at 31 December 2018 were £18,100 million.

\*\*Includes £451 million of subordinated liabilities as at 31 December 2019 and £363 million of subordinated liabilities as at 31 December 2018.

5.16 As well as the Solvency II Pillar 1 position, CLL must also calculate a Solvency II Pillar 2 position, reflecting its own assessment of CLL's capital requirements. Although this position is not publicly disclosed, I have seen details of CLL's Solvency II Pillar 2 assessment of the balance sheet and risk capital, carried out at 31 December 2018. This shows a solvency ratio significantly higher than that of the Pillar 1 assessment. This is largely due to a higher illiquidity premium compared to that used under Solvency II Pillar 1, which uses the Matching Adjustment but only for a subset of liabilities and assets contained in the ring-fenced Matching Adjustment fund. There are strict requirements on which assets and liabilities can be in the Matching Adjustment fund, which predominantly contains annuities in payment (although none of the Transferring Business).

- 5.17 The Solvency II Pillar 1 capital requirements are derived based on stresses applied to the assets and best estimate liabilities. The solvency ratio of CLL is particularly sensitive to changes in interest rates, which includes the impact on the SCR and risk margin, as well as the assets and liabilities. This is largely due to the long duration of the annuity liabilities and risk margin. During the course of 2019, the Solvency II Pillar 1 solvency ratio for CLL experienced quite high volatility as a result of the large changes in long term interest rates. CLL has provided me with sufficient explanation of this volatility and has also provided me with its capital management plan which describes its policy, the available management actions and how the firm addresses this risk, as described further in paragraph 5.33 below.
- 5.18 I have seen a business plan produced by CLL in February 2020, which shows a stable projected Solvency II Pillar 1 solvency ratio over the five-year period from 31 December 2019, after allowing for the capital required to support new business. This includes the expected implementation of a new reinsurance arrangement during 2020, which has a relatively substantial capital benefit, and also allows for the expected growth in Own Funds of ILA (a wholly-owned subsidiary of CLL). I have made separate comments on the likely high-level effect of COVID-19 on this business plan in Section 10.
- 5.19 In addition, CLL must produce the Life Insurance Capital Adequacy Test ("LICAT") disclosures under the Canadian regime, although CLL management has confirmed to me that this is a metric which has relevance primarily to the Canadian-domiciled parent companies of CLL for capital management purposes. I have been provided with information on the UK Division's LICAT ratio at 31 December 2019 (of which CLL is the largest part), which is higher than the Solvency II Pillar 1 solvency ratio, mainly due to higher credit being taken for the illiquidity premium when valuing liabilities.
- 5.20 The subordinated liabilities of £451 million as at 31 December 2019 represent different borrowings from other companies in the Group. These are all classified as either admissible own funds under Solvency II transitional arrangements (in the case of debt issued before 2016) or admissible under Solvency II regulations. In the event of the company going into liquidation, this debt would only be repaid after all other creditors have been paid.
- 5.21 The Solvency II Own Funds of CLL as at 31 December 2019 includes the value of the £1,776 million 100% holding of the Irish Life Group. The associated SCR of the Irish Life Group as at 31 December 2019 was £514 million. The Transferring Policyholders therefore already have a relatively substantial, albeit indirect, exposure to ILA.

## Reinsurance arrangements

- 5.22 CLL currently uses reinsurance as a risk mitigation technique for underwriting, credit and market risks and such arrangements form a core part of the Company's business strategy. The counterparty risk associated with these reinsurance arrangements is small due to the high credit worthiness of the counterparties and the existence of collateral arrangements.
- 5.23 The significant majority of the reinsurance cover is in place with the Barbados branch of CLA (the Canadian insurance entity which owns CLG), and relates to a quota share arrangement and several longevity swaps on the annuity business, covering in total £3.8 billion of liabilities as at 31 December 2019. Concentration of exposure to CLA is accepted as it is AA rated by three ratings agencies (as at 31 December 2019) and there is believed to be reduced operational risk as a result of close relationships within the group. In addition, there are

deposit back arrangements in place for the quota share reinsurance, which are assets that CLL would retain in the event of a failure of CLA such that CLL could continue to meet policyholder obligations, as well as collateral in place for the longevity swaps.

5.24 There are also other smaller reinsurance arrangements as follows:

- Group Life and legacy individual protection business: These are a mixture of surplus and quota share arrangements with Swiss Re, Munich Re, Pacific Life Re, General Reinsurance and Canada Life Re Ireland dac, which in total have a reinsurance asset of around £118 million on the Solvency II balance sheet as at 31 December 2019. These companies have an external credit rating of at least AA- as at 31 December 2019.
- Annuity and bulk annuity business: There are a mixture of quota share longevity swaps and quota share deposit back arrangements in place to reduce longevity risk with Royal Bank of Canada Insurance Company Limited, Canada Life Annuity Reinsurance (Barbados) Corporation, JPMorgan Chase Funding Inc, and Hannover Re, which in total have a reinsurance asset of around (£174) million on the Solvency II balance sheet as at 31 December 2019. These companies have an external credit rating of at least AA- as at 31 December 2019, except for JP Morgan, which has a rating of A-.

5.25 In addition to the above, the existing enhanced annuity reinsurance arrangements that MGMA had in place with Hannover Re were transferred to CLL as part of the Part VII transfer in January 2020.

## The risk profile of CLL

5.26 CLL's liabilities are predominately annuities, Group insurance and unit linked contracts, which expose it to the following main risks:

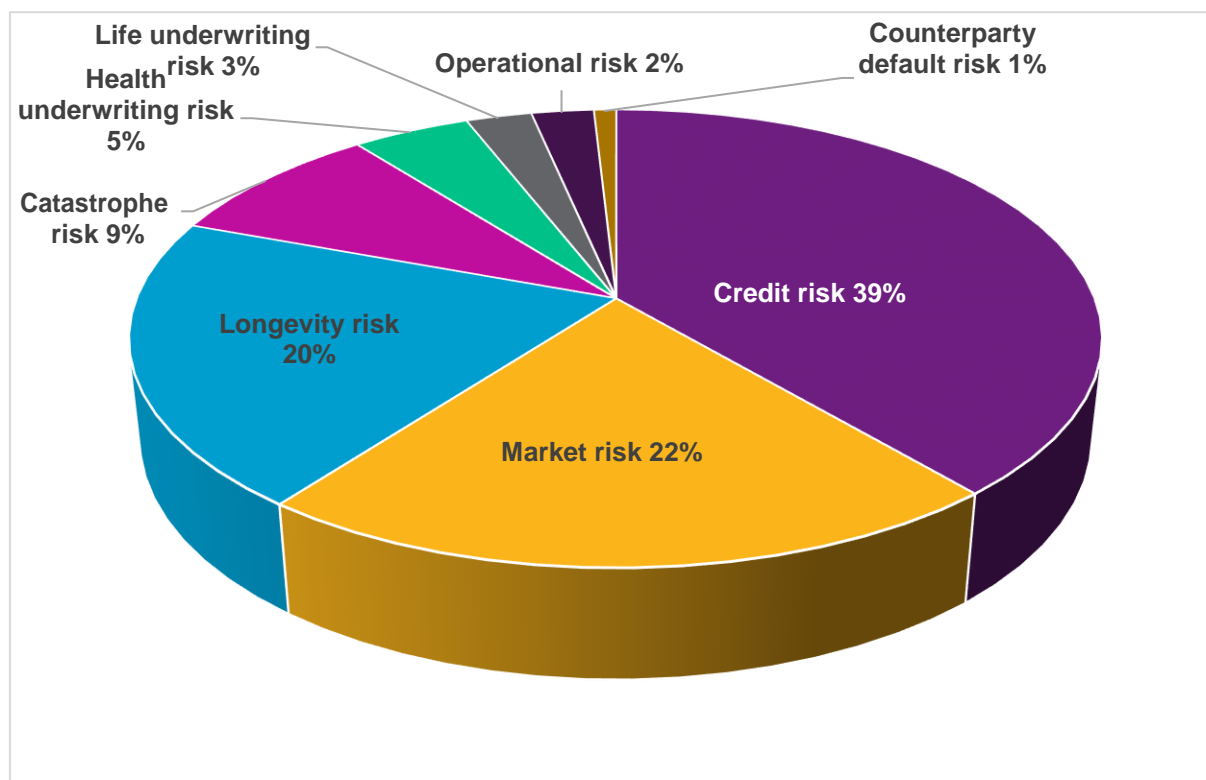
- Credit risk relating to the corporate bonds, financing arrangements and mortgages (including equity release and commercial mortgages) to back its liabilities.
- Longevity risk on CLL's large portfolio of annuity liabilities.
- Market risk on CLL's assets under management (combination of interest rate, property, equity, currency and concentration risk) and ownership of Irish Life Group Limited (which is the immediate parent company of ILA), which is shown as an equity participation on the balance sheet.
- Catastrophe risk leading to an increased incidence of death or illness of employees covered by group schemes.

5.27 The business transferred from MGMA to CLL is significantly exposed to risks relating to equity release mortgages (such as property values and property growth), although MGMA only represents a small proportion (approximately 9% of insurance liabilities (net of reinsurance)) of CLL so the combined balance sheet is much less exposed.

The underlying breakdown of the Solvency II Pillar 1 capital requirement for CLL as at 31 December 2019 can be seen below (excluding MGMA):



**Figure 5.3: Solvency II Pillar 1 pre-diversified capital requirements as at 31 December 2019**



- 5.28 Overall, there has been little change in CLL's risk exposure between 2018 and 2019 (except due to the acquisition of MGMA outlined above), with a small reduction of £57 million in the SCR over the period due to a number of offsetting factors. The move to the PIM led to a reduction in SCR, although other factors led to an increase (such as the fall in interest rates).
- 5.29 In the 2019 ORSA, scenarios were performed over the five-year business planning period. This showed that under a number of the more extreme scenarios (for example, a scenario equivalent to the 9/11 terrorist attack), the solvency ratio is estimated to fall very close to or below CLL's solvency ratio range over a five year period and before re-calculation of the TMTP. However, after re-calculating the TMTP, the solvency coverage is restored to be within the desired solvency ratio range.
- 5.30 CLL operates an Enterprise Risk Management Framework to reliably identify, measure, manage, monitor and report risks which might impact on the execution of its business plans and the ultimate achievement of its strategic objectives. For instance, climate change has the potential to drive a wide range of risks in CLL's business, so the firm is monitoring risks arising from climate change and embedding this explicitly within its Enterprise Risk Management Framework.

## Capital management

- 5.31 CLL manages its own funds so that its solvency position stays within a target range, as specified in the Risk Appetite Framework, in accordance with the Capital Management Operating Policy. The range is determined to ensure sufficient coverage above the SCR to enable the company to meet its financial liabilities in a range of stressed scenarios. CLL



manages its capital and solvency on a forward-looking basis in order to carry out its business plan within risk appetite.

- 5.32 The key requirements of the Capital Management Operating Policy cover a range of activities which can be broadly classified in terms of identification, measurement, management, monitoring and reporting of risks. A range of risk limits are covered in the Risk Appetite Framework in order to manage solvency and liquidity within risk appetite. CLL also measures its contribution to LICAT and earnings volatility through monitoring adherence to Risk Limits and Budgets set at the GWL level and included in the CLG Risk Appetite Framework.
- 5.33 CLL has a management action plan in place in case of a breach of its target solvency levels. This includes a range of actions that could be taken depending on the severity of the breach. Short term actions available include reducing or suspending dividends and re-calculating the TMTP upon a significant change in risk profile or sustained change in interest rates. The benefit of re-calculating the TMTP is not immediately available, however, as it requires formal approval from the PRA, and the benefit will reduce over time as the TMTP runs off to zero by the end of the transitional period in 2032. One action that could be taken if necessary is to raise new capital (for example, by issuing subordinated debt) or seeking a capital injection from another group company.
- 5.34 The Board maintains absolute discretion over the amount and timing of dividends and declares dividends in line with the CLL Dividend Policy.

## Irish Life Assurance plc

### Background

- 5.35 Irish Life Assurance plc ("ILA") is the main operating entity of the Irish Life Group in Ireland and since 2013 has been part of the Great-West Lifeco group of companies. Irish Life Group is a wholly-owned subsidiary of CLL.
- 5.36 ILA operates through two main divisions: Irish Life Retail (Retail Life) and Irish Life Corporate Business (Corporate Life), which together have a leading share of the Irish market. Each division's current strategic plan includes significant development of the business during the 2020 to 2024 period. ILA uses a multi-channel distribution strategy, with a large and diverse distribution network in Ireland, including a large direct sales force.
- 5.37 The 2020-2024 strategy looks to accelerate growth profitably, focused on three main areas:
- Lead in core markets through the business divisions
  - Grow in adjacent markets
  - Expand the distribution model
- Further initiatives include:
- Customer centricity: digital home for health and wealth, consistent customer delivery and customer journey management

- Operational efficiency: optimisation project
- Leading talent and capabilities: people strategy and workplace of the future.

## ILA's UK branch

- 5.38 ILA has an existing branch in imminent run off in the UK. This branch is a legacy branch with no staff and for which the servicing and administration of the remaining policies is outsourced to a third party external to the Great-West Life group of companies. The branch was actively writing, inter alia, term assurance and with-profit linked endowment policies in the UK but closed to new business in the mid-1990s. There are eight policies remaining, all of which are in run-off. Six of these will mature before 31 December 2020, with the remaining two maturing before March 2021. It is ILA's intention that this branch will enter automatically (by default) into the "supervised run-off" portion of the UK's Financial Services Contracts Regime (which will allow these remaining two policies to mature and any necessary payments to be made without any formal steps needing to be taken by ILA to change the regulatory status of its UK branch), after which the branch will be formally closed.

## ILA's long-term business

- 5.39 ILA is authorised by the Central Bank of Ireland as a "Life Insurance Undertaking" subject to Solvency II under the European Union (Insurance and Reinsurance) Regulations 2015 (S.I. No. 485 of 2015), authorised to effect and carry out, within Ireland, the business of life insurance within classes 1, 3, 4, 6 and 7. ILA has obtained permission from the CBI to carry on insurance business on a cross-border ("Freedom of Services") basis in Germany, in light of the expected transfer of the German annuity business of CLL under this Proposed Scheme.
- 5.40 The Retail Life division provides protection, pensions, investment and regular savings products to individual and small businesses in Ireland. The Corporate Life division sells pensions and risk products to employers and affinity groups in Ireland.
- 5.41 A summary of the business in force can be seen in the table below as at 31 December 2019. The total "Insurance liabilities" are equal to the Solvency II Technical provisions as at 31 December 2019 (the risk margin has not been broken down by product type but is included in the total).

**Table 5.4: Breakdown of ILA business in force as at 31 December 2019**

ILA In-force business 31 December 2019	Number of policies	Insurance liabilities (net of reinsurance) (€m)
<b>Non-profit fund</b>		
Individual insurance	456,803	592
Individual and group investment (unit-linked)	340,124	45,720
Annuities	43,755	2783
Group risk	4,314	593
Former with-profit*	57	2
Other product lines	1,683	69
<b>With-profit funds</b>		
With-profit policies	2,005	108
Risk margin	-	384
<b>Total</b>	<b>848,741</b>	<b>50,251</b>

\*These are former ILA with-profit policies that were held in a separate closed fund until it was wound up in 2012 and the policies transferred to the ILA non-profit fund as non-profit policies. Future bonuses that accrue to these policies are now fixed.

- 5.42 The unit-linked business accounts for the majority of the liabilities as measured by Technical Provisions and accounts for 94% of premiums earned in 2019. ILA's unit-linked business includes both individual and group life and pension business. The non-linked business includes annuities, income protection and term assurances.

### *Unit-linked funds with investment guarantees*

- 5.43 ILA has a number of unit-linked funds with investment guarantees. The largest funds are closed to new business, except in some cases where there are inflows from regular premiums and fund switches. The guarantees typically relate to receipt of a smoothed unit fund value on retirement or death, where a guaranteed smoothed investment return is declared on an annual basis and is subject to a minimum of zero each year. The total value of assets in these funds was €1,503 million as at 31 December 2019 relative to guaranteed liabilities of €1,242 million and there was some margin between assets and guaranteed liabilities for all the largest funds. The guaranteed liabilities were greater than the assets held as at 31 December 2019 only for some of the smallest funds where total guaranteed liabilities are less than €20 million. Additional reserves of €70 million were held outside the unit-linked funds as at 31 December 2019 to cover the potential future cost to the shareholder of the investment guarantees, as well as capital requirements of around €67 million (before diversification) at the same date.
- 5.44 One of the funds that ILA include in the above categorisation is a Unitised With-Profit ("UWP") fund, which offers some investment guarantees. This fund was transferred from Canada Life Assurance (Ireland) Limited on 1 January 2014 and is closed to new business. This fund is not treated as a ring-fenced fund under Solvency II and instead sits in the ILA non-profit fund.

