

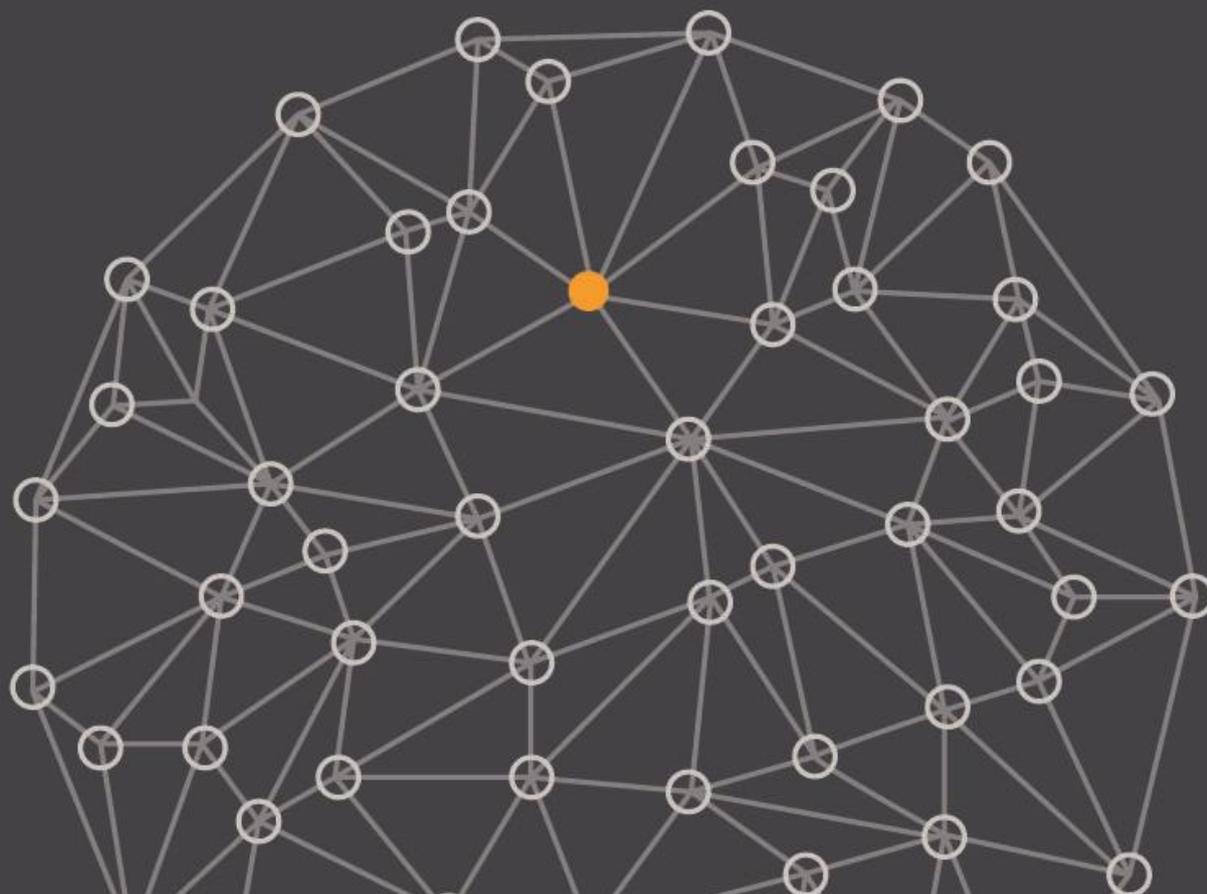
MILLIMAN CLIENT REPORT

# Assurant, Inc.

Report of the Independent Expert on the proposed transfer of business from Assurant General Insurance Limited and London General Insurance Company Limited to Assurant Europe Insurance N.V.

19 June 2020

Derek Newton, FIA





## Contents

<b>1. PURPOSE AND SCOPE</b> .....	<b>3</b>
<b>2. EXECUTIVE SUMMARY</b> .....	<b>10</b>
<b>3. BACKGROUND REGARDING THE RELEVANT REGULATORY ENVIRONMENTS</b> .....	<b>14</b>
<b>4. BACKGROUND REGARDING THE ENTITIES CONCERNED IN THE SCHEME</b> .....	<b>22</b>
<b>5. THE PROPOSED SCHEME</b> .....	<b>40</b>
<b>6. THE IMPACT OF THE SCHEME ON THE TRANSFERRING POLICYHOLDERS</b> .....	<b>51</b>
<b>7. THE IMPACT OF THE SCHEME ON THE HOLDERS OF AGIL AND LGI POLICIES THAT ARE NOT BEING TRANSFERRED UNDER THE SCHEME</b> .....	<b>69</b>
<b>8. OTHER CONSIDERATIONS</b> .....	<b>72</b>
<b>9. CONCLUSIONS</b> .....	<b>81</b>
<b>APPENDIX A DEFINITIONS</b> .....	<b>82</b>
<b>APPENDIX B CV FOR DEREK NEWTON</b> .....	<b>87</b>
<b>APPENDIX C SCOPE OF THE WORK OF THE INDEPENDENT EXPERT IN RELATION TO THE SCHEME</b> .....	<b>89</b>
<b>APPENDIX D GENERAL CONSIDERATIONS OF THE INDEPENDENT EXPERT IN RELATION TO THE SCHEME</b> .....	<b>91</b>
<b>APPENDIX E COMPLIANCE WITH THE PRA POLICY STATEMENT</b> .....	<b>93</b>
<b>APPENDIX F KEY SOURCES OF RELEVANT INFORMATION</b> .....	<b>96</b>
<b>APPENDIX G SOLVENCY II BALANCE SHEET</b> .....	<b>98</b>
<b>APPENDIX H KEY DIFFERENCES BETWEEN IFRS AND SOLVENCY II TECHNICAL PROVISIONS</b> .....	<b>100</b>

# 1. Purpose and scope

## PURPOSE OF THIS REPORT

- 1.1 It is proposed that particular blocks of business of Assurant General Insurance Limited ("**AGIL**") and of London General Insurance Company Limited ("**LGI**") be transferred to Assurant Europe Insurance N.V. ("**AEI**") by an insurance business transfer scheme ("**the Scheme**"), as defined in Section 105 of the Financial Services and Markets Act 2000 ("**FSMA**"). Together, AGIL and LGI are the "**Transferors**" and AEI is the "**Transferee**". In this report, I refer to AGIL, LGI and AEI collectively as "**the Companies**".
- 1.2 Section 109 of FSMA requires that an application to the High Court of Justice in England and Wales ("**the Court**") for an order sanctioning an insurance business transfer scheme must be accompanied by a report on the terms of the transfer ("**the Scheme Report**"). The Scheme Report must be prepared by an independent person ("**the Independent Expert**") having the skills necessary to make the report and who is nominated or approved by the Prudential Regulation Authority ("**PRA**"), having consulted with the Financial Conduct Authority ("**FCA**"). The Scheme Report is required in order that the Court may properly assess the impact of the proposed transfer, including the likely effect on the policyholders of the insurance companies in question.
- 1.3 AGIL, LGI and AEI have collectively nominated me to act as Independent Expert to provide the Scheme Report in respect of the Scheme, and the PRA has approved my appointment in consultation with the FCA (see paragraph 1.16, below).
- 1.4 This report (the "**Report**") describes the proposed transfer and discusses its likely effects on the policyholders of AEI, LGI and AGIL (in respect of all business of AEI, LGI and AGIL), including its effects on the security of policyholder benefits and levels of service. As such, this Report fulfils the requirements of the Scheme Report.
- 1.5 AGIL and LGI are domiciled, authorised and regulated in the UK. AEI is domiciled, authorised and regulated in the Netherlands.
- 1.6 AEI, LGI and AGIL are indirect subsidiaries of Assurant, Inc. ("**Assurant**"). In this Report, I refer to Assurant and its direct and indirect subsidiaries collectively as "**the Assurant Group**". In Figure 4.1, below, I show a simplified structure chart of the parts of the Assurant Group that are relevant to this Scheme.
- 1.7 A list of terms defined in this Report is shown in Appendix A. Otherwise, I use the same defined terms (which are capitalised in this Report) as are in the document that sets out the terms of the Scheme (the "**Scheme Document**").

## THE PROPOSED SCHEME

- 1.8 The liabilities to be transferred to AEI under the Scheme relate to certain insurance policies underwritten by AGIL or by LGI (collectively "**the Transferring Policies**", with those relating to AGIL being "**the AGIL Transferring Policies**" and those relating to LGI being "**the LGI Transferring Policies**"). This business comprises all policies effected by or on behalf of the respective entities whereby the risk is situated in a member state of the European Economic Area ("**EEA**") and under which any liability remains unsatisfied or outstanding at the Effective Date. For the avoidance of doubt, any risk situated in either the UK or Switzerland would not be included within the Transferring Business. I discuss the Transferring Liabilities in more detail in paragraphs 4.117-4.120 below.
- 1.9 No part of the insurance liabilities of AGIL or LGI other than that relating to the Transferring Policies will be transferred under the Scheme.
- 1.10 The assets to be transferred to AEI under the Scheme (collectively "**the Transferring Assets**" with those relating to AGIL being "**the AGIL Transferring Assets**" and those relating to LGI being "**the LGI Transferring Assets**") comprise all assets supporting the Transferring Policies, including most of the outwards reinsurance contracts that relate to the Transferring Policies and that are not intra-group. (In Section 5, below, I discuss in more detail the outwards reinsurance contracts that relate to the Transferring Policies.)

- 1.11 I refer to the Transferring Assets and the Transferring Policies, collectively, together with certain contracts and their related liabilities that will also be transferred under the Scheme to AEI, as the “**Transferring Business**”. The certain contracts that will be transferred under the Scheme to AEI relate to the Transferring Assets or Transferring Policies; for those contracts that relate to both transferring and non-transferring assets or policies of AGIL or LGI business, only the parts of those contracts that relate to the Transferring Assets or Transferring Policies will transfer to AEI.
- 1.12 The Effective Date of the Scheme is expected to be 2 November 2020.
- 1.13 AEI is a recently established entity and, as at the date of this Report, it has no policyholders. It is not expected that AEI will have written any business prior to the Effective Date and, therefore, I have not considered such policyholders further in this Report. I discuss this further in paragraph 5.14, below. If that expectation changes subsequent to this Report, then I will consider that as part of the Supplementary Report (see paragraph 1.34, below).
- 1.14 I note that the Assurant Group is applying to the Court for approval of another insurance business transfer scheme, having the same effective date as that of the Scheme. Subject to the Court’s approval, this scheme (the “**Assurant Life Scheme**”) will transfer to Assurant Europe Life Insurance N.V. (“**AEL**”) the long-term insurance business of Assurant Life Limited (“**ALL**”) and of London General Life Company Limited (“**LGL**”) that relates to risks situated in an EEA Member State. Neither the Scheme nor the Assurant Life Scheme is dependent on the approval of the other, save in respect of certain creditor insurance policies written by AGIL or LGI. I explain this in more detail in paragraphs 5.20-5.27, below.
- 1.15 The business involved in the Scheme, the arrangements for the Scheme and the effect of the Scheme are discussed in more detail in Sections 4 to 8 of this Report.

#### THE INDEPENDENT EXPERT

- 1.16 I, Derek Newton, have been appointed by AGIL, LGI and AEI as the Independent Expert to consider the Scheme under Section 109 of FSMA. My appointment has been approved by the PRA in consultation with the FCA; this was confirmed in a letter dated 10 April 2019. To the best of my knowledge, no one else has previously been approved or appointed as the Independent Expert to consider the Scheme.
- 1.17 I am a Principal of Milliman LLP (“**Milliman**”) and I am based in its UK General Insurance practice in London. I am a Fellow of the Institute and Faculty of Actuaries (“**IFoA**”), which was established in 2010 by the merger of the Institute of Actuaries and the Faculty of Actuaries. I became a Fellow of the Institute of Actuaries in 1988. My experience of general insurance includes (reserved) roles such as Signing Actuary to Lloyd’s syndicates and to Irish non-life insurance companies, as well as acting as the Independent Expert in five insurance business transfer schemes that were sanctioned in 2014, 2015, 2016, 2017 and 2019 respectively. I have included my Curriculum Vitae in Appendix B in which I explicitly note the insurance business transfer schemes for which I have acted as the Independent Expert, as well as those for which I have provided peer review support to the Independent Expert.
- 1.18 I do not have, and have never had, any direct or indirect personal interest in any of the parties involved in the proposed Scheme, and, to the best of my knowledge, have never had any such interest. I have never had any insurance policies with any of the companies within the Assurant Group, and I am not a shareholder or member of any Assurant Group entity. In addition, I am not currently working on any projects for Assurant or any of its subsidiaries.
- 1.19 I can confirm that in the period 2015 to 2019 inclusive:
- Milliman has carried out no work for AGIL or AEI. Milliman has carried out work for The Warranty Group before it became a member of the Assurant Group. Neither I, nor anyone supporting me in my work as Independent Expert, was directly involved in that work;
  - The total work carried out for the Assurant Group (including The Warranty Group) worldwide by Milliman represented 0.03% of Milliman’s global revenue; and
  - The total work carried out for the Assurant Group (including The Warranty Group) by Milliman LLP represented approximately 1% of Milliman LLP’s revenue.

- 1.20 Milliman LLP has not carried out any other work for any member of the Assurant Group, including AGIL and LGI, in the period 2015 to 2019.
- 1.21 I believe that, for all practical purposes, I am independent for the purposes of assessing the proposed Scheme.
- 1.22 The Scheme is subject to sanction by the Court under Section 111 of FSMA.
- 1.23 AGIL and LGI will meet the cost of my work as Independent Expert. No costs of the Scheme will be borne directly by any of the policyholders of either AGIL, LGI or AEI.

#### THE SCOPE OF MY REPORT

- 1.24 My terms of reference have been reviewed by the PRA and by the FCA and are set out in Appendix C.
- 1.25 I have considered the terms of the Scheme only and have not considered whether any other scheme or schemes or alternative arrangement might provide a more efficient or effective outcome.
- 1.26 The Report describes the Scheme and the likely effects on policyholders of AGIL, LGI and AEI, including effects on the security of policyholders' benefits and levels of service.
- 1.27 The Report should be read in conjunction with the full terms of the Scheme.
- 1.28 My work has required an assessment of the liabilities of AGIL, LGI and AEI for the purposes of describing the effect of the Scheme. My review of the liabilities was based on the actuarial reserve assessments conducted by internal actuaries, on behalf of AGIL and LGI (there are currently no policyholders in AEI and hence no technical provisions relating to insurance liabilities). I have reviewed the methodology and assumptions used in their work and assessed the key areas of uncertainty in relation to these liabilities. I have also taken note, where applicable, of comments made by the external auditors to AGIL and LGI. I have not attempted to review in detail the calculations performed by the internal actuaries on behalf of AGIL, LGI and AEI or to produce independent estimates of the liabilities.
- 1.29 In addition to the liabilities, I have assessed the appropriateness in nature and amount of any assets to be transferred under the Scheme, and the capital position of AGIL, LGI and AEI, both pre- and post-Scheme. Again, I have not attempted to review in detail the calculations of the capital position performed by AEI, LGI or AGIL, and I have not attempted to produce independently my own estimates.
- 1.30 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Scheme and in preparing this Report, but which nonetheless should be drawn to the attention of policyholders in their consideration of the Scheme.
- 1.31 In reporting on the Scheme as the Independent Expert, I recognise that I owe a duty to the Court to assist the Court on matters within my expertise. This duty overrides any obligation to AGIL, to LGI or to AEI. I confirm that, in preparing this Report, I have complied with this duty.
- 1.32 I have taken account of the requirements regarding experts set out in Part 35 of the Civil Procedure Rules, Practice Direction 35 and the Protocol for Instruction of Experts to give Evidence in Civil Claims.
- 1.33 I confirm that I have made clear which facts and matters referred to in this Report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.
- 1.34 Shortly before the date of the Court hearing at which an order sanctioning the Scheme will be sought, I will prepare a supplementary report ("**Supplementary Report**") that will cover any relevant matters that might have arisen since the date of this Report. As part of my preparation of the Supplementary Report, I shall review and comment on the then most up-to-date financial information relating to AGIL, LGI and/or AEI. I shall also comment on the implementation of the plan to communicate the Scheme to interested parties and the responses received, including any objections.

- 1.35 This Report has been prepared during a period of great volatility in global and local economies, in the actions of national governments, in social and work activity and in consumer habits as a result of the COVID-19 pandemic. In this Report, I have considered the impact of the pandemic on the entities involved in the Scheme (see Section 4, below) and on the Scheme itself (see Section 5, below). If I consider it necessary and immediately before the Directions Hearing, I will provide the Court with an addendum to this Report (the “**Update Addendum**”) that updates this Report, in particular the conclusions therein, in respect of material developments relating to COVID-19 that are pertinent to the Scheme. If it were produced, the Update Addendum would be considered an integral part of the Report.
- 1.36 The letters, notices and advertisements to be sent to policyholders or published in relation to the Scheme will refer all queries to a postal address or a telephone number or a website address. AGIL, LGI and AEI have stated that they will respond promptly to any such queries. Following the directions hearings relating to the Scheme, the Report will be published on the [www.assurant.co.uk](http://www.assurant.co.uk), [www.thewarrantygroup.eu](http://www.thewarrantygroup.eu) and <https://assurantnederland.nl> (the “**Transfer Websites**”), with copies being sent to any policyholders who request them. The Supplementary Report will likewise be made available at least one week before the date of the hearing of the Court at which the Scheme might be sanctioned.

### Materiality

- 1.37 After considering the likely effects of the Scheme on each of the different groups of policyholders affected by the Scheme (as identified in paragraph 5.13 below), I have drawn conclusions as to whether I believe the Scheme will materially adversely affect that group of policyholders. It should be recognised that the Scheme will affect different policyholders in different ways, and that, for any one group of policyholders, there may be some effects of the Scheme that are positive and others that are adverse. If some effects of the Scheme are adverse, that does not necessarily mean that the Scheme is unreasonable or unfair, as those adverse effects may be insignificant or they may be outweighed by positive effects.
- 1.38 In order to determine whether any effects of the Scheme on any group of policyholders are materially adverse, it has been necessary for me to exercise my professional judgement in the light of the information that I have reviewed.
- 1.39 When assessing the financial security of policyholders, I have looked at the solvency position of the Companies, both pre- and post-Scheme, relative to regulatory solvency requirements, and also at the nature of the assets that constitute each company’s capital and surplus. It should be noted that a company may have capital considerably in excess of its regulatory requirements, but that the directors of a company could legitimately reduce that level of capital (for example, through the payment of dividends, subject to regulatory approval) and still leave the company appropriately capitalised. In circumstances where the Scheme has adversely affected the financial security of a group of policyholders, in order to determine whether that impact is material, I have considered whether the level of financial security projected to be in place after the transfer would have been acceptable and permissible before the transfer had taken place. I would determine that any adverse impact to a particular group of policyholders is material if the level of financial security afforded to them after the transfer would not have been acceptable relative to the normal constraints under which the company’s capital position was managed before the transfer.

### THE STRUCTURE OF MY REPORT

- 1.40 The remainder of this Report is set out as follows:
- Section 2: I provide an executive summary of this Report (I have also provided a separate summary of this Report, as described in paragraph 1.46, below).
  - Section 3: I provide some background information regarding the regulatory environments in which AGIL, LGI and AEI operate.
  - Section 4: I provide some background information regarding AGIL, LGI and AEI.
  - Section 5: I summarise the key provisions of the Scheme.
  - Section 6: I consider the likely impact of the Scheme on the holders of Transferring Policies (“**Transferring Policyholders**”).

- Section 7: I consider the likely impact of the Scheme on the policyholders who would remain within AGIL and LGI after the transfer has taken place.
- Section 8: I cover more general issues relating to the Scheme and the management of AGIL, LGI and AEI.

1.41 I summarise my conclusions in Section 9.

#### RELIANCES AND LIMITATIONS

1.42 In carrying out my review and producing this Report, I have relied, without detailed verification, upon the accuracy and completeness of the data and information provided to me, in both written and oral form, by the Companies. Reliance has been placed upon, but not limited to, the information detailed in Appendix F. My opinions depend on the substantial accuracy of this data, information and the underlying calculations. I am unaware of any issue that might cause me to doubt the accuracy of the data and other information provided to me. All information that I have requested in relation to my review has been provided. I have been assisted in my review of the information and my analyses by colleagues of mine at Milliman but I have not relied on their work or their advice.

1.43 The Report has been prepared for the purposes of the Scheme in accordance with Section 109 of FSMA. A copy of this Report will be sent to the FCA and PRA, and will accompany the Scheme application to the Court.

1.44 The Report must be considered in its entirety as individual sections, if considered in isolation, may be misconstrued.

1.45 Neither this Report, nor any extract from it, may be published without me having provided my specific written consent, save that

- copies of this Report may be made available for inspection by policyholders who might be affected by the Scheme and by the financial regulatory authorities in the Netherlands, and
- copies may be provided to any person requesting the same in accordance with legal requirements.

I also consent to this Report being made available on the Transfer Websites.

1.46 No summary of this Report may be made without my express consent. I will provide a summary of this Report (the "**Report Summary**") for inclusion in a document that will be made available to the affected policyholders of AGIL, of LGI and of AEI, and to anyone who, or any body that, has been identified as having an interest in the policies being transferred or who has notified AGIL, LGI or AEI of their interest (further details are provided in paragraphs 5.47-5.54, below). That document will be sent to the FCA and PRA, will accompany the Scheme application to the Court, and will be available on the Transfer Websites.

1.47 This Report has been prepared within the context of the assessment of the terms of the Scheme, and must not be relied upon for any other purpose. Milliman and/or I will accept no liability for any application of this Report to a purpose for which it was not intended or for the results of any misunderstanding by any user of any aspect of this Report. In particular, no liability will be accepted by Milliman or me under the terms of the Contracts (Rights of Third Parties) Act 1999.

1.48 Actuarial estimates are subject to uncertainty from various sources, including changes in claim reporting patterns, claim settlement patterns, judicial decisions, legislation, economic and investment conditions. Therefore, it should be expected that the actual emergence of claims, premiums, expenses and investment income will vary from any estimate. Such variations in experience could have a significant effect on the results and conclusions of this Report. No warranty is given by Milliman or me that the assumptions, results and conclusions on which this Report is based will be reflected in actual future experience.

1.49 This review does not comprise an audit of the financial resources and liabilities of AGIL, LGI or AEI, or of the wider Assurant Group.

1.50 The Report should not be construed as investment advice.

1.51 Nothing in this Report should be regarded as providing a legal opinion on the effectiveness of the Scheme.

- 1.52 In considering the background to the Companies, and in considering the likely impact of the Scheme, I have made extensive use of financial information as at 31 December 2019 as that is, in general, the most recent date at which audited financial information is available. I have also taken into account updated financial information that has been made available to me, although I note that this updated information has not been audited and that, in general, it has not been publicly disclosed. I have asked the managements of the Companies for information regarding any developments between as at 31 December 2019 and the date of this Report that would have affected the Companies, in particular any development that might have affected the security of their policyholders and the standards of service provided to them, both now and in future. I have referred in this Report to the developments that they have reported to me. The managements of AGIL, LGI and AEI have confirmed to me that there have been no other such developments. I have also searched using on-line resources for information regarding any such developments. At the date of this Report, I am not aware of any material changes in circumstances since as at 31 December 2019 other than those referred to in this Report. The Report also takes no account of any information that I have not received, or of any inaccuracies in the information provided to me. I will review any further financial statements of AGIL, LGI and AEI, whether audited or unaudited, as and when they become available, and will comment on this information in my Supplementary Report.
- 1.53 All of the financial information with which I have been provided has been expressed in Pound Sterling (GBP). However, I would expect that some of the underlying assets and transactions would be or would have been denominated in other currencies. I presume that, throughout the financial information, data in other currencies has been converted to Pound Sterling (GBP) at appropriate and mutually consistent currency exchange rates.
- 1.54 The use of Milliman's name, trademarks or service marks, or reference to Milliman directly or indirectly in any media release, public announcement or public disclosure, including in any promotional or marketing materials, websites or business presentations, is not authorised without Milliman's prior written consent for each such use or release, which consent shall be given in Milliman's sole discretion.

#### My reliance on legal advice

- 1.55 I am not an expert in legal matters and hold no qualifications in UK law or Dutch law (insurance regulations or otherwise). Therefore, I have incorporated the input of experts in UK insurance law in relation to a number of areas. In particular:
- I rely on confirmation from the Assurant Group that there are no previous schemes covering in-force business that could, in conjunction with the implementation of the Scheme, result in a material adverse impact on policyholders; and
  - I incorporate the input given by legal experts in order to ensure that my understanding of the Scheme, and my description of its relevant features in this Report, is materially accurate.
- 1.56 Obtaining information in respect of the operation of the Scheme from the legal experts provides a sound basis from which to carry out my review and analysis using actuarial expertise.
- 1.57 In order to obtain a sound understanding of the legal effect of the Scheme, the options available to me are:
- to retain my own legal adviser to carry out the relevant legal review; or
  - to incorporate the advice and input of the legal firms retained by AGIL, LGI and AEI in respect of this Scheme, namely Kennedy Van der Laan N.V., in relation to the Dutch aspects of the Scheme, and Pinsent Masons LLP (in relation to all aspects of the Scheme that are not Dutch-specific).
- 1.58 In this case, I consider that it is not necessary for me to obtain independent legal input and that it is appropriate for me to incorporate the input of Pinsent Masons LLP and of Kennedy Van der Laan N.V.
- 1.59 Neither Pinsent Masons LLP nor Kennedy Van der Laan N.V. has been retained by me, and neither Pinsent Masons LLP nor Kennedy Van der Laan N.V. has any liability for any input that has been made available to me in order to provide me with information that I consider relevant to my assessment of the effects of the Scheme.
- 1.60 My reasons for incorporating the input of Pinsent Masons LLP and Kennedy Van der Laan N.V. are:

- Pinsent Masons LLP is a large international legal firm with a wide range of experience in UK insurance law and Part VII transfers. 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;
  - Kennedy Van der Laan N.V. is a large Dutch legal firm with a wide range of experience in Dutch insurance law and the application of insurance regulation. 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 Netherlands;];
  - The nature of the input from Pinsent Masons LLP that I have incorporated in this Report is factual, and deals primarily with the specifics of the Scheme and how it works in accordance with UK law;
  - The nature of the input from Kennedy Van der Laan N.V. that I have incorporated in this Report reflects general Dutch insurance law and regulation;
  - Those legal matters summarised in the two immediately preceding bullet points do not appear to be contentious; and
  - The fair treatment of policyholders is not dependent on the legal input.
- 1.61 Given the factual and non-contentious nature of the legal input provided, I am satisfied that this input was not influenced by the fact that it was obtained through appointment by Assurant rather than through independent appointment. Therefore, I am satisfied that the input given by Pinsent Masons LLP and Kennedy Van der Laan N.V. would not be different had they been retained directly by me in respect of the Scheme.
- 1.62 I am therefore satisfied that it is appropriate for me to incorporate the input of Pinsent Masons LLP and of Kennedy Van der Laan N.V. in forming my view on the Scheme.

