

MILLIMAN REPORT

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

The supplementary report of the Independent Expert

February 2020

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# 1. Executive summary

## BACKGROUND

- 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 The transferring business consists of 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.
- 1.3 I have been appointed by ReAssure and LGAS to report, pursuant to Section 109 of the Financial Services and Markets Act 2000 (“**FSMA**”), in the capacity of the Independent Expert, on the terms of this proposed scheme (the “**Scheme**”) providing for this transfer from LGAS to ReAssure.
- 1.4 I prepared a report dated 3 July 2019 (“**my Main Report**”) in which I considered the proposed Scheme for the Directions Hearing at the High Court of Justice (the “**High Court**”) on 11 July 2019. I also prepared an addendum to my Main Report (“**the addendum**”) following the news that the Initial Public Offering (“**IPO**”) of shares in ReAssure Group Plc (“**RGP**”) (ReAssure’s parent company) had been suspended.
- 1.5 At the time of finalisation of my Main Report, it was proposed that the transferring business would legally transfer from LGAS to ReAssure on 4 November 2019 and that the Scheme would become effective as between LGAS and ReAssure on 1 November 2019. Since that time, however, the proposed **Legal Effective Date** has been changed to 6 April 2020 and the **Economic Effective Date** to 1 April 2020. Accordingly, the Sanction Hearing has also been postponed from 17 October 2019 to 9 March 2020.
- 1.6 The purpose of this report (the “**Supplementary Report**”) is to provide an updated assessment of the likely effects of the proposed Scheme ahead of the Sanction Hearing on 9 March 2020.

## MY ROLE AS INDEPENDENT EXPERT

- 1.7 My appointment as Independent Expert 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 (the “**L&G Group**”). My terms of reference have been reviewed by the FCA and the PRA.
- 1.8 My role as Independent Expert is set out in Section 4 of my Main Report and this Supplementary Report has been produced for the High Court to assist in its deliberations in respect of the Scheme.
- 1.9 The Supplementary 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**”).
- 1.10 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.
- 1.11 As Hoffmann J in Re London Life Association Limited (21 February 1989) observed, it is not for the High Court to suggest amendments or improvements to the Scheme but rather to decide whether to confirm or reject the scheme placed before it. In keeping with this, I am not required to consider possible alternative schemes and I have therefore only considered the terms of the Scheme presented to me.

## THE AREAS COVERED IN THIS SUPPLEMENTARY REPORT

1.12 The updated assessment that is the purpose of this Supplementary Report includes consideration of whether the conclusions reached in my Main Report remain valid in light of developments subsequent to the date of finalisation of my Main Report (3 July 2019), and any policyholder feedback or queries in relation to the proposed Scheme.

1.13 The developments and events covered are as follows:

- **The updated financial information for LGAS and ReAssure as at 30 June 2019 (Section 2)**

The conclusions in my Main Report were based on the financial information provided by ReAssure and LGAS as at 31 December 2018. There has been a change to the financial information as at this date and I have reconsidered the conclusions of My Main Report in light of these revisions.

The financial information for LGAS and ReAssure has been updated to that as at 30 June 2019 and I have reconsidered the conclusions in my Main Report given this updated financial information.

- **The updated financial information for LGAS and ReAssure as at 31 December 2019 (Section 3)**

I have reviewed unaudited pre-Scheme and estimated post-Scheme financial information as at 31 December 2019 and reconsidered the conclusions in my Main Report given this updated financial information.

- **An update on the operational readiness of ReAssure to service the transferring business (Section 4)**

In my Main Report, I highlighted that there remained some areas of material concern regarding the migration plan and that these were being monitored closely by the ReAssure Board and the LGAS Board. I have reconsidered the operational readiness of ReAssure as at the current date and provided an update to my conclusions.

- **The proposed purchase of RGP by Phoenix (Section 5)**

On 6 December 2019, Phoenix Group Holdings plc (“**Phoenix**”) announced its intention to purchase RGP. I have reconsidered the conclusions of my Main Report in light of this proposed acquisition.

- **The purchase of the Old Mutual Wealth Life Assurance Limited business by RGP (Section 6)**

On 5 August 2019, RGP announced that it intended to purchase the heritage life and pensions division, Old Mutual Wealth Life Assurance Limited, from Quilter Plc and the change in control application was approved by the PRA on 10 December 2019. I have reconsidered the conclusions of my Main Report in light of this acquisition.

- **The potential impact of the recent judgment in respect of the Prudential Rothesay scheme (Section 7)**

In August 2019 the High Court declined to sanction an insurance business transfer scheme to move a block of in-payment annuities from The Prudential Assurance Company Limited (“**Prudential**”) to Rothesay Life Plc (“**Rothesay**”). In this section, I provide comment on the concerns raised by the judge in the Prudential Rothesay scheme and how they might relate to the proposed LGAS ReAssure Scheme.

- **Policyholder objections and feedback on the proposed Scheme (Section 8)**

Following the Directions Hearing on 11 July 2019 and the subsequent initiation of the policyholder communications proposals in accordance with the directions order issued by the High Court, LGAS and ReAssure have received comments on the Scheme from policyholders and I have considered the main themes arising from this correspondence.

- **Other considerations in respect of the proposed Scheme (Section 9)**

There were a number of places in my Main Report where I indicated that I would provide further comment in my Supplementary Report. Where not covered in Sections 2 to 8 these areas are covered in this section.

- 1.14 This Supplementary Report should be read in conjunction with my Main Report. The reliances and limitations set out in Section 1 of my Main Report apply equally to this Supplementary Report. Defined terms used in my Main Report have the same meaning in this Supplementary Report.
- 1.15 Given the inherent uncertainty of the outcome of future events, it is not possible to be certain of the effect of the proposed Scheme on the affected policies and, in order to acknowledge this inherent uncertainty, the conclusions of the Independent Expert in relation to transfers of long-term insurance business are usually framed using a materiality threshold. The framework in which I undertake my consideration of the proposed Scheme in both this report and my Main Report is set out in Section 4 of my Main Report.

#### **THE CONCLUSIONS OF THIS SUPPLEMENTARY REPORT**

- 1.16 In summary:
- Based on the financial information for LGAS and ReAssure as at 30 June 2019, I remain satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the transferring LGAS policies, the existing ReAssure policies or the non-transferring LGAS policies.
  - I am satisfied that the unaudited pre-Scheme and estimated post-Scheme financial information as at 31 December 2019 does not provide any reason to change the conclusions of my Main Report.
  - Considering the updates on the data migration from ReAssure to date and the expert review conclusions from KPMG in the First KPMG Report and the Second KPMG Report, I am satisfied that it is unlikely that the migration will lead to a material adverse effect on policyholders going forward.
  - I have considered the potential impact of the proposed purchase of RGP by Phoenix on my conclusions on the effects of the proposed Scheme on the various groups of policies and I am satisfied that the Phoenix purchase of RGP would not provide any reason to change the conclusions in my Main Report.
  - I am satisfied that the OMWLA transaction does not provide any reason to change the conclusions in my Main Report.
  - I have considered the key features that Snowden J identified as weighing against the sanctioning of the Prudential Rothesay scheme and while some of these are relevant to the LGAS ReAssure Scheme, in my view none applies to the LGAS ReAssure Scheme to the same extent as to the Prudential Rothesay scheme and I am satisfied that the conclusions of my Main Report are unaffected by the judgment in the Prudential Rothesay scheme.
  - I am satisfied that LGAS and ReAssure are dealing with the objections received in a reasonable way and are doing what they can to resolve these fully prior to the Sanction Hearing and the policyholder enquiries received do not raise any issues that were not considered in the work leading up to my Main Report and therefore I am satisfied that there are no reasons to change the conclusions in my Main Report.
- 1.17 Therefore I am satisfied that nothing has happened since the finalisation of my Main Report to provide any reason to change the conclusions in Section 15 of my Main Report.
- 1.18 I shall provide a letter to the High Court dated 6 March 2020 that will provide an update on the state of the migration at that date and the effect of this on the conclusions above.

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

- 1.19 This Supplementary 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.
- 1.20 In my opinion, my Supplementary 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 C have been

prepared or reviewed by individuals who were subject to professional standards in undertaking their work, including, where appropriate, TAS requirements.

- 1.21 In the context of the TAS, my Main Report and this Supplementary Report are component reports, which together form an aggregate report.
- 1.22 Actuarial Profession Standard (“**APS**”) X2, as issued by the Institute and Faculty of Actuaries, requires members to consider whether their work requires an independent peer review.
- 1.23 In my view, this Supplementary 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.

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

- 1.24 As mentioned in my Main Report, there are proposed schemes in:
- Jersey (the “**Jersey Scheme**”) for the transfer of any relevant business carried on by LGAS in or from within Jersey; and
  - Guernsey (the “**Guernsey Scheme**”) for the transfer of any relevant policies issued to residents of the Bailiwick of Guernsey.
- 1.25 I confirm that the comments and conclusions in this Supplementary Report apply equally to all transferring policyholders of LGAS, 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. For the avoidance of doubt, this includes policies transferring pursuant to the Jersey Scheme and Guernsey Scheme. References to the Scheme should be taken to include the Jersey Scheme and Guernsey Scheme.

## 2. The effects of the proposed Scheme given the updated financial information for LGAS and ReAssure as at 30 June 2019

### INTRODUCTION

- 2.1 The conclusions in my Main Report in respect of the security of the benefits of the affected policies were based on the financial information provided by LGAS and ReAssure as at 31 December 2018. Updated financial information as at 30 June 2019 is now available and I have considered whether this updated information would affect the conclusions in my Main Report.
- 2.2 Since the finalisation of my Main Report, there have been no changes to:
- The LGAS Risk Appetite Statement (the “**LGAS RA Statement**”) and LGAS continues to adhere to the LGAS RA Statement.
  - The ReAssure Risk Appetite Statement (the “**ReAssure RA Statement**”).
  - The risk appetite statement to which ReAssure would adhere if the ReAssure IPO were to proceed (the “**ReAssure IPO RA Statement**”).
- 2.3 However, although the ReAssure IPO did not proceed, following a Board decision on 3 December 2019, ReAssure has adopted the ReAssure IPO RA Statement which, as set out in Section 12 of my Main Report, is stronger than the ReAssure RA Statement.
- 2.4 The Solvency II balance sheets as at 30 June 2019 for both LGAS and ReAssure are shown in Appendix A. The pro-forma balance sheets (assuming the Scheme had been implemented on 30 June 2019) for both LGAS and ReAssure are shown in Appendix B.
- 2.5 In summary the transferring business of LGAS consists of approximately 1.0 million policies and assets of approximately £30 billion (as at 30 June 2019).

### THE SECURITY OF BENEFITS

#### Introduction

- 2.6 As set out in Section 8 of my Main Report, a group of policies derives its security of benefits from:
- The strength of the calculation used to set the level of assets held to cover the technical provisions and Solvency Capital Requirement (“**SCR**”) of the business as required under the Solvency II regulations;
  - The additional financial strength required by the firm’s risk appetite statement including the strength of the governance around the risk appetite statement and the governance around any future changes to it; and
  - Any additional support from outside the firm, including support from the parent and/or group.
- 2.7 The security of benefits arises primarily from the insurance company itself and its financial strength and ability to withstand severe and extreme events.
- 2.8 The availability of support from the group companies or from a parent company provides potential extra financial strength and security for the policy benefits in the event that the faith placed in the financial strength of the firm proves to be misplaced.
- 2.9 The regulators and enforcers of the laws and regulations have an important role to play in dictating how the rules and regulations are applied and in setting the likely sanctions for their breach.

#### The financial strength of the firm based on current financial information

- 2.10 The SCR is the capital that a firm is required to hold under the Solvency II regime and is set based on the risk exposures of that firm. It is an estimate of the capital required to ensure that the firm can remain solvent in all but



the most extreme scenarios<sup>1</sup> over a one-year time horizon.<sup>2</sup> The solvency coverage ratio is then the amount of 'coverage' that the firm has of its SCR and is calculated as the firm's excess capital (Own Funds in the Solvency II balance sheet) divided by its SCR.

2.11 As stated above, the security of the benefits arises primarily from the financial strength of the firm itself and its ability to withstand severe and extreme events and the solvency coverage ratio is often used as a proxy for the financial strength of a firm. As set out in the first two bullets above one must consider the solvency coverage ratio alongside the risk appetite statements and capital management policies of a firm.

2.12 In considering the likely effects of the proposed Scheme on the security of benefits under the affected policies I have considered the financial strength of LGAS and ReAssure before and after the implementation of the Scheme. This was covered in my Main Report in Sections 8, 10 and 11 based on financial information as at 31 December 2018 and is covered below based on updated financial information as at 30 June 2019.

### **The financial strength of the firm in the future**

2.13 Clearly it is not possible to know what may happen to the firm in the future as there may be any combination of events such as: acquisitions, disposals, reinsurance arrangements, new strategic initiatives, or changes to the economy or political environment.

2.14 Although the SCR and solvency coverage ratio provide part of the picture in respect of the financial strength of a firm they do not provide the full picture and, as set out in my Main Report, there are other pieces of information that I, as Independent Expert, have taken into account when considering the likely effects of the proposed Scheme on the security of the benefits under the policies affected by the proposed Scheme.

2.15 The main such pieces of information are:

- **The firms' projections of solvency if the Scheme were to be implemented.**

These projections of solvency take into account the likely effects of the Scheme and consider a range of stressed scenarios.

- **The risk appetite statements and capital management policies that would apply to the affected policies if the Scheme were to be implemented.**

This includes consideration of the levels of capital required, the procedures required for changes to the capital management policies and risk appetite statements, and the management actions required in various scenarios.

- **The strength and quality of the governance and oversight that would apply to the affected policies if the Scheme were to be implemented.**

This includes the review and challenge by the Risk function and the Internal Audit function and consideration of the various Board committees. Of particular relevance for this Scheme is the oversight from the relevant with-profits committees ("WPCs") or fairness committees and the with-profits actuaries ("WPAs").

- **The level of support that would potentially be available from outside of the firm if the Scheme were to be implemented.**

This could be from a parent and/or group company and consideration must be given to how this support could change in the future.

- **The level of external review to which the firm's financial strength would be subject.**

This includes scrutiny by the external auditors and supervision by the regulators.

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<sup>1</sup> Under Solvency II an extreme scenario is one with a likelihood of occurring of no more than 0.5%.

<sup>2</sup> Under Solvency II a full cash flow projection is undertaken and thus the expected experience over many years is taken account of in the BEL, the risk margin and the SCR.

2.16 The same approach was followed in my Main Report.

### Summary

2.17 In summary, when considering the likely effects of the proposed Scheme on the security of the benefits under the affected policies the primary consideration should be the security provided by the financial strength of the firm itself currently and in the future and in analysing this I have considered a range of qualitative and quantitative factors as described in my Main Report.

2.18 One should also consider the risk appetite statements and governance in place and the potential further support available from the parent or group companies.

2.19 I provide an update of this analysis below starting with the current and projected solvency positions of LGAS and ReAssure based on the financial information as at 30 June 2019, and followed by consideration of the effects of the Scheme on the other points listed above.

### THE CHANGE TO THE FINANCIAL INFORMATION AS AT 31 DECEMBER 2018 AS SHOWN IN MY MAIN REPORT

2.20 Since the publication of my Main Report, ReAssure has provided me with a revised pro-forma post-Scheme Solvency II balance sheet as at 31 December 2018 which has some differences to the Solvency II balance sheet as at 31 December 2018 that was shown in Appendix B of my Main Report.

2.21 As a result of a refinement to the calculation of the Transitional Measure on Technical Provisions<sup>3</sup> (“**TMTP**”), although there was no material change to the overall level of the TMTP, the TMTP allocation between the new LG With-Profits Fund (the “**LGWPF**”) and the ReAssure Non-Profit Fund (the “**RNPF**”) was changed which led to the following changes to the ReAssure Solvency II pro-forma balance sheet as at 31 December 2018:

- A reduction to the LGWPF’s pro-forma post-Scheme solvency coverage ratio from 152% quoted in my Main Report to 134%;
- An increase to the RNPF’s pro-forma post-Scheme solvency coverage ratio from 134% quoted in my Main Report to 137%; and
- An increase to ReAssure’s pro-forma post-Scheme solvency coverage ratio from 137% quoted in my Main Report to 138%.

2.22 In respect of these changes to the financial information as at 31 December 2018 shown in my Main Report I note that:

- The reduced solvency coverage ratio of 134% for the LGWPF remains:
  - Comfortably in excess of the pre-Scheme solvency coverage ratio of the LGAS WPF of 120%; and
  - Comfortably above the level required by the ReAssure IPO RA Statement (the current risk appetite to which ReAssure is being managed as stated above).
- The increased solvency ratios of the RNPF and of ReAssure continue to indicate that the RNPF and ReAssure are of considerable financial strength and therefore provide material security of benefits to the transferring LGAS policies and the existing ReAssure policies.

