

# The Part VII transfer of part of the business of Legal and General Assurance Society Limited to ReAssure Limited

The report of the Independent Expert

July 2019

Oliver Gillespie FIA





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# 1. Introduction

## THE PURPOSE OF THIS REPORT

- 1.1 It is proposed to transfer a block of long-term insurance business from Legal and General Assurance Society Limited (“LGAS”) to ReAssure Limited (“ReAssure”).
- 1.2 Under UK law a transfer of long-term insurance business must be carried out in accordance with Part VII of the Financial Services and Markets Act 2000 (“FSMA”) and an application must be made to the High Court of Justice, Business and Property Courts of England and Wales, Companies Court (the “High Court”) for approval under Section 111 of FSMA.
- 1.3 Under Section 109 of FSMA the application to the High Court for approval must be accompanied by a report (the “Scheme Report”) by an Independent Expert on the terms of the proposed transfer scheme.

## MY APPOINTMENT AS INDEPENDENT EXPERT

- 1.4 I have been appointed by LGAS and ReAssure to report, pursuant to Section 109 of FSMA, in the capacity of the Independent Expert, on the terms of the proposed scheme providing for the transfer to ReAssure of some of the long-term insurance business of LGAS.
- 1.5 I refer to the proposed scheme as “the Scheme” or “this Scheme” and throughout the remainder of this report these terms are used to cover all the proposals included in the scheme of transfer.
- 1.6 I am a Fellow of the Institute and Faculty of Actuaries (“IFoA”) and hold certificates issued by the IFoA enabling me to act as a Chief Actuary and a With-Profits Actuary.
- 1.7 I am a partner of Milliman LLP (“Milliman”) and I am based in its London office. I am an approved person on the Financial Services Register and I currently hold a number of Chief Actuary and With-Profits Actuary roles. I have fulfilled the role of Independent Expert in relation to a number of recent Part VII transfers that have subsequently been approved by the High Court.
- 1.8 My appointment was approved by the Prudential Regulation Authority (“PRA”) after consultation with the Financial Conduct Authority (“FCA”) and was confirmed in a letter dated 27 March 2018 to the Legal & General Group. My terms of reference have been reviewed by the FCA and the PRA.
- 1.9 I submitted a statement of independence to the PRA and FCA for review before my approval. I confirm that neither I nor Milliman have or have had any direct or indirect interest in any of LGAS, ReAssure or other related firms that could influence my independence. Neither I nor my immediate family have any policies with the L&G Group, LGAS, the Swiss Re Group or ReAssure.
- 1.10 As with other costs of the Scheme, my fees will be borne by LGAS and ReAssure as described in Section 7 of this report.

## MY REPORT AS INDEPENDENT EXPERT

- 1.11 The Scheme Report consists of this report and any subsequent supplementary reports.
- 1.12 This report is produced for the High Court to assist in its deliberations in respect of the Scheme. The report and a summary will be made available to policyholders via the Legal & General Group website ([www.legalandgeneral.com](http://www.legalandgeneral.com)) and the ReAssure website ([www.reassure.co.uk](http://www.reassure.co.uk)), and the summary of my report will be included in the communications pack that is sent to the appropriate policyholders. The groups of policyholders who will receive a communications pack, and the reasons why, are set out in Section 13 of this report.
- 1.13 My report has been prepared in accordance with the approach and expectations of the PRA, as set out in “The Prudential Regulation Authority’s approach to insurance business transfers” dated April 2015 (the “PRA Statement of Policy”), as well as Chapter 18 of the Supervision Manual (“SUP 18”) contained in the FCA Handbook, and the FCA’s Final Guidance “FG18/4: The FCA’s approach to the review of Part VII insurance business transfers” dated May 2018 (the “FCA Final Guidance”).

- 1.14 I confirm that the comments and conclusions in this report apply to all policyholders of LGAS and ReAssure irrespective of their place of residence and/or the jurisdiction within which the business is said to be carried on or in which their policy was issued.

#### **THE JERSEY AND GUERNSEY SCHEMES**

- 1.15 In parallel to the proposed Scheme, there will be proposed schemes in:
- Jersey (“the Jersey Scheme”) for the transfer of any business carried on by LGAS in or from within Jersey; and
  - Guernsey (the “Guernsey Scheme”) for the transfer of any policy issued to residents of the Balliwick of Guernsey.
- 1.16 The Jersey Scheme and the Guernsey Scheme will be on substantially the same terms as the Scheme and implementation of the Scheme is not conditional on the approval of the Jersey Scheme or the Guernsey Scheme.
- 1.17 For the avoidance of doubt, references to the Scheme should be taken to include the Jersey Scheme and the Guernsey Scheme.

#### **MY SUPPLEMENTARY REPORT**

- 1.18 I will prepare a further report (the “Supplementary Report”) prior to the Final Hearing to provide an update for the High Court on my conclusions in respect of the effect of the proposed transfer on the different groups of policyholders in light of any significant events subsequent to the date of the finalisation of my main report.
- 1.19 My Supplementary Report will be available to policyholders via the Legal & General Group website [www.legalandgeneral.com](http://www.legalandgeneral.com) and the ReAssure website [www.reassure.co.uk](http://www.reassure.co.uk).

#### **THE PARTIES FOR WHOM MY REPORT HAS BEEN PREPARED**

- 1.20 This report, and any extract or summary thereof has been prepared particularly for the use of:
- The High Court;
  - The Royal Courts in Jersey and Guernsey;
  - The policyholders of LGAS and ReAssure;
  - The FCA and the PRA;
  - The regulators in Jersey and Guernsey;
  - The insurance regulator of any European Economic Area (“EEA”) country who requests a copy of the report;
  - The Directors and senior management of LGAS;
  - The Directors and senior management of ReAssure;
  - The LGAS With-Profits Committee (the “WPC”);
  - The ReAssure Fairness Committee (the “ReAssure FC”); and
  - The professional advisers of any of the above.
- 1.21 In accordance with the legal requirements under FSMA, copies of my report should be made available to the policyholders of LGAS and ReAssure and to other interested parties.

#### **RELIANCES AND LIMITATIONS**

- 1.22 In preparing my report, I have had access to certain documentary evidence provided by LGAS and ReAssure, the key elements of which are listed in Appendix G. I have also had access to, and discussions with, senior management of LGAS and ReAssure. My conclusions depend on the substantial accuracy of this information and I have relied on this information without independent verification.

- 1.23 I have relied on the work of the external auditors of LGAS and ReAssure (respectively KPMG LLP or “KPMG” and PricewaterhouseCoopers LLP or “PwC”) in gaining confidence in the financial information as provided in Appendices A and B of this report.
- 1.24 LGAS and ReAssure have been separately advised by their own legal advisers, respectively Slaughter and May and Herbert Smith Freehills LLP (“Herbert Smith Freehills”), and, in respect of certain matters, I have reviewed the legal advice provided by Slaughter and May and Herbert Smith Freehills and have relied on that advice to reach my conclusions on the basis set out in Section 4. I have described in Section 4 why I think it is reasonable to use that advice in that way. For the avoidance of doubt, Slaughter and May and Herbert Smith Freehills have no liability to me in respect of that advice.
- 1.25 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 for inclusion in various communications with the policyholders (and where relevant distribution to any persons requesting a copy of it). Any other purported summary of my report or elements within my report should not be treated as having been approved or authorised by me.
- 1.26 This report has been prepared for the High Court on a basis agreed with the PRA and FCA and must not be relied upon for any other purpose. No liability will be accepted by Milliman, or me, for any application of my report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of the report. In particular, no liability will be accepted by Milliman or me under the terms of the Contracts (Rights of Third Parties) Act 1999.
- 1.27 There are no documents or other information that I have requested and that have not been provided. Appendix G contains a list of the key data items upon which I have relied.
- 1.28 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Scheme and in preparing my report, but that nonetheless should be drawn to the attention of policyholders in their consideration of the terms of the Scheme.

#### **REGULATORY AND PROFESSIONAL GUIDANCE**

- 1.29 My report has been prepared subject to the terms of the Technical Actuarial Standards (“TAS”) applicable to Insurance transformations (“TAS 200: Insurance”) issued by the Financial Reporting Council. In my opinion, my report complies with the TAS 200: Insurance and is compliant with those elements of the TAS 100: Principles for Technical Actuarial Work that are applicable to transformations. In complying with these requirements, I note that a number of the key documents listed in Appendix G have been prepared or reviewed by individuals who were subject to professional standards in undertaking their work, including, where appropriate, TAS requirements.
- 1.30 Actuarial Profession Standard (“APS”) X2, as issued by the IFoA, requires members to consider whether their work requires an independent peer review.
- 1.31 In my view this report does require independent peer review and this has been carried out by a senior actuary in Milliman LLP who has not been part of my team working on this assignment.

## 2. Executive summary

### INTRODUCTION

#### The companies involved in the transfer

- 2.1 LGAS is a proprietary composite insurance company that was founded in 1836. LGAS is the principal operating subsidiary for the Legal & General Group (the “L&G Group”) and is one of the largest providers of insurance products in the UK.
- 2.2 LGAS currently has approximately £143 billion of assets under management (as at 31 December 2018).
- 2.3 On 31 May 2019, the L&G Group announced that it had sold its general insurance business to Allianz and that the transaction was expected to complete in the second half of 2019 subject to regulatory approvals.
- 2.4 ReAssure is a proprietary insurance company that is part of the Swiss Re Group. Since February 2018, the Japanese insurance group MS&AD Insurance Group (“MS&AD”) has owned a minority stake in ReAssure and in February 2019 this increased from 15% to 25%.
- 2.5 ReAssure’s business is based on the acquisition of the closed blocks of in-force life insurance business of other life insurance companies either through reinsurance agreements or by means of legal transfers of business and this has led to ReAssure undertaking a large number of transfers of business since its first acquisitions in 1983.
- 2.6 ReAssure currently has approximately £39 billion of assets under management (as at 31 December 2018).

#### The proposed transfer

- 2.7 On 6 December 2017, the L&G Group announced that it intended to sell part of its long-term insurance business to ReAssure in order to allow it to focus on growth in other areas such as writing and acquiring blocks of annuities, and investment management.
- 2.8 It is this block of business that is proposed to be transferred from LGAS to ReAssure under the proposed transfer that is the reason for this report.

#### The transferring business

- 2.9 The transferring business consists of approximately 1.0 million policies and assets of approximately £28 billion (as at 31 December 2018). This business includes the ‘Mature Savings’ block of business and smaller volumes of other long-term insurance business of LGAS and has been largely closed to new business and in run-off since 2015.
- 2.10 The transferring business consists of with-profits business, unit-linked business and non-profit business. These are all types of long-term insurance products that are common across the UK industry and I explain these in more detail in Section 3. A summary of the transferring business is provided in Section 5.
- 2.11 If the transfer were to go ahead then the assets and liabilities associated with the transferring business would be transferred from LGAS to ReAssure. The proposed date of transfer is currently set to be 4 November 2019 (the “Legal Effective Date”) at which point the transferring business would legally transfer from LGAS to ReAssure and the Scheme will become operative between LGAS, ReAssure and the wider world.
- 2.12 The Scheme would become effective as between LGAS and ReAssure on the first day of the calendar month in which the Legal Effective Date occurs – this is the Economic Effective Date. Based on a Legal Effective Date of 4 November 2019, the Economic Effective Date would be 1 November 2019.

### MY CONSIDERATIONS WITH RESPECT TO THE PROPOSED TRANSFER

- 2.13 My key considerations in respect of each group of policyholders affected by the proposed transfer are whether the proposed transfer would have an effect on the following:

- **The security of benefits under the policies.**

The security of benefits for the transferring business is derived from the financial strength of the firm itself which depends on the assets held to back the policies, any assets held in excess of this, and any external support provided by the parent of the firm.

The level of assets held by a firm in relation to a particular block of business is determined by the appropriate regulatory regime and any extra assets required as typically set out in that firm's risk appetite statement (the "RA Statement") as a multiple of the level of assets required by the appropriate regulatory regime. The RA Statement will typically include details of the required governance around the RA Statement including the required response to a breach and how the RA Statement might be changed.

- **The profile of risks to which the policies are exposed.**
- **The reasonable expectations of the policyholders in respect of their benefits.**
- **The standards of administration, service, management and governance applied to each group of policies.**

2.14 In this report I have considered the effects of the proposed transfer on the following groups of policies:

- The transferring LGAS policies in Section 8 and Section 9;
- The existing ReAssure policies in Section 10; and
- The non-transferring LGAS policies in Section 11.

2.15 I summarise these sections below.

## **THE EFFECT OF THE TRANSFER ON THE TRANSFERRING LGAS POLICIES**

2.16 I analyse the effects of the proposed transfer on the transferring LGAS policyholders in Section 8 and 9.

### **The effect of the transfer on the security of the benefits of the transferring policies**

2.17 If the proposed transfer were to proceed, the security of benefits under the transferring policies would be derived from ReAssure rather than from LGAS as currently.

2.18 As the analysis in Section 8 shows, I am satisfied that this reliance on the financial strength of ReAssure, its risk appetite statement and its group support would not have a material adverse effect on the security of the benefits of the transferring LGAS policies.

### **The effect of the transfer on the profile of risks to which the transferring policies are exposed**

2.19 If the transfer were to go ahead, the transferring policies would become policies of ReAssure and be directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.

2.20 Whilst the transfer would result in a change to the risk exposures of the transferring policies, the transfer would have no effect on the regulatory regime to which the business would be subject as both firms are subject to the Solvency II regime and to regulation by the PRA and FCA, and the Solvency Capital Requirement ("SCR") calculated in accordance with the Solvency II regime will continue to reflect the risk exposures of ReAssure which will, after the transfer, include the transferring LGAS business.

2.21 Therefore, I am satisfied that, this would not have a material adverse effect on the security of the benefits of the transferring policies.

### **The effect of the transfer on the reasonable expectations of the transferring policyholders in respect of their benefits**

2.22 The transferring business consists of with-profits, unit-linked, and non-profit business and in Section 8 I consider the effects of the proposed transfer on the policyholders' reasonable expectations in respect of their benefits on each of these types of product separately.



- 2.23 The intention from ReAssure is that, after the transfer, the transferring business would be managed in materially the same way as it would have been had the transfer not happened and the business remained in LGAS.
- 2.24 That said, ReAssure is a different company to LGAS and has different management and governance structures and therefore, one would expect there to be some changes for the transferring policies after the transfer and I cover the proposed changes in Section 8.
- 2.25 I am satisfied that the transfer would not have a material adverse effect on the reasonable expectations of the transferring policyholders.

#### **The effect of the Transfer on the standards of administration and servicing applied to the transferring LGAS policies**

- 2.26 If the proposed transfer were to go ahead, ReAssure would take over the administration of the majority of the transferring business. The IT systems used to administer and service the transferring business would not transfer across to ReAssure and a plan has been put in place to migrate the policy data from the current LGAS administration systems to the ReAssure administration systems.
- 2.27 If this migration plan were to be completed by the Legal Effective Date then I am satisfied that there would not be a material adverse effect on the standards of the administration and servicing applied to the transferring LGAS policies.
- 2.28 However, at the time of writing this report, ReAssure and LGAS have identified some areas of material concern with the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board.
- 2.29 Both firms have provided assurance that these areas of concern are being addressed, that the migration plan has been revised, and that they are confident that the migration can be successfully delivered in time for the Legal Effective Date. It is expected that some additional manual processes will be in place for a period after the Legal Effective Date while building and testing of systems is completed.
- 2.30 It is the responsibility of the ReAssure Board and the LGAS Board to ensure that this migration is implemented successfully and without any material detriment to either transferring policyholders or existing ReAssure policyholders and I will rely on the ReAssure Board and the LGAS Board to ensure that this is the case. In particular I will rely on the Boards of the firms to ensure that the migration project is given the appropriate priority, that the required planning is carried out, and that the required resources are secured, such that the status of the migration project is quickly improved to an acceptable level.
- 2.31 Although uncertainty is not unexpected at this stage in migration projects of this complexity, the High Court will not sanction the Scheme until it is satisfied that there would not be a material adverse effect on policyholders. The firms have established readiness checkpoints to monitor and resolve these uncertainties and these will need to be passed before a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme.
- 2.32 I will report on the progress with the migration plan in my Supplementary Report for the Sanctions Hearing.

#### **The effect of the Transfer on the management and governance applied to the transferring LGAS policies**

- 2.33 A number of changes have recently been made to the governance framework within ReAssure in order to maintain the current level of governance of the transferring business within LGAS.
- 2.34 I have reviewed the ReAssure governance framework and I am satisfied that the level of oversight, including independent oversight, provided by the proposed framework is such that the proposed transfer would not have a material adverse impact on the standards of governance applied to the transferring business.

#### **Conclusion in respect of the transferring LGAS policies**

- 2.35 I am satisfied that the proposed transfer would not have a material adverse effect on:
- The security of the benefits of the transferring policies of LGAS;
  - The reasonable expectations of the transferring policyholders of LGAS in respect of their benefits; or
  - The standards of administration, service, management and governance that apply to the transferring LGAS policies.

- 2.36 As noted above there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.
- 2.37 I will provide an update on these in my Supplementary Report.

#### **THE EFFECT OF THE TRANSFER ON THE EXISTING REASSURE POLICIES**

- 2.38 I analyse the effects of the proposed transfer on the existing ReAssure policyholders in Section 10.

##### **The effect of the transfer on the security of the benefits of the existing ReAssure policies**

- 2.39 If the proposed transfer were to proceed, the security of benefits under the existing ReAssure policies would continue to be derived from ReAssure but a large amount of business would be transferred into ReAssure from LGAS.
- 2.40 As the analysis in Section 10 shows, I am satisfied that this transfer would not have a material adverse effect on the security of the benefits of the existing ReAssure policies.

##### **The effect of the transfer on the profile of risks to which the existing ReAssure policies are exposed**

- 2.41 I am satisfied that, although the transfer would cause a change to the profile of risks to which the existing ReAssure policies are exposed, this would not have a material adverse effect on the security of the benefits of the existing ReAssure policies.

##### **The effect of the transfer on the reasonable expectations of the existing ReAssure policies in respect of their benefits**

- 2.42 If the transfer goes ahead there would be no change to:
- The terms and conditions of the existing ReAssure policies;
  - The methodology used to calculate the amounts that are used to pay policyholders for claims and surrenders under with-profits, unit-linked and non-profit existing ReAssure policies;
  - The charges that apply to the existing ReAssure policies;
  - The exercise of discretion by ReAssure in respect of the management of the with-profits and unit-linked business; or
  - The rights of the existing with-profits policyholders of ReAssure to any future distributions from the inherited estates.
- 2.43 I am satisfied that the transfer would not have a material adverse effect on the reasonable expectations of the existing ReAssure policyholders in respect of their benefits.

##### **The effect of the Transfer on the standards of administration and servicing applied to the existing ReAssure policies**

- 2.44 As a result of the transfer, ReAssure would take over the administration of the majority of the transferring business.
- 2.45 The IT systems used to administer and service the transferring business would not transfer across to ReAssure and a plan has been put in place to migrate the policy data from the current LGAS administration systems to the ReAssure administration systems.
- 2.46 As noted above, there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board.
- 2.47 It is the responsibility of the Boards to ensure that this migration is implemented successfully and without any material detrimental impact to either transferring policyholders or existing ReAssure policyholders and I will rely on the ReAssure Board and the LGAS Board to ensure that this is the case.

2.48 I will report on the progress with the migration plan in my Supplementary Report for the Sanctions Hearing.

#### **The effect of the transfer on the management and governance of the existing ReAssure policies**

2.49 I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on the principles and practices used in the management of the existing business of ReAssure, the governance of the with-profits policies in the WLWPF, the NMWPF and the GAWPF, or the governance of the other ReAssure policies.

2.50 I am therefore satisfied that the implementation of the Scheme would not have a material adverse effect on the standards of management and governance that apply to the existing ReAssure policies.

#### **Conclusion for the existing ReAssure policies**

2.51 I am satisfied that the transfer would not have a material adverse effect on:

- The security of the benefits of the existing ReAssure policies;
- The reasonable expectations of the existing ReAssure policyholders in respect of their benefits; or
- The standards of administration, service, management and governance that apply to the existing ReAssure policies.

2.52 As noted above there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.

2.53 I will provide an update on these in my Supplementary Report.

#### **THE EFFECT OF THE TRANSFER ON THE NON-TRANSFERRING LGAS POLICIES**

2.54 I analyse the effects of the proposed transfer on the non-transferring LGAS policyholders in Section 11.

#### **The effect of the transfer on the security of the benefits of the non-transferring LGAS policies**

2.55 Currently, the non-transferring LGAS policies derive their security of benefits from being part of LGAS and this is derived from the financial strength available to provide security for the benefits of the non-transferring policies under the LGAS RA Statement and the external support available from the L&G Group. This would not change as a result of the implementation of the Scheme and therefore if the transfer were to go ahead I am satisfied that there would not be a material adverse effect on the security of the benefits of the non-transferring LGAS policies.

#### **The effect of the transfer on the profile of risks to which the non-transferring LGAS policies are exposed**

2.56 I am satisfied that, although the transfer would cause a change to the profile of risks to which the non-transferring LGAS policies are exposed, this would not have a material adverse effect on the security of the benefits of the non-transferring LGAS business.

#### **The effect of the transfer on the reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits**

2.57 If the transfer were to go ahead, there would be no change to the terms and conditions, the methodology used to determine claim and surrender benefits, the charges that apply, or the exercise of discretion in respect of the management of the unit-linked funds for the non-transferring LGAS policies.

2.58 I am satisfied that the transfer would not have a material adverse effect on the reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits.

### **The effect of the transfer on the standards of administration, servicing, management and governance applied to the non-transferring LGAS policies**

- 2.59 If the transfer were to go ahead there would be no change to the administration and servicing, the asset management arrangements, or the governance and management of the non-transferring LGAS policies.
- 2.60 I am satisfied that the transfer would not have a material adverse effect on the standards of administration, servicing, management and governance that apply to the non-transferring LGAS policies.

### **My conclusions for the non-transferring LGAS policies**

- 2.61 I am satisfied that the transfer would not have a material adverse effect on:
- The security of the benefits of the non-transferring LGAS policies;
  - The reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits; or
  - The standards of administration, service, management and governance that apply to the non-transferring LGAS policies.

### **THE REASSURE IPO**

- 2.62 On 3 August 2018, the Swiss Re Group announced that it was exploring the possibility of an Initial Public Offering ("IPO") of shares in the ReAssure Group in 2019.
- 2.63 In anticipation of a potential IPO, a new public parent company ("ReAssure Group plc" or "RGP") has been set up, of which ReAssure is now a subsidiary.
- 2.64 On 14 June 2019, RGP confirmed its intention to proceed with the IPO. RGP intends to apply for admission of its ordinary shares to the premium listing segment of the official list of the FCA and to trading on the London Stock Exchange's main market for listed securities. RGP's expectation is that admission will take place in July 2019.
- 2.65 A change of ownership resulting from the IPO could potentially lead to changes to the availability of parental capital support for ReAssure and to the management and governance of the insurance business within ReAssure. It is not expected that the ReAssure IPO would lead to any changes to the administration or servicing of the insurance business within ReAssure.
- 2.66 In terms of the different groups of policies considered in Sections 8, 9, 10 and 11 of this report, it is only the transferring LGAS policies that would be affected by the IPO as a result of the Transfer. I analyse the effects of the ReAssure IPO in Section 12 of this report and in summary I am satisfied that:
- If the risk appetite statement applicable to the post-IPO company were to be at least as strong as the ReAssure IPO RA Statement there would not be a material adverse effect on the security of the benefits and reasonable benefit expectations of the transferring policies.
  - There exist sufficient controls to ensure that there would not be a material adverse effect on the standards of administration, service, management and governance that apply to the transferring policies.

### **MY CONSIDERATIONS IN RESPECT OF THE FAIR TREATMENT OF CUSTOMERS**

- 2.67 I analyse the effects of the transfer on the fair treatment of customers in Section 13.

### **The approach to communications with policyholders**

- 2.68 LGAS will send a mailing pack to the LGAS transferring policyholders (subject to dispensations detailed below).
- 2.69 Due to the size of the transferring business compared to the existing business of ReAssure, ReAssure will send a letter (the "Part VII Letter") to the existing ReAssure policyholders to make them aware of the transfer (subject to dispensations).
- 2.70 LGAS and ReAssure intend to seek waivers from the regulatory requirements to send a written notice to certain groups of policyholders as set out in Section 13 and I am satisfied that the applications for waivers are reasonable.

### **The costs of the transfer**

- 2.71 The costs of the transfer will be split between the shareholder funds of LGAS and ReAssure.
- 2.72 As part of a wider expense deal with the LGWPF, a £50m contribution to the cost of migration will be taken from the LGWPF. This is covered in Section 7.
- 2.73 I am satisfied that this allocation of the costs of the transfer is reasonable.

### **MY CONCLUSIONS**

- 2.74 I confirm that I have considered the issues affecting the policyholders of LGAS and ReAssure separately, as set out in Sections 8 to 14 and that I do not consider further subdivisions (other than those in this report) to be necessary.
- 2.75 I am satisfied that the transfer would not have a material adverse effect on:
- The security of the benefits of the policies of LGAS and ReAssure;
  - The reasonable expectations of the policyholders of LGAS and ReAssure in respect of their benefits;  
or
  - The standards of administration, service, management and governance that apply to the LGAS and ReAssure policies.
- 2.76 I am satisfied that the transfer is equitable to all classes and generations of LGAS and ReAssure policyholders.
- 2.77 As noted above there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.
- 2.78 I will provide an update on these in my Supplementary Report.

### 3. The insurance market and regulatory environment

#### INTRODUCTION

- 3.1 The regulatory regime to which UK insurers are subject, and the applicable solvency requirements, are relevant to my considerations as Independent Expert.
- 3.2 This section provides some background on the types of long-term business involved in the transfer, and the solvency and governance requirements of the regulatory regimes in the UK. The background is provided in the context of this Scheme and is not intended to be a complete description of the products or regulatory environment in the UK.

#### THE UK REFERENDUM ON THE EUROPEAN UNION – “BREXIT”

- 3.3 In a referendum held in the UK on 23 June 2016, a majority voted for the UK to leave the European Union (the “EU”). The subsequent triggering by the UK government of Article 50 of the Treaty on European Union in March 2017 and associated negotiations means that as things stand the UK is currently scheduled to leave the EU no later than October 2019.
- 3.4 The exit of the UK from the EU could lead to considerable disruption in financial markets and in the market for financial services across Europe and, at the time of writing this report, there remains considerable uncertainty as to when the UK will leave the EU and around exactly what form that exit might ultimately take.
- 3.5 The current regulatory solvency framework for the EEA insurance and reinsurance industry (from 1 January 2016 onwards) is known as Solvency II and the financial information used in my analysis in writing this report is based on the Solvency II regime. It is currently not certain as to what the governing insurance regulatory regime will be after the UK’s exit from the EU.
- 3.6 In my analysis in this report, I have assumed that the current Solvency II regime will remain in place after the UK’s exit from the EU as this is in my view the most likely outcome and is consistent with policy statements made by HM Treasury and the PRA. However there exist plausible scenarios in respect of the UK leaving the EU where the UK insurance regulation would not remain under the Solvency II regime and if that were to occur then I would need to consider whether a new report would be required or whether it could be picked up in a Supplementary Report.

#### THE PRODUCTS AND LONG-TERM INSURANCE BUSINESS RELEVANT TO THE SCHEME

- 3.7 The long-term business involved in the Scheme can be divided into the following three categories: with-profits business, unit-linked business and conventional non-profit business and I summarise the key points below.

##### With-profits business

- 3.8 With-profits business refers to insurance business where policyholders are entitled to share in the surplus or profits that arise in the fund or funds of the insurer.
- 3.9 In general, the policyholder pays premiums which usually secure a minimum level of guaranteed benefit. This benefit or policy value is increased periodically through bonuses awarded at the discretion of the insurer depending on the surplus emerging in the relevant insurance fund and, once they have been awarded, bonuses are typically guaranteed. There is often a further bonus (a final or terminal bonus) payable at maturity, death or surrender. In some cases, a Market Value Reduction (“MVR”) may be applied to reflect poor investment conditions or other adverse experience.
- 3.10 It is typical for insurers to target policyholder pay-outs to be relatively close to the policy’s “asset share”, which is a measure of the true value of the policy based on actual investment returns and expenses incurred by the fund.
- 3.11 There are two main types of with-profits products:
- Conventional with-profits (“CWP”): CWP products have an initial sum assured that is increased by the addition of bonuses, declared as a percentage of the sum assured or the sum assured plus previously declared bonuses.
  - Unitised with-profits (“UWP”): UWP products operate similarly to unit-linked products (described below). The difference is in the way in which the company determines the price of the units (which

may involve some level of smoothing of returns at the discretion of the company) and therefore the benefits paid on maturity / death / surrender.

### **Unit-linked business**

- 3.12 Unit-linked business is principally a type of investment product where policyholders' premiums are used to buy units in investment funds. The value of the policyholder's units then moves in line with the performance of the investments in the fund. Charges are deducted from policyholders' premiums or from their units. At maturity, policyholders receive the value of their units.
- 3.13 Unit-linked products are often sold in the form of a pension savings vehicle with the product term running until retirement age. Examples include:
- Personal pensions: A personal pension is a tax-efficient investment vehicle which holds and builds up funds to provide retirement benefits. Tax relief is received on pension contributions paid by the individual and growth on investments is free from income and capital gains tax.
  - Stakeholder pensions: Stakeholder pensions were introduced in 2001 as a low-cost means to save for retirement. They are similar to personal pensions but are required to meet a number of conditions, including a cap on charges, low minimum contributions, and flexibility in relation to stopping and starting contributions.
  - Self-invested personal pensions ("SIPPs"): SIPPs operate in a similar manner to traditional personal pensions but allow individuals a higher degree of investment freedom and hence control. The charges can vary by type of SIPP, the underlying investments chosen and the level of trading conducted. As a general rule, the greater the degree of flexibility, the higher the cost.
  - Workplace pensions: Workplace pensions are arranged by employers, whereby a percentage of each employee's pay is put into a pension scheme. In most cases, the employer will also contribute. The accumulated savings will provide funds for employees in retirement and possibly other benefits, such as support to beneficiaries on death. There are two types of workplace pensions:
    - Group personal pensions / stakeholder pensions operate in a similar manner to the ones that can be arranged by individuals. The employer chooses the pension provider and acts as administrator but individual contracts will be set up between the employees and the provider.
    - Occupational pensions are trust-based schemes, established by employers and managed by trustees. Thus responsibility for investment and funding does not lie with the pension provider in this case. Trustee Investment Plans ("TIPs") are a product offered by insurers to trustees of occupational pension schemes that provide a mechanism for trustees to invest pension scheme funds in a tax-efficient way.
- 3.14 Unit-linked business can also include protection products. For example, life cover maybe be attached whereby a lump sum benefit equal to a fixed value is paid to the policyholder on maturity or earlier death. In this case, charges would apply to cover additional risk-based benefits.

### **Maturing with-profits and unit-linked savings products**

- 3.15 In the UK, with-profits and unit-linked pension products have, in the past, been sold with an attached guaranteed annuity option ("GAO"), whereby policyholders have the right at maturity to receive an annuity (described below under 'conventional non-profit business') calculated at a guaranteed rate. As an alternative to purchasing an annuity, unit-linked income drawdown business provides policyholders with flexible access to their savings, whereby the policyholder can cancel units and release their cash value when needed whilst the remaining savings continue to accumulate via the unit fund system.

### **Conventional non-profit business**

- 3.16 Conventional non-profit business refers to insurance business where the benefits received by policyholders are fixed in terms of monetary amount, for example a life insurance policy that pays a fixed death benefit or a pension annuity that, in return for a single premium (generally paid on retirement), pays a fixed annuity amount each year whilst the policyholder is alive.



## Individual Savings Accounts (“ISAs”)

- 3.17 Though not long-term insurance business, ISAs are worth mentioning in the context of this Scheme as they may invest in or be sold alongside life insurance products e.g. flexible mortgage ISAs.
- 3.18 ISAs combine investment in stocks and shares and cash savings and are subject to favourable tax treatment. The cash component operates much like a regular savings account, with the key distinction being that there is no tax charge on interest earned. Stocks and shares ISAs can potentially offer higher returns than cash ISAs and are typically recommended by investment advisers for longer-term investments.

## THE SOLVENCY II REGIME REQUIREMENTS

### Introduction

- 3.19 The current regulatory solvency framework for the EEA insurance and reinsurance industry (from 1 January 2016 onwards) is known as Solvency II and all but the smallest EEA insurance companies are required to adhere to the Solvency II regime.
- 3.20 The Solvency II regime is summarised in Appendix C of this report and I bring out below some of the features of the regime that are particularly important to understand in the context of the proposed transfer.

### The Solvency II capital requirements

- 3.21 Under Solvency II, assets are, broadly speaking, reported at market value.
- 3.22 A company’s liabilities are called the “technical provisions” which consist of the sum of the best estimate liabilities (the “BEL”) and the “risk margin”:
- The BEL is a market consistent<sup>1</sup> value of liabilities calculated by projecting the expected future obligations of the insurer over the lifetime of the contracts using the most up-to-date financial information (at the date of the valuation) and the best estimate actuarial assumptions. The BEL is the present value of these projected cash-flows.
  - The risk margin is an adjustment designed to bring the total 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.
- 3.23 The excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds. Own Funds can be thought of as the capital available in the company to cover capital requirements.
- 3.24 The Solvency Capital Requirement (“SCR”) 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%.
- 3.25 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.

### Regulatory approvals under Solvency II

- 3.26 Firms intending to use an Internal Model instead of the Standard Formula must apply to the regulator (the PRA in the UK) for approval to do so.
- 3.27 There are other adjustments to the technical provisions that may be made such as transitional measures, a matching adjustment and a volatility adjustment and approval for these must also be sought from the appropriate regulator. These adjustments are described in detail in Appendix C.

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<sup>1</sup> A market-consistent framework requires the values placed on assets and liabilities to be consistent with the market prices of listed securities and traded derivative instruments.



## Ring-fenced funds

- 3.28 Solvency II 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.
- 3.29 In the UK, many firms have set up ring-fenced funds in order to reflect the arrangements applicable to their with-profits funds (as defined under the previous regulatory regime) and the with-profits and non-profit business within the with-profits fund.

## THE REGULATION OF INSURANCE COMPANIES IN THE UK

- 3.30 LGAS and ReAssure are authorised by the PRA and regulated by the PRA and FCA in the UK.
- 3.31 The roles of the regulators are described in more detail in Appendix D of this report but in summary:
- The PRA is a part of the Bank of England and is responsible for the prudential regulation and supervision in the UK of banks, building societies, credit unions, insurers and major investment firms; and
  - The FCA regulates the conduct of all UK financial services firms in relation to consumer protection, market integrity and the promotion of competition in the interests of consumers.

## THE GOVERNANCE OF LONG-TERM INSURERS IN THE UK

- 3.32 The governance of long-term insurers in the UK is set out in more detail in Appendix D of this report but in summary:
- The Board of Directors of a proprietary long-term insurer 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.
  - Under Solvency II, all insurers are required to establish the following key functions:
    - Actuarial function: This function is required, inter alia, to coordinate the calculation of technical provisions, and to ensure the appropriateness of the methodologies, underlying models and assumptions used in the calculation of technical provisions.
    - Compliance function: This function is required, inter alia, to advise the insurer on compliance with the Solvency II regulations.
    - Internal audit function: This function is required, inter alia, to evaluate the adequacy and effectiveness of the insurer's internal control system and other elements of its system of governance. The internal audit function is required to be objective and independent from the company's operational functions.
    - Risk management function: This function is required, inter alia, to facilitate the implementation of the insurer's risk management system.
  - In addition to the roles listed above, those firms with with-profits business must:
    - Appoint an actuary (or actuaries) to perform the "with-profits actuary function" (the "WPA"). This individual's responsibilities include advising the firm's management on the discretion to be exercised in respect of the with-profits business of the firm.
    - Appoint a WPC (or a "with-profits advisory arrangement" if appropriate given the size, nature and complexity of the fund in question) in respect of the with-profits business. The WPC's role is to advise and provide recommendations to the firm's governing body on the management of the with-profits business, and to act as a means by which the interests of with-profits policyholders are appropriately considered within a firm's governance structures.

## **A FIRM'S RISK APPETITE AND INTERNAL CAPITAL POLICY**

- 3.33 The Board of an insurer is responsible for the management of the company and for 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 capital requirements.
- 3.34 In order to ensure that day-to-day fluctuations in markets and experience do not lead to a breach of their risk appetite and regulatory capital requirements, firms 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 internal capital policy.
- 3.35 The internal capital 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 the internal capital policy usually require Board approval and appropriate consultation with the relevant regulator (the PRA in the UK).
- 3.36 The capital 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 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 the capital policy.
- 3.37 The level of capital required may also be driven by the desire of the Board to maintain a particular credit rating with external credit rating agencies.

## **THE FINANCIAL SERVICES COMPENSATION SCHEME ("FSCS")**

- 3.38 The FSCS provides compensation (100% of the policyholder's entitlement) to individual holders of long-term insurance policies issued by UK insurers in the UK or another EEA state in the event of the insolvency of an insurer (the failure of that insurer to pay benefits). In the event of an insolvency, a call on the FSCS is covered by levies on the insurers in the UK insurance industry.

## **THE UK FINANCIAL OMBUDSMAN SERVICE ("FOS")**

- 3.39 The FOS is an independent public body that aims to resolve disputes between individuals and UK financial services companies, and may make compensation awards in favour of policyholders. Only holders of policies that constitute business carried on in the UK are permitted to bring complaints to the FOS. The FOS may direct UK financial services companies to pay compensation up to a maximum limit of £150,000 per claim.
- 3.40 The 'Dispute Resolution: Complaints' ("DISP") section of the FCA Handbook sets out the jurisdiction and scope of the FOS in the UK.

## 4. The role of the independent expert

### INTRODUCTION

- 4.1 Policyholders involved in UK insurance business transfers have four main layers of protection provided by the legal and regulatory system in the UK. These layers of protection are provided by:
- The UK regulators (the PRA and the FCA) as they:
    - Approve the appointment of the Independent Expert and the form of the Scheme Report;
    - Produce their own reports on the Scheme for consideration by the High Court;
    - Are entitled to appear in High Court; and
    - Approve the form of the notices which are published and sent to policyholders.
  - The Independent Expert. He/she produces the (publicly available) Scheme Report assessing the Scheme and an updated Supplementary Report for the Final Hearing.
  - The obligations placed on the companies to give notice of the proposed transfer to policyholders and other interested parties. Any person who considers they may be adversely affected by the Scheme may make a representation to the High Court.
  - The High Court. There are two High Court Hearings: the Directions Hearing and the Final (or Sanctions) Hearing. The High Court reviews the Scheme at the Final Hearing where the High Court also takes into account the views of the regulators, the Independent Expert, various statements by the parties to the transfer, and any objections raised by policyholders and other interested parties.
- 4.2 My role as Independent Expert, as the second layer of protection for policyholders described above, is to assess the Scheme and to report on this via the Scheme Report (this report and any supplemental reports) to the High Court. I set out below my significant areas of consideration in discharging this role.

### THE CONSIDERATIONS OF THE INDEPENDENT EXPERT

#### The regulatory requirements in respect of my role

- 4.3 The requirements in respect of my Scheme Report are set out in:
- The PRA Statement of Policy (paragraphs 2.27 to 2.40);
  - Paragraphs 31 to 41 of section 2 of SUP 18 of the FCA Handbook; and
  - The FCA Final Guidance described in Section 1.
- 4.4 My report complies with these documents.
- 4.5 In considering the Scheme, the concept of treating customers fairly should be applied. From the policyholders' perspective, the successful implementation of the Scheme must be on the basis that they are treated fairly during the process and will be treated fairly in the future.
- 4.6 As described in Section 1 of this report, the Scheme concerns two life insurance companies: LGAS and ReAssure. I need to consider the terms of the Scheme generally and how the different groups of policyholders of LGAS and ReAssure and the different generations of policyholders within the different groups are likely to be affected by the implementation of the Scheme. In particular I need to consider:
- The effect of the implementation of the 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 Scheme on the reasonable expectations of policyholders in respect of their benefits; and
  - The effect of the implementation of the Scheme on the standards of service, administration, management and governance applicable to the policies.
- 4.7 My considerations in respect of each of these areas are set out in more detail below.

- 4.8 In this report I have not restricted my assessment of the Scheme to adverse effects.
- 4.9 I am only required to comment on the effects of the implementation of the Scheme on policyholders who enter into contracts with LGAS and ReAssure prior to the date of the implementation of the Scheme which is expected to be the Legal Effective Date. I am not required to consider the effects of the Scheme on new policyholders entering into contracts after this date.
- 4.10 I am not required to consider possible alternative schemes and I have therefore only considered the terms of the Scheme presented to me.

### **The security of policyholder benefits**

- 4.11 As part of my role as Independent Expert for the Scheme, I need to consider the security of policyholder benefits, that is, the effect of the implementation of the Scheme on the likelihood that policyholders will receive their benefits when these are due.
- 4.12 The EU regulations require insurance 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.
- 4.13 Therefore, the amount by which the assets available to support the long-term insurance business exceed the long-term liabilities provides security for the benefits and security is also provided by other capital resources in the insurance company. As well as the amount of available capital, the quality of that capital is also an important consideration in the context of security of benefits.
- 4.14 The two life insurance companies involved in the Scheme have a different mix of policies and policyholders and 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 policyholders' risk exposure will be the characteristics of the company in which the policy is held such as the size of the company, the mix of different types of business, the amount and quality of capital resources available, and the internal capital policy and risk appetite of the company.

### **Policyholders' reasonable expectations in respect of their benefits and the levels of service received**

- 4.15 As Independent Expert I also need to consider the proposals in the context of the FCA's regulatory objectives and in particular the effect of the implementation of the Scheme on policyholders' reasonable expectations in respect of their benefits and the quality of the levels of administration, servicing, management and governance in respect of their policies.
- 4.16 This includes considering the effect of the implementation of the Scheme on areas where discretion is involved on behalf of the relevant insurance company with regard to the charges applied to a policy and the benefits (including with-profits bonuses) granted to the policyholder.

### **THE FRAMEWORK FOR THE INDEPENDENT EXPERT'S CONSIDERATION OF THE SCHEME**

- 4.17 The framework for my conclusions is a consequence of the High Court's consideration of prior schemes. In particular, principles stated by Evans-Lombe J. in *Re Axa Equity & Law Life Assurance Society plc and AXA Sun Life plc* (2001) (based on principles outlined by Hoffman J. in *Re London Life Association Limited* (1989)) are often used as the basis for the consideration of insurance business transfers by the Independent Expert and by the High Court.
- 4.18 In particular, Evans-Lombe J. stated in *Re AXA Equity & Law* 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 went on to state: "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 Scheme as a whole has been demonstrated.
- 4.19 As Independent Expert, my assessment of the impact of the implementation of the Scheme on the various affected policies is ultimately a matter of expert 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 of the effect on the policies.

- 4.20 A Scheme may have both positive and negative effects on a group of policies and the existence of detrimental effects should not necessarily imply that the High Court should reject the Scheme as the positive effects may outweigh the negative effects or the negative effects may be very small.
- 4.21 In order to acknowledge this inherent uncertainty, and to be consistent with the statements by the High Court noted above, the conclusions of the Independent Expert in relation to transfers of long-term insurance business are usually framed using a materiality threshold. If the potential impact under consideration is very unlikely to happen and does not have a significant impact, or is likely to happen but has a very small impact, then it is not considered to have a material effect on the policies.
- 4.22 The assessment of materiality will also take into account the nature of the potential impact so that, for example, the materiality threshold for a change that could have a direct financial impact on policyholders' benefits is likely to be lower than the materiality threshold for a change that does not have a direct financial impact.
- 4.23 This is the framework in which I undertake my consideration of the Scheme.