#### PROFESSIONAL AND REGULATORY GUIDANCE

- 1.63 I am required to comply with relevant professional standards and guidance maintained by the Financial Reporting Council and by the IFoA, including *TAS 100: Principles for Technical Actuarial Work* and *TAS 200: Insurance*. I have complied with such standards, subject to the principles of proportionality and materiality.
- 1.64 In accordance with *Actuarial Profession Standard X2*, as issued by the IFoA, I have considered whether this Report should be subject to review ("**Work Review**"). I concluded that it should and I have also decided that the Work Review should be conducted by an individual who has not otherwise been involved in the analysis underlying this Report or in the preparation of this Report, but who would have had the appropriate experience and expertise to take responsibility for the work himself. In other words, I have decided that this Report should be subject to Independent Peer Review. I confirm that this Report has been subject to Independent Peer Review prior to its publication.
- 1.65 This Report has been prepared under the terms of the guidance set out in the Statement of Policy entitled *The Prudential Regulation Authority's approach to insurance business transfers* ("**the Policy Statement**"), issued in April 2015 (see Appendix E), and in Section 18 of the FCA Supervision Manual ("**SUP18**") contained in the Handbook of Rules and Guidance to cover scheme reports on the transfer of insurance business. I have also followed the guidance contained within the FCA's May 2018 paper on transfers effected under Part VII of FSMA (FG18/4) and within some private correspondence sent by the FCA to, among others, those who had been engaged as Independent Experts.

## 2. Executive summary

### CONCLUSION

- 2.1 In summary, in my opinion, provided the proposed Scheme operates as intended, and I have no grounds for believing that it will not do so, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on:
- The benefit expectations of the Transferring Policyholders under the Transferring Policies;
  - The security of the benefits under the Transferring Policies;
  - The level and standards of administration and service that would apply to the Transferring Policies;
  - The benefit expectations of the policyholders of AGIL and LGI whose policies will not be transferred to AEI under the Scheme;
  - The security of the benefits of the policyholders of AGIL and LGI whose policies will not be transferred to AEI under the Scheme;
  - The level and standards of administration and service that would apply to the policies of AGIL and LGI that will not be transferred to AEI under the Scheme.
- 2.2 I summarise below the key aspects of the Scheme, the aspects of the Scheme that I considered, and the conclusions that I reached in respect of those aspects.
- 2.3 I will review my analyses and conclusions in the light of any relevant information of which I become aware prior to the Court hearing to sanction the Scheme, and I will summarise my additional review and conclusions, explaining any revisions to those contained within this Report, in a Supplementary Report.

### THE SCHEME

- 2.4 The Transferring Business comprises the policies written or assumed by AGIL and LGI whereby the risks are situated in an EEA Member State (which, for the avoidance of doubt, excludes the UK) and under which any liability remains unsatisfied or outstanding at the Effective Date, plus all related assets and liabilities. The Transferring Business represents a significant proportion of the technical provisions, net of reinsurance, as at 31 December 2019 or LGI and especially of AGIL.
- 2.5 Under the Scheme, the Transferring Business will be transferred from AGIL and LGI to AEI.
- 2.6 The liabilities being transferred under the Scheme to AEI shall explicitly not include tax or regulatory liabilities. In this context, regulatory liabilities would include any liabilities arising out of past mis-selling, for example of payment protection policies.
- 2.7 AGIL, LGI and AEI are all members of the Assurant Group.

#### Motivation for the Scheme

- 2.8 Following the UK's departure from the European Union ("EU") in January 2020 and during the Transition Period (see paragraph 3.27, below), there remains considerable uncertainty as to whether UK insurance companies will continue to be able to use passporting rights to write and service business into the EEA via the EU's freedom of establishment or freedom of service rules. The Assurant Group has incorporated a new subsidiary in the Netherlands, AEI, and intends that AEI will write and service insurance business written in EEA countries under EU passporting rights. Therefore, the motivation for the proposed Scheme is to ensure that the Assurant Group is able to continue to service the business of AGIL and LGI, written under EU passporting rights, regardless of the outcome of the Brexit negotiations.

#### Policyholders Affected

- 2.9 I have considered the likely effects of the Scheme on the following groups of policyholders:
- the Transferring Policyholders;
  - the current policyholders of AGIL whose policies will not be transferred under the Scheme; and

- the current policyholders of LGI whose policies will not be transferred under the Scheme.
- 2.10 I have not considered the impact of the Scheme upon existing AEI policyholders. As at the date of this Report, there are no AEI policyholders, and AEI is not expected to start writing business until the Effective Date or shortly before the Effective Date.

### Administration

- 2.11 The administration and servicing of the Transferring Business will be performed post-Scheme by the same outsourced entities as it is currently (with one exception, as services currently conducted by the Amsterdam branch of TWG Services Limited (“**TWGS**”) in respect of the Transferring Business will, post-Scheme, be conducted by AES). They will be conducted by the same staff and management as they are currently (the relevant staff will transfer from TWGS to AES), using the same processes and systems as currently used, and under the same policy framework as now. There will be no need to migrate policy data from one administration system to another. Therefore, it is neither intended nor expected that there be any change in the administration or servicing of the Transferring Business as a result of the Scheme.

### COVID-19

- 2.12 In recent weeks, the development of the COVID-19 pandemic has resulted in major changes in the ways that people across Europe (and beyond) live, work and interact. There is considerable uncertainty as to how long the pandemic will last and its likely effects on the economy, both globally and nationally. This has resulted in volatile but downward movements in the financial markets. Therefore, the pandemic has affected, and might continue to affect for a long period, the Companies.
- 2.13 Work conducted by the Companies indicates that the most immediate financial effects will be falls in the values of assets and increases in the insurance liabilities in the balance sheets. The Companies’ models indicate that COVID-19 will result in reductions in the current and projected ratios of available cover to the required solvency margin (“**Capital Cover Ratios**”), but not so much as to materially change the level of financial security within each of the Companies.
- 2.14 The Companies appear to be coping well with the operational challenges of government restrictions on movements and request to maintain social distancing. However, some services have been harder than others to maintain while complying with government guidance, resulting in some slippage of service standards from pre-pandemic levels.
- 2.15 The steps being taken by AEG in response to the disruption caused by COVID-19 appear to be reasonable. I am satisfied that the Scheme would not amplify the adverse impact of COVID-19 on the financial health of any of the Companies or on the service standards that they provide. I am further satisfied that none of the groups of policyholders identified in paragraph 2.9, above, would be materially disadvantaged by the Scheme in respect of the consequences of the COVID-19 pandemic.
- 2.16 Given the rapidly developing nature of the COVID-19 pandemic, I will provide an update on the potential risks from COVID-19 in my Supplementary Report, and will also, if necessary, provide an Update Addendum to the Court immediately before the Directions Hearing.

### THE IMPACT OF THE SCHEME UPON THE TRANSFERRING POLICYHOLDERS

- 2.17 I am satisfied that the proposed Scheme will not affect in a materially adverse way either the security or the policy servicing levels of the Transferring Policyholders. I have reached this conclusion by considering:
- the reserves of AGIL and LGI as at 31 December 2019 (and subsequently where available);
  - the excess assets of AGIL and LGI as at 31 December 2019 (and subsequently where available);
  - the projected reserves and excess assets of AEI as at the proposed Effective Date (and subsequently where available);
  - the risk exposures in the Companies and the impact that the Scheme might have on those; and
  - the standards of policy servicing in each of the Companies.
- 2.18 I concluded that:

- the reserves of AGIL and of LGI appeared reasonable as at 31 December 2019;
- there is no reason to think that the reserve strength of AEI will differ from that of AGIL or LGI;
- as at 31 December 2019, AGIL is more than sufficiently capitalised and LGI is well-capitalised (I have defined this term in paragraph 6.4, below);
- as at the Effective Date, AEI is projected to be a well-capitalised company;
- the Transferring Policyholders will not be materially adversely affected due to relative differences in the financial strength of AEI post-Scheme to those of AGIL or LGI pre-Scheme;
- the proposed Scheme will result in only minor change to the risk exposure of the Transferring Business, that will not have a materially adverse impact on the security of policyholder benefits;
- the proposed Scheme will not alter the terms and conditions of any of the Transferring Policies; and
- the proposed Scheme is unlikely to have any impact on the standards of policy servicing experienced by the Transferring Policyholders compared to their current position.

#### THE IMPACT OF THE SCHEME UPON THOSE POLICYHOLDERS REMAINING WITHIN AGIL AND LGI

2.19 I am satisfied that the proposed Scheme will not affect in a materially adverse way either the security or the policy servicing levels of the policyholders of AGIL and LGI who are not Transferring Policyholders. In reaching this conclusion I have noted that:

- there is no reason to think that the reserve strength of AGIL or LGI will be impacted by the Scheme;
- had the Scheme being implemented on 31 December 2019, on a pro forma basis<sup>1</sup> AGIL would have become a well-capitalised company and LGI would have become a very well capitalised company;
- although the proposed Scheme will lead to a change to the risk exposures of the business remaining within AGIL and LGI, this will not have a materially adverse impact on the security of benefits for the policyholders of AGIL and LGI who are not Transferring Policyholders;
- the proposed Scheme will not alter the terms and conditions of any of the policies of AGIL or LGI that are not transferring under the Scheme; and
- the proposed Scheme is unlikely to have any impact on the standards of policy servicing experienced by the policyholders of AGIL and LGI who are not Transferring Policyholders compared to their current position.

#### THE IMPACT OF THE SCHEME IN RESPECT OF OTHER MATTERS

2.20 I have considered the likely effects of the Scheme on the reinsurers whose reinsurance contracts cover the Transferring Business. All such contracts, other than an intra-group quota share agreement relating to LGI, are being transferred from AGIL or LGI to AEI by the Scheme where possible and otherwise, subject to the consent of the respective reinsurers, by novation. I am satisfied that the Scheme will not have a materially adverse effect on the writers of the reinsurance contracts that are being transferred. The administration of the Transferring Business, including the management and handling of claims, will continue to be performed post-Scheme by the same people, using the same processes, as it had been pre-Scheme, so the magnitude and timing of recoveries claimed against reinsurance contracts relating to the Transferring Business will be unaffected by the Scheme.

2.21 For the policyholders of AGIL and LGI who are not being transferred by the Scheme, there will be no change to the supervisory authorities as a result of the Scheme; they will remain the PRA and FCA. Thus, the Scheme will cause no adverse regulatory impact on such policyholders.

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<sup>1</sup> *In this context, by “on a pro forma basis” I am referring to the capital adequacy of the entities had the Scheme been approved and become effective as at 31 December 2019.*

- 2.22 The Transferring Policyholders will experience a change in the supervisor as a result of the Scheme. Pre-Scheme, the prudential supervision and conduct regulation of their insurers is the responsibility of the PRA and FCA respectively; post-Scheme, it will be the responsibility of the DNB and AFM. The PRA, FCA, DNB and AFM are all members of EIOPA and each operates within a significant and sophisticated insurance market. I have no reason to believe that the oversight standards post-Scheme for the Transferring Business would be materially different from those applied pre-Scheme.
- 2.23 I have not yet been provided with an estimate of the external costs of the Scheme. The total costs of the Scheme will be split between Assurant, AGIL, LGI and AEI, with the majority being met by Assurant. The costs of the Scheme will not be met by any policyholders of AGIL or LGI. Based on other Part VII schemes in which I have been involved, I consider it unlikely that the costs of the Scheme would be such as to jeopardise the security of any of the groups of policyholders.

#### APPROACH TO COMMUNICATION WITH POLICYHOLDERS

- 2.24 The Companies' approach to communicating the Scheme to affected policyholders and other interested parties is outlined in paragraphs 5.45-5.58, below.
- 2.25 I consider the approach being taken in relation to those Transferring Policyholders that AGIL and LGI intend contacting directly to be reasonable.
- 2.26 Neither AGIL nor LGI intends to notify directly any of their policyholders whose policies will not be transferred by the Scheme, on the basis that they are very unlikely to be materially affected by the Scheme. There will be no change to the terms and conditions of the contracts of the Transferring Policyholders, other than references to either AGIL or LGI becoming references to AEI. Similarly, there will be no change to the terms and conditions of AGIL and LGI policies that are not being transferred by the Scheme. The costs of communicating with all AGIL and LGI policyholders would be disproportionate to the likely benefits to the affected parties. Accordingly, the Companies will be applying to the Court for appropriate waivers of the requirement for them to notify all of their policyholders.
- 2.27 In addition to direct, written correspondence with the Transferring Policyholders, the Companies also plan indirect notification via advertisements in appropriate publications, including three national newspapers in the UK, as well as the international edition of the *Financial Times* and one newspaper in each of the twelve EEA member states in which AGIL and LGI have underwritten non-trivial volumes of insurance business.
- 2.28 The letters, notices and advertisements will refer all queries to a postal address, a telephone number and the Transfer Websites, all of which will be dedicated to responding promptly to any such queries.
- 2.29 In the circumstances, I regard the proposed approach to communications to be reasonable and proportionate, and the draft communications to be clear, fair and appropriate for their intended audiences.

### 3. Background regarding the relevant regulatory environments

3.1 In this section of the Report, I describe the general insurance markets and the regulatory regimes that operate in the UK and in the Netherlands.

#### OVERVIEW OF UK INSURANCE REGULATION

##### Background

3.2 UK insurers, as well as other financial services organisations, are regulated by both the PRA and the FCA using a system of dual regulation. The PRA and the FCA are statutory bodies set up under FSMA and the Financial Services Act 2012; their roles and objectives are defined by FSMA (as amended).

3.3 The PRA is part of the Bank of England and is responsible for:

- Prudential regulation of banks, building societies and credit unions, insurers and major investment firms;
- Promoting the safety and soundness of the firms it regulates, seeking to minimise the adverse effects that they can have on the stability of the UK financial system; and
- Contributing to ensuring that insurance policyholders are appropriately protected.

3.4 The FCA is a separate institution and is responsible for:

- Ensuring that the markets that it regulates function well;
- Conduct regulation of all financial firms; and
- Prudential regulation of those financial services firms that are not supervised by the PRA.

3.5 A Memorandum of Understanding has been established between the PRA and the FCA, which sets out the high-level framework by which these two regulatory bodies will co-ordinate. In particular, the Memorandum of Understanding requires the PRA and FCA to co-ordinate with each other in advance of transfers effected under Part VII of FSMA ("**Part VII transfers**").

3.6 The PRA sets the regulations governing the amount and quality of solvency capital held by firms; these are summarised below. The solvency regime is designed to protect the security of policyholders, as well as the stability of the insurance industry.

3.7 The FCA is concerned with achieving fair outcomes for consumers and seeks to ensure that firms adhere to its conduct principles. Its strategic objective is to ensure that the relevant markets function well. To support this, it has three operational objectives, which are:

- To secure an appropriate degree of protection for consumers;
- To protect and enhance the integrity of the UK financial system; and
- To promote effective competition in the interests of consumers.

##### Taxation

3.8 In the UK, proprietary general insurance companies are taxed on profits achieved at the main rate of corporation tax (currently 19%<sup>2</sup> for the financial year ending 31 March 2020).

##### Financial Services Compensation Scheme

3.9 As well as through the PRA and FCA regulations, consumer protection is also provided by the Financial Services Compensation Scheme ("**FSCS**"). This is a statutory "fund of last resort", which compensates customers in the event of the insolvency (or other defined default) of a financial services firm authorised by the PRA or FCA, subject to certain eligibility rules. Insurance protection exists for private policyholders and small businesses<sup>3</sup> that hold eligible policies in the situation when an insurer is unable to meet fully its liabilities. For general insurance business, the FSCS will pay 100% of any claim incurred before the default:

<sup>2</sup> As at the date of this Report, the UK Corporation Tax rate is expected to remain at this level for the financial years ending 31 March 2021 and 31 March 2022.

<sup>3</sup> In accordance with Section 382 of the Companies Act 2006, a small business is defined as one for which two of the following three conditions apply over the preceding financial year: turnover not more than £10.2 million; balance sheet not more than £5.1 million; and not more than 50 employees.

- In respect of a liability subject to compulsory insurance (such as employers' liability cover); or
- That arises in respect of a liability subject to professional indemnity insurance; or
- That arises from the death or incapacity of the policyholder due to injury, sickness, or infirmity

and 90% of any claim incurred before the default for other eligible types of insurance (such as home insurance). No protection is available for Goods in Transit, Marine, Aviation and Credit Insurance. Contracts of reinsurance are also not protected. The FSCS is funded by annual levies on all firms regulated by the PRA and by the FCA, with separate tariffs for each of five broad classes of activity (deposits, life and pensions, general insurance, investments and home finance).

### Financial Ombudsman Service

3.10 The Financial Ombudsman Service ("**FOS**") provides private individuals (or micro enterprises<sup>4</sup>) with a free, independent service for resolving disputes with financial companies. It is not necessary for the private individual (or micro enterprise) to live or be based in the UK for a complaint regarding an insurance policy to be dealt with by the FOS; it is necessary for the insurance policy concerned to be, or have been, administered from within the UK.

### FCA Conduct Principles

3.11 Within its document "*Fair treatment of customers*", the FCA sets out six consumer outcomes that firms should strive to achieve to ensure fair treatment of customers. These remain core to what the FCA expects of firms. These are as follows:

- Outcome 1: Consumers can be confident that they are dealing with insurers where the fair treatment of customers is central to the corporate culture;
- Outcome 2: Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly;
- Outcome 3: Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale;
- Outcome 4: Where consumers receive advice, the advice is suitable and takes account of their circumstances;
- Outcome 5: Consumers are provided with products that perform as insurers have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect; and
- Outcome 6: Consumers do not face unreasonable post-sale barriers imposed by insurers to change product, switch provider, submit a claim or make a complaint.

3.12 These outcomes, which are often summarised as "Treating Customers Fairly" ("**TCF**"), apply even for firms that do not have direct contact with retail customers. The FCA's rationale is that risks and poor conduct can be carried from wholesale to retail markets.

3.13 The FCA has supplemented its *Fair Treatment of Customers* document with guidance, published in January 2018, entitled *The Responsibilities of Providers and Distributors for the Fair Treatment of Customers* ("**RPPD**"). This provides the FCA's view on what the combination of Principles for Businesses and detailed rules require respectively of providers and distributors in certain circumstances to treat customers fairly. The RPPD looks particularly to the following Principles:

- Principle 2: A firm must conduct its business with due skill, care and diligence;
- Principle 3: A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems;
- Principle 6: A firm must pay due regard to the interests of its customers and treat them fairly; and
- Principle 7: A firm must pay due regard to the information needs of its clients, and communicate information to them in a way that is clear, fair and not misleading.

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<sup>4</sup> *Micro-enterprises (an EU term covering smaller businesses) can bring complaints to the FOS as long as they have an annual turnover of less than €2 million and fewer than ten employees.*

### The Insurers (Reorganisation and Winding-Up) Regulations 2004

- 3.14 Under UK law, the winding-up of an insurance undertaking is governed by the *Insurers (Reorganisation and Winding-Up) Regulations 2004* (as amended, including under the Solvency II Regulations 2015). Under these regulations, insurance claims have precedence over any claim on the insurance undertaking with the exception of certain preferential claims (e.g. claims by employees, etc.) with respect to the whole of the insurance undertaking's assets. Therefore, direct policyholders rank equally and above inwards reinsurance policyholders and all other unsecured/non preferential creditors in the event that an insurer is wound up.

### The Insurance Distribution Directive

- 3.15 The Insurance Distribution Directive ("**IDD**") has applied in the UK (and in all other EU Member States) with effect from 1 October 2018. The key requirements of the IDD are:
- Product oversight and governance arrangements aimed at ensuring that customers' interests are taken into consideration throughout the whole life cycle of an insurance product;
  - Transparency of inducement schemes to ensure respect of customers' interests;
  - The insurance undertaking (or insurance intermediary) providing advice to a customer is responsible for the assessment as to whether the insurance product(s) is/are suitable and appropriate, having regard to the customer's profile; and
  - A conflict of interest policy to facilitate customers' understanding of an insurance undertaking's actions taken on their behalf.
- 3.16 Business conducted via an EU branch is subject to the conduct of business regulations, including consumer protection rules, of the host country of each respective branch. The regulator in the country hosting each branch oversees the compliance of that branch with its insurance laws and regulations, implementing, if appropriate, the relevant EU Directives.

### SOLVENCY CAPITAL FRAMEWORK (SOLVENCY II)

- 3.17 The regulatory solvency-reporting framework for (re)insurers regulated within the EU, which is commonly referred to as Solvency II, introduced, with effect from 1 January 2016 and consistently across the EU, solvency requirements that reflect the risks that individual (re)insurers actually face.
- 3.18 Under Solvency II, EU (re)insurers are required to adhere to a set of risk-based capital requirements, some of the results of which are shared with the public.
- 3.19 Solvency II is a principles-based regime, based on three so-called pillars:
- Under Pillar I, quantitative requirements define a market consistent framework for valuing the company's assets and liabilities, and determining the Solvency Capital Requirement ("**SCR**").
  - Under Pillar II, insurers must meet minimum standards for their corporate governance, and also for their risk and capital management. There is a requirement for internal audit and actuarial functions. Insurers must regularly complete an Own Risk and Solvency Assessment ("**ORSA**").
  - Under Pillar III, there are explicit requirements governing disclosures to supervisors and policyholders.
- 3.20 Under Solvency II, both the assets and liabilities of insurers are valued on a market consistent basis. Therefore, under Solvency II, the technical provisions in respect of claims incurred and losses arising from unexpired exposures (together typically the largest item on the liability side of an insurer's balance sheet, and hence the balance sheet itself) are often substantially different from those calculated under the current requirements for IFRS/GAAP.
- 3.21 I set out in Appendix G simplified details for the balance sheet, and the calculation of technical provisions (in respect of claims incurred and losses arising from unexpired exposures), for an insurer under Solvency II. In this Report, I denote technical provisions under Solvency II as "**TPs**".
- 3.22 TPs as relating to general insurance business are:

- The premium provision: the expected present value (with no allowance for optimism or prudence) of all future cash-flows (claim payments, expenses and future premiums due) relating to future exposures arising from policies for which the insurer is obligated as at the valuation date;
- The claims provision: the expected present value (with no allowance for optimism or prudence) of all future cash-flows (claim payments, expenses and future premiums due) relating to claim events prior to the valuation date; and
- The risk margin: the risk margin is intended to be the balance that another (re)insurer would require over and above the sum of the premium provision and claims provision for taking on the liabilities at the valuation date. Under Solvency II, the risk margin is calculated using a cost-of-capital approach (presently employing a 6% cost of capital parameter as set out in EU regulation<sup>5</sup>).

3.23 TPs in respect of claims required under Solvency II differ from the GAAP/IFRS claims reserves in several ways including the following:

- The TPs contain no element of conservatism above a best estimate that may be held in the undiscounted GAAP reserves;
- The TPs include an allowance for events not in data ("**ENID**"), which are events or future developments that might occur but which are not represented in the historical data upon which the actuarial projections are based;
- The TPs include a discount to account for the time value of money in the future cash-flows; and
- The TPs include a risk margin.

I have set out the differences and their balance sheet implications in Appendix H.

3.24 The SCR under Solvency II is the amount of capital required to ensure continued solvency over a one-year time-frame with a probability of 99.5%. There are two main approaches to calculating the SCR:

- Using an internal model approved by the local supervisor: an internal model calculation of the SCR is based upon an assessment of the risks specific to an insurer, and is calibrated so as to correspond to a confidence level of 99.5% over a one-year trading period that net assets remain positive (i.e. the insurer remains solvent); or
- Using the standard formula specified in detail in the Solvency II legislation ("**Standard Formula**"): the Standard Formula is designed to be applicable to all insurers and is not therefore tailored to the circumstances of an individual insurer. In summary, the basic SCR consists of five risk modules (non-life, life, health, market and counterparty) that are in turn further sub-divided into 18 sub-modules (e.g. premium and reserve risk, catastrophe risk and currency risk). The results for each sub-module are aggregated using a correlation matrix to arrive at a capital charge for each of the five main modules, which in turn are aggregated using a further correlation matrix to determine the basic SCR. A further module is used to calculate operational risk, which is added to the basic SCR to produce the (Standard Formula) SCR<sup>6</sup>.

3.25 The Minimum Capital Requirement under Solvency II ("**MCR**") defines the point of intensive regulatory intervention. The MCR calculation is less risk sensitive than the SCR calculation and is calibrated to a confidence level of 85% over a one-year time-frame (compared to 99.5% for the SCR). The MCR is calculated as a linear function of the TPs and written premium but must be between 25% and 45% of the firm's SCR, subject to an absolute floor of €2.5 million (or €3.7 million for (re)insurers writing liability, credit or suretyship classes).

<sup>5</sup> Commission Delegated Regulation (EU) 2015/35 dated 10 October 2014.

<sup>6</sup> Subject to certain rules and qualifications, it is possible for insurers to replace the standard parameters in respect of certain sub-modules relating to reserve and premium risks with undertaking-specific parameters ("**USPs**"), which are based on the insurer's own experience and which are expected to reflect better the risk profile of the insurer.

- 3.26 If an insurer's available resources fall below the SCR, then supervisors are required to take action with the aim of restoring the insurer's finances back to the level of the SCR as soon as possible. If, however, the financial situation of the insurer continues to deteriorate, then the level of supervisory intervention will be progressively intensified. The aim of this "supervisory ladder" of intervention is to capture any ailing insurers before their situation becomes a serious threat to policyholders' interests. If the available resources of the insurer were to fall below the level of the MCR, then "ultimate supervisory action" would be triggered, i.e. the insurer's liabilities would be transferred to another insurer and the licence of the insurer would be withdrawn, or the insurer would be closed to new business and its in-force business placed into run-off. In practice, supervisors would be expected to have determined earlier whether or not the insurer's finances could be restored to above the level of the SCR - an insurer whose supervisor determined that it would not be able to restore its solvency position would be placed into run-off before it breached its MCR.