At maturity, policyholders receive a minimum of their guaranteed smoothed unit fund value, which is based on premiums paid in, less charges plus reversionary bonuses declared on an annual basis. The vast majority of the investment guarantees in the UWP fund are reinsured with the Barbados branch of CLA and hence the reserves held as at 31 December 2019 for the investment guarantees on the UWP fund are only €0.3 million.

### ***With-profit funds***

- 5.45 ILA has two conventional ring-fenced with-profit funds (known to ILA as the “Closed Par Fund” and the “Open Par Fund”). Both of these funds are closed to new business.
- 5.46 The policies in the two conventional with-profit funds were originally written in the Irish branch of CLA and were transferred to Canada Life Assurance (Ireland) Limited in 2012 and subsequently to ILA on 1 January 2014 (along with the UWP fund described in paragraph 5.44 above). The Closed Par Fund consists of all the with-profit policies that were in force at the date of demutualisation of CLA (on 4 November 1999). The with-profit business written after demutualisation was written into the Open Par Fund, which was closed to new business in December 2000. Both funds are subject to the Scheme of transfer from Canada Life Assurance (Ireland) Limited to ILA in 2014. These funds now consist mainly of endowment business, whole of life business and a small block of deferred annuity business.
- 5.47 The benefits payable to policyholders include basic guaranteed benefits which can be increased by the addition of reversionary dividends, as well as terminal dividends on maturity and surrender. Reversionary and terminal dividends vary depending on the experience of the funds and can be zero. Future reversionary and terminal dividends can be reduced in the event of adverse experience. For the Closed Par Fund, no transfer of assets is allowed out of the fund to the shareholder and therefore the value of the assets will be fully distributed to policyholders. For the Open Par Fund, a percentage of the dividends added to policies each year is transferred to the shareholder, which is usually around 3%. This is determined by a pre-agreed formula based on the assets held in the participating funds at the aggregate level in CLA, as set out in the Scheme of transfer in 2014. Otherwise all assets of the Open Par Fund will be distributed to policyholders.
- 5.48 The Solvency II insurance liabilities for these two with-profit funds are set to broadly (although not exactly) equal the assets in each of the funds. This is achieved by setting the assumed future dividend rate so as to distribute all the expected future assets of the fund to policyholders over their lifetime. The high-level Solvency II Pillar 1 financial information for the two with-profit funds can be seen in Table 5.5 below as at 31 December 2019:

**Table 5.5: ILA with-profit funds Solvency II Pillar 1 position at 31 December 2019**

<b>Solvency II Pillar 1 31 December 2019 (€ million)</b>	<b>Closed Par Fund</b>	<b>Open Par Fund</b>
<b>Total assets</b>	<b>84.3</b>	<b>40.4</b>
Guaranteed liabilities	19.1	22.8
Solvency II Technical provisions in excess of guaranteed liabilities	52.4	13.6
Other liabilities	13.1	3.5
<b>Total liabilities</b>	<b>84.6</b>	<b>39.8</b>
SCR	0.4	1.1

5.49 It can be seen from Table 5.5 above that there is a large margin above guaranteed liabilities in each of the funds. In calculating the SCR, management actions are assumed which reduce the future dividends assumed in the calculation of the liabilities, subject to the restriction that no more than a 15% reduction in total pay-outs is allowed in any one year. The resulting SCR in the table above is very small and is held in the non-profit fund (hence a cost to the shareholder) in respect of the following risks:

- **Expense risk:** the risk to the shareholder that the fixed expense charges taken from the funds (as set out in their operating rules) are insufficient to meet the actual expenses incurred by the non-profit fund.
- **Operational risk:** operational losses are generally expected to be borne by the shareholder (although in practice this would be assessed on a case by case basis).
- **Equity risk:** a small cost arises from the equity stress in the Open Par Fund where the management action restriction described above means the future dividends could not be reduced sufficiently to cover the complete loss arising from the equity fall required when assessing the SCR.

5.50 There are no formal capital support arrangements in place between the with-profit funds and the non-profit fund, however, the non-profit fund would be expected to provide informal support if required. Such support has not historically been provided since the transfer in 2014 and, in practice, I consider that the possibility of providing such support is remote, as the high surplus in the funds would be used as a buffer to cover smoothing costs before support is required from the non-profit fund (and which could not subsequently be passed back to the non-profit fund in the event of a subsequent rise in investment markets).

5.51 As described in paragraph 4.35, the CBI's "Domestic Actuarial Regime and Related Governance Requirements Under Solvency II" sets out specific requirements for the management of with-profit funds, including the requirement to establish and maintain a publicly available "With-Profits Operating Principles" document, setting out the management of the funds. ILA have, however, received an exemption from this requirement from the CBI due to the low scale and low complexity of their with-profit funds. There is no requirement to have a With-profit committee and the ILA Board has responsibility for ILA's with-profit funds.

## Pension schemes

5.52 ILA has three ring-fenced funds relating to the staff pension schemes, summarised as follows:

- The main defined benefit scheme has assets of €1,372 million as at 31 December 2019. It has been closed to new entrants since 1 January 2007. Employees recruited since 2007 are in either a defined contribution plan or a Hybrid pension plan in a separate scheme.
- The Hybrid pension scheme has assets of €4 million as at 31 December 2019 and has been closed to new entrants since December 2014.
- ILA has a subsidiary company, which is a legacy from its US operations, which has pension scheme obligations referred to as the “ILONA” schemes with assets of €10 million.

5.53 The excess of liabilities over assets in the pension schemes is €1.0 million as at 31 December 2019 (€0.4 million as at 31 December 2018) after allowing for future discretionary increases, and this is shown on the Solvency II balance sheet as a liability. During 2017, ILA established a Discretionary Increase Policy, which sets out the scenarios in which the company will grant discretionary increases in retirement and the factors to be considered when calculating increases. The schemes are currently in surplus and hence discretionary increases are assumed in the valuation so that they fully absorb the surplus in the schemes in aggregate (although the assumed increases are not exactly calibrated to the surplus, and hence a small liability arises at 31 December 2019). The combined level of surplus above guaranteed liabilities in the schemes is €134.5 million as at 31 December 2019 and €172.6 million as at 31 March 2020.

5.54 The associated SCR for the pensions schemes as at 31 December 2019 is €77.1 million (€51.8 million at 31 December 2018).

## Recent relevant events

5.55 During 2020 to date, ILA’s immediate parent company Irish Life Group Limited acquired Conexim Advisors Limited, Acumen & Trust DAC and announced the sale of Irish Progressive Services International Limited. None of these transactions has or is expected to have a material financial impact to ILA or with respect to its service arrangements, including the service arrangements for the Transferring Policies. In any event, as CLL is the immediate parent company of Irish Life Group Limited, the Transferring Policyholders are already exposed to the very minor impact of these transactions whether the Proposed Scheme is implemented or not.

## Financial condition

5.56 The Solvency II Pillar 1 position for ILA as at 31 December 2019 and 31 December 2018 can be seen in Table 5.6 below.

**Table 5.6: Solvency II Pillar 1 position of ILA as at 31 December 2018 and 31 December 2019**

€m	31/12/2019	31/12/2018
<b>Total Assets*</b>	<b>54,317</b>	<b>46,672</b>
Best estimate liabilities (gross of reinsurance)**	51,345	43,631
TMP	0	0
Risk margin	384	375
<b>Technical provisions***</b>	<b>51,729</b>	<b>44,007</b>
Other liabilities	654	634
<b>Total Liabilities</b>	<b>52,383</b>	<b>44,641</b>
<b>Excess of assets over liabilities</b>	<b>1,934</b>	<b>2,031</b>
<b>Eligible Own Funds to meet SCR****</b>	<b>1,934</b>	<b>1,780</b>
<b>Eligible Own Funds to meet MCR****</b>	<b>1,934</b>	<b>1,780</b>
Solvency Capital Requirement	1,145	1,019
Minimum Capital Requirement	515	458
<b>Excess resources over SCR</b>	<b>789</b>	<b>761</b>
<b>Excess resources over MCR</b>	<b>1,419</b>	<b>1,322</b>
<b>SCR coverage ratio (%)</b>	<b>169%</b>	<b>175%</b>
<b>MCR coverage ratio (%)</b>	<b>375%</b>	<b>389%</b>

\*This includes reinsurance recoverables of €1,479 million as at 31 December 2019 and €1,530 million at 31 December 2018.

\*\*This includes unit-linked liabilities of €47,021 million as at 31 December 2019 and €39,457 million as at 31 December 2018.

\*\*\*The technical provisions net of reinsurance at 31 December 2019 were €50,250 million and €42,476 million at 31 December 2018.

\*\*\*\*The eligible Own Funds as at 31 December 2018 is net of a foreseeable dividend distribution of €250 million that was paid in 2019 and €0.3 million which belongs to the ring-fenced with-profit funds. No such foreseeable dividend was expected or allowed for at 31 December 2019.

- 5.57 The SCR coverage ratio at both year-end dates was higher than ILA's target range for the solvency ratio. The SCR coverage ratio reduced over 2019, which was largely due to falls in interest rates during 2019 as the non-linked liabilities (including, in particular, the risk margin component of the Technical Provisions) are not fully duration-matched by their backing assets. The assets under management increased significantly over 2019 due to high investment returns experienced on the unit-linked policyholder funds. The Own Funds increased by €154 million in 2019 and by €127 million in 2018 (before the dividend payment of €250 million). No dividend has been declared for year-end 2019, given the evolving COVID-19 pandemic.
- 5.58 ILA does not use the Solvency II Matching Adjustment to value liabilities or the Solvency II transitional measures, however, it does use the Volatility Adjustment for some product classes.



- 5.59 As well as the Solvency II Pillar 1 position, ILA must also calculate a Solvency II Pillar 2 position, reflecting its own assessment of ILA's capital requirements and balance sheet position. Although this position is not publicly disclosed, I have seen details of ILA's Solvency II Pillar 2 assessment of the balance sheet and risk capital, carried out at 31 December 2019. This shows slightly lower excess capital (above the required capital requirements) and a slightly lower solvency ratio compared to the Pillar 1 assessment. This is mainly due to the following offsetting factors (which have been adjusted under Pillar 2):
- The Solvency II Pillar 1 capital requirements for the Group unit-linked business are considered too onerous, resulting in the combined SCR and risk margin being significantly in excess of the value of the business under Pillar 1.
  - The Solvency II Pillar 1 rules heavily restrict the credit that can be taken for future premiums on the individual unit-linked business.
  - The Solvency II Pillar 1 rules in respect of the pension scheme capital are not considered to reflect the risks on this liability, resulting in a higher capital requirement under Pillar 2 for the pension scheme. Adjusting for this aspect under Pillar 2 more than offsets the benefits outlined above on the insurance business.
- 5.60 I have seen projected business plans under a range of central scenarios carried out as at year-end 2018 and adjusted to end of Q1 2019, which forecast projected profits before dividends each year and hence a steadily increasing solvency ratio over the period. The implementation of the strategic plan as outlined above in paragraph 5.37, requires investment spend but the trajectory of the solvency ratio still increases over the five-year period. I understand from ILA management that an update to the business plan projections is expected to be completed in the coming months, so if there is anything of significance to report that impacts upon the Proposed Scheme I will cover this in my Supplementary Report.
- 5.61 Like CLL, ILA must also produce the LICAT disclosures under the Canadian regime, although ILA management has confirmed to me that this is a metric which has relevance primarily to the Canadian-domiciled parent companies of ILA and CLL for capital management purposes. Nevertheless, I have seen estimates of ILA's LICAT ratio as at 31 December 2019, which is higher than their Solvency II Pillar 1 solvency ratio.

## Reinsurance and financing arrangements

- 5.62 ILA has a high level of reinsurance in place on the individual protection and annuity product lines, where reinsurance plays an important role in limiting ILA's exposure to adverse mortality, morbidity and longevity experience. In total the reinsurance asset under Solvency II is €1,479 million as at 31 December 2019, with the highest exposures as follows:
- **Annuities:** €1,152 million of "with assets" transactions with XL Re and Markel Bermuda, where collateral is in place which materially exceeds the technical provisions relating to the reinsurance asset. These companies have credit ratings of AA- and A respectively from S&P at 23 April 2020 (with similar ratings from Moody's and Fitch). There are also longevity swaps in place with Hannover Re (rated AA- by S&P at 23 April 2020) and the Barbados branch of CLA.



- **Individual protection:** €282 million of reinsurance with Swiss Re, which is ILA's largest (uncollateralised) counterparty exposure, and €145 million with Munich Re. Both these reinsurers have a credit rating of AA- from S&P at 23 April 2020 (with a similar rating from Moody's and Fitch (the latter is unavailable for Swiss Re)).
- 5.63 ILA has limited reinsurance with other companies in the GWL group, with three treaties written with the Barbados branch of CLA, which is not one of ILA's five largest reinsurance counterparty exposures.
- 5.64 There is limited reinsurance in place on ILA's group risk portfolio and there are some legacy reinsurance arrangements on discontinued product lines.

## Governance and risk appetite

- 5.65 I have seen the Enterprise Risk Management Policy that covers Irish Life Group Limited and its subsidiaries (including ILA). This outlines the risk principles, governance and processes and defines how the requirements for prudent risk management will be implemented consistent with CLG ERM Policy, Great-West Lifeco Inc ERM Policy and relevant regulatory requirements. The system of risk management incorporates all aspects of culture, governance, risk appetite framework, processes and infrastructure in place to identify, measure, monitor, manage and report risks. The system of risk management is owned and operated by all three lines of defence and is overseen by the Board of Directors.
- 5.66 The Risk Appetite Framework reflects the aggregate levels and types of risk that ILG and ILA are willing to accept in order to achieve their business objectives. It includes the Risk Strategy, Risk Appetite Statement and Risk Limit Framework, which includes three levels of limits against which ILA regularly monitor. The structure of the Risk Appetite Framework is similar between ILA and CLL.

## Capital management

- 5.67 ILA defines capital management as the process of identification, measurement, monitoring, management and reporting of risks and capital requirements to ensure that ILA has sufficient capital, liquidity and reserves to meet its liabilities and regulatory solvency requirements under a range of stressed conditions and of a sufficient quality. ILA manages its capital with the aim of maintaining solvency at a level which enables ILA to carry out its business plan and meet its growth objectives, within its risk appetite, and has several solvency ratio target ranges and escalation triggers in place to do this.
- 5.68 The capital position is calculated by ILA's Actuarial Function on a quarterly basis as part of the financial reporting cycle. In addition, the solvency ratio is monitored on a continuous basis by tracking key drivers of the solvency ratio.
- 5.69 ILA has a Recovery Plan in place should the Solvency II Pillar 1 solvency ratio fall below a hard limit. ILA has a long list of actions that could be taken to improve solvency if required. One action that could be taken, if necessary, is to approach the parent company (either from ILG or another company higher in the Great-West Lifeco Inc ownership structure) to seek a capital injection).
- 5.70 ILA currently has no subordinated liabilities.

- 5.71 The Board maintains absolute discretion over the amount and timing of dividends. In recent years, dividends have only been declared when ILA's solvency position is in or above their target range and remains so once dividends have been declared.