## RELIANCES OF THE INDEPENDENT EXPERT IN THIS REPORT

### The financial information in this report

- 4.24 Appendices A and B show the current (i.e. before the implementation of the Scheme) and pro-forma post-Scheme Solvency II balance sheets (including capital requirements) as at 31 December 2018 for LGAS and ReAssure and this financial information is used in the analysis of the effects of the implementation of the Scheme as set out in Sections 8 to 11.
- 4.25 In respect of this financial information:
- For LGAS, the risk margin and SCR have been calculated using LGAS's approved Partial Internal Model (the "LGAS PIM");
  - For ReAssure, the risk margin and SCR have been calculated using:
    - ReAssure's approved Partial Internal Model ("the ReAssure PIM") for the ReAssure Non-Profit Funds ("RNPF"), excluding the risks arising from the Risk Transfer Agreement currently in place between LGAS and ReAssure in relation to the transferring business (as described in Section 5 of this report) which are calculated using the Standard Formula, and
    - The Standard Formula for its existing with-profits funds.
- The ReAssure PIM would not immediately apply to the LGAS business transferring into the RNPF after the implementation of the Scheme. The Standard Formula would be used for this block of business until approval is granted by the PRA to use the ReAssure PIM. The exception to this is a small block of non-profit annuities transferring to the ReAssure Matching Adjustment ("MA") portfolio, for which ReAssure expects to use the ReAssure PIM for efficiency purposes subject to non-objection of the PRA.
- For the purpose of deriving the pro-forma post-Scheme balance sheet for ReAssure, the risk margin and SCR for the transferring LGAS business have been calculated using the Standard Formula;
  - The current and pro-forma post-Scheme balance sheets for LGAS are based on a recalculated Transitional Measure on Technical Provisions ("TMTP") value (rather than the PRA approved TMTP value) as this is believed to provide the most realistic and meaningful view of the Solvency II position; and
  - The current balance sheet for ReAssure includes a recalculation of the TMTP as at 31 December 2018 allowing for the PRA's approval of the ReAssure PIM. In addition, the pro-forma post-Scheme balance sheet for ReAssure is also based on a recalculated (rather than PRA approved) TMTP value to reflect the transferring business.
- 4.26 In addition, I have been provided with financial projections showing the expected path (if the Scheme were to be implemented) for the LGAS and ReAssure Group SCR coverage until 31 December 2022. The projection figures

are not disclosed in this report; however, I comment on the broad conclusions that may be drawn from these projections as part of my analysis of the effects of the implementation of the Scheme in Sections 8 to 11.

#### **The checks that have been carried out on the financial information**

- 4.27 I have not carried out an independent review of the financial information but:
- The reported Solvency II balance sheets as at 31 December 2018 (shown in Appendix A) have been subject to an external audit by PwC LLP for ReAssure and by KPMG LLP for LGAS (other than the PIM SCR results, which are out of scope of external audit) and approved by the respective Chief Actuaries, Audit Committees and Boards.
  - I have carried out a high level reconciliation of the pro-forma post-Scheme Solvency II balance sheets as at 31 December 2018 for LGAS and ReAssure, shown in Appendix B, back to the current Solvency II balance sheets for LGAS and ReAssure shown in Appendix A.

#### **The checks on the LGAS financial information**

- 4.28 The current Solvency II balance sheet for LGAS as at 31 December 2018 has been through a full standard reporting process, including a review by the LGAS Risk Function, and a review and opinion by the KPMG audit team. To derive the pro-forma post-Scheme balance sheet, a number of overlays have been applied by an actuary on the LGAS Part VII team, which have been checked by Legal & General Group reporting and capital actuaries, and reviewed by the LGAS Head of Consolidation, the With-Profits Finance Director and approved by the LGAS Chief Actuary.
- 4.29 The Standard Formula results for the transferring LGAS business that are used to produce the pro-forma post-Scheme balance sheet for ReAssure are based on the LGAS Standard Formula results as at 31 December 2018, which have been produced by the first line team, reviewed by the LGAS With-Profits Finance Director and subject to second line review.
- 4.30 The financial projections I have received from LGAS were produced as part of the 2018 Own Risk and Solvency Assessment ("ORSA") and have undergone the normal checking, review and governance required as part of this process.

#### **The checks on the ReAssure financial information**

- 4.31 The current Solvency II balance sheet for ReAssure as at 31 December 2018 has been through a full standard reporting process, including external review by PwC LLP and internal review by ReAssure's:
- Technical Provisions Committee; and
  - The Combined Technical Committee (a body responsible for the approval of external reporting including senior members from the Risk, Actuarial and Finance teams).
- 4.32 The pro-forma balance sheet for ReAssure has been reviewed by the ReAssure Head of Actuarial Reporting.
- 4.33 As part of my high level reconciliation of the pro-forma balance sheet for ReAssure back to its current Solvency II balance sheet, I have reviewed:
- The impacts of the interaction and diversification between the existing business of ReAssure and the transferring LGAS business;
  - The impacts of Scheme provisions relating to the attribution of Scheme costs, ongoing charges to policyholders and investment management agreements; and
  - The appropriateness of the Standard Formula capital requirements in respect of the risks of the transferring business.
- 4.34 I am satisfied that the above are reasonable.
- 4.35 The pro-forma post-Scheme TMTP for ReAssure has been recalculated:
- For the transferring LGAS With-Profits Fund business, using a proxy calculation to estimate the Solvency I Pillar 1 and Pillar 2 positions. This involves using an Economic Capital model developed by ReAssure (as described in Section 8 of this report) rather than relying on figures provided by LGAS

and including the With-Profits Insurance Capital Requirement ("WPICR") in the determination of the Solvency I Pillar 1 capital requirement.

- For the transferring business outside of the LGAS With-Profits Fund, using the existing methodology for the ReAssure Non-Profit Fund.

4.36 The financial projections I have received from ReAssure are internal estimates produced as part of preparatory work for an exploration of the IPO of shares in the ReAssure Group (see Section 12 for further information on the ReAssure IPO). The projections have been subject to the following governance:

- The projections underpin the five-year cash generation targets which have been signed off by and used by the RGP Board;
- Earlier versions of the projections were used for the business plan reviewed by the RML Board; and
- There has been internal review by the senior actuaries and the reporting accountants at ReAssure.

4.37 I have used these projections to draw broad conclusions on the expected path for the ReAssure Group SCR coverage if the Scheme were to be implemented and for this purpose I am satisfied that it is appropriate to rely upon this financial information.

### **Conclusion in respect of the financial information**

4.38 Given the level of external review and internal checking and governance to which the financial information has been subject, as well as my own high-level review and reasonableness checks, I am satisfied that it is appropriate to rely upon this financial information for the purpose of this report.

4.39 My Supplementary Report will contain financial information as at 30 June 2019 and will provide an update on the effect of the implementation of the Scheme based upon these figures.

### **My reliance on legal advice**

4.40 My report is prepared for the High Court as part of the process of submission of the Scheme to the High Court. I am not an expert in legal matters and hold no qualifications in UK law (insurance regulations or otherwise) and therefore rely on experts in UK insurance law in relation to a number of areas. In particular:

- I rely on a legal review of previous schemes involving LGAS and ReAssure (as described in Section 14) to ensure that there are no provisions in previous schemes that could, in conjunction with the implementation of the Scheme, result in a material adverse impact on policyholders; and
- I rely on advice given by legal experts in order to ensure that my understanding of the Scheme, and my description of its relevant features in my report, is materially accurate.

4.41 Obtaining information in respect of the operation of the Scheme from the legal experts provides a sound basis from which to carry out my review and analysis using actuarial expertise.

4.42 In order to get a sound understanding of the legal effect of the Scheme, the options available to me are to retain my own legal adviser to carry out the relevant legal review, or to rely upon the advice and input of the legal firms retained by LGAS and ReAssure in respect of this Scheme, namely Slaughter and May and Herbert Smith Freehills. In this case, I consider that it is not necessary for me to obtain independent legal advice and that it is appropriate for me to rely upon the advice provided by Slaughter and May and Herbert Smith Freehills.

4.43 Slaughter and May and Herbert Smith Freehills have not been retained by me and Slaughter and May and Herbert Smith Freehills have no liability for any advice that has been made available to me in order to provide me with information that I consider relevant to my assessment of the effects of the Scheme.

4.44 My reasons for this reliance are:

- Slaughter and May and Herbert Smith Freehills are large international legal firms with a wide range of experience in UK insurance law and Part VII transfers and it is my view that they have the relevant and appropriate qualifications and knowledge of the laws and regulations governing insurance business transfers in the UK;

- The nature of the information and advice from Slaughter and May and Herbert Smith Freehills upon which I have relied is factual and in particular concerns how a particular aspect of LGAS or ReAssure (pre or post the implementation of the Scheme) works in accordance with UK law;
- The relevant legal matters do not appear to be contentious; and
- The fair treatment of policyholders is not dependent on the legal advice.

As such, I am satisfied that the advice or information given by Slaughter and May and Herbert Smith Freehills would not be different if they were retained directly by me in respect of the Scheme.

4.45 I am therefore satisfied that it is appropriate for me to rely on the conclusions of Slaughter and May and Herbert Smith Freehills in forming my view on the Scheme.



## 5. Background information regarding LGAS

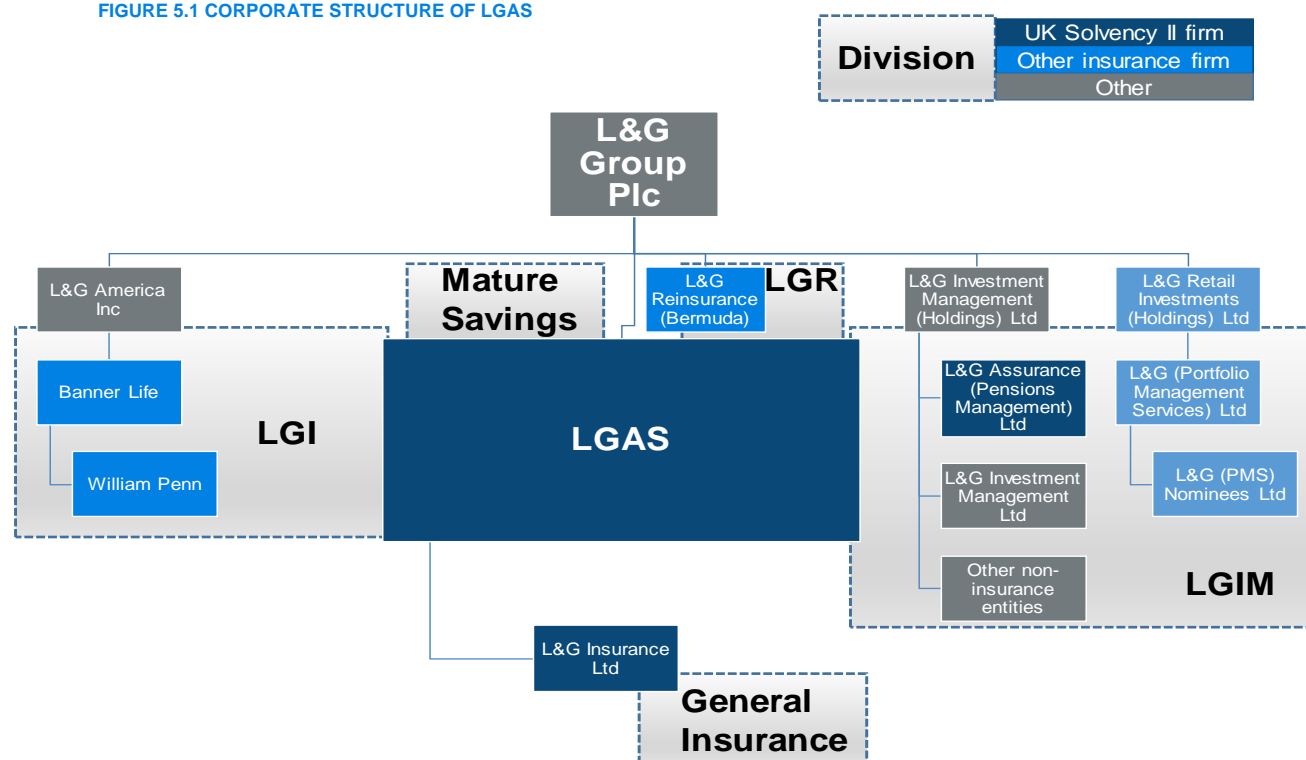
### INTRODUCTION

- 5.1 LGAS is a proprietary composite insurance company that was founded in 1836. It is an indirectly held subsidiary, and the principal operating subsidiary, of Legal & General Group plc, which is the holding company for the Legal & General Group (the “L&G Group”).
- 5.2 LGAS is authorised under the terms of FSMA to undertake long-term insurance business in Classes I to IV, VI and VII set out in Part II of Schedule 1 to the Regulated Activities Order 2001, and to transact general insurance business.
- 5.3 LGAS is one of the largest providers of insurance products in the UK. LGAS policyholders do not acquire membership rights in LGAS by virtue of their policy.

### THE CORPORATE STRUCTURE OF LGAS

- 5.4 LGAS is a principal operating subsidiary of the L&G Group and is the regulated entity through which the majority of the Group's UK individual and group insurance, pension and annuity business is executed.
- 5.5 The L&G Group is managed using a divisional structure, rather than across legal entities, and comprises the following divisions:
- Legal & General Retirement (“LGR”);
  - Legal & General Investment Management (“LGIM”);
  - Legal & General Insurance (“LGI”);
  - General Insurance (“GI”);
  - Mature Savings; and
  - Legal & General Capital (“LGC”).
- 5.6 Business written within LGAS is managed by LGR, LGI, and Mature Savings. LGIM manages the majority of the LGAS workplace pensions business with the rest managed by the Mature Savings division and LGC manages the shareholder funds of LGAS. The GI Division business is written through a subsidiary of LGAS.
- 5.7 Within the L&G Group, and of particular relevance to this Scheme:
- Legal & General (Portfolio Management Services) Nominees Limited (“PMS Nominees”) is the trustee of the SIPP Scheme and Legal & General (Portfolio Management Services) Limited (“PMS”) is the operator;
  - Legal & General (Unit Trust Managers) Limited (“UTM”) invests and manages the ISA business of LGIM; and
  - theidol.com is a financial technology company that is a subsidiary of the L&G Group that operates as an online comparison tool for life, travel and pet insurance, helping customers to get better value insurance products.
- 5.8 A simplified Group structure is shown in Figure 5.1 below. The chart summarises the relationship between entity and divisional responsibilities on a forward-looking basis.

FIGURE 5.1 CORPORATE STRUCTURE OF LGAS



## THE TRANSFERRING BUSINESS

- 5.9 The transferring business is currently predominantly within the LGAS Mature Savings division and includes unit-linked life and pension products, with-profits business, non-profit annuities linked to with-profits annuities, and a small volume of SIPPs. It can be broadly split into two parts: the “transferring non-profit business” and all of the business within the LGAS With-Profits Fund (the “LGAS WPF business”).

### The transferring non-profit business

- 5.10 The transferring non-profit business includes non-profit retail life and pension products.
- 5.11 The life products include:
- Single premium unit-linked bonds;
  - Regular premium savings plans;
  - Unit-linked protection; and
  - The term assurance component of the LGAS Flexible Mortgage Individual Savings Accounts (“FMISAs”).
- 5.12 The pension products include:
- Stakeholder pensions;
  - SIPPs;
  - Corporate TIPs;
  - Non-profit annuities that are currently administered in conjunction with with-profits annuities in the LGAS WPF; and
  - Legacy / other pensions.
- 5.13 The products were all closed to new business by the end of 2018, although increases to existing pension policies are allowed, and existing pension schemes are open to new members.

5.14 The table below summarises the in-force transferring non-profit business at 31 December 2018.

**TABLE 5.1 BREAKDOWN OF THE TRANSFERRING NON-PROFIT BUSINESS AT 31 DECEMBER 2018**

BUSINESS LINE	NUMBER OF POLICIES ('000)	BEL (£ MILLION)
Unit-linked life - savings	130	6,450
Individual protection - savings	59	69
Unit-linked life - assurance	30	133
Unit-linked pensions	72	3,404
Non-linked life	22	(2)
Non-linked pensions	1	5
Non-profit annuities	2	27
<b>Total</b>	<b>316</b>	<b>10,085</b>

### The LGAS WPF business

- 5.15 The LGAS WPF is a ring-fenced fund as defined under Solvency II. Under the Scheme all of the LGAS WPF business would be transferred to ReAssure.
- 5.16 The LGAS WPF business includes the LGAS with-profits business and any associated non-profit business. Where policies have the right to invest in both with-profits and linked savings pools, the policies are allocated to the LGAS WPF, even if there is no actual with-profits investment, and the linked investment portion is managed in line with other linked products.
- 5.17 With-profits policies in the LGAS WPF span a range of UWP and CWP business, and include:
- Life insurance policies, including bonds, mortgage endowments and other endowments;
  - Individual and group pensions policies;
  - With-profits annuities; and
  - Immediate and deferred annuities.
- 5.18 Non-profit policies (or non-participating policies) in the LGAS WPF include life and pensions business, typically unit-linked policies with an option to switch into UWP, or annuities derived from with-profits policies.
- 5.19 Each year, the Board decides the amount of profits arising from the LGAS WPF business that may be distributed to those entitled to a share. Profits are distributed such that not less than 90% is distributed to with-profits policyholders by means of bonuses, with the remainder distributed to shareholders.
- 5.20 The LGAS WPF was formally closed to new business on 31 January 2015. Only increases to existing pension policies and new members to existing group personal pension schemes, where allowed for in the policy terms and conditions, have been accepted after that date. Following the closure to new business, a formal run-off plan has been developed for the LGAS WPF.
- 5.21 The table below summarises the in-force LGAS WPF business at 31 December 2018.

**TABLE 5.2 BREAKDOWN OF THE TRANSFERRING LGAS WPF BUSINESS AT 31 DECEMBER 2018**

BUSINESS LINE	NUMBER OF POLICIES ('000)	BEL (£ MILLION)
UWP life	97	3,680
UWP pensions	170	4,058
CWP life	24	205
CWP pensions	29	844
With-profit annuities	8	361
Unit-linked	361	8,777

Other non-participating	2	189
Total	682	17,753

## THE NON-TRANSFERRING LGAS BUSINESS

5.22 The LGAS business that is not transferring consists of:

- LGR: Business written through the LGR division includes worldwide pension risk transfer business in LGR Institutional (“LGRI”), and individual retirement business in LGR Retail (“LGRR”).
- LGI: Business written through the LGI division includes UK retail and group protection business, and US protection business reinsured into LGAS from fellow Group subsidiaries in the US. LGAS also accepts a tranche of the weather catastrophe risk reinsurance placed by its general insurance subsidiary, Legal & General Insurance Limited (“LGIL”).
- A range of workplace pension solutions that focus on UK auto-enrolment schemes (the “Workplace Savings” business) written through the LGIM division.

## THE SALE OF THE TRANSFERRING BUSINESS TO REASSURE

### Introduction

5.23 On 6 December 2017, the L&G Group announced that it intended to sell part of its long-term insurance business to ReAssure. The business that it was intending to sell is the transferring business as defined in the Scheme.

5.24 The transferring business consists of traditional insurance based pensions, savings and investment products, sold primarily to the retail market, and includes both unit-linked business, and the LGAS WPF business. The transferring business has largely been closed to new business and in run-off since 2015, and consists of approximately 1.0 million policies, as described earlier in this section.

5.25 The main reason for the sale was that the LGAS traditional insurance-based savings, pensions, life and with-profits business was largely closed to new business since 2015 and it would therefore reduce the risks to LGAS arising from servicing a largely closed book of business and allow it to accelerate its growth in its core business areas of writing and acquiring blocks of annuities through LGR, investment management through LGIM, and insurance through LGI and LGIL.

5.26 Prior to the Scheme, a number of legal agreements were signed by L&G Group entities and ReAssure on 6 December 2017. These are:

- The Business Transfer Agreement (the “BTA”);
- The Risk Transfer Agreement (the “RTA”);
- The Investment Management Agreement (the “IMA”); and
- The Annuity Introducer Agreement (the “AIA”).

5.27 The IMA and the AIA would only come into force if the proposed Scheme were to be implemented and these are covered in Section 7 where the proposed Scheme is described in detail.

### The Risk Transfer Agreement (the “RTA”)

5.28 As part of the sale of the transferring business to ReAssure, on 6 December 2017, LGAS entered into an agreement with ReAssure (the RTA), the objective of which was to transfer most of the economic interest together with the associated risks of the transferring business to ReAssure from 1 January 2018 (the “Economic Transfer Date”). The RTA also contains provisions that apply to the purchase price and payments should the Scheme not occur which depend on the nature of the termination.

5.29 Under the RTA:

- ReAssure paid an advance claim amount to LGAS on 4 January 2018 equal to the agreed purchase price of the transferring business. This amount is not refundable if the Scheme does not occur;

- The mortality and morbidity risks under the unit-linked policies within the transferring non-profit business (“the reinsured liabilities”) are reinsured to ReAssure; and
- The profits (losses) on the transferring business, calculated according to agreed terms and net of claims in respect of the reinsured liabilities, are transferred to ReAssure on prescribed settlement dates.

5.30 Expense risk relating to the transferring non-profit business remains with LGAS (until the Economic Effective Date) such that any deviation in per-policy expenses from that assumed within the Solvency II BEL is paid by LGAS as well as any additional exceptional items that ReAssure has not agreed to pay. The operational risk associated with managing the transferring business is also retained by LGAS.

5.31 The transferring non-profit annuities that are currently administered in conjunction with with-profits annuities in the LGAS WPF are not within the scope of the RTA.

### **The Business Transfer Agreement (the “BTA”)**

5.32 The BTA sets out the following:

- The terms under which the assets and liabilities associated with the transferring business (excluding non-profit annuities as described below) will be transferred to ReAssure:
  - The liabilities associated with the Pensions Review, the Endowment Review, the Legacy Review and the Whole of Life Review (described in paragraphs 5.81 and 5.82) would transfer in full to ReAssure;
  - Certain capped indemnities are provided by LGAS for liabilities in relation to systemic mis-selling or mal-administration prior to 1 January 2018 (the Economic Transfer Date), which will be shared between LGAS and ReAssure according to a defined formula for a period following the transfer with LGAS’s total liability capped at £97 million;
  - LGAS also agrees to retain any liabilities in relation to:
    - Regulatory fines or penalties arising from actions or omissions of LGAS in respect of the transferring business prior to the Economic Effective Date;
    - Taxes attributable to LGAS in connection with the transferring business relating to the period prior to the Economic Effective Date; and
    - Mis-selling prior to the Economic Effective Date of any annuity sold by LGAS on the maturity of any policy that is included within the transferring business.
- Certain conduct of business restrictions relating to LGAS’s operation of the transferring business during the period between the Economic Transfer Date and the Economic Effective Date (the “Interim Period”).
- That ReAssure will take over the administration of the majority of the transferring business following the Legal Effective Date and that it shall use its reasonable endeavours to administer the transferring business:
  - For the first year following the Legal Effective Date, in the same manner in which it was administered in the year prior to the date the BTA became effective; and
  - Thereafter, to a standard at least equivalent to the level provided by ReAssure in relation to its other business.
- The general principles that LGAS and ReAssure will adhere to in relation to the separation of the transferring business from LGAS’s non-transferring business and migration to ReAssure. This includes the following:
  - Information relating to the migration of data from LGAS’s IT systems to those of ReAssure;
  - Product rationalisation changes;
  - The splitting of certain assets and insurance contracts between transferring and non-transferring business; and

- The apportionment of costs between LGAS and ReAssure.
- Provisions for the intended separation plan, the associated projects (the first being an in-depth discovery phase), the testing arrangements and minimum acceptance criteria for the separation and migration, and the migration targets to ascertain the operational readiness of LGAS and ReAssure (for example, complaints volume and handling metrics).
- The governance arrangements for the business transfer.
- Contingency arrangements in case the Part VII transfer of the business from LGAS to ReAssure incurs any delays or it is not approved by the High Court.

#### **The BTA Amendment Agreement (the “BTA side-letter”)**

- 5.33 The BTA side-letter is an amendment to the BTA to address additional items that have been agreed since the initial BTA was signed. In particular:
- The transfer of a block of non-profit annuities that are currently administered in conjunction with the with-profits annuities in the LGAS WPF to the RNPF;
  - The payment of consideration by ReAssure to LGAS in respect of the unit-linked box to be transferred to ReAssure under the Scheme;
  - The amendment of definitions of “Assumed Liabilities” and “Excluded Liabilities” to include ReAssure’s product changes (described in Section 9 of this report) within the scope of those definitions in the BTA;
  - The principles governing the terms on which ReAssure and LGAS shall agree to correct the physical storage media (the “Scheme USB”) pursuant to the terms of the Scheme;
  - An amendment to ensure that the tax payable by the new Legal & General With-Profits Fund (“LGWPF”) in ReAssure for the year in which the transfer occurs is determined such that there is no financial impact on the amount tax paid as a result of the Scheme; and
  - Minor updates relating to specific contract points, human resource matters covered in the original BTA, intellectual property rights and miscellaneous items.
- 5.34 At the time of writing this report, the BTA side-letter has yet to be finalised and I shall comment further on the contents of the BTA side-letter in my Supplementary Report.

### **OTHER RECENT RELEVANT EVENTS FOR LGAS**

#### **Transactions**

- 5.35 In May 2016, LGAS agreed to acquire approximately £3 billion of non-profit annuity liabilities from Scottish Equitable plc. This business was subsequently transferred into LGAS in September 2017.
- 5.36 The business from this acquisition will not be transferring under the Scheme that is the subject of this report.

#### **Pension buy-ins / buy-outs**

- 5.37 The L&G Group has arranged a number of large pension buy-in and buy-out schemes and the assets and liabilities in respect of these buy-in and buy-out schemes will be kept in LGAS. The more recent such transfers include a £325 million buy-in with the BAA pension scheme, announced in June 2018, a £4.4 billion buy-in of part of the British Airways pension scheme, announced in September 2018, and a £2.4 billion buy-out with the Nortel Networks pension scheme, announced in October 2018.
- 5.38 The pension scheme buy-in and buy-out transactions are not included in the business that would be transferred to ReAssure under the Scheme.

#### **The transfer of pension scheme liabilities**

- 5.39 On 4 January 2018, the LGAS WPF made a one-off payment to the shareholder fund in exchange for the removal of all future obligations from the LGAS WPF in respect of both deficit repair contributions and on-going trustee expenses for the L&G Group UK Pensions & Assurance Fund and the L&G Group UK Senior Pension Scheme.

### **The LGAS WPF fixed expense agreement**

- 5.40 The LGAS shareholders and the LGAS WPC on behalf of the LGAS WPF have agreed to cap the expense exposure of the LGAS WPF until 30 June 2019. If the Scheme has not been implemented by the end of 2019 then the expense terms would be renegotiated.
- 5.41 The maintenance expenses that will be charged to the LGAS WPF for in-force policies are fixed at the sum of £35.5 million and a per-policy expense amount for the maintenance expenses relating to any new business entered into for 2018. Shortly after the end of 2018, this cap will be translated into an equivalent per-policy expense schedule which will then be used to determine the maintenance expenses to be charged during 2019.

### **The LGAS Funds Foundation Project**

- 5.42 The Funds Foundation Project was concluded in 31 January 2019 having been approved by the LGAS Board in April 2017 and had the objective to separate the assets of the unit-linked pension funds between those held in respect of non-transferring Workplace Savings policies and those held in respect of the transferring policies. This division of the unit-linked funds included the division of the LGAS pension property fund which involved the allocation of approximately 50 directly held properties between the transferring and non-transferring business.
- 5.43 The Fund Foundation Project is not part of the Scheme but it was accelerated in order to ensure that the separation of transferring unit-linked funds from the non-transferring unit-linked funds would be complete in advance of the Legal Effective Date.

### **Platform charges for SIPP policies**

- 5.44 The SIPP business includes approximately 490 SIPP policies (out of approximately 7,000 SIPP policies in total) that currently have collective investments on the Aegon platform which provides various benefits and flexibility.
- 5.45 The terms and conditions for the Aegon platform specify that a charge will be made for the use of the platform but the charge is not disclosed in the SIPP terms and conditions and is not currently taken from the SIPP policies on the platform in all cases.
- 5.46 Approximately 40 of the 490 SIPP policies have their collective investments administered via the SIPP trustee and have not signed up to the platform terms and conditions, and therefore the platform charge has not been visible to them. The other 450 policies (the "affected SIPP policies") have had sight of the charge, and the charge has been deducted where it can be taken from other products held by the same policyholder on the platform; however, in some cases it has not been possible to take the charge since the inception of the affected SIPP policies.
- 5.47 Aegon has served notice on these SIPP policies which would mean that the assets invested on the platform would be liquidated, however, Aegon has agreed that if it can take the charge going forwards then Aegon would continue to provide an equivalent platform offering and would waive the charge accrued to date.
- 5.48 It is proposed that a change will be made to the SIPP product terms and conditions to allow the platform charge to be applied for the 450 affected SIPP policies and that, for reasons of practicality and efficiency, this change will be made following the transfer of the SIPP policies to the ReAssure Group.
- 5.49 Though not part of the Scheme or a direct consequence of the Scheme, the change will be communicated to policyholders as part of the communications regarding the Scheme, rather than in a separate policyholder mailing.

## **LGAS'S REINSURANCE AGREEMENTS**

### **Internal reinsurance**

- 5.50 A proportion of the annuity business within the LGR division is reinsured to Legal & General Reinsurance ("L&G Re"), the Bermuda-based global reinsurance hub of the L&G Group.
- 5.51 A significant amount of the unit-linked funds in LGAS are reinsured to Legal & General Assurance (Pensions Management) Limited ("PMC"), a UK insurance company within the LGIM division.

### **External reinsurance**

- 5.52 LGAS operates an approved list of external reinsurers and typically uses external reinsurance in respect of longevity and mortality risk. The exposure to the reinsurers on this list is monitored by the Group Credit Risk Committee.



- 5.53 In relation to the transferring business, LGAS currently has reinsurance (for specific products, as distinct from the RTA) in place with the Swiss Re Group.

## **SOLVENCY II FOR LGAS**

- 5.54 At the time of writing, LGAS has the following PRA approvals:
- Approval to use a MA for its immediate annuity business;
  - Approval to use a TMTP; and
  - Approval to use the LGAS PIM. This approval was granted alongside similar approvals for other entities within the L&G Group (LGIL and PMC) and the L&G Group as a whole (for the calculation of the Group SCR). Since this time, the PRA has approved several major changes to the LGAS PIM.
- 5.55 As described in Section 3 of this report, the PRA reserves the right to remove approvals granted to UK Solvency II regulated entities for the use of any of these measures.

## **THE LGAS RISK APPETITE STATEMENTS**

- 5.56 To support its overall objective for capital, the Board of LGAS has established a quantitative risk appetite statement (the “LGAS RA Statement”) for its solvency coverage ratio on a Solvency II basis. The LGAS RA Statement is part of the L&G Group Capital Management Framework and is currently articulated as follows:
- LGAS aims to maintain a solvency coverage ratio above the “LGAS RA Statement level”, which it considers a ‘green’ range within which it will pursue its strategic objectives;
  - LGAS considers an ‘amber’ range to be the range from the “LGAS RA Statement lower bound” to the LGAS RA statement level where LGAS would review and take management actions to return the LGAS solvency coverage ratio to green within three years; and
  - If the solvency coverage ratio falls below this amber range, this would be considered ‘red’ and at this point more substantive management actions would be taken.
- 5.57 In the normal course of business, to meet other commercial objectives, including demonstrating financial strength to potential pension risk transfer counterparties and rating agencies, LGAS seeks to maintain a solvency ratio above the LGAS RA Statement level at the “LGAS RA operating level” which provides a reasonable buffer over the ‘green’ risk appetite threshold and avoids the need to frequently consider the need for management actions. LGAS will consider capital releases in respect of amounts which take the coverage ratio above this LGAS RA operating level to be available to be paid as a dividend.
- 5.58 The LGAS solvency coverage ratio is monitored on a weekly basis, with formal reporting to the LGAS Board on a monthly basis.
- 5.59 A review of the LGAS RA Statement is carried out as part of the annual ORSA process and is linked to the business planning process. If changes are recommended as part of such a review these need to be approved by the LGAS Board. These changes would be reported to the PRA as part of the ORSA process.
- 5.60 In addition, the LGAS WPF has a separate risk appetite statement (the “LGAS WPF RA Statement”) to which it is managed, within the constraint of not breaching the LGAS RA Statement. The LGAS WPF should be managed:
- With the aim of maximising returns to policyholders subject to an appropriate degree of investment risk;
  - In accordance with the PPFM, with the objective of ensuring that its assets are sufficient to meet its liabilities and regulatory capital requirements without the need for additional capital from outside the LGAS WPF; and
  - To target a minimum solvency coverage ratio on a Solvency II basis of 100%, and a solvency coverage ratio on an Economic Capital basis of between 100% and 110%.
- 5.61 Since 31 December 2017, various actions have been taken to improve the solvency of the LGAS WPF including:
- The transfer of pension scheme risk out of the LGAS WPF (effective on 1 January 2018);
  - Revisions to the Pensions Review reserve to remove areas of prudence; and



- Developments and adjustments to the financial reporting models for the LGAS WPF business.

## **THE ADMINISTRATION AND SERVICING OF THE LGAS POLICIES**

- 5.62 The LGAS policies are administered and serviced using the LGAS administration platforms.
- 5.63 The administration of Defined Benefit (“DB”) pension schemes within the LGAS WPF is outsourced to Deloitte.

## **GOVERNANCE IN LGAS**

### **The LGAS Board and the L&G Group Board committees**

- 5.64 Governance in LGAS is carried out by the Board, which delegates certain matters to the following committees of the L&G Group Board:
- The Group Risk Committee; and
  - The Group Remuneration Committee.
- 5.65 The LGAS Board itself has eight committees to assist it in the management of its with-profits, savings and workplace pension businesses, as described below.

### **The LGAS Audit Committee**

- 5.66 The primary responsibility of the LGAS Audit Committee is to assist the LGAS Board in discharging its responsibilities with regards to monitoring the integrity of the Company’s financial statements, the effectiveness of internal control and the independence and objectivity of the internal and external auditors.

### **The With-Profits Management Committee (“WPMC”)**

- 5.67 The WPMC is chaired by the Chief Executive Officer (“CEO”) of the Mature Savings division. It meets monthly and is responsible for the oversight of the management of the LGAS WPF. The WPMC does not have any independent members.
- 5.68 The CEO, Finance Director, Commercial Director and Chief Operating Officer of the Mature Savings division, and the Chief Actuary are all members. The WPA, the Chief Risk Officer of the Mature Savings division, and the L&G Group Legal Manager are all standing attendees.
- 5.69 The WPMC has delegated certain investment management functions to the With-Profits Assets and Liabilities Committee (“ALCO”), a sub-committee of WPMC. In addition, the WPMC will occasionally establish sub-committees to fulfil ad-hoc functions.

### **The WPC**

- 5.70 The WPC is chaired by an Independent Chairman and is comprised of four members, two of which are independent. It meets every other month and provides independent oversight of the management of the LGAS WPF. As well as independent members, a number of key internal stakeholders are standing attendees. These include the WPA, the CEO, the Finance Director and the Chief Risk Officer of the Mature Savings division.
- 5.71 The LGAS Board considers the reports and minutes from the WPC meetings at each Board meeting. At certain times of the year, for example the annual bonus declarations and the reviews of PPFM compliance, the LGAS Board specifically considers issues in respect of with-profits business. Any such issues in respect of with-profits business will have been previously considered by the WPC.
- 5.72 Each year the Chairman of the WPC makes a formal presentation to the LGAS Board on the activities of the WPC.

### **The Unit-Linked Management Committee (“ULMC”)**

- 5.73 The ULMC meets bi-monthly and is chaired by the Finance Director of the Mature Savings division. The ULMC provides oversight of the management of the LGAS unit-linked funds. The minutes of the ULMC meetings are provided to the LGAS Board. The Chief Actuary is a member, and the Head of Conduct Risk and Governance (a

delegate of the Chief Risk Officer) and the Head of Internal Client Services for LGIM are both standing attendees. The ULMC does not have any independent members.

5.74 The minutes of the ULMC are provided to the LGAS Board.

5.75 The Fund Performance Committee ("FPC") is a sub-committee of the ULMC, which oversees that investment of policyholder assets is fair, compliant and in line with customers' reasonable expectations and monitors investment performance.

#### **The Fund Risk Oversight Committee ("FROC")**

5.76 The FROC provides oversight of the management of the company's unit-linked funds for Workplace Savings products.

#### **The Independent Governance Committee ("IGC")**

5.77 The IGC meets six times per annum, is chaired by an Independent Chairman, and is comprised of a majority of independent members. It provides oversight of the LGAS workplace pension products and in particular assesses the ongoing value for money for relevant policyholders.

5.78 The IGC produces an annual report to the LGAS Board. The minutes and key discussion points from the IGC meetings are also provided to the Board.

#### **The Pricing, Investment and Capital Committees ("PICCs")**

5.79 Oversight of underwriting and reinsurance by the actuarial function is provided through the membership of divisional PICCs. Reports are produced for each business division on underwriting and reinsurance and the actuarial function then provides its reports on these areas to the Board.

#### **The Risk and Compliance Committee ("RCC")**

5.80 Each of the divisional CEOs has established committees to assist them in the management of risk and compliance, with escalation as appropriate to the Group Risk Committee.

#### **ONGOING REVIEW WORK**

5.81 LGAS has completed a number of specific reviews as set out below:

- The Pensions Review, which is the LGAS review and actions in relation to the industry-wide review of sales of personal pension policies taken out between 29 April 1988 and 30 June 1994;
- The Endowment Review, which is the LGAS review and actions in relation to the review of endowment policies taken out between December 1999 and March 2006; and
- The Legacy Review, which is the LGAS review and actions in relation to FCA Guidance 'FG16/8 Fair treatment of long-standing customers in the life insurance sector'.

5.82 LGAS is still undertaking the Whole of Life Review, which is the LGAS review and actions in relation to unit-linked protection products as communicated to the FCA during 2015-2017 inclusive.

5.83 In March 2019, LGAS received a letter from the FCA on the findings of its review of LGAS's approach to with-profits management (the "With-Profits Thematic Review"). To address some of the points set out in the letter, LGAS subsequently sent a number of mitigating actions and associated delivery dates to the FCA.

## 6. Background information regarding ReAssure

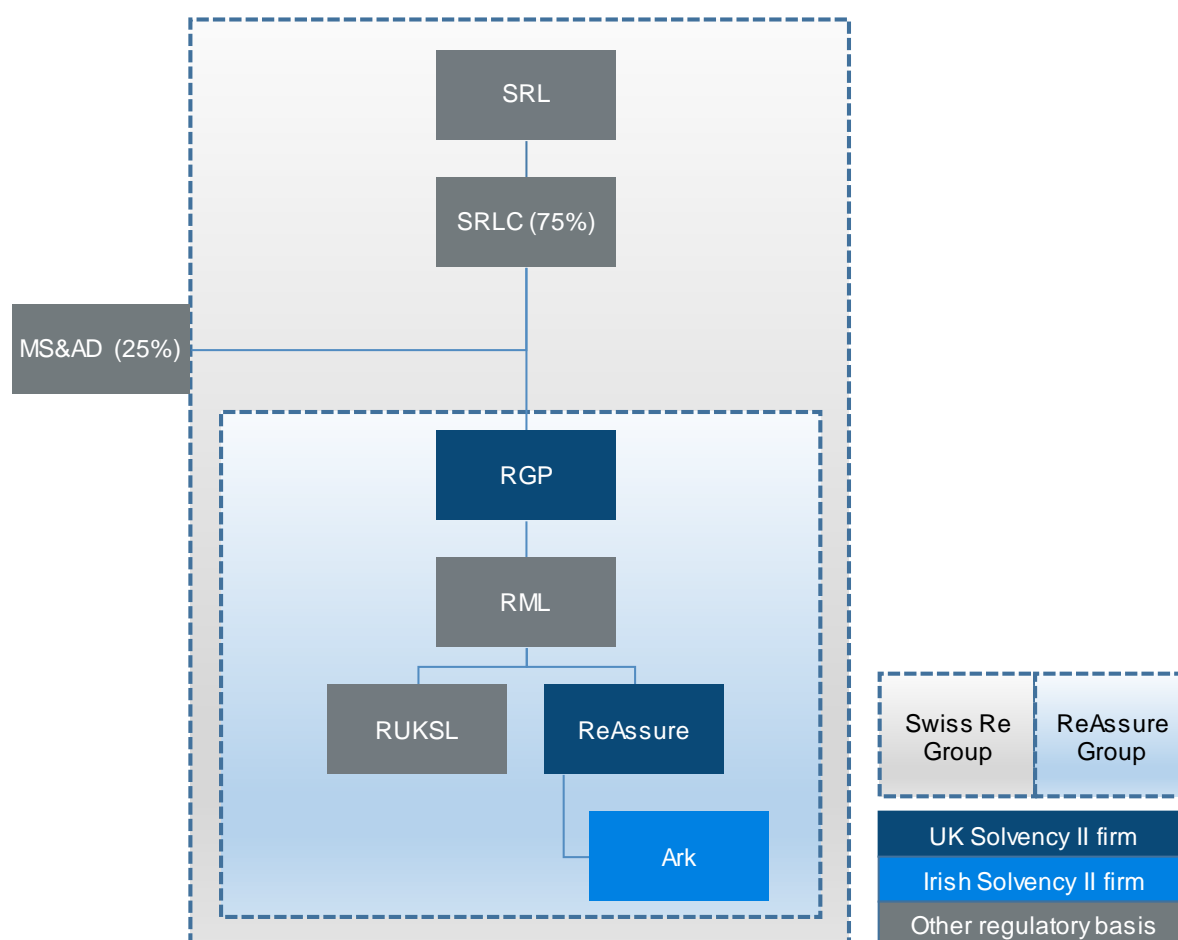
### INTRODUCTION

- 6.1 ReAssure is a proprietary insurance company whose immediate parent is ReAssure MidCo Limited (“RML”, formerly ReAssure Group Limited or “RAGL”). ReAssure is part of the Swiss Re Group: Swiss Re Life Capital Ltd (“SR Life Capital”) has a majority (75%) holding in ReAssure, and is in turn a wholly-owned subsidiary of Swiss Re Ltd, the ultimate holding company of the Swiss Re Group. Since February 2018, the Japanese insurance group MS&AD Insurance Group (“MS&AD”) has owned a minority stake in ReAssure through its (ultimate) holding in ReAssure Group plc (“RGP”), an intermediate holding company above RML in the wider Swiss Re Group. In February 2019, MS&AD’s stake increased from 15% to 25%.
- 6.2 ReAssure is authorised under the terms of FSMA to undertake long-term insurance business in Classes I to IV, VI and VII and general insurance business in Classes 1 and 2.
- 6.3 ReAssure’s business is based on the acquisition of closed blocks of in-force life insurance business, either through reinsurance agreements or by means of legal transfers of business, and creating value through efficient run off in the interests of policyholders and shareholders. This objective has led to ReAssure undertaking a large number of transfers of business since its first acquisitions in 1983.

### THE CORPORATE STRUCTURE OF REASSURE

- 6.4 A simplified ownership structure of ReAssure is shown in Figure 6.1 below.

FIGURE 6.1 SIMPLIFIED OWNERSHIP STRUCTURE OF REASSURE (SEE TEXT BELOW FOR ABBREVIATIONS)



6.5 The ReAssure Group comprises five main elements:

- RGP, the parent company;
- RML, an intermediate holding company;
- ReAssure, the UK life insurance company in the Group;
- Ark Life Assurance Company dac (“Ark Life”), an Irish life insurance company that became a subsidiary of ReAssure following the transfer of the business of ReAssure Life Limited (“RLL”, formerly Guardian Assurance Limited or “GAL”) to ReAssure in 2016 (the “RLL Scheme”); and
- ReAssure UK Services Limited (“RUKSL”), a company providing administration services to ReAssure and other life insurance companies outside the ReAssure Group.

## REASSURE’S CURRENT BUSINESS

### The ReAssure with-profits funds

6.6 ReAssure currently has three with-profits funds that are ring-fenced funds as defined under Solvency II. These are:

- **The Windsor Life With-Profits Fund (the “WLWPF”):**

This fund contains the with-profits business of the former Windsor Life Assurance Company Limited, which was renamed ReAssure in 2011.

The fund is closed to new business (apart from a small number of top ups to existing policies) and is being run so as to distribute its surplus assets over time as with-profits policies mature or otherwise discontinue.

With-Profits policyholders receive 90% of distributed profits through declared bonuses, with shareholders receiving the remaining 10%.

- **The National Mutual With-Profits Fund (the “NMWPF”):**

This fund contains the with-profits business and a small number of non-profit policies originally written by the National Mutual Life Assurance Society and transferred into ReAssure in 2007.

The fund is closed to new business (apart from a small number of top ups to existing policies) and is being run so as to distribute all its surplus assets over time to with-profits policies as they mature or otherwise discontinue.

The shareholders have no entitlement to any of the future surplus.

There is a capital support facility for the NMWPF (the “NM capital support facility”) where support is provided to the NMWPF if required by the ReAssure shareholder. The level of the capital support available was set at £200 million at the date the National Mutual Assurance Society demutualised and it has subsequently reduced in line with the run off of the NMWPF. As at 31 December 2018 it was £138 million.