2.23 Therefore, I am satisfied that the revised financial information as at 31 December 2018 does not provide any reason to change the conclusions of my Main Report.

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<sup>3</sup> The TMTP is described in more detail in Section 4 of my main report.

## THE SOLVENCY POSITIONS OF LGAS AND REASSURE BASED ON THE FINANCIAL INFORMATION AS AT 30 JUNE 2019

### The solvency position of LGAS as at 30 June 2019

- 2.24 The financial position of LGAS has been updated to show the position as at 30 June 2019.
- 2.25 In my Main Report, the financial information for LGAS was based on a recalculated TMTP in the pre-transfer and post-transfer positions as this was believed to provide the most realistic and meaningful view of the Solvency II position. The same approach has been used to derive the solvency position as at 30 June 2019.
- 2.26 The updated financial information as at 30 June 2019 shows that, prior to the implementation of the Scheme, LGAS had:
- Own Funds of £10.7 billion;
  - An SCR of £7.4 billion;
  - Excess capital above the SCR of £3.3 billion; and
  - A solvency coverage ratio of 144%.
- 2.27 As at 30 June 2019 LGAS's solvency coverage ratio was above that required by the LGAS RA Statement.

### The solvency position of ReAssure as at 30 June 2019

- 2.28 The financial position of ReAssure has been updated to show the position as at 30 June 2019.
- 2.29 As described in Section 6 of my Main Report, the financial information for ReAssure (as at 31 December 2018) included a TMTP, which had been recalculated to allow for:
- The effects of the Risk Transfer Agreement ("**RTA**"), which transferred most of the economic interest and associated risks of the transferring business from LGAS to ReAssure from 1 January 2018; and
  - The PRA approval of the ReAssure Partial Internal Model (the "**ReAssure PIM**").
- 2.30 At the time of finalisation of my Main Report, the PRA had granted its approval for ReAssure to make this recalculation of its TMTP and the recalculation had been approved by the ReAssure Audit and Risk Committee.
- 2.31 The pre-transfer financial position for ReAssure as at 30 June 2019 is shown in Appendix A of this report and includes the recalculated TMTP with allowance made for run-off over 6 months.
- 2.32 The updated financial information as at 30 June 2019 shows that, prior to the implementation of the Scheme, ReAssure had:
- Own Funds of £4.3 billion;
  - An SCR of £2.9 billion;
  - Excess capital above the SCR of £1.4 billion; and
  - A solvency coverage ratio of 151%.
- 2.33 As at 30 June 2019 ReAssure's solvency coverage ratio was above that required by the ReAssure RA Statement and the ReAssure IPO RA Statement which, as stated above, is the risk appetite statement currently being used by ReAssure.

### The Post-Scheme solvency position of LGAS as at 30 June 2019

- 2.34 The pro-forma financial position of LGAS has been calculated using the financial information as at 30 June 2019 and shows that, if the Scheme had been implemented on this date, LGAS would have had:

- Own Funds of £10.1 billion;
- An SCR of £7.0 billion;
- Excess capital above the SCR of £3.2 billion; and
- A solvency coverage ratio of 145%.

2.35 As at 30 June 2019, if the Scheme had been implemented, LGAS's solvency coverage ratio would have been above that required by the LGAS RA Statement.

#### **The post-Scheme solvency position of ReAssure as at 30 June 2019**

2.36 The pro-forma financial position of ReAssure has also been updated to reflect the financial information as at 30 June 2019.

2.37 In my Main Report, the financial information for ReAssure was based on a recalculated TMTP in the pre-transfer and post-transfer positions as this was believed to provide the most realistic and meaningful view of the Solvency II position. This meant that, in the post-transfer pro-forma financial information for ReAssure, the TMTP was recalculated to allow for the LGAS business that would be transferred in if the Scheme were to be implemented.

2.38 The pro-forma post-transfer financial position for ReAssure shown in this Supplementary Report as at 30 June 2019 (as shown in Appendix B) also includes the recalculated TMTP (assuming the transfer had taken place on 31 December 2018 and with allowance made for run-off over 6 months). ReAssure has applied for approval to use a recalculated TMTP to allow for the transferring business as at the Legal Effective Date but, at the time of writing, this PRA approval has not been received and ReAssure is in the process of updating this application such that the TMTP is calculated as at the revised Economic Effective Date.

2.39 The updated pro-forma position using the financial position as at 30 June 2019 shows that, if the Scheme had been implemented on this date ReAssure would have had:

- Own Funds of £4.8 billion;
- An SCR of £3.3 billion;
- Excess capital above the SCR of £1.5 billion; and
- A solvency coverage ratio of 145%.

2.40 As at 30 June 2019, if the Scheme had been implemented, ReAssure's solvency coverage ratio would have been above that required by the ReAssure RA Statement and the ReAssure IPO RA Statement which, as stated above, is the risk appetite statement currently being used by ReAssure.

#### **THE SECURITY OF BENEFITS CONSIDERING THE FINANCIAL INFORMATION AS AT 30 JUNE 2019**

2.41 Since my Main Report was finalised and considering the financial information as at 30 June 2019 as set out above:

- The Solvency II regime remains in place and there have been no material changes to the Solvency II regulations.
- There has been no change to the strength of the calculation used to set the level of assets held by either company to cover the technical provisions and SCR.
- There have been no changes to the LGAS RA Statement and LGAS is still adhering to it.
- Following a Board decision on 5 December 2019, ReAssure has adopted the ReAssure IPO RA Statement which, as set out in Section 12 of my Main Report, is stronger than the ReAssure RA Statement.
- Both LGAS and ReAssure have solvency levels that comfortably meet their respective risk appetite statements.

2.42 Based on the financial information as at 30 June 2019 as set out above, if the proposed Scheme were to be implemented:

- **The transferring LGAS business** would be transferred from LGAS with a solvency coverage ratio of 144% to ReAssure with a solvency coverage ratio of 145%.

This compares favourably with the position based on the financial information as at 31 December 2018 as shown in my Main Report in Section 8 where the LGAS solvency coverage ratio would have been 150% and the ReAssure post-Scheme solvency coverage ratio would have been 138%.

- **The existing ReAssure business** would have experienced a reduction in the solvency coverage of ReAssure from 151% to 145%.

This is a similar decrease as was observed in Section 10 of my Main Report where, based on the financial information as at 31 December 2018, the decrease was from 146% to 138%.

- **The non-transferring LGAS business** would have experienced an increase in the solvency coverage of LGAS from 144% to 145%.

This is a small increase and a similarly small (albeit larger) increase was observed in Section 11 of my Main Report where, based on the financial information as at 31 December 2018, the increase was from 150% to 154%.

2.43 I am satisfied that the updated financial information as at 30 June 2019 does not provide any reason to change the conclusions in my Main Report.

2.44 In Section 3 of this report I have considered estimates of both the LGAS and ReAssure pre-transfer and post-transfer solvency positions as at 31 December 2019.

#### **THE PROJECTIONS OF SOLVENCY CARRIED OUT BY LGAS AND REASSURE**

2.45 As part of the ongoing management of their business both LGAS and ReAssure carry out projections of their solvency on a best estimate or base scenario and over a range of stressed and adverse scenarios. Such projections are typically carried out over a number of years into the future – say five or ten years. Clearly, the further into the future that a projected amount is, the less certainty there is around that number, but nevertheless the projections provide useful insight into the future financial strength of the firms that can be used by the Independent Expert, the WPA and the Chief Actuary to analyse the likely effects of the proposed Scheme on the security of policyholder benefits now and into the future.

2.46 A set of 10-year projections of the solvency of ReAssure assuming the proposed Scheme were to be implemented at the end of 2019 has been provided. These projections, which also allow for the purchase of the OMWLA business (as described in Section 6), show that ReAssure is expected to comfortably exceed its Solvency II SCR and the extra requirements of the ReAssure RA Statement over this 10-year period.

2.47 I am satisfied that the latest projections do not provide any reason to change the conclusions in my Main Report.

#### **THE RISK APPETITE STATEMENTS AND GOVERNANCE THAT WOULD APPLY TO THE AFFECTED POLICIES.**

2.48 In Section 8 of my Main Report I stated that I was satisfied that if the Scheme were to be implemented the change for the LGAS transferring policies to be subject to the ReAssure RA Statement would not have a material adverse effect on the security of the benefits.

2.49 In Sections 8, 10, and 11 of my Main Report I stated that I was satisfied that the implementation of the proposed Scheme would not have a material adverse effect on the standards of administration, service, management and governance that apply to the transferring LGAS policies, the existing ReAssure policies and the non-transferring LGAS policies.

2.50 On 6 December 2019, Phoenix announced its intention to purchase RGP and, in Section 5 of this report, I have considered the likely effects of this on the conclusions in my Main Report. This includes an assessment of the likely effects of the proposed transaction on the risk appetite statements and governance that would apply to the affected policies.

#### **THE SUPPORT FROM THE PARENT AND/OR GROUP COMPANIES FOR LGAS AND REASSURE**

2.51 The availability of support from the group companies or from a parent company provides potential extra financial strength and security for the policies of the subsidiary in the event that the faith placed in the financial strength of the firm proves to be misplaced.

2.52 The group structures for LGAS and ReAssure are shown in Sections 5 and 6 of my Main Report, respectively and show that:

- LGAS is part of the L&G Group and ultimately supported by L&G Group Plc; and
- ReAssure is part of the Swiss Re Group and ultimately supported by Swiss Re Ltd and MS&AD Insurance Group ("**MS&AD**") with holdings of 75% and 25% respectively.

2.53 As stated above, on 6 December 2019, Phoenix announced its intention to purchase RGP and the transaction is subject to, amongst other things, the approval of the existing Phoenix shareholders, the PRA (through a change in control process) and the Competition and Markets Authority. Completion of Phoenix's purchase of RGP is currently expected early in the second half of 2020.

2.54 If the Phoenix transaction were to proceed then there would be implications for the parental/group support that could be provided to ReAssure and the effects of these implications on the conclusions in my Main Report are covered in Section 5 of this report.

2.55 If the necessary approvals for the Phoenix purchase of RGP were not to be granted then Swiss Re Group and MS&AD would remain the owners of RGP as currently.

2.56 Since the finalisation of my Main Report there have been no material changes to the group structures of the L&G Group or the Swiss Re Group and, as set out in Section 8 of my Main Report, both the L&G Group and the Swiss Re Group remain strong and committed to providing support to their subsidiaries.

2.57 As set out in Section 8 of my Main Report, the Swiss Re Group and MS&AD are well capitalised:

- 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.

2.58 Since the finalisation of my Main Report there has been no change to the availability of support to ReAssure and its policyholders from the Swiss Re Group and MS&AD and therefore the conclusions reached in in Section 8 of my Main Report, that the size and level of capitalisation of the Swiss Re Group and MS&AD provide material security for ReAssure and its policyholders, remain unchanged.

2.59 I am therefore satisfied that, if the Scheme were to be implemented and the Phoenix purchase of RGP were not to proceed, the change for the transferring policies to having parental support provided by the Swiss Re Group and MS&AD rather than the L&G Group would not lead to a material adverse effect on the security of the benefits guaranteed under those policies.

## THE LEVEL OF EXTERNAL REVIEW TO WHICH THE AFFECTED POLICIES WOULD BE SUBJECT

- 2.60 At the time of writing, LGAS and ReAssure are currently subject to external audit (by KPMG LLP (“KPMG”)<sup>4</sup> and PwC LLP respectively) and to regulatory supervision by the PRA and the FCA. The implementation of the proposed Scheme would not lead to a change to the external auditors or the regulators and I am satisfied that there would be no material adverse effect on the level of external review applied to the transferring business.

## MY CONCLUSIONS BASED ON THE FINANCIAL INFORMATION AS AT 30 JUNE 2019

- 2.61 Based on the financial information for LGAS and ReAssure as at 30 June 2019, I remain satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the transferring LGAS policies, the existing ReAssure policies or the non-transferring LGAS policies.
- 2.62 I am therefore satisfied that the updated financial information as at 30 June 2019 does not provide any reason to change the conclusions in my Main Report.

## THE LEVEL OF REVIEW OF THE FINANCIAL INFORMATION AS AT 30 JUNE 2019

- 2.63 I have not carried out an independent review of the financial information but:

- For LGAS:
  - The Solvency II balance sheet as at 30 June 2019 (shown in Appendix A) has been subject to review and approval by:
    - The LGAS actuarial second line function;
    - KPMG;
    - The Chief Actuary; and
    - The Board and Audit Committee.
  - The pro-forma post-Scheme balance sheet has been calculated by applying a number of overlays to the published Solvency II balance sheet and has been reviewed and approved by:
    - The L&G Group reporting actuaries;
    - The With-Profits Finance Director; and
    - The LGAS Chief Actuary.
  - 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 30 June 2019, which have been reviewed by the LGAS second line function and the LGAS With-Profits Finance Director.
- For ReAssure:
  - The Solvency II balance sheet as at 30 June 2019 (shown in Appendix A) has been subject to review and approval by ReAssure’s Technical Approval Committee (a body responsible for the approval of external reporting including senior members from the Risk, Actuarial and Finance teams).
  - The pro-forma balance sheet for ReAssure has been reviewed by the ReAssure Chief Actuary.
  - The pro-forma post-Scheme TMTP for ReAssure (which remains subject to PRA approval) has been recalculated:

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<sup>4</sup> ReAssure’s external auditor will change to be KPMG on 1 January 2020. It could change subsequent to the acquisition by Phoenix if this were to be approved.

- For the transferring LGAS With-Profits Fund (“**LGAS WPF**”) business using a proxy calculation to estimate the Solvency I Pillar 1 position and the Solvency I Pillar 2 position, as described in Section 4 of my Main Report; and
  - For the transferring business outside of the LGAS WPF, using the existing methodology for the RNPF.
- I have carried out a high level reconciliation of the pro-forma post-Scheme Solvency II balance sheets as at 30 June 2019 for LGAS and ReAssure, shown in Appendix B, back to the current Solvency II balance sheets for LGAS and ReAssure shown in Appendix A.
- 2.64 As mentioned above, ReAssure’s TMTP recalculation to allow for the transferring business following the implementation of the Scheme remains subject to PRA approval. However, in deriving its pro-forma balance sheet, ReAssure has assumed that this approval will be granted.
- 2.65 If approval for the TMTP were not to be granted by the PRA, it has been calculated that the ReAssure solvency coverage ratio (in the pro-forma balance sheet) would reduce by only 2% and therefore I am satisfied that the assumption of TMTP approval is immaterial in the context of my conclusions regarding the security of the benefits of the affected policyholders.
- 2.66 Any impacts on the LGWPF resulting from the treatment of the TMTP prior to receiving PRA approval would be discussed and agreed by the ReAssure Fairness Committee with the aim of avoiding any changes to policyholder outcomes.
- 2.67 I am satisfied that it is appropriate to rely upon the financial information as at 30 June 2019 for the purpose of this Supplementary Report.



### 3. The effects of the proposed Scheme given the updated financial information for LGAS and ReAssure as at 31 December 2019

3.1 At the date of finalisation of this Supplementary Report the financial information as at 31 December 2019 remained subject to internal scrutiny by the relevant Boards and committees and to external scrutiny by the external auditors and therefore it was not appropriate for this financial information to be included in this report.

3.2 Both LGAS and ReAssure have shared the financial information as at 31 December 2019 showing:

- The unaudited (pre-Scheme) Solvency II balance sheets for LGAS and ReAssure as at 31 December 2019 in a similar format to that shown in Appendix A of my Main Report and Appendix A of this Supplementary Report; and
- Estimated pro-forma Solvency II balance sheets showing the financial positions of LGAS and ReAssure as at 31 December 2019 if the Scheme had been implemented on this date in a similar format to that shown in Appendix B of my Main Report and Appendix B of this Supplementary Report.

3.3 I have reviewed this information and I am satisfied that based on this:

- The size of the transferring business as at 31 December 2019 has not materially changed from the position as 30 June 2019. That is, the transferring business of LGAS consisted of approximately 1.0 million policies and assets of approximately £30 billion.
- The unaudited positions (as at 31 December 2019) prior to the implementation of the proposed Scheme show that both LGAS and ReAssure remain well capitalised and comfortably meet the requirements of their respective risk appetite statements prior to the implementation of the proposed Scheme.
- The estimated pro-forma positions (based upon the financial positions as at 31 December 2019) for both LGAS and ReAssure indicate a similar impact on the solvency coverage ratios from the implementation of the proposed Scheme to that at 31 December 2018 and 30 June 2019.

This provides comfort that both LGAS and ReAssure would be well capitalised and would comfortably meet the requirements of their respective risk appetite statements if the proposed Scheme were to be implemented.