## Administration and investment management

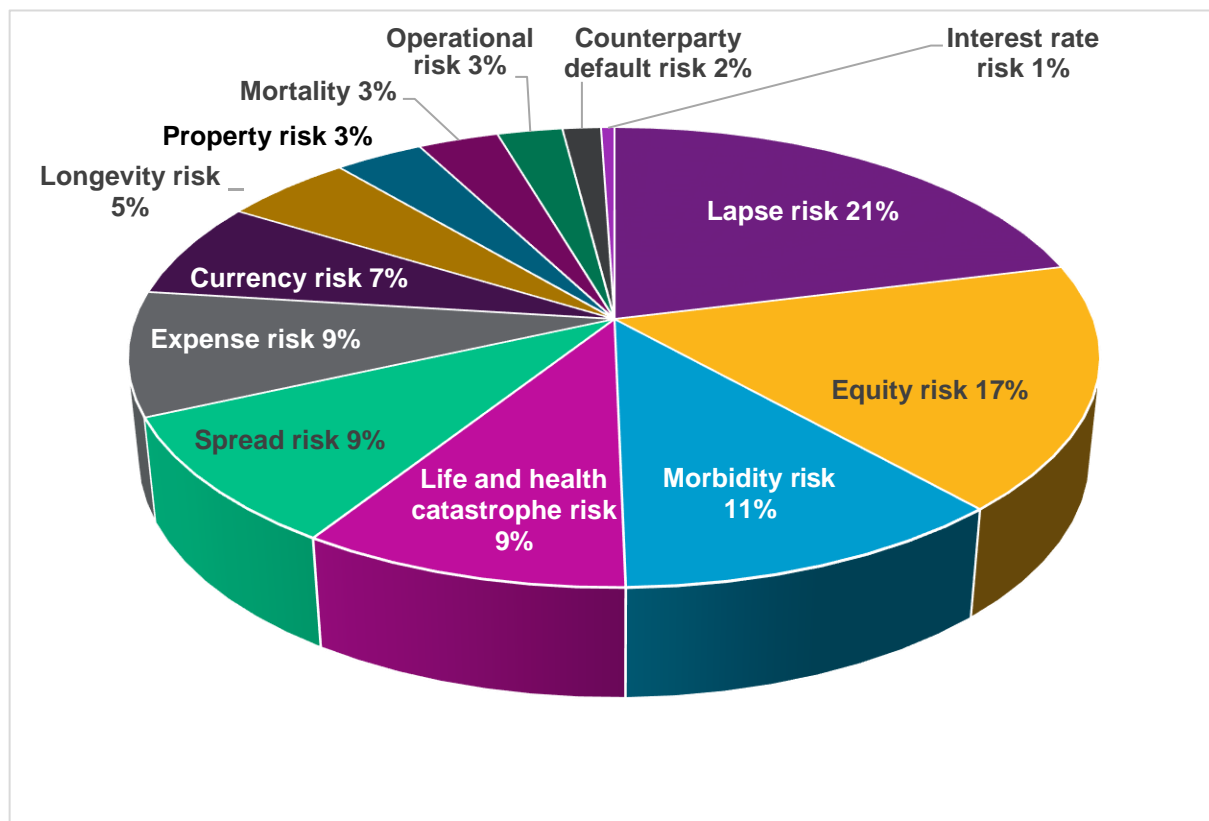
- 5.72 The administration of ILA's existing business is undertaken in-house at the company's offices in Dublin, without any external outsourcing. Other functions, which operate across all product lines, such as IT, Actuarial, Finance and Marketing are also provided internally within ILA. The general administration and payment services in respect of annuity policies such as those included in the Proposed Scheme includes the maintenance of policyholder data, managing escalation of pension payments and setting up of second life benefits as and when required. I understand from ILA management that no administration processes are expected to change and that the Transferring Policyholders will continue to contact the firm using the same postal address, email address and phone contact numbers that they currently do. It is possible that the Employers Registered Number (payroll reference) may need to change but this is still to be confirmed and in my opinion has no material impact upon the Transferring Policyholders.
- 5.73 ILA-invested assets are managed by three separate entities, all of which are currently part of the GWL group (although as described in paragraph 5.55, one of these is expected to be sold during 2020). ILA's unit-linked invested assets are primarily managed by Irish Life Investment Managers Limited, with a small proportion, comprising the third-party Self Directed Funds, being managed by Irish Progressive Services International Limited. ILA's non-linked invested assets are managed by Canada Life Asset Management Limited.

## Risks inherent in ILA

- 5.74 The largest risks that ILA is exposed to relate to market risk and lapse risk on its large unit-linked individual and group life and pension business. This reflects the fact that the value from this business (based on the annual management charges) is included in ILA's Own Funds and the value would fall following a reduction in fund values or policies lapsing.
- 5.75 In addition to this, a reasonable proportion of ILA's risk exposure is generated from ILA's annuities and protection products, for example:
- The risk of annuity policyholders living longer requiring ILA to pay more annuity payments than expected (longevity risk)
  - The risk of a significant number of deaths on the corporate and retail life insurance products, for example through pandemics (catastrophe risk)
  - The risk of higher disability and sickness rates on the individual and group Specified illness cover and Income protection products (morbidity risk)
  - The risk of higher credit spreads on the bonds used to back annuity and income protection liabilities, as well as higher default rates (spread risk and default risk)
- 5.76 Other less significant risks that ILA is exposed to are as follows:

- The risk that expenses increase above the levels assumed in the valuation of the BEL, for example, from staff costs, cost of commissions to sales intermediaries, cost of IT infrastructure and the cost of land and buildings occupied (expense risk). In addition, inflation rates could increase beyond the levels assumed in the valuation of liabilities.
  - The risk of inadequate or failed internal processes, people and systems or from external events (operational risk).
  - The risk of falls in property values, either from directly held shareholder investments and indirectly through falls in property assets in the unit-linked funds (property risk).
  - The risk of adverse movements in foreign exchange rates for non-Euro denominated assets (predominantly in the unit-linked policyholder funds), leading to falls in asset values when converted to Euros (currency risk).
  - The risk of changes in interest rates leading to changes in the valuation of the BEL, which are not directly offset by changes in the values of assets (interest rate risk).
  - The risk of loss from higher than expected mortality rates on the individual and group life insurance policies which pay benefits to insured policyholders upon death (mortality risk).
- 5.77 In addition, ILA has risks relating to each of its three pension schemes and the market risk on the assets in these schemes is included in the Solvency II Standard Formula. The trustees of the largest scheme significantly de-risked the pension scheme in 2018 by switching a proportion of its asset holdings from equities into a mixture of corporate bonds and cash, leading to a large reduction in risk capital.
- 5.78 ILA is also exposed to liquidity risk, given the requirement to generate necessary funds to meet its obligations as they fall due. Capital is not specifically held against this risk (in line with the requirements for the Solvency II Standard Formula), and instead liquidity is monitored on a daily basis by the finance function and investment limits for different liquid and illiquid asset categories are adhered to.
- 5.79 The breakdown of Solvency II Pillar 1 risk capital held by ILA as at 31 December 2019, before diversification, can be seen in Figure 5.7 below:

**Figure 5.7: Solvency II Pillar 1 pre-diversified capital requirements as at 31 December 2019**



- 5.80 The SCR has increased by €126 million since 31 December 2018 to €1,145 million at 31 December 2019. This increase was largely due to the high equity market returns during the year and lower interest rates, both leading to higher asset values as well as a higher Solvency II equity stress.
- 5.81 The risks above are managed and mitigated in accordance with the risk management and governance framework as outlined further above. In particular, risk mitigation techniques are described further in Section C of the firm's published Solvency and Financial Condition Report, available publicly on the firm's website.
- 5.82 The interest rate risk capital in Figure 5.7 above is small, being 1% of the undiversified risk capital required. This is because the assets and the base insurance liabilities are well matched. However, the solvency ratio is more sensitive to changes in interest rates, due to the impact on risk margin (which is not stressed in the SCR) and due to the changes in the values of assets and liabilities used in the different SCR stresses, as a result of the lower interest rates.
- 5.83 I have seen details of ILA's stress and scenario testing that was performed for the ORSA in 2019. This considers emerging risks, such as climate change and Irish pension reform. A range of scenarios were performed, including the most onerous severe recession scenario. This shows that ILA does not fall before its hard limit solvency ratio in any of the five years of the business planning period.

## Section 6: The Proposed Scheme

### The motivation for the Proposed Scheme

- 6.1 The intention of the Proposed Scheme is to transfer a small number of Euro-denominated policies to ILA from CLL via a Part VII transfer. These policies were originally written by ELAS on a cross border freedom of establishment (branch) basis through authorised German and Irish branches to policyholders, the vast majority of whom had their permanent residence in Germany or Ireland (except four policyholders who were resident in either France, Austria or Spain). These policies were previously transferred to CLL from ELAS by way of a previous Part VII transfer in 2016, and have subsequently been serviced by CLL on a freedom of services (cross-border) basis.
- 6.2 The end of the "implementation period" in relation to the United Kingdom's exit from the European Union is currently scheduled to occur on 31 December 2020. CLL believes that after expiry of the implementation period, it is likely to lose its legal rights to service cross-border policies based in the European Union (including the ability to pay claims), due to the loss of the "passport" rights applicable to member states of the European Union. The Board of CLL therefore considers that the transfer of the above policies pursuant to the Proposed Scheme is necessary to ensure that the GWL Group can continue to meet its legal and regulatory obligations in relation to the Transferring Business on an ongoing basis.
- 6.3 No further policies have been written by CLL for policyholders with a permanent residence outside of the UK since 2016 and I understand from CLL management that no such further policies are expected to be written prior to the Effective Date of this Proposed Scheme of 31 December 2020.

### Summary of the Proposed Scheme

- 6.4 The Proposed Scheme is expected to be presented to the Court for a Directions Hearing, on 8 September 2020, for a Final Hearing in December 2020. If approved then it is expected to be implemented by the Court with an Effective Date of 31 December 2020.
- 6.5 If the Proposed Scheme is approved by the Court, then on the Effective Date, the Irish and German non-profit annuity policies of CLL will transfer to the ILA non-profit fund, along with their allocated assets and liabilities (together comprising the "Transferring Business").
- 6.6 The amount of assets to be transferred from CLL to ILA is defined in the Proposed Scheme as the "Specified Assets Amount" and its calculation and amount is yet to be agreed between the parties. I will provide an update on this in my Supplementary Report, although I understand that the current expectation of the parties is that this amount is unlikely to be so large that it would move the solvency coverage ratio of either CLL or ILA by a material amount.
- 6.7 The terms and conditions of the policies contained within the Transferring Business will be unchanged by the Proposed Scheme.

## Transferring assets and liabilities

- 6.8 The Transferring Business relates to 622 Irish and 115 German in-payment individual non-profit annuities, in addition to 2 policies sold in Austria, 1 in Spain and 1 in France. These policies have combined Insurance liabilities (net of reinsurance) of £68 million as at 31 December 2019.
- 6.9 The policies consist of level and fixed escalating annuities (there are no contractual index-linked or unit-linked annuities). The policies are not reinsured.
- 6.10 In addition, to the Irish and German policies, there is one policyholder who is currently resident in Guernsey and was so resident when the policy was first taken out. This policy will be excluded from the Proposed Scheme, as it is not affected by the United Kingdom's exit from the European Union.
- 6.11 The Proposed Scheme makes provision for "Residual Policies", which are policies intended to be transferred under the Proposed Scheme, but due to a limited range of legal reasons cannot be transferred on the Effective Date. It is not expected that there will be any Residual Policies and I will provide an update in my Supplementary Report if this situation changes. If there are indeed any Residual Policies, these will be reinsured from CLL to ILA at the time of the Effective Date (under the "Residual Policies Reinsurance Arrangement") until such time as all necessary requirements have been obtained for the relevant Residual Policy to transfer to ILA under the terms of the Proposed Scheme. I note that in this case, these policies will need to be serviced from the UK which may not be possible post 31 December 2020. Should this position arise, CLL would liaise with the relevant local EU regulators to agree an acceptable solution for the very small number of policies likely to be affected. I will provide an update in my Supplementary Report if anything materially changes in relation to this aspect of the Proposed Scheme.
- 6.12 "Excluded Policies" are identified in the Proposed Scheme as those that have been agreed in writing not to be transferred and all those existing policies in CLL other than the policies referred to in paragraph 6.8 above. Any Residual Policy which is not subsequently transferred will become an Excluded Policy if the Residual Policies Reinsurance Arrangement is terminated.
- 6.13 The external legal advisers to CLL (Herbert Smith Freehills) have performed a legal review of relevant previous CLL schemes, namely the scheme between ELAS and CLL dated 8 February 2016, and have confirmed that there are no enduring provisions in that scheme that would be affected by this Proposed Scheme and which I would need to consider in the context of this Proposed Scheme.

## Administration

- 6.14 CLL currently has two service agreements in place with other group companies in relation to the Transferring Business, as follows:
- Services Agreement between Canada Life Group Services Limited and Canada Life Limited dated 22 February 2016 and varied on 5 July 2016, covering annuity payment processing and associated services

- Services Agreement between Irish Life Financial Services Limited and Canada Life Limited dated 30 September 2018, covering all other relevant administration services in connection with the Transferring Policyholders (for example, managing escalation of pension payments and updating records with any changes of details).

- 6.15 The above agreements only relate to the Transferring Business and no other policies of CLL.
- 6.16 It is intended that the Proposed Scheme will transfer these agreements automatically (without any changes to the provisions within these agreements) to ILA from CLL on the Effective Date. I have been informed by ILA that there is no current intention to make any changes to these agreements following the transfer.
- 6.17 The Proposed Scheme will not result in any change in the personnel who are responsible for conducting policy administration in relation to each part of the Transferring Business. In addition, the way in which policyholders can make contact with the company in relation to their policies will be unaffected.

## Costs of the Proposed Scheme

- 6.18 CLL will bear all costs and expenses in relation to the preparation and carrying into effect of this Proposed Scheme, including policyholder communications, whether before or after the Effective Date.

## Tax

- 6.19 CLL and ILA have concluded that there is insufficient uncertainty in the corporate tax, VAT and policyholder tax outcomes arising from the Proposed Scheme and, as such, the tax clearance legislation in each relevant jurisdiction cannot be engaged on its terms. No tax clearances or confirmations from the relevant tax authorities are therefore being sought. Instead, external tax advice will be sought on the tax consequences and I will comment further on the status of this tax advice in my Supplementary Report.
- 6.20 All tax liabilities and assets of CLL that are considered Excluded Liabilities and Excluded Assets will remain with CLL and will not transfer under the Proposed Scheme.

## Other

- 6.21 On and with effect from the Effective Date, all legal proceedings, whether pending, current or future against CLL (including as the plaintiff, claimant, applicant, defendant, respondent, pursuer, defender or petitioner) in respect of the Transferring Business will be continued or commenced by ILA. I have made enquiries of such matters to the management of CLL and have been informed that there are no such proceedings that significantly affect any of the Transferring Business.
- 6.22 I have made enquiries to the management of ILA and have been informed that there are no material litigation issues extant in ILA currently that would have any significant effect on the Transferring Business.



## Section 7: The effect of the implementation of the Proposed Scheme on the Transferring Policies

### Introduction

- 7.1 In this section I consider the effect of the implementation of the Proposed Scheme on the transferring CLL policies. The key points I have considered are:
- The financial resources available to provide security for the Transferring Policyholders after implementation of the Proposed Scheme, compared to those currently available.
  - Any change to the profile of risks to which the Transferring Policyholders are exposed as a result of the transfer.
  - The effect of the implementation of the Proposed Scheme on the reasonable expectations of the Transferring Policyholders, including benefit expectations, service standards, management and governance.
- 7.2 I have considered each of these further in the sections below.
- 7.3 I note that there is no intention of ILA to reinsure the Transferring Policies once transferred to ILA from CLL and these policies are not currently reinsured within CLL.
- 7.4 In the analysis below, I have converted the figures provided by ILA in euros to pounds (using the GBP/EUR exchange rate as at 31 December 2019 of £1 = €1.18175), in order to be directly comparable to that of CLL. I will provide an update on any effect the exchange rate might have on the analysis in my Supplementary Report.

### The financial resources available to provide security of benefits

#### Financial strength

- 7.5 Table 7.1 below shows the pro-forma pre-Scheme financial strength of CLL (after allowing for the MGMA transfer to CLL) and the post-Scheme financial strength of ILA as at 31 December 2019 on the Solvency II Pillar 1 basis:

**Table 7.1: CLL solvency pre-Scheme and ILA solvency post-Scheme as at 31 December 2019**

Solvency II Pillar 1 31 December 2019	CLL (pro-forma, including MGMA) pre-Scheme (£m)	ILA pro-forma post-Scheme (converted to £m)
Own Funds	4,240	1,641
SCR	2,710	974
<b>Excess resources over SCR</b>	<b>1,530</b>	<b>667</b>
<b>Solvency coverage ratio</b>	<b>156%</b>	<b>168%</b>



- 7.6 The figures in the table show that ILA is expected to have lower excess resources over its SCR in monetary amounts following the implementation of the Proposed Scheme than CLL has before its implementation. However, due to the relative size of the other business contained within each entity, the pro-forma Solvency II Pillar 1 solvency coverage ratio of ILA is 12% higher than CLL on a Solvency II Pillar 1 basis and so the security of the Transferring Policyholders is not adversely affected by the Proposed Scheme.
- 7.7 The ILA pro-forma post-Scheme figures in the table above assume a £79 million payment from CLL to ILA upon the transfer of the liabilities, which has yet to be agreed between the parties. I will provide an update on this in my Supplementary Report, however, if the payment (in excess of assets backing insurance liabilities required by ILA) was higher or lower by £10 million, this would result in only a small change to the solvency coverage ratio of ILA of around +/- 1%.
- 7.8 As shown in Table 5.1, the size of the Transferring Business is small relative to the other business in both CLL and ILA (being around 0.4% and 0.2% of the respective Insurance liabilities (net of reinsurance) for each company. Given this relatively low size of the Transferring Business and the immaterial impact of the Proposed Scheme on the Solvency II Pillar 1 basis, I have not considered the detailed impact of the Proposed Scheme on a Solvency II Pillar 2 basis or on a LICAT basis for either CLL or ILA. However, I have seen the Solvency II Pillar 2 basis for each company (for ILA as at 31 December 2019 and CLL as at 31 December 2018), as described earlier in this report. At these dates, the Solvency II Pillar 2 solvency ratio for CLL was higher than that of ILA. However, the Solvency II Pillar 2 solvency ratio for ILA is only slightly lower than its Solvency II Pillar 1 solvency ratio, which is in excess of its target range. Therefore I have no reason to consider that the security of the Transferring Policyholders will be adversely affected by the Proposed Scheme. I will provide an update on CLL's Solvency II Pillar 2 position as at 31 December 2019 in my Supplementary Report when the information is available.
- 7.9 Since 31 December 2019 there have been significant changes in the economic and insurance environment as a result of COVID-19. I comment on the preliminary indications of the likely high-level effects of this global pandemic on the financial position of both firms in more detail in Section 10 of this report, although it is still too early to have fully worked through all the financial impacts in this fast-changing situation. Consequently, I expect to provide more detailed information on how COVID-19 has affected the financial position of both firms in my Supplementary Report.