- **The Guardian Assurance With-Profits Fund (the “GAWPF”):**

This fund contains the with-profits business originally written by GAL (later renamed RLL) and transferred into ReAssure under the RLL Scheme in 2016.

The fund is closed to new business (apart from a small number of top ups to existing policies) and is being run so as to distribute its surplus assets over time as with-profits policies mature or otherwise discontinue.

With-Profits policyholders receive 90% of distributed profits through declared bonuses, with shareholders receiving the remaining 10%.

6.7 The table below summarises the in-force ReAssure ring-fenced funds business as at 31 December 2018.

**TABLE 6.1 BREAKDOWN OF THE REASSURE RING-FENCED FUNDS BUSINESS AT 31 DECEMBER 2018**

BUSINESS LINE	NUMBER OF POLICIES ('000)*	BEL (£ MILLION)**
WLWPF	11	414
NMWPF	35	1,269
GAWPF	31	1,463
Total	77	3,146

\* For reporting purposes, some policies that have UWP investments are included in the policy count for the ReAssure Non-Profit Fund.

\*\*The BEL is shown gross of reinsurance.

### The ReAssure Non-Profit Fund (the RNPF)

6.8 ReAssure refers to all of its business outside the with-profits funds as the RNPF and I follow this convention in my report. The RNPF consists of the remaining long-term insurance business (the "RNPF LT business") and all other assets and liabilities of ReAssure outside of the with-profits funds, including Ark Life and other non-material subsidiaries of ReAssure.

6.9 The RNPF LT business consists of:

- Unit-linked life and pensions business;
- Non-profit annuity business; and
- Other non-linked non-profit protection and income business.

6.10 The RNPF includes a MA portfolio and a Volatility Adjustment ("VA") portfolio. The MA portfolio consists of in-payment annuities within the RNPF with the exception of some index-linked annuities and certain other minor product classes. The VA portfolio consists of:

- Most of the index-linked in-payment annuities within the RNPF;
- In-payment annuities within the RNPF that were transferred from the WLWPF; and
- The cost of guarantees associated with with-profits business in the with-profits funds.

6.11 The RNPF is open to new business; however, other than fulfilling obligations to existing policyholders, this only arises through transactions with third parties to acquire new books of risks, for example, portfolio reinsurance agreements.

6.12 The table below summarises the in-force RNPF LT business at 31 December 2018.

**TABLE 6.2 BREAKDOWN OF THE RNPF LT BUSINESS AT 31 DECEMBER 2018**

BUSINESS LINE	NUMBER OF POLICIES ('000)	BEL (£ MILLION)*
Unit-linked life and pensions	1,052	17,376
Non-profit annuities	771	13,753
Other conventional non-profit	123	242
Health fund	138	235
Total	2,084	30,945

\*The BEL is shown gross of reinsurance and excludes the impact of the Risk Transfer Agreement between LGAS and ReAssure (described below).

6.13 None of the subsidiaries of the RNPF contain any insurance business with the exception of Ark Life, the business of which is closed-book conventional non-profit and unit-linked business. As at 31 December 2018, the material lines of business were as follows:

- Index-linked and unit-linked life insurance;
- Other life Insurance; and
- Health insurance.

## **THE SALE OF THE TRANSFERRING BUSINESS TO REASSURE**

6.14 On 6 December 2017, the L&G Group announced that it intended to sell part of its long-term insurance business to ReAssure. The business that it was intended to sell is the transferring business as defined in the Scheme.

6.15 The transferring business consists of traditional insurance based pensions, savings and investment products, sold primarily to the retail market, and includes both non-profit unit-linked business, and the LGAS WPF business. The transferring business has largely been closed to new business and in run-off since 2015, and consists of approximately 1.0 million policies, as described in Section 5.

6.16 From ReAssure's point of view, the purchase is consistent with its strategy of growing through the acquisition of closed life books, and strengthens its market position in the UK.

6.17 Prior to the Scheme, a number of legal agreements were signed by LGAS and ReAssure on 6 December 2017. These are:

- The BTA;
- The RTA;
- The IMA; and
- The AIA.

6.18 The sale of the transferring business to ReAssure and the BTA and RTA legal agreements are described in more detail in Section 5.

6.19 The IMA and the AIA would only come into force if the proposed Scheme were to be implemented and these are described in Section 7 where the proposed Scheme is described in detail.

## **OTHER RECENT RELEVANT EVENTS**

### **The acquisition of Guardian Financial Services**

6.20 In January 2016, RML (previously RAGL) completed the acquisition of Guardian Financial Services Holdings UK Limited, the parent company of Guardian Companies Services Limited, RLL (then called GAL) and RLL's subsidiary Ark Life.

### **The Part VII transfer of some of the business of Phoenix Life Limited into ReAssure**

6.21 On 31 December 2016, a block of non-profit annuity business from three of the ring-fenced funds of Phoenix Life Limited ("PLL") was transferred into the RNPF (the "PLL Annuity Scheme"). PLL is one of the insurance companies within the Phoenix Group, which is not part of the Swiss Re Group or the ReAssure Group.

### **The RLL Scheme**

6.22 On 31 December 2016, immediately after the PLL Annuity Scheme was effected, the business of RLL was transferred into ReAssure. In particular:

- The policies within RLL's non-profit fund were transferred to the RNPF;
- The hybrid policies within RLL's with-profits fund were transferred to the RNPF and the UWP elements of these policies were linked to the newly created GAWPF; and
- The remaining policies in RLL's with-profits fund were transferred to the GAWPF.

6.23 Furthermore, under the RLL Scheme:

- The hybrid business within the WLWPF, and certain non-profit annuities, were reallocated from the WLWPF to the RNPF. The UWP elements of the hybrid business remained linked via an inter-fund agreement to the NMWPF;
- The annuities in RLL's MA portfolio were transferred into a newly created MA portfolio in ReAssure, separate from ReAssure's existing MA portfolio (these two MA portfolios were subsequently merged into a single MA portfolio at the end of 2018); and
- The business of RLL's VA portfolio was transferred into ReAssure's existing VA portfolio.

## THE RTA WITH LGAS

6.24 As described in Section 5, LGAS and ReAssure entered into the RTA on 6 December 2017. The RTA aims to transfer most of the economic interest and associated risks of the transferring business from LGAS to ReAssure from 1 January 2018. Expense risk relating to the transferring non-profit business remains with LGAS (until the Economic Effective Date) such that any deviation in per-policy expenses from that assumed within the Solvency II BEL is paid by LGAS as well as any additional exceptional items that ReAssure has not agreed to pay. The operational risk associated with managing the transferring business is also retained by LGAS.

6.25 The transferring non-profit annuities that are currently administered in conjunction with with-profits annuities in the LGAS WPF are not within the scope of the RTA.

## REASSURE'S REINSURANCE ARRANGEMENTS

### Internal reinsurance

6.26 ReAssure has a number of intra-group reinsurance agreements in place with Swiss Re Europe S.A. ("SRE") and Swiss Reinsurance Company Ltd ("SRZ"). These are all reinsurance agreements structured as longevity swaps and include the transfer to SRZ of all of the longevity risk on all of the annuities transferred into the RNPF from Zurich Assurance Limited in 2008 (other than the index-linked annuities).

6.27 Inter-fund arrangements are in place which link the UWP elements of hybrid investment business (under which policyholders can choose to invest their policies in both unit-linked funds and UWP funds) within the RNPF to the NMWPF or the GAWPF, so that the investment risk associated with the UWP elements is passed to the relevant with-profits fund.

6.28 Certain unit-linked business and certain benefits of with-profits deferred annuities that are written in the GAWPF are reinsured to the RNPF.

### External reinsurance

6.29 ReAssure has external reinsurance agreements (where ReAssure is the cedant) with RGA, Generali Worldwide Insurance Company Limited, Hannover Re, PartnerRe and Aegon.

6.30 These include the RGA longevity swap and Aegon original terms agreements for the in-payment pension annuity contracts that were transferred to ReAssure under the RLL Scheme in 2016.

## SOLVENCY II FOR REASSURE

6.31 ReAssure has approval to use the ReAssure PIM to cover all the risks of the RNPF, excluding those arising from the RTA. The three with-profits funds of ReAssure are out of scope of the PIM application and ReAssure currently uses the Standard Formula for the purpose of calculating its SCR for the with-profits funds.

6.32 ReAssure currently also has the following PRA approvals:

- Approval for a MA portfolio and a VA portfolio, as described in paragraph 6.10; and
- Approval to use a TMTP.
  - ReAssure has received approval from the PRA to recalculate its TMTP following receipt of approval to use the ReAssure PIM.

- ReAssure intends to submit an application to the PRA to recalculate the TMTP to reflect the transferring business, which is subject to approval.

## THE REASSURE RISK APPETITE STATEMENTS

### The current risk appetite statement

- 6.33 ReAssure's current risk appetite statement (the "ReAssure RA Statement") requires it to maintain sufficient excess capital resources to cover:
- The ReAssure SCR in respect of its with-profits funds; and
  - A solvency coverage ratio above the "ReAssure RA Statement level" subject to the discretion of the Board and the interaction of the ReAssure RA Statement with any specific capital margins required by the PRA.
- 6.34 In addition, the target capital buffer should not be less than ReAssure's exposure to the Swiss Re Group, measured as 50% of the decrease in Own Funds in excess of the SCR were the Swiss Re Group to default on its obligations to ReAssure.
- 6.35 The ReAssure RA Statement also requires that excess capital should be managed to within a range of the target capital. For the RNPF:
- If SCR coverage is between the ReAssure RA Statement lower bound and the ReAssure RA Statement level then the projected capital position is considered and, if necessary, ReAssure would take action to restore the capital position to the ReAssure RA Statement level;
  - If the SCR coverage, is below the ReAssure RA Statement lower bound then immediate management action would be taken to restore the capital position;
  - Any assets in excess of those required to maintain the ReAssure RA Statement level may be used to finance other strategic initiatives or (subject to non-objection from the PRA) distributed to shareholders; however,
  - If there were reliance on the TMTP to cover the SCR then dividend payments would be restricted.
- 6.36 The ability of the with-profits funds to meet their capital requirements is assessed taking into account any additional Board approved management actions that are not already reflected within the SCR calculation. In particular, past miscellaneous surplus that has been used to augment asset shares may be clawed back for each of the with-profits funds if required to protect the solvency position of the respective with-profits fund.
- 6.37 Should the ReAssure RA Statement be breached, the management actions taken to restore solvency to the required level depend upon the nature of the events causing the strain on the solvency position of ReAssure. Previous management actions have involved intra-group reinsurance agreements and monetisation of future unit-linked business profits, both of which aim to reduce the SCR and technical provisions.
- 6.38 If 'organic actions' are not projected to bring ReAssure into compliance with the ReAssure RA Statement in the required timeframe, then additional share capital would be requested from the Swiss Re Group. In these circumstances, where MS&AD's maximum funding commitment has been reached (as is the case after MS&AD increased its ownership of ReAssure to 25%), both the Swiss Re Group and MS&AD would have the opportunity to provide funding pro rata according to their respective shareholdings, and if either party elected not to fund its share the other shareholder would have the option to fund the full amount, which would increase its shareholding accordingly.
- 6.39 The ReAssure RA Statement may be reviewed upon any significant change affecting the business, such as an acquisition or material change to the regulatory requirements. Any changes are subject to Board approval and the PRA would be notified.

### The impact of the ReAssure IPO

- 6.40 On 3 August 2018, the Swiss Re Group announced that it was exploring a potential IPO of the ReAssure Group in 2019. In anticipation of a potential IPO, a new public parent company (i.e. RGP) has been set up, of which RML and ReAssure are now subsidiaries. The PRA has approved the Change in Control application for RGP.



- 6.41 On 14 June 2019, RGP confirmed its intention to proceed with the IPO. RGP intends to apply for admission of its ordinary shares to the premium listing segment of the official list of the FCA and to trading on the London Stock Exchange's main market for listed securities. RGP's expectation is that admission will take place in July 2019.
- 6.42 Such a strategic move clearly has the potential to have a significant effect on ReAssure in the near future and in particular to change the availability of parental capital support (this is currently provided by the Swiss Re Group and MS&AD) and the management and governance of the insurance business within ReAssure. Consideration of the ReAssure IPO is therefore relevant to my considerations regarding the Scheme.
- 6.43 Currently ReAssure relies on the Swiss Re Group in respect of a number of functions (including asset management and risk management). In preparation for the IPO work is underway to enable ReAssure to operate on a standalone basis.
- 6.44 ReAssure considers it unlikely that the IPO would affect the membership of the ReAssure Board or the ReAssure FC.
- 6.45 Prior to the ReAssure IPO, or if the ReAssure IPO does not proceed, the current ReAssure RA Statement will continue to operate. However, a new risk appetite statement (the "ReAssure IPO RA Statement"), which has been drafted and approved by the ReAssure Board, would apply on the implementation of the ReAssure IPO. This has also been approved by the (newly created) RGP Board.
- 6.46 The ReAssure IPO RA Statement is stronger than the current ReAssure RA Statement. It requires ReAssure to hold a higher level of capital resources at a level called the ReAssure IPO RA Statement level.
- 6.47 In addition to this:
- If a with-profits fund were unable to cover its SCR following a severe scenario after allowing for management actions, the RNPF would be required to hold additional capital to cover the shortfall;
  - If ReAssure relied on the TMTP to cover the SCR then dividend payments would be restricted;
  - The target capital buffer would be subject to a minimum amount based on ReAssure's largest counterparty exposure; and
  - Excess capital would be managed to be within a range of the target capital and this range would be the same as that currently used.
- 6.48 The increase in the severity of the event that ReAssure should be able to withstand and still meet its SCR from the ReAssure RA Statement level to the ReAssure IPO RA Statement level is based on the expectation that the expected speed at which ReAssure would be able to raise capital in adverse scenarios could be reduced after the ReAssure IPO compared to currently due to the change in parental support from the Swiss Re Group and MS&AD and the exposure of ReAssure to market willingness to provide capital.
- 6.49 The derivation of the ReAssure IPO RA Statement level is based on the output from the ReAssure PIM (as at 30 June 2018). ReAssure has advised that the target capital level under the ReAssure IPO RA Statement will be recalibrated as at 30 June 2019 and the level of the buffer would be reassessed annually after the IPO and after significant changes to the risk profile of ReAssure.
- 6.50 At the level of the public parent company, RGP would also have a target capital level (the "RGP buffer"). RGP would be subject to the further restriction that it must prioritise funding ReAssure to the level targeted under the ReAssure IPO RA Statement over dividend payments.
- 6.51 Any dividend payments made in advance of the IPO would make allowance for the buffer in the ReAssure IPO RA Statement.
- 6.52 My considerations in respect of the ReAssure IPO are set out in Section 12 of this report.

## **THE ADMINISTRATION AND SERVICING OF THE REASSURE POLICIES**

- 6.53 The administration and servicing for the majority of ReAssure policies is carried out by RUKSL. This is subject to a Management Services Agreement ("MSA") and fees are agreed on a per-policy basis, increasing in line with an external inflation index. RUKSL also currently has third party administration contracts to administer part of the business of Aviva, MetLife, and Genworth.
- 6.54 In addition:

- ReAssure has a MSA with HCL Insurance BPO Services Limited for business transferred from Barclays Life Assurance Company Limited in 2011; and
- The administration for the pension annuity business transferred under the HSBC Scheme in 2015 is included under the terms of the reinsurance agreement with Hannover Re.

- 6.55 BlackRock, Aberdeen Standard Investments (“ASI”) and Swiss Re Asset Management (“SRAM”) manage the majority of ReAssure’s non-profit, non-linked assets, with a number of smaller portfolios managed by other asset managers.
- 6.56 The majority of ReAssure’s unit-linked assets are managed by ASI. In addition, there are a number of direct unit-linked policyholder investment links into external collective schemes.
- 6.57 The assets of the WLWPF and NMWPF are managed by ASI, and the assets of the GAWPF are managed by BlackRock (with derivatives managed by SRAM).

## **MANAGEMENT AND GOVERNANCE IN REASSURE**

### **The ReAssure Board and the Board committees**

- 6.58 Governance in ReAssure is carried out by the Board, which delegates certain matters to the following ReAssure Group committees:
- The ReAssure Board Audit Committee;
  - The ReAssure Management Committee;
  - The ReAssure Board Risk Committee;
  - The ReAssure Group Management Risk Committee;
  - The ReAssure Fairness Committee; and
  - The Board Investment Committee.

### **The ReAssure Management Committee**

- 6.59 The purpose of the ReAssure Management Committee is to manage the ReAssure and its scope includes oversight of strategy, risk management and governance.
- 6.60 The ReAssure Management Committee is the primary body bringing together executive management and takes input from a wide range of other committees.

### **The ReAssure Board Risk Committee (the “ReAssure BRC”)**

- 6.61 The purpose of the ReAssure BRC is to ensure compliance with legal and regulatory requirements and oversee the development and implementation of the ReAssure Group entities’ internal control environments, including risk management and compliance frameworks.

### **The ReAssure Group Management Risk Committee (the “ReAssure GMRC”)**

- 6.62 The purpose of the ReAssure GMRC is to assist the ReAssure Board Audit Committee and the ReAssure BRC, and the executive management and respective Boards of Directors of ReAssure Group entities in the oversight of risk management activities.
- 6.63 An update was made to the ReAssure GMRC terms of reference in March 2019 to explicitly document the Chair’s responsibility to provide relevant information to the ReAssure WPA(s) and the ReAssure With-Profits Management Committee (see paragraph 6.67) in relation to with-profits issues.

### **The ReAssure Fairness Committee (the “ReAssure FC”)**

- 6.64 The main purpose of the ReAssure FC is to oversee the fair treatment of the policyholders within ReAssure and to act as the ReAssure WPC. It is therefore responsible for overseeing and challenging the management of ReAssure’s with-profits funds, as well as monitoring compliance with their respective PPFMs.

- 6.65 As and when significant transactions arise within ReAssure, it is the duty of the ReAssure FC to advise the ReAssure Board on the impact of such transactions and to monitor compliance with previous transfer schemes. The Scheme therefore falls within the remit of the ReAssure FC.

#### **The Board Investment Committee (the “ReAssure BIC”)**

- 6.66 The purpose of the ReAssure BIC is to recommend overall investment strategy, policy and asset allocation for the ReAssure Board. The committee also considers, and where appropriate sponsors or approves, recommendations made in relation to investment strategy, policy and strategic asset allocations.

#### **The Reassure With-Profits Management Committee (the “ReAssure WPMC”)**

- 6.67 The With-Profits Management Committee (the “ReAssure WPMC”) was set up in March 2019 to absorb the responsibilities of the now disbanded Technical Actuarial Treating Customers Fairly Committee (the “TATCF Committee”) in respect of with-profits business and provide executive oversight of the management of the ReAssure with-profits funds (including the LGWPF following the implementation of the Scheme).
- 6.68 The ReAssure WPMC incorporates the existing responsibilities of the LGAS WPMC and ALCO and its remit includes at least the following in respect of all of the ReAssure with-profits funds:
- Overall strategy and operations including annually reviewing compliance with the PPFMs;
  - Reviewing the financial position of the with-profits funds on a quarterly basis;
  - Reviewing the capital management position of the with-profits funds (on both a Solvency II Pillar 1 and Pillar 2 basis), including risk exposures;
  - Reviewing the estate distribution approach and developments;
  - Reviewing the investment strategy and, where relevant, hedging approaches and impacts of the with-profit funds;
  - Reviewing any other product related requirements such as any relevant conduct risk issues and policyholder communications.
- 6.69 The ReAssure WPMC includes members from the actuarial, finance, risk (including the Chief Risk Officer or “CRO”), asset management, compliance and products and proposition teams and meets on at least a monthly basis. It reports to the ReAssure Management Committee monthly and provides quarterly information to the ReAssure FC.

#### **The ReAssure Independent Governance Committee (the “ReAssure IGC”)**

- 6.70 The purpose of the ReAssure IGC is to review the value for money for policyholders of the ReAssure workplace personal pensions in relation to investment strategies, investment performance, fund charges and service standards.

#### **The ReAssure Policyholder Investment Committee (the “ReAssure PIC”)**

- 6.71 The purpose of the ReAssure PIC is to oversee that investment of policyholder assets is fair, compliant and in line with customers’ reasonable expectations.
- 6.72 In preparation for the proposed implementation of the Scheme, the ReAssure PIC terms of reference were updated in March 2019 to improve the transparency of its responsibilities by highlighting the asset management information requiring its review and challenge.

#### **The ReAssure Fund Performance Working Group (the “ReAssure FPWG”)**

- 6.73 The ReAssure FPWG terms of reference were approved in March 2019 and a schedule of monthly meetings is currently being set up.
- 6.74 The purpose of the ReAssure FPWG is to devote sufficient time and resource to reviewing policyholder fund performance in light of the proposed implementation of the Scheme, which would result in a larger fund range. It reports to the ReAssure PIC.

### **The Unit-Pricing Committee (the “ReAssure UPC”)**

- 6.75 The ReAssure UPC has responsibilities regarding the monitoring and management of box positions for ReAssure’s unit-linked funds and oversight of discretion on the pricing of funds.
- 6.76 In preparation for the proposed implementation of the Scheme, minor updates were made to the ReAssure UPC terms of reference in March 2019 to provide further details in relation to box management and measurement.

### **The Treating Customers Fairly Management Committee (the “TCF Management Committee”) and the ReAssure Product Management Committee (the “ReAssure PMC”)**

- 6.77 The TCF Management Committee provides dedicated oversight of conduct and TCF related matters by both ReAssure and its chosen outsource providers. It monitors key risks and issues impacting customer outcomes to ensure appropriate actions to mitigate any customer impact.
- 6.78 The ReAssure PMC is a sub-committee of the TCF Management Committee that oversees risks and issues relating to existing and new products to ensure compliance with ReAssure’s conduct strategy. It ensures that customers’ interests remain central to how the business is run and that products and services meet customers’ needs.
- 6.79 With effect from March 2019:
- The ReAssure PMC has taken on the responsibilities of the now disbanded TATCF Committee in relation to non-profit and unit-linked business;
  - In preparation for the proposed implementation of the Scheme, minor additions have been made to the ReAssure PMC terms of reference to increase transparency in relation to the governance of unit-linked funds; and
  - Minor changes have been made to the TCF Management Committee terms of reference to ensure a standing agenda item is available to consider escalations from the ReAssure PMC in respect of non-profit business TCF considerations.

## 7. The proposed scheme

### THE MOTIVATION FOR THE SCHEME

- 7.1 For LGAS and ReAssure, the main reason for the Scheme is that its implementation would make permanent the effect of the BTA signed in December 2017 in respect of the sale of the transferring business of LGAS to ReAssure.
- 7.2 The reasons for the sale of this business by LGAS and the acquisition of this business by ReAssure are given in Sections 5 and 6 of this report.

### A SUMMARY OF THE SCHEME

- 7.3 If the Scheme were to be implemented then, on the Legal Effective Date, the assets and liabilities associated with the transferring business would be transferred from LGAS to ReAssure. Specifically:
- All of the business of the LGAS WPF would be transferred to a newly created ring-fenced fund within ReAssure (the Legal & General With-Profits Fund or LGWPF).  
For the avoidance of doubt this includes all of the with-profits business and non-profit business currently in the LGAS WPF.
  - The transferring LGAS unit-linked and non-profit business would be transferred to the RNPF.  
Although not included in the terms of the BTA, as described in Section 5 this would include the transferring non-profit annuities that are currently administered by the LGR division in conjunction with with-profits annuities in the LGAS WPF. These non-profit annuities would be transferred to the MA portfolio in the RNPF.
- 7.4 In addition the RTA would terminate and the IMA, the AIA and a new fixed expense deal (all described below) would come into effect. The BTA would continue in force to the extent possible.
- 7.5 The Scheme is expected to be presented to the High Court for its Directions Hearing on 2 July 2019 and for its Sanctions Hearing on 17 October 2019.
- 7.6 A Jersey Scheme and a Guernsey Scheme are also expected to be presented to the relevant courts in Jersey and Guernsey on substantially the same terms as the Scheme, in order to ensure the effective transfer of any business carried on by LGAS in or from within Jersey, and the effective transfer of policies of LGAS issued to residents of the Bailiwick of Guernsey that are within the scope of the transferring business.
- 7.7 The transferring business is made up of 1.0 million policies and includes assets totalling £28 billion (as at 31 December 2018). See Section 5 for further information on the transferring business.
- 7.8 The proposed date of transfer is currently set to be 4 November 2019 (the “Legal Effective Date”) at which point the transferring business would legally transfer from LGAS to ReAssure and the Scheme will become operative between LGAS, ReAssure and the wider world. The Legal Effective Date must be approved by both LGAS and ReAssure which would only happen if a successful migration of data from LGAS’s IT systems to those of ReAssure and ReAssure’s ability to operate and manage the transferring business going forward had been confirmed. Subject to certain limits, the Legal Effective Date can be delayed by mutual agreement between LGAS and ReAssure and the firms would need to reapply to the High Court if the proposed Legal Effective Date were to be after 4 February 2020 though any deferment would be discussed with the regulator at the time.
- 7.9 The Scheme would become effective as between LGAS and ReAssure on the first day of the calendar month in which the Legal Effective Date occurs – this is the Economic Effective Date. Based on a Legal Effective Date of 4 November 2019, the Economic Effective Date would be 1 November 2019.

### THE INVESTMENT MANAGEMENT AGREEMENT (THE “IMA”)

- 7.10 Currently LGIM manages the assets backing the transferring business (except for assets in respect of the existing external mandates) and it has been agreed that, if the Scheme were to be implemented, this function would remain with LGIM following the Legal Effective Date for a period of at least seven years.
- 7.11 Under the IMA (as amended on 24 May 2018), the current investment management fees paid by LGAS to LGIM in respect of the transferring business would continue to apply following the Economic Effective Date, but would be

paid by ReAssure to LGIM. The IMA contains details of when the charges may be reviewed which is on 1 January 2023 and on a 'market change' as defined in the IMA.

- 7.12 Currently no VAT is paid on the LGIM investment management fees by LGAS but after the transfer, since the services would be provided by an entity which is not in the same VAT group as ReAssure, VAT would be payable and this VAT would be charged to the RNPF initially. After the IMA period ends, the Scheme would allow VAT to be charged to the LGWPF, however, ReAssure has agreed that it would only charge VAT to the LGWPF in the event that it was able to negotiate a reduction in the existing investment management fees and, including VAT, this would not result in an increase relative to the existing fees.
- 7.13 The IMA also outlines the circumstances under which ReAssure could withdraw the assets from LGIM without a withdrawal fee before the initial seven year term has expired.

#### **THE ANNUITY INTRODUCER AGREEMENT ("AIA")**

- 7.14 Under the AIA, if the Scheme were to be implemented, ReAssure would refer eligible policyholders from the transferring business to LGAS to provide a quotation for certain guaranteed income retirement products including lifetime annuities (both enhanced and standard), fixed term retirement plans and cash-out retirement plans.
- 7.15 The AIA sets out:
- The referral fees that LGAS would pay ReAssure for a lifetime annuity and for a fixed term or cash-out retirement plan; and
  - The pricing and customer outcome benchmarks to monitor LGAS's competitiveness.
- 7.16 In respect of the annuity rates offered by LGAS, the benchmarking commitment is that:
- The annuity rates offered must be at least as favourable as those provided to LGAS's internal customers; and
  - Across an assumed business mix, LGAS annuity rates must be ahead of the market average of all external market providers on the annuity portal IRESS, over a rolling four-month period (when at least five providers respond to the request for quotation).
- Should fewer than five providers respond there are contractually agreed steps in place for ReAssure and LGAS to discuss how to proceed.
- 7.17 There would be a number of safeguards to protect policyholders from accepting an annuity rate without awareness of other rates available:
- LGAS must ensure that the process is compliant with FCA's annuity rules COBS 19.9 (Pension annuity comparison information); and
  - If LGAS did not offer a best in market quote, as identified by COBS 19.9, it would provide customers with details of its whole of market quotation, giving the customer the option to be introduced to this service. The service would be provided by theidol.com, a financial technology company that is a subsidiary of the L&G Group.
- 7.18 For policyholders in the LGAS WPF whose benefit is expressed as an annuity (i.e. those with a GAO, a guaranteed minimum pension ("GMP") or a personal retirement plan):
- The annuity would always be referred to and fulfilled by LGAS (except where policyholders could be subjected to a tax charge from breaching their annual / lifetime allowance limits or losing lifetime allowance protection, in which case they would be handed back to ReAssure for fulfilment);
  - The newly created ring-fenced fund within ReAssure (into which the LGAS WPF business would transfer under the Scheme) would purchase the annuity; and
  - The costs of any applicable GAO uplift amount would be met by the newly created ring-fenced fund.
- 7.19 This agreement would be in place for a minimum period of five years from the Economic Effective Date, and would continue indefinitely unless terminated.

## THE FIXED EXPENSE AGREEMENT FOR THE LGWPF

- 7.20 There is currently in place a fixed expense agreement between the LGAS WPF and LGAS which is scheduled to terminate on 30 June 2019. The BTA allows for this to be extended as far as 31 December 2019 (or the earlier Legal Effective Date) on the advice of the LGAS WPC. If the Scheme were to be implemented a new fixed expense agreement would be set up for the LGWPF within ReAssure whereby the per-policy charges would be fixed until the last policy runs-off increasing by RPI inflation plus 0.5% annually.
- 7.21 The per-policy amount would cover all business as usual expenses (excluding the investment management fees paid to LGIM under the IMA) and any future exceptional expenses (including any regulatory expenses) but would not cover any compensation or redress payments arising from historic actions (i.e. on or before 30 July 2009<sup>2</sup>) which would represent an additional charge to the fund, however any administration costs associated with such payments would be included within the per-policy amount.
- 7.22 The fixed per-policy charges for in-force business will be defined in 2019 such that the total expenses paid would equate to £32.4 million for 2018. This will allow for the scenario where the policy counts change as a result of the migration whereby the per-policy charges would be scaled at a product group level to ensure the charge at the product level and overall remains unchanged.
- 7.23 The fixed expense arrangement would also cover one-off additional per-policy charges for any new business written in the LGWPF (i.e. increments accepted on pension business and new members for certain workplace schemes). As for the per-policy charges for in-force business, the per-policy charges for new business would be scaled to ensure that the level of charges levied on the LGWPF are broadly similar to those levied under the previous LGAS approach.
- 7.24 The per-policy charges applied to each product group in 2019 and subsequent years will be set equal to the per-policy charges for 2018, increased in line with RPI+0.5%.
- 7.25 The LGWPF would also make a one-off payment of £50 million to the RNPF following the implementation of the Scheme as a contribution to migration costs.

## THE SCHEME IN RESPECT OF THE TRANSFERRING UNIT-LINKED FUNDS

### The structure and management of the unit-linked funds within ReAssure

- 7.26 The completion of the Funds Foundation Project means that the unit-linked funds in LGAS in respect of the transferring business are separate from the unit-linked funds in LGAS in respect of the non-transferring business. If the Scheme were to go ahead, the unit-linked funds in respect of the transferring business would close and all of the assets contained within those funds would transfer to new unit-linked funds within ReAssure. These new ReAssure unit-linked funds would have the same assets immediately after the transfer as those unit-linked funds closed in LGAS had immediately before the transfer.
- 7.27 Certain transferring unit-linked funds (which comprise approximately 80% of all transferring unit-linked funds by assets under management) have been restructured prior to the proposed transfer to ensure alignment with ReAssure's operating model.
- 7.28 As described in Section 5 a significant number of the transferring unit-linked funds (both within the LGAS WPF and outside it) are reinsured to PMC and this reinsurance would transfer to ReAssure under the Scheme.

### The management and governance of the unit-linked funds within ReAssure

- 7.29 If the Scheme were to be implemented, there would be a significant increase in the size of ReAssure's unit-linked business. ReAssure has been undertaking a programme of changes to the management and governance of unit-linked funds in advance of the Legal Effective Date and these are reflected in the description of governance and management of ReAssure in Section 6 of this report. These management and governance changes have been in place since March 2019 and will remain in place whether the proposed Scheme is implemented or not but there would be some changes as a result of the implementation of the Scheme. In particular:

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<sup>2</sup> The date at which, according to COBS TP 2.14 and COBS 20.2.25D of the FCA Handbook, compensation and redress payments arising from errors could no longer be paid out of surpluses within a with-profit fund.



- A customer-facing unit-linked guide (the “ReAssure Unit-Linked Guide”) containing important tax references has been drafted in relation to the transferring business and would be published on the Legal Effective Date if the Scheme were to be implemented. This is in addition to the unit-linked guide that has already been published for the existing policyholders of ReAssure; and
- ReAssure is currently developing and improving its existing internal unit-linked principles and practices documentation, with the aim to obtain the necessary governance approvals by 30 September 2019.

7.30 If the Scheme were to be implemented the unit-linked box in the LGAS shareholder fund relating to the transferring business would be transferred to the RNPF and the unit-linked box currently held in the LGAS WPF would transfer to the LGWPF. Following the successful implementation of the Scheme, the intention is that the unit-linked box relating to the transferring business that would then be owned by the LGWPF would be transferred to the RNPF in exchange for a compensation payment from the RNPF to the newly-created LGWPF.

7.31 The current reinsurance agreement under which a significant amount of the LGAS unit-linked funds is reinsured to PMC would be replaced by a reinsurance agreement between ReAssure and PMC following the implementation of the Scheme.

### **Future changes to the unit-linked funds permitted under the Scheme**

7.32 Under the Scheme, ReAssure would be permitted to perform the following actions in the future in relation to the unit-linked funds:

- Wind up funds;
- Close funds to new contributions;
- Amalgamate funds;
- Split funds;
- Modify the investment objectives (providing they remain reasonably similar to the current objectives); and
- Perform any of the above in combination.

7.33 Safeguards exist within the Scheme such that the above actions could only be performed if the ReAssure Board considers the actions to be equitable to affected policyholders, practical and appropriate, having considered the advice of the Chief Actuary and the ReAssure FC.

7.34 In particular:

- In the case where the ReAssure Board decides to wind up a unit-linked fund then the Scheme obliges the Board to choose an alternative unit-linked fund for affected policyholders to invest in, having considered the advice of the ReAssure FC and the Chief Actuary. This alternative should provide the policyholders with the same value and a fund that is as close as reasonably possible to the original fund without any charge to the policyholders.
- If any of the above changes to the unit-linked funds could lead to any impact on a policyholder's policy then the Scheme obliges ReAssure to allow those policyholders to switch to an alternative fund for no charge, regardless of the terms of the policy, provided that the switch occurs within 12 months of the change.
- If there is any financial impact to a policyholder's unit value then the Scheme obliges ReAssure to compensate the affected policies such that they are not materially adversely affected. This amount would be approved by the Board having considered the views of the ReAssure FC and the Chief Actuary.

## **THE SCHEME IN RESPECT OF THE TRANSFERRING LGAS WPF BUSINESS**

### **The structure and management of the LGWPF**

7.35 If the Scheme were to be implemented, a new fund, the LGWPF, would be created in ReAssure and the transferring business of the LGAS WPF would be transferred into this fund. The newly created LGWPF would be maintained as a separate ring-fenced fund within ReAssure.



- 7.36 Some products written within the LGAS WPF currently have the right to invest in both the UWP fund and unit-linked funds; however, products written outside of the LGAS WPF do not have the right to invest in the UWP fund. The Scheme would preserve this position.
- 7.37 ReAssure has proposed a number of operational simplifications to the modelling and ongoing financial management of the business in the LGWPF that would take effect following the implementation of the Scheme. These include:
- The simplification of the calculation of the asset shares for UWP business for bonus setting and reporting purposes. This includes further pooling of experience for different groups of with-profits policies, and the wider pooling of the profits and losses from surrenders when calculating asset shares, whilst respecting the main product and profitability boundaries.
  - Calculating asset shares using the asset shares calculated by LGAS as at 31 December 2018, rolled forward using LGAS premium and claims data up to the Economic Effective Date and thereafter using the actual premiums received and claims paid by ReAssure.
  - Offsetting charges for the cost of options and guarantees against distributions of the estate rather than levying an explicit charge for options and guarantees.
  - Development of a Pillar II (or Economic Capital) approach to managing the LGWPF from a risk appetite and run-off perspective, including the calculation of the Pillar II Own Funds and capital requirements for the LGWPF.
  - Changes to the management actions that would be employed in the event of deteriorating conditions.
  - Redrafting the PPFM for the LGWPF to align more closely with the structure and language of the PPFMs for ReAssure's existing with-profits funds.
- 7.38 The first five bullets above are within the scope of the existing PPFM for the LGAS WPF and so could be implemented without a change to the PPFM. Regarding the sixth bullet, the revised PPFM is in effect relating to a new fund in ReAssure and the existing PPFM permits future changes to its wording without constraints on the document structure.
- 7.39 ReAssure and LGAS have agreed that, if the Scheme were to be implemented, LGAS's actuarial models would be used to support the year-end 2019 bonus declaration in February 2020 under the dual governance of both parties. ReAssure's models would then be used for future bonus declarations.

#### **The governance of the LGWPF after the implementation of the Scheme**

- 7.40 If the Scheme were to be implemented, a WPA would be appointed to fulfil the statutory WPA role and provide oversight of the LGWPF. The existing WPA would continue to fulfil the statutory WPA role and provide oversight of the existing with-profit funds of ReAssure. The WPA for the LGWPF (which could be a new WPA, the existing LGAS WPA, or alternatively the role of the existing ReAssure WPA could be extended to cover the LGWPF) would have direct access to the ReAssure FC.
- 7.41 Leading up to the Legal Effective Date training sessions on the transferring business are scheduled for the ReAssure FC. For the first 12 months following the Legal Effective Date, the ReAssure FC meetings would be extended to four hours from the current two hour duration after which the meetings would reduce to three hours.

#### **Future changes to the LGWPF permitted under the Scheme**

- 7.42 If the Scheme were to be implemented then, should ReAssure wish to, the following actions would be permitted in the future.
- **Reallocation of the non-participating business within the LGWPF into the RNP**  
For this action the Scheme stipulates that:
    - Such a reallocation should not be inconsistent with the terms of the policies and applicable laws and regulations;
    - The reallocation would be subject to consultation with the ReAssure FC and the approval of the ReAssure Board;

- The level of assets being transferred into the RNPF should be commensurate with the transferring liability and associated level of risk;
- The reallocation should not have a material adverse impact on the affected policyholders when considering the aggregate impact of any other reallocations in the preceding five years and any planned reallocations in the following five years; and
- Where aggregate reallocations in any 12 month period involve a transfer of assets of more than £150 million (increased annually on 31 December in line with the UK Retail Prices Index ("RPI")), the Scheme ensures that ReAssure informs the regulators and obtains their non-objection within two months, and also obtains a certificate from an independent actuary to provide the view that there would be no material adverse impact on affected policyholders.
- **Merging of the LGWPF into one of the other with-profits funds within ReAssure where the value of the assets within the LGWPF falls below £400 million (increased annually on 31 December in line with the UK RPI)**

For this action the Scheme stipulates that:

- Such a reallocation should not be inconsistent with applicable laws and regulations;
  - The reallocation would be subject to consultation with the ReAssure FC and the approval of the ReAssure Board;
  - The regulators must not object within two months of notification to them;
  - Any with-profits policies should still be with-profits policies following the merger;
  - There should be no material adverse impact on the transferring policyholders or existing policyholders in the destination fund, in the opinion of the ReAssure Board and an independent actuary; and
  - The PPFM of the destination fund would be appropriately updated to take account of the provisions of the PPFM of the LGWPF.
  - **Merging of one of the other with-profits funds within ReAssure into the LGWPF**
- The requirements outlined in the Scheme in respect of this action are similar to those for the merging of the LGWPF into another ReAssure with-profits fund (as described above) except that there is no minimum size specified – this is £400 million (increased annually on 31 December in line with the UK RPI) for the LGWPF.
- **Merging of the LGWPF into the RNPF and converting the remaining with-profits policies into non-profit policies if the assets within the LGWPF fall below £400 million (increased annually on 31 December in line with the UK RPI)**

For this action the Scheme sets out the same conditions as for merging with-profits funds with the following changes:

- An appropriate allowance for the future shareholder transfers that would have otherwise been made from the LGWPF to the RNPF should be released to the RNPF;
- Following the merger, the with-profits policies will no longer participate in any profits and in particular in those of the RNPF; and
- Where the value of the assets within the LGWPF falls below £80 million (increased annually on 31 December in line with the UK RPI), a certificate from an independent actuary would no longer be required for such a merger.

- 7.43 Should any of the above actions be taken in respect of the LGWPF the Scheme allows for the fixed expense arrangement for the LGWPF to be altered as necessary.

## THE ADMINISTRATION AND SERVICING OF THE TRANSFERRING BUSINESS

- 7.44 The current administration and servicing arrangements for the transferring business are set out in Section 5.
- 7.45 If the Scheme were to be implemented, ReAssure would take over the administration of the majority of the transferring business. Deloitte would continue to administer the final salary schemes which are part of the

transferring business and have a total value of approximately £22.1 million, all of which is invested in the with-profits fund.

- 7.46 The IT systems used to administer and service the transferring business would not be transferred from LGAS to ReAssure. Rather, the data for the transferring business would be migrated from the IT systems of LGAS to ReAssure's IT systems on the Economic Effective Date, subject to prior testing and satisfaction of minimum criteria. This migration would include any necessary functional changes to accommodate the transferring business and products.
- 7.47 Transferring policyholders currently have access to online portal solutions within LGAS. This functionality is being developed, tested and put in place within ReAssure through the 'ReAssure Now' and 'ReAct' portals, for use by transferring and existing ReAssure policyholders, and sponsoring employers of occupational pension schemes respectively. These will be rolled out following the Sanctions Hearing.
- 7.48 The BTA sets out minimum standards for the administration of the transferring business within ReAssure following the implementation of the Scheme, and LGAS and ReAssure have agreed to monitor the operational stability of the transferring LGAS and existing ReAssure business in the lead up to the Economic Effective Date to ensure that ReAssure will be able to take on the incoming volumes of work and achieve these minimum standards.
- 7.49 As set out in Section 5 of this report, the administration of DB pension schemes within the LGAS WPF is currently outsourced to Deloitte and this arrangement would continue following the implementation of the Scheme.

## **NEW BUSINESS**

- 7.50 As set out in Section 5 increases to existing pension policies and new members joining existing pension schemes are currently accepted in respect of the transferring business and this would continue to be the case following the transfer of the business to ReAssure.
- 7.51 The Scheme would transfer the relevant live distribution agreements with the authorised policy advisers that were used to distribute the transferring policies including commission and facilitated adviser charging payments.

## **PRODUCT CHANGES**

- 7.52 ReAssure has proposed a number of changes to the products within the transferring business. These changes are proposed either because:
- Certain product features, and the way the business is operated cannot be easily supported by ReAssure's existing systems and operations; or
  - They would increase operational efficiency as a result of harmonisation with existing practices.
- 7.53 It is not intended that any of these changes would have a material adverse effect on the transferring policyholders.
- 7.54 Some of these changes would involve a change to the policy terms and conditions; however, all such terms and conditions changes are permitted with the requisite notice, which will be given as part of the communications issued to policyholders regarding the Scheme.
- 7.55 The proposed product changes affect the transferring with-profits, unit-linked and conventional non-profit business. The changes have been approved by the ReAssure PMC, and have been thoroughly reviewed and agreed by LGAS. A review and commentary has also been provided by the LGAS WPA and Chief Actuary in their respective reports.

## **RESIDUAL POLICIES**

- 7.56 Where policies within the scope of the transferring business are not capable of being transferred under the Scheme (or the Jersey or Guernsey Schemes) on the Legal Effective Date, they will be referred to as 'residual policies'.
- 7.57 Residual policies will remain policies of LGAS and will be fully reinsured to and administered by ReAssure with effect from the Legal Effective Date until such a time as it is possible to transfer the residual policies (and associated assets and liabilities) to ReAssure.

## THE COSTS OF THE SCHEME

- 7.58 The shareholders of LGAS and ReAssure will split the following costs equally in relation to the Scheme:
- The costs associated with the High Court process, including the appointment of Counsel in leading the High Court proceedings and the High Court fees incurred;
  - Any fees of incurred by the PRA or FCA, or other supervisory authorities;
  - The fees of the Independent Expert;
  - The costs of communicating with transferring policyholders in relation to the Scheme; and
  - The costs of newspaper advertisements in relation to the Scheme.
- 7.59 Thereafter the shareholders of LGAS and ReAssure will each bear their own costs and expenses in relation to the Scheme.
- 7.60 As described above, the LGWPF would also make a one-off payment of £50 million to the RNPF following the implementation of the Scheme as a contribution to migration costs.