3.4 I have not carried out an independent review of the financial information as at 31 December 2019 that has been provided by LGAS and ReAssure but have relied on the checks and reviews carried out by the two firms as follows:

- **LGAS:**
  - The pre-Scheme Solvency II balance sheet as at 31 December 2019 is consistent with the figures submitted to the PRA and EIOPA as part of LGAS's Q4 2019 Solvency II submission.
  - The pre-Scheme Solvency II balance sheet and the pro-forma post-Scheme Solvency II balance sheet as at 31 December 2019 have been subject to the same level of internal review as was conducted for the financial information as at 31 December 2018 (covered in Section 4 of my Main Report) and the financial information as at 30 June 2019 (covered in Section 2 of this report). That is:
    - The pre-Scheme Solvency II balance sheet as at 31 December 2019 has been subject to review and approval by:
      - The LGAS actuarial second line risk function;
      - The Chief Actuary; and
      - The Board and Audit Committee.

- The pro-forma post-Scheme balance sheet as at 31 December 2019 has been calculated by applying a number of overlays to the submitted Solvency II balance sheet as at 31 December 2019 and has been reviewed and approved by:
  - The L&G Group reporting actuaries;
  - The With-Profits Finance Director; and
  - The LGAS Chief Actuary.
- The Standard Formula results for the transferring LGAS business that are used to produce the pro-forma post-Scheme balance sheet for ReAssure have been estimated by LGAS using the Standard Formula process as at 31 December 2019 for the most material risks (with Standard Formula results as at 30 June 2019 used for the other risks).

These estimated Standard Formula results have been independently reviewed within the LGAS reporting team, and have been reviewed by the LGAS With-Profits Finance Director and the LGAS Chief Actuary.

- **ReAssure:**

- The pre-Scheme Solvency II balance sheet as at 31 December 2019 is consistent with the figures submitted to the PRA and EIOPA as part of ReAssure's Q4 2019 Solvency II submission.
- The pre-Scheme Solvency II balance sheet as at 31 December 2019 has been subject to review and approval by ReAssure's Technical Approval Committee (a body responsible for the approval of external reporting including senior members from the Risk, Actuarial and Finance teams).
- The pro-forma post-Scheme Solvency II balance sheet for ReAssure as at 31 December 2019 has been subject to review and approval by:
  - The ReAssure Chief Actuary;
  - The ReAssure WPA;
  - ReAssure reporting review actuaries; and,
  - The ReAssure second line risk function.
- The pro-forma post-Scheme TMTP for ReAssure (which remains subject to PRA approval) has been recalculated:
  - For the transferring LGAS WPF business using a proxy calculation to estimate the Solvency I Pillar 1 position and the Solvency I Pillar 2 position, as described in Section 4 of my Main Report; and
  - For the transferring business outside of the LGAS WPF, using the existing methodology for the RNPF.

3.5 I am satisfied that the (unaudited) financial information as at 31 December 2019 does not provide any reason to change the conclusions of my Main Report.

## 4. The operational readiness of ReAssure

### INTRODUCTION

4.1 In Section 8 of my Main Report, I described the plan that had been put in place to support the migration of the policy data from LGAS to ReAssure and, more widely, to ensure that both firms were operationally ready for the transfer and that the transfer would protect customer outcomes. The plan covers four key areas:

- Programme structure and tracking;
- Readiness gate assessments;
- Monitoring ongoing stability; and
- Contingency options.

4.2 The proposed transfer will not proceed unless it has been sanctioned by the High Court and it is the decision of the ReAssure Board and the LGAS Board to seek such a sanction (in the form of an Order) from the High Court to implement the Scheme.

4.3 The Boards will not seek an Order from the High Court unless they are satisfied, from review of the plan and progress against the plan, that the implementation of the Scheme would not have a material adverse effect on policyholders.

### THE CONCLUSIONS IN MY MAIN REPORT

4.4 As set out in my conclusions in my Main Report, at the date of my Main Report there were some areas of material concern regarding the migration plan that were being monitored closely by the ReAssure Board and the LGAS Board. These areas of concern required actions to be taken to reduce the risk of an unsuccessful migration back into tolerance.

### MITIGATING THE RISKS NOTED IN MY MAIN REPORT

4.5 In order to mitigate the risks from the issues on the implementation of the Scheme identified in my Main Report the following actions were taken:

- Regular updates from the LGAS and ReAssure teams tasked with preparing for, and carrying out, the migration have been provided to me;
- The ReAssure CRO has provided detailed monthly risk reports on the status of the migration project that have facilitated closer monitoring by the regulators, the Boards of LGAS and ReAssure, and me, of the progress of the project; and
- ReAssure has commissioned an independent review by an expert (KPMG) in the field of systems and data migrations to report on whether the migration would be likely to lead to material detriment to the transferring LGAS policyholders, and separately the existing ReAssure policyholders.

4.6 I am not an expert in large systems and data migrations and it is helpful for me to have experts in such matters to review the migration and therefore provide a sound basis from which to carry out my review. ReAssure has retained KPMG to carry out an independent, expert review and to report on the effect of the migration on policyholders and the options available to me are to retain my own expert or to rely upon the advice and input of KPMG. In making my decision I note that:

- KPMG is a large international firm with a wide range of experience in UK insurance and financial services companies and Part VII transfers and it is my view that it has the relevant and appropriate qualifications and knowledge of the laws and regulations governing insurance business transfers in the UK;
- KPMG has a range of relevant experience in respect of large systems and data migrations for UK insurance and financial services companies; and

- There is no reason why the advice and information provided by KPMG would be different if it was retained directly by me in respect of the Scheme.

4.7 I am therefore satisfied that it is appropriate for me to rely on the conclusions of KPMG in forming my view on the Scheme. KPMG has not been retained by me and has no liability to me for the reports on the migration that have been made available to me in order to provide me with information that I consider relevant to my assessment of the Scheme.

4.8 Since the date of my Main Report I have received:

- A number of updates from the LGAS and ReAssure teams tasked with preparing for, and carrying out, the migration. These updates indicate that good progress is being made on the migration.
- Risk reports from the ReAssure CRO providing his view on the progress of the migration as at 31 July 2019, 31 August 2019, 30 September 2019, 27 November 2019, 8 January 2020 and 11 February 2020.

In the latest report (11 February 2020) the ReAssure CRO indicated that he:

- Had the view that the overall project status was green;
- Was supportive of the decision to target an Economic Effective Date of 1 April 2020 and to proceed with the Sanction Hearing scheduled for 9 March 2020; and
- Was satisfied that no customer detriment was expected from targeting these dates.
- Two reports from KPMG dealing with the effects of the migration on the transferring LGAS policyholders and the existing ReAssure policyholders with the conclusions as set out below.

For information, 'Carbyne' was the internal project name given to the Scheme that is the subject of this supplementary report and my Main Report and that provides for the transfer to ReAssure of some of the long-term business of LGAS.

- The "**First KPMG Report**" was titled: 'Carbyne Migration Review 2 Final Report' and version 1.0 was issued on 20 December 2019.

The First KPMG Report concluded the following:

- (A) it is KPMG's view that there is a high probability that the migration will be successfully delivered to the planned timetable subject to the recommendation in this report being successfully implemented, and that progress continues in line with the planned delivery timetable;
- (B) the planned timetable is reasonable and achievable, and the programme team also have a viable contingency date defined;
- (C) there is appropriate governance in place over the delivery of the remainder of the plan; and
- (D) there is a low probability of the Carbyne migration having a material adverse effect on LGAS policyholders should progress continue in line with the plan.

- The "**Second KPMG Report**" was titled: 'Carbyne Migration Review 3' and version 1.0 was issued on 13 January 2020.

The Second KPMG Report concludes the following:

The KPMG conclusion is that: 'there is a low probability of the Carbyne migration having a material adverse effect on ReAssure policyholders should the progress of the Carbyne programme continue in line with the plans assessed in our 20 December report'. The report referred to in this conclusion is the First KPMG Report.

- Confirmation from the Chief Actuary and WPA of LGAS that they are satisfied that the migration will not lead to a material adverse effect on the transferring policyholders' benefit expectations, or on the standards of administration, service, management and governance that apply to the policies.
- Confirmation from the Chief Actuary and WPA of ReAssure that they are satisfied that the migration will not lead to a material adverse effect on the existing ReAssure policyholders' benefit expectations or on the standards of administration, service, management and governance that apply to the policies.

#### **THE MIGRATION AND THE LEGAL EFFECTIVE DATE**

- 4.9 The date of finalisation of this Supplementary Report was 24 February 2020 and at that time there was further work on the migration to be completed ahead of the Legal Effective Date of 6 April 2020.
- 4.10 Therefore it has not been possible to conclude in this report that a successful migration would be completed on time.
- 4.11 That said I note that:
- LGAS and ReAssure have put in place a number of governance safeguards that require both firms to review the migration before any final decision can be made to progress with the migration and the subsequent implementation of the Scheme;
  - The Scheme itself contains provisions to defer the Legal Effective Date (and as a result the Economic Effective Date) if, after the Sanction Hearing, there are indications that more time is needed to successfully complete the migration; and
  - In the extreme event that the implementation of the Scheme were to be delayed by more than three months, LGAS and ReAssure would need to seek a further Order from the High Court to implement the Scheme or the Scheme would lapse without becoming effective.
- 4.12 Considering these points together with the updates from ReAssure to date and the conclusions from KPMG in the First KPMG Report and the Second KPMG Report, I can conclude that, at the date of finalisation of this report (24 February 2020) I am satisfied that it is unlikely that the migration will lead to a material adverse effect on policyholders going forward.
- 4.13 I shall provide a letter dated 6 March 2020 to the High Court (which will be also published on the LGAS and ReAssure websites) that will include a further update on the state of the migration at that point.

## 5. The proposed purchase of RGP by Phoenix

### BACKGROUND

- 5.1 On 3 August 2018, the Swiss Re Group announced that it was considering an IPO to divest part of its interest in the ReAssure Group in 2019 and in anticipation of the IPO, a new public parent company (RGP) was set up – ReAssure is a subsidiary of RGP. Work was undertaken to reduce the reliance of RGP on Swiss Re Group functions, applications, policies and contracts to enable RGP to operate on a standalone basis.
- 5.2 On 11 July 2019, the Swiss Re Group announced that the IPO process had been suspended.
- 5.3 My Main Report was finalised on 3 July 2019 before the suspension of the IPO process. On 12 July 2019, following the suspension of the IPO, I wrote an addendum to my Main Report confirming that I remained comfortable that my conclusions on the proposed scheme remained unchanged despite the suspension of the IPO.
- 5.4 On 6 December 2019, Phoenix announced its intention to purchase RGP from the Swiss Re Group and MS&AD for £3.25 billion paid via a mixture of cash and shares in Phoenix.
- 5.5 On 13 February 2020, the Phoenix Group shareholders approved the proposed acquisition of RGP.
- 5.6 Although the purchase of RGP has been agreed between Swiss Re Group and Phoenix and subsequently by the shareholders of Phoenix Group it is still subject to the approval of (a non-exhaustive list):

- **The PRA**

A “change in control” process is required under FSMA to pass control of a company from one corporate body to another.

Under FSMA responsibility for the change in control process lies with the PRA, which is required to approve the acquisition unconditionally, approve the acquisition with conditions or object to the acquisition.

- **The Competition and Markets Authority.**

- 5.7 Completion of Phoenix’s purchase of RGP is currently expected early in the second half of 2020.
- 5.8 If these approvals are not forthcoming then Swiss Re Group and MS&AD would remain the owners of RGP. Given that the Swiss Re Group has previously stated its intention to further deconsolidate RGP (as mentioned above), it is possible that under such a scenario the Swiss Re Group would return to its plans to undertake an IPO.

### MY CONSIDERATIONS WITH RESPECT TO THE PROPOSED PURCHASE OF RGP BY PHOENIX

- 5.9 As set out above, under FSMA the purchase of RGP by Phoenix is subject to a change in control process overseen by the PRA. There is no role in the change in control process for an independent expert and my role as Independent Expert (also set out in FSMA) for the LGAS ReAssure Scheme is limited to an assessment of the effects of the Scheme on the relevant policyholders and to reporting on this to the High Court.
- 5.10 I must therefore ensure that in discharging my role as Independent Expert for the proposed Scheme I do not prejudice the change in control process by commenting on the merits or otherwise of the proposed purchase of RGP by Phoenix.
- 5.11 The LGAS ReAssure Scheme involves the policies and policyholders of LGAS and ReAssure, and Phoenix is not a party to the Scheme. This means that:
- If the Scheme were to be sanctioned by the High Court, then although Phoenix would be bound by the terms of the Scheme as a legally enforceable scheme under UK law, the Scheme would place no restrictions on Phoenix outside of the ReAssure business and transferring LGAS business.

There is therefore limited usefulness in the analysis of the possible strategic direction that Phoenix might take in the future.

- In any case, with access to information regarding Phoenix limited to that in the public domain it would not be possible to carry out such an analysis that was rigorous and robust.
- 5.12 Taking all of this together suggests that my role as Independent Expert for the LGAS ReAssure Scheme should, in respect of the proposed purchase of RGP by Phoenix:
- Be limited to a review of the possible impact of this potential purchase on my conclusions set out in my Main Report on the effects of the Scheme on the policyholders of LGAS and ReAssure; and
  - Not include opinion or comment on the merits or otherwise of the proposed purchase of RGP by Phoenix.
- 5.13 The change in control process will not be concluded before the Sanction Hearing of the LGAS ReAssure Scheme and is likely to conclude in the second half of 2020 and therefore, due to this uncertainty I have, in this section, considered the scenarios where the proposed purchase of RGP by Phoenix does and does not proceed.

#### **THE EFFECT OF THE PROPOSED PURCHASE OF RGP BY PHOENIX ON THE PROPOSED SCHEME**

- 5.14 In terms of the different groups of policies considered in Sections 8, 9, 10 and 11 of my Main Report:
- **The transferring LGAS policies:**  
If the Scheme were to be implemented, the transferring LGAS policies would be transferred into ReAssure and thus would become exposed to the effects of the Phoenix purchase of RGP.
  - **The existing ReAssure policies:**  
If the Scheme were to be implemented, the existing ReAssure policies would remain in ReAssure and thus would be exposed to the effects of the Phoenix purchase of RGP, however, this would also be true in the absence of the Scheme and I am satisfied that the potential effects of the Scheme on the existing ReAssure policies would not be affected by the Phoenix purchase of RGP.  
  
The impact of the Phoenix purchase of RGP on the existing ReAssure policies is not within the scope of my considerations as Independent Expert for this Scheme.
  - **The non-transferring LGAS policies:**  
If the Scheme were to be implemented, the non-transferring LGAS policies would remain policies of LGAS and would therefore be unaffected by the Phoenix purchase of RGP.
- 5.15 Therefore, I only need to consider the likely impact of the proposed purchase of RGP by Phoenix on my conclusions on the effects of the proposed Scheme in respect of the transferring LGAS policies.
- 5.16 Clearly, it would not be sensible to try and anticipate all the potential future decisions taken by Phoenix in respect of RGP but I have spoken with Phoenix regarding its current plans with respect to the purchase of RGP and I cover these below.

#### **THE IMPACT OF THE PROPOSED PURCHASE OF RGP BY PHOENIX ON MY CONCLUSIONS IN RESPECT OF THE SECURITY OF THE BENEFITS OF THE TRANSFERRING LGAS POLICYHOLDERS**

##### **Introduction**

- 5.17 In Section 8 of my Main Report I set out my analysis and my conclusion that if the proposed Scheme were to be implemented then there would not be a material adverse effect on the security of the benefits of the transferring LGAS policyholders. In this sub-section I have reconsidered this conclusion in the context of the proposed purchase of RGP by Phoenix.
- 5.18 As set out above, although agreed between the Swiss Re Group and Phoenix, the purchase of RGP by Phoenix remains subject to various approvals and the expected completion date is currently early in the second half of 2020 and therefore I need to consider the scenarios where the proposed acquisition does and does not proceed.

5.19 Compared to the scenario where the purchase of RGP by Phoenix does not proceed, the proposed purchase would only have an impact on the provider of parental support as the ownership of RGP would change from the Swiss Re Group and MS&AD to the Phoenix Group and I cover the impact from this change below.

#### **The scenario where the Phoenix purchase of RGP does not proceed**

5.20 If the Phoenix purchase of RGP were not to proceed then the Swiss Re Group and MS&AD would continue to own RGP (75% and 25% respectively).

5.21 As set out in Section 2 of this report, since the finalisation of my Main Report, there have been no material changes to:

- The group structures of the L&G Group or the Swiss Re Group;
- The availability of support to ReAssure and its policyholders from the Swiss Re Group and MS&AD; or
- The availability of support to LGAS and its policyholders from the L&G Group.