## Brexit

- 3.27 Although the UK formally left the EU on 31 January 2020, there is currently a transition period ("**Transition Period**") that will last until 31 December 2020, during which the existing trading relationships will continue unaltered and the future relationship between the UK and the EU will be negotiated. The Transition Period may be extended to either 31 December 2021 or 31 December 2022, subject to the mutual agreement of the EU and UK, that agreement to be reached by 1 July 2020. The UK's withdrawal and the Transition Period to final separation are colloquially referred to as "**Brexit**".
- 3.28 I consider some of the possible impacts of Brexit as they might affect the Scheme later in this Report, but at this stage I note that, following Brexit, the UK Government might seek to cancel certain pieces of legislation that were enacted in accordance with EU Directives. One such legislative item might be that which implemented Solvency II. However, I note the following:
- The UK played a prominent role in the design, structuring and development of Solvency II;
  - The costs for the UK insurance industry of implementing Solvency II were considerable and it is likely that the costs of implementing a replacement solvency regime that was materially different from Solvency II would also be very large;
  - Solvency II took many years to develop and to implement, and it is likely that any materially different replacement solvency regime would also take a long time to develop and to implement;
  - There is a strong desire within the UK insurance industry that the UK solvency and prudential regime maintains "equivalence" with the Solvency II regime that will remain in place throughout the remaining countries of the EU, to facilitate cross-border operations without unnecessary duplication of regulation; and
  - A UK Treasury Select Committee was formed in September 2016 to consider the Solvency II Directive, its impact on the UK insurance industry and what improvements could be made in the interests of the consumer. The Committee reported in October 2017. While it called for the development of a clear agreed strategy to refine the Directive post-Brexit in order to foster innovation, competition and competitiveness for the benefit of UK consumers, it did not recommend the dismantling of the Directive; rather it looked for greater harmonisation between UK insurance and international capital standards and emerging accounting standards.
- 3.29 I further note that, on 19 October 2019, the UK and EU agreed a Political Declaration setting out the framework for their future relationship. The declaration indicated that they expect arrangements for financial services to be included within the scope of a future trade deal, that this would include close cooperation on regulatory and supervisory matters, and that an assessment of the equivalence of each other's regulatory and supervisory regimes would be completed before the end of June 2020. It is possible that the completion of this review will be delayed as a consequence of the COVID-19 pandemic, but, as at the date of this Report, I had seen no official notice to that effect.
- 3.30 Therefore, notwithstanding Brexit, I believe it to be very unlikely that there will be any material change to the UK solvency capital regime in the short to medium-term. I have therefore not considered further this possibility in this Report.

- 3.31 It is possible that the negotiations between the UK and EU regarding the terms of Brexit might result, post-Brexit, in continuation of the current passporting regime for UK insurers, or at least in some transitional arrangements that enable insurers to carry on cross UK/EEA border activities for a fixed period after the UK formally exits the EU. However, most insurers currently operating across UK/EEA borders have made contingency plans in case the existing passporting arrangements are discontinued promptly on Brexit. Some that are UK based are establishing, or have established, a regulated entity in a (continuing) EU-member country, from which non-UK EEA business can be conducted and into which existing non-UK EEA business can be transferred from the UK-based entity. Others are considering what additional requirements will be imposed upon them to enable them to continue to be able to conduct cross-border EEA activities as, in effect, third country insurers.

## OVERVIEW OF THE NETHERLANDS INSURANCE REGULATION

### Background

- 3.32 Insurers (and other financial services organisations) in the Netherlands are regulated by both the Dutch Central Bank (“**DNB**”) and the Netherlands Authority for the Financial Markets (“**AFM**”). The DNB exercises prudential supervision of Dutch insurance companies, and monitors Dutch insurance companies’ compliance with rules and regulations under *Wet op het financieel toezicht* (the “**Dutch Act on Financial Supervision**”). The AFM performs conduct of business supervision on financial markets for Dutch insurance companies.
- 3.33 The DNB works with its European partners to achieve:
- Price stability and a balanced macroeconomic development;
  - A shock-resilient financial system and a secure, reliable and effective payment system; and
  - Strong and sound financial institutions that meet their obligations and commitments.
- 3.34 The AFM is a separate institution and has the following three strategic objectives :
- Promoting the fair and conscientious provision of financial services;
  - Promoting the fair and efficient operation of the capital markets; and
  - Contributing to the stability of the financial system.
- 3.35 The DNB and the AFM cooperate with one another in line with terms and conditions set out in a cooperation covenant. In addition, cooperation and information exchange takes place on subjects of mutual interest between the DNB and the AFM, such as on enforcement, remuneration policy and controlled and ethical business operations.
- 3.36 The solvency capital framework applicable to Dutch insurers is the same Solvency II framework described in paragraphs 3.17-3.26, above.

### Dutch Corporate Governance Code

- 3.37 Both financial regulation and Dutch corporate law are fundamental to the principles and practices for the governance of Dutch insurers.
- 3.38 The major Dutch insurers use a two-tier governance structure, whereby management and supervision are divided between two company bodies: the management board and the supervisory board, with the management board consisting solely of executive directors and the supervisory board consisting solely of non-executive directors. The Dutch Corporate Governance Code provides guidance relating to this governance structure, as well as guidance for firms operating a one-tier governance structure.
- 3.39 The management board of a Dutch insurer is responsible for the continuity of the company and for setting a strategy in line with its view on long-term value creation. The supervisory board is responsible for supervising the manner in which the management board implements its strategy, and must be independent from the management board, which is achieved in part by consisting only of non-executive directors.

## Taxation

- 3.40 In the Netherlands, proprietary insurance companies are taxed on profits achieved at the main rate of corporation tax (as at 31 December 2019 this was 19% of taxable income up to €200,000 and 25% of taxable income above this threshold<sup>7</sup>).

## Dutch Financial Services Complaints Institute

- 3.41 The Dutch Financial Services Complaints Institute (*Klachteninstituut Financiële Dienstverlening* or “**KiFiD**”) provides private individuals with an independent service for resolving disputes with financial services companies, which is free other than a fee charged for any appeals made regarding the KiFiD’s decision. KiFiD will deal with most consumer complaints concerning any financial services provider that is registered with KiFiD.
- 3.42 In the case that the KiFiD is unable to resolve a dispute between an individual and a financial company, a decision is made with regards to the resolution by the Disputes Committee within KiFiD. Decisions made by the Disputes Committee are usually legally binding, provided both parties have accepted that such decision will be legally binding prior to the decision being made. However, if unsatisfied with the decision of the Disputes Committee and the decision is not binding, in general, an individual may take the case to court, where any decision made would be legally binding.
- 3.43 Although KiFiD has some jurisdiction over policyholder disputes arising outside the Netherlands, in practice such disputes will normally be referred to the local competent dispute resolution service under the arrangements agreed by **FIN-NET**. FIN-NET is an international partnership of financial complaint institutes of which KiFiD is a member. FIN-NET published a memorandum setting out its intent on cross-border-cooperation between the affiliated complaint institutes, such as KiFiD. The memorandum outlines the mechanisms and other conditions according to which the affiliated complaint institutes intend to co-operate.
- 3.44 KiFiD does not act on claims above €1m.

## Policyholder ranking upon the wind-up of a Dutch insurer

- 3.45 Under Dutch law, the winding-up of an insurance undertaking is governed by the Dutch Insolvency Act. Under this regulation, policyholders of insurance policies are preferential creditors and, as such, insurance claims have precedence over any claim on the insurance undertaking, with the exception of certain preferential claims with respect to the whole of the insurance undertaking’s assets. The preferential claims ranking ahead of insurance claims include claims from creditors with a mortgage claim over the assets of the insurer, claims relating to employee pensions and some claims relating to employee wages. Therefore, direct policyholders rank equally and above inwards reinsurance policyholders and all other unsecured/non preferential creditors in the event that an insurer is wound up.

## COMPARISONS BETWEEN THE REGULATORY ENVIRONMENT IN THE UK AND THE NETHERLANDS

### Supervision, governance and conduct

- 3.46 The supervision of insurers in both the Netherlands and the UK is conducted by two regulators, one that deals with the prudential regulation and the other with conduct against required principles. While the detail of the governance and conduct requirements in the two countries appears different, the effect is similar.

### Capital and reserve requirements

- 3.47 All EU regulators have expected insurers under their supervision to comply with the Solvency II requirements with effect from 1 January 2016. This included the UK regulators, as the UK was then a member of the EU. This has had the effect of putting regulatory capital and reserve requirements in the UK and the Netherlands onto essentially the same basis. Although the UK has since ceased being a member state of the EU, it has retained the Solvency II regime and, as discussed in paragraphs 3.28-3.30, above, I do not think it likely to change that regime in the foreseeable future.

<sup>7</sup> These percentages are expected to reduce to 16.5% and 25% in 2020, and to 15% and 21.7% in 2021.

### Security under winding-up

- 3.48 The rules governing the winding-up of an insurance or reinsurance company are broadly similar in the UK and the Netherlands. In both cases, where assets are insufficient to meet fully the company's liabilities, holders of direct policyholders rank equally or behind certain preferential claims but rank above inwards reinsurance policyholders and all other unsecured/non preferential creditors.

### Consumer protection

- 3.49 In the UK, the FSCS compensates eligible customers of authorised financial firms (including insurers) in the event that the firm has insufficient assets to meet claims, and the FOS provides eligible customers with a free, independent service to help settle disputes with financial firms (including insurers). The FOS has compulsory jurisdiction in respect of complaints raised by eligible policyholders (as identified in paragraph 3.10, above).
- 3.50 In the Netherlands, there is no scheme directly equivalent to the FSCS and the benefits of holders of insurance contracts that contain no investment element are not protected against the failure of their insurer.
- 3.51 KiFiD fulfils a role in respect of policyholder complaints against insurers registered with KiFiD that is similar to that fulfilled by the FOS in respect of policies administered in the UK. I note that registration with KiFiD is not compulsory for Dutch insurers, although AEI has applied to be a registered member of KiFiD. I have been told by AEI that it expects the process of registration to be completed by 31 July 2020.

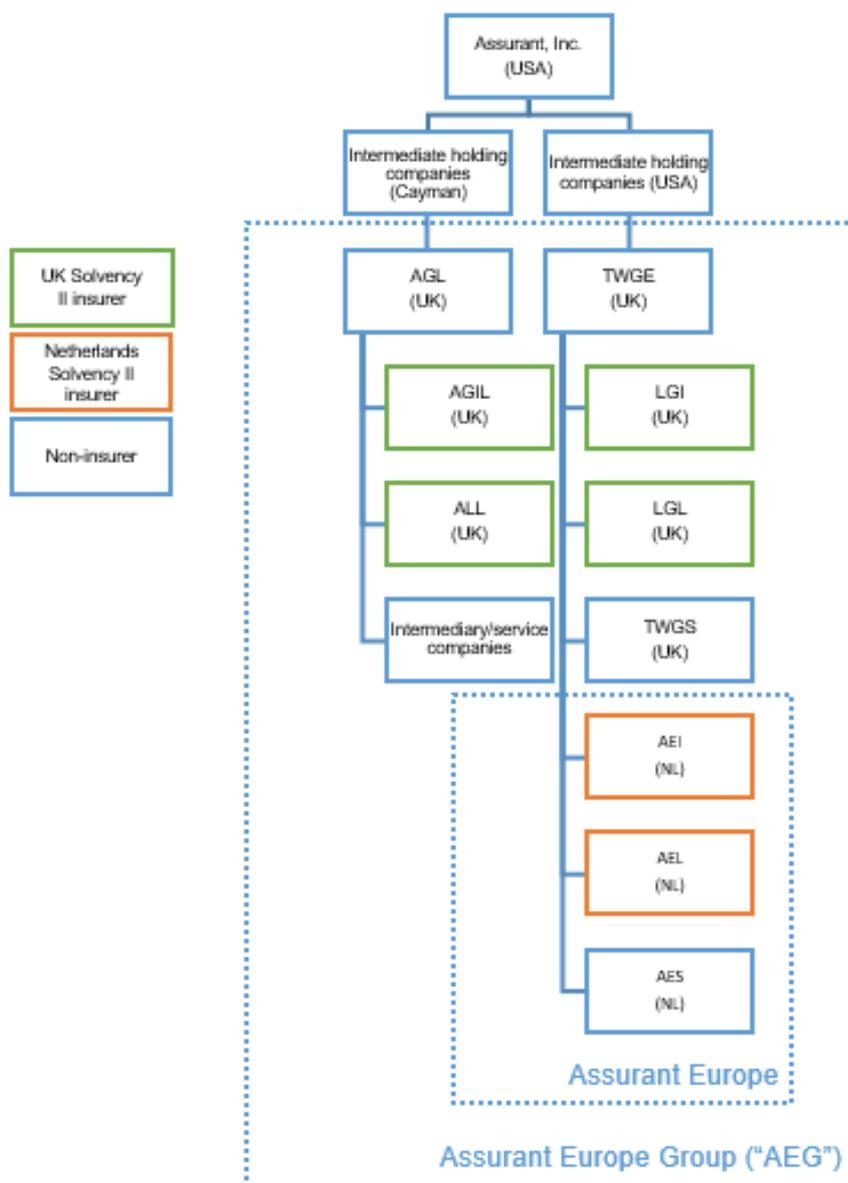
## 4. Background regarding the entities concerned in the Scheme

4.1 In this section of the Report, I set out some background information and key metrics relating to the entities that are involved in the Scheme.

### Assurant Europe Group structure

4.2 All three entities that are involved in the Scheme are members of a group of indirect subsidiaries of Assurant, known as “Assurant Europe Group” (“**AEG**”). Within AEG, there is a subset of recently formed companies, including AEI, collectively known as “**Assurant Europe**”. In Figure 4.1, below, I set out a simplified structure chart for AEG, capturing the entities that will be affected by the Scheme.

FIGURE 4.1 SIMPLIFIED ASSURANT EUROPE GROUP STRUCTURE



## AGIL

### AGIL's background

- 4.3 AGIL is an insurance company, incorporated as a private limited company in England and Wales (registered number 02341082) under the Companies Act 1985. It is a wholly owned direct subsidiary of Assurant Group Limited ("AGL"), a limited liability insurance holding company incorporated in England and Wales.
- 4.4 AGIL is authorised:
- to write the following classes of business in the UK: 1 (Accident), 2 (Sickness), 3 (Land vehicles), 6 (Ships), 7 (Goods in transit), 8 (Fire and natural forces), 9 (Damage to property), 10 (Motor vehicle liability), 12 (Liability for ships), 13 (General liability), 16 (Miscellaneous financial loss) and 18 (Assistance); and
  - (until the end of the Transition Period) to conduct general insurance business in the following countries on a freedom of services basis: Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, the Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, Spain and Sweden. It also passports from the UK into France, Germany, Italy and Spain on a freedom of establishment (branch) basis. As at the date of this Report, AGIL has unexpired business in some but not all of these territories.
- 4.5 AGIL's issued and fully paid share capital as at 31 December 2018 was made up of 71,947,766 ordinary shares of £1 each.

### AGIL's business written

- 4.6 AGIL underwrites mobile phone, gadget, extended warranty, furniture and creditor insurance. It predominantly writes business in the UK, Germany, Spain, Italy and France but has also written business in Hungary, Ireland, Romania and Sweden.
- 4.7 The majority of policies are sold via retailers and other third party clients, with a small amount sold direct to the consumer.
- 4.8 The mix of business has shifted over time from longer-term business, such as creditor insurance, to shorter terms property risks. The core business focus is now on mobile phone, gadget and extended warranty insurance. AGIL is progressively exiting the creditor insurance market. It has placed its creditor insurance portfolio into run-off and is not writing new creditor insurance business. AGIL is not authorised to carry risks that are categorised as long-term assurance; therefore, the long-term portion of its creditor insurance covers (i.e. life assurance and permanent health insurance) is underwritten by an insurer that is authorised by the PRA to carry such risks, that insurer being ALL.
- 4.9 Gross premiums written in the year ending 31 December 2019 totalled £300.8 million. Of this, £73.7 million was ceded to reinsurers, leaving net premiums written in the year ending 31 December 2019 totalling £227.1 million.

### AGIL's key financial information

- 4.10 As at 31 December 2019, on a UK GAAP basis, the technical provisions within AGIL were as set out in Figure 4.2, below. I show separately the provisions in respect of the unearned portions of existing insurance commitments (unearned premium reserves ("UPR")) and the provisions in respect of business already earned (i.e. the provision for outstanding claims).

**FIGURE 4.2 AGIL'S TECHNICAL PROVISIONS ON A UK GAAP BASIS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance	Ceded	Net of Reinsurance
Unearned Premium Reserves ("UPR")	36,196	-6,925	29,271
Claims Outstanding	16,142	-4,379	11,763
<b>TOTAL RESERVES</b>	<b>52,337</b>	<b>-11,304</b>	<b>41,034</b>

- 4.11 AGIL management considers that the UK GAAP booked reserves remain reasonable and comply with AGIL's reserving policy. I discuss AGIL's reserves in more detail in paragraphs 6.5-6.23, below.

- 4.12 As at 31 December 2019, on a UK GAAP basis, the total assets and the total liabilities of AGIL amounted to £190.8 million and £107.2 million respectively, giving net assets of £83.6 million. The net assets represent the capital of the company under UK GAAP (it should be noted that this is not the same as the own funds available to meet the solvency capital requirements under Solvency II).
- 4.13 As at 31 December 2019, on a UK GAAP basis, AGIL held investment assets valued at £77.4 million. These comprised wholly debt securities.
- 4.14 In Figure 4.3 and Figure 4.4, below, I show the Solvency II technical provisions as at 31 December 2019, split by cover type and then by the location of the insured risk.

**FIGURE 4.3 BREAKDOWN BY COVER TYPE OF AGIL'S SOLVENCY II TECHNICAL PROVISIONS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance			Net of Reinsurance		
	Premium Provision	Claims provision	Total	Premium Provision	Claims provision	Total
Added Value Account Barclays clients	-2,511	1,803	-708	-2,511	1,803	-708
Added Value Account Lloyds clients	-1,687	1,380	-307	-1,687	1,380	-307
Added Value Account Other clients	0	1,556	1,556	0	1,556	1,556
Disability	1	234	235	1	234	235
Furniture	0	75	75	0	0	0
Gadgets	106	688	794	106	688	794
Mobile Phone Insurance	-1,153	620	-533	109	0	109
Property	629	45	674	629	45	674
Unemployment	78	207	285	78	207	285
<b>Total Non-Transferring Business</b>	<b>-4,538</b>	<b>6,609</b>	<b>2,071</b>	<b>-3,275</b>	<b>5,914</b>	<b>2,638</b>
Disability	36	87	122	34	-45	-11
Gadgets	11,474	5,022	16,496	11,474	5,022	16,496
Miscellaneous	1,505	88	1,593	0	0	0
Mobile Phone Insurance	-667	2,422	1,755	63	0	63
Property	216	8	224	216	8	224
Unemployment	43	63	105	33	48	82
<b>Total Transferring Business</b>	<b>12,607</b>	<b>7,689</b>	<b>20,296</b>	<b>11,820</b>	<b>5,033</b>	<b>16,854</b>
<b>TOTAL</b>	<b>8,069</b>	<b>14,298</b>	<b>22,367</b>	<b>8,545</b>	<b>10,947</b>	<b>19,492</b>

**FIGURE 4.4 BREAKDOWN BY GEOGRAPHY OF AGIL'S SOLVENCY II TECHNICAL PROVISIONS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance			Net of Reinsurance		
	Premium Provision	Claims provision	Total	Premium Provision	Claims provision	Total
UK	-4,538	6,609	2,071	-3,275	5,914	2,638
<b>Total Non-Transferring Business</b>	<b>-4,538</b>	<b>6,609</b>	<b>2,071</b>	<b>-3,275</b>	<b>5,914</b>	<b>2,638</b>
France	6,988	1,738	8,725	6,988	1,738	8,725
Germany	3,520	1,426	4,946	3,518	1,403	4,921
Hungary	-300	1,042	742	28	0	28
Ireland	-94	299	204	-28	62	34
Italy	132	36	169	123	-87	36
Netherlands	-171	9	-162	16	0	16
Romania	-30	13	-16	3	0	3
Spain	1,057	3,038	4,095	1,173	1,917	3,090
Sweden	1,505	88	1,593	0	0	0
<b>Total Transferring Business</b>	<b>12,607</b>	<b>7,689</b>	<b>20,296</b>	<b>11,820</b>	<b>5,033</b>	<b>16,854</b>
<b>TOTAL</b>	<b>8,069</b>	<b>14,298</b>	<b>22,367</b>	<b>8,545</b>	<b>10,947</b>	<b>19,492</b>

- 4.15 I note that Figure 4.3 and Figure 4.4 both omit the risk margin, which amounts to £4,268k, of which £3,691k is attributable to the Transferring Business.

- 4.16 A comparison of the technical provisions under UK GAAP, as shown in Figure 4.2, above, and those under Solvency II, as shown in Figure 4.3 and Figure 4.4, above, shows that the claims provisions under the two accounting systems are similar but that the premium provisions are very different. This reflects a key difference between the Solvency II and UK GAAP accounts, which is the treatment of expected future profit on unearned business.
- 4.17 A key accounting principle underlying UK GAAP accounts is that profits should be recognised when they are earned but not before. Hence, the UPR is calculated on the assumption that all of the unearned premium (net of deferred acquisition costs) will be required to meet the costs of the claims and expenses to be incurred in the period to the expiry of cover. If the business is profitable (or loss making), that profit (or loss) will be recognised over time as the UPR is earned. However, as explained in paragraph 3.22, above, within a market consistent framework, the Solvency II premium provision comprises the expected present value (with no allowance for optimism or prudence) of all future cash-flows (claim payments, expenses and future premiums due) to be incurred in the period to the expiry of cover.
- 4.18 Therefore, for businesses that are expected to be profitable, the Solvency II premium provisions (which include an allowance for future expected profits) would be lower than the equivalent UK GAAP UPRs. That situation is compounded for businesses such as AGIL for which the premiums for many policies are paid regularly (e.g. monthly) throughout the period of cover. This can be seen in Figure 4.3 and Figure 4.4, above, which show several lines of business and territories for which the Solvency II premium provisions are negative. For these lines of business and territories, the future cash-flows relating to the unearned period include expected future payments of (profitable) premiums.

#### AGIL's reinsurance

- 4.19 Generally, AGIL does not rely upon reinsurance as a key insurance risk management tool. However, as part of the overall commercial structure of the relationship, certain client relationships use reinsurance as a key part of the commercial arrangement.
- 4.20 In all cases:
- the reinsurance contract covers one particular client
  - the coverage is always on a quota share basis (mostly, but not always, 100%)
  - contracts covering UK risks are separate from those covering non-UK risks.

#### AGIL's governance arrangements

- 4.21 Ultimate responsibility for AGIL's business rests with the AGIL Board. The AEG Board oversees a number of entities within AEG, as well as AGIL. There is common membership between the AGIL Board and the AEG Board, comprising a combination of executive directors, group non-executive directors and independent non-executive directors. Thus, the AGIL Board has delegated to the AEG Board general governance oversight of the business of AGIL, subject to certain reserved matters that must remain with the AGIL Board.
- 4.22 The AEG Board is supported by the UK Audit, Risk and Compliance Committee ("**UK ARCC**"), which is a board-level committee chaired by an independent non-executive director. The UK ARCC's key responsibilities include assessing the integrity of the annual report and accounts, scrutinising internal financial systems and control and risk management systems, overseeing the solvency and capital position of the AEG companies (including AGIL) and ensuring compliance with legal and regulatory requirements.
- 4.23 In addition, the AEG Board is supported by the European Leadership Committee, which is responsible for overseeing the day-to-day management of AEG, including ensuring that activities are consistent with business strategy, risk appetite and policies approved by the AEG Board. The European Leadership Committee has various management-level sub-committees and forums to enable it to perform its duties, including the UK Insurance Committee, the UK Management Risk Committee, the Solvency & Capital Forum and the Reserving Forum.
- 4.24 While the AEG Board delegates certain responsibilities to the European Leadership Committee, there are a number of matters reserved for the AEG Board's decision covering specified aspects of strategy and management, structure and capital, financial reporting and controls, risk management and internal controls, communications, board membership and corporate governance.

### AGIL's risk management strategy

- 4.25 AEG maintains a Risk Management Framework, through which risk management is embedded throughout AGL, including AGIL. The AEG Board is responsible for ensuring appropriate governance over risk across AEG, and the CEO of AEG is ultimately responsible for ensuring that the risk profiles of the AEG companies remain within the risk appetite approved by the AEG Board.
- 4.26 The key components of the AGL Risk Management Framework include:
- **Risk appetite statement:** specifies the amount and type of risk that AGL is willing to accept in pursuit of strategic goals. These are expressed as a series of appetite statements, limits and measures that enable to AGL Board to set, monitor and manage risk appetite, risk capacity and risk profile.
  - **Risk taxonomy:** categorises the universe of risks to which AGL is exposed. The Risk Taxonomy consists of six main categories of risk, namely: insurance risk, market risk, credit risk, operational risk, regulatory risk and strategic risk. Within each of these main categories are a number of sub-categories of risk.
  - **Risk management process:** sets out the agreed protocols for identifying, measuring, managing, monitoring and reporting risks.
  - **Key risk policies:** a series of Solvency II policies, owned by members of the European Leadership Committee and reviewed at least annually. These policies define the scope, objective or reason for the policy, the key responsibilities for complying with the policies and the relevant policy statement, which outline the key controls in place to ensure proper governance of the risk.
  - **Risk event escalation and breach reporting:** specifies the requirements for reporting risk events and the means by which risk events are monitored and escalated.
  - **Stress testing and scenario analysis:** performed at least annually to ensure the adequacy of capital resources under a range of stresses and scenarios.
  - **ORSA:** a forward-looking assessment of risks, solvency needs and adequacy of capital resources. The ORSA is produced at least annually or with each significant change in risk profile, and provides a company-specific assessment of the risk profile and solvency requirements. A single ORSA is used for AGL, which is applicable to AGIL.

### AGIL's key risks

#### Insurance risk

- 4.27 The main risk for AGIL is that of insurance risk, predominantly non-life underwriting risk. Underwriting risk is defined as the financial and contractual risks involved when writing or administering insurance policies. Unmitigated, the risk exposure would have a large, material impact on the total risk exposure of AGIL.
- 4.28 AGIL manages insurance risk through its underwriting strategy, ability to reprice business after one year, its regular review of outstanding claims liabilities, and reinsurance arrangements.

#### Liquidity risk

- 4.29 Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. AGIL manages liquidity risk by maintaining adequate reserves and banking facilities and ensuring that the spread of investments across short, medium and long-term funds will enable any short-term funding requirements to be met. The liquidity is monitored continuously by review of actual and forecast cash-flows.