## SIPPS

- 7.61 If the Scheme were to be implemented, a portfolio of SIPPs would transfer from the L&G Group to the ReAssure Group.
- 7.62 The SIPPs contain:
- Insured assets, where the policyholder chooses to invest in the unit-linked funds in LGAS through a TIP; and
  - Uninsured assets, where the policyholder chooses to invest directly in other asset classes outside of LGAS.
- 7.63 There is currently one in-force TIP policy in respect of the insured assets. This policy would transfer as part of the Scheme in the same way as the other transferring business. The uninsured assets would transfer under an ancillary order.
- 7.64 To operate SIPP business, a trustee is required to hold the legal title to the SIPP holder's assets (i.e. the TIP policy and the uninsured assets) and an operator is required to administer the business. Currently, within the L&G Group, PMS Nominees is the trustee and PMS is the operator, both of which are L&G Group entities.
- 7.65 If the Scheme were to be implemented, G Trustees Limited ("G Trustees") and RUKSL, both ReAssure Group entities, would become the respective trustee and operator for the transferring SIPP business. In addition, the administration of the uninsured assets would be outsourced to an external administrator, Jardine Lloyd Thomson plc ("JLT").
- 7.66 Under the proposed ReAssure Group target operating model for transferring SIPP business:
- The administration systems used to administer the SIPPs would change;
  - The initial contact for the administration of the SIPPs would move to RUKSL;
  - For certain purposes the initial contact would move to JLT; however, a dedicated line would be set up at JLT for the ReAssure Group SIPP customers;
  - The legal title of the assets would transfer from PMS Nominees to G Trustees but the beneficial ownership would remain with the SIPP holder; and
  - The investment options available to SIPP policyholders would be unchanged as a result of the Scheme.
- 7.67 As set out in Section 5, although not directly related to the Scheme, a change would be made to the SIPP product terms and conditions to allow a platform charge to be applied directly for approximately 450 SIPP policies with uninsured collective investments following their transfer to the ReAssure Group.
- 7.68 Other than a reduction to some other charges, the charges levied on SIPP policyholders would be unchanged as a result of the Scheme.

## THE LGAS STAKEHOLDER PENSION POLICIES

- 7.69 If the Scheme were to be implemented:
- The individual stakeholder pension policies in LGAS would transfer to ReAssure.
  - The group stakeholder pension policies will remain in LGAS.
- 7.70 The individual stakeholder pension policies currently form part of the Legal & General Stakeholder Pension Scheme and it is intended that they would be transferred to ReAssure and become part of a registered Stakeholder Pension Scheme held by ReAssure (the “ReAssure Stakeholder Pension Scheme”).
- 7.71 The underlying stakeholder pension policies could be transferred as part of the Scheme but in order for the associated pension scheme memberships to be transferred it is necessary for the Pension Tax Relief at Source (“PTRAS”) Declarations to be transferred from the scheme administrator of the Legal & General Stakeholder Pension Scheme to that of the ReAssure Stakeholder Pension Scheme.
- 7.72 The transfer of the PTRAS Declarations would only be required for those transferring stakeholder pension policyholders that will continue to make contributions to their stakeholder pension policies within the Legal & General Stakeholder Pension Scheme (the “Contributing LGAS Stakeholder Members”).
- 7.73 Thus, at the Sanctions Hearing, LGAS will seek a Court Order that deems, for the Contributing LGAS Stakeholder Members, that the ReAssure Stakeholder Pension Scheme has held the existing PTRAS Declarations with effect from the same date(s) as the Legal & General Stakeholder Pension Scheme had first held the transferring policies.
- 7.74 In a letter to LGAS dated 17 June 2019, HMRC confirmed that they do not have an objection to the parties seeking such a Court Order.

## THE LGAS FLEXIBLE MORTGAGE ISAS

- 7.75 The LGAS flexible mortgage ISA (“FMISA”) is a regular savings plan that combines savings (through an ISA) and term life assurance. It is designed to contribute to an interest only mortgage repayment at the end of a specified term or to pay an earlier lump sum if the policyholder dies or becomes eligible to claim terminal or critical illness benefits. Policyholders pay regular premiums, part of which is invested in an ISA and part of which is used to fund life assurance cover (and other risk benefits as applicable).
- 7.76 LGAS currently handles the communications, premium collections and claims processing in respect of the FMISA business. It deducts applicable policy fees and risk charges from premiums received and passes the balance on to UTM to invest into the ISA.
- 7.77 If the Scheme were to be implemented, ReAssure and UTM would enter into an agreement so that the insurance element of the FMISA business (currently handled by LGAS) would be transferred to ReAssure and UTM would retain the ISA element. ReAssure would replace LGAS as the principle point of contact for policyholders, receiving premiums, deducting policy fees and risk charges, passing the balance on to UTM, and processing policyholder claims.
- 7.78 LGAS and ReAssure will develop their respective systems prior to the Legal Effective Date to facilitate this arrangement and the necessary information sharing and segregation of policyholder funds, including development of a client account within ReAssure to monitor the aggregate balance of ISA funds (the “ISA Fund Account”). This development is due to be tested and subject to minimum acceptance criteria as part of wider testing to ascertain overall business readiness of UTM and ReAssure in advance of the proposed transfer.

## LINKED UNEMPLOYMENT COVER

- 7.79 LGAS administers unemployment cover policies that are linked to approximately 2,000 transferring mortgage protection insurance (“MPI”) policies.
- 7.80 MPI was a stand-alone product designed to pay a percentage of policyholders’ mortgage payments should they be unable to work due to illness. An additional feature of the product allowed the policyholder to also purchase cover should they become unemployed. The unemployment cover can be cancelled independently from the MPI but not vice versa. In other words, the unemployment cover cannot exist as a separate independent contract.
- 7.81 If the Scheme were to be implemented:

- The unemployment cover policies would remain with LGAS and policyholders of the transferring MPI policies to which they are linked would need to continue to contact LGAS separately regarding any queries or changes relating to their unemployment cover; and
- ReAssure would manually maintain the link between the unemployment cover policies and the transferring MPI policies so that unemployment cover would be terminated if the transferring MPI policy to which it is linked was terminated.

7.82 This change will be clearly communicated to the affected transferring policyholders in advance of the Legal Effective Date.

#### **PROPERTY ASSETS**

7.83 The legal title to certain properties held within the LGAS WPF is currently held jointly by two L&G Group entities: Legal & General Property Partners (Life Fund) Limited (the “General Partner”) and Legal & General Property Partners (Life Fund) Nominee Limited, with the beneficial title held by Legal & General Life Fund Limited Partnership (an English Limited Partnership or “ELP” constituted between LGAS as sole limited partner and the General Partner). It is intended that, if the Scheme were to be implemented, the individual properties within the scope of the ELP structure would transfer from the ELP to ReAssure directly, with the ELP structure remaining with the L&G Group.

7.84 The assets backing the transferring business include interests in a number of property unit trusts, which are held 99.99% by LGAS and 0.01% by Legal & General Property Limited. These interests would transfer to ReAssure Group entities if the Scheme were to be implemented.

#### **OTHER AREAS**

7.85 If the Scheme were to be implemented, any existing agreements between the LGAS shareholders and the LGAS WPF in relation to the notional allocation or reallocation of assets and liabilities of the LGAS WPF prior to 6 December 2017 (i.e. the date of signing of the BTA) would become enforceable between LGAS and the newly created LGWPF.

7.86 This would include any rights or obligations that, at the Economic Effective Date, have not yet been discharged in relation to with-profits expenses for the period between the Economic Transfer Date and the Economic Effective Date.

## 8. The effect of the Scheme on the transferring LGAS policies

### INTRODUCTION

- 8.1 If the Scheme were to be approved by the High Court and implemented:
- The transferring LGAS WPF business (the with-profits business and the associated non-profit business currently in the LGAS WPF) would transfer into a newly created ring-fenced fund in ReAssure called the LGWPF; and
  - The transferring LGAS unit-linked and non-profit business that is currently outside of the LGAS WPF would transfer into the RNPF.
- 8.2 Based on the financial information as at 31 December 2018, the transferring business consisted of approximately 1.0 million policies and £28 billion of assets under management split as follows:
- Approximately £18 billion of assets currently in the LGAS WPF; and
  - Approximately £10 billion of assets currently backing the unit-linked and non-profit business.
- 8.3 In this section and Section 9 I consider the likely effects of the implementation of the Scheme on the transferring LGAS policies.
- 8.4 The key points to consider in respect of the transferring LGAS policies are the likely effects of the Scheme on the following:
- **The security of the benefits of the transferring policies**  
The security of benefits for the transferring policies is derived from the financial strength available to provide security under the appropriate risk appetite statements and applicable capital policy and any external support available from the parent company by virtue of being part of a group.  
This is covered in paragraphs 8.7 to 8.53.
  - **The profile of risks to which the transferring policies are exposed**  
If the Scheme were to be implemented, the transferring LGAS policies would become direct policies of ReAssure and directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.  
This is covered in paragraphs 8.54 to 8.61.
  - **The reasonable expectations of the transferring policyholders in respect of their benefits**  
This is covered in paragraphs 8.62 to 8.127.
  - **The standards of administration, service, management and governance applied to the transferring policies**  
This covers the management, oversight and administration of the transferring policies and in particular the process for migrating from LGAS to ReAssure.  
This is covered in paragraphs 8.128 to 8.171.
- 8.5 In addition, I have separately considered the impact of the IMA and the AIA (described in Section 7) on the transferring policies, which would come into effect following the implementation of the Scheme, as well as the customer retirement journey for the transferring with-profits policies.
- 8.6 Each of these areas is covered separately in the following sections.

### THE EFFECT OF THE SCHEME ON THE SECURITY OF THE BENEFITS OF THE TRANSFERRING POLICIES

#### Introduction

- 8.7 The financial strength available to provide security for the benefits under the transferring LGAS policies is currently provided by:



- The strength of the calculation used to set the level of assets held by LGAS to cover the technical provisions and SCR of the transferring LGAS business as required under the Solvency II regulations;
- The additional financial strength required by the LGAS RA Statement including the strength of the governance around the LGAS RA Statement and the governance around any future changes to the LGAS RA Statement; and
- Any additional support from outside LGAS, including support from the L&G Group.

8.8 The implementation of the Scheme would mean that LGAS would cease to have a defined contractual obligation in respect of the transferring policies and that these obligations would be transferred to ReAssure. After the implementation of the Scheme, the transferring policies would derive their security of benefits from:

- The strength of the calculation used to set the level of assets held by ReAssure to cover the technical provisions and SCR of the transferring LGAS business. These would be as required under the Solvency II regulations and would be:
  - In the RNPF in respect of the transferring business outside of the LGAS WPF; and
  - In the LGWPF in respect of the transferring LGAS WPF business.
- The additional financial strength required by the ReAssure RA Statement including the strength of the governance around the ReAssure RA Statement and the governance around any future changes to the ReAssure RA Statement.
- Any additional support from outside ReAssure including the Swiss Re Group and MS&AD.

8.9 I consider the effect of the implementation of the proposed Scheme on the security of the transferring LGAS policies by considering each of these below.

#### **The security of benefits provided by the technical provisions and SCR**

8.10 Both LGAS and ReAssure are within the scope of the Solvency II regime and this will not change as a result of the implementation of the Scheme and so the technical provisions and SCR in respect of the transferring business will continue to be calculated in accordance with the Solvency II regulations.

8.11 There are some differences between the way that LGAS currently calculates the technical provisions and the SCR in respect of the transferring business, and the way that, if the Scheme were to be implemented, ReAssure would calculate the technical provisions and SCR in respect of the transferring business. These are:

- In respect of the Solvency II technical provisions:
  - LGAS has approval from the PRA for the use of the TMTP and a MA.
  - ReAssure does not have such PRA approvals in respect of the transferring business but does have approvals from the PRA for the use of the TMTP, a MA and the VA in respect of its existing business.
- In respect of the Solvency II SCR:
  - LGAS has PRA approval to use the LGAS PIM to calculate the SCR for all of its business and therefore currently calculates the SCR in respect of the LGAS transferring business using the LGAS PIM.
  - ReAssure has PRA approval to use the ReAssure PIM for its existing RNPF business, excluding the risks arising in respect of the transferring LGAS business covered by the RTA.

The Standard Formula calculation as prescribed in the Solvency II regulations is currently used for business in ReAssure's existing with-profits funds and the risks arising from the LGAS transferring business through the RTA.

If the Scheme were to be implemented, ReAssure would use the Standard Formula for the SCR in respect of the transferring business (except for the small block of non-profit annuities transferring to the ReAssure MA portfolio, for which ReAssure expects to use the ReAssure PIM for efficiency purposes subject to non-objection of the PRA).

8.12 For the technical provisions, both companies adhere to the Solvency II regulations and currently have PRA approval for the TMTP and MA. ReAssure also makes use of the VA. The Solvency II rules do not allow for an automatic transfer of any TMTP approval from LGAS to ReAssure and therefore, in preparation for the implementation of the



Scheme, ReAssure intends to submit an application to seek approval from the PRA to recalculate the TMTP to reflect the transferring business. I will comment further on the status of the application to recalculate the TMTP in relation to the transferring business in my Supplementary Report.

- 8.13 In respect of the calculation of the SCR for the LGAS transferring business it should be noted that the LGAS PIM calculation of the SCR for the transferring business and the ReAssure Standard Formula calculation of the SCR for the transferring business are both calibrated to provide a probability of at least 99.5% that the firm remains solvent over a one year time horizon.
- 8.14 Since LGAS and ReAssure calculate the technical provisions in a consistent way and the SCR such that the probability of remaining solvent over a one year time horizon is at least 99.5%, I am satisfied that although differences exist between the way that LGAS currently calculates the technical provisions and the SCR in respect of the transferring business, and the way that, if the Scheme were to be implemented, ReAssure would calculate the technical provisions and SCR in respect of the transferring business, these differences would not have a material adverse effect on the security of the benefits of the transferring policies.

### **The security of benefits provided by the applicable risk appetite statement**

#### *Introduction*

- 8.15 If the Scheme were to be implemented, the risk appetite statement applicable to the transferring business would change from the LGAS RA Statement to the ReAssure RA Statement.
- 8.16 The risk appetite statements and the approaches to capital management for LGAS and ReAssure are described in Section 5 and Section 6 and, if the Scheme were to be implemented, there would be no change to these for either company.
- 8.17 As stated in Section 6, ReAssure intends to proceed with an IPO and although the Scheme itself would not lead to changes in the ReAssure RA Statement, there would be changes if the ReAssure IPO were to proceed. I consider the impact of such changes on the security of policyholders' benefits in Section 12 of this report.
- 8.18 As set out in Section 3 of this report:
- By requiring additional capital to be held on top of the regulatory requirements, the risk appetite statement increases the likelihood of remaining solvent over a particular timeframe and therefore increases the security of the policies covered by the risk appetite statement; and
  - When considering the financial strength available to provide security for the benefits of a particular group of policies, reliance should only be placed upon the assets held in accordance with the risk appetite statement, as assets held in excess of the risk appetite statement requirements need not be kept in the company and could, subject to appropriate governance procedures, be transferred out of the company (for example, through dividend payments or passing capital through other group entities).
- 8.19 The strength of a risk appetite statement is a function of both:
- The relative level of capital required; and
  - The qualitative aspects in respect of the governance surrounding the risk appetite statement for example in respect of the required response of management to a breach in the risk appetite statement.
- 8.20 These two parts are covered in turn below.

#### *A comparison of the capital required under the risk appetite statements of LGAS and ReAssure*

- 8.21 The level of capital required by a risk appetite statement increases the security of the policies within the business covered by the risk appetite statement. The level of capital required by a company's risk appetite statement can usually be approximated by a statement that an unlikely event with a likelihood of 1 in X could occur and the company would still be able to cover its SCR over a certain time horizon. The capital requirements of the LGAS RA Statement and the ReAssure RA Statement are set out in Sections 5 and 6 respectively and the companies have presented the 1 in X likelihoods as follows:

- **The LGAS RA Statement:**

- The LGAS solvency coverage ratio should be maintained at or above the level of the LGAS RA Statement level.
- The LGAS WPF solvency coverage ratio should be maintained at the level of 100% and the LGAS WPF should be managed with the objective of ensuring that its assets are sufficient to meet its liabilities and regulatory capital requirements without the need for additional capital from outside the LGAS WPF.

- **The ReAssure RA Statement:**

- The RNPF solvency coverage ratio should be maintained at or above the level of the ReAssure RA Statement level.
- The ReAssure with-profits funds' solvency coverage ratios should be maintained at the level of 100% and each with-profits fund should be managed with the objective of ensuring that its assets are sufficient to meet its liabilities and regulatory capital requirements without the need for additional capital from outside of the relevant with-profits fund.

8.22 A comparison of the capital levels required by each risk appetite statement might suggest that the ReAssure RA Statement is less strong than the LGAS RA Statement. However, the risk appetite statements of ReAssure and LGAS are not directly comparable for the following reasons:

- The required solvency capital ratios apply to different entities.
- The LGAS RA Statement refers to holding capital based on the SCR of LGAS as a whole whereas the ReAssure RA Statement refers to holding capital based on the SCR of the RNPF.
- The methodologies used by LGAS and ReAssure in deriving their risk appetite statements are different. This means that the likelihoods derived for the scenarios that each company is intended to withstand without breaching their SCRs are not directly comparable.
- LGAS is open to new business whereas ReAssure is closed to new business. All else being equal, one might expect a lower target capital target level for ReAssure due to it being closed to new business and expecting to receive surplus as the closed book runs off whereas LGAS needs to finance new business.

8.23 Whilst not directly comparable, the derivations of the risk appetite statements provided by LGAS and ReAssure aim to ensure that each company could withstand severe events without breaching their SCR over a 1 year time horizon.

8.24 In considering the effect of the change in applicable risk appetite statement the primary consideration is the security that would be afforded the transferring policies by the ReAssure RA Statement when in ReAssure after the implementation of the Scheme and this can be summarised as follows:

- The security inherent in holding capital to cover the SCR:  
As described in Section 3 of this report, the capital requirements under Solvency II (the SCR) are set such that the likelihood of the firm failing to meet its obligations over a one year time horizon is less than 1 in 200.
- The additional security from holding capital to meet the requirements of the ReAssure RA Statement.

8.25 Taking the SCR together with the level of capital required under the ReAssure RA Statement means that the possibility of ReAssure becoming unable to meet its obligations in respect of policyholder claims when due is extremely remote and I am satisfied that, if the Scheme were to be implemented, the change for the transferring policies to be covered by the ReAssure RA Statement would, in terms of the capital required, not lead to a material adverse effect on the security of benefits under the transferring policies.

8.26 I cover the implications of the change to the ReAssure RA Statement in terms of the governance around it in the next sub-section.

#### *A comparison of the governance around the risk appetite statements of LGAS and ReAssure*

8.27 Part of the security provided by a risk appetite statement is due to the governance around the risk appetite statement and this includes:

- The required response to a breach of the risk appetite statements;

- The process and frequency behind the review of the risk appetite statements; and
  - The procedures and processes required to change the risk appetite statements.
- 8.28 The management actions available to respond to breaches of risk appetite in LGAS are different to those available in ReAssure. These differences reflect the differences between the two companies in size, type of business written and risk exposures, and hence it is not useful to compare the two sets of available management actions.
- 8.29 For both firms, where a risk appetite breach occurs, aside from any specific internal management actions, recourse to the relevant parent company is available for capital support. This is discussed further below.
- 8.30 The LGAS RA Statement is reviewed as part of the annual ORSA process and more frequently if there is a significant change to the LGAS risk profile.
- 8.31 The ReAssure RA Statement is reviewed at least annually and on an ad-hoc basis where there is a material change to the financial or risk position of the company or the legal or regulatory environments.
- 8.32 For LGAS, any changes to the LGAS RA Statement must be approved by the LGAS Board and reported to the regulator. For ReAssure, any changes to the ReAssure RA Statement must be approved by the ReAssure Board and reported to the regulator.
- 8.33 I am satisfied that the governance arrangements in place in respect of the ReAssure RA Statement do not represent a material change relative to the governance arrangements currently in place in respect of the LGAS RA Statement and that therefore, if the Scheme were to be implemented, there would not be a material adverse effect on the security of the benefits under the transferring policies.

#### *Conclusion regarding the effects of the change in the applicable risk appetite statement*

- 8.34 I am satisfied that, if the Scheme were to be implemented, the change for the transferring policies to be covered by the ReAssure RA Statement rather than the LGAS RA Statement would not have a material adverse effect on the security of their benefits.

### **The security of benefits due to being part of ReAssure after the Scheme**

#### *The projected financial strength of ReAssure*

- 8.35 Based on the financial information as at 31 December 2018 shown in Appendices A and B of this report:
- Prior to the implementation of the Scheme, the capital resources of LGAS cover its SCR with a ratio of 150% and with excess capital (above the SCR) of £3.5 billion; and
  - If the proposed Scheme had been implemented on 31 December 2018, the capital resources of the RNPF of ReAssure would have covered its SCR with a ratio of 134% and excess capital of £0.8 billion.
- 8.36 As described in Section 3 when considering the security of benefits derived from the financial strength of a company, one should not place reliance on capital held above that required by the relevant risk appetite statement as this could, subject to appropriate governance procedures, be reduced by the owners of the company. Therefore, LGAS could reduce its SCR coverage to the LGAS RA Statement level in line with the LGAS RA Statement.
- 8.37 If the Scheme were to be implemented, the expected financial strength of the ReAssure RNPF as at 31 December 2018 would indicate a position of considerable strength as it is materially above both the level of 100% of SCR and the level of the ReAssure RA Statement level required.
- 8.38 For the same reasons as above, when considering the security of benefits derived from the financial strength of a company, one should not place reliance on the capital held above that required by the relevant risk appetite statement and therefore in the absence of any commitment to hold capital in excess of the ReAssure RA Statement level required by the ReAssure RA Statement, consideration of the effect that the Scheme would have on the security of benefits under the transferring policies boils down to consideration of the security of benefits if capital is held at the ReAssure RA Statement level.
- 8.39 Therefore, although the proposed Scheme is expected to lead to a reduction in the SCR coverage for the transferring business from 150% in LGAS to 134% in ReAssure I am satisfied that this does not imply that the proposed Scheme is expected to have a material adverse effect on the security of the benefits of the transferring LGAS policies. The SCR coverage ratios are indicators of, or proxies for, financial strength and a significant

decrease in the SCR coverage ratio does not necessarily indicate a material reduction in the likelihood of benefits on the transferring business not being paid and therefore would not indicate a material reduction in the security of those benefits.

- 8.40 As set out in Section 3 of this report, the SCR is itself calculated such that there is a 99.5% likelihood of the company remaining solvent and able to meet its liabilities as they fall due over a one year time horizon and hence a company covering 100% of SCR would have a considerable margin above the level at which the company would be unable to pay its claims as they were due. The ReAssure RA Statement requires ReAssure to hold material margin over that.
- 8.41 A comparison of the LGAS RA Statement with the ReAssure RA Statement was carried out above with the conclusion that the change for the transferring policies to be covered by the ReAssure RA Statement rather than the LGAS RA Statement would not have a material adverse effect on the security of their benefits.
- 8.42 In addition, I have been provided with financial projections showing the expected path for the ReAssure Group SCR coverage (calculated using the ReAssure PIM) in the future if the Scheme were to be implemented. These projections show that the SCR coverage ratio for the ReAssure Group is expected to remain strong (significantly higher than 100% of SCR) and higher than the level required under the ReAssure IPO RA Statement over the projection period. The ReAssure IPO RA Statement sets out RGP's commitment to ensuring that risk appetite is adhered to at the level of the ReAssure entity and that the interests of the ReAssure entity are maintained. I am therefore satisfied that the projected financial strength of the ReAssure Group is indicative of that for ReAssure specifically.
- 8.43 As stated above, one might expect a higher capital level to be required for a company such as LGAS that is open to new business as compared with a company like ReAssure that would expect to receive surplus as the closed book runs off.
- 8.44 Taking all of the above into consideration, I am satisfied that the implementation of the Scheme and the associated change to rely on the financial strength of ReAssure would not have a material adverse effect on the security of the benefits of the transferring LGAS policies.

#### *The capital support provided by the ReAssure parent*

- 8.45 LGAS is the principal operating subsidiary of the L&G Group and has recourse to the L&G Group should the need for capital support arise. The L&G Group has an A rating from Standard & Poor's and the risk appetite and associated capital policy of the L&G Group requires it to hold capital at the L&G Group RA Statement level.
- 8.46 ReAssure is a subsidiary of the Swiss Re Group, with a minority investment from MS&AD, and has recourse to the Swiss Re Group and MS&AD should the need for capital support arise:
- The Swiss Re Group has a strong AA- rating from Standard & Poor's and, as at 31 December 2018, covered its regulatory capital requirements under the Swiss solvency regime (the Swiss Solvency Test) with a ratio of 251%, which is comfortably above its approved capitalisation target of 220%.
  - MS&AD has an AA rating from Japan Credit Rating Agency Limited and had an Economic Solvency Ratio of 211% as at 31 December 2017, which is within its target range of 180% to 220%. This Economic Solvency Ratio metric is, like the Solvency II SCR, based on a 99.5% probability of remaining solvent over a one year time horizon.
- 8.47 If the Scheme were to be implemented, the transferring LGAS policies would be transferred to ReAssure and provision of their security would change from LGAS supported by the L&G Group to ReAssure supported by the Swiss Re Group and MS&AD.
- 8.48 The size and level of capitalisation of the Swiss Re Group and MS&AD provide material security for ReAssure and its policyholders as in all but the most extreme scenarios Swiss Re Group and MS&AD would provide support to ReAssure if and when required. The possible forms of capital support that could be provided include cash injections and other financial arrangements that could provide the relevant support including reinsurance or contingent loans.
- 8.49 I am satisfied that the level of security provided by the support from the Swiss Re Group and MS&AD is sufficient to ensure that the implementation of the Scheme and the change for the transferring policies to having group support provided by the Swiss Re Group and MS&AD rather than the L&G Group is such that there would not be a material adverse effect on the security of the benefits guaranteed under those policies.

- 8.50 As set out above, ReAssure intends to proceed with an IPO and I consider the possible implications of a ReAssure IPO on the transferring policyholders in Section 12 of this report.

#### **The security of benefits provided by the FSCS**

- 8.51 Both ReAssure and LGAS are UK-regulated companies and so the security of benefits conferred on the transferring policies by the FSCS is unaffected by the transfer.

#### **Conclusion on the effect of the Scheme on the security of benefits**

- 8.52 I have considered the likely effects of the implementation of the proposed Scheme on:
- The assets covering the technical provisions and SCR of the transferring business as required under the Solvency II regulations;
  - The additional financial strength required by the relevant risk appetite statement and associated capital policy; and
  - The additional support available from the parent/owners of the company.
- 8.53 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the transferring policies.

#### **THE EFFECT OF THE SCHEME ON THE PROFILE OF RISKS TO WHICH THE TRANSFERRING POLICIES ARE EXPOSED**

- 8.54 If the Scheme were to be implemented, the transferring policies would become policies of ReAssure and be directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.
- 8.55 Both LGAS and ReAssure have a large variety of in-force business that exposes both firms to a range of different risk types, including insurance risk (such as mortality risk, longevity risk and persistency risk), expense risks, market risks, and credit and counterparty risks.
- 8.56 If the Scheme were to be implemented, the transferring LGAS policies would continue to be exposed to similar risk categories but, due to the different business mix, risk preferences, business model and demographic profile of ReAssure, the levels of exposure to each risk would be likely to change for the incoming LGAS policyholders.
- 8.57 Alongside the risks due to the different in-force business, LGAS and ReAssure hold different portfolios of assets and have different exposures to market risk, credit risk and liquidity risk.
- 8.58 Whilst the implementation of the Scheme would result in a change to the risk exposures of the transferring policies, it should be noted that:
- The SCR calculated in accordance with the Solvency II regime will reflect the risk exposures of the relevant company, including the transferring business, if relevant;
  - The capital held in ReAssure comfortably exceeds the required SCR; and
  - As at 31 December 2018, the capital held in ReAssure exceeds the level required under the ReAssure RA Statement.
- 8.59 In respect of liquidity risk, ReAssure has carried out a comparison of its liquidity risk policy with that of LGAS and:
- In respect of the transferring unit-linked business not currently in the LGAS WPF, where any gaps have been identified relative to the safeguards provided under the LGAS policy, ReAssure has incorporated updates to address these areas as part of its recent review of the liquidity policy in April 2019 (unless disproportionately onerous to implement relative to the expected increase in policy strength).
  - In respect of the business of the LGAS WPF that would transfer into the LGWPF, ReAssure has agreed to adopt the existing LGAS approach to liquidity risk management in the medium term.
- 8.60 ReAssure's amended liquidity policy includes a commitment to maintain the prevailing liquidity management standards for the transferring LGAS WPF business in the medium term following the implementation and I am satisfied that the latest updates to ReAssure's liquidity policy would provide sufficient safeguards for the transferring

business. These updates are subject to review and approval by the ReAssure Board and have not yet been finalised and I will comment further on ReAssure's liquidity policy in my Supplementary Report.

- 8.61 Based on the information I have received to date, I am satisfied that, although the implementation of the Scheme would cause a change to the profile of risks to which the transferring policies are exposed, this would not have a material adverse effect on the security of the benefits of the transferring policies.

## **THE EFFECT OF THE SCHEME ON THE REASONABLE EXPECTATIONS OF THE TRANSFERRING POLICYHOLDERS IN RESPECT OF THEIR BENEFITS**

### **Introduction**

- 8.62 The transferring LGAS business consists of with-profits, unit-linked, and non-profit business. For these types of business the policyholders' reasonable expectations in respect of their benefits are that:

- They receive any guaranteed benefits payable under their policy on the dates and in the contingencies specified in the terms and conditions;
- In respect of unit-linked policies that the Scheme does not have a material adverse effect on:
  - The range of funds available, the management of those funds, the investment objectives applied to those funds, the charges applied to those funds or the pricing of those funds;
  - The benefits received by the policyholders as these should continue to reflect the investment performance of the assets in which their units are invested and the contractual charges payable under the policies; or
  - The assets in which the units under unit-linked policies are invested as these should continue to be materially in line with the target investment allocation in the relevant fund literature.
- In respect of with-profits policies that the Scheme does not have a material adverse effect on:
  - The level of discretionary benefits (i.e. declared bonuses) applied to their policies;
  - The charges taken, as specified in the policy conditions; or
  - The link between the level of bonuses received and the investment performance of the LGAS WPF and the appropriateness of the levels of smoothing applied.
- In respect of non-profit policies that the Scheme does not have a material adverse effect on:
  - The likelihood that they receive their benefits when due; or
  - The size or frequency of those benefits.

- 8.63 In the following sections I cover the effect that the implementation of the Scheme would have on the reasonable expectations of the transferring policyholders in respect of unit-linked, with-profits and non-profit policies.

### **The reasonable expectations of the transferring unit-linked policyholders in respect of their benefits**

#### *Introduction*

- 8.64 If the Scheme were to be implemented, the unit-linked funds associated with the transferring LGAS business would transfer to ReAssure and the investment management of the funds would be outsourced to LGIM. The unit-linked liabilities associated with the transferring business would also transfer to ReAssure.
- 8.65 A large proportion of the transferring unit-linked business has been written into the LGAS WPF but does not participate in the profits of the fund. In terms of the reasonable expectations of these policyholders in respect of their benefits, there is no difference to those of the holders of unit-linked policies that have been written outside of the LGAS WPF and so I have considered these together.

#### *Restructuring of the transferring unit-linked funds*

- 8.66 Some of the transferring unit-linked funds have recently been restructured to ensure alignment with ReAssure's operating model. I have reviewed these restructurings and I am satisfied that this change would not have an impact



on the unit prices or charges that apply and therefore would not have a material adverse effect on the transferring policyholders.

#### *Future changes to the transferring unit-linked funds*

- 8.67 If the Scheme were to be implemented, ReAssure would be permitted to make changes to unit-linked funds in the future as long as the ReAssure Board considers that the changes are equitable between the affected policyholders and are not impracticable, inappropriate or unfair to policyholders affected having taken advice from the ReAssure Chief Actuary and the ReAssure FC.
- 8.68 I have reviewed these proposals and I am satisfied that:
- ReAssure's powers for making such changes are not materially different to those of LGAS currently; and
  - Sufficient safeguards are in place under the Scheme such that should such an action be performed by management in the future it would not have a material adverse effect on the transferring policyholders.

#### *The division of the unit-linked funds with both transferring and non-transferring policies*

- 8.69 Until recently, the units in some of the LGAS unit-linked funds were held by both transferring and non-transferring policies. These unit-linked funds would have needed to be divided to enable the transferring policies to be transferred to ReAssure.
- 8.70 As set out in Section 5 LGAS has implemented a project, called the Funds Foundation Project, which had as one of its objectives the division of the unit-linked funds. This included the division of the LGAS pension property fund, which involved the allocation of approximately 50 directly held properties between the transferring and non-transferring business.
- 8.71 The Funds Foundation Project was initiated in 2017 and is therefore not part of the Scheme. However, it has been accelerated in order to ensure that the separation of unit-linked funds between transferring and non-transferring business will be complete in advance of the Economic Effective Date and it is therefore appropriate that I comment on the effect of the project as part of my assessment of the Scheme.
- 8.72 The division of the unit-linked funds (including the property fund) presented the following risks to the transferring and non-transferring policies:
- The resulting funds may have a different risk and return profile to the pre-division fund:

The majority of the unit-linked funds have been straightforward to apportion due to the divisibility of the assets held within the fund. However, the approach to splitting the property fund involved apportioning the individual property assets between two funds (as property assets are not straightforward to divide) and it was not possible to create two new funds with identical risk and return profiles as the original portfolio.
  - The risk of mis-valuation of the assets:

The difficulty of constructing objective valuations for property assets presented a material risk of mis-valuation in respect of any particular property and the risk of an adverse effect on the policies concerned is increased in the situation where property assets are being allocated to funds. This presented a challenge in terms of determining a split that is fair to all groups of policyholders.

In valuing the properties underlying the property funds, LGAS carry out one valuation for each property. Given the lack of comparability between properties and the non-standard nature of property valuations it might be considered prudent to undertake more than one valuation of each property to provide a check on the valuation received from their valuer (CBRE). LGAS did not see the benefit of further valuations because:

    - CBRE is a market leader in UK property valuations with over 300 valuation experts and 11 offices across the UK.
    - CBRE has acted as the valuer for the LGAS property fund for over a decade and possess knowledge of the specific properties that could not easily be obtained by another valuer in the timeframe.
    - Back-testing of the sale of recent properties within the fund has shown the accuracy of CBRE's valuations as they have been either in line with, or higher than, the CBRE valuations. Where sales have been higher than the valuation, reasons can be explained for the difference.

- The valuations that are received by LGAS from CBRE are reviewed and challenged, where necessary, by LGIM 'Real Assets', which is one of the UK's largest real assets managers and an expert in this field.
- The risk of a material effect from a change in the pricing basis used for the unit-linked funds:

The division of the unit-linked funds could result in a change in the pricing basis for the unit-linked fund. For example, where a unit-linked fund is currently expanding, the unit price will be calculated using an 'offer' basis such that the unit price allows for the costs of purchasing additional assets in the fund. Where the fund is a contracting fund, the unit price will be calculated using a lower 'bid' basis such that the unit price allows for the costs of selling assets within the fund. A separation of a unit-linked fund could lead to a change of pricing basis (between offer and bid) which could have an effect on the value of the policy. This effect could be larger for a property fund due to the typically larger difference between an offer and bid pricing basis for property funds.

- 8.73 Following completion of the work, LGIM's Valuations team has undertaken a full reconciliation of the activity undertaken and identified a number of operational issues that resulted in post-split errors relating to some assets. Adjustments will be made by LGIM to correct the position of the funds. The corrective positions, net asset value impact, and proposed recommended actions will be overseen by the ULMC.
- 8.74 LGAS commissioned a two-part report from Deloitte to first comment on the fairness of the proposed methodology and secondly to comment on the implementation of the approved methodology of the separation of the property fund. I have seen the Deloitte report and I am satisfied that the recommendations within the Deloitte report have been actioned and therefore the methodology adopted to separate the unit-linked property fund and the implementation of this methodology do not result in a material adverse impact on transferring policyholders.
- 8.75 However, the Deloitte report does not directly address the issues described above regarding the valuations of the properties within the property fund nor the effect of the separation on the pricing basis. I have raised this with LGAS and have been persuaded that the use of a single valuation from CBRE is reasonable and that the fund will not be systematically impacted by a change in pricing basis. I am therefore satisfied that the separation of the LGAS pension property fund does not lead to a material adverse impact on the transferring policyholders.
- 8.76 In respect of the other unit-linked funds, I have queried this issue with LGAS and I have been provided with a statement from LGAS that indicates that the funds would not be affected by a systematic change in the pricing basis.
- 8.77 Although the pricing basis of each of the funds is assessed on a daily basis dependent on the net cash flow position of each fund, the statement from LGAS indicates that, in the long-term, because the funds are predominantly legacy funds, that are not actively marketed, they are currently contracting and are expected to remain contracting for the foreseeable future.
- 8.78 I am therefore satisfied that the separation of these unit-linked funds does not lead to a material adverse impact on the reasonable expectations of the transferring LGAS unit-linked policyholders in respect of their benefits.

#### *Conclusion in respect of the reasonable expectations of transferring unit-linked policyholders*

- 8.79 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the transferring LGAS unit-linked policyholders in respect of their benefits.

### **The reasonable expectations of the transferring with-profits policyholders in respect of their benefits**

#### *Introduction*

- 8.80 If the Scheme were to be implemented, all of the assets and liabilities within the LGAS WPF would move into a newly created with-profits fund within ReAssure called the LGWPF. The LGWPF would be a ring-fenced fund in line with the definition under Solvency II and the assets within this fund would not be available to support any of the other ReAssure funds or to provide additional capital in support of the capital policies for those funds.
- 8.81 The LGWPF would be intended to replicate the LGAS WPF such that, if the Scheme were to be implemented, ReAssure would be able to treat the transferring with-profits policies as they would be treated if the Scheme were not implemented and they remained in LGAS.



8.82 That said, ReAssure is a different company to LGAS and has different management and governance structures and therefore, if the Scheme were to be implemented, there would be some changes for the with-profits policies that would be transferred to the LGWPF in ReAssure:

- The management of the with-profits business would change from LGAS to ReAssure. ReAssure has proposed a number of practical changes to the management of the fund. These changes are described in Section 7 and are largely required as a result of changing from the existing LGAS systems.
- The tax position of the LGWPF if the Scheme were to be implemented compared to that of the LGAS WPF currently.
- Any changes to the investment strategy of the LGWPF.
- The LGWPF would make a one-off payment of £50 million to the RNPF as a contribution to migration costs.
- The fixed expense agreement for the LGWPF.
- The potential for the future reallocation of the non-profits business in the LGWPF to the RNPF.
- The introduction of 'sunset clauses' in relation to the LGWPF.

8.83 I cover these in turn below.

#### *Changes to the bonus methodology for the transferring with-profits business*

8.84 The bonus rates that apply to the with-profits policies in the LGAS WPF are currently calculated by LGAS, recommended by the LGAS WPA, reviewed by the LGAS WPC and approved by the LGAS Board. If the Scheme were to be implemented there would be a number of changes to the bonus rate setting process as:

- The bonus rates would be calculated by ReAssure, recommended by the ReAssure WPA, reviewed by the ReAssure FC and subject to the approval of the ReAssure Board.
- ReAssure would simplify the current (LGAS) approach to setting bonuses on UWP policies in order to:
  - Reduce the associated operational risk; and
  - Reduce volatility in the bonus rates by further pooling the experience, and the profits and losses from surrender, for different groups of UWP policies in the LGWPF.

8.85 I have reviewed the proposed changes to the bonus setting process and, in my view, the proposed changes would help to ensure that ReAssure has the capability and capacity to manage the LGWPF following the implementation of the Scheme and I am satisfied that the proposed changes would not have a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

8.86 The LGAS WPA has also reviewed the proposed changes and she is satisfied that there would not be any systematic increase or decrease in the benefits paid to with-profits policyholders overall nor a material adverse effect on any particular group of with-profits policyholders as a result of these changes.

8.87 While the approach to setting bonuses on CWP policies is also due to change for the year end 2019 bonus declaration, for the avoidance of doubt, this is solely to reflect changes to the nature and duration of the in-force portfolio as the business runs off and not a consequence of the proposed implementation of the Scheme.

8.88 In light of the narrow timeframe between the Legal Effective Date and the year-end 2019 bonus declaration, in order to ensure that there would be no material adverse effect on the transferring with-profits policyholders' benefits as a result of the implementation of the Scheme, ReAssure and LGAS have agreed that LGAS's actuarial models would be used to support the year-end 2019 bonus declaration in February 2020 under the dual governance of both parties. ReAssure's models would then be used for future bonus declarations.

#### *Changes to the capital management of the transferring with-profits business*

8.89 The LGAS WPF is currently managed with reference to both its Solvency II and Economic Capital (Pillar 2) solvency coverage ratios for risk appetite and run-off purposes and, if the Scheme were to be implemented, this would continue to be the case for the LGWPF within ReAssure.

- 8.90 ReAssure does not have access to the LGAS Economic Capital model and so ReAssure has developed the methodology by which it would calculate the Economic Capital position of the LGWPF if the Scheme were to be implemented.
- 8.91 ReAssure has shared indicative calculations of the Economic Capital calculated using the proposed methodology for the LGWPF as at 30 June 2018 and 31 December 2018. This proposed methodology is based on:
- The Standard Formula for the Solvency II SCR for its with-profits funds;
  - Comparable Economic Capital calculations that are used for the risk management and estate distribution of two of its existing with-profits funds (the WLWPF and the NMWPF);
  - Economic stress parameters and results for the LGAS WPF which are used for asset liability management purposes by LGAS; and
  - Standard Formula results for the LGAS WPF for non-economic variables shared by LGAS.
- 8.92 In developing its proposed approach to deriving the Economic Capital position of the LGWPF, ReAssure has applied the following principles:
- Achieve a similar Economic Capital result to that currently calculated by LGAS for the LGAS WPF so that the speed of any future estate distribution would be unaffected by the transfer;
  - Ensure coverage of all relevant risks, including those excluded from the Standard Formula calculation;
  - Ensure the overall calibration of risk stresses is broadly consistent with the LGAS model; and
  - Use an approach that is consistent with that used for the WLWPF and NMWPF.
- 8.93 The proposed methodology has been updated to reflect an analysis of the differences between the indicative calculations and the results of the LGAS Economic Capital model as at 30 June 2018 and 31 December 2018.
- 8.94 ReAssure will carry out a more detailed analysis of the Economic Capital position within 12 months of the Legal Effective Date and will update the methodology where this is deemed necessary. The methodology will also be refined to take into account industry developments and any changes to the risk profile of the LGWPF. Any changes to the methodology would be escalated to the ReAssure FC for review and subsequently to the ReAssure Board for approval.
- 8.95 The proposals for the future management of the LGWPF have been reviewed and approved by the ReAssure WPA, the ReAssure FC, and the ReAssure Board and various papers have been circulated that examine the effects of the proposed approach at both 30 June 2018 and 31 December 2018.
- 8.96 The proposals have also been reviewed and approved by the LGAS WPA and the LGAS Chief Actuary who have stated that they believe that the proposed Economic Capital approach to the management of the LGWPF by ReAssure as set out in the ReAssure proposals would not lead to a material adverse effect on capital management of the LGWPF compared to that of the LGAS WPF and therefore no material adverse effect on the reasonable expectations of the transferring business in respect of their benefits.
- 8.97 I have reviewed the results of this indicative calculation and the comparison against the LGAS Economic Capital results as at 30 June 2018 and 31 December 2018, and I am satisfied that the proposed methodology would not have a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

#### *The investment management strategy of the LGWPF*

- 8.98 If the Scheme were to be implemented, ReAssure has committed that it would not make any major changes to the investment strategy (including the management of liquidity and the hedging of economic risks within the LGWPF) within two years of the implementation of the Scheme. There is an exception in the event that the governance bodies overseeing the LGWPF consider that an 'economic shock' has occurred, the assessment of which would depend on the specific circumstances at the time including the effectiveness of the hedging strategy in place.
- 8.99 This commitment has been discussed and agreed by both the ReAssure FC and the ReAssure Board.
- 8.100 Following this, ReAssure expects to manage the LGWPF investment strategy in accordance with its generalised treatment of with-profit funds in run off and subject to ReAssure governance.