5.22 Therefore the conclusions reached in in Section 8 of my Main Report, that the size and level of capitalisation of the Swiss Re Group and MS&AD provide material security for ReAssure and its policyholders, remain unchanged, and I am satisfied that the change to the (potential) provider of parental support for the transferring LGAS policies from the L&G Group to the Swiss Re Group and MS&AD would not lead to a material adverse effect on the security of the benefits guaranteed under the transferring LGAS policies.

#### **The scenario where the Phoenix purchase of RGP does proceed**

5.23 As set out in Section 2, the security of benefits for the policies in ReAssure arises primarily from ReAssure and the availability of support from the group companies or from a parent company (in this case RGP and the owners of RGP) provides potential extra financial strength and security for the policy benefits on top of this primary security.

5.24 ReAssure is currently well capitalised and comfortably meets the requirements of the ReAssure IPO RA Statement (the risk appetite currently used by ReAssure) and there exist controls to protect the security of the ReAssure policies in the event that ReAssure were to get close to breaching the requirements of this risk appetite statement.

5.25 If the Phoenix purchase of RGP were to be completed successfully then:

- There would be no change to ReAssure as the primary source of security for the benefits of the ReAssure policies which would, post Scheme, include the transferring LGAS policies;
- There would be no change to the financial strength of ReAssure, ReAssure would still be required to adhere to the ReAssure IPO RA Statement and there exist various controls around any changes to this risk appetite statement (as set out in Section 6 of my Main Report) including the non-objection of the regulators; and
- Phoenix would be the sole owner of RGP, and, if required, RGP would look to Phoenix to provide parental/group support.

5.26 Therefore, the only impact of the proposed purchase of RGP by Phoenix would be that the extra security provided by parental/group support would be provided by Phoenix rather than Swiss Re Group and MS&AD.

5.27 I do not have access to non-public financial information regarding Phoenix as part of my work on this Scheme and, based on public information, as at 30 September 2019 Phoenix was well capitalised with £3.0 billion of capital in excess of its SCR and a solvency coverage ratio (on a shareholder capital basis) of 156%. Although I cannot review the basis of calculation of this solvency coverage ratio, I take comfort from the following:

- The solvency coverage ratio was comfortably within the stated target range of its shareholder basis Solvency II solvency ratio as set out in its risk appetite and capital management policy of 140% to 180%.
- Phoenix currently has an insurer financial strength rating of A+ (Stable) from Fitch Ratings.



- The solvency coverage ratio and associated capital management policy were made public in Phoenix's investor presentation on 6 December 2019 and in its 'Combined Circular and Prospectus' to shareholders dated 17 January 2020. Therefore, particularly as Phoenix is a publicly listed company, it is to be expected that this ratio would have been subject to external and internal scrutiny.
- Given the reputational damage that would apply to the firm and to the Board of the firm if it were to not support an insurance subsidiary in the scenario where such support were to be required, one would expect that in all but the most extreme scenarios, as the owner of RGP, Phoenix would be likely to provide support to its group subsidiaries (which would include RGP and ReAssure) if it were required. It should also be noted that there are considerable financial resources available in Phoenix to provide such support.

5.28 I am satisfied that if the Scheme were to be implemented and the Phoenix purchase of RGP were to successfully complete, the change for the transferring LGAS policies to have parental support available from Phoenix would not provide any reasons to change the conclusions in my Main Report.

#### **THE IMPACT OF THE PROPOSED PURCHASE OF RGP BY PHOENIX ON MY CONCLUSIONS IN RESPECT OF THE REASONABLE BENEFIT EXPECTATIONS OF THE TRANSFERRING LGAS POLICYHOLDERS**

5.29 In Section 8 of my Main Report I set out my analysis and my conclusion that if the proposed Scheme were to be implemented then there would not be a material adverse effect on the reasonable expectations of the transferring LGAS policyholders in respect of their benefits. In this sub-section I have reconsidered this conclusion in the context of the proposed purchase of RGP by Phoenix.

5.30 In respect of the transferring LGAS policies, the Phoenix purchase of RGP would not in and of itself cause any material changes to:

- The terms and conditions of any of the policies.
- The likelihood that the policies receive their benefits when due.
- The size or frequency of those benefits.
- In respect of unit-linked policies:
  - The managers of the unit-linked funds, the investment objectives applied to those funds, the charges applied to those funds or the pricing of those funds;
  - The range of funds available;
  - 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.

5.31 I am satisfied that the successful completion of the proposed purchase of RGP by Phoenix would not affect the conclusions in my Main Report that the implementation of the proposed Scheme would not have a material adverse effect on the reasonable expectations of the LGAS transferring policyholders in respect of their benefits.

**THE IMPACT OF THE PROPOSED PURCHASE OF RGP BY PHOENIX ON MY CONCLUSIONS IN RESPECT OF THE STANDARDS OF ADMINISTRATION, SERVICE, MANAGEMENT AND GOVERNANCE APPLIED TO THE TRANSFERRING LGAS POLICIES**

5.32 In Section 8 of my Main Report I set out my analysis and my conclusion that if the proposed Scheme were to be implemented then there would not be a material adverse effect on the standards of administration, service, management and governance applied to the transferring LGAS policies. In this sub-section I have reconsidered this conclusion in the context of the proposed purchase of RGP by Phoenix.

5.33 Phoenix has confirmed to me that, if its purchase of RGP were to proceed, it would make no immediate changes to the current ReAssure operating model and that although Phoenix plans to start the process of alignment of RGP with the Phoenix risk appetite statements and capital management policy, the ReAssure operating model would otherwise remain materially unchanged for at least two years.

5.34 This specifically includes continuing with no material changes to:

- The existing RGP capital management policy and risk appetite statement (the ReAssure IPO RA Statement).  
Although Phoenix may start the alignment of the capital management policies within two years.
- The AIA and IMA.
- The existing customer operating model.  
For the avoidance of doubt this includes RUKSL continuing to administer the existing ReAssure business and the transferring LGAS business on its own IT systems.
- The investment strategy in the LGWPF, the NMWPF, the GAWPF and the WLWPF.
- The governance model for the ReAssure business and the transferring LGAS business.

Although Phoenix may start alignment of the governance of all of ReAssure's with-profit funds with that of its existing with-profits funds within two years (as discussed further below) which, for the avoidance of doubt, includes the ReAssure Fairness Committee, the current ReAssure WPA role and the planned WPA role in respect of the LGWPF.

5.35 Given these assurances from Phoenix, I am satisfied that the operating model that I considered in arriving at the conclusions of my Main Report would be materially unchanged if the Scheme were to be implemented and the Phoenix purchase of RGP were to proceed.

5.36 I am satisfied that the successful completion of the proposed purchase of RGP by Phoenix would not affect the conclusions in my Main Report that the implementation of the proposed Scheme would not have a material adverse effect on the standards of administration, service, management and governance applied to the transferring policies.

**LONGER TERM CONSIDERATIONS**

5.37 As mentioned above, if the purchase of RGP were to proceed then in order to harmonise the companies across the group, Phoenix plans to align the capital calculation applying to the RGP business with its risk appetite and capital management policy as derived from the Phoenix Internal Model.

5.38 Further, Phoenix plans to align the governance model with the approach for its existing life companies. Specifically, the existing Phoenix life companies have a group level WPC that has oversight of all the with-profits funds in the

Phoenix Group. Each life company has a Chief Actuary (as defined under the SMCR) and each with-profits fund has an assigned WPA (although one WPA may be assigned to multiple with-profit funds).

5.39 Phoenix's long-term plans may include the eventual transfer of the long-term insurance business of RGP into one of Phoenix's existing life companies via a Part VII transfer but such a transfer would be at least two years into the future and any subsequent transfer of the acquired ReAssure business would require a Part VII scheme of transfer and the approval of the High Court following scrutiny from an independent expert, the PRA, the FCA and the Boards and senior management of the firms involved.

5.40 I am satisfied that, in any such subsequent Part VII scheme of transfer, the transferring LGAS policyholders would be protected through an equivalent court process as has been conducted in respect of this Scheme.

## **CONCLUSION**

5.41 Since my Main Report was finalised, Phoenix has announced its intention to purchase RGP from Swiss Re Group and MS&AD and this will be subject to the change in control process that is the responsibility of PRA as set out above.

5.42 I have considered the potential impact of the proposed purchase of RGP by Phoenix on my conclusions on the effects of the proposed Scheme on the various groups of policies and I am satisfied that the Phoenix purchase of RGP would not change my overall conclusions as set out in Section 15 of my Main Report, because:

- I am comfortable that Phoenix is financially strong and well capitalised such that the purchase does not have a material adverse impact on the transferring policyholders relative to RGP (and therefore ReAssure) being owned by Swiss Re Group and MS&AD.
- Phoenix has provided assurances that for a period of at least two years following the successful completion of the purchase there would be no material changes to:
  - The ReAssure operating model; and
  - The ReAssure governance structure for the post-Scheme ReAssure (including the transferring LGAS policies) as reviewed when forming the conclusions of my Main Report.
- Any changes to the risk appetite statements or operating models or any subsequent restructuring would be subject to scrutiny from the PRA and the FCA to ensure no adverse effect on policyholders and, in the case of any future Part VII transfer from ReAssure to Phoenix there would also be scrutiny from the High Court and an independent expert.

5.43 If the purchase of RGP by Phoenix were not to proceed for any reason then it is possible that the Swiss Re Group would revert to its plan of an IPO for ReAssure. I considered the likely effect of the IPO on my conclusions on the likely effects of the implementation of the proposed Scheme on the LGAS and ReAssure policyholders in Section 12 of my Main Report and I concluded that if the ReAssure IPO were to proceed, sufficient controls were in place to ensure that there would not be a material adverse effect on the policyholders of LGAS or ReAssure.

## 6. The ReAssure purchase of Old Mutual Wealth Life Assurance Limited

### BACKGROUND

- 6.1 On the 5 August 2019, RGP (see Section 6 of my Main Report for a full company structure) announced that it intended to purchase the heritage life and pensions division, Old Mutual Wealth Life Assurance Limited (“**OMWLA**”), from Quilter Plc for £425 million.
- 6.2 The transaction was subject to regulatory approval and the change in control application was approved by the PRA on 10 December 2019. The transaction effective date was 31 December 2019 (the “**OMWLA Completion Date**”).
- 6.3 As at 30 June 2019, OMWLA managed £12.3 billion of assets in respect of pensions, investments, savings and protection products.
- 6.4 OMWLA has become a sister company of ReAssure within RGP and therefore the purchase will not have a direct impact on the security of the benefits of the ReAssure policyholders or of the transferring policyholders.

### THE REINSURANCE OF OMWLA INTO REASSURE

- 6.5 An intra-group reinsurance treaty became effective on the OMWLA Completion Date in order to transfer the economic interest in, and associated risks of, OMWLA from RGP to ReAssure (to the RNPF).
- 6.6 The terms of the reinsurance agreement were subject to the approval of the ReAssure Board and the OMWLA Board and the reinsurance transaction obtained non-objection from the PRA.
- 6.7 The current expectation is that the majority of the OMWLA business would subsequently be transferred into ReAssure using a Part VII scheme of transfer within two years of the OMWLA Completion Date.
- 6.8 The acquisition of OMWLA by RGP, and the subsequent reinsurance agreement with ReAssure and Part VII transfer do not have any effect on the risk appetite statements, the capital management policies or the business plans and models of ReAssure or RGP. Furthermore, OMWLA will have a risk appetite statement and capital management policy consistent with that of ReAssure.
- 6.9 I have seen 10-year financial projections that allow for the effect of the purchase of OMWLA, and the reinsurance and Part VII transfer of the business to ReAssure. The results indicate that ReAssure is projected to remain within the requirements of the risk appetite statement currently being used by ReAssure (the ReAssure IPO RA Statement).
- 6.10 Any subsequent transfer of acquired business into ReAssure would require a Part VII scheme of transfer and the approval of the High Court following scrutiny from an independent expert, the PRA, the FCA and the Boards and senior management of the firms involved.
- 6.11 Therefore I am satisfied that the transferring LGAS policyholders and existing policyholders of ReAssure would be protected through an equivalent court process as has been conducted in respect of this Scheme.

### CONCLUSION

- 6.12 I am satisfied that the OMWLA transaction does not provide any reason to change the conclusions in my Main Report.

## 7. The recent judgment on the Prudential Rothesay Scheme

### INTRODUCTION

- 7.1 On 16 August 2019, the High Court declined to sanction the transfer of a £12 billion portfolio of annuities from Prudential to Rothesay. Prudential and Rothesay had sought to effect the transfer of the portfolio pursuant to Part VII of FSMA. I understand that Prudential and Rothesay are appealing the decision.
- 7.2 It is at the discretion of the High Court as to whether or not to sanction a scheme that is put before it but, in my experience it is unusual for a Part VII transfer between life insurers to be declined by the Court, and so I have considered the LGAS ReAssure Scheme in the context of the High Court's decision on the Prudential Rothesay transfer and as I set out below I am satisfied that the conclusions of my Main Report are unaffected by the judgment in the Prudential Rothesay Scheme.

### THE JUDGMENT ON THE PRUDENTIAL ROTHESAY SCHEME

- 7.3 The presiding judge for the Prudential Rothesay Scheme was Snowden J and he set out his decision not to sanction the Prudential Rothesay Scheme in his Approved Judgment for Case No: CR-2018-003686 dated 16 August 2019 (the "Approved Judgment") and I have summarised the reasons for his decision into the following subsections:
- **The policy types (annuities) that were to be transferred under the Prudential Rothesay Scheme**  
Snowden J asked the question, "Can annuity policies be transferred?" and considered the nature of annuity policies in the context of the Scheme.
  - **The reasonable expectations of policyholders**
  - **The security of the benefits under the policies affected by the Scheme**  
Snowden J considered the analysis that had been carried out by the Independent Expert and the regulators based on the solvency coverage ratios, the capital management policies and the provision of support from the parent company or group companies.  
Snowden J stated that, in his opinion, he could not 'disregard as fanciful the possibility that Prudential or Rothesay might require external [e.g. parental] financial support over the lifetime of the annuitants'.
  - **The age and reputation (sometimes called the 'venerability') of the transferee (Rothesay) compared to that of the transferor (Prudential)**
  - **The balance between the interests of the policyholders and the interests of the commercial parties to the transfer**
  - **The complaints about, and objections to, the Scheme**

- 7.4 Further detail on each of these areas is provided below along with my views on the relevance to the proposed LGAS ReAssure Scheme of each such area.

### THE POLICIES TO BE TRANSFERRED UNDER THE LGAS REASSURE SCHEME

#### The policies in the Prudential Rothesay Scheme

- 7.5 Under the Prudential Rothesay Scheme the transferring business consisted exclusively of annuity policies. Such policies typically provide an income in retirement to customers while they are still alive, in return for a single payment at outset. The following features of these policies were highlighted in the judgment:

- The customers had no realistic option to change the annuity to another provider;
- The initial investment made and the subsequent income provided by the annuity were likely to be a significant part of the customer's wealth; and
- Given these annuities paid an income to customers in retirement it was likely that if the risk of failure by the company however remote, were to eventuate, then the result would be catastrophic for policyholders.

#### The policies in the LGAS ReAssure Scheme

- 7.6 I have not conducted a detailed review of the portfolio of Prudential policies that were the subject of the Prudential Rothesay transfer but there are various pieces of publicly available information from which I have been able gain a high level insight into the demographic profile of the portfolio. I have reviewed a breakdown of the LGAS transferring business from LGAS in order to ascertain its demographic profile.
- 7.7 Based on these it appears that the business intended for transfer under the Prudential Rothesay Scheme had certain important differences to the LGAS transferring business under the LGAS ReAssure Scheme that is the subject of this report. The main differences were that the (intended) transferring portfolio of Prudential policies had:
- A profile of older policyholders;
  - Fewer different types of policy; and
  - No flexible surrender and withdrawal conditions (as they were annuities).
- 7.8 Consequently, when compared to the Prudential policies in the Prudential Rothesay transfer, the LGAS transferring policyholders would be expected to be less vulnerable to the type of catastrophic consequences of insurance company failure that was envisaged by Snowden J in the Prudential Rothesay judgment.
- 7.9 It should also be noted that, as the Prudential Rothesay Scheme only concerned annuity policies, Snowden J's judgment only concerned annuity business.
- 7.10 There are some annuities in the transferring business; these annuities are both with-profits and non-profit in nature. As at 31 December 2018 this business makes up only 1.5% of the transferring business by BEL with 1.4% of this consisting of with-profits annuities and 0.1% consisting of non-profit annuities. There are approximately 9,000 annuity policyholders.
- 7.11 The with-profits annuities in the transferring business would be transferred to the new LGWPF in ReAssure and would benefit from the security provided by that fund:
- The LGWPF is projected to be a financially strong ring-fenced fund with a solvency coverage ratio of 141% (as at 30 June 2019) comfortably in excess of its regulatory requirements and those of the ReAssure RA Statement (as shown in Appendix B)<sup>5</sup>; and
  - The LGWPF would be subject to governance and oversight of the ReAssure Board, the ReAssure Fairness Committee, the ReAssure With-Profits Management Committee and the LGWPF WPA.
- 7.12 I am satisfied that the security provided by being part of a strong ring-fenced fund and part of ReAssure means that the LGAS transferring policyholders with annuities would not be materially adversely affected if the Scheme were to be implemented.
- 7.13 If the Scheme were to be implemented the non-profit annuities in the transferring business would be transferred to the RNPF.