*Market risk*

- 4.30 Market risk is the risk that, because of market movements, a firm might be exposed to fluctuations in the value of its assets, the amount of its liabilities, or the income from its assets. Sources of general market risk include movements in interest rates, equities, exchange rates and real estate prices. It is important to note that none of these sources of risk is independent of the others. AGIL monitors its exposure to market risk through the UK ARCC. The investment portfolio is structured so that asset quality is a primary feature rather than investment return. As a result, the portfolio is limited to Government Bonds, Sovereign and Sub-Sovereign debt, Collateralised Securities and investment grade Corporate Bonds, which are actively traded. Investments are required to be above investment grade (BBB-) at purchase. Those that fall below investment grade subsequently are investigated, using subject matter experts, and the costs of early exit are assessed.
- 4.31 AGIL operates in the UK and, via branches, in other European countries, and is also part of a wider group, which has its head office in the USA. Accordingly, its net assets are subject to currency risk. The primary foreign currency exposures are to Euro and US Dollar. If the value of Sterling strengthens then the value of the non-Sterling net assets will decline when translated into Sterling. AGIL incurs currency risk in two ways:
- Operational currency risk - by holding assets and by underwriting liabilities in currencies other than the currency of the primary environment in which the business units operate (non-functional currencies)
  - Structural currency risk - by operating overseas branches where the currency of the primary environment differs to that of the principal business and being part of an international insurance group
- 4.32 Operational and structural currency risk is managed by broadly matching assets and liabilities by currency. Currency balance sheets are prepared and reviewed by management quarterly.

*Credit risk*

- 4.33 Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. AGIL is exposed to credit risk in four primary ways:
- default or delay in payments due upon cash;
  - reinsurance counterparties failing to meet financial obligations or entering into restructuring arrangements that may adversely affect reinsurance recoveries;
  - default or delay of repayment of loans and receivables; and
  - in respect of amounts due from other group companies.
- 4.34 Exposures to all counterparties are analysed and assessed each quarter and quantified in the calculation of the solvency capital requirement, using the Standard Formula. The output from the resulting analysis is presented to the UK ARCC, detailing any material changes from the previous period.
- 4.35 AGIL holds cash balances with a number of banks within Europe but diversifies its exposure to ensure that any bank failures do not materially affect liquidity. This includes holding cash in highly liquid money market funds with next day access, which AGIL treats as a counterparty exposure.
- 4.36 Holdings must follow the Financial Risk Policy, which requires cash holdings to be held in counterparties classified as investment grade or above by the main ratings agencies of Moody's, Fitch and/or S&P.
- 4.37 Third party reinsurers are required to be credit scored at 'A' (or equivalent) by two out of three of the main rating agencies (Fitch, Moody's or S&P) or be Solvency II regulated in the EU, and in compliance with their solvency capital requirements, in order to be accepted unless appropriate collateral is provided to mitigate the exposure.

### Operational risk

- 4.38 Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. In particular, this includes the risk of business interruption, of compliance or regulatory breaches, or of poor service delivery, any of which could result in damage to AGIL's reputation and could adversely affect its ability to meet its stated objectives. This includes the risk of AGIL being investigated for and found guilty of mis-selling payment protection insurance, resulting in a substantial fine. Operational risks are captured through AGIL's risk register and risk reporting processes as part of the Risk Management Framework.
- 4.39 AGIL has established policies, processes and controls to manage and mitigate its key operational risks. The process through which the AGIL's operational risk universe is determined, and subsequent estimates of frequency and severity are assessed, is captured in the Operational Risk Policy document. This process safeguards the ongoing improvement of the control environment and ensures that operational risk is identifiable and mitigated as the Group continues to grow.
- 4.40 AGL also has a comprehensive insurance programme that provides protection against the majority of material operational risks, e.g. property cover, business interruption etc.

### AGIL's capital management

- 4.41 AGIL prepares its Solvency II results in accordance with the Standard Formula.
- 4.42 I have been provided with AGL's Capital Management Policy, which covers the capital management of AGIL. The AGL Capital Management Policy sets out requirements for the assessment of Own Fund items, the maintenance of a medium-term capital management plan and the use of two capital buffers, which represent margins to be held above the SCR.
- 4.43 AGL's internal capital target is to hold the Pillar 1 SCR, or the requirement identified during the ORSA process if higher, plus a Board-approved buffer. The level at which the two capital buffers are set is reassessed with each ORSA process, which takes place at least annually.
- 4.44 The two capital buffers are intended to ensure that AGIL maintains sufficient Own Funds to cover the adverse events defined in the ORSA stress tests. The capital buffers are defined as specified ratios of Own Funds to SCR. The higher of the two capital buffers is referred to as the AGIL Target Working Capital Ratio. If the ratio of AGIL Own Funds to SCR, referred to hereafter as the "AGIL SCR Ratio", is below the AGIL Target Working Capital Ratio, then it has 'Amber' status, as specified in the AGL Capital Management Policy. The lower of the two capital buffers is referred to as the "AGIL Capital Buffer". If the AGIL SCR Ratio is below the AGIL Capital Buffer, then it has 'Red' status. The AGL Capital Management Policy sets out the management actions that will be considered to return the SCR Ratio to above the AGIL Target Working Capital Ratio when the AGIL SCR Ratio has 'Amber' or 'Red' status, with more stringent actions specified under the 'Red' status.
- 4.45 AGIL's capital position is formally assessed quarterly, and reported to the UK ARCC, to ensure that own funds continue to meet the targets set.
- 4.46 The Solvency II Pillar 1 results for AGIL as at 31 December 2019 are set out in Figure 4.5, below. Results are shown on a net of reinsurance basis. As at 31 December 2019, the AGIL SCR Ratio was in excess of the Target Working Capital and therefore complied with its strategic objective regarding its SCR Ratio, i.e. it had a 'Green' status.

**FIGURE 4.5 AGIL'S SOLVENCY II PILLAR 1 AS AT 31 DECEMBER 2019 (£'000)**

	MCR	SCR
Eligible Own Funds to meet the solvency requirement	87.9	87.9
Solvency requirement	19.3	59.6
Surplus	68.6	28.3
<b>Coverage</b>	<b>456%</b>	<b>148%</b>

- 4.47 Under Solvency II, assets are classified into three tiers depending on their quality, with tier 1 representing the highest quality. As at 31 December 2019, 100% of the assets held in respect of Own Funds are tier 1 assets.

#### AGIL's conduct and complaints procedures

- 4.48 AEG has adopted a consistent framework of corporate policies and processes across its European business. This includes specific policies covering all customer facing services such as:
- Product Governance;
  - Complaints Handling;
  - Claims Management; and
  - Treating Customer Fairly
- 4.49 The policies cover as a minimum the regulatory requirements applicable to both the home state (i.e. the UK), and are also subject to the requirements of the host states across the EEA in which business is conducted.
- 4.50 The processes implemented in accordance with these policies are documented at a functional level, including all appropriate service level and key performance indicators and controls. Oversight of the operational areas is supported by the Operational Governance team.
- 4.51 A range of periodic reports is provided to management setting out key measurements, issues and actions. Material issues are escalated to the boards as appropriate. Specifically, these reports include elements such as complaints and disputes and any potential breaches of relevant service levels and key performance indicators.
- 4.52 These processes apply throughout the AEG's operations.

#### AGIL's administration and servicing arrangements

- 4.53 The administration and servicing of AGIL's policies is currently outsourced through a combination of internal services provided by other companies within AEG or specialist external service providers.
- 4.54 AGIL manages all of its outsourcing relationships in accordance with the corporate Outsourcing Policy and related framework Corporate Outsourcing Policy and related framework, which applies across AEG. This framework sets out the roles and responsibilities in relation to the outsourcing of services, the controls in place to monitor outsource providers and the governance structure surrounding the management of outsourcing.
- 4.55 Outsourcing contracts are structured in accordance with the Corporate Outsourcing Policy and related framework and relevant regulatory guidelines. Specific service levels and key performance indicators are documented within each outsourcing contract.
- 4.56 Typical service levels will include:
- IT systems availability;
  - Telephone answering times;
  - Claims handling and response timescales;
  - Query and complaint handling timescales; and
  - Adherence to TCF principles and outcomes

and appropriate measures and key performance indicators enable these to be monitored and tracked. The outcomes of this monitoring feed the periodic reporting to the relevant management forums. A key report is the Customer Need & Value Measures Dashboard, which summarises all aspect of customer service including any root cause analysis and remedial actions. I have seen examples of the management information provided, which appear to set out clearly these key metrics by client and by country.

## LGI

## LGI's background

- 4.57 LGI is an insurance company, incorporated as a private limited company in England and Wales (registered number 01865673). It is a wholly owned direct subsidiary of TWG Europe Limited, a limited liability insurance holding company incorporated in England and Wales.
- 4.58 LGI is authorised:
- to write the following classes of business in the UK: 1 (Accident), 2 (Sickness), 3 (Land vehicles), 9 (Damage to property), 13 (General liability) and 16 (Miscellaneous financial loss); and
  - (at least until the end of the Transition Period) to conduct general insurance business in the following countries on a freedom of services basis: Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Luxembourg, the Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Spain and Sweden. It also passports from the UK into Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Poland, Portugal and Spain on a freedom of establishment (branch) basis. As at the date of this Report, LGI has unexpired business in some but not all of these territories.
- 4.59 LGI's issued and fully paid share capital as at 31 December 2018 was made up of 34,000,000 ordinary shares of £1 each.

## LGI's business written

- 4.60 LGI underwrites motor warranty, appliance and technology, and creditor insurance.
- 4.61 These are primarily consumer insurance products that are marketed across Europe through a combination of branches and freedom of service arrangements. These are distributed on a Business-to-Business basis through relationships with a range of motor dealers, manufacturers, retailers, financial institutions and other distributors.
- 4.62 LGI is progressively exiting the creditor insurance market. It has placed its creditor insurance portfolio into run-off and is not writing new creditor insurance business. LGI is not authorised to carry risks that are categorised as long-term assurance; therefore, the long-term portion of its creditor insurance covers (i.e. life assurance and permanent health insurance) is underwritten by an insurer that is authorised by the PRA to carry such risks, that insurer being LGL.
- 4.63 Gross premiums written in the year ending 31 December 2019 totalled £82.4 million. Of this, £30.4 million was ceded to reinsurers, leaving net premiums written in the year ending 31 December 2019 totalling £51.9 million.

## LGI's key financial information

- 4.64 As at 31 December 2019, on a UK GAAP basis, the reserves within LGI were as set out in Figure 4.6, below.

**FIGURE 4.6 LGI'S TECHNICAL PROVISIONS ON A UK GAAP BASIS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance	Ceded	Net of Reinsurance
Unearned Premium Reserves ("UPR")	143,437	-41,832	101,605
Claims Outstanding	32,318	-6,865	25,453
<b>TOTAL RESERVES</b>	<b>175,755</b>	<b>-48,697</b>	<b>127,058</b>

- 4.65 LGI management considers that the UK GAAP booked reserves remain reasonable and comply with LGI's reserving policy. I discuss LGI's reserves in more detail in paragraphs 6.37-6.61, below.
- 4.66 As at 31 December 2019, on a UK GAAP basis, the total assets and the total liabilities of LGI amounted to £336.1 million and £245.9 million respectively, giving net assets of £90.2 million. The net assets represent the capital of the company under UK GAAP (it should be noted that this is not the same as the own funds available to meet the solvency capital requirements under Solvency II).
- 4.67 As at 31 December 2019, on a UK GAAP basis, LGI held investment assets valued at £165.0 million. The largest share of this (£152.5 million) comprised debt securities.

4.68 In Figure 4.7 and Figure 4.8, below, I show the TPs as at 31 December 2019, split by cover type and then by geography. I note that Figure 4.7 and Figure 4.8 both omit the risk margin, which amounts to £4,735k, of which £3,216k is attributable to the Transferring Business.

**FIGURE 4.7 BREAKDOWN BY COVER TYPE<sup>8</sup> OF LGI'S SOLVENCY II TECHNICAL PROVISIONS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance			Net of Reinsurance		
	Premium Provision	Claims provision	Total	Premium Provision	Claims provision	Total
Appliance Accidental Damage	10,592	372	<b>10,964</b>	8,611	253	<b>8,864</b>
Appliance Warranty	4,581	334	<b>4,915</b>	3,344	150	<b>3,494</b>
Motor GAP	9,365	792	<b>10,157</b>	8,344	633	<b>8,977</b>
Motor Warranty	5,352	429	<b>5,782</b>	4,646	345	<b>4,991</b>
Specialty Accident and Sickness	0	8	<b>8</b>	0	6	<b>6</b>
Specialty Loss of Work	0	30	<b>30</b>	0	2	<b>2</b>
<b>Total Non-Transferring Business</b>	<b>29,890</b>	<b>1,965</b>	<b>31,855</b>	<b>24,945</b>	<b>1,389</b>	<b>26,334</b>
Appliance Accidental Damage	2,033	1,121	<b>3,154</b>	1,807	914	<b>2,722</b>
Appliance Warranty	13,190	700	<b>13,890</b>	11,398	547	<b>11,946</b>
Motor GAP	55	6	<b>61</b>	43	5	<b>48</b>
Motor Warranty	17,000	3,082	<b>20,082</b>	12,834	2,392	<b>15,226</b>
Specialty Accident and Sickness	2,038	23,493	<b>25,531</b>	1,662	18,795	<b>20,457</b>
Specialty Loss of Work	898	633	<b>1,531</b>	743	507	<b>1,250</b>
<b>Total Transferring Business</b>	<b>35,214</b>	<b>29,036</b>	<b>64,249</b>	<b>28,488</b>	<b>23,161</b>	<b>51,648</b>
<b>TOTAL</b>	<b>65,104</b>	<b>31,001</b>	<b>96,105</b>	<b>53,433</b>	<b>24,550</b>	<b>77,982</b>

**FIGURE 4.8 BREAKDOWN BY GEOGRAPHY OF LGI'S PROVISION FOR SOLVENCY II TECHNICAL PROVISIONS AS AT 31 DECEMBER 2019 (£'000)**

	Gross of Reinsurance			Net of Reinsurance		
	Premium Provision	Claims provision	Total	Premium Provision	Claims provision	Total
UK	29,275	1,805	<b>31,080</b>	24,322	1,229	<b>25,551</b>
South Africa	233	142	<b>375</b>	240	142	<b>382</b>
Switzerland	382	18	<b>401</b>	382	18	<b>401</b>
<b>Total Non-Transferring Business</b>	<b>29,890</b>	<b>1,965</b>	<b>31,855</b>	<b>24,945</b>	<b>1,389</b>	<b>26,334</b>
Austria	678	42	<b>719</b>	474	33	<b>507</b>
Belgium	267	993	<b>1,260</b>	181	771	<b>952</b>
Czech Republic	845	40	<b>886</b>	682	36	<b>719</b>
France	-1,045	417	<b>-628</b>	-993	312	<b>-681</b>
Germany	8,158	350	<b>8,508</b>	7,233	279	<b>7,512</b>
Hungary	909	10	<b>919</b>	716	7	<b>723</b>
Ireland	481	131	<b>612</b>	462	102	<b>564</b>
Italy	12,240	2,596	<b>14,836</b>	10,000	2,063	<b>12,063</b>
Netherlands	2,324	23,161	<b>25,486</b>	1,857	18,529	<b>20,386</b>
Poland	3,016	539	<b>3,555</b>	2,549	431	<b>2,980</b>
Spain	6,528	541	<b>7,069</b>	4,729	410	<b>5,139</b>
Other	812	214	<b>1,027</b>	598	187	<b>785</b>
<b>Total Transferring Business</b>	<b>35,214</b>	<b>29,036</b>	<b>64,249</b>	<b>28,488</b>	<b>23,161</b>	<b>51,648</b>
<b>TOTAL</b>	<b>65,104</b>	<b>31,001</b>	<b>96,105</b>	<b>53,433</b>	<b>24,550</b>	<b>77,982</b>

4.69 "Other" comprises Denmark, Estonia, Finland, Greece, Luxembourg, Latvia, Norway, Romania, Portugal, Slovakia and Sweden. LGI's technical provisions relating to risks in each of these countries are less than £0.25 million, both gross and net of reinsurance.

<sup>8</sup> Although I consider that all of the TPs shown in Figure 4.7 relate to non-life business, I note that, in LGI's SFCR as at 31 December 2019, the TPs relating to Specialty Accident and Sickness are disclosed in the balance sheet template under the classification 'Health Similar to Life' and are also included within life technical provisions template.

- 4.70 A comparison of the technical provisions under UK GAAP, as shown in Figure 4.6, above, and those under Solvency II, as shown in Figure 4.7 and Figure 4.8, above, shows that the claims provisions under the two accounting systems are similar but that the premium provisions are very different. The explanation for this is the same as set out in paragraphs 4.17-4.18, above.

#### LGI's reinsurance

- 4.71 Generally, LGI does not rely upon reinsurance as a key insurance risk management tool. More recently, LGI has made use of reinsurance to enhance its capital management through internal group reinsurance arrangements. In addition, as part of the overall commercial structure of the relationship, certain client relationships use reinsurance as a key part of the commercial arrangement.
- 4.72 The intra-group reinsurance arrangement is with Virginia Surety Company, Inc. ("**VSC**"), which is domiciled in the USA. VSC reinsures, on a quota share basis, 20% of all of LGI's business that is denominated in Sterling, Euros or Zlotys and which has been earned since the inception of the contract.
- 4.73 Aside from the quota share contract with VSC, all other reinsurance contracts that protect LGI:
- Each cover one particular client;
  - Are mostly on a quota share basis (although there is also an Excess of Loss contract with VSC that protects LGI against UK Motor Gap insurance claims for £14.5 million in excess of £0.5 million);
  - Protect risks for different regions, i.e. cover for UK risks is separate from cover for Swiss risks and from cover for EEA risks;
  - Apply before application of the quota share contract with VSC.

#### LGI's governance arrangements

- 4.74 Following the acquisition of The Warranty Group Europe ("**TWGE**") by the Assurant Group, the governance arrangements for TWGE and its subsidiaries, which includes LGI, have been combined with those for AGL. As such, there is a single governance structure used across AEG. In this respect, paragraphs 4.21-4.24, above, which refer to the governance arrangements for AGIL apply equally to LGI.

#### LGI's risk management strategy

- 4.75 I understand that the TWGE Risk Management Framework is currently being redrafted to reflect the acquisition of TWGE by the Assurant Group. Given that the redrafting had not been completed as at the date of this Report, in this Report I consider the existing TWGE Risk Management Framework that is in place, and will address any subsequent changes in my Supplementary Report.
- 4.76 TWGE maintains a Risk Management Framework, through which risk management is embedded throughout TWGE, including LGI. The UK Board is responsible for ensuring appropriate governance of risk across TWGE, and the Chief Executive Officer of TWGE is ultimately responsible for ensuring TWGE's risk profile remains within the risk appetite as agreed by the UK Board.
- 4.77 The key components of TWGE Risk Management Framework include:
- Risk strategy:** this summarises TWGE's approach to managing risks, including the risk lifecycle of: identification, assessment, management and reporting, and monitoring.
- Risk appetite:** this articulates the short to medium term willingness of TWGE to accept a certain level of risk, for each material risk to which it is exposed, with associated tolerances.
- Risk framework:** this details, for each identified key risk category, the committees within AEG who oversee the risk profile, the relevant underlying policies and the risk sub-categories.
- Risk register:** this sets out the requirement to maintain a risk register for all identified risks, which includes, for each risk, a risk owner, risk likelihood and impact and the controls in place.
- Event management:** this specifies the requirement for reporting risk events and ensuring suitable mitigating actions are considered.
- ORSA:** this provides a comprehensive assessment of how TWGE manages risk, its current and forward-looking risk exposure and the ability to meet capital requirements.

**Stress and scenario testing:** this considers forward-looking stresses of extreme, but realistic scenarios that could affect TWGE. This is performed on an annual cycle.

#### LGI's key risks

4.78 Although the LGI insurance policies are longer term in nature than those of AGIL, the key risks and mitigation strategies for LGI are similar to those for AGIL, described above in paragraphs 4.27-4.40.

#### LGI's capital management

4.79 LGI prepares its Solvency II results in accordance with the Standard Formula, with one undertaking specific parameter (“**USP**”) adjustment. LGI has received PRA approval to use a USP for the miscellaneous financial loss risk category. This amends the Standard Formula parameter of 13% to a parameter that reflects LGI's actual volatility experience. The parameter is updated annually in line with the TWGE USP Policy

4.80 I understand that the TWGE Capital Management Policy is currently being redrafted to reflect the acquisition of TWGE by the Assurant Group. Given that the redrafting had not been completed as at the date of this Report, in this Report I consider the existing TWGE Capital Management Policy that is in place, and will address any subsequent changes in my Supplementary Report.

4.81 I have been provided with TWGE's Capital Management Policy, which covers the capital management of LGI. The TWGE Capital Management Policy sets out requirements for the assessment, monitoring and reporting of LGI's capital position, the capital planning process, the capital allocation process and rules surrounding dividend declarations.

4.82 LGI's capital position is assessed with reference to the LGI Risk Appetite Buffer, and the TWGE Capital Management Policy sets out actions available depending on how the LGI SCR Ratio (the ratio of LGI's Own Funds to its SCR) compares to the LGI Risk Appetite Buffer.

4.83 If the LGI SCR Ratio is:

- Above the LGI Risk Appetite Buffer, then no action is taken and a dividend distribution is considered;
- Is, or is projected to be, below the LGI Risk Appetite Buffer but above the regulatory capital requirement, then management actions will be proposed by the Chief Financial Officer for approval by the TWGE Operating Board and a dividend distribution will not be considered;
- Below, or has the potential be below, the regulatory capital requirement, then, in addition to the actions in response to the LGI SCR Ratio being below the LGI Risk Appetite Buffer, LGI will notify the PRA and will agree an action plan.

4.84 The Solvency II Pillar 1 results for LGI as at 31 December 2019 are set out in Figure 4.9, below. Results are shown on a net of reinsurance basis. As at 31 December 2019, the LGI SCR Ratio was in excess of the LGI Risk Appetite Buffer and therefore complied with LGI's strategic objective regarding its SCR Ratio, i.e. it had a 'Green' status.

**FIGURE 4.9 LGI'S SOLVENCY II PILLAR 1 AS AT 31 DECEMBER 2019 (£'000)**

	MCR	SCR
Eligible Own Funds to meet the solvency requirement	89.3	90.8
Solvency requirement	15.4	46.2
Surplus	73.9	44.5
<b>Coverage</b>	580%	196%

4.85 Under Solvency II, assets are classified into three tiers depending on their quality, with tier 1 representing the highest quality. As at 31 December 2019, 98% of the assets held in respect of Own Funds are tier 1 assets.

#### LGI's conduct and complaints

4.86 AEG has adopted a consistent framework of corporate policies and processes across its European business. As such, LGI's approach to conduct and complaints is as set out for AGIL, in paragraphs 4.48-4.51, above.

### LGI's administration and servicing arrangements

- 4.87 The administration and servicing of LGI policies is currently outsourced to TWG Services Limited, a subsidiary of TWGE, or to other external specialist providers. LGI manages all of its outsourcing relationships in accordance with the Corporate Outsourcing Policy and related framework, which is structured at a European group level. This framework sets out the roles and responsibilities in relation to outsourcing, the controls in place to monitor outsource providers and the governance structure surrounding the management of outsourcing.
- 4.88 Outsourcing contracts are structured in accordance with the Corporate Outsourcing Policy and related framework and relevant regulatory guidelines. Specific service levels and key performance indicators are included within each contract and are monitored within the aforementioned operational governance framework.
- 4.89 I reiterate the comments made on service levels and their monitoring in paragraph 4.56, above.

### AEI

#### AEI's background

- 4.90 AEI is a limited liability company incorporated in the Netherlands. It is registered in the trade register of the Dutch Chamber of Commerce under number 72959320.
- 4.91 AEI has recently (in 2020) been authorised by the DNB to carry on General Insurance Business in the Netherlands in classes 1 (Accident), 2 (Sickness), 3 (Land Vehicles), 7 (Goods in Transit), 8 (Fire and natural forces), 9 (Damage to property) and 16 (Miscellaneous financial loss).
- 4.92 AEI intends to exercise its right to passport certain of its permissions on a freedom of services basis into the following EEA states: Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Hungary, Ireland, Italy, Latvia, Poland, Portugal, Romania, Spain and Sweden.
- 4.93 As explained in paragraphs 5.11-5.12, below, Brexit means that AGIL and LGI, as UK authorised insurance undertakings, will no longer have the ability to effect contracts of insurance in the EEA, and are unlikely to be able to continue to carry out those contracts of insurance that were originally sold in EEA Member States after the expiry of the Transition Period, due to their inability to continue to "passport" into those jurisdictions under the relevant provisions of the Solvency II Directive. The establishment and authorisation of AEI as a non-life insurer in the Netherlands and the implementation of the Scheme will enable the Transferors' existing EEA insurance business to continue to be serviced and new EEA insurance business to be conducted within AEG after the Transition Period ends.
- 4.94 AEG has also set up two other subsidiaries in the Netherlands. These are:
- AEL (into which it is intended that the EEA business of ALL and LGL will be transferred, by a separate but concurrent scheme); and
  - Assurant Europe Services B.V. ("**AES**"), which is expected to provide all administrative services relating to the business to be written by AEI and to the business transferred to AEI, in so far as those services cannot continue to be provided by the current suppliers.
- 4.95 Collectively, AEL, AEL and AES are referred to as "**Assurant Europe**".
- #### AEI's key financial information
- 4.96 As at the date of this Report, AEI has not yet written any business and it does not yet have any policyholders or insurance liabilities.

### AEI's reinsurance

- 4.97 Reinsurance arrangements are expected to be used in a similar way to how they are currently used for AGIL and LGI. In paragraphs 4.19-4.20, above, I have explained the reinsurance arrangements that apply in respect of AGIL and, in paragraphs 4.71-4.73, above, I explain the reinsurance arrangements that apply in respect of LGI. It is intended that other than the quota share arrangement between VSC and LGI, the existing reinsurance contracts that relate to the Transferring Policies will be transferred by the Scheme to AEI from AGIL or LGI. As noted in the above explanations of the reinsurance arrangements for AGIL and LGI, the reinsurance contracts cover specific geographic regions and there is no overlap in reinsurance coverage between the Transferring Business and that remaining in AGIL or LGI. This will facilitate the transfer of the reinsurance.
- 4.98 The quota share arrangement between VSC and LGI will not be replicated within AEI; its main purpose had been to provide additional capital support to LGI (by reducing the capital requirement). In contrast, AEI will rely on its own funds to provide its solvency capital. Otherwise, AEI intends that, post-Scheme, it will be protected in respect of the Transferring Policies by a reinsurance programme that largely replicates the programmes currently protecting this business.