- 8.101 The target operating model for derivatives in the LGWPF within ReAssure is currently being developed, with the intention being for ReAssure to use LGIM to manage derivatives for the LGWPF on a client-directed basis. Furthermore, processes are being developed to legally transfer existing derivatives positions to the LGWPF within ReAssure as part of the proposed Scheme, and to replicate existing derivatives documentation with bank counterparties to allow ongoing trading and collateralisation. LGAS and ReAssure have committed to providing regular updates on progress relative to plan. However, based on the proposals and on progress to date, I do not envisage any material issues arising. I will provide an update on this issue, if necessary, in my Supplementary Report.
- 8.102 As set out in Section 7, following the successful implementation of the Scheme, the unit-linked box owned by the LGWPF would be transferred to the RNPF in exchange for a compensation payment from the RNPF to the LGWPF. The level of such compensation has not yet been determined but would be subject to the governance of the ReAssure Board and the ReAssure FC. I will comment further on this issue in my Supplementary Report.
- 8.103 Based on the information I have received to date, I am satisfied that the proposed investment management strategy for the LGWPF would not have a material adverse effect on the reasonable expectations of the transferring LGAS business in respect of their benefits.

*The tax position of the LGWPF compared to that of the LGAS WPF*

- 8.104 The effects of the implementation of the Scheme on the tax position of the LGWPF compared to that of the LGAS WPF are discussed in Section 14 of this report and I am satisfied that any change in the tax position of the LGWPF compared to that of the LGAS WPF as a result of the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

*The one-off charge for the cost of the transfer and the introduction of a fixed expense arrangement*

- 8.105 If the Scheme were to be implemented there would be a one-off payment by the LGWPF of £50 million to the RNPF as a contribution to migration costs, which would reduce the assets in the LGWPF. At the same time, there would be a corresponding release of the £50 million reserve currently held by the LGWPF in respect of migration costs, resulting in no net impact on the LGWPF estate. Other than this charge, the implementation of the Scheme would leave the level of assets within the fund unchanged relative to that before the Scheme.
- 8.106 Alongside this charge a fixed expense arrangement has been agreed between the LGWPF and ReAssure whereby the expenses charged to the LGWPF would be fixed until the last policy runs-off, matures, lapses or is surrendered, subject to increases each year of RPI + 0.5%. These charges would:
- Cover all business as usual expenses (excluding in respect of the investment management fees paid to LGIM under the IMA) and exceptional expenses, including those related to regulatory activities; and
  - Exclude any compensation or redress payments arising from historic actions (i.e. on or before 31 July 2009) which would represent an additional charge to the fund, however, it would cover administration payments in relation to such payments.
- 8.107 The fixed expense arrangement would:
- Provide certainty to the with-profits policyholders and therefore reduce the expense risk of the LGWPF and release the associated regulatory capital requirement; and
  - Remove the benefit to LGWPF of any potential future expense savings.
- 8.108 The fixed per-policy schedule for in-force business will be defined in 2019 such that the total charges would equate to £32.4 million for 2018. This is below the cap of £35.5 million for the per-policy expenses charged to the LGAS WPF in 2018 under the current fixed expense deal in LGAS. The fixed expense arrangement would also cover one-off additional per-policy charges for any new business written in the LGWPF.
- 8.109 If the policy counts were to change as a result of the migration then adjustments would be made to both the in-force and new business per-policy charges to ensure that the overall charge per product group (and for the LGWPF as a whole) remained unchanged. These adjustments will be subject to the approval of the ReAssure Board having regard to the advice of the ReAssure WPA and the ReAssure FC.

- 8.110 The per-policy charges applied to each product group in 2019 and subsequent years will be set equal to the per-policy charges for 2018, increased in line with RPI + 0.5%.
- 8.111 Other than in respect of increments accepted on pension business and new members for certain workplace schemes (which would be covered under the fixed expense arrangement), the LGAS WPF is already, and the LGWPF would be, closed to new business and in run-off. It would be exposed to expense diseconomies of scale as the overheads associated with the ongoing maintenance of the fund would be spread over a decreasing population of policyholders and therefore the per-policy costs would be expected to increase (in excess of expense inflation) over time. A fixed expense arrangement would therefore be of value to the with-profits policies in the LGWPF.
- 8.112 Analysis has been carried out by LGAS to demonstrate that the expected economic benefit of the fixed expense arrangement to the LGWPF is greater than the contribution to migration costs of £50 million. I have reviewed this analysis for reasonableness, and the conclusions of the LGAS WPA and the WPC in respect of the fixed arrangement for the LGWPF, and I am satisfied that the payment of the one-off charge for the cost of the migration and the introduction of the fixed expense agreement would not have a material adverse effect on the reasonable expectations of the with-profits policyholders in the LGWPF in respect of their benefits.

#### *The potential future reallocation of non-participating business*

- 8.113 If the Scheme were to be implemented, the non-profit business of the LGAS WPF would be transferred to the LGWPF in ReAssure and the Scheme provides for a reallocation of this non-profit business to the RNPF in the future should the ReAssure management choose to do so. A number of safeguards exist within the Scheme to ensure that if and when this reallocation were to take place it would be fair to affected policyholders. These include that the reallocation would:
- Be consistent with the terms of the affected policies;
  - Be in accordance with relevant laws and regulations;
  - Not change the terms and conditions of the affected policies;
  - Require approval by the ReAssure Board and be subject to consultation with the ReAssure FC;
  - For aggregate reallocations in any 12 month period involving a transfer of assets above £150 million (adjusted for inflation), require a report by an independent actuary and non-objection from the appropriate regulator; and
  - Provide, in the opinion of the ReAssure Board following receipt of adequate actuarial advice, compensation to the LGWPF that is fair and equitable to affected policyholders.
- 8.114 ReAssure has also advised me that an internal reinsurance arrangement would be set up between the RNPF and the LGWPF so that the non-profit policies could retain the right to switch into UWP units in the future.
- 8.115 As stated above, if the reallocation were to be less than a certain threshold then the Scheme would only require Board approval (after consulting the Fairness Committee) for the reallocation to take place. This was discussed at the joint Fairness Committee/Board meeting in May 2019 and it was agreed (as reflected in the minutes) that in practice for transfers below the £150 million threshold, Board notification to the regulators would take place regardless of the threshold.
- 8.116 I consider these safeguards to be sufficient to protect the interests of the transferring with-profits policyholders in the instance of a reallocation of the non-participating business from the LGWPF to the RNPF subsequent to the implementation of the Scheme such that there would not be a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

#### *The introduction of 'sunset clauses' to the LGWPF*

- 8.117 The Scheme allows for the following, so called, 'sunset' clauses in relation to the LGWPF such that when the assets held within the LGWPF fall below certain threshold levels:
- The remaining policies can be converted into non-profit policies and reallocated to the RNPF; or
  - The remaining policies can be absorbed into one of the other existing with-profits funds of ReAssure.
- 8.118 In addition, the Scheme allows for the possibility that the LGWPF could absorb one of the existing with-profits funds of ReAssure.

- 8.119 In such circumstances, the Scheme provides a range of safeguards such that the implementation of such sunset clauses would:
- Be in accordance with relevant laws and regulations;
  - Be approved by the ReAssure Board and be subject to consultation with the ReAssure FC;
  - Not be objected to by either the PRA or the FCA within two months of notification;
  - Not, in the opinion of the ReAssure Board following receipt of adequate actuarial advice, materially adversely affect the affected policyholders;
  - Not, in the opinion of an independent actuary, materially adversely affect the affected policyholders;
  - Take the provisions of the fixed expense arrangement for the LGWPF into account;
  - For a merger of the LGWPF with an existing with-profits fund of ReAssure:
    - Require all with-profits policies to still be with-profits policies following the merger, and
    - Require the PPFM of the destination fund to be appropriately updated to take account of the provisions of the incoming with-profits fund;
  - For a reallocation of the LGWPF policies to the RNPF, make appropriate allowance for the future shareholder transfers that would have otherwise been made from the LGWPF to the RNPF.
- 8.120 I consider these safeguards to be sufficient to protect the interests of the transferring with-profits policyholders in the instance that any of these sunset clauses are triggered and implemented following the implementation of the Scheme such that there would be a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

#### *The With-Profits Thematic Review*

- 8.121 As described in Section 5, LGAS has recently sent a number of mitigating actions and associated delivery dates to the FCA in relation to the With-Profits Thematic Review.
- 8.122 Given the timing of delivery dates relative to the proposed Scheme, it has been jointly agreed by LGAS and ReAssure that, if the Scheme were to be implemented, ReAssure would take responsibility for an agreed set of actions relating to items that would reasonably require review after the implementation of the Scheme.
- 8.123 I have reviewed the FCA feedback to LGAS in relation to the With-Profits Thematic Review, and the proposed actions and delivery dates and there does not appear to be any reason to suggest that ReAssure would deliver these actions any less effectively than LGAS would in the absence of the Scheme.
- 8.124 I am therefore satisfied that the implementation of the Scheme would not have a material adverse effect on the work conducted as part of the With-Profits Thematic Review.

#### *Conclusion in respect of the reasonable expectations of transferring with-profits policyholders*

- 8.125 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

#### **The reasonable expectations of the transferring non-profit policyholders in respect of their benefits**

- 8.126 If the Scheme were to be implemented then there would be no change to the terms and conditions of the transferring non-profit policies (except that the policies would become policies of ReAssure) or to the charges that apply to the transferring policies other than those described in the 'product changes' section below.
- 8.127 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the transferring non-profit policyholders in respect of their benefits.

## THE EFFECT OF THE SCHEME ON THE STANDARDS OF ADMINISTRATION AND SERVICING APPLIED TO THE TRANSFERRING LGAS POLICIES

### Data migration and operational readiness

8.128 If the Scheme were to be implemented ReAssure would take over the administration of the majority of the transferring business. As the IT systems used to administer and service the transferring business would not transfer, all of the policy data would migrate from the current LGAS administration systems to the ReAssure administration systems ahead of the Legal Effective Date.

8.129 To support the migration of the policy data from LGAS to ReAssure and, more widely, to ensure operational readiness of both parties for the transfer and the protection of customer outcomes, a plan has been put in place that covers four key areas:

- **Programme structure and tracking:**

The plans and status of all Part VII workstreams are tracked using detailed metrics relating to the data migration and systems development. Progress against agreed targets is reported regularly, with any issues arising escalated to joint governance committees to ensure the programme remains on track to achieve a successful cutover.

- **Readiness gate assessments:**

Readiness criteria have been set by LGAS and ReAssure based on the outcomes that need to be achieved in order to safely transfer the business, including ReAssure having:

- Suitable capabilities to support the business functions with the necessary staff and skills to deliver customer service standards;
- Fit for purpose systems with extended systems functionality (all fully tested);
- Third party providers transitioned with relationship management in place; and
- Financial reporting readiness and reconciliation.

The readiness criteria are supported by a set of defined evidence (e.g. completion reports, specific sign-offs, signed contracts) and used to make formal 'Go / No go' decisions at four key points or 'readiness gates':

- Regulatory submission;
- The Directions Hearing;
- The Sanctions Hearing; and
- The Legal Effective Date.

The specific criteria for the Directions Hearing have been finalised by LGAS and ReAssure but those for subsequent readiness gates will be agreed closer to the time of these assessments.

- **Monitoring ongoing stability:**

Jointly agreed metrics such as complaints, breaches and call handling response times will be monitored for both the transferring business and the existing business of ReAssure to ensure that ReAssure will be able to take on the volumes of work being transferred.

- **Contingency options:**

LGAS and ReAssure have defined the scenarios that may delay the Part VII and agreed a Plan B should this be required.

8.130 ReAssure is developing online portals called 'ReAssure Now' and 'ReAct', for use by transferring policyholders and sponsoring employers of occupational pension schemes respectively. Testing to ensure that these portals provide broadly equivalent functionality to transferring LGAS policyholders as the existing LGAS online portal, including a review by LGAS subject matter experts and stakeholders, will be conducted. I will cover the results of this review in my Supplementary Report.

8.131 ReAssure has identified the additional resources that it requires to ensure that it has adequate skilled staff to support the transferring business following the Legal Effective Date. The recruitment process, including the relevant training



is ongoing. In addition, a satellite office is being set up for LGAS actuarial resources that are due to transfer over to ReAssure to support its existing actuarial resources. Ongoing monitoring and reporting of this recruitment process is being conducted as part of the plan set out above.

- 8.132 LGAS and ReAssure have committed to providing me with regular updates on business readiness and in particular with the reports, risk review results and other management information that are to be sent to the appropriate governance committees in advance of each of the four readiness gates.

#### **The report of the ReAssure CRO dated 17 June 2019**

- 8.133 I have received a private report dated 17 June 2019 from the ReAssure CRO addressed to the ReAssure Board. This report was provided in order to give the ReAssure Board an overview of the overarching risk position of the migration plan in relation to the firm's risk appetite. The report indicated that, in the CRO's opinion, the project was behind schedule and in particular:
- There were a number of material issues with the migration project that required management actions to be taken to reduce the risk of the migration back into tolerance;
  - A number of the key indicators were tracking below target; and
  - This assessment was driven by the volume of changes still required to meet the Legal Effective Date and the overall complexity of the migration.
- 8.134 I have subsequently had a number of discussions with both ReAssure and LGAS and the CRO and the CEO of ReAssure have provided assurance that the issues outlined in the CRO's report of 17 June 2019 are being addressed, that the extra resource requirements have been quantified, and that the required recruitment of these resources is underway. The CEO and CRO of ReAssure have provided further assurance that the migration plan has been revised and, that they are confident that the migration can be successfully delivered in time for the Legal Effective Date although it is expected that some additional manual processes will be in place for a period after the Legal Effective Date while building and testing of systems is completed.
- 8.135 Migration projects, particularly one involving such a large and diverse portfolio of business as the LGAS transferring business, are complex, have unpredictable resource demands, and can give rise to substantial unforeseen issues arising throughout. That said, the conclusions in the CRO's report were not encouraging regarding the status at that point and the likelihood of a successful migration in time for the Legal Effective Date. The consequences of "going live" with new systems before they are fully ready and tested can be extremely serious, and it is essential the migration is undertaken in a controlled way.
- 8.136 It is the responsibility of the ReAssure Board and the LGAS Board to ensure that this migration is implemented successfully and without any detrimental effect on service standards or the accuracy of benefit calculations for either transferring policyholders or existing ReAssure policyholders and I will rely on the ReAssure Board and the LGAS Board in this respect. In particular I will rely on the Boards of the firms to ensure that the migration project is given the appropriate priority, that the required planning is carried out, and that the required resources are secured, such that the status of the migration project is quickly improved and the CRO is able to report that the risks have been reduced to an acceptable level.
- 8.137 To facilitate this monitoring by the Boards and to enable me to keep track of progress on the migration project, I have requested that the ReAssure CRO provides a detailed monthly report (in a similar format to the CRO Report dated 17 June 2019) on the status of the migration project. These reports will be produced as at 30 June 2019, 31 July 2019, 31 August 2019, 30 September 2019, 24 October 2019 and beyond if the Legal Effective Date is moved beyond the current expected date of 4 November 2019.
- 8.138 These CRO reports will be addressed to the ReAssure Board and made available to the LGAS Board, me, the LGAS WPA, the LGAS Chief Actuary, the ReAssure WPA and the ReAssure Chief Actuary (and would be available for the regulators if requested).
- 8.139 The purpose of these CRO reports is to ensure that the Boards and senior management of both firms are aware of any issues which may threaten an orderly migration as they arise, and are able to react to these issues quickly and efficiently. The reports will enable me, and the WPAs and the Chief Actuaries of the firms to continue to monitor progress against plan and be aware of any issues as they arise.
- 8.140 I will report on the outcome of these updates in my Supplementary Report for the Sanctions Hearing.

### Approach to tracing “gone-aways”

8.141 A policyholder is considered a gone-away where their provider is unable to contact the customer regarding the policy or benefits using paper or electronic correspondence<sup>3</sup>. Both LGAS and ReAssure conduct tracing processes for gone-aways as part of their business as usual processes.

8.142 For LGAS, once a policyholder is classified as a gone-away other potential sources of information are checked such as:

- Alternative email addresses or telephone numbers if they have been provided.
- Other details, for example, if there is another policyholder listed on the policy.
- Details held in relation to other products, if applicable.

The tracing uses sources such as Experian, Google searches, BT directory enquiries, 192.com database search, insolvency data, agreed social media, and Companies House website (for trustees). Once initial tracing has been performed, further tracing is carried out every three years thereafter.

8.143 ReAssure use an external supplier (Equifax) to perform the gone-away tracing and the tracing process is carried out every two years.

8.144 Further tracing processes in respect of gone-aways are being carried out as part of the transfer and further detail is provided on the additional work in Section 13.

8.145 While there are differences between the approaches taken by LGAS and ReAssure in tracing policyholders that have been classified as gone-aways, I am satisfied that both processes are suitably comprehensive and robust.

### THE STANDARDS OF MANAGEMENT AND GOVERNANCE APPLIED TO THE TRANSFERRING LGAS POLICIES

#### The governance arrangements under ReAssure

8.146 Currently the transferring business is in LGAS and:

- The LGAS WPA fulfils the statutory role of WPA and provides oversight for the LGAS WPF;
- Executive oversight of the management of the LGAS WPF is provided by the WPMC and ALCO;
- The LGAS WPC provides independent oversight and challenge in respect of the management of the LGAS WPF;
- The ULMC provides oversight of the management of the transferring unit-linked funds of the Mature Savings business;
- The FPC is a sub-committee of the ULMC that provides oversight of investment of policyholder assets and monitors investment performance;
- The divisional PICCs provide oversight of underwriting and reinsurance by the actuarial function;
- The divisional RCCs assist LGAS CEOs in the management of risk and compliance, with escalation as appropriate to the Group Risk Committee;
- The IGC provides oversight of the LGAS workplace pension products; and
- Ultimate responsibility for governance resides with the LGAS Board.

8.147 LGAS and ReAssure have undertaken governance reviews to determine the governance framework and requirements of ReAssure should the Scheme be implemented and in light of the outcome of these reviews a number of changes have recently been made. The revised ReAssure governance framework would provide oversight of the management of the transferring business through:

- A ReAssure WPA to fulfil the statutory role of WPA and provide oversight for the LGWPF;
- A newly created executive committee, the ReAssure WPMC, which was set up in March 2019 and incorporates the existing responsibilities of the LGAS WPMC and ALCO;

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<sup>3</sup> ABI Framework for the Management of ‘Gone-Away’ Customers in the Life and Pensions Market



- The ReAssure FC, which provides independent oversight of the management of ReAssure's with-profits funds and the fair treatment of policyholders and would extend its scope to include the transferring business;
- The ReAssure BIC, which recommends overall investment strategy, policy and asset allocation and would take on the main duties and responsibilities of the ULMC;
- The ReAssure PIC, which oversees that investment of policyholder assets is fair, compliant and in line with customers' reasonable expectations;
- A newly created ReAssure FPWG, for which the terms of reference were approved in March 2019 and a schedule of monthly meetings is currently being set up to review policyholder fund performance and report to the ReAssure PIC;
- The ReAssure UPC, which has responsibilities regarding the monitoring and management of box positions for ReAssure's unit-linked funds and oversight of discretion on the pricing of funds;
- The TCF Management Committee, including the ReAssure PMC sub-committee, which provides dedicated oversight of non-profit and unit-linked conduct and TCF related matters by both ReAssure and its chosen outsource providers;
- The ReAssure BRC;
- The ReAssure GMRC;
- The ReAssure IGC, which reviews the value for money for policyholders of the ReAssure workplace personal pensions; and
- The ReAssure Board.

#### **The WPA in respect of the LGWPF**

- 8.148 A WPA would be appointed to provide oversight for the LGWPF, which may either involve an extension of the existing ReAssure WPA role or the appointment of a second, dedicated WPA in respect of the LGWPF.
- 8.149 In either case, as a UK insurer writing long-term with-profits insurance business, ReAssure must adhere to the rules of the PRA and FCA and in particular:
- Chapter 4 of the Supervision Manual of the FCA Handbook; and
  - The FCA's Senior Management and Certification Regime.
- 8.150 As the person appointed as WPA in respect of the LGWPF must be approved by the PRA (after consultation with the FCA) this will ensure that the person appointed as WPA in respect of the LGWPF is fit and proper, and has the relevant expertise and experience to carry out the role. ReAssure has also advised that it would assess the candidate's knowledge, competency and capacity to fulfil the role and build plans to address any gaps.

#### **The ReAssure WPMC**

- 8.151 The membership of the ReAssure WPMC is materially the same as that of the LGAS WPMC and ALCO and includes the Heads of the areas responsible for management of the with-profits funds as additional attendees. In particular, the ReAssure CRO is a member of the WPMC and can provide input from the risk function on with-profits issues.
- 8.152 Furthermore, the ReAssure WPMC was set up in March 2019 to allow sufficient time to build knowledge prior to the implementation of the Scheme.
- 8.153 I have reviewed the differences between the terms of reference and membership for the ReAssure WPMC against those of the LGAS WPMC and the ALCO and I am satisfied that these differences would not have a material adverse effect on the transferring policies.

#### **The ReAssure FC**

- 8.154 ReAssure has provided a comparison of the terms of reference for the LGAS WPC with the updated terms of reference for the ReAssure FC and I am satisfied that there are no material gaps in terms of responsibilities.
- 8.155 There are two key challenges presented by the transfer of the LGAS WPF to ReAssure in terms of the management and governance of the new fund.

- 8.156 Firstly, the complexity of the LGAS WPF: the LGAS WPF has complexity in its operation, for example in respect of its hedging strategies that does not currently exist with the existing ReAssure with-profits funds.
- 8.157 At this point I have not been provided with information on the members of the LGAS WPC who have agreed to join the ReAssure FC (if any) but it is expected that at least one other member of the LGAS WPC would transfer across. I note also that the Chairman of the LGAS WPC is also currently the Chairman of the ReAssure FC and that, if the Scheme were to be implemented, this person would remain the Chairman of the ReAssure FC which would have responsibility for the new LGWPF. This provides continuity of knowledge that would be to the advantage of the transferring policyholders.
- 8.158 ReAssure will also arrange training to ensure that all ReAssure FC members are familiar with the LGWPF business and processes prior to the implementation of the Scheme.
- 8.159 The second key challenge due to the implementation of the Scheme arises from the size of the transferring LGAS WPF which, at assets under management of approximately £20 billion, is about five times the size of the combined existing ReAssure with-profits funds. The challenge is whether the ReAssure FC would have sufficient capacity to govern the LGWPF to the same standard as the LGAS WPC. I have discussed this with ReAssure and:
- For the first 12 months following the Legal Effective Date, the ReAssure FC meetings would be extended to four hours from the current two hour duration to allow the committee sufficient time to oversee both the existing ReAssure business and the newly transferred LGAS business, and to embed business as usual operations; and
  - After the first 12 months, the meetings would potentially reduce to three hours depending on the Chairman's view.

### **The ReAssure GMRC**

- 8.160 The ReAssure GMRC terms of reference have been changed to explicitly include the responsibility of the Chair of the ReAssure GMRC to provide relevant information to the ReAssure WPA and to the ReAssure WPMC in relation to with-profits issues.

### **The management and governance of unit-linked funds**

- 8.161 In order to ensure that ReAssure's unit-linked management and governance would be commensurate with that currently in place in LGAS, there is a programme of changes underway. In particular:
- The establishment of the ReAssure FPWG, reporting to the ReAssure PIC, ensures that sufficient time and resource can be devoted to reviewing policyholder fund performance for a larger fund range;
  - The production of a customer-facing ReAssure Unit-Linked Guide for the transferring business and development of ReAssure's existing internal unit-linked principles and practices documentation will ensure that ReAssure's future management of unit-linked funds is consistent with the approach currently taken by LGAS; and
  - Minor changes that have already been made to the terms of reference of other committees (notably the ReAssure PIC, the ReAssure UPC and the ReAssure PMC) have increased transparency in relation to responsibilities for the governance of ReAssure's unit-linked funds.
- 8.162 Based on the outcomes of the review conducted by LGAS comparing the LGAS and ReAssure governance frameworks, I am satisfied that the above adjustments will adequately address any gaps or differences that could be perceived as a weakening in systems and controls for the transferring LGAS unit-linked policies. I am therefore satisfied that the implementation of the Scheme would not have a material adverse effect on the standards of governance applied to the transferring LGAS unit-linked policies.

### **The ReAssure IGC**

- 8.163 Following its review of ReAssure's governance framework, LGAS raised the question as to whether scheme leavers and deferred members, which are currently overseen by the LGAS IGC, would fall within the scope of the ReAssure IGC if the Scheme were to be implemented.
- 8.164 ReAssure has since confirmed that this is the case and further has committed that the ReAssure IGC would oversee all of the transferring policies that are currently overseen by the LGAS IGC.

### **The ReAssure Board**

- 8.165 Following the implementation of the Scheme, the ReAssure Board would replace the LGAS Board as the governing body with ultimate responsibility for the transferring business. The ReAssure Board has relevant experience and expertise in managing the types of business that make up the transferring business. Furthermore, ReAssure has advised me that it will arrange training to ensure that all ReAssure Board members are familiar with the specificities of the LGWPF business and processes prior to the implementation of the Scheme.

### **Conclusion in respect of the governance arrangements under ReAssure**

- 8.166 I am satisfied that the ReAssure governance framework that will apply to the transferred LGAS policies if the Scheme were to be implemented would not have a material adverse effect on the transferring LGAS business.

### **The LGWPF PPFM**

- 8.167 The revised PPFM that would apply if the Scheme were to be implemented has been finalised to reflect the changes to the management of this business as a result of the Scheme and the different style of the existing ReAssure PPFMs.
- 8.168 I am satisfied that the changes to the PPFM would not have a material adverse effect on the transferring with-profits policyholders.

### **The risk management under ReAssure**

- 8.169 The LGAS Mature Savings Chief Risk Officer carried out a review comparing the management and control of risks between LGAS and ReAssure. I have been provided with a report on the outcome of this review, which concluded that although there are some differences in approach the core risk management and control activities are broadly comparable between LGAS and ReAssure.
- 8.170 Having reviewed this report, I am satisfied that the above conclusion is reasonable and that the implementation of the Scheme would not materially reduce the strength and effectiveness of the risk and control framework applied to the transferring LGAS business.

### **Conclusion**

- 8.171 I am satisfied that if the Scheme were to be implemented there would not be a material adverse effect on the standards of management and governance that would apply to the transferring LGAS business.

### **THE INVESTMENT MANAGEMENT AGREEMENT**

- 8.172 As described in Section 5, the IMA is an agreement between LGIM and ReAssure whereby investment management services in respect of the transferring LGAS business would remain with LGIM following the Economic Effective Date for a minimum period of 7 years.
- 8.173 Safeguards are built into the agreement such that, should LGIM underperform relative to investment benchmarks or manage the funds such that there is a breach of any regulatory requirements, the assets could be withdrawn by ReAssure.
- 8.174 As set out in Section 7 any VAT on the fee for the investment management services would initially be paid for from the RNPF and would not affect policyholder benefits. After the IMA period ends, the Scheme would allow VAT to be charged to the LGWPF, however, ReAssure has agreed that it would only charge VAT to the LGWPF in the event that it was able to negotiate a reduction in the existing investment management fees and, including VAT, this would not result in an increase relative to the existing fees.
- 8.175 The investment management fees would be reviewed on 1 January 2023 or before, where there has been a market wide reduction in investment management fees. Safeguards exist within the agreement to ensure that both LGIM and ReAssure are able to come to an agreement regarding any fee reductions at the point of such a review.
- 8.176 I am satisfied that, if the Scheme were to be implemented, for the period that the IMA remains in place:

- There is no reason to expect that investment performance under the IMA would be any worse than if the Scheme were not implemented;
- The service levels would remain the same as would be experienced by the transferring policyholders if the Scheme were not implemented;
- The investment management fee would remain the same as if the Scheme were not implemented; and
- Sufficient safeguards exist that would mean that the investment performance and management fees would remain competitive.

## THE ANNUITY INTRODUCER AGREEMENT

- 8.177 As described in Section 7, an annuity introducer arrangement (the AIA) has been agreed such that, after the transfer to ReAssure the transferring LGAS policyholders would, upon reaching retirement, be directed to LGAS should they wish to purchase an annuity. This agreement would be in place for a minimum of five years.
- 8.178 Under the AIA, the transferring LGAS policyholders would be provided with equivalent options at retirement as are currently available within LGAS. If the Scheme were to be implemented, with the AIA in place:
- For policies under which the benefits are defined in terms of a guaranteed annuity, the annuity would be purchased by the LGWPF from LGAS at the equivalent rate as would have been paid by the LGAS WPF prior to implementation of the Scheme.
  - For policies under which the benefits are not defined in terms of a guaranteed annuity, the policyholders would be directed towards LGAS in the first instance and where this is not the best in market rate, would be referred to LGAS's market panel of annuity providers. The panel process guarantees market leading rates and so is a benefit to policyholders:
    - Unhealthy lives would have the opportunity to provide lifestyle and medical information and benefit from an enhanced annuity income; and
    - Healthier lives will receive a standard annuity but on market leading rates that would be potentially better than the LGAS rates and would not be disadvantaged.
- 8.179 The approach means policyholders have access to market leading rates and as a result I am satisfied that there would be no detriment to the policies transferring to the LGWPF.
- 8.180 If the AIA were to terminate then the transferring policyholders would continue to have access to the annuity market through the ReAssure portal and would continue to have access to LGAS annuity rates on the open market. The fees charged and terms available to the policyholders would be unaffected by the existence or otherwise of the AIA and I am satisfied that the termination of the AIA after five years would not have a material adverse effect on the transferring policies.

## THE CUSTOMER RETIREMENT JOURNEY

- 8.181 An exercise has been undertaken to consider the effect of the Scheme on the process that transferring with-profits policyholders would experience when retiring and taking out an annuity (the "retirement journey"). Overall the companies have attempted to ensure that the interaction for the transferring with-profits policyholders between LGAS and ReAssure is as smooth as possible. The necessary IT development for the retirement journey in ReAssure is being continually monitored as part of the business readiness programme.
- 8.182 There are a number of known differences as described below:
- For transferring personal retirement plans, the impact of guarantees on policyholders' benefits would be produced using a different basis (i.e. the ReAssure basis). Although this basis is unlikely to be the same as that used currently by LGAS, I am satisfied that the ReAssure basis would provide a fair representation of the impact of policyholders' guarantees and that this difference would not have a systematic or material adverse effect on the transferring personal retirement plan policies.
  - Following the implementation of the Scheme, the transferring with-profits policyholders would be able to take out an annuity by talking to LGAS staff on the telephone (a telephone journey) rather than through written correspondence (a paper journey). For some of the policyholders, this would replicate what they currently experience in LGAS but for others this would replace the paper journey that is currently followed. The

policyholders' calls would be dealt with by telephone agents specially trained and experienced in dealing with annuity products and I am satisfied that this difference would not have a material adverse effect on the transferring with-profits policyholders.

- If a transferring with-profits policyholder required a quote for both a drawdown product and an annuity then ReAssure would issue a drawdown quote and LGAS would issue an annuity quote. The policyholder would therefore receive two separately branded documents and enter into two separate but potentially concurrent processes.

This would represent a slight inconvenience for the transferring with-profits policyholders relative to dealing solely with LGAS; however, it is similar to the current process for existing ReAssure policyholders whereby drawdown and annuity quotes are provided by ReAssure and LV= respectively, and I am satisfied that it would not have a material adverse effect on the transferring with-profits policyholders.

- As described in paragraphs above, the transferring with-profits policyholders would benefit from access to LGAS's market panel of annuity providers and an enhanced level of underwriting within LGAS following the implementation of the Scheme.

8.183 I am satisfied that changes to the customer retirement journey as a result of the implementation of the Scheme would not have a material adverse effect on the transferring with-profits policyholders.

#### **CONCLUSION IN RESPECT OF THE TRANSFERRING LGAS POLICIES**

8.184 I am satisfied that the implementation of the Scheme would not have a material adverse effect on:

- The security of the benefits of the transferring policies of LGAS;
- The reasonable expectations of the transferring policyholders of LGAS in respect of their benefits; or
- The standards of administration, service, management and governance that apply to the transferring LGAS policies.

8.185 As noted above there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.

8.186 I will provide an update on these in my Supplementary Report.

## 9. The effect of the Scheme on particular transferring LGAS products

### INTRODUCTION

9.1 The transferring LGAS business includes a wide variety of product types that, if the Scheme were to be implemented, would be either changed or affected in a non-standard way. In this section I consider these products and the issues raised as follows:

- General changes to LGAS products as a result of the proposed Scheme;
- Changes to the communications issued to policyholders as a result of the proposed Scheme;
- Changes to the operation of unit-linked funds as a result of the proposed Scheme;
- The effect of the Scheme on the L&G Group SIPPs;
- The effect of the Scheme on the LGAS Stakeholder Pensions;
- The effect of the Scheme on the LGAS FMISAs; and
- The effect of the Scheme on linked unemployment cover.

### CHANGES TO LGAS PRODUCTS IN RESPECT OF THE TRANSFERRING LGAS POLICIES

#### Introduction

9.2 As set out in Section 7 of this report, ReAssure has proposed a number of changes to transferring with-profits, unit-linked and conventional non-profit products. These changes are as a result of where:

- Certain product features, and the way the business is operated cannot be easily supported by ReAssure's existing systems and operations; and/or
- The changes would enable the harmonisation of operational practices in respect of the transferring business with those in respect of ReAssure's existing business and therefore increase operational efficiency and reduce operational risks.

9.3 Where the changes involve a change to the policy terms and conditions it is the case that the changes are permitted as long as the required notice is given and the required notice will be given as part of the communications issued to policyholders regarding the Scheme. Furthermore, none of the changes are expected to have a material adverse effect on the transferring policyholders.

9.4 I cover the various product changes below divided into general changes and those changes specific to unit-linked products.

#### General changes to the LGAS products as a result of the proposed transfer

9.5 Of particular importance in the context of my considerations in respect to the possible effects of the changes on the transferring policies are those changes where ReAssure proposes to:

- **Make a number of changes to the method by which bonuses are calculated and the application of bonuses to with-profits products.**

I have reviewed these changes and I am satisfied that they would not be expected to have a material adverse effect on the transferring with-profits policyholders' benefits. In more extreme scenarios, there could be an effect on individual policies; however, I am satisfied that any impact would be non-systematic and that there would not be a material adverse effect for any particular group of policies.

- **Align the way in which premiums are collected and benefits are paid with its current operations, including moving regular premium payments on 29th, 30th and 31st of each month to alternative payment dates.**

I have reviewed these changes and though these may lead to a reduction in the flexibility afforded to the transferring policyholders I am satisfied that any such reduction would be marginal and that the changes would not have a material adverse effect on the transferring policies.

- **Align the approach to deferring policyholders' retirement benefits with its existing operations, including deferring benefits to the maximum age confirmed in the policy terms and conditions on initial deferral, not automatically continuing premium payments post-deferral but rather requiring policyholders to request they continue, and not accepting premium payments beyond the age of 75.**

I have reviewed these changes and I am satisfied that they would not be expected to have a material adverse effect on the transferring policies. In particular, I am reassured by the fact that: tax benefits are lost on contributions paid beyond age 75, very low volumes of transferring policyholders currently continue to pay premiums beyond age 75, and ReAssure is committed to clearly communicating and explaining this change to the affected transferring policyholders.

- **Adopt the ReAssure approach of not allowing policyholders with a GMP to retire at a claim date where the policy funds cannot provide at least the discounted GMP from the claim date.**

This is different to the current LGAS approach of allowing policyholders to retire at the claim date where a reduced annuity can be paid until the GMP age.

There is no management information to suggest that LGAS's facility of providing a reduced annuity from the claim date has been recently used by policyholders; however, to the extent there are live cases of such reduced annuities at the Legal Effective Date, ReAssure is committed to honouring these. Under the proposed ReAssure approach, policyholders will receive the equivalent value of benefits, just at a later date and in a different form. Therefore, I am satisfied that there would not be a material adverse effect on the transferring policyholders' benefits.

- **Waive policy charges for setting up drawdown for certain products.**

This would be a benefit to the transferring policyholders.

- **Increase the rate at which policyholders are given the option to increase their premiums and benefits, by way of indexation, for certain products.**

I am satisfied that there would not be a material adverse effect on policyholders as a result of this change, as the offer of more frequent indexation presents the opportunity for policyholders to experience more gradual premium increases, with less risk of big hikes, and receive more benefits sooner.

- **Make a number of changes to the derivation of charges for risk benefits.**

I have reviewed these changes and I am satisfied that they would be expected to give a broadly equivalent result and reflect the actual experience of the business over time, and therefore would not have a material adverse effect on the transferring policyholders' benefits.

- **Adopt the ReAssure approach of using the date of notification of death as the valuation date for death claims instead of the date of receipt of satisfactory evidence of death, which is currently used by LGAS.**

I am satisfied that this change would not have a material adverse effect on the transferring policyholders' benefits.

- **Make a number of changes to the way performance reviews of certain products are carried out.**

These performance reviews may give rise to changes to policy premiums or guaranteed benefits. I have reviewed these changes and I am satisfied that they would not have a material adverse effect on the transferring policyholders' benefits. Furthermore, LGAS has advised me that if the Scheme were not to be implemented it could make similar changes to its review mechanism at any time and has done so in the past.

- **Continue to accept new business in respect of increases to existing pension policies and new members joining existing pension schemes.**

It should be noted that certain LGAS products that currently allow policy increases would become closed to new business within ReAssure and instead policyholders would be able to top up or transfer in via alternative products. I have reviewed this change and I am satisfied that the alternative products offered by ReAssure are sufficiently similar such that there would be no material adverse effect on the transferring policyholders.

## Changes to communications issued to policyholders

9.6 ReAssure intends to make a number of changes to communications issued to policyholders, including:



- Disclosing only gross annuity amounts in annual statements sent to transferring annuitants, whereas currently LGAS also provides an estimate of tax and net amounts;
- Including bonus information in annual statements sent to members of occupational pension schemes, whereas currently separate bonus notices are issued for most schemes;
- Decoupling bi-annual statements for Flexible Mortgage Plan (“FMP”) and FMISA policies, whereas currently customers receive combined statements for FMP and FMISA policies within their plan;
- Issuing annual statements for pension policies on policyholders’ birthday or 180 days before, whereas currently LGAS issues certain statements on the policy anniversary;
- Providing tailored, up-to-date policy details letters on request, but not offering interim statements as currently available from LGAS;
- For UWP policyholders with a guaranteed minimum surrender value benefit at their 10 year anniversary, ReAssure proposes to issue a one-off mailing after the Legal Effective Date (which could be two to three years before the 10 year anniversary) to remind policyholders of their guarantee. This would replace the current LGAS approach of mailing policyholders both six months and one month before their 10 year anniversary. However, ReAssure has confirmed that it would continue to monitor guarantees at bonus declarations and when MVRs are applied or changed and issue a further reminder to policyholders should the guarantees be at risk of becoming in the money.

9.7 I have reviewed the proposed changes to communications issued to policyholders and I am satisfied that they would not have a material adverse effect on the transferring policyholders.

#### **Changes to the operation of unit-linked funds**

9.8 ReAssure intends to make a number of changes to the operation of the unit-linked funds used by the transferring policies currently in LGAS. The significant changes are to:

- Calculate and deduct annual management charges on a daily basis (within LGAS charges are calculated on a daily basis but deducted monthly);
- Align the allocation date of policyholder premiums with the later of the date of receipt or the due date (within LGAS premiums are allocated on the date of receipt); and
- Align the cut off times and valuation points used to generate prices for policy processing with ReAssure’s existing approach, under which:
  - The normal asset valuation point is close of business on the day prior to pricing;
  - The normal policyholder transaction cut off time is 5pm on the day of pricing;
  - Prices are loaded at 5pm the day of pricing; and
  - The pricing used for switches is tomorrow’s price based on a valuation point of close of business today. The exception to this is transferring funds currently administered by State Street and PMC, for which ReAssure has agreed to more closely align switch timings with the current LGAS approach by adding one day to processing times.

9.9 Furthermore, ReAssure intends to align the approach to fund switch charges with ReAssure’s existing model whereby each policy would be entitled to 20 switches free of charge each year and a £10 charge would be applied for each switch thereafter.

9.10 LGAS currently applies no switch charges for approx. 275k transferring policies, so this move to the ReAssure model (20 free switches and £10 per subsequent switch) is a potential source of detriment for transferring unit-linked policies. However, it has been confirmed to me that:

- There were only two instances of more than 20 switches on a policy in the last twelve months;
- Where the terms and conditions of the policy allow unlimited free switches, this would be continued in ReAssure; and
- For all other transferring policies, ReAssure’s switch charges would be lower than those currently applied.

- 9.11 Although these changes could alter the price at which units are bought or sold, I am satisfied that any price differences would not be systematic or have a material adverse effect on the transferring policyholders' benefits.

## Conclusion

- 9.12 In reviewing the proposed product changes I have given consideration to whether or not they require changes to policy terms and conditions and to whether, and how, the various changes will be communicated to transferring policyholders. I have also considered the view of the LGAS WPA and Chief Actuary, who have commented on the proposed product changes in their respective reports and are satisfied that these would not have a material adverse effect on the transferring policies.
- 9.13 I am satisfied that the proposed product changes (as described above) will not have a material adverse effect on the policyholders' policies.

## THE EFFECT OF THE SCHEME ON THE TRANSFERRING LGAS SIPPS

- 9.14 As described in Section 7, under the proposed ReAssure Group target operating model for transferring SIPP business:
- The administration systems used to administer the SIPPs would change;
  - The initial contact for the administration of the SIPP would move to RUKSL;
  - For certain purposes the initial contact would move to JLT; however, a dedicated line will be set up at JLT for the ReAssure Group SIPP customers; and
  - The legal title of the assets would be transferred from PMS Nominees to G Trustees but the beneficial ownership would remain with the SIPP holder.
- 9.15 The investment options available to SIPP policyholders would be unchanged as a result of the Scheme.
- 9.16 As set out in Section 5, it is proposed to change the SIPP product terms and conditions to allow a platform charge to be applied for approximately 450 SIPP policies with uninsured collective investments following their transfer to the ReAssure Group. Though specified in the Aegon Cofunds platform terms and conditions, the charge is not currently disclosed in the SIPP product terms and conditions. The charge has been deducted where it can be taken from other products held by the same policyholder on the platform; however, in some cases it has not been possible to take the charge since the inception of the SIPP policies.
- 9.17 Out of a total of approximately 490 SIPP policies with collective investments on the platform, only the 450 policies described above have some sight of the accrued charge on the platform (the affected SIPP policies). The platform terms and conditions do not apply, nor has the charge been disclosed, to the remaining 40 and LGAS and ReAssure have agreed not to apply this charge to these 40 policies.
- 9.18 The charge has not been reflected in benefit illustrations sent to the affected policyholders.
- 9.19 This charge varies by customer but is subject to a maximum of 29 basis points (as set out in the Aegon charging documentation). The application of this charge might be considered to have a material adverse impact on the affected SIPP policies, however it should be noted that:
- The platform charge is a valid charge for the services provided by Aegon and should have been incurred by affected policyholders in the past. However, Aegon is prepared to waive the accrued charge.
  - The alternative to not applying the charge would be for Aegon to terminate the current platform services, which would have an adverse impact on the transferring SIPP policies in terms of the loss of the benefits and flexibility currently afforded to policyholders by the platform.
  - LGAS and ReAssure consider Aegon's offer to be a fair outcome for policyholders.
  - This change will be clearly communicated to the affected SIPP policyholders as part of the communications regarding the Scheme (as described in Section 13 of this report).
- 9.20 Furthermore, the application of the charge is not part of the Scheme and LGAS has confirmed that, if the Scheme were not to be implemented, the charge would be applied to the affected SIPP policies within the L&G Group.
- 9.21 I am satisfied that the application of the platform charge would not have a material adverse impact on the affected SIPP policies and is, in any case, not part of the Scheme.

- 9.22 Other than a reduction to some other charges, the charges levied on SIPP policyholders would be unchanged as a result of the Scheme.
- 9.23 I have seen the target operating model of the SIPP business under the ReAssure Group and I am satisfied that the implementation of the Scheme would not have a material adverse effect on the transferring SIPP policies.