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<sup>5</sup> The solvency coverage ratio for the LGWPF of 141% includes a TMTP recalculation to allow for the transferring business (assuming the transfer had taken place on 31 December 2018 and with allowance made for run-off over 6 months). At the time of writing, ReAssure has applied for approval to recalculate the TMTP to allow for the transferring business as at the Legal Effective Date; however, this recalculation remains subject to PRA approval. Further, ReAssure is in the process of updating this application such that the TMTP is calculated as at the revised Economic Effective Date.

7.14 These non-profit annuities are linked to the above with-profits annuities as they were set up for the associated protected rights benefits of the annuitants. They were not in the scope of the original sale of the transferring business but were subsequently included in the proposed Scheme in order to avoid a detrimental outcome where policyholders with transferring with-profits annuities would have had their pensions split and paid by two different firms and would have been exposed to potential tax disadvantages.

7.15 It therefore seems reasonable to transfer the non-profit annuities in order to avoid the adverse effects on policyholders if they remained in LGAS.

### **Conclusion**

7.16 I am satisfied that the points made by Snowden J (summarised above) in the judgment on the Prudential Rothesay Scheme do not have the same weight in the LGAS ReAssure Scheme and therefore do not change the conclusions of my Main Report.

## **THE REASONABLE EXPECTATIONS OF POLICYHOLDERS**

### **The expectations in respect of the transfer of a policy**

7.17 In the context of a Part VII scheme, the concept of the "reasonable expectations" of policyholders refers to how an insurer will perform its obligations under the policy.

7.18 For the Prudential Rothesay Scheme Snowden J stated that he considered there to be merit in the arguments from policyholders that they had "reasonable assumptions" that Prudential would not transfer its obligations under the policyholder's policy to another company. In forming this view Snowden J made reference to:

- The absence of any reference in the policy documents to the possibility of a transfer of the policy in the future; and
- Various statements made over the years by Prudential regarding its longevity and trustworthiness.

7.19 Snowden J raised these as points for consideration in the exercise of his discretion in accordance with section 111(3) of FSMA and stated that whilst it is reasonable that these points should be taken into consideration, on their own they do not lead to the conclusion that the Scheme should not be sanctioned as a matter of law.

7.20 Both of these points apply to an extent to the LGAS policies that would be transferred to ReAssure and so I have considered this part of the Approved Judgment in the context of the LGAS ReAssure Scheme.

7.21 For the annuities in the transferring business and as stated above:

- The with-profits annuities would be transferred to the LGWPF (a new with-profits fund in ReAssure) and will benefit from the security provided by a strong, ring-fenced fund with an established governance and management structure around it; and
- The non-profit annuities are linked to the above with-profits annuities (these were set up for the associated protected rights pots of the annuitants) and were included in the proposed Scheme in order to avoid a detrimental outcome to policyholders.

7.22 LGAS and ReAssure have analysed the transferring policies and concluded that all of the non-annuity products in the transferring business are more flexible than annuities and allow surrender and/or lapse (albeit sometimes with a penalty).

### **The Approved Judgment of Snowden J**

7.23 In paragraphs 127 to 131 of his Approved Judgment Snowden J sets out his views on the reasonable expectations or assumptions of policyholders and in particular he makes reference to past judgments on Part VII schemes and how these have established the framework for current considerations around the reasonable expectations of policyholders in the context of a Part VII scheme. These past judgments include that by Evans-Lombe J in Re Axa

Equity & Law Life Assurance Society plc and AXA Sun Life plc (2001) to which I refer in Section 4 of my Main Report.

- 7.24 As well as referencing past schemes, Snowden J describes how the concept of policyholders' reasonable expectations is currently "**generally** understood [my emphasis] to relate to how an insurer will perform its obligations under the policy." Snowden J does not appear to suggest that this represents a change.
- 7.25 Taking into account the references to past judgments on Part VII schemes, the adherence to the "generally" accepted understanding of policyholder expectations, the exercising of discretion in line with FSMA, and my subsequent discussions with ReAssure's legal advisers (Herbert Smith Freehills) it is my view that the judgment does not seek to change the way in which the reasonable expectations of policyholders should be understood and considered in a Part VII Scheme.

#### **Conclusion on the reasonable expectations of policyholders**

- 7.26 It should also be noted that, in the time since the publication of Snowden J's Approved Judgment there have been a number of other Part VII schemes that have been approved by the High Court. These Part VII schemes include one between Canada Life and Scottish Friendly Assurance Society and one between Equitable Life and Utmost Life and Pensions. The judgments in these Part VII schemes have not viewed policyholders' reasonable expectations in a different way to that in the Part VII schemes prior to the Prudential Rothesay scheme.
- 7.27 Taking all this together I am satisfied that the Prudential Rothesay judgment does not provide any reason to change the way in which I should consider the reasonable expectations of policyholders and therefore the conclusions in my Main Report remain that the implementation of the LGAS ReAssure Scheme would not contravene the reasonable expectations of the transferring policyholders.

#### **THE SECURITY OF BENEFITS UNDER THE POLICIES AFFECTED BY THE SCHEME**

- 7.28 In his Approved Judgment on the Prudential Rothesay Scheme, Snowden J highlighted the potential differences in the availability of financial resources between Prudential and Rothesay. In particular, it was his view that Prudential's parent provided greater security to Prudential than Rothesay's parent companies did for Rothesay because he felt that Rothesay's three main shareholders could more easily distance themselves from their subsidiary should they wish to do so.
- 7.29 This has been covered in Section 8 of my Main Report and Section 2 (paragraph 2.6 onwards) of this Supplementary Report and in summary:
- The security of the benefits under the policies within a firm arises primarily from the financial strength of the firm itself and its ability to withstand severe and extreme events; and
  - The availability of support from the group companies or from a parent company provides extra financial strength and security for the policy benefits in the event that this extra security is required because the faith placed in the financial strength of the firm proves to be misplaced.
- 7.30 Therefore the security of benefits would be provided primarily from ReAssure and additional security and financial strength would be provided by RGP and the ultimate owner of RGP. There are two possible scenarios to consider:



- The Phoenix purchase of RGP proceeds:

In this scenario the transferring LGAS policyholders would have the Phoenix Group as the ultimate last resort for security. As discussed in Section 5 of this report, I have not carried out a detailed comparison of the risk appetite statements used by the L&G Group and the Phoenix Group but I note that:

- Both meet their respective risk appetite statements and capital management policies; and
- Both have strong ratings from an external, independent ratings agency.

The external rating given to the L&G Group and the Phoenix Group is the same at A+ (by Fitch Ratings) and, while it is not straightforward to objectively compare the ratings for different companies, in terms of the security provided by the parent company, the relative levels of the ratings matter less than the rating of that parent.

As the Phoenix Group is rated as strong, this implies a high level of financial strength, a low probability of insolvency, and a high probability that it would be able to provide support to the ReAssure and transferring LGAS business in the future if called upon to do so.

- The Phoenix purchase of RGP does not proceed:

As discussed in Section 2 of this report, I am satisfied that, if the Scheme were to be implemented and the Phoenix purchase of RGP were not to proceed, the change for the transferring policies to having parental 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.

7.31 In conclusion, I am satisfied that if the Scheme were to be implemented and the Phoenix purchase of RGP were to successfully complete, the change for the transferring LGAS policies to having parental support available from Phoenix would not have a material adverse effect on the security of the benefits of those policies.

#### **THE AGE AND REPUTATION OF THE FIRMS INVOLVED IN THE SCHEME**

7.32 For the Prudential Rothesay Scheme, Snowden J considered that it was relevant for the Court to consider the “respective ages and reputations of the transferor and transferee” when considering whether to sanction the transfer. In this context he compared Rothesay unfavourably with Prudential.

7.33 In considering the relative ‘vulnerability’ of the parties to this Scheme, there are arguably some similarities when comparing the age and reputations of LGAS with ReAssure. However, I note that:

- Although the name Legal and General might be considered as more widely known than that of ReAssure:
  - The difference in longevity is not as marked as that between Prudential and Rothesay as ReAssure has a long (over 50 years) history as a provider of life and pensions business in the UK;
  - As an acquirer and manager of closed books it is to be expected that ReAssure does not have as high a public profile to LGAS which has been selling life and financial services business directly to the public for many years; and
  - Legal and General has not had any significant name changes whereas ReAssure was, for the majority of the company’s existence prior to 2011, known as Windsor Life.
- On 6 December 2017, the L&G Group announced that it intended to sell part of its long-term insurance business to ReAssure and it is this block of business that would be transferred from LGAS to ReAssure under the LGAS ReAssure Scheme.

The main reasons for the sale were that the LGAS traditional life and pensions business had been largely closed to new business since 2015 and its sale would reduce the short-term, medium-term, and long-term risks to LGAS arising from servicing a largely closed book of business and allow it to focus on growth in other areas such as writing and acquiring blocks of annuities, and investment management.

In my view, it would not be advantageous for policyholders to stay in a company that has made a strategic decision not to provide similar traditional products. This is particularly relevant when there is an alternative company whose strategy is to acquire and manage such closed books of traditional insurance business. In my view, an insurer that is strategically focussed on a particular business is more likely to be incentivised to make the investments of time and resource needed to effectively manage that business over the long term than an insurer whose strategic focus has shifted elsewhere.

- ReAssure's strategy is to acquire closed books of insurance business from other insurance companies and it has completed a number of such transfers since the company was originally founded in 1963 such that it is now one of the leading life insurers in the UK.
- From previous acquisitions and transfers carried out over a long period of time, ReAssure has experience in managing business similar in nature and age to the transferring business.

7.34 I am satisfied that if the Scheme were to be implemented and the transferring policies to transfer from LGAS to ReAssure, the difference between the respective ages and reputations of the companies would not lead to a material adverse effect on the transferring policies.

#### **THE BALANCE BETWEEN THE INTERESTS OF THE POLICYHOLDERS AND THOSE OF THE COMMERCIAL PARTIES TO THE TRANSFER.**

##### **Introduction**

7.35 The main purpose of the Prudential Rothesay transaction was stated to be to enable the release of solvency capital for the Prudential de-merger plans and in his judgment on the scheme, Snowden J noted that most of the economic benefits of the transaction had already been achieved via the reinsurance arrangement that had been put in place between the two firms in respect of the transferring business.

7.36 Snowden J was of the opinion that whereas Prudential and Rothesay had largely achieved their business purpose without the Prudential Rothesay Scheme, the implementation of this Scheme would lead to a 'fundamental change' to the transferring Prudential annuitants and Snowden J therefore felt there was an imbalance between the interests of the policyholders and those of the commercial parties to the transfer.

##### **The rationale for the LGAS ReAssure Scheme**

7.37 As stated in Section 7 of my Main Report, 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.

7.38 In respect of the sale of this business by LGAS and the acquisition of this business by ReAssure:

- 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 to be sold consisted 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.

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

- ReAssure's business strategy 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 ReAssure has undertaken a large number of transfers of business since its first acquisitions in 1983.

From ReAssure's point of view, the purchase of this block of business from LGAS was consistent with its strategy of growing through the acquisition of closed life books, and would strengthen its market position as one of the leading life insurers in the UK.

7.39 The LGAS withdrawal from the traditional insurance-based pensions, savings and investment business can be contrasted with the position of Prudential if the Prudential Rothesay Scheme were to be implemented as, in that case, Prudential would have continued to have a substantial portfolio of in-force annuity business.

#### **Achieving the aims of the Scheme through reinsurance**

7.40 In the judgment on the Prudential Rothesay Scheme, Snowden J made the point that there was already in place a reinsurance agreement between Prudential and Rothesay and that this reinsurance agreement had already enabled the achievement of the main business and commercial reasons for the Prudential Rothesay Scheme and that this would be the case whether or not that scheme was subsequently sanctioned.

7.41 As set out in Section 5 of my Main Report a reinsurance agreement has also been put in place between LGAS and ReAssure (the RTA) in order to transfer much of the economic risk and reward of the business to be transferred under the LGAS ReAssure Scheme to ReAssure.

7.42 However, absent the implementation of the LGAS ReAssure Scheme the RTA would not fully achieve the business and commercial objectives of LGAS and ReAssure. In particular:

- LGAS would not achieve its objective of exiting the traditional insurance based pensions, savings and investment business and would not, for example, be able to decommission and simplify the IT infrastructure necessary to administer the business, or divert employee resources and management time towards its strategic objectives.
- ReAssure would not be able to realise the expected cost savings that motivated the transaction or fully integrate the transferring business with its existing business. The implementation of the Scheme would allow ReAssure to better manage and calculate its capital requirements in relation to the transferring business as the complexity and costs associated with obtaining data from LGAS's administration systems would no longer apply and ReAssure would have a direct relationship with the transferring policyholders.

#### **Conclusion**

7.43 Broadly speaking the motivations for Part VII transfers could almost always be classified as 'commercial' in some sense but whereas the transfer of the Prudential annuities to Rothesay was being undertaken for apparently purely financial reasons (i.e. to release capital and reduce costs), in the case of the LGAS ReAssure Scheme, the main motivations are operational and strategic being, in essence:

- A decision by the L&G Group to sell a block of business that no longer fits with its strategy; and
- A decision by ReAssure to acquire a block of business because this would be in line with its strategy.

7.44 Under UK law, such transfers of long-term business are permitted under FSMA and it seems legitimate for companies to use Part VII transfers to facilitate implementation of a change in strategy and several other companies have recently used Part VII Schemes as part of a process to enable them to implement a particular strategy.

7.45 I am satisfied that in the case of the LGAS ReAssure Scheme there is an appropriate balance between the commercial interests of L&G Group Plc and RGP and the interests of the different groups of policyholders for the following reasons:

- As stated above, it should be an advantage to policyholders to move out of a company that has made a strategic decision not to provide similar business into a company whose strategy is to acquire such closed

books of insurance business from other insurance companies and to manage those blocks of business as they run off.

An insurer that is strategically focussed on a particular business is more likely to be incentivised to make the investments of time and resource needed to effectively manage that business over the long term than an insurer whose strategic focus has shifted elsewhere.

- The Fixed Expense Agreement:

As set out in Section 5 of my Main Report, there is currently in place a fixed expense agreement between the LGAS WPF and LGAS.

If the proposed Scheme were to be implemented a new fixed expense agreement (the “**Fixed Expense Agreement**”) would be set up for the LGWPF within ReAssure until the last policy in the LGWPF runs-off. As described in Section 7 and Section 8 of my Main Report, the Fixed Expense Agreement would have a number of advantages for policyholders in the LGWPF including:

- Increased certainty regarding future unit costs applying to the with-profit policies until the last policy in the LGWPF runs-off, reducing the capital requirements of the with-profit fund; and
- Coverage of 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).

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. In Section 8 of my Main Report I indicated that I had seen analysis that this payment would be more than offset by the effect of the Fixed Expense Agreement and subsequent to that I have seen an updated analysis that shows that this remains the case.

I noted in my Main Report that the Fixed Expense Agreement would only come into effect on completion of the transfer of the business before 31 December 2019 and that, if no transfer was 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. However, LGAS and ReAssure have since agreed that the Fixed Expense Agreement and the associated £50 million payment would come into effect on the Legal Effective Date (6 April 2020) despite the fact that this would be after 31 December 2019.

- The Scheme would allow ReAssure to take certain actions (including to merge the LGWPF with other with-profits funds managed by ReAssure upon the attainment of the sunset clauses) which are intended to allow ReAssure to manage the transferring business in an efficient way over time as it (and they) run off to ensure that economies of scale are achieved where reasonably possible (although due to the Fixed Expense Agreement such economies of scale would not accrue for the benefit of the policies in the LGWPF). The Scheme sunset clauses would also be expected to improve the stability of returns for the transferring with-profits policyholders during the latter stages of run-off.

This would be in the interests of the transferring LGAS policyholders and the existing policyholders of ReAssure.

In contrast, LGAS has no other with-profits funds with which the LGAS WPF could merge in future.

- The reinsurance agreement already in place (the RTA) does not mean that all of the economic or ‘business’ benefits of the Scheme have already been realised.

## THE NUMBER OF COMPLAINTS ABOUT, AND OBJECTIONS TO, THE SCHEME

7.46 Under the Prudential Rothesay Scheme, around 1,000 of the responses received could be classified as objections and this was considered a significant level of objections from policyholders even though it only amounted to around 0.4% of total communications (Prudential sent out approximately 250,000 communications packs to policyholders).