### AEI's governance arrangements

- 4.99 There is a single governance structure used across all companies within Assurant Europe, including AEI. This governance structure for AEI is separate to the governance structure for the rest of AEG, as described in paragraphs 4.21 to 4.24 above, although AEI, as part of Assurant Europe, does report into the wider AEG Board.
- 4.100 Each company within Assurant Europe uses a two-tier board structure (see paragraphs 3.38-3.39, above):
- The NL Supervisory Board ("**NLSB**"): this consists solely of independent board members. One of these individuals is also a member of the AEG Board, providing alignment with the wider Assurant Europe Group. The primary objective of the NLSB is to supervise the NL Management Board and Assurant Europe's general course of affairs and business, and to advise the NL Management Board.  
  
The NLSB of each Assurant Europe company has common membership and thus operate as a consolidated governance structure for the Assurant Europe companies and will normally sit as a consolidated Supervisory Board representing each of the Assurant Europe Supervisory Boards. Certain matters are reserved for the specific NLSB where individual company board approval is required.
  - The NL Management Board ("**NLMB**"): this consists of three Assurant Europe managing directors. The NLMB sits below the NLSB, and the primary objective of the NLMB is to manage Assurant Europe in accordance with applicable good governance rules, codes and regulations and in line with company objectives.  
  
The NLMB of each Assurant Europe company has common membership and thus operate as a consolidated governance structure for the Assurant Europe companies and will normally sit as a consolidated Management Board representing each of the Assurant Europe Management Boards. Certain matters are reserved for the specific NLSB where individual company board approval is required.
- 4.101 The NLSB is supported by the Board Audit Risk and Compliance Committee ("**NL ARCC**"). The key responsibilities of the NL ARCC include overseeing the statutory audit, monitoring the financial reporting process, monitoring the effectiveness of the internal quality control and risk management systems and monitoring the audit of the annual and consolidated financial statements.
- 4.102 In addition, the NLMB is supported by a number of management-level sub-committees and forums to enable it to perform its duties, including the EU Management Risk Committee, the EU Insurance Committee, the Solvency and Capital Forum and the Reserving Forum.
- 4.103 While the NLMB is responsible for day-to-day management, there are a number of matters reserved for the NLSB's decision covering specified aspects of corporate governance, corporate structure, strategy, risk management, capital and liquidity, internal controls etc. Where appropriate, such matters are also referred to the individual company board for approval.

### AEI's risk management strategy

- 4.104 Assurant Europe will maintain a Risk Management Framework, through which risk management is embedded throughout Assurant Europe, including AEI, consistent with that in place within AEG. The Assurant Europe Head of Risk will be responsible for oversight of the application of the Risk Management Framework.
- 4.105 The key components of the Assurant Europe Risk Management Framework include:
- **Risk strategy:** this summarises Assurant Europe's approach to managing risks, including the risk lifecycle of: identification, assessment, management and reporting, and monitoring.
  - **Risk appetite:** this articulates the short to medium term willingness of Assurant Europe to accept a certain level of risk, for each material risk that it is exposed to, with associated tolerances.
  - **Risk framework:** this details for each identified key risk category: the committees within Assurant Europe who oversee the risk profile, the relevant underlying policies and the risk sub-categories.
  - **Risk register:** this sets out the requirement to maintain a risk register for all identified risks, which includes, for each risk, a risk owner, risk likelihood and impact and the controls in place.
  - **Event management:** this specifies the requirement for reporting risk events and ensuring suitable mitigating actions are considered.
  - **ORSA:** this provides a comprehensive assessment of how Assurant Europe manages risk, its current and forward-looking risk exposure and the ability to meet capital requirements.
  - **Stress and scenario testing:** this considers forward-looking stresses of extreme, but realistic scenarios that could affect Assurant Europe. This is performed on an annual cycle.

### AEI's capital management

- 4.106 AEI intends to prepare its Solvency II results in accordance with the Standard Formula and does not intend to make use of the Solvency II USP adjustments.
- 4.107 I have been provided with Assurant Europe's Capital Management Policy, which covers the capital management of AEI. The Assurant Europe Capital Management Policy sets out requirements for the assessment, monitoring and reporting of AEI's capital position, the capital planning process, the capital allocation process and rules surrounding dividend declarations and intragroup transactions.
- 4.108 AEI's capital position is assessed with reference to two capital buffers, and the Assurant Europe Capital Management Policy sets out actions available depending on how the AEI SCR Ratio compares to the two capital buffers. The capital buffers are set with reference to the SCR.
- 4.109 The higher of the two capital buffers is referred to as the AEI Target Capital, and the lower of the two capital buffers is referred to as the AEI Minimum Capital Buffer. If the AEI SCR Ratio:
- Is above the AEI Target Capital then no action is taken and a dividend distribution is considered;
  - Is, or is projected to be, below the AEI Target Capital but above the AEI Minimum Capital Buffer then no action is taken but a dividend distribution is not considered; or
  - Is, or is projected to be, below the AEI Minimum Capital Target Buffer but above the regulatory capital requirement then management actions will be proposed by the Chief Financial Officer for approval by the Assurant Europe Management Board and a dividend distribution will not be considered.
  - Is below, or has the potential be below, the regulatory capital requirement then, in addition to the actions shown above, AEI will notify the DNB and will agree an action plan.
- 4.110 The two capital buffers are set by the NLSB, with consideration to the volume of business within AEI and the duration of the remaining liabilities.
- 4.111 AEI Target Capital has initially been set at 140%, which I note is higher than the Target Capital levels of both AGIL and LGI.

### AEI's conduct and complaints

- 4.112 AEG has adopted a consistent framework of corporate policies and processes across its European business. As such, AEI's approach to conduct and complaints will be as set out for AGIL, in paragraphs 4.48-4.51, above.
- 4.113 As there will be no material change in the staff, other resources and operational framework supporting AEI from those already supporting the relevant business of LGI and AGIL's business, the conduct and complaints processes are effectively already embedded in the operational framework of AEI, in readiness for the implementation of the Scheme.

### AEI's administration and servicing arrangements

- 4.114 The administration and servicing of the Transferring Policies will continue to be outsourced to AEG member companies in the relevant territories and to external specialist providers, exactly as they currently are.
- 4.115 The only change to the internal AEG companies involved in providing these services will be on policies underwritten by LGI, in respect of which policy servicing is outsourced currently to the Amsterdam branch of TWGS, a direct subsidiary of TWGE. TWGS is authorised in the UK and operates in the EEA under passporting arrangements. Therefore, its Amsterdam branch is unlikely to remain authorised to operate in EEA states after the termination of the Transitional Period and therefore is likely to be unable to continue to carry out its servicing of the LGI Transferring Policies. AES will be the new legal entity that will administer and service the LGI Transferring Policies post the Effective Date. All employees from the Amsterdam branch of TWGS will move to AES and the administration and servicing will be provided via the same systems. The staff and management and the processes and controls in place for such servicing will be fundamentally the same as before the Scheme.
- 4.116 No change will take place as a result of the Scheme to the location, resources or processes used in administering these transferred policies. The service providers will make use of the same systems and the staff and management responsible and the processes and controls in place for such servicing will be fundamentally the same as before the Scheme. Thus, the Transferring Policyholders should not experience any material change in the services or quality of services to support their Transferring Policies.

### THE TRANSFERRING POLICIES

- 4.117 The Transferring Policies comprise the following lines of business:
- AGIL Transferring Policies: mobile phone insurance, electronic gadget insurance, extended warranty programmes covering consumer electronic devices, creditor insurance, furniture warranty and jewellery warranty;
  - LGI Transferring Policies: motor warranty (including Guaranteed Asset Protection and ancillary insurance cover), appliance and technology covers and creditor insurance.
- 4.118 As at 14 April 2020, there were approximately 1.2 million AGIL Transferring Policies and approximately 3.9 million LGI Transferring Policies for the purposes of the Scheme.
- 4.119 In Figure 4.10, below, I set out the technical provisions, on a UK GAAP basis, relating to the Transferring Policies as at 31 December 2019. The ceded amounts for LGI included the amounts (£12,912k) ceded to VSC. In Figure 4.11, below, I set out the same information but on a Solvency II basis.

FIGURE 4.10 UK GAAP TECHNICAL PROVISIONS RELATING TO THE TRANSFERRING POLICIES AS AT 31 DECEMBER 2019 (£'000)

		Gross of Reinsurance	Ceded	Net of Reinsurance
AGIL	UPR	30,763	-2,595	28,168
	Claims Outstanding	6,652	-2,045	4,607
	<b>TOTAL GAAP RESERVES</b>	<b>37,415</b>	<b>-4,640</b>	<b>32,775</b>
LGI	UPR	79,929	-23,837	56,092
	Claims Outstanding	29,824	-6,056	23,768
	<b>TOTAL GAAP RESERVES</b>	<b>109,752</b>	<b>-29,892</b>	<b>79,860</b>
TOTAL	UPR	110,692	-26,432	84,260
	Claims Outstanding	36,476	-8,101	28,375
	<b>TOTAL GAAP RESERVES</b>	<b>147,168</b>	<b>-34,532</b>	<b>112,635</b>

FIGURE 4.11 SOLVENCY II TECHNICAL PROVISIONS RELATING TO THE TRANSFERRING POLICIES AS AT 31 DECEMBER 2019 (£'000)

		Gross of Reinsurance	Risk margin	Ceded	Net of Reinsurance
AGIL	Premium Provisions	12,607		-787	11,820
	Claims Provisions	7,689		-2,656	5,033
	<b>TOTAL TECHNICAL PROVISIONS</b>	<b>20,296</b>	<b>3,873</b>	<b>-3,443</b>	<b>20,727</b>
LGI	Premium Provisions	35,214		-6,726	28,488
	Claims Provisions	29,036		-5,875	23,161
	<b>TOTAL TECHNICAL PROVISIONS</b>	<b>64,249</b>	<b>3,165</b>	<b>-12,601</b>	<b>54,814</b>
TOTAL	Premium Provisions	47,821		-7,513	40,308
	Claims Provisions	36,725		-8,531	28,194
	<b>TOTAL TECHNICAL PROVISIONS</b>	<b>84,546</b>	<b>7,039</b>	<b>-16,044</b>	<b>75,541</b>

4.120 Figure 4.11, above, when considered in the context of Figure 4.3 and Figure 4.7, both above, shows that the AGIL Transferring Policies account for nearly 98% of AGIL's TPs, net of reinsurance, as at 31 December 2019. It also shows that the LGI Transferring Policies account for nearly 82% of LGI's TPs, net of reinsurance, as at 31 December 2019.

#### IMPACT OF THE COVID-19 PANDEMIC ON THE COMPANIES

4.121 The COVID-19 pandemic has affected, and will affect, many aspects of the Companies, in particularly operationally and financially.

##### Operational impact

4.122 The entities within AEG have been following national government guidance, with the result that many of their offices have been closed and will remain closed until restrictions are lifted. Some offices remain open for access by critical staff members but, where possible, staff are working from home. All contact centres are now successfully working 100% remotely. The IT infrastructure has been enhanced to increase its capability to support mass home working.

4.123 The closedown has resulted in some operating restrictions for AEG's contact centres (for example, reduced access) and repair/warehouse providers.

4.124 It is likely that these operational factors will have some impact upon claims patterns, claims notification patterns and claims settlement patterns.

##### Financial impact

4.125 A number of other possible risks, which are largely financial, have been identified and their impact is being assessed. These include:

- Possible impact on new business due to reduced consumer economic activity and the closure of retail distribution channels in the UK and EU;

- Possible impact on claims costs due to a scarcity of supply of parts for repair (which might also lead to increased use of replacement or cash settlement as an alternative to repair);
  - Possible impact on claims costs relating to creditor/payment protection portfolios. These policies provide cover in the event of long-term sickness or unemployment. It is not expected that there will be a material increase in sickness-related claims but (and despite the support packages initiated by many national governments, aimed at reducing levels of pandemic-induced redundancies) there is a risk of heightened claims triggered by unemployment;
  - Possibility of increased creditor claims due to higher mortality and unemployment rates, and possibly to cancellation rates;
  - Liquidity risk from reduced cash inflow due to reduction in new business, although a significant proportion of the insurers' business comes through monthly pay products that may continue to provide cashflow;
  - Risk of failure of counterparties including:
    - clients in the retail sector / high street who collect premiums from end customers on behalf of AEG;
    - banking counterparties who might suffer material credit losses themselves; and
    - reinsurance counterparties (although the exposure to reinsurers is limited);
  - Possible losses on the investment portfolios – reducing interest rates and widening credit spreads as well as the potential for default or downgrade or material parts of the portfolio.
    - The investment portfolios of AGIL and LGI comprise high quality fixed income government securities and corporate bonds with a small proportion of collateralised securities, with an average duration of 4-5 years for AGIL and 2-3 years for LGI. Worsening credit spreads to the end of March have caused the value of these portfolios to reduce but not to the extent that materially affected the Capital Cover Ratio of either entity.
    - Liaising with Assurant's global investment team and with Assurant's external investment advisors, the AEG actuarial team has been considering various extreme stress scenarios. None of those evaluated materially affected the Capital Cover Ratio of either entity.
    - The assets of AEI are currently all in cash and so have been unaffected by the COVID-19 pandemic (although the bank counterparty risk might have increased).
- 4.126 It is possible that there will be further consequences to the insurance industry throughout Europe, including to AEG, from COVID-19. There is, for example, the risk of changes to insurance regulation, the risk of levies against insurance premiums to help pay for some of the support programmes that governments have introduced for businesses and individuals in their respective countries, and the risk of further government intervention in the market. Such measures may well differ between countries, even between EU member states.

## 5. The proposed Scheme

### SUMMARY OF THE SCHEME

- 5.1 In this section of the Report, I summarise the terms of the Scheme, as set out in the Scheme Document. For the avoidance of doubt, the terms of the Scheme as set out in the Scheme Document are definitive.
- 5.2 Assuming that the Court approves the Scheme as proposed, the Transferring Business will be transferred from AGIL and from LGI (the Transferors) to AEI (the Transferee) at and with effect from 23.59 hours GMT on the Effective Date (2 November 2020). The Transferring Business will include, without limitation, all of the assets, liabilities and policies of AGIL and of LGI that relate to the Transferring Policies, including all rights, liabilities and obligations that pertain to those assets, liabilities and policies. This will include all data in relation to the Transferred Business to enable AEI to assume its rights and obligations, including all relevant Personal Data.
- 5.3 The Transferring Assets will also include most of those outwards reinsurance contracts pertaining to the Transferring Policies, other than the quota share reinsurance contract issued by VSC, which will remain with LGI.
- 5.4 The liabilities being transferred under the Scheme to AEI shall explicitly not include tax or regulatory liabilities. In this context, regulatory liabilities would include any liabilities arising out of past mis-selling, for example of payment protection policies.
- 5.5 Each party shall ensure that all Personal Data transferred to AEI as part of the Transferring Business is transferred in compliance with the provisions of all relevant Data Protection Laws and in a manner that permits AEI to process the Personal Data in the normal course of operating the Transferring Business on and from the Effective Date. This includes, but is not limited to, requesting the Court to order the transfer of all relevant Personal Data (including special categories of personal data) as defined in the Data Protection Laws from AGIL and LGI to AEI.
- 5.6 There will be no changes to the terms and conditions of any policy included within the Transferring Business as a result of the Scheme. The rights and obligations of AGIL and of LGI under the policies that comprise the Transferring Business will be transferred, without alteration, to AEI. Similarly, it is intended that there will be no change in how the Transferring Business is administered as a result of the Scheme. All holders of policies included within the Transferring Business will be entitled to the same rights against AEI as were available to them against AGIL or LGI under such policies and will be accountable to AEI for any further or additional premiums or other amounts attributable or referable thereto as and when the same become due and payable.
- 5.7 Any pending or current proceedings or complaints issued or served before the Effective Date by or against either AGIL or LGI in connection with the Transferring Business shall be continued by or against AEI in place of AGIL or LGI, and AGIL and LGI shall cease to have any liability under those proceedings following the Effective Date. Any proceedings or complaints issued or served on or after the Effective Date that would hitherto have been by or against AGIL or LGI will instead be by or against AEI. AEI shall be entitled to all defences, claims, counterclaims and rights of set-off that would have been available to either AGIL or LGI in respect of the Transferring Business.
- 5.8 Any judgment, order or award in respect of the AGIL Transferring Business or the LGI Transferring Business that is not fully satisfied before the Effective Date will become enforceable by or against AEI in the place of AGIL or LGI respectively.
- 5.9 With effect from the Effective Date, AEI shall indemnify AGIL and LGI against any loss or expense incurred by AGIL or LGI that is attributable to the Transferring Business.
- 5.10 The terms of the Scheme are governed by English law.

## MOTIVATION FOR THE SCHEME

- 5.11 As outlined in paragraphs 3.27-3.31, above, following the UK's departure from the EU in January 2020, there is considerable uncertainty as to whether UK insurance companies will continue to be able to use passporting rights to write and service business into the rest of the EEA via the EU's freedom of establishment or freedom of service rules. Indeed, in a white paper, dated July 2018 and entitled "*The Future Relationship between the United Kingdom and the European Union*", the UK government made clear its expectation that future arrangements relating to financial services "*will not replicate the EU's passporting regimes*". It is still possible that a future trade deal between the UK and EU will include arrangements that would allow AGIL and LGI to continue run-off their existing EEA business from the UK. It is also possible that some or all of those individual EEA member states that are places of management for the EEA business of AGIL and LGI would introduce domestic legislation that would permit allowing AGIL and LGI to continue the run-off of their respective EEA business from the UK. However, it appears unlikely that AGIL or LGI would be able, post the Transition Period, to write new or to renew existing EEA business from the UK.
- 5.12 TWGE, LGI's parent company, has incorporated in the Netherlands a new subsidiary, AEI, which has been authorised by the DNB as an insurance company. Under EEA passporting rights, AEI is able to write insurance business for risks situated in EEA states and to service EEA business. Therefore, the primary motivation for the proposed Scheme is to enable adequate certainty and security for all stakeholders involved in the Transferring Policies, in particular to ensure that AEG is able to continue to service the business of AGIL and LGI that was written under EEA passporting rights, regardless of the outcome of the Brexit negotiations.

## POLICYHOLDERS AFFECTED

- 5.13 I have considered the effects of the Scheme on the following groups of policyholders:
- the Transferring Policyholders;
  - the policyholders of AGIL whose policies are not being transferred to AEI by the Scheme; and
  - the policyholders of LGI whose policies are not being transferred to AEI by the Scheme.
- 5.14 Currently, AEI has no policyholders. I have been told by AEG that it intends that AEI will only start writing business with effect from the Effective Date. However, it is possible that, prior to the Effective Date and in specific circumstances, AEI will write some policies. Those circumstances would be if AEG wrote EEA business relating to a new scheme, or to a new product within an existing scheme, within that period. I understand that, as at the date of this Report, AEG is pursuing eight such opportunities. I further understand that, once identified, it usually takes several months for such opportunities to become new business, if indeed they do come to fruition. Therefore, it is unlikely that any opportunity that manifests itself in future will develop into written new business prior to the Effective Date (as currently scheduled). Of the eight existing opportunities, it is uncertain how many (if any) will develop into written new business, but it is unlikely that any such business written prior to the Effective Date would be material. Moreover, I understand that policyholders of any such business would be informed ahead of the business of the planned Scheme. Therefore, in this Report I have not considered further the effects of the Scheme on the policyholders of any such business. If, by the time that I prepare my Supplementary Report, it has become apparent that there will be existing AEI policyholders by the Effective Date, then I will consider the impact of the Scheme on them within the Supplementary Report.
- 5.15 I do not consider that the policyholders of any other insurance companies are affected by the Scheme.

## RESIDUAL POLICIES

- 5.16 "**Residual Policies**" are those policies within the Transferring Policies that, for some reason<sup>9</sup>, cannot be transferred to AEI as at the Effective Date. All assets and liabilities that relate to the Residual Policies will not be transferred to AEI as at the Effective Date but will remain with AGIL or LGI, as appropriate, with the intention that each Residual Policy (and related assets and liabilities) will be transferred to AEI subsequently.

<sup>9</sup> As an example, a possible reason for a Transferring Policy becoming a Residual Policy would be because not all of the necessary consents or permissions had been received as at the Effective Date.

- 5.17 As and when all consents, permissions or other requirements for the transfer of a Residual Policy from AGIL or LGI to AEI have been obtained, such Residual Policy will promptly be transferred to AEI, together with the assets and liabilities that relate to the Residual Policy. Thereafter, it shall be treated in all respects as if it had been transferred to AEI with effect from the Effective Date.
- 5.18 If any Residual Policy is novated to AEI, then such Residual Policy shall thereafter be dealt with by AEI under the provisions of this Scheme in all respects as if such Residual Policy had been transferred to AEI with effect from the Effective Date.
- 5.19 It is not intended that there will be any Residual Policies.

#### CREDITOR INSURANCE POLICIES

- 5.20 Both AGIL and LGI have written policies that cover one or more of the following insurance risks: death, disability, sickness and unemployment. I refer to such policies in this document as “**Assurant Creditor Policies**”.
- 5.21 Most of the Assurant Creditor Policies are included within the Transferring Business.
- 5.22 Some of the Assurant Creditor Policies that were written by LGI contain a life insurance element. That element of the cover has been provided by LGL. None of the Creditor Policies written by AGIL contains any life insurance element.
- 5.23 I refer to those Assurant Creditor Policies that were written by LGI, that contain a life insurance element and which are included within the Transferring Business as “**LGI EEA Creditor Policies**”.
- 5.24 In Figure 5.1, below, I set out the numbers of Assurant Creditor Policies as at 31 December 2019. The LGI EEA Creditor Policies are shown in the column headed “LGI (linked with LGL)”.

**FIGURE 5.1 NUMBERS OF CREDITOR POLICIES AS AT 31 DECEMBER 2019**

	AGIL	LGI (stand-alone)	LGI (linked with LGL)	TOTAL
UK	170	106		276
<b>TOTAL Not Transferring</b>	<b>170</b>	<b>106</b>	<b>0</b>	<b>276</b>
Belgium		146	3,591	3,737
Germany		13		13
Ireland		665	22	687
Italy	4,495	351		4,846
Netherlands		50,992	249	51,241
Spain	1,957	278		2,235
Miscellaneous	639			639
<b>TOTAL Transferring</b>	<b>7,091</b>	<b>52,445</b>	<b>3,862</b>	<b>63,398</b>
<b>TOTAL</b>	<b>7,261</b>	<b>52,551</b>	<b>3,862</b>	<b>63,674</b>

- 5.25 In Figure 5.2, below, I set out the TPs in respect of the Assurant Creditor Policies as at 31 December 2019. The table does not differentiate between the LGI EEA Creditor Policies and the remaining Assurant Creditor Policies written by LGI.

FIGURE 5.2 SOLVENCY II TECHNICAL PROVISIONS IN RESPECT OF EEA CREDITOR POLICIES AS AT 31 DECEMBER 2019 (€'000)

	Gross of Reinsurance			Net of Reinsurance		
	Premium Provision	Claims provision	Total	Premium Provision	Claims provision	Total
<b>Non-transferring Business</b>						
<b>AGIL</b>						
Disability	1	234	235	1	234	235
Unemployment	78	207	285	78	207	285
<b>TOTAL AGIL</b>	<b>79</b>	<b>441</b>	<b>520</b>	<b>79</b>	<b>441</b>	<b>520</b>
<b>LGI</b>						
Specialty Accident and Sickness	0	8	8	0	6	6
Specialty Loss of Work	0	30	30	0	2	2
<b>TOTAL LGI</b>	<b>0</b>	<b>38</b>	<b>38</b>	<b>0</b>	<b>8</b>	<b>8</b>
<b>TOTAL Non-Transferring</b>	<b>79</b>	<b>479</b>	<b>558</b>	<b>79</b>	<b>449</b>	<b>527</b>
<b>Transferring Business</b>						
<b>AGIL</b>						
Disability	36	87	122	34	-45	-11
Unemployment	43	63	105	33	48	82
<b>TOTAL AGIL</b>	<b>78</b>	<b>150</b>	<b>228</b>	<b>67</b>	<b>3</b>	<b>70</b>
<b>LGI</b>						
Specialty Accident and Sickness	2,038	23,493	25,531	1,662	18,795	20,457
Specialty Loss of Work	898	633	1,531	743	507	1,250
<b>TOTAL LGI</b>	<b>2,936</b>	<b>24,127</b>	<b>27,063</b>	<b>2,405</b>	<b>19,302</b>	<b>21,707</b>
<b>TOTAL Non-Transferring</b>	<b>3,014</b>	<b>24,276</b>	<b>27,290</b>	<b>2,471</b>	<b>19,305</b>	<b>21,777</b>
<b>TOTAL ALL BUSINESS</b>	<b>3,093</b>	<b>24,755</b>	<b>27,848</b>	<b>2,550</b>	<b>19,754</b>	<b>22,304</b>

- 5.26 Subject to the sanction by the Court of the Assurant Life Scheme, LGL's rights and obligations under each of the LGI EEA Creditor Policies will be transferred to AEL.
- 5.27 The transfer of LGI's rights and obligations under each of the LGI EEA Linked Policies to AEI under this Scheme shall be subject to:
- the Court sanctioning the Assurant Life Scheme; and
  - the Scheme and the Assurant Life Scheme both becoming effective on the Effective Date.
- 5.28 Were the Assurant Life Scheme not to be approved or its implementation to be delayed, the LGI EEA Creditor Policies would become Residual Policies on the Effective Date. They would remain so until the Assurant Life Scheme were implemented or until the Companies arranged by other means (e.g. novation) the transfer to LGL of the life insurance element of the LGI EEA Creditor Policies.

#### POLICY ADMINISTRATION

- 5.29 The current administration and servicing arrangements for the Transferring Business are set out in paragraphs 4.48-4.56, above, in respect of AGIL, and in paragraphs 4.86-4.89, above, in respect of LGI. The post-Scheme administration and servicing arrangements for the Transferring Business are set out in paragraphs 4.112-4.116, above.
- 5.30 The administration and servicing of the Transferring Business will be conducted post-Scheme by the same outsourced entities (with one exception<sup>10</sup>) as it is currently, conducted with the same staff and management as it is currently, using the same processes and systems as currently used, and under the same policy framework as now. There will be no need to migrate policy data from one administration system to another. Therefore, it is neither intended nor expected that there be any change in the administration or servicing of the Transferring Business as a result of the Scheme.

<sup>10</sup> As explained in paragraph 4.115, above, policy servicing for the LGI Transferring Business is currently outsourced to the Amsterdam branch of TWGS. Post-Scheme, policy servicing for the LGI Transferring Business will be outsourced to AES. All employees from the Amsterdam branch of TWGS will move to AES with effect from the Effective Date and the administration and servicing will be provided via the same systems

- 5.31 On and with effect from the date on which the Scheme is effected (“**Effective Date**”), AEI shall become and assume the responsibilities of the Controller of any Personal Data, to the extent that it relates to the Transferred Business and is subject to the Data Protection Laws, in place of AGIL or LGI, as appropriate. Each of AGIL and LGI shall provide such assistance to AEI as AEI may reasonably require from time to time in order to meet its obligations under Data Protection Laws.