#### **THE EFFECT OF THE SCHEME ON THE TRANSFERRING LGAS STAKEHOLDER PENSIONS**

- 9.24 As described in Section 7 of this report, if the Scheme were to be implemented it is intended that the individual stakeholder pension policies in LGAS would transfer to ReAssure and become part of a ReAssure Stakeholder Pension Scheme.
- 9.25 LGAS will seek a Court Order that deems that the ReAssure Stakeholder Pension Scheme has held the existing PTRAS declarations of the transferring policyholders with effect from the same date(s) as the Legal & General Stakeholder Pension Scheme had first held the transferring policies.
- 9.26 Given the HMRC non-objection that was received in a letter dated 19 June 2019, it is likely the Court will grant the Court Order at the Sanctions Hearing and therefore, if the Scheme were to be implemented, the transferring stakeholder pension policyholders' policies and existing PTRAS declarations would be transferred to the scheme administrator of the ReAssure Stakeholder Pension Scheme.
- 9.27 I am therefore satisfied that the Scheme would not have a material adverse effect on the transferring stakeholder pension policies.

#### **THE EFFECT OF THE SCHEME ON THE TRANSFERRING LGAS FMISAS**

- 9.28 If the Scheme were to be implemented, the insurance element of the LGAS FMISA business, which is currently handled by LGAS, would be transferred to ReAssure and the ISA (investment) element would be retained by the L&G Group investment entity UTM.
- 9.29 ReAssure would replace LGAS as the principle point of contact for policyholders; however, certain queries specific to the ISA investment would be redirected to UTM as is currently the case. Hence, the customer journey would be the same as prior to the transfer other than the change from LGAS to ReAssure.
- 9.30 ReAssure would receive policyholder premiums, deduct policy fees and risk charges, pass the balance on to UTM, and process policyholder claims. To facilitate this arrangement, and the necessary information sharing and segregation of policyholder funds between the two entities, LGAS and ReAssure will need to develop their respective systems prior to the Legal Effective Date. This includes development of an ISA Fund Account within ReAssure to monitor the aggregate balance of ISA funds.
- 9.31 I have reviewed the migration programme for this aspect of the migration due to the Scheme and I am satisfied this arrangement would not lead to any delay or reduction in service standards for the affected transferring policyholders.
- 9.32 The required systems development, and testing of this against minimum acceptance criteria, will form part of a wider plan described in Section 8 to ascertain the overall preparedness of LGAS and ReAssure in advance of the proposed transfer. LGAS and ReAssure have committed to providing me with regular updates on progress relative to plan, and I will provide an updated view on this issue in my Supplementary Report.
- 9.33 The legal advisors to ReAssure have given the opinion that the Scheme proposals in respect of the FMISA contracts would not give rise to potential client money issues under the CASS rules. As stated in Section 4, I am satisfied that it is reasonable to rely on the opinion of ReAssure's legal advisors.
- 9.34 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the transferring FMISA policies.

#### **THE EFFECT OF THE SCHEME ON THE TRANSFERRING LGAS LINKED UNEMPLOYMENT COVER**

- 9.35 LGAS administers unemployment cover policies that are linked to approximately 2,000 transferring MPI policies.
- 9.36 If the Scheme were to be implemented:
- The unemployment cover policies would remain with LGAS and policyholders of the transferring MPI policies to which they are linked would need to continue to contact LGAS separately regarding any queries or changes relating to their unemployment cover; and

- ReAssure would manually maintain the link between the unemployment cover policies and the transferring MPI policies so that unemployment cover would be terminated if the transferring MPI policy to which it is linked was terminated.

9.37 I have reviewed this change, which has been agreed by LGAS and ReAssure and will be clearly communicated to the affected transferring policyholders in advance of the Legal Effective Date, and I am satisfied that it would not have a material adverse effect on the transferring MPI policyholders.

#### **CONCLUSION IN RESPECT OF PARTICULAR TRANSFERRING LGAS PRODUCTS**

9.38 I am satisfied that the implementation of the Scheme would not have a material adverse effect on:

- The security of the benefits of the transferring policies of LGAS;
- The reasonable expectations of the transferring policyholders of LGAS in respect of their benefits; or
- The standards of administration, service, management and governance that apply to the transferring LGAS policies.

9.39 As noted in Section 8 there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.

9.40 I will provide an update on these in my Supplementary Report.

## 10. The effect of the Scheme on the existing ReAssure policies

### INTRODUCTION

- 10.1 If the Scheme were to be approved by the High Court and implemented, the transferring business would be transferred from LGAS into ReAssure, with the transferring non-profit business transferring into the RNPF and the LGAS WPF business transferring into a newly created ring-fenced fund called the LGWPF.
- 10.2 In this section of my report I consider the effect of the implementation of the Scheme on the existing ReAssure policies, which can be divided into the following groups:
- The policies in the RNPF;
  - The policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF; and
  - The policies in Ark Life.
- 10.3 As at 31 December 2018, the transferring business consisted of approximately 1.0 million policies and £28 billion of assets under management, and ReAssure had approximately 2.2 million policies and £39 billion of assets under management.
- 10.4 At over 70% (by assets under management as at 31 December 2018) of the existing business of ReAssure, the transferring business can be considered significant relative to the existing ReAssure business.
- 10.5 In my consideration of the Scheme, the key points in respect of the existing ReAssure policies are the likely effects of the transfer of the transferring business into ReAssure on the following:
- **The security of the benefits of the existing ReAssure policies**

This is derived from the financial strength available to provide security for the benefits of the ReAssure policies after the implementation of the Scheme and the strength of the appropriate risk appetite statements and applicable capital policy and external support received from the parent company by virtue of being part of a group.

This is covered in paragraphs 10.7 to 10.48.
  - **The profile of risks to which the existing ReAssure policies are exposed**

If the Scheme were to be implemented, the transferring LGAS policies would become policies of ReAssure and this introduction of policies written by a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles, could potentially change the profile of risks to which the existing ReAssure policies are exposed.

This is covered in paragraphs 10.49 to 10.65.
  - **The reasonable expectations of the existing ReAssure policyholders in respect of their benefits**

This is covered in paragraphs 10.66 to 10.73.
  - **The standards of administration, service, management and governance applied to the existing ReAssure policies**

This covers the management, oversight and administration of the existing ReAssure policies.

This is covered in paragraphs 10.74 to 10.93.
- 10.6 These are considered in turn below for each of the groups of policies identified above in paragraph 10.2.

### THE EFFECT OF THE SCHEME ON THE SECURITY OF THE BENEFITS OF THE EXISTING REASSURE POLICIES

#### Introduction

- 10.7 The financial strength that provides security for the benefits of the existing ReAssure policies is currently provided by:

- The assets covering the technical provisions and SCR held by ReAssure as required under the Solvency II regulations;
- The additional financial strength required by the ReAssure RA Statement including the strength of the governance around the ReAssure RA Statement; and
- Any additional support from outside ReAssure including the Swiss Re Group and MS&AD.

10.8 If the Scheme were to be implemented, the existing ReAssure policies would continue to be policies of ReAssure and:

- There would be no change to the Solvency II regime as a result of the Scheme and the technical provisions and SCR for the existing ReAssure policies would remain calculated in accordance with the Solvency II regime;
- ReAssure's PRA approval to use a PIM to cover the risks of the existing RNPF LT business would not change as a result of the Scheme;
- There would be no change to the ReAssure RA Statement as a result of the implementation of the Scheme; and
- There would be no change to the additional support provided from outside of ReAssure by the Swiss Re Group and MS&AD (though this may be affected by the ReAssure IPO as discussed in Section 12 of this report).

10.9 The security of benefits are considered in turn below for each of the groups of existing ReAssure policies identified above in paragraph 10.2:

- The policies in the RNPF;
- The policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF; and
- The policies in Ark Life.

#### **The existing policies of the RNPF**

10.10 If the Scheme were to be implemented, a new ring-fenced fund (the LGWPF) would be introduced to ReAssure.

10.11 The potential risks in respect of the security of the benefits of the RNPF business due to the implementation of the Scheme arise from:

- The change in the financial strength of the RNPF;
- The risk that, at some point in the future, capital support would be required for the new fund which would potentially weaken the financial position of the RNPF and in turn reduce the security of the benefits of the existing RNPF business; and
- Under the Scheme provisions, as described in Section 7 of this report, non-profit policies in the LGWPF may be allocated to the RNPF or the business of the LGWPF may be merged with the business of the RNPF in certain future circumstances.

10.12 Consideration of these potential effects of the Scheme on the policies in the RNPF is set out below.

#### *The financial strength of the RNPF*

10.13 The tables in Appendices A and B show that the RNPF is expected to be financially strong before and after the implementation of the Scheme with the SCR coverage changing from 145% to 134% and the excess capital changing from £1.1 billion to £0.8 billion as at 31 December 2018.

10.14 The reduction in the SCR coverage from 145% in LGAS to 134% in the RNPF could, in isolation, be taken to imply a negative impact on the security of the benefits of the transferring LGAS policies. However, the SCR coverage ratios are indicators of, or proxies for, financial strength and a decrease in the coverage ratio does not necessarily indicate a significant or material reduction in security.

10.15 If the Scheme were to be implemented, the expected financial strength of the RNPF of 134% indicates a position of considerable strength as it is materially above both the required regulatory level of 100% and the level required to satisfy the ReAssure RA Statement. As stated in Section 3 of this report the SCR is itself calculated such that

there is a 99.5% likelihood of the company remaining solvent and able to meet its liabilities as they fall due over a one year time horizon.

- 10.16 In addition, I have been provided with financial projections showing the expected path for the ReAssure Group SCR coverage (calculated using the ReAssure PIM) if the Scheme were to be implemented. These projections show that the SCR coverage ratio for the ReAssure Group is expected to remain strong (relative to 100% of SCR) and higher than the level required under the ReAssure IPO RA Statement over the projection period.
- 10.17 The ReAssure IPO RA Statement sets out RGP's commitment to ensuring that risk appetite is adhered to at the level of the ReAssure entity and that the interests of the ReAssure entity are maintained. I am therefore satisfied that the projected financial strength of the ReAssure Group is indicative of that for ReAssure specifically.
- 10.18 Therefore, I am satisfied that the implementation of the Scheme would not have a material adverse effect on the financial strength of the RNPF, the likelihood of extra calls on the capital in ReAssure, or on the likelihood of the RNPF becoming insolvent on a claims-paying basis.

#### *The ReAssure RA Statement*

- 10.19 If the Scheme were to be implemented, the RNPF would remain subject to the ReAssure RA Statement and the ReAssure RA Statement would not change as a result of the Scheme.
- 10.20 The ReAssure RA Statement could be changed in the future but that would be subject to the governance procedures set out in the ReAssure RA Statement which would also not change as a result of the Scheme.

#### *The risks to ReAssure from the introduction of the LGWPF*

- 10.21 If the Scheme were to be implemented, a new ring-fenced fund called the LGWPF would be set up in ReAssure and the business currently in the LGAS WPF would be transferred into the LGWPF. The LGWPF would be managed in accordance with the current LGAS WPF RA Statement and the current LGAS PPFM and so would be managed with the objective of ensuring that its assets would be sufficient to meet its liabilities and regulatory capital requirements without the need for additional capital from outside the LGWPF.
- 10.22 Under the terms of the RTA, ReAssure is currently exposed to the risk of shareholder support being required to the LGAS WPF, as the profits transferred from LGAS to ReAssure under the RTA are net of any such support. Therefore, there would not be a material change when, if the Scheme were to be implemented, ReAssure would be exposed to the risk of support being required for the LGWPF.
- 10.23 The tables in Appendices A and B show that the LGWPF is projected to be strong at 152% after the implementation of the Scheme and therefore has a low likelihood of requiring support from ReAssure or from the Swiss Re Group.

#### *The future allocation of non-profit policies in the LGWPF to the RNPF*

- 10.24 As described in Section 7 of this report, the Scheme allows for ReAssure to allocate non-profit policies in the LGWPF to the RNPF or to merge the business of the LGWPF with the business of the RNPF in certain future circumstances. However, a number of safeguards are in place to ensure that there would not be a material adverse effect on the security of the benefits of the policies in the RNPF in the case of such a reallocation or fund merger.
- 10.25 In particular, in the case of a reallocation of non-profit policies in the LGWPF to the RNPF:
- Such a reallocation should not be inconsistent with the terms of the policies and applicable laws and regulations;
  - The approval of the ReAssure FC and the ReAssure Board, having considered this report and the report of the LGAS WPF in relation to this Scheme, would be required;
  - The level of assets being transferred into the RNPF should be commensurate with the transferring liability and associated level of risk;
  - The reallocation should not have a material adverse impact on the affected policyholders when considering the aggregate impact of any other reallocations in the preceding five years and any planned reallocations in the following five years; and
  - Where aggregate reallocations in any 12 month period involve a transfer of assets of more than £150 million (increasing annually with RPI inflation from the Economic Effective Date), the Scheme ensures that ReAssure



informs the regulators and obtains their non-objection within two months, and also obtains a certificate from an independent actuary to provide the view that there would be no material adverse impact on affected policyholders.

10.26 In the case of a merger of the LGWPF into the RNPF and converting the remaining with-profits policies into non-profit policies:

- Such a merger would only take place if the assets within the LGWPF fall below £400 million (increased annually on 31 December in line with the UK RPI), which is a small proportion (2%) of the current LGWPF assets of approximately £20 billion which I have been informed is not currently projected to occur before 2045 (assuming that no new business is written into the fund and no non-profit business is transferred out of the fund). If the non-profit business is transferred out of the fund, the limit is projected to be occur 3 years earlier in 2042;
- An appropriate allowance for the future shareholder transfers that would have otherwise been made from the LGWPF to the RNPF should be released to the RNPF;
- The approval of the ReAssure FC and the ReAssure Board, having considered this report and the report of the LGAS WPA in relation to this Scheme, would be required;
- Non-objection should be sought from the regulators; and
- There should be no material adverse impact on existing policyholders in the RNPF, in the opinion of the ReAssure Board and (where the value of the assets within the LGWPF is £80 million or more) an independent actuary.

10.27 I am satisfied that the above safeguards are appropriate and sufficient to protect the interests of the policyholders in the existing RNPF.

#### *Conclusion for the existing policies of the RNPF*

10.28 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the existing RNPF business.

#### **The policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF**

10.29 If the Scheme were to be implemented, there would be no business transferred into the WLWPF, the NMWPF or the GAWPF and there would be no change to the solvency position of these ring-fenced funds.

10.30 The potential changes in respect of the security of the benefits of the policies in these funds due to the implementation of the Scheme are therefore of a secondary nature and arise from:

- The possibility of an increase in the contagion risk to the existing ring-fenced funds of ReAssure due to the possibility that the new fund would require capital support from the RNPF or the existing ring-fenced funds; and
- Under the Scheme provisions, as described in Section 7 of this report, the business of the LGWPF may be merged with the business of the existing ring-fenced funds of ReAssure in certain future circumstances.

10.31 Consideration of these potential effects of the Scheme on the policies in the existing ring-fenced funds of ReAssure is set out below.

#### *The possibility of an increase in contagion risk from the introduction of the LGWPF to ReAssure*

10.32 If the Scheme were to be implemented, a new ring-fenced fund (the LGWPF) would be introduced to ReAssure. This would increase the risk of contagion to the RNPF as it may in the future be required to provide capital support for the new fund which would:

- Reduce the ability of the RNPF to provide support to the WLWPF and the GAWPF if such support were required;
- Reduce the ability of ReAssure to provide support to the NMWPF as required under the NM capital support facility described in Section 6; and/or

- Could lead to the RNPF becoming unable to meet its claims and the breakdown of the restrictions on the use of the assets in the existing ring-fenced funds.

- 10.33 As described above in paragraphs 10.13 to 10.18, the tables in Appendices A and B show that the RNPF is expected to be financially strong before and after the implementation of the Scheme and the projected financial strength of the RNPF after the implementation of the Scheme indicates a position of considerable financial strength.
- 10.34 In addition, as discussed above, the projected post implementation solvency of ReAssure on realistic best estimate assumptions and under a range of adverse scenarios shows that the SCR coverage ratio is expected to remain strong and higher than the level required under the ReAssure RA Statement over the projection period.
- 10.35 Therefore, I am satisfied that the implementation of the Scheme would not have a material adverse effect on the financial strength of the RNPF, the likelihood of extra calls on the capital in ReAssure, or on the likelihood of the RNPF becoming insolvent on a claims-paying basis.

#### *The financial strength of the RNPF*

- 10.36 Based on the financial information as at 31 December 2018 shown in Appendices A and B of this report:
- Prior to the implementation of the Scheme, the capital resources of the ReAssure RNPF covered its SCR with a ratio of 145% and with excess capital (above the SCR) of £1.1 billion; and
  - If the Scheme were to be implemented the capital resources of the ReAssure RNPF would have covered its SCR with a ratio of 134% and excess capital of £0.8 billion.
- 10.37 The projected decrease in the SCR coverage ratio as a result of the Scheme might, in isolation, be taken to imply a negative impact on the security of the benefits of the existing RNPF LT business. However, for the reasons given above in paragraphs 10.13 to 10.18, I am satisfied that, the implementation of the Scheme would not have a material adverse effect on the financial strength of the RNPF, the likelihood of extra calls on the capital in ReAssure, or on the likelihood of the RNPF becoming insolvent on a claims-paying basis.

#### *The ReAssure RA Statement*

- 10.38 If the Scheme were to be implemented, the WLWPF, the NMWPF, the GAWPF and the RNPF would remain subject to the ReAssure RA Statement and the ReAssure RA Statement will not change as a result of the Scheme.
- 10.39 The ReAssure RA Statement could be changed in the future but that would be subject to the governance procedures set out in the ReAssure RA Statement which are also not changing as a result of the Scheme.

#### *The potential future merger of the LGWPF into one of the WLWPF, the NMWPF or the GAWPF*

- 10.40 As described in Section 7 of this report, a number of safeguards have been put in place to ensure that, if the merger of the LGWPF into one of these funds were to proceed, the security of the benefits of the policies in the existing ring-fenced funds of ReAssure would not be materially adversely affected. In particular such a merger would require:
- The assets within the LGWPF to fall below £400 million (increased annually on 31 December in line with the UK RPI).  
  
This threshold is a small proportion (2%) of the current LGWPF assets and is not projected to occur before 2045 (assuming that no new business is written into the fund and no non-profit business is transferred out of the fund). In the scenario where the non-profit business were to be transferred out of the fund, the threshold is projected to be reached 3 years earlier in 2042.
  - To be consistent with applicable laws and regulations.
  - Consultation with the ReAssure FC.
  - The approval of the ReAssure Board.
  - Non-objection from the PRA and the FCA within two months.
  - That any with-profits policies remain with-profits policies in nature following the merger.

- That, in the opinion of the ReAssure Board and an independent actuary, there would be no material adverse effect on the policyholders in the existing ring-fenced funds of ReAssure.
- The maintenance of the provisions of the PPFM of the existing ring-fenced funds of ReAssure.

10.41 I am satisfied that these safeguards are appropriate and sufficient to protect the interests of the policyholders in the existing ring-fenced funds of ReAssure in the case of such a merger.

*The potential future merger of one of the WLWPF, the NMWPF or the GAWPF into the LGWPF*

10.42 The merger of one of the WLWPF, the NMWPF or the GAWPF into the LGWPF would be governed by the Schemes of transfer that established the WLWPF, the NMWPF and the GAWPF. This is no change to the current situation.

*Conclusion for the policies in the WLWPF, the NMWPF and the GAWPF*

10.43 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the policies within the WLWPF, the NMWPF or the GAWPF.

**The policies in Ark Life**

10.44 With the exception of Ark life, none of the subsidiaries of the RNPF contain any insurance business. Ark Life is closed to new business and its existing business is conventional non-profit and unit-linked business.

10.45 If the Scheme were to be implemented:

- Ark Life would remain a subsidiary of the RNPF.
- There would be no business transferred into or out of Ark Life; and
- There would be no change to Ark Life's solvency position or to the capital policy to which it is managed.

10.46 To the extent that the implementation of the Scheme could have an adverse impact on the financial strength of ReAssure, it could in turn have an adverse impact on the level of parental capital support available to Ark Life. However, as described above, I am satisfied that the implementation of the Scheme would not have a material adverse effect on the financial strength of ReAssure, nor on ReAssure's ability to provide capital support to Ark Life if and when this is required.

10.47 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the policyholders of Ark Life.

**Conclusion on the effect of the Scheme on the security of the benefits of the existing ReAssure policies**

10.48 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the existing ReAssure policies.

**THE EFFECT OF THE SCHEME ON THE PROFILE OF RISKS TO WHICH THE EXISTING REASSURE POLICIES ARE EXPOSED**

**The policies in the RNPF**

10.49 The existing RNPF business is primarily unit-linked life and pensions business, and non-profit annuity business. The risk exposures of the RNPF are currently principally credit risk, longevity risk, lapse risk and equity risk.

10.50 The transferring business is primarily UWP and unit-linked business, and therefore, if the Scheme were to be implemented, additional equity and lapse risk would be introduced to the RNPF.

10.51 The transfer of a significant volume of long-term business from LGAS into the RNPF would be expected to change the risk profile of the RNPF due to the different mix of the products of the transferring business relative to the existing RNPF business. In addition, the business transferred in may have arisen from different sources, through different sales channels, and the underlying policyholder group may have different demographic characteristics from the existing RNPF LT policyholders.

10.52 However, it should be noted that:

- The RTA has been in effect since the Economic Transfer Date and hence most of the risks associated with the transferring business are currently borne by ReAssure, and any diversification of risks and other interactions between the transferring business and the existing RNPF business are already reflected in the ReAssure Solvency II balance sheet;
- The additional equity and lapse risk introduced by the transferring business diversifies well against the RNPF's existing credit and longevity risk, and results in a less concentrated profile of risks for the RNPF than that currently;
- Following implementation of the Scheme, the RNPF is projected to meet its capital requirements under Solvency II (which reflect any additional expense and operational risks transferred to ReAssure with the transferring business on the Economic Effective Date) and to comfortably meet the capital requirements of the ReAssure RA Statement.

10.53 I am satisfied that, although the implementation of the Scheme would cause a change to the profile of risks to which the existing RNPF business is exposed, this would not have a material adverse effect on the security of the benefits of the existing RNPF business.

#### **The policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF**

10.54 As described above, if the Scheme were to be implemented, there would be no business transferred into the WLWPF, the NMWPF or the GAWPF and therefore no direct impact on the risk profile to which the policies in these funds would be exposed. The ReAssure RA Statement requires that the ReAssure with-profits funds are managed so that each should meet its own liabilities and regulatory capital requirements without the need for additional capital from outside.

10.55 However, the policies in the ReAssure with-profits funds would be indirectly exposed to the risks associated with the transferring business through any:

- Increase in contagion risk so that, for example, extra calls on the capital in ReAssure are such that the capital available to support the existing ring-fenced funds becomes restricted;
- Future merger of the LGWPF into the existing ring-fenced funds of ReAssure; and
- Future merger of the existing ring-fenced funds into the LGWPF.

10.56 As described above, I am satisfied that the change in risk exposures of the RNPF as a result of the implementation of the Scheme would not have a material adverse effect on the security provided by the RNPF.

10.57 Due to the RTA being in effect, most of the risks associated with the transferring business are currently borne by ReAssure and the policies in the existing ring-fenced funds of ReAssure are currently exposed to the increase in contagion risk described in the first bullet above. Furthermore, the probability of these risks crystallising is low as the RNPF and the LGWPF are projected to be financially strong after the implementation of the Scheme, with solvency coverage above that required by the ReAssure RA Statement.

10.58 As described above, there are a number of safeguards in place to protect the interests of the policyholders in the existing ring-fenced funds of ReAssure in the instance of a future merger of the LGWPF into one of the existing ring-fenced funds of ReAssure.

10.59 The future merger of the existing ring-fenced funds of ReAssure into the LGWPF would be subject to the schemes of transfer that established these ring-fenced funds. The Scheme that is the subject of this report will not change the provisions of these schemes of transfer.

10.60 I am satisfied that, although the implementation of the Scheme would cause a change to the profile of risks to which the policies of the WLWPF, the NMWPF and the GAWPF are exposed, this would not have a material adverse effect on the security of the benefits of the policies in the WLWPF, the NMWPF and the GAWPF.

#### **The policies in Ark Life**

10.61 If the Scheme were to be implemented, there would be no business transferred into or out of Ark Life and therefore no direct impact on the risk profile to which the Ark Life policies are exposed. However, Ark Life would be indirectly exposed to the risks associated with the transferring business through any resulting loss in the financial strength of, and the available capital support from, ReAssure.

- 10.62 As described above, I am satisfied that the change in risk exposures of ReAssure as a result of the implementation of the Scheme would not have a material adverse effect on the security provided to Ark Life by ReAssure.
- 10.63 Projections show that, if the Scheme were to be implemented the financial strength of Ark Life would be significantly above that of ReAssure both immediately after the implementation of the Scheme and in the future. It is therefore unlikely that, if the Scheme were to be implemented, Ark Life would require capital support from ReAssure and, given the projected strength of ReAssure (as discussed in Section 8) it would be extremely unlikely that ReAssure would not be able to provide capital support to Ark Life if required.
- 10.64 I am satisfied that, although the implementation the Scheme would indirectly expose the policyholders of Ark Life to the risks associated with the transferring business and thus change the profile of the risk exposure, this would not have a material adverse effect on the security of the benefits of the policyholders of Ark Life.

#### **Conclusion on the effect of the Scheme on the profile of risks to which the existing ReAssure policies are exposed**

- 10.65 I am satisfied that, although the implementation of the Scheme would cause a change to the profile of risks to which the existing ReAssure policies are exposed, this would not have a material adverse effect on the security of the benefits of the policies in Ark Life.

#### **THE EFFECT OF THE SCHEME ON THE REASONABLE EXPECTATIONS OF THE EXISTING REASSURE POLICIES IN RESPECT OF THEIR BENEFITS**

##### **The policies in the RNPF**

- 10.66 The existing RNPF business is unit-linked or non-profit in nature and, as such, policyholders' expectations in respect of their benefits are that:
- They receive their benefits as guaranteed under the policy, on the dates and in the contingencies specified in the terms and conditions; and
  - The benefits they receive reflect the investment performance of the assets in which their units are invested, net of contractual charges payable under the policies.
- 10.67 If the Scheme were to be implemented, there would be no change to:
- The terms and conditions of the existing RNPF policies;
  - The methodology used to calculate the surrender values of the existing RNPF policies;
  - The charges that apply to the existing RNPF policies; or
  - The exercise of discretion in respect of the management of the unit-linked funds.
- 10.68 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the existing RNPF policyholders in respect of their benefits.

##### **The policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF**

- 10.69 If the Scheme were to be implemented, there would be no change to:
- The terms and conditions of the policies in the existing ring-fenced funds of ReAssure;
  - The rights of the existing with-profits policyholders of ReAssure to any future distributions from the inherited estates;
  - The methodology used to calculate asset shares and surrender values of the existing with-profits policies of ReAssure;
  - The bonus and pay-out policies applied to the existing with-profits policies of ReAssure;
  - The charges that apply to the policies in the existing ring-fenced funds of ReAssure; or
  - The likelihood of capital support being required by the existing ring-fenced funds of ReAssure.

- 10.70 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the policyholders in the existing ring-fenced funds of ReAssure in respect of their benefits.

#### **The policies in Ark Life**

- 10.71 There would be no changes to the terms and conditions of the policies or Ark Life and the policy servicing arrangements, investment management, management and governance for these policies will not change as a result of the implementation of the Scheme.
- 10.72 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the Ark Life policyholders in respect of their benefits.

#### **Conclusion**

- 10.73 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the existing ReAssure policyholders in respect of their benefits.

### **THE EFFECT OF THE SCHEME ON THE STANDARDS OF ADMINISTRATION, SERVICING, MANAGEMENT AND GOVERNANCE APPLIED TO THE EXISTING REASSURE POLICIES**

#### **The administration and servicing applied to the existing ReAssure policies**

- 10.74 The existing RNPF policies are unit-linked or non-profit in nature and, as such, policyholders' expectations in respect of the standards of administration, servicing, management, and governance that apply to their policies are that they are in line with the contractual terms under the policies, and are not materially worse than those they currently receive.
- 10.75 The existing ReAssure with-profits policyholders' expectations in respect of the standards of administration, servicing, management, and governance that apply to their policies are that they are treated fairly and in accordance with the relevant PPFM, and that they are in line with the contractual terms under the policies, and are not materially worse than those they currently receive.
- 10.76 Online 'ReAssure Now' and 'ReAct' portals will be developed, tested and put in place within ReAssure for use by existing ReAssure policyholders and sponsoring employers of occupational pension schemes respectively. This reflects an enhancement to the current ReAssure service. Testing of these portals will be conducted as part of the wider LGAS and ReAssure plan to ascertain business readiness for the transfer (see below). These will be rolled out following the Sanctions Hearing.
- 10.77 Other than this, if the Scheme were to be implemented, there would be no change to:
- The administration and servicing of the existing RNPF policies and the policies in the WLWPF, the NMWPF and the GAWPF (the majority of which is carried out by RUKSL). These would be carried out by the same teams and according to the same service standards and procedures as currently, none of which would change as a result of the implementation of the Scheme.
  - The asset management arrangements for the existing RNPF policies and the policies in the WLWPF, the NMWPF and the GAWPF and the governance around these including the performance standards to which these arrangements are held.
- 10.78 The migration of the transferring business to ReAssure will include any necessary systems functionality and business process developments to accommodate the transferring business and products. Such changes will be subject to testing and satisfaction of minimum acceptance criteria to ensure there are no consequential adverse impacts on the existing ReAssure business and products. Furthermore, ReAssure will need to ensure that it is operationally ready to take on the volumes of work being transferred such that there is no deterioration in the ongoing administration and servicing of the existing ReAssure policies.
- 10.79 As described in Section 8, to support the migration of the data from LGAS to ReAssure and, more widely, to ensure operational readiness of both parties for the transfer and the protection of customer outcomes, a plan has been put in place that covers four key mechanisms:
- Programme structure and tracking;
  - Readiness gate assessments;



- Monitoring ongoing stability; and
  - Contingency options.
- 10.80 ReAssure has identified the additional permanent resources it needs, and has commenced recruitment activity, to ensure that it will have adequate skilled staff to support all of its business (including its existing business) following the implementation of the Scheme. ReAssure has identified a requirement for c458 additional employees to administer this business and to date 359 new employees have been recruited and accredited as competent in role. The recruitment plan for 2019 requires a further 52 new employees and delivery is on track with all 52 already in the business and undergoing training. The remaining new employees will be transferring across from LGAS. A satellite office is being sourced in the Brighton and Hove area to accommodate the transferring actuarial community. Under the recruitment plan all new starters being subject to ReAssure's onboarding procedures and IT systems training.
- 10.81 Ongoing monitoring and reporting of this recruitment process is being conducted as part of the plan set out above. The recruitment plan is set to be completed by August 2019.
- 10.82 LGAS and ReAssure have committed to providing me with regular updates on business readiness and in particular with the reports, risk review results and other management information sent to the appropriate governance committees in advance of each of the four readiness gates.
- 10.83 I have received a private report dated 17 June 2019 from the ReAssure CRO addressed to the ReAssure Board. This report indicated that, in the CRO's opinion, the migration project was behind schedule. The CRO and the CEO of ReAssure have subsequently provided assurance that the issues outlined in this report are being addressed and that they are confident that the migration can be successfully delivered in time for the Legal Effective Date although it is expected that some additional manual processes will be in place for a period after the Legal Effective Date while building and testing of systems is completed.
- 10.84 It is the responsibility of the ReAssure Board and the LGAS Board to ensure that this migration is implemented successfully and without any detrimental effect on service standards or the accuracy of benefit calculations for either transferring policyholders or existing ReAssure policyholders and I will rely on the ReAssure Board and the LGAS Board in this respect. In particular I will rely on the Boards of the firms to ensure that the migration project is given the appropriate priority, that the required planning is carried out, and that the required resources are secured, such that the status of the migration project is quickly improved and the CRO is able to report that the risks have been reduced to an acceptable level.
- 10.85 To facilitate this monitoring by the Boards and to enable me to keep track of progress on the migration project, I have requested that the ReAssure CRO provides a detailed monthly report (in a similar format to the CRO Report dated 17 June 2019) on the status of the migration project. These reports will be produced as at 30 June 2019, 31 July 2019, 31 August 2019, 30 September 2019, 31 October 2019 and beyond if the Legal Effective Date is moved beyond the current expected date of 4 November 2019.
- 10.86 I will report on the outcome of these updates in my Supplementary Report for the Sanctions Hearing.

### **The management and governance applied to the existing ReAssure policies**

#### *The with-profits policies in the ring-fenced funds of ReAssure: the WLWPF, NMWPF and the GAWPF*

- 10.87 The principles and practices used in the management of the existing ring-fenced funds of ReAssure would not change as a result of the implementation of the Scheme (though the background text of the PPFM documents may be amended). However, the provisions of the Scheme allow for the PPFMs to be amended at a future point in the instance of a merger of one of the existing ring-fenced funds of ReAssure with the LGWPF. I am satisfied that sufficient safeguards and governance arrangements are in place to ensure that any consequential changes to the PPFMs of the existing ring-fenced funds and to the provisions of the Scheme would not have a material adverse effect on the reasonable expectations of the existing with-profits policyholders of ReAssure in respect of their benefits.
- 10.88 The governance of the with-profits policies in the WLWPF, the NMWPF and the GAWPF is currently the responsibility of:
- The ReAssure Board;
  - The ReAssure BRC;



- The ReAssure GMRC;
- The ReAssure WPA;
- The ReAssure FC;
- The ReAssure WPMC;
- The ReAssure BIC;
- The ReAssure PIC;
- The ReAssure UPC;
- The TCF Management Committee, including the ReAssure PMC sub-committee; and
- The ReAssure IGC.

10.89 If the Scheme were to be implemented, there would be no change to the above other than that:

- A WPA would be appointed to provide oversight for the LGWPF, which may either involve an extension of the existing ReAssure WPA role or the appointment of a second, dedicated WPA in respect of the LGWPF. In either case the appointment would need approval by the PRA (after consultation with the FCA) and would therefore need to meet the fit and proper criteria of the current SM&CR in respect of its statutory role for each with-profits fund and Chapter 4 of the Supervision Manual of the FCA Handbook.
- The remit of the ReAssure FC would be extended to provide independent oversight of the LGWPF, while continuing to do so for the existing with-profits funds of ReAssure.

10.90 There is a risk that the ReAssure FC would not have sufficient capacity to govern the existing ReAssure with-profits funds and unit-linked business to the same standard as currently, given the scale and complexity of the incoming LGWPF and transferring LGAS unit-linked business. However:

- It is expected that at least one other member of the LGAS WPC will transfer across to the ReAssure FC following the implementation of the Scheme;
- ReAssure will arrange training to ensure that all ReAssure FC members are familiar with the LGWPF business and processes prior to the implementation of the Scheme;
- For the first 12 months following the Legal Effective Date, the ReAssure FC meetings would be extended to four hours from the current two hour duration to allow the committee sufficient time to oversee both the existing ReAssure business and the newly transferred LGAS business, and to embed business as usual operations; and
- After the first 12 months, the meetings would potentially reduce to three hours depending on the Chairman's view.

#### *Other policies in ReAssure*

10.91 Updates have been made to the terms of reference of the various ReAssure committees to ensure that the governance of unit-linked funds is at least as strong as that in LGAS prior to the implementation of the Scheme. These updates have no adverse effect on the existing policies of ReAssure.

10.92 There would be no other changes to the governance and management of the other ReAssure policies. This would remain the responsibility of the ReAssure Board, the corresponding Board and Executive Committees, and the ReAssure senior management team. None of these would change as a result of the implementation of the Scheme other than as described above.

#### *Conclusion*

10.93 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the standards of management and governance that apply to the existing ReAssure policies.

### **CONCLUSION FOR THE EXISTING REASSURE POLICIES**

10.94 I am satisfied that the implementation of the Scheme would not have a material adverse effect on:

- The security of the benefits of the existing ReAssure policies;

- The reasonable expectations of the existing ReAssure policyholders in respect of their benefits; or
- The standards of administration, service, management and governance that apply to the existing ReAssure policies.

10.95 As stated in Section 8 there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.

10.96 I will provide an update on these in my Supplementary Report.

## 11. The effect of the Scheme on the non-transferring LGAS policies

### INTRODUCTION

- 11.1 If the Scheme were to be approved by the High Court and implemented, all of the transferring business would be transferred out of LGAS and into ReAssure.
- 11.2 As at 31 December 2018, the transferring business consisted of approximately 1.0 million policies and a BEL of £28 billion, and LGAS had approximately 11.7 million policies and a BEL of £115 billion. The transferring business makes up 24% of the total LGAS BEL as at 31 December 2018.
- 11.3 In this section of my report I consider the likely effects on the non-transferring LGAS policies of the implementation of the Scheme. The key points to consider in respect of the non-transferring LGAS policies are the likely changes in the following due to the transfer:
- **The security of the benefits of the non-transferring LGAS policies**  
This is derived from the financial strength available to provide security for the benefits of the non-transferring policies under the appropriate risk appetite statements and applicable capital policy and external support received from the parent company by virtue of being part of a group.  
This is covered in paragraphs 11.5 to 11.11.
  - **The profile of risks to which the non-transferring LGAS policies are exposed**  
If the Scheme were to be implemented, the transferring LGAS policies would be transferred out of LGAS potentially changing the profile of risk exposures of LGAS.  
This is covered in paragraphs 11.12 to 11.18
  - **The reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits**  
This is covered in paragraphs 11.19 to 11.23.
  - **The standards of administration, servicing, management and governance applied to the non-transferring LGAS policies**  
This is covered in paragraphs 11.24 to 11.28.
- 11.4 Each of these areas is covered separately in the following sections.

### THE EFFECT OF THE SCHEME ON THE SECURITY OF THE BENEFITS OF THE NON-TRANSFERRING LGAS POLICIES

- 11.5 The financial strength that provides security for the benefits of the non-transferring LGAS policies is currently provided by:
- The assets covering the technical provisions and SCR of the transferring business held by LGAS as required under the Solvency II regulations;
  - The additional financial strength required by the LGAS RA Statement including the strength of the governance around the LGAS RA Statement and changes to it; and
  - Any additional support from outside LGAS, including the L&G Group.
- 11.6 If the Scheme were to be implemented, the non-transferring LGAS policies would continue to be policies of LGAS and would continue to derive their security as described in paragraph 11.5. In addition there would be no change to:
- The Solvency II regime and the technical provisions and SCR for the non-transferring LGAS policies would remain calculated in accordance with the Solvency II regime;
  - The approval for the use of the LGAS PIM: the risk margin and SCR for the non-transferring LGAS policies would continue to be calculated using the LGAS PIM;
  - The LGAS RA Statement; and
  - Any additional support from outside LGAS.

- 11.7 Given the above, I need to consider the effect of the Scheme on the financial strength available to provide security for the benefits of the non-transferring LGAS business.
- 11.8 Based on the financial information as at 31 December 2018 shown in Appendices A and B of this report:
- Prior to the implementation of the Scheme, the capital resources of LGAS covered its SCR with a ratio of 150% and with excess capital (above the SCR) of £3.5 billion; and
  - Following the implementation of the Scheme, the capital resources of LGAS would have covered its SCR with a ratio of 154% and excess capital of £3.5 billion.
- 11.9 The pro-forma Solvency II financial information shows that the implementation of the Scheme would be expected to slightly improve the Solvency II position of LGAS in terms of the SCR coverage and lead to an immaterial reduction in the absolute amount of excess capital. The projected financial strength shown in the pro-forma accounts of LGAS of 154% (using financial information as at 31 December 2018) indicates a position of considerable strength materially above both the required regulatory level of 100% and the level required to satisfy the LGAS RA Statement.
- 11.10 In addition, I have been provided with financial projections showing the expected path for the LGAS SCR coverage if the Scheme were to be implemented. These projections show that the SCR coverage ratio is expected to remain strong (relative to 100% of SCR) and higher than the level required under the LGAS RA Statement over the projection period.
- 11.11 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the non-transferring LGAS policies.

#### **THE EFFECT OF THE SCHEME ON THE PROFILE OF RISKS TO WHICH THE NON-TRANSFERRING LGAS POLICIES ARE EXPOSED**

- 11.12 The transfer of a significant volume of long-term business out of LGAS will change the risk profile of the non-transferring LGAS policies due to a different overall mix of products for the remaining business relative to that which exists currently.
- 11.13 The transferring business is primarily UWP and unit-linked business, with the main associated risks being equity and lapse risk.
- 11.14 The non-transferring LGAS business comprises:
- As written through the LGR division: worldwide pension risk transfer business, and individual retirement and lifetime mortgage business, the main associated risks being longevity and credit risks;
  - As written through the LGI division: UK retail and group protection business, US protection business reinsured in from Group subsidiaries in the US, and a tranche of the weather catastrophe risk reinsurance placed by LGIL, the main associated risks being mortality and morbidity risks; and
  - A range of workplace pension solutions focusing on UK auto-enrolment schemes (the Workplace Savings business) written through LGIM.
- 11.15 The RTA has been in effect since the Economic Transfer Date and most of the risks associated with the transferring business are currently borne by ReAssure rather than LGAS as was the case prior to the RTA being in force. Any change, as a result of the inception of the RTA, in the risk profile to which the non-transferring LGAS policies are exposed is therefore currently reflected in the Solvency II balance sheet of LGAS.
- 11.16 If the Scheme were to be implemented, there would be a change to the risk exposure for the non-transferring LGAS policies as the fixed per-policy expenses that are in place due to the RTA will no longer be applicable (thus reducing the exposure to expense risk), and any operational risks associated with managing the transferring LGAS policies and operating the RTA will be removed (other than certain historic mis-selling and mal-administration liabilities as discussed in Section 5). Furthermore, the non-transferring LGAS policies would no longer be exposed to the risks associated with the transferring non-profit annuities that are currently administered in conjunction with with-profits annuities in the LGAS WPF and are not within the scope of the RTA.
- 11.17 Following implementation of the Scheme, LGAS is projected to comfortably meet its capital requirements under Solvency II (which would reflect the risk profile of the non-transferring LGAS policies) and the capital requirements of the LGAS RA Statement.

- 11.18 I am satisfied that, although the implementation of the Scheme would cause a change to the profile of risks to which the non-transferring LGAS policies are exposed, this would not have a material adverse effect on the security of the benefits of the non-transferring LGAS business.

#### **THE EFFECT OF THE SCHEME ON THE REASONABLE EXPECTATIONS OF THE NON-TRANSFERRING LGAS POLICYHOLDERS IN RESPECT OF THEIR BENEFITS**

- 11.19 The non-transferring LGAS policies are unit-linked or non-profit in nature and, as such, policyholders' reasonable expectations in respect of their benefits are that:
- They receive their benefits as guaranteed under the policy, on the dates and in the contingencies specified in the terms and conditions; and
  - The benefits they receive reflect the investment performance of the assets in which their units are invested, net of contractual charges payable under the policies.
- 11.20 If the Scheme were to be implemented, there would be no change to:
- The terms and conditions of the non-transferring LGAS policies;
  - The methodology used to calculate the surrender values of the non-transferring LGAS policies;
  - The charges that apply to the non-transferring LGAS policies; or
  - The exercise of discretion in respect of the management of the unit-linked funds.
- 11.21 Though the Funds Foundation Project was already in place prior to the signing of the legal agreements for the proposed transaction, its implementation has been accelerated for the purposes of the Scheme and therefore I consider it appropriate to comment on the impact of the Funds Foundation Project on the reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits as part of my assessment of the Scheme.
- LGAS will notify the affected Workplace Savings policyholders of the fund separation exercise, as it is likely to lead to temporary systems outages that would disrupt the pension contribution cycle. The Workplace Savings policyholders will also bear the costs involved in the transition of assets to new funds. However, this action was underway prior to and is independent of the Part VII processes, and I therefore do not consider the associated disruption and costs for non-transferring Workplace Savings policyholders to be an effect of the implementation of the Scheme.
  - The separation of funds could have an adverse impact on the affected Workplace Savings policyholders if it resulted in them being invested in materially smaller funds with higher per-policy costs and less bargaining power. However, the Workplace Savings business is of a significant size and is growing, with £27.6 billion of assets under management and a 2.7 million customer base in 2017 versus £20.8 billion of assets under management and 2.1 million customers in 2016, and, with the sale of the transferring business, LGAS intends to focus on continued growth in this area. Therefore, I am satisfied that the reduction in fund size as a result of the implementation of the Funds Foundation project would not have a material adverse effect on the non-transferring Workplace Savings policyholders.
  - I have reviewed the proposals in relation to the split of the linked pension property fund and reallocation of approximately 50 directly held properties between the Workplace Savings and transferring business. I would note that:
    - Due to the nature of the asset class, and the proposed approach of apportioning the physical property assets between two funds rather than developing a structure which would allow the notional unitisation of the property assets, it is not possible to create two new portfolios with exactly the same risk, return and other key features as the original linked pension property fund;
    - The subjective nature of property valuations presents a material risk that the valuation provided for any given property is not realisable in a sale scenario, which in turn presents a challenge in terms of determining a split that is fair to all groups of policyholders; and
    - The exercise could lead to a change of pricing basis (between offer and bid) which could have an impact on the value of the policyholder units held within the fund.