### **Capital policies**

- 7.10 The capital policies of CLL and ILA require them to hold additional capital over and above their Solvency II Pillar 1 capital requirements, so that the companies have sufficient capital and reserves to meet their liabilities and regulatory solvency requirements under a range of stressed scenarios. This increases the security of policyholders and is normal practice in the UK and Irish life insurance industries. Both firms have appropriate (and very similar) processes in place to identify, measure, monitor, manage and report on risks and capital requirements.
- 7.11 The risk appetite and capital policies of both CLL and ILA will be unchanged by the Proposed Scheme. Therefore, we can compare the current target range of solvency ratios of each company in order to help understand the relative security of each company as at the Effective

Date. I have been provided with details of the Capital Management Policies of both CLL and ILA, including the target ranges for solvency coverage and intervention levels for further management actions and escalation. Both firms operate with similar target ranges in excess of the statutory minimum coverage requirements and with intervention levels/triggers, and I have been provided with details of the various management actions that would be utilised if and when these intervention levels are breached. Both firms have similar governance arrangements in place in case of a breach, and in addition both firms have comparable trigger levels in the case of further falls in solvency capital coverage, each having similar escalation protocols and governance arrangements. I therefore consider that there are comparable arrangements in place in both CLL and ILA to monitor and manage the financial strength and solvency capital position of each firm.

### **Management actions**

- 7.12 Both CLL and ILA have a management action plan in place in case of a breach of their target solvency levels as referred to above. CLL has prepared a list of actions which it would seek to implement in the event of a breach. Short term actions available include reducing or suspending dividends and re-calculating the TMTP upon a significant change in risk profile or sustained change in interest rates. ILA has similarly prepared a list of actions which it would seek to implement in the event of a breach, and although the option to re-calculate the TMTP is not available to ILA, ILA's solvency position is less sensitive to changes in interest rates (although still has a large negative exposure to falls in interest rates). However, I note that the benefit of re-calculating the TMTP will not be immediately available as a mitigating action for CLL as it requires formal approval from the PRA, and the benefit will reduce over time as the TMTP runs off to zero by the end of the transitional period in 2032. One action available for both companies, if necessary, is the possibility of raising new capital (for example, by issuing subordinated debt) or seeking a capital injection from another group company.
- 7.13 For both companies, the Board maintains absolute discretion over the amount and timing of dividends and will not declare dividends if the solvency position of either company is threatened.

### **Capital projections**

- 7.14 Both CLL and ILA produce business plans and financial projections that project business volumes and financial/solvency information over a five-year period. These projections are subject to a range of uncertainties including, for instance, volumes of future new business, future economic and demographic conditions, future taxation and expense levels for both entities and future dividends payable to shareholders, as well as future regulatory requirements. As such, these provide an approach to indicating how the financial position of each entity might develop during the five-year period and can be used as a benchmark against which to consider how future events might impact upon the financial position. However, these should not be seen as projections that have a high degree of likelihood of being met exactly, as the existing COVID-19 pandemic readily demonstrates. When considering these business plans and capital projections therefore, I am particularly considering whether there is anything in the general direction of travel which would cause particular concern in respect of the security afforded to policyholders in either CLL or ILA, rather than being beholden to a particular level of solvency capital coverage that is demonstrated at any particular future point in time.

## CLL

- 7.15 I have seen a business plan produced by CLL in February 2020, which shows a stable projected solvency ratio over the five-year period from 31 December 2019, after allowing for the capital required to support future new business levels (as agreed with GWL group). This includes the expected implementation of a new reinsurance arrangement during 2020, which has a relatively substantial capital benefit, and also allows for the expected growth in Own Funds of Irish Life (which is a wholly-owned subsidiary of CLL), but does not directly include any financial impacts expected from the current COVID-19 pandemic. I understand from CLL management that the current expectation is that the new reinsurance arrangement will be completed during 2020. As this will materially affect the solvency position of CLL I will provide an update on this in my Supplementary Report. I have made separate comments on the effect of COVID-19 on this business plan in Section 10.

## ILA

- 7.16 I have seen the ILA business plan projected for five years from year-end 2018 and adjusted to take into account known changes as at 31 March 2019. This shows forecasted profits before dividends each year and hence a steadily increasing solvency ratio over the period, before dividends. The implementation of the strategic plan requires investment spend but, after taking this into account, the trajectory of the solvency ratio still increases over the five-year period, allowing the capacity to declare dividends to ILG. I expect that this will be affected in some way by COVID-19 and I will provide an update on any more recent business plans that become available in my Supplementary Report.

## Stress and scenario testing

### CLL

- 7.17 As noted earlier, the Solvency II Pillar 1 solvency ratio of CLL is very sensitive to falls in interest rates. However, this is largely mitigated once the TMTP has been recalculated, although there will be a delay in the time required to receive an approval from the PRA. CLL's solvency ratio is also sensitive to improvements in longevity assumptions, given the large volume of annuities in-force, which is less affected by a re-calculation of the TMTP. CLL is also sensitive to the capital strain from the new business written, however, new business volumes can be adjusted if required over time, and capital made available from the GWL group to support such future new business as agreed.
- 7.18 In the 2019 ORSA, scenarios were performed over the five-year business planning period. This showed that under a number of the more extreme scenarios (for example, a scenario equivalent to the 9/11 terrorist attack), the solvency ratio is estimated to fall very close to or below CLL's target range over a five year period and before re-calculation of the TMTP. However, after re-calculating the TMTP, the solvency coverage is restored to be within the target range.
- 7.19 In the above scenarios, further management actions would be available to CLL as outlined further above.

## **ILA**

- 7.20 The scenario testing performed by ILA in their 2019 ORSA includes a “severe recession scenario”, which is of a similar nature as some of the extreme scenarios performed by CLL. This scenario shows that ILA are expected to remain within ILA’s target range throughout the five-year projection. This incorporates a reduction in dividends to zero throughout the period. Further management actions would be available to ILA as outlined further above.

## **ILA pension schemes**

- 7.21 ILA has three ring-fenced defined benefit pension schemes, of which the total assets are €1,386 million as at 31 December 2019 (99% of which relates to a single scheme). The combined surplus of the schemes is €134.5 million as at 31 December 2019 and €172.6 million as at 31 March 2020 and there is additional regulatory capital held in the ILA non-profit fund of €77.1 million as at 31 December 2019 to cushion against adverse experience. I therefore do not consider that the ILA pension schemes will have a material adverse impact on the security of the Transferring Policyholders, particularly given the high solvency coverage ratio of ILA overall.

## **ILA with-profit funds**

- 7.22 ILA contains two ring-fenced with-profit funds which, in extreme circumstances, may require capital support from the ILA non-profit fund on an informal basis. The with-profit funds are well capitalised with a high surplus above guaranteed benefits and capital requirements. I therefore consider the risk of capital support being required a remote possibility and one that would not affect the security of the Transferring Policyholders.

## **Financial Services Compensation Scheme**

- 7.23 As described in paragraphs 10.32 to 10.36 below I have taken into account the loss of the FSCS protection from which the Transferring Policyholders currently benefit. In my opinion, having certainty that the Transferring Policies can continue to be serviced lawfully after Brexit is fundamentally important, and will be of considerable importance to the Transferring Policyholders. The loss of any FSCS protection is a consequence of achieving this certainty. In addition, I have considered that the FSCS only provides protection to covered policyholders following an insolvency or default event of an insurer. Given that ILA is, and will continue to be, well capitalised and will continue to be required to comply with the Solvency II Directive in EU law, the likelihood of default or insolvency of ILA is, in my opinion, remote. I have also considered that ILA believes it would be disproportionately expensive and onerous to either maintain its existing, or establish a new, UK branch in order to service the Transferring Policyholders, particularly as ILA will not have any ongoing business with UK policyholders and the regulatory landscape will be much more onerous for a “third country” entity once the UK has exited the European Union. In conclusion, I am satisfied that the loss of the perceived benefit of the FSCS protection as a result of the Proposed Transfer is sufficiently low, so that the Transferring Policyholders are not being materially adversely affected by the loss of the FSCS protection.

## **Conclusion**

- 7.24 In conclusion, I am satisfied that:

- After implementation of the Proposed Scheme, the financial strength of ILA, as measured by the solvency coverage ratio on the Solvency II Pillar 1 basis, to which both companies manage their capital, is expected to be no lower than that of CLL.
- The capital policies of ILA and CLL are of a similar strength and the risk management frameworks and processes of both firms are very similar, therefore the security offered to the Transferring Policyholders will not change materially as a result of the Proposed Scheme. The Solvency II Pillar 1 solvency ratio of ILA is expected to be well above its target range following the implementation of the Proposed Scheme.
- The Transferring Policyholders are not being materially adversely affected by the loss of the FSCS protection.

7.25 After taking into consideration the above factors, I consider that after implementation of the Proposed Scheme, at least as high a level of security will be provided to the Transferring Policyholders compared to the situation where the Proposed Scheme is not implemented.

### The profile of risks to which the transferring CLL policies are exposed

- 7.26 CLL and ILA each have differing risk profiles containing a diverse range of risks, reflecting the different business they have sold. CLL is predominantly exposed to risks arising from its large annuity book of business, as well as Group insurance and unit linked contracts, leading to high credit risk, market risk and longevity risk capital. ILA, on the other hand, is largely exposed to risks on its significant unit linked individual and group life and pension business, which mainly relate to market risk and lapse risk.
- 7.27 Given that ILA holds capital to meet these risks, in line with their Capital Management Policy, and their financial strength is high (as outlined above), I do not consider that the change in risk profile to which the Transferring Policyholders will be exposed following the implementation of the Proposed Scheme will affect the security of their benefits.

### Governance and management of the transferring CLL policies

- 7.28 Both ILA and CLL have a similar governance structure in which the Board of Directors of each entity is responsible for the governance and oversight of all operations and risks. Both firms are currently required to comply with the Solvency II rules on systems of governance and have a similar Enterprise Risk Management Framework in place involving the three lines of defence.
- 7.29 ILA is a “high-impact” rated entity under the CBI’s risk-based framework for the supervision of regulated firms, known as PRISM (Probability Risk and Impact System). They must comply with the CBI’s Corporate Governance Requirements for Insurance Undertakings 2015, which include requirements in relation to the composition of the Board and its Committees. ILA annually reviews the performance of its governance committees and commissions independent reviews of governance periodically. There is an independent evaluation of the overall performance of the Board and individual directors every three years.
- 7.30 ILA already has close to €4 billion of annuities (gross of reinsurance) in force and has the necessary expertise in managing these. Of the €4 billion of annuities, €1,152 million is reinsured in order to reduce ILA’s exposure to adverse longevity experience, however, ILA has no plans to reinsure the liabilities associated with the Transferring Policies.

- 7.31 I have seen ILA's Investment Policy in relation to their existing non-linked business, which shows that the assets are managed prudently, with restrictions on different asset types and criteria on the credit quality of the assets backing the liabilities, which would seem to be at least as prudent than the restrictions which CLL applies in its Investment Policy in respect of its own non-linked business. The non-linked investments within ILA are outsourced to another group company Canada Life Asset Management Limited. ILA have a Board-approved Outsourcing Policy that sets out the principles and requirements for managing outsourcing arrangements and their risks.
- 7.32 I am satisfied that the implementation of the Proposed Scheme will not materially affect the standards of governance and management applicable to the Transferring Business.

### **The administration and service standards applied to the transferring CLL policies**

- 7.33 As described in Section 6 of this report, CLL currently has two service agreements in place with other group companies in relation to the Transferring Business. It is intended that the Proposed Scheme will transfer these agreements automatically (unchanged) to ILA from CLL on the Effective Date. I have been informed that following the transfer no changes will be made to the agreements by ILA. In addition, I have been informed by the management of CLL and ILA that there is no plan to make any change in the way the administration is operated for the Transferring Business, for example, with regards to the personnel responsible for conducting policy administration or the way in which the policyholders can make contact with ILA.
- 7.34 There will be no changes to the terms and conditions of the Transferring Policies as a result of the implementation of the Proposed Scheme, except for the fact that they will become policies of ILA rather than CLL. There will also be no changes to the benefits of the Transferring Policies.
- 7.35 Given the above, I am satisfied that there will be no reduction to service levels or other changes to the administration that could materially impact the Transferring Policyholders as a result of the Proposed Scheme.

### **The reasonable expectations of the transferring CLL policyholders**

- 7.36 As the Transferring Policies are all non-profit, non-linked, in-payment annuities, the reasonable expectations of the policyholders will principally relate to the continued fulfilment of the unchanged contractual terms of their policies, with regard to receipt of their annuity payments and no changes in the standards of servicing of the policy.
- 7.37 I am satisfied that the reasonable expectations of the Transferring Policyholders will continue to be met to the same levels following implementation of the Proposed Scheme.

### **Conclusion for the transferring CLL policies**

- 7.38 I am satisfied that implementation of the Proposed Scheme will not have a material effect on:
- The security of benefits under the transferring CLL policies;

- The service standards and governance applicable to the transferring CLL policies; or
- The reasonable expectations of the transferring CLL policyholders.



## Section 8: The effect of the Proposed Scheme on the non-transferring CLL policies

### Introduction

8.1 In this section I consider the effect of the implementation of the Proposed Scheme on the non-transferring CLL policies. The key points I have considered are:

- The financial resources available to provide security for the non-transferring policyholders after implementation of the Proposed Scheme, compared to those currently available.
- Any change to the profile of risks to which the non-transferring policyholders are exposed as a result of the transfer.
- The effect of the implementation of the Proposed Scheme on the reasonable expectations of the non-transferring policyholders, including benefit expectations, service standards, management and governance.

8.2 I have considered each of these further in the sections below.

8.3 The non-transferring CLL policies all reside in the only non-profit fund of CLL. There are no with-profit funds remaining in CLL, following the Part VII transfer of legacy business to Scottish Friendly in 2019.

### The financial resources available to provide security of benefits

8.4 As described earlier in this report, the Transferring Business reflects an immaterial part of the total liabilities in CLL. The Transferring Business represents 0.4% of CLL's Insurance liabilities (net of reinsurance) as at 31 December 2019.

8.5 Table 8.1 below shows the pre-Scheme financial strength of CLL and the post-Scheme financial strength of CLL as at 31 December 2019 on the Solvency II Pillar 1 basis (after allowing for the MGMA transfer to CLL in both):

**Table 8.1: CLL solvency pre and post-Scheme as at 31 December 2019**

Solvency II Pillar 1 31 December 2019	CLL (pro-forma, including MGMA) pre-Scheme (£m)	CLL post-Scheme (£m)
Own Funds	4,240	4,230
SCR	2,710	2,699
<b>Excess resources over SCR</b>	<b>1,530</b>	<b>1,531</b>
<b>Solvency coverage ratio</b>	<b>156%</b>	<b>157%</b>



- 8.6 The figures in Table 8.1 show that there is expected to be an immaterial impact on the solvency ratio of CLL post implementation of the Proposed Scheme, with the solvency ratio increasing by 1% to 157%. I note that the CLL post-Scheme figures in the table above assume a payment of £79 million from CLL to ILA upon the transfer of the liabilities, which has yet to be agreed between the parties. I will provide an update on this financial information in my Supplementary Report, however, if the payment (in excess of assets backing insurance liabilities required by ILA) was higher or lower by £10 million, this would result in an immaterial change to the solvency coverage ratio of less than +/- 1%. Given the low size of the Transferring Business relative to the remaining business of CLL and the immaterial impact of the Proposed Scheme on the Solvency II Pillar 1 basis, I have not considered the impact of the Proposed Scheme on the Solvency II Pillar 2 basis, LICAT basis or on any financial projections from 31 December 2019 for CLL.
- 8.7 Since 31 December 2019 there have been significant changes in the economic and insurance environment as a result of COVID-19. I comment on the preliminary indications of the likely high-level effects of this global pandemic on the financial position of both firms in more detail in Section 10 of this report, although it is still too early to have fully worked through all the financial impacts in this fast-changing situation. Consequently I expect to provide more detailed information on how COVID-19 has affected the financial position of both firms in my Supplementary Report.
- 8.8 Given the low size of the Transferring Business relative to the remaining business of CLL, the implementation of the Proposed Scheme will not have any impact on the capital management policy of CLL.
- 8.9 Given the above, I am satisfied that the implementation of the Proposed Scheme will not lead to a material change in the benefit security of the non-transferring policies in CLL.