7.47 As at 5 January 2020, total objections for the proposed Scheme were:

- 1,129 from unique LGAS policyholders which equates to less than 0.2% of total communications to LGAS policyholders (note that many individual policyholders raised objections on multiple topics)
- 56 from ReAssure policyholders which equates to less than 0.01% of total communications to ReAssure policyholders.

7.48 At the present time there are 33 policyholders who have indicated they will appear in Court.

7.49 At an overall rate of less than 0.1% I do not consider the number of policyholder objections to be significant in the context of the total number of communications.

7.50 Further information on the correspondence and objections received from policyholders is provided in Section 8 of this report.

#### **OVERALL CONCLUSIONS REGARDING THE RECENT JUDGMENT ON THE PRUDENTIAL/ROTHESAY SCHEME**

7.51 As set out in this section of the Supplementary Report, I have considered the key features that Snowden J identified as weighing against the sanctioning of the Prudential Rothesay scheme.

7.52 While some of the factors which influenced the judgment on the Prudential Rothesay scheme are relevant to the LGAS ReAssure Scheme, in my view none applies to the LGAS ReAssure Scheme to the same extent as to the Prudential Rothesay scheme, and the overall relevance of these factors in combination is much reduced.

7.53 I am satisfied that the conclusions of my Main Report are unaffected by the judgment in the Prudential Rothesay scheme.

## 8. Correspondence and objections received from policyholders

### INTRODUCTION

- 8.1 Following the Directions Hearing on 11 July 2019 and in accordance with the Scheme communication proposal, subject to the specific waivers received, a communication pack was sent to all transferring LGAS policyholders (approximately 0.7 million policyholders) and a letter was sent to all existing ReAssure policyholders (approximately 1.7 million policyholders).
- 8.2 LGAS and ReAssure have received comments on the Scheme from policyholders via email, letter and through their call centre and I have been provided with copies of the correspondence with policyholders up to 16 February 2020 in respect of the Scheme, including all enquiries, objections and transcripts of phone calls and letters where necessary.
- 8.3 At the time of writing this report, there have been 1,195 formal objections to the Scheme by policyholders (of both LGAS and ReAssure), 47 of which have requested presentation of their objections in person to the High Court during the Sanction Hearing.
- 8.4 The 1,141 formal objections received from transferring LGAS policyholders cover a range of issues including:
- Customer loyalty to LGAS (347 instances) and concerns with respect to ReAssure as a provider of life insurance and pensions (542 instances);
  - The Part VII transfer process (195 instances);
  - The treatment of policyholders after the transfer (206 instances);
  - The policy specifics (147 instances);
  - Non-specific concerns relating to the transfer (214 instances);
- 8.5 However, of the policyholders who have logged an objection, 271 no longer hold in-force transferring policies.
- 8.6 The 54 formal objections received from existing ReAssure policyholders largely fall into the following categories:
- The impact of the transferring business on their existing policy in terms of security of benefits, risk profile changes, benefit expectations and service levels (73 instances); and,
  - The notice provided to policyholders and the provision of information (12 instances).
- 8.7 Where individual policyholders raised an objection on multiple topics LGAS and ReAssure recorded these as separate objection themes and therefore the total number of objection instances shown across the above themes accounts for more than the total number of formal objections.
- 8.8 I have reviewed a summary of each objection received by LGAS and ReAssure and for a sample of objections I have reviewed the full correspondence with the objector. I have also reviewed the approach by which the firms have categorised the objections and I consider the approach taken to appropriately cover the variety of objections received.
- 8.9 Additionally, I have also commented on the following two topics that arose as a result of policyholder responses to the proposed Scheme:
- The effect of the Scheme on coverage by the FSCS; and
  - The migration of the LGAS policies to ReAssure.
- 8.10 I have addressed each of these areas below.
- 8.11 As set out in Section 5, Phoenix recently announced its intention to purchase RGP. At the time of writing this has led to 21 objections from policyholders (20 to LGAS and 1 to ReAssure). All policyholders who have made objections have been written to and apprised of this change in circumstances, as well as being made aware of the new

proposed date of the transfer. My analysis of the impact of this proposed purchase is set out in Section 5 of this report.

## **CUSTOMER LOYALTY TO LGAS AND CONCERNS REGARDING THE STRENGTH OF REASSURE**

### **Introduction**

8.12 Objections were raised by LGAS policyholders in respect of the perceived relative strengths of LGAS and ReAssure. These can be summarised as follows:

- A perception that ReAssure is not financially strong (particularly relative to LGAS) and that LGAS would be better equipped to absorb losses.
- The reputation and brand strength of LGAS was better than that of ReAssure:
  - It was unfair to transfer policyholders out of LGAS as they had chosen LGAS because of its reputation and because they felt it could be trusted with their investments.
  - LGAS had more brand recognition than ReAssure and there was a lack of awareness of ReAssure in the insurance and pensions market.
- The L&G Group would be more inclined to protect its name by not allowing LGAS to fail.
- A perception that ReAssure has a bad reputation in terms of customer service and/or previous experience of ReAssure has been negative, particularly in relation to policies transferring as part of other schemes and concern that there would be a reduction in service levels immediately following the transfer
- Concern around the recent suspension by the Swiss Re Group of the IPO of RGP and the prospect of an IPO in the future.

8.13 I cover these in turn below.

### **The perceived strength of ReAssure relative to LGAS**

8.14 Some policyholders had not heard of ReAssure and were concerned as to the relative strength, and ability to withstand adverse scenarios, of ReAssure when compared to LGAS.

8.15 Reputation, length of existence, brand recognition and size are metrics that are accessible to policyholders and it is understandable that these are used as proxies for the financial strength and security provided by a life insurer.

8.16 However, I have been provided with detailed financial information in respect of ReAssure including the effect of various adverse scenarios on the financial strength of the company and I set out my analysis in Section 8 of my Main Report and in Section 2 in this report. My conclusions in all cases were that if the Scheme were to be implemented, there would be no material adverse impact on the security of policyholder benefits, the reasonable expectations of policyholders in respect of their benefits or the standards of administration, service, management and governance applying to the transferring policies.

8.17 Therefore, I am satisfied that ReAssure would be no less strong or trustworthy a provider for the transferring policyholders than LGAS.

8.18 I have commented further on this point in Section 7 in relation to the recent judgment on the Prudential Rothesay Scheme.

### **The reputation and brand strength of LGAS**

8.19 ReAssure is a closed-book consolidation company and therefore is not open to new business. Consequently, ReAssure does not market its services to the public and so it would be expected that ReAssure would not be as well-known to policyholders as LGAS as a provider of insurance and pension services.

8.20 In my assessment in Section 8 of my Main Report, I concluded that the Scheme would not result in a material detriment to the transferring policyholders in terms of the security of policyholder benefits, policyholders' reasonable

expectations in respect of their benefits and the level of governance, servicing and administration applying to the transferring policies. I do not consider the relative brand strengths of LGAS and ReAssure to affect these conclusions.

8.21 Furthermore, ReAssure's origins can be traced back over 50 years and, as set out in Section 5 of my Main Report, it has been successfully undertaking large acquisitions of closed blocks of in-force life insurance business since 1983. It therefore has a long and proven track record in this area of business, which should be of some comfort to policyholders who are unfamiliar with the company.

#### **The L&G Group would be more inclined to protect its name by not allowing LGAS to fail**

8.22 As set out in Section 8 of my Main Report and Section 2 of this report,

- The security of the benefits under the policies within a firm arises primarily from the financial strength of the firm itself and its ability to withstand severe and extreme events; and
- The availability of support from the group companies or from a parent company provides extra financial strength and security for the policy benefits in the event that this extra security is required because the faith placed in the financial strength of the firm proves to be misplaced.

8.23 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 either:

- ReAssure supported by the Swiss Re Group and MS&AD if the Phoenix Group purchase of RGP were not to proceed; or
- ReAssure supported by the Phoenix Group if the Phoenix Group purchase of RGP were to proceed.

8.24 As set out in Section 8 of my Main Report, the parent/group company in an insurance group would, in all but the most extreme scenarios, provide support if and when required and 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.

8.25 As set out in Sections 2 and 5 in this report, the Phoenix Group, the Swiss Re Group and MS&AD are well capitalised with strong ratings from external, independent ratings agencies and I am satisfied that if the Scheme were to be implemented the change in the provision of parental support for the transferring LGAS policies is such that there would not be a material adverse effect on the security of the benefits guaranteed under those policies whether or not the proposed purchase of RGP by Phoenix proceeds.

#### **Concern that there would be a reduction in service levels immediately following the transfer**

8.26 In Sections 8, 10, and 11 of my Main Report I considered the effect of the transfer on the standards of administration, service, management and governance applying to the transferring policies, the existing policies of ReAssure and the non-transferring policies of LGAS.

8.27 In each case I concluded that if the proposed Scheme were to be implemented there would be no material adverse effect on the standards of administration, service, management and governance that would apply to these policies.

8.28 There was a particular concern from policyholders that were due to retire close to the Effective Date that the systems migration activities could lead to disruptions in respect of the retirement process.

8.29 I am satisfied that there would not be a material adverse effect on the service and administration levels received by policyholders due to the following:

- The conclusions in the First KPMG Report and the Second KPMG Report as set out in as set out in Section 4 of this report; and
- I have seen the cutover plans of LGAS and ReAssure with respect to the systems migration and I am satisfied that sufficient preparatory work has been performed to limit the effect of any disruption.



### **The suspension of the ReAssure IPO**

- 8.30 In Section 12 of my Main Report, I considered the effect of the proposed IPO of ReAssure on my conclusions and concluded that the occurrence of the proposed IPO would not change my conclusions.
- 8.31 In an addendum to my Main Report, I commented on the effect of the subsequent suspension of the proposed IPO on my conclusions.
- 8.32 Since this time, Phoenix has announced its intention to purchase RGP from Swiss Re Group and MS&AD and I have considered the effects of this development in Section 5 of this report.

### **Conclusion**

- 8.33 I am satisfied that the objections raised by LGAS policyholders in respect of the perceived relative strengths of LGAS and ReAssure do not provide any reason to change the conclusions of my Main Report.

### **OBJECTIONS IN RESPECT OF THE PART VII PROCESS**

#### **Introduction**

- 8.34 A number of objections were raised by transferring policyholders relating to concerns around the Part VII transfer process. The points raised were:
- Whether the Independent Expert could be considered to be independent;
  - Dissatisfaction regarding the notice provided to policyholders and the provision of information;
  - Dissatisfaction that LGAS did not request the permission of policyholders; and
  - Dissatisfaction that policyholders did not get to vote on the transfer or receive compensation for the transfer.

- 8.35 I have considered each of these topics below.

#### **Whether the Independent Expert could be considered independent**

- 8.36 Some policyholders questioned whether the Independent Expert could genuinely be considered to be independent, given that the costs associated with the role were being paid by LGAS and ReAssure.
- 8.37 My appointment was approved by the PRA after consultation with the FCA, and I believe that, as set out in Section 1 of my Main Report, I am suitably independent, qualified and experienced having been the independent expert in a number of other schemes. There is no realistic alternative to LGAS and ReAssure paying my costs.
- 8.38 I confirm that I am aware of, and have complied with, the requirements applicable to experts as set out in the appendices to my Main Report and I confirm that I have understood, and have complied with, my duty to the High Court.

#### **Dissatisfaction regarding the notice provided to policyholders and the provision of information**

- 8.39 Transfers of insurance business are subject to a legal process under Part VII of FSMA. The guidance in Chapter 18 of the Supervision Manual 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" specifies that policyholder communications are required to be sent at least six weeks ahead of the Sanction Hearing Date and LGAS and ReAssure have sent out their policyholder packs well in advance of this required time.
- 8.40 I reviewed the policyholder communications and was satisfied that they were fit for purpose.

#### **Dissatisfaction that LGAS did not request the permission of policyholders**

- 8.41 Under Part VII of FSMA, companies are able to undertake a transfer of insurance business but are required to obtain High Court approval to do so. This legislation means companies do not have to obtain prior consent for the transfer from each transferring policyholder. Instead, an Order must be sought from the High Court to transfer all of

the relevant policies, and it is for the High Court to determine whether it is fair to affected policyholders (and more widely, appropriate in all circumstances of the case) to grant such an Order.

#### **Dissatisfaction that policyholders did not get to vote on or receive compensation for the transfer.**

8.42 Under the Part VII process, there is no requirement for policyholders to have a vote on or receive compensation in relation to a proposed transfer and, for the avoidance of doubt, the Prudential Rothesay judgment described in Section 7 of this report does not alter this position.

8.43 Although the consent of policyholders is not required under this process, as set out in Section 4 of my Main Report policyholders involved in UK insurance business transfers have four main layers of protection provided by the legal and regulatory system in the UK:

- 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 the High Court; and
  - Approve the form of the notices which are published and sent to policyholders.

- The Independent Expert.

He/she is appointed to assess the Scheme and owes statutory duties to the High Court in respect of the (publicly available) Scheme Report assessing the Scheme for the Directions Hearing 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.

This policyholder communication process is reviewed by the Regulators and, as in the present case, by the High Court at the Directions Hearing. Any person who considers they may be adversely affected by the Scheme may make a representation to the High Court.

- The High Court.

The High Court must determine whether it is appropriate to sanction the scheme.

There are two High Court Hearings: the Directions Hearing and the Final (or Sanction) Hearing. The High Court reviews the Scheme at the Final Hearing where it 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.

8.44 The High Court has repeatedly endorsed the robustness of these safeguards in many schemes over the years.

#### **Conclusion on objections raised in respect of the Part VII process**

8.45 I am satisfied that the objections raised by LGAS policyholders in respect of concerns around the Part VII transfer process do not provide any reason to change the conclusions of my Main Report.

#### **THE TREATMENT OF POLICYHOLDERS AFTER THE TRANSFER**

8.46 A number of objections were raised by transferring policyholders relating to concerns around the treatment of policyholders after the transfer.

#### **Concerns relating to the treatment of policyholder policies and their benefits**

8.47 In Section 8 of my Main Report, I considered the effect of the Scheme on the security of policyholder benefits, policyholders' reasonable expectations in respect of their benefits and the level of governance, servicing and administration applying to the transferring policies.

- 8.48 I concluded that there would be no material adverse impact as a result of the transfer and in particular that:
- The transferring policyholders would 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, the Scheme would not have a material adverse effect on the range of funds available or the management, investment objectives, charges and pricing applicable to those funds;
  - In respect of with-profits policies, the Scheme would not have a material adverse effect on the level of discretionary benefits applied, the charges taken, the link between bonuses received and investment performance, and the levels of smoothing applied; and
  - In respect of non-profit policies, the Scheme would not have a material adverse effect on the likelihood that policyholders receive their benefits when due or the size or frequency of those benefits.

#### **Concerns that investment performance will deteriorate following the transfer**

- 8.49 There were some objections raised on the basis that it was felt that, following the transfer, ReAssure would not be able to manage the assets in the same way as LGAS and therefore policyholder benefits would be lower than they may have otherwise been. Reasons given for this included that ReAssure is not as large as LGAS and would therefore not benefit in the same way from economies of scale and that, since ReAssure is not open to new business, it would be less focused on providing competitive returns for its policyholders in order to protect its reputation.

- 8.50 In Section 8 of my Main Report, I explained that the investment management of the transferring policyholder assets would remain with LGIM following the implementation of the Scheme for a period of at least seven years and that sufficient safeguards exist to ensure that investment performance and management fees would remain competitive. Further, the funds that the transferring policyholder assets are invested in would be directly replicated within ReAssure. I therefore concluded that there would be no material adverse impact as a result of the Scheme on the reasonable expectations of the policyholders in respect of their benefits.

#### **Concern that there will be changes to policy terms and relevant charges following the transfer**

- 8.51 Objections were raised in relation to concerns around ReAssure's intentions with regard to changing policy terms in its favour and increasing charges.
- 8.52 In Section 9 of my Main Report, I discussed a number of changes to the term and conditions with respect to the transferring with-profits, unit-linked and conventional non-profit products that ReAssure proposes to make following the implementation of the Scheme and I concluded that these changes would not have a material adverse effect on the transferring policies.

#### **Conclusion**

- 8.53 I am satisfied that the objections raised by LGAS policyholders in respect of concerns around the treatment of policyholders after the transfer do not provide any reason to change the conclusions of my Main Report.

#### **OBJECTIONS RELATING TO POLICY SPECIFICS**

- 8.54 Objections were raised by transferring policyholders relating to various concerns around the transfer that are linked to the specifics of the policyholders and policies in question. Examples of such objections relate to the following:
- With-profits policyholders who were concerned that implementation of the Scheme would adversely affect them. Specific concerns were regarding the potential impact of:
    - Changes to the management of the with-profits business (including changes to the bonus methodology, capital management and principles and practices documentation);
    - The new Fixed Expense Agreement in respect of the LGWPF replacing the existing agreement in respect of the LGAS WPF and the £50 million contribution to migration costs;

- The introduction of the reallocation clause (clause 19) in the Scheme; and
- The introduction of sunset clauses in relation to the LGWPF.
- Concern that the online portal solution being put in place by ReAssure would not be of the same standard of that currently in LGAS; and
- Have both transferring and non-transferring policies with LGAS, and did not want these policies being split across two companies.