#### EFFECT OF THE SCHEME ON THE BALANCE SHEETS AND CAPITAL COVER RATIO OF AGIL, LGI AND AEI

- 5.32 Figure 5.3, below, shows simplified balance sheets for AGIL as at 31 December 2019 in two situations (all on a UK GAAP basis):

- The "Actual" column shows the actual balance sheet as at 31 December 2019.
- The "Post-Scheme" column shows what the balance sheet would have looked like as at 31 December 2019 had the Scheme been approved and become effective as at 31 December 2019. This would have removed all assets and liabilities that related to the AGIL Transferring Policies from the AGIL balance sheet. This assumes no Residual Policies remain within AGIL post-Scheme.

- 5.33 I show the same in Figure 5.4, below, but on a Solvency II basis.

**FIGURE 5.3 SIMPLIFIED UK GAAP BALANCE SHEETS FOR AGIL AS AT 31 DECEMBER 2019 (IN £M)**

	Actual	Impact of Scheme	Post-Scheme
<b>Assets</b>			
Investments	77.4	-8.5	68.9
Reinsurers' share of technical provisions	11.3	-4.6	6.7
Cash	5.3	0.0	5.3
Deferred acquisition costs ("DAC")	11.4	-10.9	0.4
Other assets	85.5	-19.2	66.3
<b>Total Assets</b>	<b>190.8</b>	<b>-43.2</b>	<b>147.6</b>
<b>Liabilities</b>			
Capital and reserves	83.6	0.0	83.6
Gross technical provisions	52.3	-37.4	15.0
Reinsurance share of DAC	0.0	0.0	0.0
Other liabilities	54.9	-5.9	49.0
<b>Total Liabilities</b>	<b>190.8</b>	<b>-43.2</b>	<b>147.6</b>

**FIGURE 5.4 SIMPLIFIED SOLVENCY II BALANCE SHEETS FOR AGIL AS AT 31 DECEMBER 2019 (IN £M)**

	Actual	Impact of Scheme	Post-Scheme
<b>Assets</b>			
Investments	78.4	-8.5	70.0
Reinsurers' share of technical provisions	2.9	-3.4	-0.6
Cash	5.3	0.0	5.3
Deferred acquisition costs ("DAC")	0.0	0.0	0.0
Other assets	83.0	-19.2	63.7
<b>Total Assets</b>	<b>169.6</b>	<b>-31.1</b>	<b>138.4</b>
<b>Liabilities</b>			
Capital and reserves	87.9	-1.1	86.8
Gross technical provisions	26.6	-24.2	2.5
Reinsurance share of DAC	0.0	0.0	0.0
Other liabilities	55.0	-5.9	49.2
<b>Total Liabilities</b>	<b>169.6</b>	<b>-31.1</b>	<b>138.4</b>

5.34 Figure 5.5, below, shows simplified balance sheets for LGI as at 31 December 2019 in two situations (all on a UK GAAP basis):

- The "Actual" column shows the actual balance sheet as at 31 December 2019.
- The "Post-Scheme" column shows what the balance sheet would have looked like as at 31 December 2019 had the Scheme been approved and become effective as at 31 December 2019. This would have removed all assets and liabilities that related to the LGI Transferring Policies from the LGI balance sheet. At the same time (or shortly beforehand), LGI would have paid a dividend, which would then have been paid by AEG into AEI to provide it with the planned level of capital. This assumes no Residual Policies remain within LGI post-Scheme. I also show explicitly the impact of cancelling the quota share reinsurance arrangement with VSC in respect of the Transferring Business.

5.35 I show the same in Figure 5.6, below, but on a Solvency II basis.

**FIGURE 5.5 SIMPLIFIED UK GAAP BALANCE SHEETS FOR LGI AS AT 31 DECEMBER 2019 (IN £M)**

	Actual	Dividend payment	Recapture of QS	Impact of Scheme	Post-Scheme
<b>Assets</b>					
Investments	165.0	-25.8	0.0	-66.1	73.1
Reinsurers' share of technical provisions	48.7	0.0	-20.0	-9.9	18.8
Cash	2.6	0.0	0.0	0.0	2.6
Deferred acquisition costs ("DAC")	76.3	0.0	5.8	-29.1	53.1
Other assets	43.4	0.0	14.8	-16.2	42.0
<b>Total Assets</b>	<b>336.1</b>	<b>-25.8</b>	<b>0.6</b>	<b>-121.3</b>	<b>189.6</b>
<b>Liabilities</b>					
Capital and reserves	87.0	-25.8	0.0	0.0	61.2
Gross technical provisions	175.8	0.0	0.0	-109.8	66.0
Reinsurance share of DAC	3.2	0.0	0.6	-3.2	0.6
Other liabilities	70.1	0.0	0.0	-8.3	61.8
<b>Total Liabilities</b>	<b>336.1</b>	<b>-25.8</b>	<b>0.6</b>	<b>-121.3</b>	<b>189.6</b>

**FIGURE 5.6 SIMPLIFIED SOLVENCY II BALANCE SHEETS FOR LGI AS AT 31 DECEMBER 2019 (IN £M)**

	Actual	Dividend payment	Recapture of QS	Impact of Scheme	Post-Scheme
<b>Assets</b>					
Investments	177.1	-25.8	0.0	-66.1	85.2
Reinsurers' share of technical provisions	18.1	0.0	-12.9	0.3	5.5
Cash	4.5	0.0	0.0	0.0	4.5
Deferred acquisition costs ("DAC")	0.0	0.0	0.0	0.0	0.0
Other assets	5.2	0.0	12.9	-12.9	5.2
<b>Total Assets</b>	<b>205.0</b>	<b>-25.8</b>	<b>0.0</b>	<b>-78.7</b>	<b>100.5</b>
<b>Liabilities</b>					
Capital and reserves	90.8	-25.8	0.0	-2.9	62.0
Gross technical provisions	100.8	0.0	0.0	-67.4	33.4
Reinsurance share of DAC	0.0	0.0	0.0	0.0	0.0
Other liabilities	13.4	0.0	0.0	-8.3	5.0
<b>Total Liabilities</b>	<b>205.0</b>	<b>-25.8</b>	<b>0.0</b>	<b>-78.7</b>	<b>100.5</b>

5.36 Figure 5.7, below, shows what AEI's balance sheet would have looked like as at 31 December 2019, on a GAAP basis, had AEI received LGI's projected dividend payment as at that date, had AEI been authorised by then by the DNB to write and accept insurance business, and had the Scheme been approved and become effective as at that date. Figure 5.8, below, replicates Figure 5.7 but on a Solvency II basis.

FIGURE 5.7 SIMPLIFIED GAAP BALANCE SHEETS FOR AEI AS AT 31 DECEMBER 2019 (IN £M)

	Actual	Capital injection	Impact of Scheme	Post-Scheme
<b>Assets</b>				
Investments	0.0	25.8	74.6	100.3
Reinsurers' share of technical provisions	0.0	0.0	14.5	14.5
Cash	35.1	0.0	0.0	35.1
Deferred acquisition costs ("DAC")	0.0	0.0	40.0	40.0
Other assets	0.0	0.0	35.4	35.4
<b>Total Assets</b>	<b>35.1</b>	<b>25.8</b>	<b>164.5</b>	<b>225.4</b>
<b>Liabilities</b>				
Capital and reserves	35.1	25.8	0.0	60.9
Gross technical provisions	0.0	0.0	147.1	147.1
Reinsurance share of DAC	0.0	0.0	3.2	3.2
Other liabilities	0.0	0.0	14.2	14.2
<b>Total Liabilities</b>	<b>35.1</b>	<b>25.8</b>	<b>164.5</b>	<b>225.4</b>

FIGURE 5.8 SIMPLIFIED SOLVENCY II BALANCE SHEETS FOR AEI AS AT 31 DECEMBER 2019 (IN £M)

	Actual	Capital injection	Impact of Scheme	Post-Scheme
<b>Assets</b>				
Investments	0.0	25.8	74.6	100.3
Reinsurers' share of technical provisions	0.0	0.0	3.1	3.1
Cash	35.1	0.0	0.0	35.1
Deferred acquisition costs ("DAC")	0.0	0.0	0.0	0.0
Other assets	0.0	0.0	41.7	41.7
<b>Total Assets</b>	<b>35.1</b>	<b>25.8</b>	<b>119.4</b>	<b>180.2</b>
<b>Liabilities</b>				
Capital and reserves	35.1	25.8	5.9	66.8
Gross technical provisions	0.0	0.0	99.2	99.2
Reinsurance share of DAC	0.0	0.0	0.0	0.0
Other liabilities	0.0	0.0	14.2	14.2
<b>Total Liabilities</b>	<b>35.1</b>	<b>25.8</b>	<b>119.4</b>	<b>180.2</b>

5.37 I note that, on a Solvency II basis, the sum of the "Gross technical provisions" for AGIL and LGI shown transferring under the Scheme is £7.6 million less than the "Gross technical provisions" being received under the Scheme by AEI. There is also an identical difference between the sum of the "Other assets" for AGIL and LGI shown transferring under the Scheme and those being received under the Scheme by AEI. The reason for this is that, hitherto, AGIL and LGI have presented differently from each other their technical provisions in their respective Solvency II balance sheets:

- LGI presents its technical provisions on the liability side of the balance sheet net of expected future premium receipts;
- AGIL presents its technical provisions on the liability side of the balance sheet gross of expected future premium receipts, and then books expected future premium receipts on the asset side of the balance sheet, under "Other assets" (receivables).

5.38 Post-Scheme, the transferred technical provisions have to be treated consistently within the AEI Solvency II balance sheet. AEI has decided to adopt the AGIL approach. Therefore, on transfer, the gross technical provisions for the LGI Transferring Business will be "grossed-up" by £7.6 million so that they are gross of expected future premium receipts, and there will be an equal addition "Other assets" (receivables). As this adjustment affects both sides of the Solvency II balance sheet equally, there is no impact on the Own Funds.

5.39 I discuss the reserving strength of AGIL, LGI and AEI in more detail in Section 6, below.

5.40 Figure 5.9, below, shows AGIL's eligible own funds and solvency capital requirements as at 31 December 2019 in two situations:

- The "Pre-Scheme" columns shows the actual eligible own funds and solvency requirements as at 31 December 2019.
- The "Post-Scheme" columns show what the actual eligible own funds and solvency requirements would have been as at 31 December 2019 had the Scheme been approved and become effective as at 31 December 2019.

5.41 In Figure 5.10 and Figure 5.11, further below, I provide the equivalent information to that in Figure 5.9, relating to LGI and AEI respectively (post-Scheme only for AEI).

**FIGURE 5.9 ELIGIBLE OWN FUNDS AND SOLVENCY CAPITAL REQUIREMENTS FOR AGIL AS AT 31 DECEMBER 2019 (IN £M)**

	MCR	SCR	MCR	SCR
<b>Eligible Own Funds to meet the solvency requirement</b>	87.9	87.9	86.8	86.8
<b>Solvency requirement</b>	19.3	59.6	13.7	54.9
<b>Surplus</b>	68.6	28.3	73.1	31.9
<b>Coverage</b>	456%	148%	633%	158%

**FIGURE 5.10 ELIGIBLE OWN FUNDS AND SOLVENCY CAPITAL REQUIREMENTS FOR LGI AS AT 31 DECEMBER 2019 (IN £M)**

	Pre-Scheme		Post-Scheme	
	MCR	SCR	MCR	SCR
<b>Eligible Own Funds to meet the solvency requirement</b>	89.3	90.8	61.0	62.0
<b>Solvency requirement</b>	15.4	46.2	5.1	20.4
<b>Surplus</b>	73.9	44.5	55.9	41.7
<b>Coverage</b>	580%	196%	1199%	305%

**FIGURE 5.11 ELIGIBLE OWN FUNDS AND SOLVENCY CAPITAL REQUIREMENTS FOR AEI AS AT 31 DECEMBER 2019 (IN £M)**

	MCR	SCR
<b>Eligible Own Funds to meet the solvency requirement</b>	66.8	66.8
<b>Solvency requirement</b>	10.9	43.5
<b>Surplus</b>	55.9	23.3
<b>Coverage</b>	614%	154%

5.42 I note that all of the Companies exceed their target capital ratios both pre-Scheme and post-Scheme (post-Scheme only for AEI, the pre-Scheme position being irrelevant).

#### Balance sheets as at the Effective Date

5.43 The Effective Date will be approximately 10 months after 31 December 2019. I have been provided with pro forma balance sheets, similar to those shown in Figure 5.3-Figure 5.11, above, that allow for the planned movements in the balance sheets of AGIL and LGI and in the assets and liabilities relating to the Transferring Business between 31 December 2019 and the Effective Date. These show a broadly similar picture, but with some differences. I explain these differences in paragraphs 5.43.1-5.43.6, below. However, the forecast Capital Cover Ratios are confidential and so I cannot detail them in this Report. Instead, I have indicated their broad magnitude, using qualitative descriptions defined in paragraph 6.4, below.

*UK GAAP basis*

- 5.43.1 **AGIL:** the pre-Scheme capital and reserves are projected to be greater as at the Effective Date than as at 31 December 2019, with the liabilities reducing over the period by more than the reduction in assets, i.e. the business is expected to generate an operating profit on a UK GAAP basis during the period. The forecast reduction in the liabilities during the period up to the Effective Date reduces the forecast value of the AGIL Transferring Business (and hence also of the AGIL Transferring Assets). The expected effect of the Scheme on AGIL's UK GAAP capital and reserves remains neutral.
- 5.43.2 **LGI:** the pre-Scheme capital and reserves are projected to be greater as at the Effective Date than as at 31 December 2019, with the liabilities reducing over the period by more than the reduction in assets, i.e. the business is expected to generate an operating profit on a UK GAAP basis during the period. The forecast reduction in the liabilities during the period up to the Effective Date reduces the forecast value of the LGI Transferring Business (and hence also of the LGI Transferring Assets). The expected effect of the Scheme on LGI's UK GAAP capital and reserves remains neutral.
- 5.43.3 **AEI:** (these figures are all post-Scheme) the capital and reserves are projected to be slightly less as at the Effective Date than they would have been as at 31 December 2019.

*Solvency II basis*

- 5.43.4 **AGIL:** the pre-Scheme Eligible Own Funds are projected to be greater as at the Effective Date than as at 31 December 2019, with the liabilities reducing over the period by more than the reduction in assets, i.e. the business is expected to generate an operating profit on a Solvency II basis during the period. The pre-Scheme SCR is also projected to be less than as at 31 December 2019, due to the reduced liabilities, leading to an increased Capital Cover Ratio. As at the Effective Date, AGIL is forecast to be a well-capitalised insurer. The forecast reduction in the liabilities during the period up to the Effective Date reduces the forecast value of the AGIL Transferring Business (and hence also of the AGIL Transferring Assets). Post-Scheme, AGIL remains forecast to be a well-capitalised insurer.
- 5.43.5 **LGI:** the pre-Scheme Eligible Own Funds are projected to be less as at the Effective Date than as at 31 December 2019, with the liabilities reducing over the period by less than the reduction in assets, i.e. the business is expected to generate an operating loss on a Solvency II basis during the period (I note that, on a UK GAAP basis, this business generates an operating profit – this reflects in particular the unwinding of the UPR, which does make any allowance for expected future profit). However, the reduced liabilities lead to the forecast pre-Scheme SCR being less than as at 31 December 2019, by an amount greater than the reduction in the Eligible Own Funds. This results in an increased Capital Cover Ratio. As at the Effective Date, LGI is forecast to be a very well-capitalised insurer. The forecast reduction in the liabilities during the period up to the Effective Date reduces the forecast value of the LGI Transferring Business (and hence also of the LGI Transferring Assets). Post-Scheme, LGI remains forecast to be a very well-capitalised insurer.
- 5.43.6 **AEI:** (these figures are all post-Scheme) the Eligible Own Funds are projected to be less as at the Effective Date than they would have been as at 31 December 2019, whereas the (post-Scheme) SCR is unchanged. These movements reduce slightly the Capital Cover Ratio, but that is forecast to remain above the Target Capital level and for AEI then to remain a well-capitalised insurer.
- 5.44 The above projections were largely prepared by the Companies prior to the COVID-19 pandemic starting to affect materially Western Europe. As discussed in paragraphs 4.121-4.126, above, the Assurant Group has considered the possible impact of the pandemic upon its current and forecast assets and liabilities. I have further discussed the impact of the COVID-19 pandemic on the Scheme in paragraphs 8.7-8.19, below. In my Supplementary Report, I will revisit the above forecast balance sheets and SCRs and will consider them in the light of the then most recent thinking about the likely effects on them of the pandemic.

## APPROACH TO COMMUNICATION WITH POLICYHOLDERS

- 5.45 The Companies have set out the approach that they intend to take in communicating information about the proposed Scheme to the affected policyholders and other parties. Their plans will be subject to approval by the Regulators and by the Court before the Companies can implement them.
- 5.46 The main objectives of the communications are to:
- Give those policyholders and others who might be affected by the Scheme the information that they need to understand the proposed changes;
  - Inform those policyholders and others who might be affected by the Scheme about the implications for them of the proposed changes;
  - Give those policyholders and others who might be affected by the Scheme access to further relevant information (beyond that in the communications pack);
  - Let those policyholders and others who might be affected by the Scheme know what steps they should take if they object to any of the proposed changes;
  - Maintain customers' confidence in AEI's willingness and ability to continue to meet its obligations in respect of the Transferring Business; and
  - Meet legal and regulatory requirements.
- 5.47 Where possible, the Companies intend to notify all existing Transferring Policyholders about the Scheme. They will each receive a covering letter and an information pack including
- a summary of the terms of the Scheme;
  - a summary of this Report;
  - a copy of the Notice which includes only the contact details which are relevant to the particular Policyholder;
  - answers to common questions that Policyholders may have regarding the Scheme;
  - where relevant, information about the cessation of coverage under the Financial Services Compensation Scheme for Transferring Policyholders; and
  - an overview of the legal process and the rights that policyholders and other persons who consider that they would be adversely affected by the proposed transfer have to object to the Scheme.
- 5.48 Following the issue of notification letters to existing Transferring Policyholders, the Companies also intend to provide copies of such letters to each new Transferring Policyholders up to the date of the final Court hearing.
- 5.49 AGIL and LGI intend notifying those of the Transferring Policyholders with whom they communicate on a business-as-usual basis and for whom they therefore hold the current contact information. For those Transferring Policyholders with whom AGIL and LGI communicate via the distributor or intermediary, AGIL and LGI will liaise with the relevant distributors/intermediaries, will provide them with notification letters and will arrange that they provide a copy to each of their underlying policyholders. AGIL and LGI will oversee the effectiveness of this process.
- 5.50 I note that it is possible that holders of EEA Creditor Policies might receive two letters, one relating to the Scheme and the other relating to the Assurant Life Scheme, which is running parallel to the Scheme. This aspect will be explained in the policyholder communications accordingly.
- 5.51 On the assumption that this Report concludes that the Scheme will not materially adversely affect Transferring Policyholders (see Sections 2, above, and 9, below), neither AGIL or LGI has taken any additional steps to obtain valid contact addresses for those identified, by AGIL, LGI or the distributors/intermediaries as having no valid contact address.
- 5.52 The Companies will be applying to the Court for waivers in respect of the requirement to make similar direct notification to the following groups:

- Transferring Policyholders for whom AGIL, LGI or the relevant distributors/intermediaries hold no valid contact details;
  - Transferring Policyholders whose contracts expired and for whom there is no on-going period of cover and no known current claims exposure; and
  - Those policyholders of AGIL and LGI who are not Transferring Policyholders.
- 5.53 AEI has not planned a communication programme with AEI policyholders, as, as at the date of this Report, it is not expected that there will be any prior to the Effective Date.
- 5.54 The Companies will include within the communication programme those reinsurers of either AGIL or LGI whose contracts will be transferred by the Scheme to AEI.
- 5.55 The Companies will monitor the contact process, recording the dates on which letters are sent (and returned and resent, also noting all address changes), any queries or objections raised by policyholders or other interested parties and, in each such case, their response.
- 5.56 In addition to direct, written correspondence, the Companies also plan to make indirect notification. FSMA indicates that such indirect notification will include notices in at least two national newspapers in the UK and in the other EEA states in which the risks are situated.
- 5.56.1 In the UK, a notice will be carried by the *Daily Mail*, *Financial Times* (UK edition) and *The Times*.
- 5.56.2 Between them, AGIL and LGI have distributed insurance in the following 18 EEA member states: Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Hungary, Ireland, Italy, Latvia, the Netherlands, Poland, Portugal, Romania, Spain and Sweden. AEG considers it very unlikely that the risk of any of the Transferring Policies is situated in an EEA member state other than the aforementioned 18 states as it was only in these states that it had relationships with insurance intermediaries and other distributors who then sold the Transferring Policies to their customers in the relevant member state. AGIL and LGI will publish the notice (translated if necessary into the local language) in a national newspaper in each of the above EEA states, other than Czech Republic, Denmark, Estonia, Finland, Latvia and Portugal. In those six states, there are a very low number of Transferring Policyholders, all of whom are commercial motor dealers, who will receive a direct communication about the Scheme from AGIL or LGI, as applicable. Additionally, the notice will be published in the international edition of the *Financial Times* - that newspaper is circulated in all EEA Member States, except Iceland and Liechtenstein. Hence, the Companies intend to publish in one national newspaper, not two, in each of Austria, Belgium, France, Germany, Hungary, Ireland, Italy, the Netherlands, Poland, Romania, Spain and Sweden, and not at all in the other 18 EEA member states.
- 5.56.3 In addition, a notice will be published in each of the London Gazette, the Edinburgh Gazette, the Belfast Gazette and the Irish Gazette. The notifications will also be placed on relevant websites where applicable.
- 5.57 The letters, notices and advertisements will include a postal address, a telephone number and a website address through any of which readers can lodge queries about the Scheme, and all of which will respond promptly (within standard UK working hours) to any such queries. It is intended that both this Report and the Supplementary Report will be published on the Transfer Websites, on pages dedicated to the Scheme, and that copies will be sent to any policyholders who request them. The Report will be made available in this way following the directions hearing relating to the Scheme and the Supplementary Report will likewise be made available at least one week before the date of the Court hearing at which the Scheme might be sanctioned.
- 5.58 I comment on this proposed approach to communications with policyholders in Section 8, below.

## 6. The impact of the Scheme on the Transferring Policyholders

### INTRODUCTION

- 6.1 Under the Scheme, the Transferring Business will be transferred to AEI.
- 6.2 The main issues affecting the Transferring Policyholders as a result of the Scheme are likely to arise from relative differences in:
- The financial strength of AEI post the Effective Date compared with that of AGIL and LGI pre the Effective Date. Financial strength is derived from:
    - the strength of the reserves held, relative to a best estimate of the outstanding liabilities;
    - excess assets or capital; and
    - specific financial support arrangements.
  - The risk exposures in AEI compared with those in AGIL and LGI.
  - The policy servicing levels provided by AEI post the Effective Date compared with those currently enjoyed by the Transferring Policyholders.

In this section of this Report, I deal with each of these in turn.

- 6.3 I note that the reserves held on a UK GAAP basis differ from the TPs that are used to determine the own funds available to meet the solvency capital requirements under Solvency II. However, the best estimate of the claims liabilities that underlie those shown in the Report & Accounts is usually used as the base for the best estimate of the claims provision under Solvency II, which then forms a key part of the TPs.
- 6.4 While key metrics under Solvency II, such as the SCR, MCR and Eligible Own Funds, are intended to be made public as part of each insurer's annual Solvency and Financial Condition Report ("**SFCR**"), other relevant metrics (for example, projected values of own funds and of solvency capital requirements as set out in insurers' ORSAs or in their quarterly Quantitative Reporting Templates ("**QRTs**")) are private matters between the entities and the relevant regulators. Therefore, I am not at liberty to disclose in this Report the actual values of those private metrics, or figures by which those values could be calculated. In this Report, I have considered the extent to which of AGIL, LGI and AEI each hold capital in excess of various solvency capital measures. Each entity will have different Capital Cover Ratios for different solvency measures. Where permitted (e.g. when dealing with publicly available information), I have expressed Capital Cover Ratios in numeric terms. In other instances, for comparative purposes in this Report, I have defined the following terms:
- "sufficiently capitalised" refers to a Capital Cover Ratio between 100% and 119%;
  - "more than sufficiently capitalised" refers to a Capital Cover Ratio between 120% and 149%;
  - "well-capitalised" refers to a Capital Cover Ratio between 150% and 199%, and
  - "very well-capitalised" refers to a Capital Cover Ratio in excess of 200%.

### RESERVE STRENGTH OF AGIL (PRE-SCHEME)

- 6.5 As set out in Figure 4.2, above, in its statutory accounts as at 31 December 2019, AGIL held gross technical provisions of £52.3 million (made up of £36.2 million of UPR and £16.1 million of outstanding claims). Reinsurers' share of technical provisions totalled £11.3 million (made up of £6.9 million of UPR and £4.4 million in respect of claims outstanding).
- 6.6 In this section of the Report, I provide details of my review of the reserve strength of AGIL. As the work underlying the reserves booked by AGIL has been used in its capital calculations (albeit indirectly), the appropriateness of these reserves is important in assessing the security currently afforded to the AGIL Transferring Policyholders.

- 6.7 I have been provided with details of the outstanding claims provision for AGIL as at 31 December 2019, the process by which the provisions were established and details of the actuarial review that underlies those provisions. The outstanding claims provision so developed and included in AGIL's financial statements (as at 31 December 2019) were prepared in accordance with UK GAAP.
- 6.8 I have not attempted to review in detail the calculations performed by the AEG actuary responsible for the actuarial review. Instead, I have reviewed the process by which reserves were set, the approach followed by the actuary, the key areas of reserve uncertainty and the apparent strength of the reserves based on this review.