### **The profile of risks to which the non-transferring policies in CLL are exposed**

- 8.10 Given the low level of size of the Transferring Business relative to the remaining business of CLL, it will have very limited impact on the risk exposure of the remaining policyholders in CLL.

### **The governance, management and service standards applicable to the non-transferring policies in CLL**

- 8.11 As a result of the Proposed Scheme, I am satisfied that there will be no change to the operations of CLL in relation to the remaining policies. In particular,
- There will be no change to how CLL is governed and managed or to its business plans.
  - There will be no changes to the terms and conditions or benefits of the remaining policies.
  - There will be no changes to the administration or investment services in relation to the remaining policies.
  - There will be no changes to the service levels of CLL as a result of the Proposed Scheme.

## **The reasonable benefit expectations of the non-transferring policyholders in CLL**

- 8.12 The non-transferring policyholders in CLL are all non-profit policies and their expectations will principally relate to the continued fulfilment of the unchanged contractual terms of their policies, the management and governance of their policies, and the servicing of their policy. Following implementation of the Proposed Scheme, I understand from the management of CLL that there will be no change to any of these items.
- 8.13 I can therefore confirm that I am satisfied that the reasonable expectations of the non-transferring CLL policyholders will continue to be met to the same levels following implementation of the Proposed Scheme. I am also satisfied that the Proposed Scheme is equitable to all classes and generations of the CLL policyholders.

## Section 9: The effect of the implementation of the Proposed Scheme on the existing ILA policies

### Introduction

- 9.1 In this section I consider the effect of the implementation of the Proposed Scheme on the existing ILA policies. The existing ILA policies can be broken down into policies in the following funds:
- ILA non-profit fund
  - ILA ring fenced with-profit fund 1
  - ILA ring fenced with-profit fund 2
- 9.2 The key points I have considered in respect of the above groups of policyholders are:
- The financial resources available to provide security for the existing ILA policyholders after implementation of the Proposed Scheme, compared to those currently available.
  - Any change to the profile of risks to which the ILA policyholders are exposed as a result of the transfer.
  - The effect of the implementation of the Proposed Scheme on the reasonable expectations of the existing ILA policyholders, including benefit expectations, service standards, management and governance.
- 9.3 I have considered each of these further in the sections below.

### The financial resources available to provide security of benefits

- 9.4 As described earlier in this report, the Transferring Business reflects only a small part of the total liabilities in ILA. The Transferring Business represents 0.2% of ILA's Insurance liabilities (net of reinsurance) as at 31 December 2019. This equates to approximately €85 million as at 31 December 2019 gross and net of reinsurance (as these policies will not be reinsured).
- 9.5 Table 9.1 below shows the pre-Scheme financial strength of ILA and a pro-forma of the post-scheme financial strength of ILA as at 31 December 2019 on the Solvency II Pillar 1 basis:

**Table 9.1: ILA solvency pre and post-Scheme as at 31 December 2019**

<b>Solvency II Pillar 1 31 December 2019</b>	<b>ILA pre-Scheme (€m)</b>	<b>ILA post-Scheme (€m)</b>
Own Funds	1,934	1,939
SCR	1,145	1,151
<b>Excess resources over SCR</b>	<b>789</b>	<b>788</b>
<b>Solvency coverage ratio</b>	<b>169%</b>	<b>168%</b>

- 9.6 The figures in Table 9.1 show that there is expected to be an immaterial impact on the Solvency II Pillar 1 solvency ratio of ILA post implementation of the Proposed Scheme, with the solvency ratio expected to reduce by 1% to 168%. Given the low size of the Transferring Business relative to the existing business of ILA and the immaterial impact of the Proposed Scheme on the Solvency II Pillar 1 basis, I have not considered the impact of the Proposed Scheme on the Solvency II Pillar 2 basis, LICAT basis or on any financial projections from 31 December 2019 for ILA.
- 9.7 The ILA pro-forma post-Scheme figures in the table above assume a £79 million payment from CLL to ILA upon the transfer of the liabilities, which has yet to be agreed between the parties. I will provide an update on this in my Supplementary Report, however, if the payment (in excess of assets backing insurance liabilities required by ILA) was higher or lower by £10 million, this would result in only a small change to the solvency coverage ratio of ILA of around +/- 1%.
- 9.8 Since 31 December 2019 there have been significant changes in the economic and insurance environment as a result of COVID-19. I comment on the preliminary indications of the likely high-level effects of this global pandemic on the financial position of both firms in more detail in Section 10 of this report, although it is still too early to have fully worked through all the financial impacts in this fast-changing situation. Consequently I expect to provide more detailed information on how COVID-19 has affected the financial position of both firms in my Supplementary Report.
- 9.9 Under the Proposed Scheme, no assets or liabilities will be transferred into or out of the two ILA with-profit funds. Therefore, the only potential change in the exposure of these funds, as a result of the Proposed Scheme, is due to changes in the financial strength of the ILA non-profit fund, potentially limiting the availability of capital support to the with-profit funds. The solvency coverage ratio of the ILA non-profit fund would slightly reduce as a result of the Proposed Scheme, in a similar way as to ILA overall, as shown in Table 9.1. There will therefore be very limited impact of the Proposed Scheme on the ability of the ILA non-profit fund to be able to support the ILA with-profit funds if required.
- 9.10 Given the low size of the Transferring Business relative to the existing business of ILA, the implementation of the Proposed Scheme will not have any impact on the Capital management policy of ILA, including in relation to the with-profit funds.
- 9.11 I am therefore satisfied that the implementation of the Proposed Scheme will not lead to a material change in the benefit security of the existing policies in ILA, including those in the ring-fenced with-profit funds.

## The profile of risks to which the existing policies in ILA are exposed

- 9.12 Given the low size of the Transferring Business relative to the existing business of ILA, the Proposed Scheme will have very limited impact on the risk exposure of the existing non-profit policyholders and with-profit policyholders in ILA.

## The governance, management and service standards applicable to the existing policies in ILA

- 9.13 As a result of the Proposed Scheme, I am satisfied that there will be no change to the operations of ILA in relation to the existing policies. In particular,
- There will be no change to how ILA is governed and managed or to its business plans.
  - The implementation of the Proposed Scheme will not lead to any changes to the management of the with-profit business.
  - There will be no changes to the terms and conditions or benefits of the existing policies.
  - There will be no changes to the administration or investment services in relation to the existing policies (both non-profit and with-profit policyholders).
- 9.14 There will be no changes to the service levels of the existing policyholders in ILA as a result of the Proposed Scheme.

## The reasonable benefit expectations of the existing policyholders in ILA

- 9.15 The expectations of the existing non-profit policyholders in ILA principally relate to the continued fulfilment of the unchanged contractual terms of their policies, the management and governance of their policies, and the servicing of their policy. For with-profit policyholders, they will additionally have reasonable expectations of future regular and terminal bonuses, as well as their share of the surplus in the relevant with-profit fund.
- 9.16 Following implementation of the Proposed Scheme, there will be no material change to any of the above items.
- 9.17 I can therefore confirm that I am satisfied that the reasonable expectations of the existing policyholders in ILA will continue to be met to the same levels following implementation of the Proposed Scheme. I am also satisfied that the Proposed Scheme is equitable to all classes and generations of the ILA policyholders.

## Section 10: Other considerations arising from the Proposed Scheme

### The approach to communication with policyholders

- 10.1 Regulations made under FSMA require a communication regarding the proposed transfer to be sent to every policyholder of the parties under the Proposed Scheme, including information set out in paragraph 10.5 below. However, this requirement may be waived at the discretion of the Court, which will give consideration to issues such as the practicality and costs of sending notices against the likely benefits for policyholders of receiving such communications. In order to comply with SUP 18.2.46G, the companies would be expected to notify the policyholders, or interested persons, at least six weeks before the date of the Court hearing at which the application to sanction the Proposed Scheme will be heard.
- 10.2 Regulations require that a legal notice in a form approved by the PRA is published in the London, Edinburgh and Belfast Gazettes, as well as two national newspapers in the relevant EEA states in which Transferring Policyholders are resident. As well as the London, Edinburgh and Belfast Gazettes, CLL and ILA have opted to publish legal notices in *Suddeutsche Zeitung*, *Frankfurter Allgemeine Zeitung*, *The Irish Times* and *The Irish Independent* plus *The Daily Mail* and *the Times* and will make information available on the CLL website. On materiality grounds, the court will be asked to waive the requirement to publish legal notices in Austria, France or Spain given those countries were the state of commitment for only four policyholders in total.
- 10.3 Policyholders and other interested parties will be able to obtain further information from the CLL website. This will contain documents regarding the Proposed Scheme, including the full Scheme document, this report, a summary of the terms of the Proposed Scheme, a summary of this report (written by me) and the CLL and ILA Chief Actuary reports. In addition, the CLL website will include a sample copy of the Policyholder Letter being sent to Transferring Policyholders.

### Notifications to Transferring Policyholders

- 10.4 CLL has proposed a communication plan, including the CLL policyholder pack, to provide notification of the proposed transfer to all Transferring Policyholders.
- 10.5 It is proposed that each Transferring Policyholder will receive a policyholder pack that comprises a covering Policyholder Letter and a Policyholder Guide, which will include amongst other things:
- A summary of the terms of the Proposed Scheme;
  - A summary of the report by the Independent Expert; and
  - A questions and answers section.
- 10.6 I have reviewed and considered the contents of advanced drafts of the Policyholder Guide and the accompanying letter (the "Policyholder Letter") which are intended to be sent to all

transferring policyholders of CLL, subject to the expected waivers discussed in paragraph 10.9 below. I consider that the most recent drafts I have reviewed provide a satisfactory level of information on the Proposed Scheme and a clear explanation of the consequences for Transferring Policyholders.

### ***Transferring Policyholders that cannot be traced***

10.7 CLL has reviewed its policyholder registers and has identified three untraceable Transferring Policyholders whose policies were originally written by ELAS through its Irish branch, which are referred to as “gone-away” policies. There are no “gone-away” policies which were originally written by ELAS through its German branch. These have been identified as untraceable “gone-away” policies when a letter that has been sent during a policyholder communication exercise is returned undelivered. The three “gone-away” Transferring Policyholders represents approximately 0.4% of the Transferring Policyholders.

10.8 CLL undertakes industry-standard methods to try to trace the policyholder, including using services provided by Deutsche Post and Supercheck in Germany and by the Department of Social Protection in Ireland. The steps taken to trace the three “gone-away” policyholders so far are as follows:

- Each policyholder’s file was checked to see if any other address details were held (none were);
- The website “rip.ie” was checked to see if a death was registered for each of the three policyholders – none have been identified on this website; and
- Annuity payments to the three policyholders were suspended (one was suspended in June 2018 and the other two in July 2019). No policyholders have made contact since payment was suspended. The decision to suspend payments in the above circumstances is in line with the way in which CLL deals with “gone-aways” in its UK annuity business.

I understand that the services provided by the Department of Social Protection will be used shortly by ILA to try to trace the three “gone-away” policyholders. If ILA manage to establish an up-to-date address over the coming months then the policyholder communications in relation to the proposed transfer will be sent to these three policyholders.

### ***Notification waivers***

10.9 CLL expects to request waivers from notifying the following groups:

- Contingent beneficiaries of a Transferring Policy (i.e. where the benefits of the policy revert to someone else on death of the policyholder);
- Personal representatives or executors of deceased policyholders; and
- Three “gone-away” Transferring Policyholders, which represents approximately 0.4% of the Transferring Policyholders.

### ***Non-notification of policyholders of CLL that are not Transferring Policyholders***

- 10.10 CLL intends to seek a waiver from the requirement to notify all other existing CLL policyholders that are not Transferring Policyholders on the grounds that they will not be materially affected by the Proposed Scheme. CLL management contends, and I concur with this view, that individual notifications would be of limited benefit to such CLL policyholders while giving rise to significant cost for CLL's shareholders.
- 10.11 I note that the financial impact of the transfer on CLL is immaterial with no change in the overall SCR coverage ratio. I note also that the number of Transferring Policyholders, and the value of liabilities attributable to them, are both extremely small (less than 1%) by comparison with the remainder of CLL's business.
- 10.12 I am satisfied that the proposal to seek a waiver from notifying these groups is reasonable.

### ***Non-notification of existing policyholders of ILA***

- 10.13 ILA intends to seek a waiver from the requirement to notify all existing ILA policyholders on the grounds that they will not be materially affected by the Proposed Scheme. ILA management contends, and I concur with this view, that individual notifications would be of limited benefit to such ILA policyholders while giving rise to significant cost for ILA's shareholders.
- 10.14 I note that the financial impact of the transfer on ILA is small, representing a 0.3% increase in Own Funds and a 1% decrease in the SCR coverage ratio.
- 10.15 I am satisfied that the proposal to seek a waiver from notifying these groups is reasonable.

### ***Overall conclusion on the approach to communication and policyholders***

- 10.16 I consider these to be valid reasons and am satisfied that the proposed approach to communication with policyholders is fair and reasonable.

### ***The United Kingdom's exit from the European Union***

- 10.17 As described in Section 6 above, the main purpose for the Proposed Scheme is for CLL and the wider GWL Group to ensure that the legal obligations it has to policyholders who purchased their policy when they were resident in other EEA states outside of the UK can continue to be met following Brexit.
- 10.18 On 31 January 2020, the UK formally exited the European Union and entered a transition period expected to last until the end of 2020. The exact implications continue to remain uncertain until formal negotiations are concluded between the UK and European Union.
- 10.19 CLL believes that after expiry of the transition period, it is likely to lose its legal rights to service the cross border policies issued to policyholders who were habitually resident at the time of purchase in the European Union but outside the UK (including the ability to pay claims), due to the loss of the "passport" rights applicable to member states of the European Union. The Board of CLL therefore considers that the transfer of the relevant policies pursuant to the Proposed Scheme is necessary to ensure that the GWL Group can continue to meet its legal and regulatory obligations in relation to the Transferring Business on an ongoing basis.



## Prudential-Rothsay case

10.20 On 16 August 2019, Mr Justice Snowden declined to sanction a scheme to transfer a large number of annuities from The Prudential Assurance Company Limited to Rothsay Life plc. I understand that this decision is subject to appeal, but at the time of writing such appeal has yet to be heard. I have considered whether the reasons given for this decision are relevant to the Proposed Scheme, and have concluded that they are not. I summarise below the main features of the Prudential/Rothsay scheme which appear to have influenced Mr Justice Snowden's decision, with my views of the applicability of each such feature to the Proposed Scheme in bold/italics.

- The transferring business was annuity business, and policyholders have no option to cancel their policies or switch to another provider. ***Mr Justice Snowden stated in his judgement that this did not mean that all schemes to transfer annuities should be rejected, but that each should be considered on its merits.***
- Prudential is a long-established company with a strong brand, whereas Rothsay has been in existence for 12 years and has no retail brand. ***Both CLL and ILA have been in existence for many years, and each entity has a strong brand in their respective markets.***
- In the view of Mr Justice Snowden, the fact that Prudential Assurance Company's current parent shares the Prudential name and has significant financial resources at its disposal means that it is more likely to provide additional capital to its subsidiary if needed than is the case with Rothsay's parent, which has limited resources of its own and three main shareholders which could more easily distance themselves from Rothsay. ***Since CLL and ILA are both part of the same GWL Group, this concern does not apply to the Proposed Scheme.***
- The stated purpose of the sale of some of Prudential's annuities to Rothsay was purely commercial (enabling Prudential to release solvency capital) and most of the benefit had already been achieved via the reinsurance arrangement, which could remain in place if the transfer was not sanctioned. ***The purpose of the Proposed Scheme is to ensure that the legal obligations to continue paying benefits to, and servicing, Transferring Policyholders can continue to be met following Brexit.***

## The costs of the Proposed Scheme

10.21 CLL will bear the entire costs of the Proposed Scheme, including costs such as the costs of policyholder communications, my Independent Expert fees, Court fees and Counsel's fees.

10.22 I am satisfied that this approach to meeting the costs associate with the Proposed Scheme is fair and reasonable.

## COVID-19

10.23 In the course of preparing this Scheme Report, it has become evident that the coronavirus outbreak named as COVID-19, a rapidly developing global pandemic, is having significant short-term effects on economic activity and creating extensive social disruption, both within the UK and globally. Longer term socio-economic implications and the impact on both liabilities

and assets remain uncertain. The situation is fast-moving and changing daily, leading to a high degree of uncertainty about the eventual type and scale of impacts and financial losses that may emerge.