- 11.22 For the same reasons as described in Section 8 in respect of the transferring business, I am satisfied that the separation of the unit-linked funds, including the property fund, does not lead to material adverse impact on the non-transferring policyholders.
- 11.23 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits.

#### **THE EFFECT OF THE SCHEME ON THE STANDARDS OF ADMINISTRATION, SERVICING, MANAGEMENT AND GOVERNANCE APPLIED TO THE NON-TRANSFERRING LGAS POLICIES**

- 11.24 The non-transferring LGAS policies are unit-linked or non-profit in nature and, as such, policyholders' expectations in respect of the standards of administration, servicing, management, and governance that apply to their policies after the Legal Effective Date are that they are in line with the contractual terms under the policies, are not materially worse than those they currently receive.
- 11.25 If the Scheme were to be implemented, there would be no change to:
- The administration and servicing of the non-transferring LGAS policies – these would be carried out by the same teams and according to the same service standards and procedures as currently, none of which would change as a result of the implementation of the Scheme.
  - The asset management arrangements for the non-transferring LGAS policies and the governance around these including the performance standards to which these arrangements are held.
  - The governance and management of the non-transferring LGAS policies – this will remain the responsibility of the LGAS Board and the corresponding Board and LGAS Committees, and the senior management team at LGAS. None of these would change as a result of the implementation of the Scheme.
- 11.26 There are a small number (26) of employers that have group personal pension schemes and group stakeholder schemes which are currently automated via a single interface. If the Scheme were to be implemented, these employers would need to interact with two separate entities and there would be no impact on the individual members of the schemes.
- 11.27 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the standards of administration, servicing, management and governance that apply to the non-transferring LGAS policies.

#### **CONCLUSION FOR THE NON-TRANSFERRING LGAS POLICIES**

- 11.28 I am satisfied that the implementation of the Scheme would not have a material adverse effect on:
- The security of the benefits of the non-transferring LGAS policies;
  - The reasonable expectations of the non-transferring LGAS policyholders in respect of their benefits; or
  - The standards of administration, service, management and governance that apply to the non-transferring LGAS policies.

## 12. My considerations in respect of the ReAssure IPO

### INTRODUCTION

- 12.1 As set out in Section 4 and Section 6 of this report, on 3 August 2018, the Swiss Re Group announced that it was considering whether to proceed with an IPO of shares in the ReAssure Group in 2019.
- 12.2 In anticipation of a potential IPO, a new public parent company (i.e. RGP) has been set up, of which RML and ReAssure are now subsidiaries. The PRA has approved the Change in Control application for RGP.
- 12.3 As set out in Section 4 and Section 6 of this report, on 14 June 2019, RGP confirmed its intention to proceed with the IPO.
- 12.4 A change of ownership resulting from the IPO could potentially lead to changes to the availability of parental capital support for ReAssure (which is currently provided by the Swiss Re Group and MS&AD) and to the management and governance of the insurance business within ReAssure.
- 12.5 In terms of the different groups of policies considered in Sections 8, to 11 of this report:
- **The transferring LGAS policies (Section 8):**

If the Scheme were to be implemented, these would be transferred into ReAssure and thus would become exposed to any changes resulting from the IPO.

Therefore, my conclusions in Section 8 of this report in respect of the effect of the Scheme on the transferring LGAS policies could be affected by the ReAssure IPO.
  - **The existing ReAssure policies (Section 10):**

If the Scheme were to be implemented, these would remain in ReAssure. Although such policies might be affected by the ReAssure IPO, the potential effects of the ReAssure IPO would not be altered by the implementation of the Scheme and so the effect of the ReAssure IPO on the existing ReAssure policies is therefore not within the scope of my considerations as Independent Expert for this Scheme.

Therefore, my conclusions in Section 10 of this report in respect of the effect of the Scheme on the existing ReAssure policies would be unaffected by the ReAssure IPO.
  - **The non-transferring LGAS policies (Section 11):**

If the Scheme were to be implemented, these would remain policies of LGAS and are therefore unaffected by the ReAssure IPO.

Therefore, my conclusions in Section 11 of this report in respect of the effect of the Scheme on the non-transferring LGAS policies would be unaffected by the ReAssure IPO.
- 12.6 In this section of my report I therefore need only to consider, if the Scheme were to be implemented, the likely effects of the ReAssure IPO on the transferring LGAS policies.

### THE EFFECT OF THE REASSURE IPO ON THE SECURITY OF THE BENEFITS OF THE TRANSFERRING POLICIES

#### Introduction

- 12.7 If the ReAssure IPO were to go ahead:
- The transferring LGAS policies would, once in ReAssure, continue to have their technical provisions and SCR calculated in accordance with the Solvency II regime (which would not change as a result of the IPO).
  - There would be no change to the ReAssure PIM: it would remain approved by the PRA for use in respect of the SCR for the risks of the existing RNPf business.
  - There would be a change to the risk appetite statement applicable to the business in ReAssure (which if the Scheme were to be implemented would include the transferring LGAS business).



The current proposed version of the risk appetite statement to apply to the post-IPO company is the ReAssure IPO RA Statement as set out below and in Section 6 of this report.

- There would be a change to the capital support that ReAssure could turn to from the group of owners in the event that it is required. This is currently provided by the Swiss Re Group and MS&AD but the post-IPO company would have a wider group of owners.

### **The risk appetite statement that would apply to the post-IPO company**

#### *The ReAssure IPO RA Statement*

- 12.8 If the ReAssure IPO were to proceed then, as described in Section 6 of this report, as approved by the ReAssure Board and the RGP Board, the ReAssure IPO RA Statement would apply.

#### *The target level of capital required by the ReAssure IPO RA Statement*

- 12.9 The ReAssure IPO RA Statement requires ReAssure to hold sufficient capital resources to cover the ReAssure IPO RA Statement level which is stronger than the current ReAssure RA Statement. This is to be expected for the following reasons:

- After the IPO, it is likely that it would take longer (by an estimated 6 to 12 months) for ReAssure to raise capital than currently as the existing parental support from the Swiss Re Group and MS&AD would change.
- Under the Solvency II requirements, EIOPA sets out an extended recovery period for firms in the case of an 'exceptional adverse situation' and, based on analysis of past significant market events, ReAssure considers the likelihood of an exceptional adverse market risk scenario to be less likely than a breach of the ReAssure IPO RA Statement level.

- 12.10 The ReAssure IPO RA Statement level has been derived using the ReAssure PIM as at 30 June 2018 and this will be recalibrated as at 30 June 2019 and, if the ReAssure IPO proceeds, would be reassessed annually thereafter or after significant changes to the risk profile of ReAssure. It would also be subject to a minimum level.

- 12.11 Any dividend payments made in advance of the IPO would make allowance for the ReAssure IPO RA Statement level.

#### *Additional restrictions under the ReAssure IPO RA Statement*

- 12.12 The proposed ReAssure IPO RA Statement also sets out that:

- **If a with-profits fund were unable to cover its SCR following a stress scenario after allowing for management actions, the RNPF would be required to hold additional capital to cover the shortfall.**

This provides additional security for transferring policyholders relative to the current ReAssure RA Statement, which contains no explicit requirements for the capitalisation of the with-profits funds other than to maintain 100% SCR coverage, to pay 100% of asset shares on surrender, death and maturity over the long-term (subject to any minimum guaranteed amount), and to distribute the estates over the remaining terms of the policies in the funds.

- **If there were reliance on the TMTP to cover the SCR, dividend payments would be restricted.**

This is the same as the current ReAssure RA Statement.

- **The target capital buffer would be subject to a minimum based on ReAssure's largest counterparty exposure.**

This is similar to an existing restriction under the ReAssure RA Statement.

Currently, ReAssure's main counterparty risk exposure is to the Swiss Re Group and to manage this risk the target capital buffer is subject to a minimum that is based on the capital impact of the Swiss Re Group defaulting on its obligations to ReAssure. As the implementation of the ReAssure IPO would likely result in changes to the counterparty risk profile of ReAssure, restating this minimum relative to ReAssure's largest counterparty exposure (rather than to the Swiss Re Group specifically) ensures that the minimum would continue to serve the same purpose post-IPO.

- **Excess capital would be managed to be within a range of the target capital.**

This is similar to the current ReAssure RA Statement with the red / amber / green ranges now explicitly defined such that:

- A solvency coverage ratio above the ReAssure IPO RA Statement level is considered a green range within which ReAssure would pursue its strategic objectives;
- Below the ReAssure IPO RA Statement level is an amber range within which management actions would be taken to return the solvency coverage ratio to green; and
- Below the amber range is considered a red range within which more substantive recovery actions would be triggered to restore amber status as soon as possible but in any event within 12 months.

#### *Conclusion regarding the ReAssure IPO RA Statement*

- 12.13 If the ReAssure IPO were to proceed then I am satisfied that if the ReAssure IPO RA Statement were to apply to the post-IPO ReAssure then there would not be a material adverse effect on the transferring policies.
- 12.14 If there are further developments in the form and content of the ReAssure IPO RA Statement, I shall consider them in my Supplementary Report.

#### *The uncertainty regarding the risk appetite statement that would apply to the post-IPO company*

- 12.15 Whilst it is helpful that the ReAssure Board and the RGP Board have approved the ReAssure IPO RA Statement, adherence to the ReAssure IPO RA Statement will not be a formal condition of the IPO and there is the risk that a new owner could change the risk appetite for both RGP and ReAssure.
- 12.16 This report has been written based on the assumption that in the event of the IPO the risk appetite adopted by the post-IPO company would be at least as strong as the ReAssure IPO RA Statement and if the risk appetite and capital policy adopted by the post-IPO company were to be weaker than the ReAssure IPO RA Statement then the conclusions of this report would need to be revisited.
- 12.17 I have discussed with ReAssure the likely outcomes of the IPO in respect of the company structure and the risk appetite of the post-IPO company and the following should be noted:
- After an IPO the current owners, SR Life Capital and MS&AD would retain significant proportions of the post-IPO company: MS&AD would retain 25% and SR Life Capital is aiming to retain a significant proportion. It is unlikely that SR Life Capital and MS&AD would allow either:
    - The risk appetite for the post-IPO company to be weaker than the ReAssure IPO RA Statement; or
    - The risk appetite for the post-IPO company to be changed without due analysis and governance.
  - Where a material proportion of the ownership changes (new owners with greater than a 10% share) there would be the need for a Change in Control approval process through which the PRA would, in consultation with the FCA, consider the impact of a proposed change in control on the firm's ability to comply and continue to comply with the PRA's prudential requirements, including the relevant threshold conditions. This may include, the resilience of the target firm's business model, capital and liquidity position, governance, risk management and controls, and the group structure. Thus the regulators would ensure that the future owners:
    - Pay due regard to the importance of treating customers fairly in respect of policyholder benefit security; and
    - Understand the importance of governance and management in accordance with the PRA Rulebook and the FCA's SMCR regime.

If the application for Change in Control is approved the PRA will issue an approval notice.

- Should the post-IPO ReAssure Board wish to make material changes to the ReAssure IPO RA Statement after the IPO, non-objection would be required from the PRA and it would ensure that any such changes would not lead to a material reduction in the security of the benefits of the ReAssure policies.
- 12.18 Based on the above, I am satisfied that there exist protections and controls in place to ensure that if there were to be an IPO the risk appetite that would apply to the post-IPO company would be such that there would not be a material adverse effect on the security of the benefits under the transferring LGAS policies.

- 12.19 In the event of the IPO completing before the Sanctions Hearing for this Scheme, I would report in a Supplementary Report for the Sanctions Hearing on the effects of the IPO on the conclusions of this report and this would include consideration of the effects of any changes to the ReAssure IPO RA Statement.

*Conclusion regarding the risk appetite statement that would apply to the post-IPO company*

- 12.20 If the ReAssure IPO were to proceed then I am satisfied that if the ReAssure IPO RA Statement were to apply to the post-IPO ReAssure then there would not be a material adverse effect on the transferring policies.
- 12.21 Although there is the potential for new owners to propose a different risk appetite statement to apply to the post-IPO ReAssure, I am satisfied that there exist protections and controls in place to ensure that there would not be a material adverse effect on the transferring policies.
- 12.22 If the IPO were to happen before the Sanctions Hearing I would consider the effects of the IPO in a Supplementary Report for the High Court at the Sanctions Hearing.

**The capital support available from the Group to the post-IPO company**

- 12.23 The parent company, RGP, would have its own target capital level (the "RGP buffer"), which would be higher than the ReAssure IPO RA Statement level.
- 12.24 If the ReAssure IPO were to proceed, RGP would initially target a solvency ratio above the RGP buffer.
- 12.25 In the future the RGP Board would review the risk appetite statement and determine whether future changes should be made.
- 12.26 RGP would be subject to the further restriction that dividends would not be possible if ReAssure was not adhering to its risk appetite.
- 12.27 I am satisfied that, if the IPO were to proceed the support available from the post-IPO RGP would be such that there would not be a material adverse effect on the security of the benefits of the transferring policies.

**THE EFFECT OF THE REASSURE IPO ON THE REASONABLE EXPECTATIONS OF THE TRANSFERRING POLICYHOLDERS IN RESPECT OF THEIR BENEFITS**

- 12.28 The implementation of the ReAssure IPO would not lead to any material changes to:
- The terms and conditions of the transferring policies.
  - The likelihood that they receive their benefits when due.
  - The size or frequency of those benefits.
  - In respect of unit-linked policies:
    - The range of funds available, the management of those funds, the investment objectives applied to those funds, the charges applied to those funds or the pricing of those funds;
    - The benefits received by the policyholders as these would continue to reflect the investment performance of the assets in which their units are invested and the contractual charges payable under the policies; or
    - The assets in which the units under unit-linked policies are invested as these would continue to be materially in line with the target investment allocation in the relevant fund literature.
  - In respect of with-profits policies:
    - The rights of the transferring with-profits policyholders to any future distributions from the LGWPF estate;
    - The methodology used to calculate asset shares and surrender values of the transferring with-profits policies;
    - The bonus and pay-out policies applied to the transferring with-profits policies;
    - The investment strategy applicable to the transferring with-profits policies; or

- The charges that apply to the transferring with-profits policies.
- In respect of non-profit policies:
  - The methodology used to calculate the surrender values of the transferring non-profit policies; or
  - The charges that apply to the transferring non-profit policies.

12.29 I am therefore satisfied that the ReAssure IPO would not have a material adverse effect on the reasonable expectations of the transferring policyholders in respect of their benefits.

**THE EFFECT OF THE REASSURE IPO ON THE STANDARDS OF ADMINISTRATION, SERVICING, MANAGEMENT AND GOVERNANCE APPLIED TO THE TRANSFERRING POLICIES**

12.30 Currently ReAssure relies on or is integrated with the Swiss Re Group in respect of a number of functions (including asset management and risk management), applications, policies and contracts.

12.31 In preparation for the IPO, plans have been developed and work is underway to transfer dedicated Swiss Re Group employees to ReAssure, replace Swiss Re Group services and contracts and enable ReAssure to operate on a standalone basis. In particular:

- A transitional service agreement would be put in place for the provision of back office asset management services from the Swiss Re Group for a period of 12 months post-IPO;
- A consultancy-lead solution would provide ReAssure with necessary risk management support; and
- The provision of the assurance functions has been closely reviewed at both management and Board level and, to the extent that internal resource is unavailable or insufficient, ReAssure would seek external supplementary resource for key activities.

12.32 It is difficult to be certain at this point what the impact of the IPO and associated programme of separation of work would be but, if the ReAssure IPO were to go ahead, there would not be expected to be changes to:

- The administration and servicing of the transferring policies, the majority of which would be carried out by RUKSL following the implementation of the Scheme; or
- The governance and management of the transferring policies, which would be the responsibility of the following:
  - In respect of the non-profit policies: the ReAssure Board, the corresponding Board and Executive Committees, and the ReAssure senior management team; and
  - In respect of the LGAS WPF policies: in addition to the above, there would be the ReAssure FC and the ReAssure WPA in respect of the LGWPF.

12.33 Though these structures and their membership could change following the ReAssure IPO, ReAssure considers such changes unlikely. Furthermore, I would expect any such changes to meet the Solvency II requirements, and the requirements and expectations of the PRA and the FCA, including the requirements of COBS 20 in respect of with-profits business.

- Fit and proper individuals would continue to run the business and be responsible for key functions;
- The PPFM for the LGWPF would not be expected to be materially different in substance to that prior to the IPO and in any case, any proposed material changes would require approval by the ReAssure WPA for the LGWPF and the ReAssure FC and would usually be notified to the FCA; and
- The governance and management of ReAssure would remain the responsibility of the ReAssure Board, the ReAssure FC, the corresponding Board and Executive Committees, and the ReAssure senior management team.

12.34 The progress of IPO programme will be regulatory reviewed by the Chairs of the ReAssure Board and the ReAssure Board Audit Committee, with comprehensive risk assessments provided to inform formal Go / No go decisions, and ReAssure has committed to providing me with regular updates on this.

12.35 Based on the information I have received to date, I am satisfied that if the ReAssure IPO were to go ahead then there exist sufficient controls to ensure that there would not be a material adverse effect on the standards of administration, servicing, management and governance that apply to the transferring policies.

## CONCLUSION REGARDING THE EFFECT OF THE REASSURE IPO ON THE TRANSFERRING POLICIES

- 12.36 I have discussed with ReAssure the likely outcomes of the ReAssure IPO in respect of the company structure and the risk appetite of the post-IPO company and although it is not possible to know with certainty what that structure might be or what form the applicable risk appetite statement might take, I am satisfied that, if the ReAssure IPO were to proceed:
- If the risk appetite statement applicable to the post-IPO company were to be at least as strong as the Board-approved ReAssure IPO RA Statement there would not be a material adverse effect on the security of the benefits of the transferring policies.
  - Although there is the potential for new owners to propose a different risk appetite statement to apply to the post-IPO ReAssure there exist protections and controls in place to ensure that there would not be a material adverse effect on the transferring policies.
  - The support available from the post-IPO RGP would be such that there would not be a material adverse effect on the security of the benefits of the transferring policies.
  - There would not be a material adverse effect on the reasonable expectations of the transferring policyholders in respect of their benefits.
  - There exist sufficient controls to ensure that there would not be a material adverse effect on the standards of administration, service, management and governance that apply to the transferring policies.
- 12.37 If the IPO were to proceed before the Sanctions Hearing I would consider the effects of the IPO in a Supplementary Report for the High Court at the Sanctions Hearing.

## 13. My considerations in respect of the fair treatment of customers

### THE APPROACH TO COMMUNICATIONS WITH POLICYHOLDERS

#### Introduction

- 13.1 Regulations under FSMA require a communication regarding the Scheme to be sent to every policyholder of the parties under the Scheme. However, this requirement may be waived at the discretion of the High Court which will give consideration to issues such as the practicality and costs of sending notices relative to the likely benefits for policyholders of receiving such communications.
- 13.2 The proposed communications regarding the Scheme can be split into two broad groups:
- Communications to LGAS policyholders; and
  - Communications to ReAssure policyholders.
- 13.3 LGAS will send a mailing pack to the LGAS transferring policyholders (subject to dispensations detailed below). The mailing pack is covered in greater detail in paragraphs 13.12 to 13.17.
- 13.4 Due to the size of the transferring business compared to the existing business of ReAssure, ReAssure will send a letter (the "Part VII Letter") to the existing ReAssure policyholders to make them aware of the Scheme (subject to dispensations). The Part VII Letter will provide less information than the mailing pack and is covered in paragraphs 13.20 to 13.28.

#### Definition of policyholder

- 13.5 The definition of policyholder has a wide scope under FSMA. In addition, in its publication on "the FCA's approach to the review of Part VII insurance business transfers", the FCA states that its definition of "policyholder" is broad.
- 13.6 LGAS and ReAssure acknowledge the FCA's broad interpretation of "policyholder" but propose to follow the approach proposed by the FCA as set out in paragraph 7.6 of "the FCA's approach to the review of Part VII insurance business transfers" which states:
- "Some Applicants take a different view of the scope of the definition of 'Policyholder'. We also acknowledge that there are compelling different views about some of the categories above. For example, employees who have not made a claim - and where there are currently no circumstances where they can - and where the employer is not at risk of default, and 'buy in' policies. However, in these cases, the Applicants have decided not to pursue their interpretation of the point, while also not conceding it, which we are content with, and instead use dispensations to achieve the same outcome."
- 13.7 The dispensations that are being sought by LGAS are detailed in paragraph 13.10 below and those being sought by ReAssure are detailed in paragraphs 13.18 and 13.19. In addition, LGAS has chosen to define PMS members of the PMS SIPP who have only invested in non-insured investments (and are proposed to be transferred to ReAssure under the proposed Scheme) as policyholders. ReAssure agrees with this interpretation in respect of the PMS members of the PMS SIPP but ReAssure have not defined ReAssure members of the ReAssure SIPP who have only invested in non-insured investments as policyholders.
- 13.8 LGAS and ReAssure intends to seek a dispensation from the wide scope of the definition of policyholder as specified in FSMA as it would not be possible to identify every person who may have a beneficial or underlying interest in every policy. For example,
- Persons may have become "policyholders" without LGAS or ReAssure having been notified.
  - All policyholders may not be able to be identified as some may have changed names and/or addresses without notifying LGAS or ReAssure.
  - The operational records used by LGAS or ReAssure may not always identify every policyholder.
  - The contact details of some policyholders may not be known, for example ex-spouses that are a beneficiary under a policy following a divorce settlement.
- 13.9 I have reviewed the justification for the definition of policyholder proposed by LGAS and ReAssure and am satisfied that it is appropriate.

## The proposed “waiver” applications: LGAS

13.10 LGAS intends to seek a waiver, which will have the effect it is not required to send a written notice to:

- The policyholders of LGAS (c.9m policyholders) that would not be transferred if the Scheme were to be implemented.

The cost of mailing these existing policyholders of LGAS has been estimated to be approximately £3.5 million (with the additional related cost of providing global call centre services estimated to exceed £2 million) and therefore the cost of mailing such policyholders is considered by LGAS to be disproportionate relative to the benefits to the policyholders that would result from any such mailing given that:

- There would be no change to the terms and conditions of any non-transferring LGAS policies.
- The financial impact of the Scheme on the non-transferring LGAS policyholders is not considered to be material as discussed in Section 10.
- As described in earlier sections of this report, in my view there would be no material adverse effect on:
  - The security of the benefits of any such policies;
  - The reasonable expectations of any such policyholders in respect of their benefits; or
  - The governance, administration and servicing arrangements applicable to such policies.
- Those policyholders classified as “gone-aways” c.62k policyholders, which is estimated as 6.5% of the transferring business (as at February 2019) on the grounds that it would not be possible to contact them.

To reduce the level of gone-aways, any policyholders (and trustees) that have been identified as gone-aways on the legacy pensions administration system (which covers c.75% of the LGAS gone-aways) have been through an initial tracing process in addition to the normal business as usual process. This process has identified potential new addresses for c16,000 policyholders and letters have been sent to validate the revised information. As at 6 March 2019, the addresses of 8,054 policyholders have been fully validated.

The DWP tracing service will also be used for the remaining legacy pensions business that LGAS was not able to trace using the above process (along with a group of 2,000 buy-out plan policyholders) where LGAS has a valid NI number.

The other policyholders identified as gone-aways not on the legacy pension administration system will have been put through the LGAS normal tracing processes within the 12 to 18 months prior to the mailing.

In addition to this a further trace may be performed using a variety of sources such as Experian, BT directory enquiries and 192.com database searches

- Minors (c.2,700 policyholders) who are policyholders as the guardian/responsible adult will be contacted instead as LGAS consider it appropriate for these adults to be involved in the decision process given the complexity of the matter under consideration.
- Assignees where LGAS does not hold the current address will not be contacted on the grounds that it would not be possible to contact them as LGAS has no practical means of obtaining the required information.
- Multiple policyholders under a single LGAS policy. LGAS will follow its usual approach for communications in these circumstances. That is, LGAS will notify:
  - Both policyholders in one communication if they reside at the same address; and
  - The first or nominated policyholder when there are more than two policyholders and/or the policyholders reside at different addresses.

LGAS may also not hold the details of any additional policyholders or only have recorded limited information on these policyholders. In adopting the above approach, LGAS estimate that approximately 10k policies where we cannot be sure if they are issuing a mailing pack directly to all of the Policyholders on that policy.

- Policies with more than one beneficiary (including dependants), for example joint life annuitants and policies held in trust, including discretionary trust arrangements. For these policyholders a mailing pack will be sent to the main policyholder which include a request for the content to be shared with other beneficiaries and



potential claimants. Furthermore, contact details of the additional format are typically not held and therefore it would not be possible to contact all such beneficiaries.

- Beneficiaries of trust-based pension schemes. Under these circumstances, LGAS will make the mailing pack available to the trustees to distribute to the scheme members at LGAS's expense (including printing, paper and postage, for distributing the pack to their members). LGAS will contact the trustees to discuss the Scheme and mailing with them as well as provide a letter template in Word format. In addition, LGAS will mail the Scheme member where the member's address is available and LGAS typically contact the member directly.
- "Not in force" policyholders where there is an on-going business review or remediation outstanding as the details of such policyholders are not easily accessible (particularly for those policies that have not been in force for a significant period of time). Furthermore, these not in force policyholders may find the Communications Pack confusing as they no longer have an in force policy with LGAS.

13.11 I am satisfied that the application for a waiver from the regulatory requirements to send a written notice to the LGAS policyholders as set out above is reasonable.

### **The mailing pack: LGAS**

13.12 Both the PRA Statement of Policy and the FCA Final Guidance state that, in respect of insurance business transfers, companies are required to notify the policyholders, or interested persons, at least six weeks before the date of the High Court hearing at which the application to sanction the Scheme will be heard. LGAS will notify the policyholders three or four months prior to the Sanctions Hearing.

13.13 All the transferring policyholders for whom LGAS holds a name and address on its computerised databases, except for those populations where a mailing waiver has been granted by High Court will be sent a mailing pack about the Scheme prior to the Sanctions Hearing to enable them to make representations to the High Court if they feel they may be disadvantaged by the Scheme.

13.14 After a tender process, LGAS has selected an external printing house (Communis plc) which is already familiar with working with data from LGAS. The printing house has demonstrated that it is able to handle a mailing programme of the size and complexity required by the Scheme.

13.15 The mailing pack will contain:

- A covering letter, for which there will be several bespoke variants, depending on the recipient; and
- A standardised brochure, which will contain:
  - A summary of the Scheme and a summary of this report;
  - Questions & Answers; and
  - A copy of the legal notice to the High Court.

13.16 LGAS captures data within the business when a customer expresses a requirement to receive communication in a different format and will also make the mailing pack available in large print / braille / audio upon request. Furthermore, LGAS will provide a helpline number which customers may call if they have difficulties reading the relevant documents.

13.17 I have reviewed the final mailing pack and covering letters and I am satisfied that sufficient information on the potential impact of the proposed transfer has been included and that this information has been provided in a suitable format.

### **The proposed "waiver" applications: ReAssure**

13.18 ReAssure intends to seek a waiver, which will mean that ReAssure would not be required to send a written notice to:

- Those policyholders classified as "gone-aways" on the grounds that it would not be possible to contact them.  
The number of gone-aways is currently c.152k policyholders, which is estimated as 9% of the existing business of ReAssure (as at 1 September 2018). For the majority of cases, ReAssure uses Equifax to automatically trace policyholders that have been recorded as a gone-away as part of its standard procedure.

- Minors who are policyholders as the guardian/responsible adult will be contacted instead as ReAssure consider it appropriate for these adults to be involved in the decision process given the complexity of the matter under consideration. Furthermore, this approach is in accordance with ReAssure's standard procedures to communicate with policyholders who are minors.
- Dependants under policies. Contact details of the additional format are typically not held and therefore it would not be possible to contact all such beneficiaries.
- Beneficiaries of trust-based pension schemes. Unless ReAssure has the member's address and ReAssure typically contacts the member directly, ReAssure will contact the trustees and not the members/beneficiaries. As part of the contact with the trustees, ReAssure will instruct the trustees to contact members and therefore ReAssure consider that further direct contact with the members would give limited additional benefit compared to the associated costs. Furthermore, ReAssure may not hold contact details for the beneficiaries and given the limited detail that is held, they may be hard to trace.
- Assignees where ReAssure does not hold the current address on the grounds that it would not be possible to contact them as ReAssure has no practical means of obtaining this information. In the case of an assignee with more than one address, ReAssure will notify the assignee at the assignee's headquarters.
- Multiple policyholders under a single policy. ReAssure will follow its usual approach for communications in these circumstances. That is, ReAssure will notify:
  - Both policyholders in one communication if they reside at the same address; and
  - The first or nominated policyholder when there are more than two policyholders and/or the policyholders reside at different addresses.

ReAssure may also not hold the details of any additional policyholders or only have recorded limited information on these policyholders.

- Deceased policyholders (where the policy has already been divested and is being held in cash waiting to be distributed). In these circumstances, ReAssure believe that the manual process required to contact or notify beneficiaries, executors or any other relevant person would be impractical.

13.19 I am satisfied that the application for a waiver from the regulatory requirements to send a written notice to the ReAssure policyholders as set out above is reasonable.

#### **The Part VII Letter: ReAssure**

13.20 All the existing ReAssure policyholders for whom ReAssure holds a name and address on its computerised databases, except for those populations where a mailing waiver has been granted by the High Court, will be sent the Part VII Letter prior to the Sanctions Hearing. This will enable them to make representations to the High Court if they feel they may be disadvantaged by the Scheme.

13.21 As discussed in paragraph 13.4, the Part VII Letter that will be sent to the existing ReAssure policyholders will not include the same information as the mailing pack that will be sent to transferring policyholders. The letter will notify the existing ReAssure policyholders of the Scheme and include the conclusions in respect of the effect of the Scheme on the existing ReAssure policyholders as set out in Section 10 of this report.

13.22 The Part VII Letter will also provide information regarding the ReAssure website ([www.reassure.co.uk/LGAS-transfer](http://www.reassure.co.uk/LGAS-transfer)) where policyholders can view or download the key documents in respect of the Scheme including the Scheme itself and this report. The letter will also set out that a supplementary report will be produced and made available at least two weeks prior to the Sanctions Hearing.

13.23 ReAssure will start sending the Part VII Letter to the existing ReAssure policyholders (or will notify them via the online portal or email, where these are the customary forms of notification) four months prior to the Sanctions Hearing for a period of two months.

13.24 There are existing ReAssure policyholders who are typically contacted by third parties rather than ReAssure. These include policyholders of:

- The National Mutual Personal Pension Scheme which is a SIPP where Namulas Pension Trustees Limited (a subsidiary of ReAssure) is the trustee and LV Life Services Limited ("LV") is the administrator.

- The Tomorrow Personal Pension Scheme which is a SIPP where NM Trustees Limited is the trustee and LV is the administrator.
- A block of annuities that were acquired by ReAssure from HSBC Life. These annuities are administered by Hannover Re.

13.25 In each of these cases the Part VII Letter will be sent to the policyholders by ReAssure:

- Branded with the LV brand for The National Mutual Personal Pension Scheme;
- Branded with the LV brand for The Tomorrow Personal Pension Scheme; and
- Branded with the Hannover brand for block of Hannover annuities.

13.26 In addition to the Part VII Letter, an accompanying ReAssure branded covering letter will be sent to the policyholders by ReAssure.

13.27 ReAssure will also make the Part VII Letter available in large print / braille / audio upon request. Furthermore, ReAssure will provide a helpline number which customers may call if they have difficulties reading the relevant documents.

13.28 I have reviewed the Part VII Letter and am satisfied that sufficient information on the potential impact of the proposed transfer has been included and that this information has been provided in a suitable format.

#### **Further publication of the Scheme and distribution of information in respect of the Scheme**

13.29 The LGAS website ([www.LegalandGeneral.com](http://www.LegalandGeneral.com)) and the ReAssure website ([www.reassure.co.uk/LGAS-transfer](http://www.reassure.co.uk/LGAS-transfer)) will contain the following information (accessible via a single click from the homepages):

- My report (this report), a summary of my report and any supplementary reports;
- The full Scheme document and a summary of the Scheme document;
- A copy of the legal notice of the High Court hearing;
- Questions and answers regarding the transfer; and
- The PPFMs that would apply after the implementation of the Scheme.

13.30 The reports from the LGAS Chief Actuary and the LGAS WPA, plus any supplementary reports, will be put on the LGAS website. The reports of the ReAssure Chief Actuary and the ReAssure WPA report will not be made available to the public.

13.31 LGAS and ReAssure will publish a notice in a form approved by the PRA in the following publications in the UK:

- The London Gazette;
- The Edinburgh Gazette;
- The Belfast Gazette; and
- The Times, The Daily Telegraph, The Sun, The Guardian, and The Daily Mail.

13.32 LGAS and ReAssure will publish a notice in respect of the Jersey and Guernsey Schemes in the following publications for the business carried on in or from within Jersey, and policyholders resident in the Bailiwick of Guernsey:

- The Jersey Gazette;
- La Gazette Officielle in Guernsey;
- The Alderney Gazette in Alderney; and
- The Sark Public Notice Box in Sark.

13.33 LGAS is seeking a dispensation to advertise in two national newspapers in EEA states other than the UK as the transferring policies:

- Were marketed and sold exclusively in the UK;

- Have terms and conditions that state that the policyholder must have been a resident in the UK when the policy was taken out; and
  - Are governed by English law.
- 13.34 LGAS has estimated the costs of advertising in two national newspapers in EEA states other than the UK as approximately £500,000. Due to the small number of LGAS and ReAssure policyholders now resident in the EEA (other than UK) (7,584 or 0.8% of transferring policyholders for LGAS, 19,383 or 1.1% for ReAssure), this cost is considered by LGAS and ReAssure to be disproportionate to the benefit that will be gained.
- 13.35 LGAS and ReAssure will also publish a newspaper notice in the international editions of the Financial Times, Daily Mail and the Times. LGAS and ReAssure believe that these papers are more likely to be read by any policyholders in EEA states as this is likely to have arisen due to normal migration trends.
- 13.36 Furthermore:
- For policyholders who have access to the LGAS or ReAssure online portals, a notification will be placed online with a link to the web-page detailing the Proposed Transfer.
  - Paper copies of the full scheme document and the full version of this report will be made available without charge to any person who requests them by calling a number (ReAssure will be offering a freephone number for UK callers and a standard rate number call for any overseas callers) or by writing to LGAS or ReAssure.
  - Notifications will also be posted on Legal & General social media accounts, including Facebook, Twitter and LinkedIn.

#### **New business**

- 13.37 LGAS is making current and prospective policyholders aware that their policy may be transferred to ReAssure prior to completing any application for new products or top-ups via a highlighted text box on relevant consumer and adviser pages with a link to a more detailed explanatory page. It should be noted that most of the product lines within the transferring LGAS business are closed to new business and were all closed by the end of 2018, with the exception of increases to existing pension policies and new members joining existing pension schemes.
- 13.38 Furthermore, new policyholders who take out policies close to the Sanctions Hearing will be sent a mailing pack as soon as possible after becoming a policyholder in order to ensure that they are informed of the Scheme.

#### **Platform charges for SIPP policies**

- 13.39 As described in Section 5, it is proposed that a change would be made to the SIPP product terms and conditions to allow a platform charge to be applied for approximately 450 SIPP policies with uninsured collective investments following their transfer to the ReAssure Group.
- 13.40 Though distinct to the Scheme, the change will be communicated to policyholders as part of the communications regarding the Scheme, rather than in a separate policyholder mailing.
- 13.41 One of the covering letter variants referred to in paragraph 13.15 is specifically targeted at the transferring LGAS policyholders that hold a SIPP policy. In addition to information in the standard letter, this letter variant contains details of the application of the platform charge discussed in paragraphs Section 5.
- 13.42 There will also be a dedicated phone line for these policyholders to call with specially trained staff attending to the calls.
- 13.43 I am satisfied that the covering letter makes it sufficiently clear to affected policyholders that the change to the application of the platform charge is not as a result of the proposed transfer.

#### **Other communications**

- 13.44 Along with the communication packs relating to the Scheme, there will be a separate 'Welcome' communication from ReAssure to the transferring policyholders after the Sanctions Hearing. The timing of these communications will be chosen so as to not detract from the messages within the Scheme mailing pack. This will also be the case for other communications, such as:
- Bonus notices; and

- The effect of the Funds Foundation Project, referred to in Section 5, on the affected policyholders.

## **Conclusion**

- 13.45 The Chief Actuaries and WPAs of both LGAS and ReAssure have confirmed that in their view the proposed approach to communication with policyholders is fair and reasonable and that the information contained in the notification to policyholders adequately describes the proposals to policyholders.
- 13.46 I am satisfied that the proposed approach to communication with policyholders, including the application for the waivers, is fair and reasonable.

## **THE COSTS OF THE SCHEME**

- 13.47 As described in paragraphs 7.58 to 7.60, the costs of the Scheme will be split entirely between the shareholder funds of LGAS and ReAssure.
- 13.48 I have separately considered the one-off payment of £50 million from the LGWPF to the RNPF as a contribution to migration costs alongside the introduction of the fixed expense arrangement in paragraphs 8.105 to 8.112 and concluded that, overall, this would not have a material adverse effect on the reasonable expectations of the with-profits policyholders in the LGWPF in respect of their benefits.
- 13.49 I am satisfied that the allocation of the costs of the Scheme to the shareholder funds of LGAS and ReAssure is appropriate given the motivation for the Scheme was to allow LGAS to focus on its growth in core business areas (as described in Section 5) and ReAssure to continue its strategy of growing through the acquisition of closed life books (as described in Section 6).

## **ACCESS TO THE FOS**

- 13.50 Since ReAssure is a UK-regulated company like LGAS the access for the transferring policyholders to the FOS is unaffected by the transfer.

## **OTHER CREDITORS**

- 13.51 LGAS and ReAssure have confirmed that there are no bondholders or third parties to securitisation arrangements or any other creditors of either company who would be affected by the Scheme.

## 14. My other considerations arising from the scheme

### THE ECONOMIC EFFECTIVE DATE AND LEGAL EFFECTIVE DATE OF THE SCHEME

- 14.1 As I set out in Section 4 and Section 7, if approved by the High Court, the Scheme will become operative on the Legal Effective Date (currently expected to be 4 November 2019) at which point the transferring business will legally transfer from LGAS to ReAssure.
- 14.2 The Scheme provides that it will take effect as between LGAS and ReAssure, including for accounting purposes from the Economic Effective Date (currently expected to be 1 November 2019).
- 14.3 The Legal Effective Date and Economic Effective Date are on different dates (which is unusual although by no means unique) for logistical reasons as it will enable LGAS and ReAssure to prepare a valuation at the end of month and to allow time for the data to be migrated between the appropriate systems.
- 14.4 I have discussed this with senior management of LGAS and ReAssure, who are satisfied that there is no scope for the mechanism to materially adversely affect policyholders and steps will be taken to ensure that any adverse effects are mitigated.
- 14.5 There may be slight delay to some policyholder transactions during the migration process but LGAS and ReAssure will aim to ensure that transactions continue to meet the existing service level agreements ("SLAs") (noting that the SLAs may differ between LGAS and ReAssure in some cases). In order to help to achieve this aim, during the migration process, transactions will be "stockpiled" and prioritised. Where the date and time of a policyholder transaction affects policyholder benefits and a transaction is carried out during the migration, ReAssure has committed that policyholders will not be financially exposed, positively or negatively, as the transaction will reflect the unit price that would have applied under business as usual operations.
- 14.6 This has also been discussed with Slaughter and May and Herbert Smith Freehills and their view is that, because the Scheme provides that this mechanism only applies as between LGAS and ReAssure and does not affect the rights of policyholders or third parties in relation to the transferring business, from a legal perspective the mechanism will not have a material adverse effect on the policyholders affected by the Scheme.
- 14.7 As I set out in Section 4, I am satisfied that it is appropriate for me to rely on the conclusions of Slaughter and May and Herbert Smith Freehills in relation to the legal effect of the Scheme.

### THE FUTURE OPERATION OF THE SCHEME

- 14.8 If the Scheme is approved by the High Court and subsequently implemented LGAS and ReAssure are committed to implementing the Scheme as set out in the Scheme document (and reflected in this report). In giving effect to those obligations, the Directors of LGAS and ReAssure must act in accordance with their fiduciary responsibilities under UK company law.
- 14.9 At any time after the High Court's sanction of the Scheme, LGAS and ReAssure must apply to the High Court for sanction of any amendments to the Scheme, except where the amendment is considered to be minor or technical, in which case the PRA and FCA must be notified. In respect of the Jersey and Guernsey Schemes, ReAssure must apply to the Royal Courts of Jersey or Guernsey for sanction of any amendments to the Jersey or Guernsey Scheme, except where the amendment is considered to be minor or technical, in which case the Jersey Financial Services Commission or Guernsey Financial Services Commission must be notified.
- 14.10 In my opinion there are reasonable safeguards in place to ensure that, if approved by the High Court, the Scheme will be operated as presented to the High Court.

### WHAT WOULD HAPPEN IF THE SCHEME WERE NOT TO BE IMPLEMENTED?

- 14.11 If the Scheme does not proceed for any reason, then the transferring LGAS policies would not become policies of ReAssure and would remain within LGAS. The BTA contains further details of what would happen if this were to occur:
- LGAS and ReAssure would work together to effect an alternative scheme to transfer the policies and, in the interim, administration of the business would be retained by LGAS.

- Should no transfer be completed by 1 January 2021, LGAS and ReAssure would look to outsource the administration of the business to ReAssure. If this were successful, the BTA would cease but the RTA would continue. As part of the outsourcing arrangement:
  - A new IMA would be agreed on similar terms to that detailed in Section 5 ceasing no earlier than 30 June 2026.
  - A new AIA would be agreed on similar terms to that detailed in Section 5 ceasing no earlier than 30 June 2024.
- If no outsourcing arrangement could be agreed, a new scheme would be considered periodically to effect the transfer of the business.
- The fixed expense deal detailed in paragraphs 5.40 to 5.42 would only come into effect on completion of the transfer of the business before 31 December 2019. If no transfer is completed before this date, the fixed expense deal would no longer apply and the associated payment of £50 million for migration costs by the LGWPF would not be made.

14.12 I am satisfied that, if the Scheme were not implemented for any reason, then the process set out in the BTA would ensure that there would not be a material adverse effect on the ReAssure or LGAS policies.

## THE IMPLICATIONS OF THE SCHEME FOR SOLVENCY II APPROVALS

14.13 Prior to the Economic Effective Date, ReAssure intends to apply for PRA approval to recalculate the TMTP to reflect the transferring business. Although the transferring non-profit annuities will be allocated to the existing ReAssure MA portfolio, ReAssure does not believe that a formal application will be required as ReAssure's existing MA approval will be sufficient. I will comment further on the status of the application to recalculate the TMTP relating to the transferring business in my Supplementary Report.

14.14 For LGAS, the Scheme will:

- Lead to a change to the LGAS PIM;
- Not have an impact on LGAS's MA application; and
- LGAS does not believe that it will lead to a recalculation of the LGAS TMTP.

## THE EFFECT OF THE SCHEME ON PREVIOUS SCHEMES

### Previous schemes of LGAS

14.15 LGAS has commissioned a review by their legal advisors (Slaughter and May) of the previous schemes to which LGAS has been party:

- ALLAC / LGAS 2003;
- Skandia / LGAS 2006;
- Nationwide Life / LGAS 2009;
- Lucida / LGAS 2014;
- Nationwide Life / LGAS 2014;
- LGAS / Canada Life 2016; and
- Scottish Equitable / LGAS 2017.

14.16 On the basis of this review Slaughter and May is satisfied that, if the Scheme were to be implemented:

- There would not be a material effect on any of the previous schemes to which LGAS has been party; and
- The terms of the previous schemes would not conflict with the terms of the Scheme.

14.17 I set out in Section 4 why I believe it is reasonable for me to rely on information provided by Slaughter and May as legal experts and therefore, I consider that it is reasonable and appropriate to rely on this confirmation.