### Reserving Policy

- 6.9 I have been provided with the reserving policy that covers both AGIL and LGI. The purpose of the policy is to ensure:
- That there is a clearly defined process for reserving;
  - That estimates of the actuarial reserves are computed in accordance with relevant actuarial standards and make reasonable provision for all unpaid loss and loss expense obligations;
  - That there is adequate and timely reporting of reserve activities to management; and
  - Allowance for solvency technical provision responsibilities falling under the SIMR20 role.
- 6.10 Claims reserving analyses are conducted on a periodic basis, no less than annually. The level of reserves held should:
- Be based on an actuarial best estimate (“**ABE**”) that is derived using industry-standard actuarial analyses in compliance with professional best practice;
  - Ensure that adequate reserves are booked, i.e. limited/no appetite for booked reserves to be less than ABE;
  - Accept that (slight) over-reserving is the default position, while minimising unnecessary surpluses;
  - Augment the ABE with a Provision for Adverse Deviation (“**PAD**”).
- 6.11 The global Assurant Group reserving policy dictates that claims reserves are booked in the financial statements at the 75<sup>th</sup> percentile. The PAD is the difference between the ABE and the 75<sup>th</sup> percentile position and is usually expressed as a percentage of the total reserve. The level of the PAD is derived by statistical analysis of reserve volatility, carried out annually and at an entity level.
- 6.12 The UPR for UK GAAP is estimated using earnings factors, earnings formulas or an actuarial selection. The appropriateness of these estimates is reviewed on a periodic basis, no less than annually.
- 6.13 Under Solvency II technical provisions, a probability weighted discounted cash-flow reserve is held for future claims and expenses, minus any premiums not yet received, plus a risk margin. The computation of this technical provision is a responsibility of the holder of the Chief Actuary role<sup>11</sup> - in the case of AGIL, this is AEG actuary who was mentioned in paragraph 6.8, above - and reflects the Solvency II Delegated Acts and relevant PRA guidance. The technical provisions and above claim reserves and unearned premium reserves are linked as part of a common actuarial framework. These technical provisions are computed quarterly by the actuarial function to feed TWGE and AGL's quantitative reporting templates (QRTs) for the regulator.
- 6.14 The Reserving Forum has a key role to play in the governance framework as outlined below:
- Review quarterly reserving positions;
  - Discuss any current issues such as claims backlogs or changes to deal structures that may impact the setting of reserves;
  - Discuss any changes to methodology in calculating the Actuarial Best Estimate; and
  - Provide approval for quarterly reserve bookings as a key governance forum.

<sup>11</sup> This is a specified senior management function (SMF20) under the FCA's Senior Managers and Certification Regime (<https://www.fca.org.uk/publication/policy/guide-for-insurers.pdf>).

### Actuarial projections of outstanding claims costs

- 6.15 For projection purposes, AGIL's reserving actuary segments the business by client and line of business, which means that ABE reserves are currently projected separately for the Transferring Business (i.e. EEA policies separate from UK policies). I note that, for creditor contracts, the life and non-life elements are dealt with separately as they are carried by different entities.
- 6.16 In the case of AGIL, the booked reserves are carried from quarter to quarter, with estimates calculated retrospectively after quarter close in an actuarial reserving platform. Based on these estimates, the Actuarial Function computes a surplus position (difference between booked and actuarial reserves and recommends adjustments to the business).
- 6.17 The actuarial reserve estimates for AGIL are calculated using vendor-based models, which use the average cost per claim reserving method for the most recent Accident Years and Chain Ladder<sup>12</sup> ("CL") reserving method for the prior Accident Years.
- 6.18 The AGIL PAD is held as a margin above the actuarial best estimate reserves. This PAD is not allocated to specific clients but is a separate PAD item in the general ledger. The PAD has been set to ensure the reserves are at approximately the 75<sup>th</sup> percentile of the range of possible outcomes. This equates to 5% of the gross ABE.
- 6.19 The actuarial reserve model was fully refreshed in January 2020, using claims data up to 31 December 2019. The results were then compared to the figures booked in the 31 December 2019 management accounts. Any proposed adjustments will be carried forward to the booked numbers in future periods. I have been provided with a report summarising the results of this analysis.
- 6.20 The key assumptions underlying the standard methods as applied to the data are as follows:
- The historic development patterns are indicative of future development, which in turn implies the following further assumptions:
  - Case reserving standards are consistent (and are applied consistently) over time;
  - Claims inflation is broadly stable; and
  - Claims settlement processes are broadly unchanged over time.
- 6.21 I have been told that these assumptions are valid for AGIL and I have no reason to doubt this.
- 6.22 From my review of the various documents supporting the reserve calculations, as I have described above, I am satisfied that:
- the reserving methodologies adopted by the AGIL reserving actuary are broadly consistent with usual market practice; and
  - the major assumptions adopted by the AGIL reserving actuary appear reasonable in the context of the underlying portfolios and of my market knowledge.

Therefore, I conclude that AGIL's best estimate reserves as at 31 December 2019 appear reasonable.

### Unallocated Loss Adjustment Expenses

- 6.23 No provision is required in respect of future Unallocated Loss Adjustment Expenses ("ULAE"). As discussed in paragraphs 4.53-4.56, above, AGIL outsources its claims handling and is charged a fee at the point of sale for such future costs.

### Solvency II Technical Provisions

- 6.24 TPs are conceptually valued on a market consistent basis, i.e. the amount a third party would require to be paid to assume the liabilities. They consist of three components:

<sup>12</sup> *The Chain Ladder method is an actuarial method commonly used to estimate claim reserve amounts. The method considers the historical development of reported paid and incurred claims and then extrapolates this historical claim development into the future in order to estimate future claim development. An important assumption underlying this method is that it expects the future development of claims to be similar to the historical average. The method involves some actuarial judgement in determining the assumption for the pattern of future claims from the historical data.*

- a discounted best estimate claims provision for incurred claims (whether or not reported at the valuation date);
  - a discounted best estimate premium provision (comprising cash-flows from unearned premiums, both claim payments from future exposures and certain elements of future premiums); and
  - a risk margin calculated using a cost-of-capital approach. Appendix G provides further details on the calculation of TPs.
- 6.25 AGIL's starting point for calculating its TPs is the best estimate claims reserves calculated on the UK GAAP basis, as described above (and which underlie the booked reserves). I have been provided with a copy of the Actuarial Function Report ("**AFR**") prepared by the Actuarial Function in respect of the TPs as at 31 December 2019. In the AFR, the Actuarial Function describes and assesses the process undertaken by AGIL in calculating its TPs as at 31 December 2019. The Actuarial Function considered:
- the methodology and assumptions;
  - the results of a comparison of actual claims development with that expected based on the preceding reserve review;
  - sensitivities and concerns;
  - the systems used for data storage, administration and analysis; and
  - co-ordination of technical provision calculation.
- 6.26 AGIL has made a number of adjustments to its held reserves to calculate its TPs, as set out below (see Appendix H for further information):
- Removal of both ULAE and the PAD to ensure that the outstanding claims are on a "best estimate" basis;
  - Allowance for future premiums on business that has already incepted (i.e. recognition of profits expected to arise on such business);
  - Allowance for Bound But Not Incepted ("**BBNI**") business (e.g. recognition of profits expected to arise in respect of tacit renewals, multi-year contracts, delegated authorities and any quotes that AGIL was legally obliged to honour if the quote were then accepted);
  - Allowance for ENIDs;
  - Allowance for reinsurance bad debt;
  - Allowance for discounting, using the relevant risk-free interest rate term structure for each material settlement currency;
  - Future expenses for running off the business (ULAE and other "non-ULAE" expenses, such as those relating to depreciation (tangible and intangible), investment management expenses and policy administration); and
  - Risk margin (i.e. the additional payment that a knowledgeable third party would require in order for it to assume the liabilities covered by these TPs). The risk margin is based on the future SCRs required to back AGIL's business as it runs off into the future (excluding risks not relevant to such a run-off, such as those associated with new business), discounted to a present value using discount rates as prescribed by EIOPA.
- 6.27 The main input to calculation of the premium provision is a set of loss ratios. These are taken from the current business plan, having been derived separately for each client and geography, and are then applied to the unearned premium reserve cashflows.
- 6.28 As part of the validation of these assumptions, AGIL compares the selected business plan loss ratios with experience loss ratios, allowing for material differences to the exposure profile, to ensure they remain appropriate for use in the calculations of the TPs. It conducts various sensitivity tests on the more material accounts. AGIL has also provided me with a summary report from its external auditors in which it reviewed AGIL's Solvency II balance sheet (and SCR calculation) as at 31 December 2019. There were no issues raised in that report that caused me concern.

- 6.29 Based on my review of this validation work, I conclude that the loss ratios selected are within a reasonable range of values.
- 6.30 Overall, the process and assumptions used by AGIL in its calculation of both the premium provision and the claims provision under Solvency II are typical of those that I have seen adopted by other UK insurance companies.

#### Sensitivities

- 6.31 I have considered the sensitivity of AGIL's TPs to changes in the assumptions. In particular, I have seen the results of a sensitivity test conducted by AGIL as at 30 September 2019 in which it considered the impact of different assumptions in the calculation of the premium provision, specifically:
- higher or lower loss ratios;
  - higher or lower volumes of business;
  - less favourable exchange rates; and
  - higher expense ratios
- than those within the business plan.
- 6.32 Based on the current mix of business and considering only adverse movements:
- a 1% increase in the assumed loss ratio would have increased the TPs by 2.3%, net of reinsurance;
  - a 5% fall in the assumed premium volume would have increased the TPs by 0.8%, net of reinsurance;
  - a 10% increase in the assumed expense ratio would have increased the TPs by 1.0%, net of reinsurance; and
  - a 5% fall in the assumed value of sterling relative to other currencies would have increased the TPs by 0.9%, net of reinsurance.
- 6.33 By way of comparison, the value of AGIL's Eligible Own Funds as at 31 December 2019 was equivalent to 370% of the TPs, net of reinsurance, and the Eligible Own Funds in excess of the SCR as at 31 December 2019 was equivalent to 119% of the TPs, net of reinsurance.
- 6.34 According to the ORSA for AGIL (most recent as at the date of this Report):
- a one in 3-5 year insurance event would be equivalent (all other things being equal) to roughly a 5% deterioration in the assumed loss ratio;
  - a one in 10-15 year insurance event would be equivalent (all other things being equal) to roughly a 15% deterioration in the assumed loss ratio; and
  - a one in 200 year insurance event would be equivalent (all other things being equal) to roughly a 55% deterioration in the assumed loss ratio.

#### Conclusion with regard to the reserve strength of AGIL pre-Scheme

- 6.35 Based on my review of the technical provisions of AGIL (both on a UK GAAP and Solvency II basis) as at 31 December 2019, as described above, I have concluded that
- the methodologies and major assumptions underlying the reserve analyses as performed by AGIL as at 31 December 2019 are reasonable;
  - the best estimates of unpaid claim amounts also appear reasonable; and
  - the TPs booked by AGIL as at 31 December 2019 include appropriate margins and other adjustments over those actuarial indications.

Therefore, I conclude that AGIL's reserves (both on a UK GAAP basis and on a Solvency II basis) appear reasonable as at 31 December 2019, notwithstanding the uncertainty present.

- 6.36 I note in passing that the premium provisions for AGIL on a UK GAAP basis differ materially from those on a Solvency II basis. I explain the reason for this in paragraphs 4.16-4.18, above but, in essence, under Solvency II, any expected profit from premiums yet to be earned (including those yet to be received) is recognised immediately whereas, under UK GAAP, it would emerge only as the premiums were earned.

#### RESERVE STRENGTH OF LGI (PRE-SCHEME)

- 6.37 As set out in Figure 4.6, above, in its statutory accounts as at 31 December 2019, LGI held gross technical provisions of £175.8 million (made up of £143.4 million of UPR and £32.3 million of outstanding claims). Reinsurers' share of technical provisions totalled £48.7 million (made up of £41.8 million of UPR and £6.9 million in respect of claims outstanding).
- 6.38 In this section of the Report, I provide details of my review of the reserve strength of LGI. As the work underlying the reserves booked by LGI has been used in its capital calculations (albeit indirectly), the appropriateness of these reserves is important in assessing the security currently afforded to the LGI Transferring Policyholders.
- 6.39 I have been provided with details of the outstanding claims provision for LGI as at 31 December 2019, the process by which the provisions were established and details of the actuarial review that underlies those provisions. The outstanding claims provision so developed and included in LGI's financial statements (as at 31 December 2019) were prepared in accordance with UK GAAP.
- 6.40 I have not attempted to review in detail the calculations performed by the actuary responsible for the actuarial review. Instead, I have reviewed the process by which reserves were set, the approach followed by the actuary, the key areas of reserve uncertainty and the apparent strength of the reserves based on this review.

#### Reserving Policy

- 6.41 I have been provided with the reserving policy that covers both AGIL and LGI. For a summary of key items in this reserving policy, see paragraph 6.9 to paragraph 6.14 above.

#### Actuarial projections of outstanding claims costs

- 6.42 For projection purposes, LGI's reserving actuary segments the business by client and line of business, which means that ABE reserves are currently projected separately for the transferring business (i.e. EU policies vs UK policies). I note that, for creditor contracts, the life and non-life elements are dealt with separately as they are carried by different entities.
- 6.43 The actuarial reserving models were updated for claims data up to the end of November 2019, except in respect of the Netherlands creditor insurance business for which data was available up to 31 December 2019, and both case reserves and IBNR reserves were re-calculated. The results were then compared to the figures booked in the 31 December 2019 management accounts.
- 6.44 The majority of the actuarial reserve estimates for LGI are calculated using models prepared using Microsoft Excel. These models are based on either a CL method or a Bornhuetter Ferguson<sup>13</sup> ("B-F") approach, or a blend of the two. The exceptions to this are the reserves relating to Toyota, to John Lewis and to the Netherlands creditor insurance business. These also use standard actuarial methods with a blend of one or more of the following:
- B-F using paid claims
  - B-F using incurred claims
  - CL
  - Expected Loss Ratio.

<sup>13</sup> *The Bornhuetter Ferguson method is a commonly used actuarial method for estimating claim reserves. It can be thought of as a weighted mixture of the Chain Ladder method and the expected ultimate losses (less paid losses) the latter being typically based on the underwriter's view. For more recent accident (or underwriting) years more weight is given to the expected ultimate losses (where claim based methods are less reliable); for older accident (or underwriting) years more weight is given to the Chain Ladder method (where claim data provides more information).*

- 6.45 The LGI PAD is held as a margin above the actuarial best estimate reserves. This PAD is not allocated to specific clients but is a separate PAD item in the general ledger. The PAD has been set to ensure the reserves are at approximately the 75<sup>th</sup> percentile of the range of possible outcomes. This equates to 5% of the gross ABE.
- 6.46 The key assumptions underlying the standard methods as applied to the data are as follows:
- The historic development patterns are indicative of future development, which in turn implies the following further assumptions:
  - Case reserving standards are consistent (and are applied consistently) over time;
  - Claims inflation is broadly stable; and
  - Claims settlement processes are broadly unchanged over time.
- 6.47 I have been told that these assumptions are valid for LGI and I have no reason to doubt this.
- 6.48 From my review of the various documents supporting the reserve calculations, as I have described above, I am satisfied that:
- the reserving methodologies adopted by the LGI reserving actuary are broadly consistent with usual market practice; and
  - the major assumptions adopted by the LGI reserving actuary appear reasonable in the context of the underlying portfolios and of my market knowledge.

Therefore, I conclude that LGI's best estimate reserves as at 31 December 2019 appear reasonable.

#### Unallocated Loss Adjustment Expenses

- 6.49 No provision is required in respect of future ULAE. As discussed in paragraphs 4.87-4.88, above, LGI outsources its claims handling to TGWE, which charges a fee at the point of sale for such future costs.

#### Solvency II Technical Provisions

- 6.50 TPs are conceptually valued on a market consistent basis, i.e. the amount a third party would require to be paid to assume the liabilities. They consist of three components: (1) a discounted best estimate claims provision for incurred claims (whether or not reported at the valuation date); (2) a discounted best estimate premium provision (comprising cash-flows from unearned premiums, both claim payments from future exposures and certain elements of future premiums); and (3) a risk margin calculated using a cost-of-capital approach. Appendix G provides further details on the calculation of TPs.
- 6.51 LGI's starting point for calculating its TPs is the best estimate claims reserves calculated on the UK GAAP basis as described above (which underlie the booked reserves). I have been provided with a copy of the AFR prepared by the Actuarial Function in respect of the TPs as at 31 December 2019. In the AFR, the Actuarial Function describes and assesses the process undertaken by AGIL in calculating its TPs as at 31 December 2019. The Actuarial Function considered:
- the methodology and assumptions;
  - the results of a comparison of actual claims development with that expected based on the preceding reserve review;
  - sensitivities and concerns;
  - the systems used for data storage, administration and analysis; and
  - co-ordination of technical provision calculation.
- 6.52 LGI has made a number of adjustments to its held reserves to calculate its TPs, as set out below (see Appendix H for further information):
- Removal of both ULAE and the PAD to ensure that the outstanding claims are on a "best estimate" basis;
  - Allowance for future premiums on business that has already incepted (i.e. recognition of profits expected to arise on such business);

- Allowance for BBNI business (e.g. recognition of profits expected to arise in respect of tacit renewals, multi-year contracts, delegated authorities and any quotes that AGIL was legally obliged to honour if the quote were then accepted);
- Allowance for ENIDs;
- Allowance for reinsurance bad debt;
- Allowance for discounting, using the relevant risk-free interest rate term structure for each material settlement currency;
- Future expenses for running off the business (ULAE and other “non-ULAE” expenses, such as those relating to depreciation (tangible and intangible), investment management expenses and policy administration); and
- Risk margin (i.e. the additional payment that a knowledgeable third party would require in order for it to assume the liabilities covered by these TPs). The risk margin is based on the future SCRs required to back AGIL’s business as it runs off into the future (excluding risks not relevant to such a run-off, such as those associated with new business), discounted to a present value using discount rates as prescribed by EIOPA.

6.53 The main input to the premium provision calculation is a set of loss ratios. These are taken from the current business plan, having been derived separately for each client and geography, and are then applied to the unearned premium reserve cashflows.

6.54 As part of the validation of these assumptions, LGI compares the selected business plan loss ratios with experience loss ratios, allowing for material differences to the exposure profile, to ensure they remain appropriate for use in the calculations of the TPs. It conducted a sensitivity test, replacing the business plan loss ratios selected with the experience loss ratios. This sensitivity gave TPs that were not materially different to those selected for year-end 2019.

6.55 Based on my review of this validation work, I conclude that the loss ratios selected sit within a reasonable range of values.

6.56 Overall, the process and assumptions used by LGI in its calculation of both the premium provision and the claims provision under Solvency II are typical of those that I have seen adopted by other UK insurance companies.

### *Sensitivities*

6.57 I have considered the sensitivity of LGI’s TPs to changes in the assumptions. In particular, I have seen the results of a sensitivity test conducted by LGI as at 30 September 2019 in which it considered the impact of different assumptions in the calculation of the premium provision, specifically:

- higher or lower loss ratios;
- higher or lower volumes of business;
- less favourable exchange rates; and
- higher expense ratios

than those within the business plan.

6.58 Based on the current mix of business and considering only adverse movements:

- a 1% increase in the assumed loss ratio would have increased the total TPs by 0.5%, net of reinsurance;
- a 5% increase in the assumed premium volume would have increased the total TPs by 3.1%, net of reinsurance;
- a 10% increase in the assumed expense ratio would have increased the total TPs by 0.4%, net of reinsurance; and
- a 5% fall in the assumed value of sterling relative to other currencies would have increased the total TPs by 0.9%, net of reinsurance.

6.59 By way of comparison, the value of LGI's Eligible Own Funds as at 31 December 2019 was equivalent to 110% of the TPs, net of reinsurance, and the Eligible Own Funds in excess of the SCR as at 31 December 2019 was equivalent to 54% of the TPs, net of reinsurance.

6.60 According to the ORSA for LGI (most recent as at the date of this Report):

- a one in 3-5 year insurance event would be equivalent (all other things being equal) to roughly a 1% deterioration in the assumed loss ratio;
- a one in 10-15 year insurance event would be equivalent (all other things being equal) to roughly a 4% deterioration in the assumed loss ratio; and
- a one in 200 year insurance event would be equivalent (all other things being equal) to roughly a 25% deterioration in the assumed loss ratio.

These percentages are lower than the equivalent percentages for AGIL, reflecting the less volatile nature of LGI's business relative to that of AGIL.

### Conclusion with regard to the reserve strength of LGI pre-Scheme

6.61 Based on my review of the technical provisions of LGI (both on a UK GAAP and Solvency II basis) as at 31 December 2019, as described above, I have concluded that

- the methodologies and major assumptions underlying the reserve analyses as performed by LGI as at 31 December 2019 are reasonable;
- the best estimates of unpaid claim amounts also appear reasonable; and
- the TPs booked by LGI as at 31 December 2019 include appropriate margins and other adjustments over those actuarial indications.

I therefore conclude that LGI's reserves (both on a UK GAAP basis and on a Solvency II basis) appear reasonable as at 31 December 2019, notwithstanding the uncertainty present.

6.62 As I noted in paragraph 4.70, above, the premium provisions for LGI on a UK GAAP basis differ materially from those on a Solvency II basis. I explained the reason for this in paragraphs 4.17-4.18, above but, in essence, under Solvency II, any expected profit from premiums yet to be earned (including those yet to be received) is recognised immediately whereas, under UK GAAP, it would emerge only as the premiums were earned.

### RESERVE STRENGTH OF AEI (PRE-SCHEME)

6.63 There are currently no outstanding claims liabilities in AEI as no business has been written as at the date of this report.

### RESERVE STRENGTH OF AEI (POST-SCHEME)

6.64 Post the Effective Date, the Transferring Business will be included within AEI, and the reserves for the Transferring Business will be wholly included within the reserves for AEI.

6.65 I have been told that post transfer the intention is to maintain the reserving process (including data, assumptions, methodology and systems) in its current form. The same team and the same processes are expected to remain in place to analyse the portfolio. It is intended that reserves will continue to be booked at the 75<sup>th</sup> percentile confidence level. The reserving policy, although I have not yet seen a copy, is expected to be similar the current policy that covers AGIL and LGI. It is possible that, at some future date, the AEI Board will revise the policy (and possibly the target confidence levels). However, that will be in response to the then prevailing conditions and AEI's own circumstances.

### Sensitivities

- 6.66 I have considered the sensitivity of AEI's forecast post-Scheme TPs to changes in the assumptions. I have used the results of the sensitivity tests conducted by AGIL and LGI as at 30 September 2019 as discussed in paragraphs 6.31-6.57, above, and have assumed that, in percentage terms, they would still apply as at the Effective Date. I have combined them in proportion to the value of business, net of reinsurance, transferring from AGIL and LGI. This would be valid were the profile of the business being transferred from each of AGIL and LGI the same as the profile of the respective business pre-Scheme. As there are differences, the following sensitivities should be considered as purely illustrative.
- 6.67 Based on the current mix of business and considering only adverse movements:
- a 1% increase in the assumed loss ratio would have increased the total TPs by 0.8%, net of reinsurance;
  - a 5% increase in the assumed premium volume would have increased the total TPs by 1.9%, net of reinsurance;
  - a 10% increase in the assumed expense ratio would have increased the total TPs by 0.5%, net of reinsurance; and
  - a 5% fall in the assumed value of sterling relative to other currencies would have increased the total TPs by 0.7%, net of reinsurance.
- 6.68 By way of comparison, on a *pro forma* basis as at 31 December 2019:
- the value of AEI's Eligible Own Funds would have been equivalent to 68% of the value of the TPs, net of reinsurance;
  - the value of AEI's Eligible Own Funds in excess of the SCR would have been equivalent to 24% of the value of the TPs, net of reinsurance; and
  - the value of AEI's Eligible Own Funds in excess of the Target Capital would have been equivalent to 6% of the value of the TPs, net of reinsurance.
- 6.69 By combining the findings set out in the ORSAs for AGIL and LGI (most recent as at the date of this Report) and assuming no diversity credit between the AGIL Transferring Business and the LGI Transferring Business:
- a one in 3-5 year insurance event would be equivalent (all other things being equal) to roughly a 2% deterioration in the assumed loss ratio;
  - a one in 10-15 year insurance event would be equivalent (all other things being equal) to roughly a 6% deterioration in the assumed loss ratio; and
  - a one in 200 year insurance event would be equivalent (all other things being equal) to roughly a 30% deterioration in the assumed loss ratio.
- 6.70 It is apparent that, post-Scheme, the TPs could be strengthened considerably without jeopardising the solvency of AEI, or even its ability to meet its SCR.

### Conclusion

- 6.71 There will be no change in the strength of the reserves held post-Scheme by AEI in respect of the Transferring Business relative to the strength of the reserves held pre-Scheme by AGIL and LGI in respect of the same business.

### EXCESS ASSETS OF AGIL

- 6.72 AGIL monitors actual and projected solvency capital requirements.

- 6.73 In assessing its SCR for regulatory purposes, AGIL uses the Standard Formula provided by EIOPA. It has assessed the appropriateness of using the Standard Formula and has concluded that, overall, the Standard Formula leads to a higher valuation of risk than is reflected in AGIL's own risk profile. This is not an unreasonable conclusion – as an insurer, focusing on a small number of specialised products, AGIL is not directly comparable to the "average insurer" upon whose experience the EIOPA standard formula parameters have been based. That is not to say that the Standard Formula measures all of AGIL's risk components conservatively, rather that its measure in totality is expected to be conservative.
- 6.74 For AGIL's ORSA calculations, AGIL has developed its own model that reflects the characteristics of its business. The model is based on a proprietary modelling platform licensed to AGL, adjusted to suit the underlying needs, assumptions and risk profile of AGL and its entities, including AGIL. The model is operated and implemented by the Actuarial Function with model oversight and second line validation provided by the Risk Function.
- 6.75 Two key differences between the ORSA model and the Standard Formula are:
- Catastrophe risk is modelled as part of the Standard Formula SCR. Catastrophe risk is not considered within the AGIL ORSA model as it is not deemed to be a material risk for the products on which AGIL focuses. This leads to a lower assessment of insurance risk in the ORSA model.
  - Conversely, the ORSA model has a higher assessment of operational risk than does the equivalent Standard Formula approach. The business model that AGIL has and the size of the company means that the exposure to operational risk is perceived to be higher than average and hence the capital allocated to operational risk within the ORSA model is greater than that in the SCR.
- 6.76 The higher operational risk within the ORSA model diversifies with the Insurance risk, so that the overall capital impact is less than the stand-alone.
- 6.77 The ORSA figure is also based on a 3-year time horizon, in line with the internal requirement, whereas, under Solvency II, the SCR is based on a 1-year view.
- 6.78 The most significant component of AGIL's regulatory SCR is insurance risk, which, as at 31 December 2019, comprises 61% of the SCR on a Solvency II basis, prior to application of diversification benefits. As at the same date, market risk contributes 9%, operational risk 13% and credit risk 17% of the undiversified SCR.
- 6.79 I have reviewed the work undertaken in estimating capital requirements for AGIL, as documented in the AGIL report entitled *2019 Annual ORSA: Supervisory Report*, in order to satisfy myself that it is reasonable for me to rely on that work. This included reviewing the process by which capital estimates have been made, the approach followed by AGIL's modelling team, the key assumptions employed, and the resulting capital amounts. Based on my review, I consider the methodology and modelling techniques used by AGIL to be in line with industry practice and generally appropriate. I note that AGIL's modelling team (which also conducts the modelling for LGI – see below) is staffed with experienced personnel with experience of both AGIL and LGI. The team is supervised by the Chief Actuary of both AGIL and LGI, with review from actuarial expertise embedded within AGIL and LGI's risk function. As a result, I believe it is reasonable for me to rely on the work of the AGIL modelling team, and, therefore, I have not attempted to review in detail the calculations performed by AGIL in order to estimate its SCR.
- 6.80 As at 31 December 2019, as shown in Figure 4.5, above, AGIL was then more than sufficiently capitalised relative to its SCR, with a Capital Cover Ratio of 148%.
- 6.81 AGIL's *2019 Annual ORSA: Supervisory Report* shows that (on a standalone basis and ignoring the planned Scheme) the one-year time horizon Capital Cover Ratio for AGIL is expected to increase from its level as at 31 December 2018 as the European business is no longer written into AGIL.
- 6.82 The Capital Cover Ratios underlying the above analysis are on a statutory (Standard Formula) basis. The Capital Cover Ratios based on AGIL's own assessment of its risks (to ultimate) are higher, reflecting AGIL's view that the Standard Formula SCR is a prudent (albeit not unreasonable) measure of the underlying risk of its business.