- 10.24 I have been provided with some preliminary analyses of the anticipated impact of COVID-19 on the financial position of both CLL and ILA, which have been provided to their respective Boards. These show that, based on known market effects to the end of Q1 2020, and making allowance for the currently estimated demographic impacts on each firm, the solvency positions for both firms are expected to be within risk appetite. Some scenario analysis has also been undertaken, with further work currently underway, which is recognised as being preliminary as more information becomes available and the longer-term financial and demographic impacts are better understood.
- 10.25 I will further consider the expected effects of COVID-19 on the financial positions of both CLL and ILA in my Supplementary Report, as well as any resulting impacts on my conclusions.

### The effect of the Proposed Scheme on previous schemes

- 10.26 The external legal advisers to CLL (Herbert Smith Freehills) have reviewed relevant previous CLL Part VII schemes, namely the scheme between ELAS and CLL dated 8 February 2016, and this review has confirmed that there are no enduring provisions in that scheme that would be affected by this Proposed Scheme and which I would need to consider in the context of this Proposed Scheme.

### Other creditors

- 10.27 CLL and ILA have informed me that there are no third-party bondholders or parties to securitisation arrangements or any other external creditors of either company whose interests would be affected by the implementation of the Proposed Scheme.

### The future operation of the Proposed Scheme

- 10.28 If the Proposed Scheme is approved by the Court (and subject to any subsequent amendment of the Proposed Scheme, as considered below), the Directors of CLL and ILA are committed to implementing the Proposed Scheme as set out in the Scheme document (and reflected in this report) in according with their fiduciary responsibilities under UK and Irish company law.
- 10.29 At any time after the Court's sanction of the Proposed Scheme, CLL and ILA must apply to the Court for sanction of any amendments to it, except where the amendment is considered to be minor, technical or required by law. In such cases the companies must notify the PRA and FCA.
- 10.30 Following implementation of the Proposed Scheme, CLL will continue to operate within the UK regulatory framework for insurance companies, overseen by the PRA and the FCA, and ILA will continue to operate within the Irish regulatory framework for insurance companies, overseen by the CBI. This provides considerable protection for the interests of policyholders, without the need for specific additional obligations under the Proposed Scheme.
- 10.31 In my opinion there are reasonable safeguards in place to ensure that, if approved by the Court, the Proposed Scheme will be operated as presented to the Court.

## Financial Services Compensation Scheme ("FSCS")

- 10.32 Currently policyholders of CLL, including the Transferring Policyholders, are covered by the FSCS. The FSCS is a statutory "fund of last resort" which compensates customers in the event of the insolvency or default of insurers authorised in the UK or EEA insurers with a UK branch. Insurance protection exists for private policyholders and small businesses (those with an annual turnover of less than £1,000,000) when an insurer is unable to meet its liabilities fully. For long-term insurance policies, the FSCS will ensure 100% of any successful eligible claim is paid. The policyholder protection provided under the FSCS applies to direct policyholders of the insurer only. The FSCS is funded by levies on those firms authorised by the UK Regulators. For long-term insurance business, there is no equivalent to the FSCS in Ireland.
- 10.33 The Transferring Business is currently covered by the FSCS. After the Proposed Scheme is implemented the Transferring Policyholders will hold policies with ILA, which is an Irish insurance company, and (given there is no equivalent to the FSCS providing such protection in Ireland) will therefore lose entitlement to this form of protection. The question that I must therefore address is whether this is a material loss in the context of the Proposed Scheme.
- 10.34 The purpose of the Proposed Scheme is to effect the transfer of the Transferring Business from CLL to ILA, in order to enable the continued servicing (e.g. paying annuity payments) of the Transferring Business, regardless of the outcome of the Brexit process. In my opinion, having certainty that the Transferring Policies can continue to be serviced lawfully after Brexit is fundamentally important, and will be of considerable importance to the Transferring Policyholders. The loss of any FSCS protection is a consequence of achieving this certainty. In addition, I have considered that the FSCS only provides protection to covered policyholders following an insolvency or default event of an insurer. Given that ILA is, and will continue to be, well capitalised and will continue to be required to comply with the Solvency II Directive in EU law, the likelihood of default or insolvency of ILA is, in my opinion, remote.
- 10.35 I have also considered the possibility of the Transferring Business moving into the existing UK branch of ILA (as described in paragraph 5.38). However, ILA does not intend to maintain this branch and neither does ILA intend to establish a separate long-term UK branch for the Transferred Business, on the basis that it would be disproportionate and would place onerous obligations on ILA as the branch will have no ongoing business with UK policyholders following maturity of the remaining legacy policies. In addition, the regulatory landscape for an Irish (or any other EEA) entity wishing to establish or maintain a UK branch will be much more onerous after 31 December 2020 than before, as ILA would be treated as a "third country" entity following expiry of the "implementation period" in relation to the UK's exit from the European Union. ILA considers that maintaining a branch in the UK, to service Irish and German policies for the purpose of the Transferred Business, would be disproportionately expensive and onerous given the small number of policies that are the subject of the transfer and the other safeguards built into the regulatory regime.
- 10.36 Having considered all of the above, I am satisfied that the loss of the perceived benefit of the FSCS protection as a result of the Proposed Transfer is sufficiently low, so that the Transferring Policyholders are not being materially adversely affected by the loss of the FSCS protection.

## Financial Ombudsman Service / Financial Services and Pensions Ombudsman

- 10.37 Currently policyholders of CLL, including the Transferring Policyholders, can contact the UK Financial Ombudsman Services (“FOS”), while policyholders of ILA can contact the Financial Services and Pensions Ombudsman (“FSPO”) in Ireland, if there is a dispute regarding their policy. After the implementation of the Proposed Scheme, the Transferring Policyholders of CLL will lose access to the FOS, unless the complaint relates to activities carried out by CLL prior to the Effective Date. However, as policyholders of ILA, they will then be able to contact the FSPO if the complaint relates to the conduct of ILA after the Effective Date.
- 10.38 The FOS and the FSPO fulfil similar roles in the UK and Ireland respectively. The main difference is that the decisions made by the FSPO are legally binding and can only be appealed to the High Court in Ireland on points of law, whilst decisions made by the FOS are only final and binding on the business if they are accepted by the complainant. There is nothing, however, to indicate that the outcome of a complaint will be different for a policyholder having to raise it with the FSPO, rather than the FOS, notwithstanding the legal differences between the two.
- 10.39 The FSPO and the FOS operate on similar principles governing their independence and impartiality, their clarity of scope and powers, accessibility, effectiveness, fairness, transparency and accountability. For the FSPO, the compensation limit for complaints relating to financial service providers is €52,000 per annum, where the subject of the complaint is an annuity, and €500,000 in respect of all other complaints. For the FOS, the following limits apply:
- £355,000 for complaints referred on or after 1 April 2020 about acts or omissions by firms on or after 1 April 2019;
  - £350,000 for complaints referred between 1 April 2019 and 31 March 2020 about acts or omissions by firms on or after 1 April 2019;
  - £160,000 for complaints about acts or omissions by firms before 1 April 2019 and which are referred after that date; and
  - £150,000 for any complaints referred before 1 April 2019.
- 10.40 There are also some differences in the time limits in which complaints must be made to the FOS or FSPO. Consent from the relevant firm is generally required in order for the FOS to investigate complaints that are referred more than six months after the business sends the consumer a final response to the complaint. The same condition applies for complaints that are made more than six years after the event in question (or three years from when the consumer could reasonably have known they had cause to complain). The FOS can also consider a complaint outside the six month and six year time limits if it decides that the failure to comply was as a result of exceptional circumstances (for example, as a result of incapacity).
- 10.41 For the FSPO, where the complaint does not relate to a long-term financial service, the complaint must be made to the Ombudsman no more than six years from the date of conduct giving rise to the complaint. However, for a long-term financial service (which a life annuity

may fall under), the FSPO will consider complaints within whichever of the following periods is the last to expire:

- six years from the date of conduct giving rise to the complaint;
- three years from the earlier of the date on which the person making the complaint became aware, or ought reasonably to have become aware, of the conduct giving rise to the complaint;
- such longer period as the Ombudsman may allow where it appears to him or her that there are reasonable grounds for requiring a longer period and that it would be just and equitable, in all the circumstances, to so extend the period.

10.42 The decision to investigate complaints relating to events that occurred over six years previously may lie with the relevant firm under the UK regime and with the FSPO under the Irish regime. Therefore, in this respect the Transferring Policyholders would have better protection under the FSPO than they currently do under FOS, as the decision to investigate such complaints is made independently by the Ombudsman service rather than by the relevant firm.

10.43 Given that the Transferring Policyholders are very likely to be classed as having a long-term financial service post implementation of the Proposed Scheme, both the FOS and FSPO will conceivably consider complaints made by these policyholders more than six years from the date of conduct giving rise to the complaint.

10.44 Overall therefore, I am satisfied the Transferring Policyholders will not be materially adversely affected as a result of the change in ombudsman jurisdiction for events occurring after the implementation of the Proposed Scheme.

## Tax

### *Policyholder tax*

10.45 I am not an expert in tax matters and, therefore, in forming my opinion on the impact of policyholder tax, I have relied on documents produced by CLL's and ILA's in-house tax experts based on the tax advice the companies have received from their external tax advisers. I have reviewed this information to ensure it is in line with my expectations given my understanding of the structure and business of CLL and ILA before and after the Proposed Scheme. I have also discussed the various tax issues with the CLL tax director.

10.46 I do not anticipate that there will be a change in policyholder taxation for the Transferring Policies, as the Proposed Scheme does not result in any changes to the terms and conditions of the Transferring Business.

10.47 Therefore, based on my analysis of advice currently available, I am satisfied that there will not be any change to any policyholder's tax liability as a result of the Proposed Scheme.

### Corporation tax

- 10.48 Profits on the Transferring Business are currently subject to UK corporation tax at a rate of 19%. After the Proposed Scheme, any profits on the Transferring Business will be subject to Irish corporation tax at a rate of 12.5%. The reduction in taxation rate applicable to potential future profits or losses arising as a result of the Proposed Scheme is expected to be immaterial and will not affect the Transferring Policies because these are non-profit policies. Similarly, any profit or loss arising on the sale and purchase of the Transferring Business is expected to result from arm's length pricing and, in any event, any tax arising from the transfer will not impact these policies as the Transferring Policies are non-profit.

### VAT

- 10.49 As the Transferring Policies are non-profit and policyholder benefits are fixed, any VAT impact of the Proposed Scheme will not impact these policies.

### Tax clearances

- 10.50 CLL and ILA have concluded that there is insufficient uncertainty in the corporate tax, VAT and policyholder tax outcomes arising from the Proposed Scheme and, as such, the tax clearance legislation in each relevant jurisdiction cannot be engaged on its terms. No tax clearances or confirmations from the relevant tax authorities are therefore being sought. Instead, external tax advice will be sought on the tax consequences and I will comment further on the status of this tax advice in my Supplementary Report.

### Conclusion

- 10.51 I am satisfied, based on the tax advice currently available, that the tax implications of the Proposed Scheme will not materially adversely affect the Transferring Policyholders because:
- There is no change to the policyholder's tax position; and
  - As the Transferring Policies are non-profit, there are no other tax impacts.

## Section 11: Conclusions

- 11.1 Due to the legal situation following the UK's exit from the European Union, it will become a legal necessity for CLL to transfer the Transferring Business to another insurance entity domiciled within a remaining EEA member state in order to ensure that the Transferring Policies can still legally be serviced, in particular to continue making annuity payments to the Transferring Policyholders. The Proposed Scheme has been prepared in order to meet this legal necessity.
- 11.2 I am satisfied that implementation of the Proposed Scheme will not have a material adverse effect on:
- The security of benefits of the policyholders of CLL and ILA, including the Transferring Policyholders;
  - The reasonable expectations of the policyholders of CLL and ILA, including the Transferring Policyholders; or
  - The service standards and governance applicable to the CLL and ILA policies, including the Transferring Policyholders.



Jeremy Nurse  
Senior Director

28 August 2020

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## Section 12: Reliances and limitations

12.1 In addition to the reliances and limitations shown in paragraphs 1.23 to 1.26 of this Scheme Report, the following reliances and limitations also apply.

### Reliances

12.2 In carrying out my review and producing this Scheme Report I have relied without independent verification upon the accuracy and completeness of the data and information provided to me, both in written and oral form. Where possible, I have reviewed the information provided for reasonableness and consistency with my knowledge of the insurance and reinsurance industry. I have also met or spoken with representatives of CLL and ILA to discuss in detail the information which they have provided to me in relation to the Proposed Scheme. I consider it is reasonable for me to rely on these individuals since they are PRA and FCA approved persons (or hold equivalent PCF roles approved by the CBI in Ireland) or are senior professionals employed by either CLL or ILA.

12.3 Reliance has been placed upon, but not limited to, the data and information detailed in Appendix B. In particular, I have relied upon the pro-forma balance sheet and capital impacts of the Proposed Scheme provided by CLL and ILA as at 31 December 2019, without independent verification.

12.4 I have obtained confirmation from each of CLL and ILA that, to the best of their knowledge and belief:

- All of the items of data and information which they have provided to me for the purposes of this Scheme Report are accurate and complete;
- There are no significant errors or omissions in the descriptions in this Scheme Report of the business of their respective company or of the Proposed Scheme; and
- There are no other material items of data and information which have not been provided to me regarding their respective companies and which are likely to be relevant to this Scheme Report.

12.5 Based on my review, I am satisfied that the data and information detailed in Appendix B represents an appropriate basis for the conclusions set out in this Scheme Report and I consider that it is reasonable for me to rely on this information. There is no information which I requested from CLL or ILA which has not been provided to me.

12.6 I met with the PRA and FCA at an early stage to establish whether there were matters or issues which they wanted me to consider in this Scheme Report, which I have taken into consideration.

### Limitations

12.7 No unreasonable limitations have been imposed on the scope of my work and the opinions in this Scheme Report about the Proposed Scheme are mine, based on the data and information



provided to me and the answers given to the questions I have raised. In my opinion, all significant matters that are relevant to policyholders' consideration of the Proposed Scheme have been considered in this Scheme Report.

12.8 This Scheme Report is based on:

- Audited financial information in respect of CLL and ILA as at 31 December 2019;
- Financial projections performed by CLL to the end of 2024, using the management accounts as at 31 December 2019 as the start point; and
- Financial projections performed by ILA to the end of 2023, using the management accounts as at 31 December 2018 as the start point and reflecting some experience in early 2019.

12.9 This Scheme Report does not take into account any developments after the dates noted above unless stated explicitly to the contrary in this Scheme Report.

12.10 I expect to produce a Supplementary Report in due course, based on the updated financial position of CLL and ILA, and revised financial projections, as at the latest quarter and/or year-end for which appropriate data is available given the proposed date of the transfer and the timing of the production of the Supplementary Report. Given the proposed timings of the Directions Hearing and the Final Hearing, I currently expect that my Supplementary Report will reflect the financial position of the firms as at 30 June 2020.

12.11 This Scheme Report must not be construed as legal, investment or tax advice.

12.12 Figures in all tables in this Scheme Report are subject to possible rounding differences.

12.13 This report was based on data available to Willis Towers Watson at, or prior to, 27 August 2020, and takes no account of developments after that date. Willis Towers Watson is under no obligation to update or correct inaccuracies which may become apparent in this report.

12.14 This report is subject to the terms and conditions, including limitation of liability, set out in our engagement letter of 6 March 2019.



## Appendix A: Statement of independence

Canada Life Limited ("CLL") has agreed to transfer a block of its non-profit annuity business to Irish Life Assurance plc ("ILA"). It is proposed that the business should be transferred to ILA under section 109 of the Financial Services and Markets Act 2000 by means of a scheme to be submitted to High Court in England and Wales for approval.

I have been appointed as the Independent Expert to report on the proposed transfer. My appointment has been approved by the PRA in consultation with the FCA.

I am a Senior Director in Willis Towers Watson ("WTW"), based in its UK Insurance Consulting and Technology business. The purpose of this statement is to disclose all connections between myself and CLL and ILA including their major shareholders and subsidiaries (together "the Companies"), and between WTW and the Companies.

I am not a shareholder in any of the Companies.

I do not hold any policies with any of the Companies, and am not a member of any group pension scheme or other group arrangement which holds a policy with any of the Companies.

It is important that our independence in undertaking this project is not prejudiced by our existing relationships with the Companies. Both CLL and ILA are member companies of Canada Life Group and the wider Great-West Life group. WTW has relationships with Great-West Life and with Canada Life Group, including both CLL and ILA, however we have undertaken a formal conflict check in accordance with our procedures and this has not identified any issues preventing us from acting as Independent Expert (IE) for the proposed transfer.