## Previous schemes of ReAssure

- 14.18 ReAssure has commissioned a review by its legal advisors (Herbert Smith Freehills) of the certain previous schemes to which ReAssure has been party:
- The Gresham Scheme 1992;
  - The NM Scheme 2007;
  - The Guardian Scheme 2016;
  - ReAssure UK / Virgin Money Life 2005;
  - The HSBC Scheme 2015;
  - The Phoenix Scheme 2016;
  - The ALICO Scheme 2012;
  - The Barclays Life Scheme 2011;
  - The Crown Life Scheme 1995; and
  - The Zurich Scheme 2008.
- 14.19 On the basis of this review, Herbert Smith Freehills is satisfied that, if the Scheme were to be implemented:
- There would not be a material effect on any of the previous schemes to which ReAssure has been party; and
  - The terms of the previous schemes would not conflict with the terms of the Scheme.
- 14.20 I set out in Section 4 why I believe it is reasonable for me to rely on information provided by Herbert Smith Freehills as legal experts and therefore, I consider that it is reasonable and appropriate to rely on this confirmation.

## THE TAX IMPLICATIONS OF THE SCHEME

- 14.21 LGAS Group Tax have produced a report to identify any significant tax issues arising from the Scheme. I refer to this report as the “LGAS tax report”.
- 14.22 I have seen the final version of the LGAS tax report and, in forming my view on the Scheme, I have relied on this as expert opinions on the tax implications of the Scheme for LGAS shareholders and policyholders.

## Tax charged to the LGWPF

- 14.23 The methodology used to calculate the tax that would be charged to the LGWPF after the Economic Effective Date will be subject to the approval of the ReAssure FC and it is expected that the basis of calculation (standalone entity) would be unchanged by the implementation of the Scheme.
- 14.24 This would mean that the with-profits fund would be subject to two separate tax calculations in 2019: one for the LGAS WPF in LGAS and one for the LGWPF in ReAssure. I understand that this would not be expected to lead to a material change to the total tax charged to the fund but it may lead to an acceleration in cash tax payments. In order to ensure that there is no detriment to policyholders of the LGWPF, ReAssure has committed to put the LGWPF back in the same position as it would have been had there been only one tax calculation over 2019.
- 14.25 In addition, the Scheme may have an effect on certain “capital allowances” and “transitional adjustments” that currently apply to the LGAS WPF. Furthermore, the utilisation of any “Excess BLAGAB expenses” by LGAS in 2019 ahead of the Economic Effective Date may also impact the tax charged to the with-profits fund. Considering each of these in turn:
- Capital allowances: It is anticipated that the capital allowances would not transfer as part of the Scheme and, in order for the LGWPF to not lose the future benefit of these capital allowances, LGAS has committed to settle with the LGAS WPF the tax value of those capital allowances that do not transfer as part of the Scheme. It is expected that this would accelerate tax deductions and give rise to a cash tax benefit in the fund. Hence it is not considered that this, in isolation, would adversely affect the transferring policyholders.

- Transitional adjustments: Certain transitional adjustments will crystallise at the Economic Effective Date. It is expected that this would accelerate tax deductions and give rise to a cash tax benefit in the fund. Hence it is not considered that this, in isolation, would adversely affect the transferring policyholders.
- Excess BLAGAB expenses: LGAS may utilise excess BLAGAB expenses which arise from 1 January 2019 to the Economic Effective Date in respect of the LGAS WPF which will not transfer to ReAssure as part of the Scheme. LGAS has committed to settle with the LGAS WPF the tax value of any such utilised excess BLAGAB expenses which will give a cashflow and timing advantage to the LGWPF as the related benefit will be realised earlier than would otherwise be the case.

14.26 There is an outstanding technical issue on the operation of a specific provision that, in the worst case, would lead to a tax disadvantage for the with-profits fund. If such a disadvantage were to occur, LGAS will seek to collect any tax amounts from ReAssure rather than the LGWPF as permitted under the BTA. Both firms have provided written assurances that shareholders will make any payments necessary to ensure that there is no detrimental impact on the LGWPF.

### **Conclusion**

14.27 The LGAS tax report and opinions of LGAS Group Tax support the conclusion that the implementation of the Scheme will not affect the tax position of the policyholders of the transferring LGAS business.

### **THE REASSURE PPFMS**

14.28 There is a separate PPFM for each of the WLWPF, the NMWPF and the GAWPF. If the Scheme were to be implemented the only changes to these documents would be to the background information on each company and this will be picked up in the normal round of updates to the ReAssure PPFMs.

## 15. My conclusions

- 15.1 I confirm that I have considered the issues affecting the policyholders of LGAS and ReAssure separately, as set out in Sections 5 to 14 and that I do not consider further subdivisions (other than those in this report) to be necessary.
- 15.2 I am satisfied that the implementation of the Scheme would not have a material adverse effect on:
- The security of the benefits of the policies of LGAS and ReAssure;
  - The reasonable expectations of the policyholders of LGAS and ReAssure in respect of their benefits; or
  - The standards of administration, service, management and governance that apply to the LGAS and ReAssure policies.
- 15.3 I am satisfied that the Scheme is equitable to all classes and generations of LGAS and ReAssure policyholders.
- 15.4 As noted in Section 8 there are some areas of material concern regarding the migration plan that are being monitored closely by the ReAssure Board and the LGAS Board. The transfer will not be able to proceed until a decision is made by the ReAssure and LGAS Boards to seek an Order from the High Court to implement the Scheme and the High Court is satisfied that the implementation of the Scheme would not have a material adverse effect on policyholders.



Oliver Gillespie

3 July 2019

Partner of Milliman LLP

Fellow of the Institute and Faculty of Actuaries

## Appendix A – Selected financial information before the implementation of the scheme

### LGAS SOLVENCY II FINANCIAL INFORMATION AS AT 31 DECEMBER 2018

£ million	Non-Transferring	Transferring Non-Profit	Transferring Unit-Linked	LGAS WPF	RTA	Total
<b>Assets<sup>1</sup></b>	<b>96,601</b>	<b>0</b>	<b>10,461</b>	<b>18,393</b>	<b>18</b>	<b>125,473</b>
			<b>0</b>	<b>0</b>		
<b>BEL</b>	<b>86,250</b>	<b>2</b>	<b>10,055</b>	<b>17,753<sup>2</sup></b>	<b>640</b>	<b>114,701</b>
<b>Risk margin</b>	<b>3,984</b>	<b>0</b>	<b>4</b>	<b>76</b>	<b>(4)</b>	<b>4,060</b>
<b>TMTP<sup>3</sup></b>	<b>(3,771)</b>	<b>0</b>	<b>(16)</b>	<b>(76)</b>		<b>(3,863)</b>
			<b>0</b>	<b>0</b>		<b>0</b>
<b>Technical provisions</b>	<b>86,464</b>	<b>2</b>	<b>10,043</b>	<b>17,753<sup>4</sup></b>	<b>636</b>	<b>114,898</b>
<b>Own Funds</b>	<b>10,137</b>	<b>(2)</b>	<b>418</b>	<b>640</b>	<b>(618)</b>	<b>10,574</b>
<b>SCR</b>				<b>532</b>		<b>7,039</b>
<b>Excess Assets</b>				<b>107</b>		<b>3,535</b>
<b>Solvency coverage ratio</b>				<b>120%</b>		<b>150%</b>

Notes:

1. Assets are shown net of current liabilities and deferred tax.
2. The LGAS WPF BEL includes a reserve of £50 million in respect of migration costs.
3. The technical provisions are based on a recalculated TMTP value (rather than the TMTP approved by the LGAS Audit Committee pursuant to a recalculation request granted by the regulator). This recalculated TMTP allows for the implementation of the RTA and a number of recent changes to the management and modelling of the LGAS WPF business. The solvency coverage ratio excluding this recalculation would be 160%.
4. The technical provisions for the LGAS WPF are calculated based on the fixed expenses that will apply within ReAssure following the implementation of the Scheme.

## REASSURE SOLVENCY II FINANCIAL INFORMATION AS AT 31 DECEMBER 2018

£ million	WLWPF	NMWPF	GAWPF	RNPF	Total
<b>Assets<sup>1</sup></b>	<b>490</b>	<b>1,436</b>	<b>1,851</b>	<b>35,190</b>	<b>38,967</b>
<b>BEL</b>	<b>414</b>	<b>1,269</b>	<b>1,465</b>	<b>30,926</b>	<b>34,074</b>
<b>Risk margin</b>	<b>8</b>	<b>13</b>	<b>15</b>	<b>1,360</b>	<b>1,397</b>
<b>TMTP<sup>2</sup></b>	<b>0</b>	<b>0</b>	<b>(16)</b>	<b>(756)</b>	<b>(772)</b>
<b>Technical provisions</b>	<b>422</b>	<b>1,282</b>	<b>1,464</b>	<b>31,530</b>	<b>34,699</b>
<b>Unrestricted Own Funds</b>	<b>68</b>	<b>154</b>	<b>387</b>	<b>3,660</b>	<b>4,268</b>
<b>SCR</b>	<b>11</b>	<b>27</b>	<b>113</b>	<b>2,528</b>	<b>2,678</b>
<b>Restriction to Own Funds</b>					<b>367</b>
<b>Excess Assets<sup>3</sup></b>	<b>58</b>	<b>128</b>	<b>274</b>	<b>1,132</b>	<b>1,223</b>
<b>Solvency coverage ratio</b>	<b>648%</b>	<b>581%</b>	<b>342%</b>	<b>145%</b>	<b>146%</b>

Notes:

1. Assets are shown net of current liabilities and deferred tax.
2. The Value of the TMTP includes a recalculation of the TMTP as at 31 December 2018 allowing for the PRA approval of the ReAssure PIM
3. Under the RTA, the present value of shareholder transfers are treated as an asset of the RNPF with an associated SCR and capital management buffer.

## Appendix B – Selected financial information after the implementation of the scheme

### LGAS POST-SCHEME BALANCE SHEET AS AT 31 DECEMBER 2018

£ million	Non-Transferring
<b>Assets<sup>1</sup></b>	<b>96,554</b>
<b>BEL</b>	<b>86,269</b>
<b>Risk margin</b>	<b>3,984</b>
<b>TMTP<sup>2</sup></b>	<b>(3,771)</b>
<b>Technical provisions</b>	<b>86,482</b>
<b>Own Funds</b>	<b>10,071</b>
<b>SCR</b>	<b>6,558</b>
<b>Excess Assets<sup>3</sup></b>	<b>3,512</b>
<b>Solvency coverage ratio</b>	<b>154%</b>

Notes:

1. Assets are shown net of current liabilities and deferred tax.
2. The technical provisions are based on a recalculated TMTP value (rather than the TMTP approved by the LGAS Audit Committee pursuant to a recalculation request granted by the regulator) as this is believed to provide the most up-to-date and meaningful view of the Solvency II position. The post-Scheme solvency coverage ratio excluding this recalculation was 164%.
3. The reduction in excess assets relative to the pre-Scheme position reflects the loss of tax synergies between the transferring business and the remaining LGAS business, and LGAS's share of the costs of the transfer.

**REASSURE POST-SCHEME BALANCE SHEET AS AT 31 DECEMBER 2018**

£ million	WLWPF	NMWPF	GAWPF	LGWPF	RNPF	Total
<b>Assets<sup>1</sup></b>	<b>491</b>	<b>1,436</b>	<b>1,851</b>	<b>18,323</b>	<b>45,735</b>	<b>67,836</b>
<b>BEL</b>	<b>414</b>	<b>1,269</b>	<b>1,465</b>	<b>17,703<sup>2</sup></b>	<b>41,743<sup>3</sup></b>	<b>62,594</b>
<b>Risk margin</b>	<b>8</b>	<b>13</b>	<b>15</b>	<b>88</b>	<b>1,357</b>	<b>1,481</b>
<b>TMT<sup>4</sup></b>	<b>0</b>	<b>0</b>	<b>(16)</b>	<b>(171)</b>	<b>(648)</b>	<b>(836)</b>
<b>Technical provisions</b>	<b>422</b>	<b>1,282</b>	<b>1,464</b>	<b>17,620</b>	<b>42,452</b>	<b>63,240</b>
<b>Unrestricted Own Funds</b>	<b>68</b>	<b>154</b>	<b>386</b>	<b>703</b>	<b>3,283</b>	<b>4,594</b>
<b>SCR<sup>5</sup></b>	<b>11</b>	<b>27</b>	<b>113</b>	<b>464</b>	<b>2,453</b>	<b>3,067</b>
<b>Restriction to Own Funds</b>						<b>385</b>
<b>Excess Assets<sup>6</sup></b>	<b>57</b>	<b>127</b>	<b>273</b>	<b>239</b>	<b>830</b>	<b>1,143</b>
<b>Solvency coverage ratio</b>	<b>618%</b>	<b>570%</b>	<b>342%</b>	<b>152%</b>	<b>134%</b>	<b>137%</b>

Notes:

- Assets are shown net of current liabilities and deferred tax.

The post-scheme balance sheet allows for the net-of-tax transfer of £45 million from the LGWPF to the RNPF as a contribution towards the costs of migration.

- The reserve of £50 million in respect of migration costs is released from the LGWPF.
- Additional reserves of £59 million and £60 million are held in the RNPF for migration costs and the VAT on the investment management fees payable to LGIM respectively. The lapse basis for unit-linked pension business is also updated to reflect the ReAssure age-related structure, resulting in a small increase in the BEL of £9 million.
- The TMT has been recalculated to reflect the move to the ReAssure PIM and this recalculation has been approved by the PRA. ReAssure also intends to submit an application to recalculate the TMT to reflect the transferring business, which is subject to PRA approval. Based on the proposed methodology:
  - The TMT for the LGWPF has been recalculated using a proxy calculation to estimate the Solvency I Pillar 1 and Pillar 2 position. This involves using the Economic Capital model developed by ReAssure for the LGWPF rather than relying on figures provided by LGAS and including the WPICC in the determination of the Solvency I Pillar 1 capital requirement.



- The TMTP for the RNPF has been recalculated using the existing methodology for the RNPF.
- 5. The risk margin and SCR for the transferring LGAS business have been calculated using the Standard Formula for the purposes of deriving the pro-forma post-Scheme balance sheet for ReAssure. The risk margin and SCR for the existing business in the RNPF has been calculated using the ReAssure PIM, with no allowance for diversification between the existing RNPF business and the transferring LGAS business.
- 6. The LGWPF restriction to Own Funds is set such that the present value of shareholder transfers contributes to the excess assets with an associated SCR in the LGWPF.

## Appendix C – The Solvency II regulatory regime

### INTRODUCTION

- C.1 A new 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 aims to introduce solvency requirements that better reflect the risks that insurers and reinsurers actually face and to introduce consistency across the EEA.
- C.2 All but the smallest EEA insurance companies must comply with Solvency II and are required to adhere to a set of new, risk-based capital requirements and the results will be shared with the public.
- C.3 Solvency II is based on three pillars:
- Under Pillar 1, quantitative requirements define a market consistent<sup>4</sup> framework for valuing the company’s assets and liabilities, the results of which will be 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 policyholders. Firms will produce private reports to supervisors and a public solvency and financial condition report.

### THE PILLAR 1 REQUIREMENTS

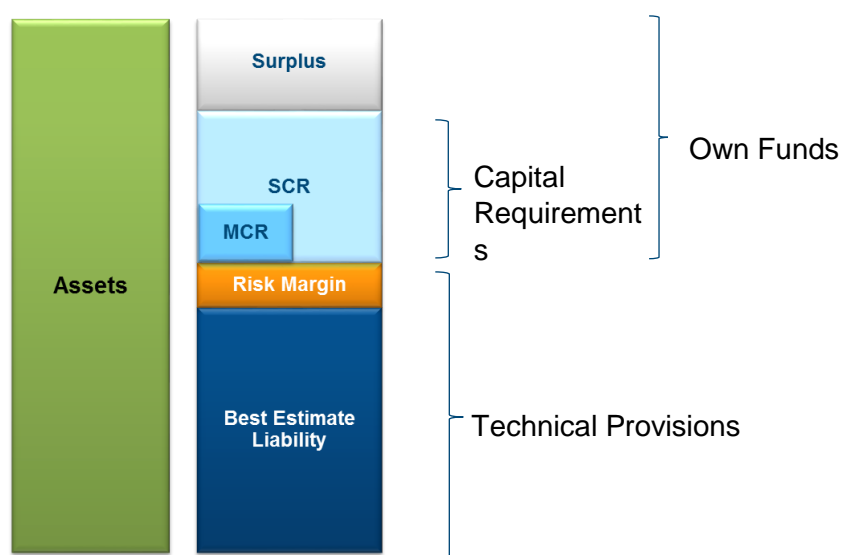
- C.4 Assets are, broadly speaking, reported at market value under Pillar 1.
- C.5 The determination of a market consistent value of liabilities under Solvency II requires the insurer to calculate the best estimate liabilities (“BEL”). The expected future obligations of the insurer are projected over the lifetime of the contracts using the most up-to-date financial information and the best estimate actuarial assumptions, and the BEL represents the present value of these projected cash-flows.
- C.6 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.
- C.7 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%.
- C.8 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.
- C.9 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
- C.10 EIOPA has published the implementing technical standards (“ITS”) and guidelines for the new regime and these have been endorsed by the European Commission, are legally binding and apply to all national regulators under the scope of Solvency II.
- C.11 Many of the technical requirements of Solvency II are contained in Commission Delegated regulation (EU) 2015/35, known as the Delegated Acts, adopted by the European Commission in October 2014.

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<sup>4</sup> A market-consistent framework requires the values placed on assets and liabilities to be consistent with the market prices of listed securities and traded derivative instruments.

## OWN FUNDS AND CAPITAL

- C.12 Under the Solvency II regime, the excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds. Own Funds can be thought of as the capital available in the company to cover capital requirements.
- C.13 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.
  - 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.
- C.14 Own Funds that are classified as Tier 2 or Tier 3 are of a lower quality, with less ability to fully absorb losses.
- C.15 The following diagram shows the structure of the balance sheet for a UK life insurance company under a Solvency II market consistent valuation.



## REGULATORY APPROVALS UNDER SOLVENCY II

- C.16 Any UK firms intending to use an internal model, transitional measures, a matching adjustment or a volatility adjustment (as described in the paragraphs below) must apply to the PRA for approval.
- C.17 At the end of 2018, 28 life insurers in the UK had applied and been approved for the volatility adjustment and 27 life insurers had been approved for the matching adjustment.
- C.18 Under the Solvency II regulations, the PRA has the right to remove approvals for the use of any of these measures if the firm is found to be in breach of the restrictions and conditions on which the original approval was based.
- C.19 Firms must apply to the PRA if they wish to make changes to the terms of their existing approvals. For example, firms would seek approval from the PRA to make a major change to their internal model and would not be expected to submit more than one major change application per year. A major change can comprise a single change or an accumulation of minor changes that, in aggregate, comprise a major change.
- C.20 Additionally, firms are permitted to seek approval to undertake a recalculation of their Transitional Measure on Technical Provisions (the "TMTP" as described below) every six months if their risk profile has changed materially since the previous recalculation.

## THE MATCHING ADJUSTMENT

- C.21 In calculating the BEL, the Solvency II regulations permit firms to apply to their regulator to make use of the "matching adjustment". The matching adjustment 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 (swap rates under Solvency II) 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.

- C.22 Firms using the matching adjustment 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

- C.23 Where insurers have liabilities that are not eligible for use of the matching adjustment, the Solvency II regulations permit firms to apply to their regulator to make use of the “volatility adjustment”. The volatility adjustment is an increase to the discount rate used in the calculation of the BEL (other than for liabilities that are subject to the matching adjustment) which aims to prevent forced sales of assets in the event of extreme bond spread movements.
- C.24 The volatility adjustment is based on the spreads on a representative portfolio of assets for each relevant currency and the risk-free discount curves which include the volatility adjustment are published by EIOPA.

### THE TRANSITIONAL MEASURES

- C.25 Insurers are also permitted to apply to their regulator (the PRA in the UK) to make use of transitional measures. Transitional measures allow firms to phase in the balance sheet impact of moving from the former Solvency I regulatory regime to the Solvency II regulatory regime. The transitional measures can be applied in one of two ways:
- The TMTP allows firms to phase in the increase in technical provisions under Solvency II Pillar 1 (in relation to business written prior to 1 January 2016) over a sixteen year period. In the UK, the increase is measured relative to the firm’s Solvency I Pillar II liabilities.
  - 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 regime over a sixteen year period.
- C.26 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 difference, to the extent that this difference is a positive number, between the firm’s technical provisions under Solvency II and the firm’s insurance liabilities under the previous Solvency I Pillar II regime.
- C.27 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 Pillar I and Pillar II regimes at the same valuation date.
- C.28 The FRR for a given solvency regime is calculated as the 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 the Solvency I regime (Pillar I and Pillar II) then the calculated TMTP must be reduced to a level that ensures that this is no longer the case. The purpose of the FRR test is to ensure that firms are not able to hold lower amounts of financial resources under Solvency II than under the Solvency I regime as a result of the use of the TMTP.
- C.29 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.
- C.30 The PRA has stated publicly<sup>5</sup> that it regards the financial benefit conferred by the TMTP as Tier 1 capital.
- C.31 The Solvency II Directive provides for firms’ TMTPs to be subject to recalculation every two years, with more frequent recalculations permitted if the firm’s risk profile has materially changed, as described above.

### RING-FENCED FUNDS

- C.32 Solvency II 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.

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<sup>5</sup> <http://www.bankofengland.co.uk/publications/Pages/speeches/2015/829.aspx>

- C.33 In the UK, many firms have set up ring-fenced funds in order to reflect the arrangements applicable to their with-profits funds (as defined under the previous regulatory regime) and the with-profits and non-profit business within the with-profits fund.

#### **THE LONG-TERM FUND AND SHAREHOLDERS' FUND IN THE UK**

- C.34 Prior to the implementation of Solvency II, proprietary firms in the UK writing long-term insurance business were required to identify the assets attributable to their long-term insurance business and keep those assets separate from shareholder funds in what was referred to as a long-term insurance fund (the "LTF"). The other assets of a proprietary company were typically allocated to the shareholders' fund (the "SHF"). Under the PRA rules, the assets in the LTF were only available to be used to support the firm's long-term insurance business and firms were required to maintain assets in the LTF sufficient in value to cover the fund's mathematical reserves.
- C.35 Following the implementation of Solvency II, the requirement to maintain a separate LTF has been removed and therefore a firm's "fund structure" now consists of the ring-fenced funds and the business outside of the ring-fenced funds. This business outside the ring-fenced funds is often called the "non-profit fund" (if it is all long-term business) or the "shareholder backed fund" (this could include short-term or general insurance business) but whatever the name it includes the assets and liabilities of what were, under the previous regime, called the non-profit fund (in the LTF) and the shareholders' fund (outside of the LTF).
- C.36 Although not required to do so for regulatory purposes, some firms continue to maintain a notional fund for accounting purposes in respect of long-term business outside of the ring-fenced funds. Such a notional fund is sometimes referred to as the non-profit fund.

## Appendix D – The regulation and governance of insurance companies in the UK

### THE REGULATORS IN THE UK

- D.1 Since 1 April 2013, responsibility for the regulation of insurance companies in the UK has been split between the PRA and the FCA.
- D.2 The PRA is a part of the Bank of England, and is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.
- D.3 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 UK insurers have resilience against failure (although this is not a 'zero failure' regime) and that disruption to the stability of the UK financial system from regulated UK insurers is minimised.
- D.4 The FCA regulates the conduct of all UK financial services firms in relation to consumer protection, market integrity and the promotion of competition in the interests of consumers. The FCA does not have conduct of business responsibility for the policies serviced under the EU's passporting regime as responsibility for the conduct of business of such policies lies with the host state supervisors.

### GOVERNANCE IN THE UK

- D.5 The Board of Directors of a proprietary long-term insurer 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.
- D.6 Under Solvency II, all insurers are required to establish the following key functions:
- Actuarial function: This function is required, inter alia, to coordinate the calculation of technical provisions, and to ensure the appropriateness of the methodologies, underlying models and assumptions used in the calculation of technical provisions.
  - Compliance function: This function is required, inter alia, to advise the insurer on compliance with the Solvency II regulations.
  - Internal audit function: This function is required, inter alia, to evaluate the adequacy and effectiveness of the insurer's internal control system and other elements of its system of governance. The internal audit function is required to be objective and independent from the company's operational functions.
  - Risk management function: This function is required, inter alia, to facilitate the implementation of the insurer's risk management system.
- D.7 These functions are not defined by the Solvency II regulations as being performed by an individual, however, in the UK, the PRA and FCA have introduced a governance regime for UK insurers called the Senior Managers and Certification Regime ("SM&CR") which became effective on 10 December 2018, and which defines a set of senior management functions ("SMF"), including:
- SMF 1 - Chief Executive Officer;
  - SMF 2 - Chief Financial Officer;
  - SMF 4 - Chief Risk Officer;
  - SMF 5 - Head of Internal Audit;
  - SMF 20 - Chief Actuary; and
  - SMF 20a – With-Profits Actuary.
- D.8 Under SMR, the persons having responsibility for the actuarial function, internal audit function and risk management under Solvency II are the Chief Actuary, Head of Internal Audit and Chief Risk Officer respectively, and the individuals responsible for these functions will be subject to PRA approval.
- D.9 Those firms with with-profits business must appoint an actuary (or actuaries) to perform the "with-profits actuary function" (the "WPA"). This individual's responsibilities include advising the firm's management on the key aspects

of the discretion to be exercised affecting those classes of the with-profits business of the firm in respect of which he has been appointed. .

- D.10 Under the SM&CR, SMFs will be subject to a 'Duty of Responsibility'. If a firm breaches a regulatory requirement, the regulator can take action directly against the SMF responsible for the area relevant to the breach if the regulator can show that the SMF holder had failed to take reasonable steps to prevent or stop the breach.
- D.11 Firms with with-profits business must appoint a With-Profits Committee ("WPC") (or a "with-profits advisory arrangement" if appropriate given the size, nature and complexity of the fund in question) in respect of the with-profits business. The WPC's role is to advise and provide recommendations to the firm's governing body on the management of the with-profits business, and to act as a means by which the interests of with-profits policyholders are appropriately considered within a firm's governance structures.



## Appendix E – Certificate of compliance

I understand that my duty in preparing my report is to help the High 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, and have complied with, the requirements applicable to experts set out in Part 35 of the Civil Procedure Rules, Practice Direction 35 and Guidance for the instruction of Experts in Civil Claims 2014. As required by rule 35.10(2) of Part 35 of the Civil Procedure Rules and by paragraph 3.2(9)(b) of Practice Direction 35, I hereby confirm that I have understood, and have complied with, my duty to the High 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.

## Appendix F – Glossary of terms

A glossary of abbreviations used throughout the report is given below

### A

<b>AIA</b>	Annuity Introducer Agreement
<b>ALCO</b>	The With-Profits Assets and Liabilities Committee within LGAS, which ensures that the Fund's assets and liabilities are appropriately managed
<b>APS</b>	Actuarial Profession Standards
<b>Ark Life</b>	Ark Life Assurance Company dac
<b>ASI</b>	Aberdeen Standard Investments
<b>Asset Share</b>	A measure of the value of a policy based on actual investment returns and expenses incurred by the fund

### B

<b>BEL</b>	Best Estimate Liabilities
<b>Brexit</b>	The departure of the United Kingdom from the European Union
<b>BTA</b>	Business Transfer Agreement

### C

<b>Capital Allowances</b>	Fixed asset expenditure that a firm can claim tax relief on by allowing it to be expensed against annual pre-tax income. Similar to a tax-deductible expense
<b>CEO</b>	Chief Executive Officer
<b>CRO</b>	Chief Risk Officer
<b>CWP</b>	Conventional With-Profits

### D

<b>DB</b>	Defined Benefit
<b>Directions Hearing</b>	An initial Court hearing at which the companies' plans for notifying policyholders are considered
<b>DISP</b>	The section of the FCA Handbook, Dispute Resolution: Complaints, that sets out the jurisdiction and scope of the FOS in the UK

### E

<b>Economic Effective Date</b>	The date the Scheme becomes effective as between LGAS and ReAssure, being the first day of the calendar month in which the Legal Effective Date occurs, expected to be 1 November 2019
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<b>Economic Transfer Date</b>	1 January 2018 - the date on which most of the economic interest and associated risks of the transferring business was transferred from LGAS to ReAssure
<b>EEA</b>	<b>The</b> European Economic Area
<b>EIOPA</b>	The European Insurance and Occupational Pensions Authority
<b>ELP</b>	English Limited Partnership
<b>EU</b>	The European Union
<b>Excess Assets</b>	Assets in a fund in excess of the amounts required to meet expected liabilities and any regulatory capital requirements for that fund
<b>Existing Policyholders</b>	Existing policyholders of ReAssure
<b>Expense Risk</b>	The risk of loss caused by the fact that the timing and/or the amount of expenses incurred differs from those expected
<b>F</b>	
<b>FCA</b>	Financial Conduct Authority
<b>Final Hearing</b>	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 High Court is asked to approve the Part VII transfer
<b>FMISAs</b>	The LGAS Flexible Mortgage Individual Savings Accounts
<b>FMP</b>	Flexible Mortgage Plan
<b>FOS</b>	Financial Ombudsman Service, an independent public body set up to resolve disputes between consumers and businesses
<b>FPC</b>	Fund Performance Committee, an LGAS committee which oversees the investment of policyholder assets and monitors investment performance
<b>FROC</b>	Fund Risk Oversight Committee, an LGAS committee which provides oversight of the management of the company's unit-linked funds for Workplace Savings products
<b>FRR</b>	Financial Resources Requirement. Equal to total liabilities plus capital requirements under a given solvency regime
<b>FSCS</b>	Financial Services Compensation Scheme. A scheme which provides compensation to holders of long-term insurance policies in the event of the insolvency of a UK or an EEA or other overseas insurer in respect of its UK customers
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>G</b>	
<b>GAL</b>	Guardian Assurance Limited
<b>GAWPF</b>	Guardian Assurance With-Profits Fund
<b>General Partner</b>	Legal & General Property Partners (Life Fund) Limited
<b>GI</b>	General Insurance
<b>GMP</b>	Guaranteed minimum pension
<b>Goldman Sachs</b>	The Goldman Sachs Group, Inc.

<b>Gone-aways</b>	Policies where the company does not have a valid address for the policyholder or pension scheme and subsequent reasonable attempts to trace the policyholder or scheme have been unsuccessful
<b>G Trustees</b>	G Trustees Limited
<b>Guernsey Scheme</b>	The Guernsey court-approved scheme process that, together with the Scheme, will effect the transfer of certain policies of LGAS issued to residents of the Bailiwick of Guernsey to ReAssure
<b>H</b>	
<b>Herbert Smith Freehills</b>	Herbert Smith Freehills LLP
<b>High Court</b>	The High Court of Justice of England and Wales
<b>HMRC</b>	HM Revenue & Customs
<b>I</b>	
<b>IFoA</b>	Institute and Faculty of Actuaries, the UK chartered professional body which is responsible for regulating actuaries
<b>IGC</b>	Independent Governance Committee, an independent LGAS committee which provides oversight of the LGAS workplace pension products
<b>IMA</b>	Investment Management Agreement
<b>In-payment annuities</b>	An annuity which is currently being paid to the policyholder
<b>Interim Period</b>	The period between the Economic Transfer Date and the Economic Effective Date
<b>IPO</b>	Initial Public Offering
<b>IRESS</b>	Means IRESS The Exchange, an online annuity quotation portal
<b>ISA</b>	Individual Savings Account
<b>ISA Fund Account</b>	A client account within ReAssure to monitor the aggregate balance of ISA funds
<b>J</b>	
<b>Jersey Scheme</b>	The Jersey court-approved scheme that, together with the Scheme, will effect the transfer of any business carried on by LGAS in or from within Jersey to ReAssure
<b>JLT</b>	Jardine Lloyd Thomson plc
<b>K</b>	
<b>KPMG</b>	KPMG LLP
<b>L</b>	
<b>L&amp;G Group</b>	Legal and General Group

<b>L&amp;G Re</b>	Legal and General Reinsurance
<b>Legal Effective Date</b>	The date the Scheme becomes operative (as specified in a transfer certificate signed by LGAS and ReAssure), expected to be 4 November 2019
<b>LGAS</b>	Legal and General Assurance Society Limited
<b>LGAS PIM</b>	LGAS's Partial Internal Model
<b>LGAS RA Statement</b>	A quantitative risk appetite statement established by the Board of LGAS for its solvency coverage ratio on a Solvency II basis
<b>LGAS Tax Report</b>	A report produced by LGAS Group Tax to identify any significant tax issues arising from the Scheme
<b>LGAS WPF</b>	The transferring with-profits fund within LGAS before the implementation of the Scheme
<b>LGAS WPF RA Statement</b>	A separate risk appetite statement established for the LGAS WPF.
<b>LGAS WPF Business</b>	All of the business within the LGAS WPF
<b>LGC</b>	Legal & General Capital
<b>LGI</b>	Legal & General Insurance
<b>LGIL</b>	Legal & General Insurance Limited
<b>LGIM</b>	Legal & General Investment Management
<b>LGR</b>	Legal & General Retirement
<b>LGRI</b>	LGR Institutional
<b>LGRR</b>	LGR Retail
<b>LGWPF</b>	The newly created with-profits fund within ReAssure after the implementation of the Scheme, the Legal & General With-Profits Fund
<b>Liquidity Risk</b>	The risk of being unable to meet financial obligations as they fall due, for example from not being able to sell sufficient assets in time to meet cash flow requirements or not having sufficient funds available to meet cash flow requirements
<b>Longevity Risk</b>	The risk of loss resulting from changes in mortality rates whereby a decrease in mortality rates (i.e. policyholders being expected to live longer) causes an increase in the value of insurance liabilities
<b>M</b>	
<b>MA</b>	Matching Adjustment. 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 (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 Best Estimate Liabilities
<b>Market Risk</b>	The risk of loss caused by market prices or volatilities of market prices differing from their expected values
<b>MCR</b>	Minimum Capital Requirement
<b>Milliman</b>	Milliman LLP
<b>MPI</b>	Mortgage Protection Insurance
<b>MS&amp;AD</b>	MS&AD Insurance Group

<b>MSA</b>	Management Services Agreement
<b>MVR</b>	Market Value Reduction
<b>N</b>	
<b>NM capital support facility</b>	A facility for the NMWPF, where the ReAssure shareholders would provide capital support to the fund if required
<b>NMWPF</b>	National Mutual With-Profits Fund
<b>Non-Transferring LGAS Policies</b>	The policies of LGAS which are not transferring as a result of the Scheme
<b>O</b>	
<b>Operational Risk</b>	The risk that actual losses incurred for inadequate or failed internal processes, people and systems, or from external events, differ from the expected losses
<b>ORSA</b>	Own Risk and Solvency Assessment. A requirement under SII whereby Insurers must regularly undertake a forward looking assessment of risks, solvency needs and adequacy of capital resources
<b>Own Funds</b>	The excess of assets over liabilities under Solvency II
<b>P</b>	
<b>Partial Internal Model</b>	A model which is used to calculate some components of the SCR that is bespoke to an individual company
<b>Part VII Letter</b>	A letter sent by ReAssure to the existing ReAssure policyholders to make them aware of the Scheme
<b>Persistency Risk</b>	The risks of losses caused by deviations of the actual rates of policy lapses from the expected rates
<b>PICCs</b>	Pricing, Investment and Capital Committees (within LGAS)
<b>PLL</b>	Phoenix Life Limited
<b>PLL Annuity Scheme</b>	The transfer of a block of non-profit annuity business from three of the ring-fenced funds of Phoenix Life Limited into the RNPF in 2016
<b>PMC</b>	Legal & General Assurance (Pensions Management) Limited
<b>PMS</b>	Legal & General (Portfolio Management Services) Limited
<b>PMS Nominees</b>	Legal & General (Portfolio Management Services) Nominees Limited
<b>PRA</b>	Prudential Regulation Authority
<b>PRA Statement of Policy</b>	"The Prudential Regulation Authority's approach to insurance business transfers", dated April 2015
<b>PPFM</b>	Principles and Practices of Financial Management. A public document outlining how a with-profits fund is managed
<b>PwC</b>	PricewaterhouseCoopers LLP
<b>R</b>	
<b>RAGL</b>	ReAssure Group Limited

<b>RCC</b>	LGAS Risk and Compliance Committee
<b>ReAssure</b>	ReAssure Limited
<b>ReAssure BIC</b>	ReAssure Board Investment Committee. A committee which recommends overall investment strategy, policy and asset allocation for the ReAssure Board
<b>ReAssure BRC</b>	ReAssure Board Risk Committee. A committee which ensures compliance with legal and regulatory requirements and oversees the development and implementation of the ReAssure Group entities' internal control environments
<b>ReAssure FC</b>	ReAssure Fairness Committee. A committee which oversees the fair treatment of ReAssure policyholders, and oversees and challenges the management of ReAssure's with-profits funds
<b>ReAssure FPWG</b>	ReAssure Fund Performance Working Group. A group which reviews policyholder fund performance and reports to the ReAssure PIC
<b>ReAssure GMRC</b>	ReAssure Group Management Risk Committee
<b>ReAssure IGC</b>	ReAssure Independent Governance Committee. An independent committee which reviews the value for money of ReAssure workplace personal pensions for policyholders
<b>ReAssure IPO RA Statement</b>	A new risk appetite statement agreed by the ReAssure Board that would apply in the future if the ReAssure IPO were to go ahead
<b>ReAssure PIC</b>	ReAssure Policyholder Investment Committee. A committee which oversees the investment of policyholder assets
<b>ReAssure PIM</b>	ReAssure's Partial Internal Model
<b>ReAssure RA Statement</b>	ReAssure's risk appetite statement
<b>ReAssure Stakeholder Pension Scheme</b>	A new registered Stakeholder Pension Scheme held by ReAssure
<b>ReAssure UPC</b>	ReAssure Unit-Pricing Committee. A committee which has responsibilities regarding the monitoring and management of box positions for ReAssure's unit-linked funds and oversight of discretion on the pricing of funds
<b>ReAssure WPMC</b>	ReAssure With-Profits Management Committee. A committee which provides executive oversight of the management of ReAssure's with-profits funds
<b>Reinsured liabilities</b>	The mortality and morbidity risks relating to the transferring unit-linked policies, which are reinsured to ReAssure under the RTA
<b>Relief at Source</b>	A way of giving tax relief on contributions a member makes to their pension scheme
<b>RGP</b>	ReAssure Group plc
<b>Risk Margin</b>	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
<b>RLL</b>	ReAssure Life Limited
<b>RLL Scheme</b>	The transfer of the business of ReAssure Life Limited to ReAssure in 2016
<b>RML</b>	ReAssure Midco Limited
<b>RNPF</b>	ReAssure Non-Profit Fund
<b>RNPF LT business</b>	The remaining long-term insurance business within the RNPF



<b>RTA</b>	Risk Transfer Agreement
<b>RUKSL</b>	ReAssure UK Services Limited
<b>S</b>	
<b>Sanctions Hearing</b>	A hearing of the High Court to approve the terms of the Scheme prior to the effective date of the Scheme
<b>Scheme</b>	The proposed Scheme and all proposals included in the Scheme, including any documents referred to in the Scheme relating to its proposed implementation and operation
<b>Scheme Report</b>	A report on the terms of the Scheme by an Independent Expert
<b>SCR</b>	Solvency Capital Requirement
<b>SCR Coverage Ratio</b>	Own Funds divided by SCR
<b>SHF</b>	Shareholders' fund
<b>SIPP</b>	Self-Invested Personal Pension
<b>SMF</b>	Senior Management Function
<b>SM&amp;CR</b>	Senior Manager and Certification Regime
<b>Solvency II</b>	Regulatory solvency framework for the European Economic Area insurance and reinsurance industry
<b>SRAM</b>	Swiss Re Asset Management
<b>SRE</b>	Swiss Re Europe S.A.
<b>SRZ</b>	Swiss Reinsurance Company Ltd
<b>Standard Formula</b>	EIOPA prescribed method of calculating SCR
<b>SUP</b>	Supervision Manual contained in the FCA Handbook
<b>SUP 18</b>	Chapter 18 of the Supervision Manual contained in the FCA Handbook
<b>Supplementary Report</b>	A further report produced prior to the Final Hearing to provide an update for the High Court on the Independent Expert's conclusions in the light of any significant events subsequent to the date of the finalisation of this report
<b>T</b>	
<b>TAS</b>	Technical Actuarial Standards
<b>TAS 200: Insurance</b>	The Technical Actuarial Standards applicable to Insurance transformations (such as the Scheme), issued by the Financial Reporting Council
<b>TATCF Committee</b>	Technical Actuarial Treating Customers Fairly Committee. A subcommittee of the TCF Management Committee
<b>TCF Management Committee</b>	Treating Customers Fairly Management Committee. A ReAssure committee which provides dedicated oversight of all conduct and customer fairness related matters in relation to both ReAssure and its chosen outsource providers
<b>TCFS Committee</b>	Treating Customers Fairly Service Committee. A subcommittee of the TCF Management Committee
<b>Technical Provisions</b>	Pillar 1 liabilities under Solvency II consisting of BEL and Risk Margin

<b>TIPs</b>	Corporate Trustee Investment Plans
<b>TMTP</b>	Transitional Measure on Technical Provisions. The TMTP is intended to phase in (over 16 years) any increase in reserves that must be held for business written prior to 2016 arising from the introduction of the Solvency II regime on 1 January 2016
<b>Transitional Adjustments</b>	Transitional measures (such as the TMTP) which are intended to phase in the impact of the introduction of the Solvency II regime. Firms must apply to the PRA to be permitted to apply transitional measures
<b>Transferring Non-Profit Business</b>	The Transferring Non-Profit Policies, together with the associated assets and liabilities which will be included in the proposed transfer to ReAssure
<b>TUPE</b>	Transfer of Undertakings (Protection of Employment) regulations
<b>U</b>	
<b>ULMC</b>	Unit-Linked Management Committee
<b>UTM</b>	Legal & General (Unit Trust Managers) Limited
<b>UWP</b>	Unitised With-Profits
<b>V</b>	
<b>VA</b>	Volatility Adjustment
<b>Volatility Adjustment</b>	An increase to the discount rate used in the calculation of the BEL (other than for liabilities that are subject to the Matching Adjustment) 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 Best Estimate Liabilities
<b>W</b>	
<b>Waiver</b>	Permission to be exempt from the regulatory requirements to notify certain groups of policyholders
<b>With-profits Advisory Arrangement</b>	An independent person or one or more non-executive directors appointed to provide independent judgement to the firm's governing body
<b>With-Profits Actuary function</b>	A function with responsibility for advising the firm's management on the discretion to be exercised in respect of the with-profits business of the firm
<b>Workplace Savings Business</b>	A range of workplace pension solutions that focus on UK auto-enrolment schemes, written through LGIM
<b>WPA</b>	With-Profits Actuary. The person or person fulfilling the With-Profits Actuary function
<b>WPC</b>	With-Profits Committee. A committee which provides oversight of the management of a with-profits fund
<b>WPICC</b>	With-Profits Insurance Capital Requirement
<b>WPMC</b>	With-Profits Management Committee. An internal LGAS committee which is responsible for the oversight of the management of the LGAS WPF
<b>WLWPF</b>	Windsor Life With-Profits Fund

## Appendix G – Data relied upon

In addition to discussions (both orally and electronically) with LGAS and ReAssure staff, I have relied upon the information shown in the table below in formulating my conclusions:

Document
The reports of the Chief Actuary and WPA of LGAS and ReAssure on the proposed transfer
LGAS and ReAssure financial information as at 31 December 2018
LGAS and ReAssure financial projections
LGAS and ReAssure RA Statements, incl. the post-IPO RA Statement for ReAssure
Background information on LGAS and ReAssure including group structure, existing business, financial management, governance arrangements and recent events
Information on the Funds Foundation Project
Transaction agreements: the RTA, the BTA, the IMA, the AIA
Scheme document
LGAS and ReAssure witness statements
Legal reviews of the effect of the Scheme on previous LGAS and ReAssure schemes
Communications strategy, and LGAS and ReAssure communications packs
LGAS tax report
ReAssure economic capital, financial management and governance proposals for the LGWPF and RNPF
PPFM for the LGWPF
LGAS comparison of the LGAS and ReAssure risk management and governance frameworks
LGAS comparison of the LGAS and ReAssure economic capital calculations for the LGWPF
LGAS analysis of the economic benefit of the fixed expense agreement for the LGWPF
Log of product changes
Business readiness updates, including internal risk review results for ReAssure
Information on the targeting operating model for FMISAs, SIPPs, Stakeholder Pensions and vesting annuities within the LGWPF



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### CONTACT

Oliver Gillespie

[oliver.gillespie@milliman.com](mailto:oliver.gillespie@milliman.com)