8.55 I cover these in turn below.

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

8.56 In Section 8 of my Main Report I considered the likely effects, if the Scheme were to be implemented, on the following aspects of management of the transferring with-profits business:

- The ReAssure staff and corporate bodies responsible for the management of the with-profits business including:
  - The ReAssure Board;
  - The Reassure With-Profits Management Committee;
  - The ReAssure Fairness Committee;
  - Other ReAssure governance and management committees such as the GMRC and the IGC; and
  - The ReAssure With-Profits Actuaries.
- The new PPFM that would apply to the transferring business.
- Risk management at ReAssure.

8.57 I concluded that I was 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 and the events since do not provide any reason to change the conclusions in my Main Report.

#### **The Fixed Expense Agreement and £50 million contribution to migration costs**

8.58 Some concerns were raised in relation to the one-off payment of £50 million by the LGWPF to the RNPF as part of the new Fixed Expense Agreement.

8.59 As set out in Section 5 of my Main Report there is currently in place a fixed expense agreement under which LGAS agreed to cap the expense exposure of the LGAS WPF for a temporary period and if the proposed Scheme were to be implemented, a new fixed expense agreement (the Fixed Expense Agreement) would be set up for the LGWPF within ReAssure which would last until the last policy in the LGWPF runs-off.

8.60 The Fixed Expense Agreement sets out an annual per-policy fee that ReAssure will charge the LGWPF and this fee will increase in line with the Retail Price Index, plus 0.5% per annum. This annual fee is paid for services provided to the LGWPF by ReAssure in the administration and maintenance of the fund.

8.61 The Scheme specifies that a one-off, fixed payment of £50 million should be paid from the LGWPF to the ReAssure Non-Profit Fund as a contribution to the costs of the migration of the business. 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.

8.62 I covered the effects of the Fixed Expense Agreement and the £50 million one-off payment in Section 8 of my Main Report and the LGAS WPA and the LGAS WPC have reviewed the Fixed Expense Agreement for the LGWPF and are 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.

8.63 I concluded 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 and there is no reason to change that conclusion.

#### **The introduction of the reallocation clause (clause 19) in the Scheme**

8.64 If the proposed Scheme were to be implemented, clause 19 (Re-Allocation of Policies) of the Scheme would allow ReAssure to re-allocate any non-participating business within the LGWPF into the RNPF.

8.65 Clause 19 is intended to enable ReAssure, if the Scheme were to be implemented, to take the same type of actions as LGAS is able to currently undertake in respect of the transferring LGAS business in relation to non-participating business. As such, I am comfortable that the inclusion of this clause in the Scheme would not be unfair to the transferring LGAS policyholders.

8.66 If ReAssure were to wish to undertake a re-allocation in accordance with this clause 19 ReAssure would have to ensure that any such reallocation would be:

- Consistent with the terms of the policies and applicable laws and regulations;
- Subject to consultation with the ReAssure Fairness Committee and the approval of the ReAssure Board; and
- Such that it did not have a material adverse impact on affected policyholders when considering the aggregate impact of any other re-allocations in the preceding five years and any planned allocations in the following five years.

8.67 As such, I am comfortable that the inclusion of this clause in the Scheme would not be a material change for the transferring policies and that any reallocation carried out under this clause would be subject to appropriately robust safeguards to ensure that there would not be a material adverse effect on the transferring LGAS policyholders.

#### **The introduction of the sunset clauses in relation to the LGWPF**

8.68 In Section 8 of my Main Report I used the phrase 'sunset clauses' to refer to the clauses (20 and 22) in the Scheme that set out the actions available and necessary if the assets held within the LGWPF were to 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.

8.69 In addition, the Scheme allows for the possibility that the LGWPF could absorb one or more of the existing with-profits funds of ReAssure.

8.70 As set out in Section 8 of my Main Report, 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 Agreement 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.

8.71 The sunset clauses have been included in the Scheme for the following reasons:

- They would allow ReAssure to take remedial action if it were to become economically inefficient to run the LGWPF on a stand-alone basis as a result of diseconomies of scale and the tontine effects that would arise as the assets of the LGWPF decreased over time. These inefficiencies would include:
  - Increased difficulties in sharing profits and losses across policies in an equitable manner;
  - Increased difficulties in 'smoothing' benefits in line with the LGWPF's established approach to minimise volatility in policyholder returns over time;
  - Increased difficulties in maintaining an estate distribution that is fair across different generations of policyholders; and
  - Increased difficulties in maintaining the existing asset mix within the LGWPF.
- Note that rising costs due to diseconomies of scale would not be an issue because of the Fixed Expense Agreement described above.
- Some of these benefits would not be achievable for the LGAS WPF currently. For example, in contrast to ReAssure, Legal & General only operates a single with-profits fund, and so it does not have the ability to merge with-profits funds to achieve greater economies of scale.
- The sunset clauses would improve the stability of returns for transferring policyholders during the latter stages of run-off.

8.72 I am satisfied that the inclusion of the sunset clauses in the Scheme should be to the advantage of transferring policyholders for the reasons given above and I consider the safeguards in place 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. Therefore I am satisfied that the inclusion of these sunset clauses would not lead to a material adverse effect on the reasonable expectations of the transferring with-profits policyholders in respect of their benefits.

#### **The ReAssure online portal**

8.73 LGAS's subject matter experts are satisfied that the ReAssure portals will be at least as good as the current LGAS portal.

8.74 Furthermore, ReAssure is committed to future investment, development and improvement in functionality in relation to the online portals in order to best manage its closed-book business over time and meet the needs of these policyholders.

8.75 I am therefore satisfied that the conclusions outlined in Section 8 of my Main Report remain unchanged.

#### **Policyholders with both transferring and non-transferring policies with LGAS**

8.76 As set out in my Main Report, I am satisfied that the implementation of the Scheme would not have a material adverse effect on:

- The standards of administration, service, management and governance that apply to the transferring LGAS policies (Section 8 of my Main Report); and/or

- The standards of administration, service, management and governance that apply to the non-transferring LGAS policies (Section 11 of my Main Report).

8.77 Therefore, although it would be a change for policyholders to have policies with two providers where previously they had one provider, I do not consider this to be a material adverse change as they will continue to receive the appropriate documentation in respect of each policy from the relevant provider.

### **Conclusion**

8.78 I have reviewed all of these policy specific objections and I have raised queries with LGAS and ReAssure where I have deemed it necessary and I am satisfied that these objections do not provide any reason to change the conclusions of my Main Report.

### **THOSE FROM EXISTING REASSURE POLICYHOLDERS**

8.79 Objections were raised by existing ReAssure policyholders relating to concerns about:

- The impact of the transferring business on their existing policy in terms of security of benefits, risk profile changes, benefit expectations and service levels; and
- The notice provided to policyholders and the provision of information.

8.80 In Section 9 of my Main Report, I considered the effect of the Scheme on the security of policyholder benefits, policyholders' reasonable expectations in respect of their benefits and the level of governance, servicing and administration applying to the existing ReAssure policies. I concluded that there would be no material adverse impact as a result of the transfer.

8.81 As mentioned above, transfers of insurance business are subject to a legal process under Part VII of FSMA. The point at which policyholders are informed of the proposed transfer, and provided with the relevant communications pack, forms a part of this legal process and ReAssure and LGAS met the requirements as specified in FSMA.

8.82 I am satisfied that the objections from existing ReAssure policyholders do not provide any reason to change the conclusions of my Main Report.

### **THE EFFECT OF THE SCHEME ON COVERAGE BY THE FSCS**

8.83 A number of policyholders asked about the coverage of the FSCS and the likely effect of the Scheme on coverage of their policy under the FSCS.

8.84 If the Scheme were to be implemented there would be no effect on the eligibility of any of the policyholders of LGAS or ReAssure for compensation from the FSCS. That is, they would be covered at the same level as they would have been if the proposed scheme had not been implemented.

### **CONCERNS AROUND THE PROGRESS OF THE DATA MIGRATION AND ITS EFFECTS**

8.85 I have considered the effect of the data migration on the levels of administration and servicing applying to the transferring policyholders following the implementation of the Scheme in Section 4 of this report.

### **CONCLUSION**

8.86 I am satisfied that LGAS and ReAssure are dealing with the objections received in a reasonable way and are doing what they can to resolve these fully prior to the Sanction Hearing.

8.87 The policyholder objections received do not raise any issues that were not considered in the work leading up to my Main Report and therefore I am satisfied that the objections do not provide any reason to change the conclusions of my Main Report.

## 9. Other considerations in respect of the proposed Scheme

### THE DEPARTURE OF THE UK FROM THE EUROPEAN UNION – “BREXIT”

- 9.1 At the time of finalisation of my Main Report, the UK was scheduled to leave the European Union no later than 31 October 2019.
- 9.2 The UK formally left the European Union on 31 January 2020 and is now in a transition period with the European Union until 31 December 2020.
- 9.3 There remains uncertainty as to what form that exit might ultimately take following the transition period and in particular, it is not certain whether Solvency II will remain the governing insurance regulatory regime after the UK’s exit from the EU.
- 9.4 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.
- 9.5 Even if changes to the regime are made over time, as both LGAS and ReAssure are established in the UK, they would continue to be regulated subject to the same rules as determined by UK legislation and the UK regulators.

### THE POLICYHOLDER COMMUNICATIONS

- 9.6 LGAS received a waiver from the requirement to communicate directly with the non-transferring policyholders of LGAS in respect of the Scheme. Further waivers were received by both ReAssure and LGAS for various subsets of policyholders and these are discussed in detail in Section 13 of my Main Report.
- 9.7 Following the Directions Hearing on 11 July 2019 and in accordance with the Scheme communication proposal:
- A communication pack was sent to all transferring LGAS policyholders (subject to the specific waivers received).  
  
The communications pack included an explanatory letter specific to the policy held by the policyholder and a standardised Scheme brochure which included a summary of the Scheme, a summary of my Main Report, questions and answers on the Scheme, and a copy of the legal notice to the High Court. The pack included information on the procedure for policyholders to follow if they would like to object to the transfer.
  - A letter was sent to all existing ReAssure policyholders (subject to the specific waivers received).  
  
The letter provided the conclusions from my Main Report in respect of the existing ReAssure policyholders and information regarding the ReAssure website where policyholders can view or download the key documents in respect of the Scheme.
- 9.8 The Scheme was also publicised via:
- The LGAS and ReAssure websites.
  - Notices 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, The Financial Times and The Daily Mail.
  - Notices in a form approved by the PRA in the following international publications:
    - The Times – International;
    - The Daily Mail – Spain, Northern Europe and Greece; and



- The Financial Times – Continental Europe, US and Asia.
- Notices in respect of the Guernsey Scheme in the following publications:
  - La Gazette Officielle in Guernsey
  - The Alderney Gazette in Alderney; and
  - The Sark Public Notice Box in Sark.
- A notice in respect of the Jersey Scheme in the Jersey Gazette

9.9 This Supplementary Report will also be made available on the LGAS and ReAssure websites.

#### **NOTIFICATION OF EEA STATES**

9.10 LGAS and ReAssure asked the PRA to notify the supervisory authorities in all EEA states of the proposed Scheme.

9.11 At the time of writing this report, there have been no objections from supervisory authorities.

#### **CHANGES TO THE SCHEME**

9.12 There have been a small number of minor changes to the Scheme since the submissions for the Directions Hearing in July 2019.

9.13 The most significant change was the postponement of the Legal Effective Date and the Economic Effective Date to 6 April 2020 and 1 April 2020 respectively.

9.14 I have reviewed these changes and I am satisfied that none of them alter the conclusions outlined in Section 8 of my Main Report.

#### **CHANGES TO THE REASSURE REINSURANCE ARRANGEMENTS**

9.15 Since the time of finalisation of my Main Report, ReAssure has decided (subject to full governance approvals) to recapture a number of reinsurance treaties relating to the transferring business, including two reinsurance treaties between LGAS and the Swiss Re Group relating to the business in the LGAS WPF, immediately following the implementation of the Scheme.

9.16 The principles for the recapture have been subject to ReAssure's normal internal governance processes, including a review by the ReAssure Fairness Committee; however, the final recapture calculations remain subject to review by the LGWPF WPA and Fairness Committee and to formal approval once available. The current LGAS WPA has also reviewed the principles and terms for the recapture and is comfortable that it should not have any material impact on the transferring with-profits policyholders.

9.17 ReAssure has provided me with documentation on the principles and terms for the proposed recapture, alongside evidence of the internal review and governance to which it is subject. In light of this information, the low materiality of the reinsurance treaties in question and the conclusions of the LGAS WPA with respect to the recapture, I am satisfied that the recapture does not provide any reason to change the conclusions in my Main Report.

#### **THE REASSURE ONLINE PORTAL**

9.18 As outlined in Section 8 of my Main Report, ReAssure has been developing two online portals called 'RAL Now' and 'ReAct' for use by transferring policyholders and sponsoring employers of occupational pension schemes respectively.

9.19 At the time of finalisation of my Main Report the testing to ensure that the functionality provided by these portals is equivalent to that currently provided by LGAS had not been completed.

9.20 I have now been informed that the functionality testing has been completed for the RAL Now portal and that it is in use by ReAssure policyholders. I have seen a report from LGAS subject matter experts and stakeholders outlining

the conclusions from its review of the portals that indicates that the functionality will achieve equivalent or better results than are currently achieved with the LGAS portal.

- 9.21 The only functionality that will not be available immediately will be the ability for customers to opt out of paper statements, however, this is in ReAssure's development plans.
- 9.22 The functionality testing for the ReAct portal is still ongoing but this is included within the conclusions made by KPMG that are shown in Section 3 of this report.
- 9.23 Furthermore, ReAssure is committed to future investment, development and improvement in functionality in relation to the online portals in order to best manage its closed-book business over time and meet the needs of these policyholders.
- 9.24 I am therefore satisfied that the conclusions outlined in Section 8 of my Main Report remain unchanged.

#### **THE REASSURE LIQUIDITY POLICY**

- 9.25 As outlined in Section 8 of my Main Report, ReAssure had amended its liquidity policy to include a commitment to maintain the prevailing liquidity management standard for the transferring LGAS WPF business in the medium term. However at the time of finalisation of my Main Report this amendment had not been through the required governance processes, and in particular it had not been approved by the ReAssure Board.
- 9.26 I have now been informed that the amended liquidity policy has received the required sign-off from the RGP Board and that the risk policies apply to all group entities and therefore the conclusions with respect to the change in the profile of risks to which the transferring policies are exposed remain unchanged.

#### **THE AMENDMENT AGREEMENT TO THE BUSINESS TRANSFER AGREEMENT AND THE SPLIT EFFECTIVE DATE AGREEMENT**

- 9.27 In Section 5 of my Main Report I outlined a number of additional items that had been agreed between ReAssure and LGAS since the initial Business Transfer Agreement was signed. An amendment agreement had been drafted (and termed the "BTA side-letter"). However, at the time of the finalisation of my Main Report the BTA side-letter had not been finalised.
- 9.28 I have now been provided with the final BTA side-letter, which was signed on 12 July 2019, and there are no material changes relative to those outlined in my Main Report. Therefore I am satisfied that my conclusions, as outlined in my Main Report, are unaffected by the finalisation of the BTA side-letter.
- 9.29 The Split Effective Date Agreement was also signed at the same time as the BTA side-letter. This includes provisions for:
- The application of financials between LGAS and ReAssure during the period between the Economic Effective Date and the Legal Effective Date (the "**Interim Period**");
  - The process by which LGAS and ReAssure will sign the transfer certificate for the Scheme; and
  - The conduct of business and expenses relating to the transferring business during the Interim Period.
- 9.30 I have reviewed the Split Effective Date Agreement and I am satisfied that my conclusions, as outlined in my Main Report, are unaffected by the finalisation of this agreement.

#### **THE TARGET OPERATING MODEL FOR THE DERIVATIVES WITHIN THE TRANSFERRING FUNDS**

- 9.31 Since the finalisation of my Main Report, there have been some process changes to the operating model for assets (including derivatives) that would be in place after the implementation of the proposed Scheme.
- 9.32 These changes are not, in the view of the LGAS WPA and the LGAS Chief Actuary, material and I do not expect the ReAssure asset operating model to result in any material detriment to policyholders when compared with the current operating model in LGAS.