At the start of 2019, I provided consulting support to CLL by assisting the Line 2 Risk team in its internal review of the processes and methodologies undertaken by the Line 1 Bulk Annuity team, in particular providing input on approaches other firms use in the UK bulk annuity market, as well as providing a view to CLL's CEO on the performance of the Line 2 team during this review. In addition, I previously held the SIMF20 Chief Actuary role for MGM Advantage Life Limited (which was bought by Canada Life Group and which has now been fully transferred into CLL by way of a Part VII transfer approved by the Court in 2019) – my involvement with this work finished in April 2018. WTW and I consider that these assignments were sufficiently remote and/or ended sufficiently long ago and are sufficiently distinct from the business included in the proposed transfer that we do not consider this provides us or me with a conflict. Furthermore, earlier in 2020, I retired from full-time work at WTW and am now only undertaking any work for WTW on a part-time contract and only in relation to this IE work.

Separately, WTW currently performs the outsourced actuarial services for Canada Life Group, which requires aggregation of results produced for the Canada Life Group subsidiaries (including CLL and ILA) as inputs without full independent verification. These inputs are all signed-off at the individual subsidiary level by Canada Life staff. I, as IE in the proposed Part VII transfer (and the WTW team supporting me), only interacts with CLL and ILA staff and have no direct involvement with Canada Life Group nor with the outsourced actuarial services team within WTW. In addition, I and the team working with me on the proposed Part VII transfer will continue to have no involvement with the outsourced actuarial services team within WTW for the duration of this assignment as IE. We

Scheme Report of the Independent Expert of the Proposed Transfer of non-profit annuity business from Canada Life Limited to Irish Life Assurance plc under Part VII of the Financial Services and Markets Act 2000

therefore consider that this WTW involvement with Canada Life Group will not have any effect on the independence of my work.

WTW was engaged by CLL in 2019 to provide an Independent Person (IP) for CLL's Manulife Fund (MF). As part of this role, the IP was required to provide the CLL Board with feedback and comments on the appropriateness and completeness of an update to the MF run-off plan, as well as an independent assessment of compliance with the requirement to conduct the MF with-profits business in accordance with the Principles and Practices of Financial Management. Both Trevor Fannin and Rosie Anssari-Benam (respectively the Senior Peer Reviewer and the day-to-day Project Lead for the current IE work) provided support to the IP last year, but other than this neither has had any involvement within the last 5 years whatsoever with the legal entities involved in the potential transfer, nor with other companies in the Canada Life Group.

Jeremy Nurse

Fellow of the Institute and Faculty of Actuaries

28 August 2020

## Appendix B: Data relied upon

In addition to discussions (both orally and electronically) with CLL and ILA staff, I have relied upon the following principal documents in formulating my conclusions:

- Draft CLL Chief Actuary report on the Scheme (received 11 August 2020)
- Draft ILA Chief Actuary report on the Scheme (received 26 August 2020)
- Draft Scheme document (received on 11 August 2020)
- Draft Transferor and Transferee witness statements (received on 27 August 2020)
- CLL 2019 and 2018 Actuarial Function reports (received 12 May 2020 and 6 April 2020 respectively)
- ILA 2019 and 2018 Actuarial Function reports (received 6 May 2020 and 6 April 2020 respectively)
- CLL 2019 and 2018 annual report and accounts (received 4 May 2020)
- ILA 2019 and 2018 annual report and accounts (received 6 May 2020 and 6 April 2020 respectively)
- CLL 2019 and 2018 Solvency and Financial Condition Reports (received 4 May 2020 and 6 April 2020 respectively)
- ILA 2019 and 2018 Solvency and Financial Condition Reports (publicly available)
- CLL 2019 ORSA report (received on 6 April 2020)
- ILA 2019 ORSA report (including business plan) (received on 6 April 2020)
- ILA 2020 ORSA – Own Solvency Needs Assessment (received on 29 May 2020)
- CLL Capital management policy (received on 6 April 2020)
- CLL Management actions summary (received on 12 May 2020)
- CLL Risk appetite framework (received on 6 April 2020)
- CLL 2020 Business plan (received on 7 May 2020)
- ILA Capital management policy (received on 6 April 2020)
- ILA Recovery plan (received on 19 May 2020)
- ILA Risk appetite framework (received on 6 April 2020)
- ILA COVID-19 Board papers (received on 11 May 2020)
- CLL COVID-19 Board paper (received on 19 May 2020)
- Draft Policyholder Guide and Letter (received on 11 August 2020)



## Appendix C: Certificate of Compliance

I understand that my duty in preparing my report is to help the Court on all matters within my expertise and that this duty overrides any obligations I have to those instructing me and / or paying my fee. I confirm that I have complied with this duty.

I confirm that I am aware of the requirements applicable to experts set out in Part 35 of the Civil Procedure Rules, the Practice Direction and the Guidance for the Instruction of Experts in Civil Claims 2014. As required by Part 35 of the Civil Procedure Rules, I hereby confirm that I have understood my duty to the Court.

I confirm that I have made clear which facts and matters referred to in my report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.

Jeremy Nurse

Fellow of the Institute and Faculty of Actuaries

28 August 2020





## Appendix D: Glossary of Terms

A glossary of abbreviations used throughout the report is given below. All terms used are utilised within the context of the United Kingdom, except where indicated (in parentheses), where the terminology is specific to the country mentioned.

APS	Actuarial Profession Standards
BEL	Best Estimate Liability
Brexit	The exit of the United Kingdom from the European Union
CBI	Central Bank of Ireland (Ireland)
CLA	The Canada Life Assurance Company (Canada)
CLG	The Canada Life Group (UK) Limited
CLL	Canada Life Limited
Court	The High Court of Justice of England and Wales
COVID-19	The global coronavirus pandemic named as COVID–19 by the World Health Organisation in February 2020
Directions Hearing	An initial Court hearing at which the companies' plans for notifying policyholders are considered.
EEA	European Economic Area
Effective Date	The date on which the transfer is effected (expected to be 31 December 2020)
EIOPA	European Insurance and Occupational Pensions Authority
ELAS	The Equitable Life Assurance Society
EU	European Union
FCA	Financial Conduct Authority
FCA Guidance	FG 18/4 published in May 2018 by the FCA entitled “The FCA’s approach to the review of Part VII insurance business transfers”
Final Hearing	Also known as a ‘Sanctions Hearing’, this is a subsequent Court hearing that takes place once the notification requirements (decided in the Directions Hearing) have been met, at which the Court is asked to approve the Part VII transfer.

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FOS	Financial Ombudsman Service
FRC	Financial Reporting Council
FRR	Financial Resources Requirement
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
FSPO	Financial Services and Pensions Ombudsman (Ireland)
Guaranteed non-participating immediate annuities	A type of insurance policy that makes regular payments to the policyholder, typically throughout their lifetime, where these payments are made from the start of the policy (rather than starting at a later date or age) and whose amounts do not change throughout the term of the policy except by either (a) a fixed percentage specified at outset or (b) by reference to an inflation index
GWL	Great-West Life Inc. (Canada)
IFoA	Institute and Faculty of Actuaries
ILA	Irish Life Assurance plc (Ireland)
LICAT	Life Insurance Capital Adequacy Test (Canada)
MA	Matching Adjustment - an increase to the discount rate used in the calculation of the BEL under Solvency II that allows firms to take credit for the additional investment return in excess of the risk-free rate (swap rates under Solvency II) that they expect to earn from a “hold to maturity” investment strategy. Its effect is to reduce the market value of the assets that must be held by an insurer to cover its BEL.
MGMA	MGM Advantage Life Limited
MCR	Minimum Capital Requirement
ORSA	Own Risk and Solvency Assessment – a requirement under Solvency II whereby firms must regularly undertake a forward-looking assessment of risks, solvency needs and adequacy of capital resources
Own Funds	The excess of assets over liabilities under Solvency II
PCF	The Pre-Approval Controlled Functions described in the “Fitness and Probity Standards” (issued under Section 50 of the Central Bank Reform Act 2010) by the CBI (Ireland)

PIM	Partial Internal Model – a model which is used to calculate some components of the SCR that is bespoke to an individual firm under Solvency II
Policyholder Guide	The summary documents being sent to Transferring Policyholders in relation to the Proposed Scheme
Policyholder Letter	The cover letter accompanying the Policyholder Guide being sent to Transferring Policyholders
PRA	Prudential Regulation Authority
PRA Policy Statement	The Policy Statement issued in April 2015 by the PRA entitled “The Prudential Regulation Authority’s approach to insurance business transfers”
PRISM	The “Probability Risk and Impact System” risk-based framework for the supervision of regulated firms issued by the CBI (Ireland)
Proposed Scheme	The proposed Part VII transfer of the Transferring Policies from CLL to ILA
Scheme Report	This Independent Expert’s report as required in relation to the Proposed Scheme under Part VII of the FSMA
Scottish Friendly	Scottish Friendly Assurance Society Limited
SCR	The Solvency Capital Requirement under Solvency IISM&CR Senior Managers and Certification Regime
SMF	Senior Management Functions
Solvency II	The regulatory solvency framework for the EEA insurance and reinsurance industry that came into effect on 1 January 2016
Standard Formula	The EIOPA-prescribed method of calculating SCR
Summary	An abbreviated version of this Scheme Report prepared for policyholders interested in understanding the transfer but who may not wish to read this Scheme Report in its entirety
SUP	The Supervision Manual contained in the FCA Handbook
SUP18	Chapter 18 of the Supervision Manual contained in the FCA Handbook
Supplementary Report	A further report produced prior to the Final Hearing to provide an update for the Court on the Independent Expert’s conclusions in the light of any significant events subsequent to the date of the finalisation of the Scheme Report

TAS	Technical Actuarial Standards
Technical Provisions	Pillar 1 liabilities under Solvency II consisting of BEL and a risk margin
TMTP	Transitional Measure on Technical Provisions
Transferring Business	The Irish and German non-profit annuity policies of CLL, along with their allocated assets and liabilities
Transferring Policies	The Euro-denominated in-payment individual non-profit annuities currently written in CLL which, under the Proposed Scheme, are to be transferred to ILA
Transferring Policyholders	The holders of the Transferring Policies
TWL	Towers Watson Limited, a member company of WTW
UWP	Unitised With-Profit
VA	Volatility Adjustment – an increase to the discount rate used in the calculation of the BEL (other than for liabilities that are subject to the MA) which aims to prevent forced sales of assets in the event of extreme bond spread movements. Its effect is to reduce the market value of the assets that must be held by an insurer to cover its BEL.
WTW	Willis Towers Watson

## Appendix E: Compliance with Regulatory Requirements

The table below indicates how I have complied with the provisions of the PRA Policy Statement, SUP 18.2 and the FCA Guidance FG 18/4 that pertain to the form of the Scheme Report.

PRA Policy Statement reference	SUP 18.2 reference	Requirement	Scheme Report paragraph reference
2.30 (1)	SUP 18.2.33 (1)	Who appointed the Independent Expert and who is bearing the costs of that appointment.	1.2, 6.18
2.30 (2)	SUP 18.2.33 (2)	Confirmation that the Independent Expert has been approved or nominated by the appropriate regulator.	1.13
2.30 (3)	SUP 18.2.33 (3)	A statement of the Independent Expert's professional qualifications and (where appropriate) descriptions of the experience that fits him for the role.	1.9
2.30 (4)	SUP 18.2.33 (4)	Whether the Independent Expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest.	1.10-1.12, Appendix A
2.30 (5)	SUP 18.2.33 (5)	The scope of the report.	1.15 - 1.22
2.30 (6)	SUP 18.2.33 (6)	The purpose of the scheme.	2.2-2.6
2.30 (7)	SUP 18.2.33 (7)	A summary of the terms of the scheme in so far as they are relevant to the report.	Section 6
2.30 (8)	SUP 18.2.33 (8)	What documents, reports and other material information the Independent Expert has considered in preparing his report and whether any information that he requested has not been provided.	12.5, Appendix B
2.30 (9)	SUP 18.2.33 (9)	The extent to which the Independent Expert has relied on: (a) information provided by others; and (b) the judgment of others	Section 12
2.30 (10)	SUP 18.2.33 (10)	The people on whom the Independent Expert has relied and why, in his opinion, such reliance is reasonable.	1.23, Section 12
2.30 (11)	SUP 18.2.33 (11)	His opinion of the likely effects of the scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee	Sections 7,8 and 9
2.30 (12)	SUP 18.2.33 (11A)	His opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme	n/a

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PRA Policy Statement reference	SUP 18.2 reference	Requirement	Scheme Report paragraph reference
2.30 (13)	SUP 18.2.33 (12)	What matters (if any) that the Independent Expert has not taken into account or evaluated in the report that might, in his opinion, be relevant to policyholders' consideration of the scheme.	1.20
2.30 (14)	SUP 18.2.33 (13)	For each opinion that the Independent Expert expresses in the report, an outline of his reasons.	Throughout report
2.32 (1)	SUP 18.2.35 (1)	The summary of the terms of the scheme should include a description of any reinsurance arrangements that it is proposed should pass to the transferee under the scheme.	n/a
2.32 (2)	SUP 18.2.35 (2)	The summary of the terms of the scheme should include a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred.	6.11
2.33 (1)	SUP 18.2.36 (1)	The Independent Expert's opinion of the likely effects of the scheme on policyholders should include a comparison of the likely effects if it is or is not implemented.	Section 11
2.33 (2)	SUP 18.2.36 (2)	The Independent Expert's opinion of the likely effects of the scheme on policyholders should state whether he considered alternative arrangements and, if so, what	1.21
2.33 (3)	SUP 18.2.36 (3)	The Independent Expert's opinion of the likely effects of the scheme on policyholders should, where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences he considers may be material to the policyholders	Throughout the report
2.33 (4)	SUP 18.2.36 (4)	The Independent Expert's opinion of the likely effects of the scheme on policyholders should include his views on: (a) the effect of the scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer; (b) the likely effects of the scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect: (i) the security of policyholders' contractual rights; (ii) levels of service provided to policyholders; or (iii) for long-term insurance business, the reasonable expectations of policyholders; and (c) the cost and tax effects of the scheme, in so far as they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations	Sections 7, 8 and 9
2.35 (1)	SUP 18.2.38 (1)	For any mutual company involved in the scheme, the report should describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders	n/a

PRA Policy Statement reference	SUP 18.2 reference	Requirement	Scheme Report paragraph reference
2.35 (2)	SUP 18.2.38 (2)	For any mutual company involved in the scheme, the report should state whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights.	n/a
2.35 (3)	SUP 18.2.38 (3)	For any mutual company involved in the scheme, the report should comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without.	n/a
2.36 (1)	SUP 18.2.39 (1)	For a scheme involving long-term insurance business, the report should describe the effect of the scheme on the nature and value of any rights of policyholders to participate in profits	Sections 7 and 9
2.36 (2)	SUP 18.2.39 (2)	For a scheme involving long-term insurance business, the report should, if any such rights will be diluted by the scheme, how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders;	n/a
2.36 (3)	SUP 18.2.39 (3)	For a scheme involving long-term insurance business, the report should describe the likely effect of the scheme on the approach used to determine: (a) the amounts of any non-guaranteed benefits such as bonuses and surrender values; and (b) the levels of any discretionary charges	Section 9
2.36 (4)	SUP 18.2.39 (4)	For a scheme involving long-term insurance business, the report should describe what safeguards are provided by the scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm	10.27-10.30
2.36 (5)	SUP 18.2.39 (5)	For a scheme involving long-term insurance business, the report should include the Independent Expert's overall assessment of the likely effects of the scheme on the reasonable expectations of long-term insurance business policyholders	Sections 7, 8 and 9
2.36 (6)	SUP 18.2.39 (6)	For a scheme involving long-term insurance business, the report should state whether the Independent Expert is satisfied that for each firm the scheme is equitable to all classes and generations of its policyholders	8.13 and 9.17
2.36 (7)	SUP 18.2.39 (7)	For a scheme involving long-term insurance business, the report should state whether, in the Independent Expert's opinion, for each relevant firm the scheme has sufficient safeguards (such as principles of financial management or certification by a with-profits actuary or actuarial function holder) to ensure that the scheme operates as presented.	n/a

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FCA FG18/4 reference	Requirement	Scheme Report reference
6.2	Report is constructed in such a way that it is easily readable and understandable by all its users, paying attention to the following: 1) Technical terms and acronyms should be defined on first use. 2) There should be an executive summary that explains, at least in outline, the proposed transfer and the IE's conclusions. 3) The business to be transferred should be described early in the report. 4) The detail given should be proportionate to the issues being discussed and the materiality of the Transfer when viewed as a whole. While all material issues must be discussed, IEs should try to avoid presenting reports that are disproportionately long. 5) IEs should prepare their reports in a way that makes it possible for nontechnically qualified readers to understand.	1) Appendix D 2) Section 2 3) 2.2 4) Throughout the report 5) Throughout the report
6.3	Report must consider and compare: - Reasonable benefit expectations (including impact of charges). - Type and level of service (including claims handling). - Management, administration and governance arrangements.	Sections 7-9
6.4	We also sometimes see an imbalance between factual description and supporting analysis. IE reports often include a very detailed description of the transaction and background but much less analysis of the effect on each Policyholder group's reasonable expectations. Our concern here is that the IE often uses the detailed description of the background to compensate for the lack of analysis and challenge of the Applicants.	Throughout the report. Most of the analysis is in Sections 5 and 7-9.
<b>The level of reliance on the Applicants assessments and assertions</b>		
6.6	Question the adequacy of assessments carried out by Applicants before relying on them to reach own conclusions (including requesting additional work and evidence from Applicants in order to support their assertions).	Not explicitly demonstrable but discussed in detail with CLL and ILA management during the process, with the key change being the Proposed Scheme no longer applies to Guernsey residents.
6.7	Explain the nature of any challenges made to the Applicants and the outcome of these within the IE report, rather than just stating the final position.	As above
6.8	Where conclusions are supported solely or largely by statements such as 'I have discussed with the firm's management and they tell me that...' followed by 'I have no reason to doubt what they have told me...', then: - Where a feature of the proposed transfer forms a significant part of the IE's own assessment of the Scheme's impact, the IE should review relevant underlying material, rather than relying on the Applicants' analysis of the material and subsequent assertions. - If there are concerns about matters that fall outside the IE's sphere of expertise, such as legal issues, the Applicants must provide the IE with any advice that they have received. If the issue is significant or remains uncertain, the IE must ensure that the Applicants had obtained appropriate advice from a suitably qualified independent subject matter expert.	As above



FCA FG18/4 reference	Requirement	Scheme Report reference
6.9	IE has challenged calculations carried out by the Applicants if there is cause for doubt on review of the Scheme and supporting documents. As a minimum, the IE should: 1) review the methodology used and any assumptions made to satisfy themselves that the information is likely to be accurate and to challenge it where appropriate 2) challenge the factual accuracy of matters that, on the face of the documents or considering the IE's knowledge and experience, appear inconsistent, confusing or incomplete	1) Not explicitly demonstrable but discussed in detail with CLL and ILA management during the process, with some minor changes being made to the pro-forma financial statements. 2) n/a
6.10	Documents provided by the Applicants have been challenged where they contain an insufficient level of detail or analysis. For example: - Applicants' assertions that service levels will be maintained to at least the pre-transfer standard: IE should include not only details of the Applicant's plans and any gap analyses that have been produced but also include their view of their adequacy. - Change in governance arrangements in the Transferee that may lead to poorer customer outcomes: the IE must review and compare the governance arrangements in the Transferor which produce good customer outcomes (e.g. any committees with conduct responsibilities) within the Transferee's governance arrangements. - Consideration of the strain on resources that may occur post-transfer and that could impact on the service standards of the Transferee's existing customers and/or control over conduct of business risk. The IE report should include a review of relevant management information indicators and related contingency planning.	Section 7
<b>Sufficient comparative regulatory framework analysis</b>		
6.11	Where the regulatory framework is different for the Transferor and Transferee, the IE has carried out sufficient analysis of the differences including, where appropriate, taking independent advice.	Section 4
6.12	For cross-border transfers ensure there is a sufficiently detailed analysis of regulatory protections post-transfer. This can include: 1) The extent to which existing regulatory requirements and protections continue, including whether there is continued access to the Financial Ombudsman Service and the Financial Services Compensation Scheme. In the context of EU withdrawal this is expected at least until the point of policy renewal. 2) The comparative regulatory requirements and conduct protections across any relevant jurisdictions, including but not limited to complaints or compensation bodies compared to the UK. 3) Analysis of the likely impacts. For example, the number of Policyholders affected, the size of possible claims and any potential actions or provisions to mitigate this. 4) Post EU Withdrawal, non-UK EEA customers may be subject to the local conduct of business rules regime, which may not include FOS or FSCS issues. In these cases, firms taking proportionate approaches to compare regimes are likely to be accepted. For example a high level analysis may be appropriate, selecting key UK protections for consumers that are not harmonised in the EEA, and that could be relevant to servicing contracts. This could be accompanied	1)-3) Sections 4 and 7 4) 10.32-10.44

FCA FG18/4 reference	Requirement	Scheme Report reference
	by an explanation that a full gap analysis has not been carried out, but that policyholders can contact the Applicants if they are concerned. Some firms are able to continue to service contracts from UK branches to preserve continuity of regime at least until renewal.	
6.13	The IE report must contain a statement describing the two regimes as well as a considered comparison, highlighting points of significant difference that could adversely impact Policyholders. The level of detail to be included must be sufficient for the Court to be in a position to be satisfied.	Sections 4 and 7, 10.32-10.44
6.14	If the IE's analysis is inconclusive or there are potential conduct risks due to differences in the regulatory framework, we expect to see sufficient explanation of how Policyholders may be affected and the Applicant's proposals to mitigate these risks.	n/a
6.15	When stating that the IE is satisfied by referencing the Scheme, the IE must adequately explain how the features have led to their satisfaction. The IE must include both the evidence and their reasoning.	Throughout the report
<b>Balanced judgements and sufficient reasoning</b>		
6.16	The IE must state in their report whether they are certain there will be no material adverse impact to Policyholders or whether this is their best judgement, but lacks certainty. In these instances, the IE must consider the following: - Where the IE takes the view that there is probably no material adverse impact, the IE must challenge the Applicants about further work the Applicants could undertake to enable the IE to be satisfied to a greater degree. - The IE should challenge the Applicants in order to gain the necessary level of confidence that their report's conclusions are robust. Applicants and IEs should be aware that they will need to consider how any proposed changes/mitigations will impact all Policyholder groups.	Throughout the report
6.17	The IE must check that the documents they are relying, and forming judgements, on are the most up-to-date available when finalising their report.	Appendix B
6.18	If market conditions have changed significantly since the IE's analysis was carried out and they formed their judgement, the Applicants must discuss any changes with the IE and for the IE to update their report as necessary. If the Scheme document has been finalised, the IE should comment in more detail in their Supplementary Report or by issuing supplementary letters to the Court to confirm whether their judgement is unchanged.	COVID-19 explicitly covered in Section 10, but will be considered more fully in the Supplementary Report when more details are available.
<b>Sufficient regard to relevant considerations affecting Policyholders</b>		
6.19	Consider all relevant issues for each individual group of Policyholders in both firms, as well as how an issue may impact each group. The IE is expected, when giving their opinion, to consider the: - Current and proposed future position of each Policyholder group - Potential effects of the transfer on each of the different Policyholder groups	Sections 7-9

FCA FG18/4 reference	Requirement	Scheme Report reference
	- Potential material adverse impacts that may affect each group of Policyholders, how these impacts are inter-related and how they will be mitigated	
6.20	Consider whether the groups of affected Policyholders have been identified appropriately. For example, this could include instances where certain Policyholder groups' services are provided by an outsourced function which is changing, but other Policyholder groups do not.	When considering the issues covered in my report I have had regard to the impact the issues may have on a range of policyholder groups.
6.21	Review and give opinion on administrative changes affecting Policyholders, including: - Consideration of the impact of an outsourcing agreement entered into by the parties before the Part VII process began, where the administration duty 'moved' from the Transferor to the Transferee in preparation for the transfer. Provide a comparison of the pre and post-outsourced administration arrangements so the IE can clearly review and compare any changes to Policyholder positions and service expectations. - For the case where the IE concludes that because the transfer will not create any change to the administrative arrangements, there will be no material impact on Policyholders: consider what might happen if the Transfer does not proceed and the possibility that the outsourcing agreement could be cancelled, returning the administrative arrangements to the original state. In such circumstances, consider the impact on Policyholders and claimants of the outsourcing agreement as part of the Part VII process.	n/a
6.22	Review and provide opinion on all relevant issues for all Policyholder groups where reinsurance was entered into in anticipation of a transfer: - Some firms pre-empt regulatory scrutiny by buying reinsurance against risks before they begin the transfer process. In these instances, consider if it is appropriate to compare the proposed Scheme with the position the Transferor would be in if they did not benefit from the reinsurance contract. - If the transfer is not sanctioned and the reinsurance either terminates automatically or can be terminated by the Transferee, consider the Scheme as if the reinsurance was not in place.	n/a
6.23	If the IE identifies particular sub-groups of Policyholders whose benefits, without other compensating factors, are likely to be adversely affected, the IE should take into account the Transferor's obligations under Principle 6 (Customers' interests) of the FCA's Principles for Businesses.	Explained in detail throughout the report.
6.24	Ensure there is consideration and analysis of alternatives when a loss is expected for a particular subgroup of Policyholders, even if the IE does not consider this loss to be material.	Section 7
6.25	Provide the analysis outlined in 6.24 even if the IE is able to conclude that the Policyholder group as a whole is not likely to suffer material adverse impact, even if a minority may. For example where: - Some Policyholders within a group/sub-group will suffer higher charges post-transfer because the Transferee has a different charging structure.	n/a

FCA FG18/4 reference	Requirement	Scheme Report reference
	- Some Policyholders within a group/sub-group had free access to helplines that will no longer be available or have a significantly altered service after the transfer.	
6.26	Ensure that no conclusions are reached based on the balance of probabilities and without adequately considering the possible impact on all affected Policyholder groups.	Section 7, 10.32-10.44
6.27	As a specific example, we might consider the right of Policyholders to make a claim on the FSCS following a cross-border general insurance transfer: - The IE may say they are satisfied that there is no material adverse impact on Policyholders because of the Transferee's capital position (meeting relevant requirements), and the short term nature of the liabilities (for example, annually renewable). The IE may conclude from this that it is unlikely the Transferee will fail and Policyholders need recourse to the FSCS as a result. While we accept that this is a potentially relevant consideration, we would not be satisfied with this view without further evidence. For example, some evidence and analysis of why the size and complexity of a particular firm may make a default, before the time that policyholders have to claim on policies, extremely unlikely.	Section 7, 10.32-10.44
6.28	Present the consideration, evidence and reasoning to support the IE's opinion that a change due to the Part VII Transfer will not materially adversely impact a group of Policyholders.	Sections 7-9
<b>Commercially sensitive or confidential information</b>		
6.29	When considering commercially sensitive information, consider Policyholders interests as the information will not be publicly available.	Key commercially sensitive information: Capital Management Framework, plus Solvency II Pillar 2 and LICAT capital positions
6.30	In these situations, document the analysis and the information relied upon. Consider sending a separate document with further details, solely for the Court's use and not for public disclosure.	Appendix B
<b>The level of reliance on the work of other experts</b>		
6.31	For large scale and complex insurance business transfers, if relying on the analytical work of other qualified professionals, it is still expected the IE to have carried out their own review of this analysis to ensure they have confidence in, and can place informed reliance on, the opinions they draw from another professional's work.	10.43-10.49 and 12.2-12.5
6.32	Obtain a copy of any legal advice given to the Applicants. This should be in writing or transcribed, and approved by the advisor. It should also be in a sufficiently final form for the IE to be able to review and rely on it. The IE should reflect this review, and the opinions drawn from the advice, within their report.	10.25
6.33	If referring to factors outside of expertise and relying on advice received by the Applicants, the IE should consider whether or not to obtain their own independent advice on the relevant issue.	3.20-3.22 and 10.43-10.49

FCA FG18/4 reference	Requirement	Scheme Report reference
6.34	Consider if the IE needs to obtain separate legal advice, this will depend on the significance and materiality of the issue.	3.20-3.22
6.35	Consider whether it is reasonable for the IE to rely on advice and whether their independence is compromised by doing so. Whether or not the legal advisor has acknowledged that it owes a duty of care to the IE will be relevant to this consideration. Depending on how complex the legal issue is, IEs who rely on the Applicants' legal advice and merely state that they have no reason to doubt the advice and/or that it is consistent with their understanding of the position or experience of similar business transfers may be challenged.	3.20-3.22
6.36	When deciding whether to obtain independent legal advice, the IE should consider, amongst other things, the following: <ul style="list-style-type: none"> <li>- The significance of the issue and the degree of potential adverse impacts to Policyholders if the position turns out to be different from that considered likely in the legal advice.</li> <li>- How much the IE relies on the legal advice to reach their conclusions and, if they did not rely on the legal advice, would the report contain too little information to justify the view that there is no material adverse impact?</li> <li>- The difficulty, novelty or peculiarity of the issue to the Applicants' own circumstances.</li> <li>- Applicants' proposals to explain to Policyholders in communication documents the issues involved, any uncertainty, and any residual risks.</li> <li>- Whether, depending on the issue's significance or uncertainty, the Applicants have obtained an adequate level of advice. Where relevant, whether the Applicants have engaged external advisors with the appropriate expertise and qualifications for the specific subject or jurisdiction.</li> <li>- Whether any advice already received is heavily caveated, qualified or there is a significant degree of uncertainty.</li> </ul>	Not explicitly demonstrable but considered in the undertaking of the work.
6.37	The IE may need to explain why they consider that they do not need to get independent advice to be adequately satisfied on a point. The IE's assessment should consider whether there are credible alternative arguments that could be made, whether identified in the Applicant's advice or otherwise. Consider where risks are identified with no suggestion about how they can be mitigated, or what the impact on Policyholders may be if the risks do occur. These considerations would allow the IE to consider the worst case scenario of these impacts.	Throughout the report I have explained how I have reached the conclusions I have drawn.
6.38	Consider the Applicant's contingency plans if the risks identified in the legal advice occur and whether this may create negative consequences for Policyholders.	n/a
6.45	At the start of the document, the IE should provide a description of where they propose to rely on information provided by the Applicants. Overly general reliance will indicate a lack of critical assessment or challenge.	1.23, 4.56-4.57
6.47	If the report does not reach a clear conclusion, either generally or on a specific issue, the IE report should state clearly: 1) That the IE has considered and is satisfied about the likely level of impact on a particular point. Where uncertainty remains, the IE report needs to include details of, and reasons for, this uncertainty as well as any further steps the	1) Demonstrated throughout the report, including Sections 7-9 2) n/a

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FCA FG18/4 reference	Requirement	Scheme Report reference
	IE has taken to get clarification, such as seeking further advice from a subject matter expert. 2) How the IE satisfied themselves about the identified uncertainty and formed an opinion on any potential impact.	
<b>Demonstrating challenge</b>		
6.48	To ensure the IE report is complete and considered there should be challenge from all involved parties. Including evidence that Applicants have made appropriate challenges, particularly when believed that the IE has not fully addressed issues. Applicants have an interest in ensuring that the Court, regulators and Policyholders are able to rely on the IE report, taking into account to the IE's disclaimers. Applicants should make the challenges without compromising the IE's independence. It should be confirmed that the near-final version of the IE's report had the relevant challenge at the time it was submitted.	CLL, ILA and their legal advisers have all had the opportunity to challenge all aspects of the report. In order to arrive at my conclusions I have regularly discussed issues with the management teams of CLL and ILA.
6.49	To ensure effective two-way challenge it is expected the IE engages with FCA or PRA approved persons of sufficient seniority at the Applicant firm, such as senior actuaries, including possibly the Chief Actuary, the Chief Financial Officer, Senior Underwriters and so on.	I have engaged with key subject matter experts from both CLL and ILA, including their respective Chief Actuaries, to gain comfort on the appropriateness of the methodology and conclusions for the most material quantitative aspects of the Proposed Scheme.
6.50	IEs who are members of the Institute & Faculty of Actuaries should pay proper regard to the Technical Actuarial Standards (TAS) published by the Financial Reporting Council, particularly those for compiling actuarial reports.	1.30
6.51	IEs should be particularly aware that the revised versions of the TAS which came into force with effect from 1 July 2017 (TAS 100: Principles for Technical Actuarial Work and TAS 200: Insurance) specifically apply to technical actuarial work to support Part VII Transfers.	1.30
6.52	Ensure compliance with paragraph 5 of TAS 100 which states that actuarial communications should be 'clear, comprehensive and comprehensible so that users are able to make informed decisions understanding the matters relevant to the actuarial information' and to paragraph 5.2 of TAS 100 which states that 'the style, structure and content of communications shall be suited to the skills, understanding and levels of relevant technical knowledge of users'.	1.30
6.53	Actuarially qualified IEs and peer reviewers should also bear in mind the Actuaries' Code and Actuarial Profession Standards documents APS X2: Review of Actuarial Work and APS L1: Duties and Responsibilities of Life Assurance Actuaries.	1.30-1.32
<b>Review of the communications strategy</b>		
7.3	IEs should include consideration of the proposed communications strategy and any supporting requests for dispensations from the Transfer Regulations in their report. There should be evidence that the IE has challenged proposed communications that are not clear and fair and do	10.1-10.15

FCA FG18/4 reference	Requirement	Scheme Report reference
	not adequately explain the transfer and the potential impacts on Policyholders and how these have been addressed.	