### **THE COMPENSATION PAYMENT FOR THE UNIT-LINKED BOX**

- 9.33 As outlined in Section 8 of my Main Report, with effect from the Economic Effective Date ReAssure intends to transfer the unit-linked box that currently resides in the LGAS WPF into the RNPF. As the time of finalisation of my Main Report, the approach to the valuation of the unit-linked box had not been agreed and so the approach for calculating the consideration payment to be made from the RNPF to the LGWPF upon transfer of the unit-linked box had not been determined.
- 9.34 The BTA side-letter outlines the agreed approach to the valuation methodology. I have reviewed this approach and I am comfortable that the approach is in line with standard industry valuation techniques and is fair to the transferring with-profits policyholders.
- 9.35 At the time of the calculation of the consideration payment, to ensure that the calculation methodology is appropriately applied and the consideration payment is fair, it will need to be subject to review by the ReAssure Fairness Committee and recommendation to the ReAssure Board for approval.

### **THE MANAGEMENT OF THE UNIT-LINKED FUNDS WITHIN REASSURE**

- 9.36 At the time of finalisation of my Main Report, ReAssure was in the process of producing a customer-facing ReAssure unit-linked guide (the "ReAssure Unit-Linked Guide") for the transferring business and developing its existing internal unit-linked principles and practices documentation to ensure that its future management of unit-linked funds is consistent with the approach currently taken by LGAS.
- 9.37 The ReAssure Unit-Linked Guide and the updated unit-linked principles and practices documentation have since been finalised, approved by the ReAssure Unit Pricing Committee and reviewed by the ReAssure Fairness Committee. They have also been shared with LGAS and subject to review by the LGAS Chief Actuary, who has concluded that ReAssure's proposed management of unit-linked funds does not present a material detriment to the benefit expectations of the transferring policyholders.
- 9.38 I have reviewed the final ReAssure Unit-Linked Guide and unit-linked principles and practices documentation and, in light of my review, the review and governance that has taken place within ReAssure, and the conclusions of the LGAS Chief Actuary, I am satisfied that the conclusions in my report are unaffected by this development.

## 10. My conclusions

10.1 I prepared my Main Report dated 3 July 2019 in which I considered the proposed Scheme based on information available at that time and the purpose of this Supplementary Report is to provide an updated assessment of the likely effects of the proposed Scheme ahead of the Sanction Hearing on 9 March 2020.

10.2 I have considered whether anything has happened since the date of finalisation of my Main Report, including the updated financial information as at 30 June 2019 and the pro forma figures showing ReAssure and LGAS if the Scheme had been implemented on that date, that would cause me to change the conclusions in my Main Report.

10.3 In summary:

- The updated financial information (Section 2 and Section 3).

Based on the financial information for LGAS and ReAssure as at 30 June 2019, I remain satisfied that the implementation of the Scheme would not have a material adverse effect on the security of the benefits of the transferring LGAS policies, the existing ReAssure policies or the non-transferring LGAS policies.

I am satisfied that the financial information as at 31 December 2019 does not provide any reason to change the conclusions of my Main Report.

- The data migration from LGAS to ReAssure (Section 4).

Considering the updates from ReAssure to date and the expert review conclusions from KPMG in the First KPMG Report and the Second KPMG Report, I can conclude that, at the date of finalisation of this report I am satisfied that it is unlikely that the migration will lead to a material adverse effect on policyholders going forward.

- The proposed purchase of RGP by the Phoenix Group (Section 5).

Since my Main Report was finalised, Phoenix has announced its intention to purchase RGP from Swiss Re Group and MS&AD and this will be subject to the approvals set out in Section 5.

I have considered the potential impact of the proposed purchase of RGP by Phoenix on my conclusions on the effects of the proposed Scheme on the various groups of policies and I am satisfied that the Phoenix purchase of RGP would not change the conclusions in my Main Report.

- The ReAssure purchase of OMWLA (Section 6).

I am satisfied that the OMWLA transaction does not provide any reason to change the conclusions in my Main Report.

- The recent judgment on the Prudential Rothesay Scheme (Section 7).

I have considered the key features that Snowden J identified as weighing against the sanctioning of the Prudential Rothesay scheme and while some of these are relevant to the LGAS ReAssure Scheme, in my view none applies to the LGAS ReAssure Scheme to the same extent as to the Prudential Rothesay scheme, and the overall relevance of these factors in combination is much reduced.

I am satisfied that the conclusions of my Main Report are unaffected by the judgment in the Prudential Rothesay scheme.

- Correspondence and objections received from policyholders (Section 8).

I am satisfied that LGAS and ReAssure are dealing with the objections received in a reasonable way and are doing what they can to resolve these fully prior to the Sanction Hearing and the policyholder enquiries received do not raise any issues that were not considered in the work leading up to my Main Report and therefore I am satisfied that there are no reasons to change the conclusions in my Main Report.

10.4 Therefore nothing has happened since the finalisation of my Main Report to provide any reason to change the conclusions in Section 15 of my Main Report that:

- 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 or 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.
- I am satisfied that the Scheme is equitable to all classes and generations of LGAS and ReAssure policyholders.

10.5 I shall provide a letter to the Court dated 6 March 2020 that will provide an update on the state of the migration at that date and the effect on the conclusions above.



Oliver Gillespie

24 February 2020

Partner of Milliman LLP

Fellow of the Institute and Faculty of Actuaries

## Appendix A – Solvency II financial information as at 30 June 2019 prior to the implementation of the Scheme

### LGAS SOLVENCY II FINANCIAL INFORMATION AS AT 30 JUNE 2019

£ million	Non-Transferring	Transferring Non-Profit	Transferring Unit-Linked	LGAS WPF	RTA	Total
<b>Assets<sup>1</sup></b>	<b>111,620</b>	<b>30</b>	<b>10,775</b>	<b>19,070</b>	<b>21</b>	<b>141,516</b>
<b>BEL</b>	<b>101,333</b>	<b>30</b>	<b>10,345</b>	<b>18,321</b>	<b>692</b>	<b>130,721</b>
<b>Risk margin</b>	<b>4,313</b>	<b>0</b>	<b>4</b>	<b>88</b>	<b>(4)</b>	<b>4,401</b>
<b>TMTP<sup>3</sup></b>	<b>(4,183)</b>	<b>0</b>	<b>(16)</b>	<b>(88)</b>	<b>0</b>	<b>(4,288)</b>
<b>Technical provisions</b>	<b>101,462</b>	<b>30</b>	<b>10,333</b>	<b>18,321</b>	<b>688</b>	<b>130,835</b>
<b>Own Funds</b>	<b>10,158</b>	<b>(0)</b>	<b>442</b>	<b>749</b>	<b>(667)</b>	<b>10,681</b>
<b>SCR</b>				<b>531</b>		<b>7,429</b>
<b>Excess Assets</b>				<b>218</b>		<b>3,253</b>
<b>Solvency coverage ratio</b>				<b>141%</b>		<b>144%</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 143%.
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 30 JUNE 2019

£ million	WLWPF	NMWPF	GAWPF	RNPF	Total
<b>Assets<sup>1</sup></b>	<b>511</b>	<b>1,489</b>	<b>1,951</b>	<b>37,049</b>	<b>41,001</b>
<b>BEL</b>	<b>437</b>	<b>1,338</b>	<b>1,531</b>	<b>32,383</b>	<b>35,688</b>
<b>Risk margin</b>	<b>8</b>	<b>14</b>	<b>16</b>	<b>1,352</b>	<b>1,391</b>
<b>TMTP</b>	<b>0</b>	<b>0</b>	<b>(16)</b>	<b>(727)</b>	<b>(743)</b>
<b>Technical provisions</b>	<b>445</b>	<b>1,352</b>	<b>1,531</b>	<b>33,008</b>	<b>36,336</b>
<b>Unrestricted Own Funds</b>	<b>67</b>	<b>137</b>	<b>420</b>	<b>4,041</b>	<b>4,664</b>
<b>SCR</b>	<b>11</b>	<b>31</b>	<b>130</b>	<b>2,691</b>	<b>2,863</b>
<b>Restriction to Own Funds</b>					<b>352</b>
<b>Excess Assets<sup>2</sup></b>	<b>57</b>	<b>106</b>	<b>290</b>	<b>1,350</b>	<b>1,449</b>
<b>Solvency coverage ratio</b>	<b>638%</b>	<b>442%</b>	<b>323%</b>	<b>150%</b>	<b>151%</b>

Notes:

1. Assets are shown net of current liabilities and deferred tax.
2. 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 – Solvency II financial information as at 30 June 2019 after the implementation of the Scheme

### LGAS POST-SCHEME BALANCE SHEET AS AT 30 JUNE 2019

£ million	Non- Transferring
<b>Assets<sup>1</sup></b>	<b>111,596</b>
<b>BEL</b>	<b>101,352</b>
<b>Risk margin</b>	<b>4,313</b>
<b>TMTP<sup>2</sup></b>	<b>(4,183)</b>
<b>Technical provisions</b>	<b>101,482</b>
<b>Own Funds</b>	<b>10,114</b>
<b>SCR</b>	<b>6,961</b>
<b>Excess Assets<sup>3</sup></b>	<b>3,153</b>
<b>Solvency coverage ratio</b>	<b>145%</b>

#### Notes:

- Assets are shown net of current liabilities and deferred tax.
- 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 also 145%.
- 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 30 JUNE 2019

£ million	WLWPF	NMWPF	GAWPF	LGWPF	RNPF	Total
<b>Assets<sup>1</sup></b>	<b>511</b>	<b>1,489</b>	<b>1,951</b>	<b>18,998</b>	<b>47,942</b>	<b>70,892</b>
<b>BEL</b>	<b>437</b>	<b>1,338</b>	<b>1,531</b>	<b>18,271</b>	<b>43,542</b>	<b>65,119</b>
<b>Risk margin</b>	<b>8</b>	<b>14</b>	<b>16</b>	<b>90</b>	<b>1,345</b>	<b>1,473</b>
<b>TMTP<sup>4</sup></b>	<b>0</b>	<b>0</b>	<b>(16)</b>	<b>(90)</b>	<b>(697)</b>	<b>(804)</b>
<b>Technical provisions</b>	<b>445</b>	<b>1,352</b>	<b>1,531</b>	<b>18,271</b>	<b>44,190</b>	<b>65,789</b>
<b>Unrestricted Own Funds</b>	<b>67</b>	<b>137</b>	<b>420</b>	<b>727</b>	<b>3,752</b>	<b>5,103</b>
<b>SCR<sup>5</sup></b>	<b>11</b>	<b>31</b>	<b>131</b>	<b>517</b>	<b>2,576</b>	<b>3,266</b>
<b>Restriction to Own Funds</b>						<b>352</b>
<b>Excess Assets<sup>6</sup></b>	<b>57</b>	<b>106</b>	<b>289</b>	<b>210</b>	<b>1,176</b>	<b>1,485</b>
<b>Solvency coverage ratio</b>	<b>638%</b>	<b>442%</b>	<b>323%</b>	<b>141%</b>	<b>146%</b>	<b>145%</b>

Notes:

- Assets are shown net of current liabilities and deferred tax.

The post-Scheme deferred tax calculations performed at 31 December 2018 have been scaled in line with the change in the ReAssure deferred tax assets and liabilities over the first half of 2019 and also allowing for relevant information from LGAS. The effect of this approximation is not material.

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 £29 million and £63 million are held in the RNPF for remaining 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 £13 million.

4. ReAssure has submitted an application to recalculate the TMTP to reflect the transferring business, which is subject to PRA approval. Based on the proposed methodology:
  - The TMTP 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 – 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 supplementary reports of the Chief Actuaries and With-Profit Actuaries of both LGAS and ReAssure on the proposed transfer
LGAS and ReAssure financial information as at 30 June 2019
LGAS and ReAssure estimated financial information as at 31 December 2019
ReAssure Change in Control application for the OMWLA transaction
ReAssure 10-year financial projections
Transaction agreements: the BTA side-letter and the Split Effective Date Agreement
Updated Scheme document
LGAS and ReAssure witness statements for the Sanction Hearing
Updated LGAS analysis of the economic benefit of the Fixed Expense Agreement for the LGWPF
Business readiness updates, including internal risk review results for ReAssure and updates on the ReAssure portal functionality
The KPMG reports on the operational readiness of ReAssure
The ReAssure CRO's Risk Management Carbyne T-30 Update
Information on the targeting operating model for derivatives in the LGAS WPF
Information on the recapture of reinsurance treaties relating to the transferring business
Analysis of potential disincentives to exit for transferring products
ReAssure Unit-Linked Guide and unit-linked principles and practices documentation

## Appendix D – Glossary of terms

A glossary of abbreviations used throughout the report is given below

### A

<b>AIA</b>	Annuity Introducer Agreement
<b>APS</b>	Actuarial Profession Standards
<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>CRO</b>	Chief Risk Officer
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### D

<b>Directions Hearing</b>	An initial Court hearing at which the companies' plans for notifying policyholders are considered
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### 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 April 2020
<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>	The European Economic Area
<b>EIOPA</b>	The European Insurance and Occupational Pensions Authority
<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

### F

<b>FCA</b>	Financial Conduct Authority
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<b>Final Hearing</b>	Also known as a 'Sanction 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>Fixed Expense Agreement</b>	If the proposed Scheme were to be implemented a new fixed expense agreement (the "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.
<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>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>I</b>	
<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>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>K</b>	
<b>KPMG</b>	KPMG LLP

## L

<b>L&amp;G Group</b>	Legal and General Group
<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 6 April 2020
<b>LGAS</b>	Legal and General Assurance Society Limited
<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 WPF</b>	The transferring with-profits fund within LGAS before the implementation of the Scheme
<b>LGAS WPF Business</b>	All of the business within the LGAS WPF
<b>LGIM</b>	Legal & General Investment Management
<b>LGR</b>	Legal & General Retirement
<b>LGWPF</b>	The newly created with-profits fund within ReAssure after the implementation of the Scheme, the LG With-Profits Fund

## M

<b>Milliman</b>	Milliman LLP
<b>MS&amp;AD</b>	MS&AD Insurance Group

## N

<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

## O

<b>OMWLA</b>	Old Mutual Wealth Life Assurance Limited
<b>Own Funds</b>	The excess of assets over liabilities under Solvency II

## P

<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>Phoenix</b>	Phoenix Group Holdings plc
<b>Phoenix Internal Model</b>	The internal model used by Phoenix for the calculation of its SCR
<b>PPFM</b>	Principles and Practices of Financial Management. A public document outlining how a with-profits fund is managed
<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>Prudential</b>	Prudential Assurance Company Limited

**PwC** PricewaterhouseCoopers LLP

## R

**ReAssure** ReAssure Limited

**ReAssure FC** 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

**ReAssure IPO RA Statement** A risk appetite statement agreed by the ReAssure Board that would apply if the ReAssure IPO were to go ahead.

However, although the ReAssure IPO did not proceed, at a Board meeting on 3 December 2019, ReAssure adopted the ReAssure IPO RA Statement.

**ReAssure PIM** ReAssure's Partial Internal Model

**ReAssure RA Statement** ReAssure's risk appetite statement

**RGP** ReAssure Group Plc

**Risk Margin** 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

**RNPF** ReAssure Non-Profit Fund

**Rothsay** Rothsay Life Plc

**RTA** Risk Transfer Agreement

**RUKSL** ReAssure UK Services Limited

## S

**Sanction Hearing** A hearing of the High Court to approve the terms of the Scheme prior to the effective date of the Scheme

**Scheme** 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

**Scheme Report** A report on the terms of the Scheme by an Independent Expert

**SCR** Solvency Capital Requirement

**Solvency coverage ratio** Own Funds divided by SCR

**Solvency II** Regulatory solvency framework for the European Economic Area insurance and reinsurance industry

**Split Effective Date Agreement** An agreement between LGAS and ReAssure regarding the splitting of the Scheme effective date between the Economic Effective Date and the Legal Effective Date.

**Standard Formula** EIOPA prescribed method of calculating SCR

**SUP 18** Chapter 18 of the Supervision Manual contained in the FCA Handbook

**Supplementary Report** A further report produced prior to the Final Hearing to provide an update for the 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

## T

**TAS** Technical Actuarial Standards

**TAS 200: Insurance** The Technical Actuarial Standards applicable to Insurance transformations (such as the Scheme), issued by the Financial Reporting Council

**Technical Provisions** Pillar 1 liabilities under Solvency II consisting of BEL and Risk Margin

**TMTP** 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

**Transferring Non-Profit Business** The Transferring Non-Profit Policies, together with the associated assets and liabilities which will be included in the proposed transfer to ReAssure

## W

**Waiver** Permission to be exempt from the regulatory requirements to notify certain groups of policyholders

**With-Profits Actuary function** 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

**WPA** With-Profits Actuary. The person or person fulfilling the With-Profits Actuary function

**WPC** With-Profits Committee. A committee which provides oversight of the management of a with-profits fund

**WPICC** With-Profits Insurance Capital Requirement

**WLWPF** Windsor Life With-Profits Fund





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