- 6.83 As noted in paragraph 5.43, above, I have been provided with pro forma balance sheets that indicate that, by the Effective Date, AGIL's eligible own funds are expected to have increased and its SCR is expected to have decreased. As a result, AGIL's Capital Cover Ratio is expected to increase by the Effective Date, moving AGIL from being a more than sufficiently capitalised insurer to being a well-capitalised insurer.

### Conclusion

- 6.84 I have explained above why I consider that AGIL's calculations and projections of its solvency requirements and available capital, and hence of its excess assets, are reasonable. Overall, these lead me to conclude that the policyholders of AGIL, including those who will transfer under the proposed Scheme, currently benefit from the financial strength provided by a more than sufficiently capitalised company (indeed, between 31 December 2019 and the Effective Date, it is expected to become a well-capitalised insurer).

### EXCESS ASSETS OF LGI

- 6.85 LGI monitors actual and projected solvency capital requirements.
- 6.86 In assessing its SCR for regulatory purposes, LGI uses the Standard Formula provided by EIOPA. However, on 14 March 2017, the PRA approved LGI's application to use a USP in its calculations of regulatory capital. Specifically, this parameter measures the premium risk associated with the Miscellaneous Financial Loss class. The use of the USP means that the resultant SCR better reflects the risk profile and volatility of the business in LGI. In accordance with the TWGE USP Policy, the parameter is updated at least annually.
- 6.87 LGI has assessed the appropriateness of using the Standard Formula (with the USP adjustment) and has concluded that, overall, the Standard Formula leads to a higher valuation of risk than is reflected in LGI's own risk profile. This is not an unreasonable conclusion – as an insurer, focusing on a small number of specialised products, LGI is not directly comparable to the "average insurer" upon whose experience the EIOPA Standard Formula parameters have been based. That is not to say that the Standard Formula measures all of LGI's risk components conservatively, rather that its measure in totality is expected to be conservative.
- 6.88 For LGI's ORSA calculations, LGI has developed its own models that reflect the characteristics and its business. The ORSA capital requirement for LGI is calculated by replacing the non-life premium and reserve risk module of the Solvency II Standard Formula SCR with TWGE's own internal calculation.
- 6.89 This calculation is performed within a proprietary modelling platform. The calculation applies stochastic modelling to the LGI ABE, and uses the outputs equivalent to a 1-in-200 event. All other modules within the Standard Formula SCR calculation remain unchanged. This reflects LGI's conclusion that the remaining elements of the Standard Formula calculation model the business appropriately.
- 6.90 To perform the stochastic element of the calculation, the historic loss ratio experience is analysed for each major product line (motor warranty, GAP, unemployment, theft & damage, A&T Warranty), to provide a view of the volatility (measured by standard deviation) inherent in that line. This allows the derivation of the 1-in-200 loss ratio for each product line. Comparison of these loss ratios to the baseline LGI best estimate (calculated using business plan loss ratios) provides a view of the losses that would be generated under each. A correlation matrix is then applied.
- 6.91 The ORSA calculation is expected to reflect better the volatility of performance of the elements of the underlying business and the diversity within the business than does the Standard Formula (with USP). For example, in the SCR, almost all LGI business is categorised as Miscellaneous Financial Loss. In contrast, in its ORSA, LGI considers the volatility of motor warranty, GAP, unemployment, theft & damage and A&T warranty business separately and allows for diversification between those classes of business that are not greatly correlated with one another. However, the largest contribution to the difference between LGI's ORSA and its Standard Formula (with USP) SCR is caused by the latter's use of premiums gross of commission as a key driver for the premium risk component. Much of the business written by LGI has commission rates in excess of 50%, leading to a higher premium risk in the capital requirements than is recognised within the ORSA.

- 6.92 The most significant component of LGI's regulatory SCR is insurance risk, which, as at 31 December 2019, comprises 69% of the SCR on a Solvency II basis, prior to application of diversification benefits. As at the same date, market risk contributes 22%, operational risk 6% and counterparty default risk 3% of the undiversified SCR.
- 6.93 I have reviewed the work undertaken in estimating capital requirements for LGI, as documented in the LGI report entitled *Group Own Risk and Solvency Assessment Supervisory Report including London General Insurance Company Limited and London General Life Company Limited: 2019 Annual Report*, in order to satisfy myself that it is reasonable for me to rely on that work. This included reviewing the process by which capital estimates have been made, the approach followed by LGI's modelling team, the key assumptions employed, and the resulting capital amounts. Based on my review, I consider the methodology and modelling techniques used by LGI to be in line with industry practice and generally appropriate. As commented in paragraph 6.79, above, LGI's modelling team is the same as that for AGIL. As a result, I believe it is reasonable for me to rely on the work of the LGI modelling team, and, therefore, I have not attempted to review in detail the calculations performed by LGI in order to estimate its SCR.
- 6.94 As at 31 December 2019, as shown in Figure 4.9, above, LGI was then well-capitalised relative to its SCR, with a Capital Cover Ratio of 196%.
- 6.95 LGI's *Group Own Risk and Solvency Assessment Supervisory Report including London General Insurance Company Limited and London General Life Company Limited: 2019 Annual Report* shows that (on a standalone basis and ignoring the planned Scheme) the one-year time horizon Capital Cover Ratio for LGI are expected to increase from its level as at 31 December 2018 as the European business is no longer written into LGI.
- 6.96 The Capital Cover Ratios underlying the above analysis are on a statutory (Standard Formula) basis. The Capital Cover Ratios based on LGI's own assessment of its risks (to ultimate) are higher, reflecting LGI's view that the Standard Formula SCR is a prudent (albeit not unreasonable) measure of the underlying risk of its business.
- 6.97 As noted in paragraph 5.43, above, I have been provided with pro forma balance sheets that indicate that, by the Effective Date, LGI's eligible own funds are expected to have reduced slightly and its SCR is expected also to have reduced. As a result, LGI's Capital Cover Ratio is expected to increase by the Effective Date, to the extent that it would then be a very well capitalised insurer.

## Conclusion

- 6.98 I have explained above why I consider that LGI's calculations and projections of its solvency requirements and available capital, and hence of its excess assets, are reasonable. Overall, these lead me to conclude that the policyholders of LGI, including those who will transfer under the proposed Scheme, currently benefit from the financial strength provided by a well-capitalised company (indeed, between 31 December 2019 and the Effective Date, it is expected to become a very well capitalised insurer).

## EXCESS ASSETS OF AEI

- 6.99 In assessing its SCR for regulatory purposes, AEI will use the Standard Formula provided by EIOPA. It does not currently plan to apply to use USPs.
- 6.100 The capital modelling, including that for the ORSA, will be conducted by the same modelling team as used by AGIL and LGI, using essentially the same models and same approach as documented above. This would be appropriate, bearing in mind that the Transferring Assets and the liabilities relating to the Transferring Policies that will form the bulk of AEI's balance sheet post-Scheme comprise very material parts of the current balance sheets of both AGIL and LGI.
- 6.101 The most significant component of AEI's regulatory SCR is expected to be insurance risk, with market risk, operational risk and counterparty default risk also contributing materially to the undiversified SCR.
- 6.102 Having reviewed the work undertaken in estimating capital requirements for AGIL and LGI, I concluded that it is reasonable for me to rely on the work of the AGIL and LGI modelling team in respect of their modelling of the risks in respect of AGIL and LGI. I have extrapolated from that conclusion to conclude further that I can also rely on their work in respect of the modelling for AEI. Therefore, I have not attempted to review in detail the calculations performed in order to forecast the SCR for AEI.

- 6.103 As shown in Figure 5.11, above, had the Scheme been effective as at 31 December 2019 (and subject to it having received an injection of capital of £25.8 million), AEI would then have been well-capitalised relative to its SCR, with a Capital Cover Ratio of 154%.
- 6.104 As noted in paragraph 5.43, above, I have been provided with pro forma balance sheets that indicate that, by the Effective Date, AEI's eligible own funds, post-Scheme, would be expected to have reduced slightly compared with that in the year-end 2019 pro forma, and its SCR is expected to remain unchanged. As a result, as at the Effective Date, AEI's post-Scheme Capital Cover Ratio is expected to be less than it would have been as at 31 December 2019, but not to the extent that its Capital Cover Ratio falls below the target level. AEI is projected to be, post-Scheme, a well-capitalised insurer as at the Effective Date.

### Conclusion

- 6.105 I have explained above why I consider that the calculations and projections of AEI's solvency requirements and available capital, and hence of its excess assets, are reasonable. Overall, these lead me to conclude that, post-Scheme, the Transferring Policyholders will be policyholders of a company that is expected to be well-capitalised as at the Effective Date.

### RELATIVE FINANCIAL STRENGTH ENJOYED BY TRANSFERRING POLICYHOLDERS PRE- AND POST-SCHEME

- 6.106 I have concluded, above, that the AGIL Transferring Policyholders currently benefit from the financial strength provided by a more than sufficiently capitalised company (which is expected to be well-capitalised as at the Effective Date) and the LGI Transferring Policyholders currently benefit from the financial strength provided by a well-capitalised company. I have also concluded that, if the Scheme is implemented, the Transferring Policyholders will become policyholders of an insurance company that is projected to be, post-Scheme, well-capitalised as at the Effective Date. Therefore, relative to the solvency capital requirements of the respective entities, the AGIL Transferring Policyholders will see a marginal increase in the financial strength afforded to them but LGI Transferring Policyholders will see a small decline in the financial strength afforded to them, i.e. they will be adversely impacted. However, I do not consider this decline in the financial strength to be material because the Capital Cover Ratio of AEI, post the Effective Date, indicates that the likelihood of the LGI Transferring Policyholders not receiving the benefits to which they are entitled remains very small.
- 6.107 I note that the Capital Cover Ratio of AEI, post-Scheme, is projected to be above AEI's target level of capital to only a small degree. Were it to fall below the target level then, as outlined in paragraph 4.109, above, and according to Assurant Europe's Capital Management Policy, AEI would not be permitted to distribute a dividend. If it were to fall further, to below the AEI Minimum Capital Target Buffer, then the Chief Financial Officer would be required to propose management actions intended to restore the capital to above the minimum level and, preferable, to above the target level.
- 6.108 I further note that, were its Capital Cover Ratio to fall to a level consistent with the AEI Minimum Capital Target Buffer, AEI would still be considered a more than sufficiently capitalised insurer.

### Conclusion

- 6.109 The Transferring Policyholders will be moving to an insurer with a lower post-Scheme Capital Cover ratio than those, pre-Scheme, of their current insurers, which would indicate a decline in the financial security of the benefits to which they are entitled under the Transferring Policies. However, I consider that they will not be adversely affected to a material degree by the Scheme as the likelihoods of AGIL or LGI, pre-Scheme, or AEI, post-Scheme, becoming insolvent are remote.

## CHANGES IN RISK EXPOSURES

- 6.110 If the Scheme is sanctioned, the Transferring Policyholders will no longer be exposed to the risks within AGI or LGIL, but will be exposed to those of AEI. In the main, AEI is a mirror of the Transferors. The risks in AGIL and LGI are very similar, and are managed using the same risk management framework. That same management framework will be used to manage the risks within AEI. However, the Transferring Policyholders will be moving from an entity (either AGIL or LGI) that has a limited range of product types to one that has a more diversified range of insurance risks (created by the Transferring Policies from the other entity). At least partially offsetting the impact of that increased diversification of product types, there is reduced diversification through the geographical spread of the risks, the Transferring Business no longer sitting beside UK risks and, in the case of LGI, Swiss risks.
- 6.111 Different risk profiles, insofar as they might affect the future financial security of policyholders, are reflected in the relative capital requirements of AGIL, LGI and AEI, although I note that the SCR Standard Formula does not reflect differences between uncorrelated products classed as Miscellaneous Financial Loss products. To allow for this diversification, as well as the differing volatilities experienced by the underlying products, LGI uses a USP adjustment within its Standard Formula SCR calculation. Insofar as AEI will not be using a USP adjustment within its Standard Formula SCR calculation, all other things being equal its SCR is more prudent than that of LGI.
- 6.112 As noted in paragraph 4.111, above, the Target Capital of AEI has been set at a higher than the Target Capital level of either AGIL or LGI. This implies that AEI has less appetite for risk than either AGIL or LGI, which, all other things being equal, would suggest that AEI would be more secure than either AGIL or LGI. However, as discussed above, the actual capital cover ratios of AGIL and LGI are currently well above both their respective Target Capital ratios and also AEI's Target Capital ratio.
- 6.113 As I have already concluded, AGIL is currently a more than sufficiently capitalised company (and is expected to be well-capitalised by the Effective Date) and LGI is a well-capitalised company (and is expected to be well-capitalised by the Effective Date). AEI is projected to be well-capitalised. Therefore, I am satisfied that, even were the Scheme to result in adverse change to the Transferring Policyholders' risk exposures (which I do not believe that it will), the capital protection available to them post-Scheme (while reduced in the case of LGI Transferring Policyholders) will not be materially different to that which they enjoyed pre-Scheme. Therefore, I conclude that any change in their risk exposure will not have a materially adverse impact on the security of the Transferring Policyholders.
- 6.114 There is also a likely benefit to the Transferring Policyholders in that, as explained in paragraph 5.11, above, there is a material risk that, following the expiry of the Transition Period, should they remain within AGIL or LGI it will be impossible for AGIL and LGI both to service their policies and to comply with the prevailing regulations. Avoiding this potential situation is the primary motivation behind the decision of AEG to pursue the Scheme.

### Conclusion

- 6.115 I am satisfied that the Scheme will not result in a changes in the risk exposures currently experienced by the Transferring Policyholders that will adversely affect the Transferring Policyholders to a material degree.

## POLICY SERVICING

- 6.116 As explained in paragraphs 5.29-5.31, above, it is intended that there will be no effective change in the administration and servicing of the Transferring Business. The only difference will be that, as explained in paragraph 4.109, above, policy servicing for the LGI Transferring Business will be outsourced to AES rather than to the Amsterdam branch of TWGS. Otherwise, all existing policy serving processes and systems will continue to be used, by the same staff and management.

### Conclusion

- 6.117 I am satisfied that the Scheme will not result in a material deterioration in the standard of policy servicing currently enjoyed by the Transferring Policyholders.

## POLICY TERMS AND CONDITIONS

6.118 As noted in paragraph 5.6, above, there will be no changes to the terms and conditions of any policy included within the Transferring Business as a result of the Scheme. The rights and obligations of AGIL and of LGI under the policies that comprise the Transferring Business will be transferred, without alteration, to AEI.

### Conclusion

6.119 I am satisfied that the Scheme will result in no change to the benefits that the Transferring Policyholders should expect.

## IN THE EVENT OF INSOLVENCY

6.120 As discussed in paragraph 3.48, above, the rules governing the winding-up of an insurance or reinsurance company are broadly similar in the UK and the Netherlands. In both cases, where assets are insufficient to meet fully the company's liabilities, holders of direct policyholders rank equally or behind certain preferential claims but rank above inwards reinsurance policyholders and all other unsecured/non preferential creditors.

6.121 Circumstances that, pre-Scheme, would cause the insolvency of AGIL and LGI are likely, post-Scheme, to cause the insolvency of AEI, as there is considerable commonality of the risks faced by AGIL and LGI pre-Scheme and AEI post-Scheme. As the relative ranking of the Transferring Policyholders in the event of winding-up is unchanged post-Scheme relative to pre-Scheme, it appears that the Scheme would not disadvantage the Transferring Policyholders.

6.122 In any event, pre-Scheme, the Capital Cover Ratios indicate that both AGIL and LGI are unlikely to become insolvent (LGI the more so); post-Scheme, the Capital Cover Ratios indicate that AEI is still unlikely to become insolvent.

### Conclusion

6.123 I am satisfied that the Scheme will not result in a material change in the rights of the Transferring Policyholders in the event of the winding-up of their insurer.

## COMPENSATION AND COMPLAINTS

6.124 Post-Scheme, it is likely (although not certain) the Transferring Policyholders will no longer be eligible (in the event that AEI fails to satisfy their contractual rights) for compensation under the FSCS. There is no alternative compensation scheme that they would be eligible to access. This is an adverse development for the Transferring Policyholders resulting from the Scheme. However, I note that:

6.124.1 The purpose of the proposed Scheme is to effect the transfer of the Transferred Business to AEI in order to enable its continued servicing and for the Transferring Policyholders to receive the benefits to which they are entitled, regardless of the outcome of the Brexit negotiations. It is of primary importance that, post the Implementation Period, there will be certainty that the Transferred Policies will continue to be serviced lawfully and the Transferring Policyholders will receive their benefits under their policies, and the loss of FSCS protection is an unavoidable consequence of this; and

6.124.2 Given that AEI is projected to be well-capitalised and will be required to comply with Solvency II, I consider the likelihood of the default or insolvency of AEI to be remote.

6.125 In addition, I note that there have been a number of recent Part VII transfers presented to the Court from other insurers with a similar motivation as the motivation for this Scheme, i.e. in preparation for the possible loss of EU passporting rights as a result of Brexit. The loss of FSCS protection or deterioration in protection was a key matter in these past Part VII transfers. Some examples of the Court's judgments in relation to this matter are as follows:

- In the Part VII transfer of EEA business from The Royal London Mutual Insurance Society Limited to Royal London Insurance D.A.C., which was sanctioned by the Court on 31 January 2019, Snowden J concluded that "*I regard the potential loss of FSCS protection for some transferring policyholders as being a largely theoretical risk, as against the very real prejudice that all EEA policyholders would face in the event of a 'no-deal' Brexit if the Scheme were not implemented.*"

- In the Part VII transfer of EEA business from Scottish Widows Limited to Scottish Widows Europe S.A., which was sanctioned by the Court on 14 March 2019, Snowden J concluded that "*In my view, the loss of FSCS protection is too remote a potential prejudice to policyholders to warrant refusing to sanction the Scheme which will provide the means by which, if required, [Scottish Widows Limited] can provide far more immediate benefit of certainty of continued service to all its EEA policyholders.*"
- 6.126 It is my opinion that these conclusions could equally be applied in the case of this proposed Scheme, given that the motivation for the proposed Scheme is the same as the motivation for the schemes in the examples above, and that I have demonstrated in this Report that I consider the likelihood of the default or insolvency of AEI to be remote.
- 6.127 Post-Scheme, the Transferring Policyholders will no longer be eligible to bring complaints to the FOS, save those relating to acts or omissions of AGIL or LGI prior to the Effective Date. Instead, assuming that, by then, AEI will be registered with KiFiD, they will be eligible to bring to KiFiD complaints relating to acts or omissions of AEI post the Effective Date. In circumstances where AGIL or LGI currently refer policyholders to the FOS, AEI would refer those policyholders to KiFiD or to the competent dispute resolution agency within the relevant territory of the policyholder.
- 6.128 Thus, in practice, the transferring policyholder will continue to have access to the local dispute resolution processes in their own territory and any changes to their access to the FOS should not be material.
- 6.129 Therefore, I need to consider whether the ombudsman services provided by KiFiD rather than the FOS constitutes a material weakening in the ombudsman services available for Transferring Policyholders.
- 6.130 The complaints procedures for both the FOS and KiFiD are broadly similar. The FOS will not consider any appeals against its decisions, and, once accepted by the individual, decisions are legally binding. Under KiFiD, if an individual does not accept KiFiD's decision in relation to the individual's case, a decision is made regarding the resolution by the Disputes Committee within KiFiD, whose decisions are usually legally binding. The limit to the amount the FOS can make a business pay an individual is £150,000, whereas the KiFiD does not act on claims above €1 million.
- 6.131 I consider the services provided by the FOS and KiFiD to be broadly similar and I do not consider the differences outlined above to represent a material weakening in the ombudsman protections available to Transferring Policyholders.
- 6.132 Members of AEG management have told me that, in practice, non-UK policyholders of AGIL and LGI who have complaints are currently offered access to the local dispute resolution service that is in operation in a policyholder's own member state in addition to FOS. In the Transferors' experience, such policyholders do not normally refer disputes to the FOS and they instead utilise the local dispute resolution service in their own member state. It is proposed that AEI will adopt similar processes. In circumstances where AGIL or LGI currently refers policyholders to the FOS, AEI would refer those policyholders to KiFiD and to the policyholder's local dispute resolution process
- 6.133 AEI is registered with KiFiD. Although KiFiD has some jurisdiction over policyholder disputes arising outside the Netherlands, in practice they will normally be referred to the local competent dispute resolution service under the arrangements agreed by FIN-NET.
- 6.134 Thus, in practice, the transferring policyholder will continue to have access to the local dispute resolution processes in their own territory and any changes to their access to the FOS should not be material. Overall, given the similarities in the services provided by the FOS and KiFiD, and the continued access to local ombudsman services, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on the rights of the Transferring Policyholders in relation to their access to the services of a financial ombudsman.
- 6.135 I note that, in respect of any proceedings in relation to the Transferring Policies which (a) have commenced but not been settled before the Effective Date, or (b) commence after the Effective Date in respect of acts or omissions of AGIL or LGI prior to the Effective Date, AEI will (subject to prevailing regulatory requirements) comply with:
- the relevant provisions of Dispute Resolution Complaints rules issued by the FCA that would apply to the handling of any complaints brought to the FOS that fall under the jurisdiction of the FOS; and

- any valid judgment, settlement, order or award (or relevant part thereof) of the FOS, made under its jurisdiction.

#### **IMPACT WERE THE ASSURANT LIFE SCHEME TO BE DELAYED BEYOND THE EFFECTIVE DATE**

- 6.136 If the Life Scheme were to be delayed beyond the Effective Date then the EEA Creditor Policies would be Residual Policies until such time as the Life Scheme were effected on until another means were arranged to transfer the EEA Creditor Policies to AEI.
- 6.137 Until the transfer to AEI were completed, AEI would have neither assets nor liabilities relating to the Residual Policies. As AEI would have been capitalised on or before the Effective Date to a level to receive the Transferring Business (including the Residual Policies), this will mean that AEI's own funds are unchanged from the level forecast but that the SCR will be less due to there being less insurance risk within AEI.
- 6.138 This will improve the security of benefits enjoyed by the Transferring Policyholders for whom the transfer is effected on the Effective Date.

#### **CONCLUSION FOR THE TRANSFERRING POLICYHOLDERS**

- 6.139 I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on:
- The security of benefits under the Transferring Policies;
  - The benefits that the Transferring Policyholders could reasonably expect to receive; or
  - The standards of administration, service, management and governance that apply to the Transferring Policies.

## 7. The impact of the Scheme on the holders of AGIL and LGI policies that are not being transferred under the Scheme

- 7.1 In this section of the Report, I consider the impact of the Scheme on those policyholders of AGIL whose policies will not be transferred to AEI but who therefore will remain AGIL policyholders after the Effective Date. I also consider the impact of the Scheme on those policyholders of LGI whose policies will not be transferred to AEI but who therefore will remain LGI policyholders after the Effective Date.
- 7.2 Those policyholders remaining after the Effective Date will include holders of Residual Policies, if any. As noted in paragraph 5.19, above, it is intended that there will be no Residual Policies. The Companies shall work towards transferring to AEI each and every Residual Policy, if any, by novation or by other means.

### FINANCIAL STRENGTH OF AGIL AND LGI, PRE AND POST-SCHEME.

- 7.3 In Section 6, above, I have established that:
- that AGIL's reserves (both on a UK GAAP and Solvency II basis) appear reasonable as at 31 December 2019 (paragraph 6.35, above); and
  - that LGI's reserves (both on a UK GAAP basis and on a Solvency II basis) appear reasonable as at 31 December 2019 (paragraph 6.61, above).
- 7.4 I have no reason to expect any change in the strength of the reserves held post-Scheme by AGIL or LGI in respect of their business that is not transferred by the Scheme, relative to the strength of the reserves held pre-Scheme by AGIL and LGI in respect of the same business.
- 7.5 In Section 6, above, I have further established that:
- the policyholders of AGIL currently benefit from the financial strength provided by a more than sufficiently capitalised company, which is expected to become a well-capitalised insurer by the Effective Date (paragraph 6.84, above); and
  - the policyholders of LGI currently benefit from the financial strength provided by a well-capitalised company, which is expected to become a very well capitalised insurer as at the Effective Date (paragraph 6.98).
- 7.6 As shown in Figure 5.9, above, had the Scheme been effective as at 31 December 2019, post-Scheme AGIL would have been considered a well-capitalised insurer. Similarly, as shown in Figure 5.10, above, had the Scheme been effective as at 31 December 2019, post-Scheme LGI would have been considered a very well-capitalised insurer. I note that this remains the case for both AGIL and LGI when Solvency II balance sheets for AGIL and for LGI are projected forward to the Effective Date.
- 7.7 These projections indicate that the Capital Cover Ratios within both AGIL and LGI are enhanced as a result of implementation of the Scheme.
- 7.8 Change in risk profile within AGIL and LGI, with less prominence to insurance risk and more to other risk types, especially market risk. Having said that, changes in the risk profiles within AGIL and LGI should be reflected in the SCR calculations.

### Conclusion

- 7.9 I have explained above why I consider that the calculations and projections of AEI's solvency requirements and available capital, and hence of its excess assets, are reasonable. Overall, these lead me to conclude that the policyholders who are not transferring will continue to benefit from the financial strength provided by their respective insurers, which are expected to be well-capitalised (AGIL) or very well capitalised (LGI) as at the Effective Date.

### POLICY SERVICING AND TERMS & CONDITIONS

- 7.10 The existing arrangements for servicing and administering the business of AGIL and LGI that is not being transferred by the Scheme will remain unchanged post-Scheme. Likewise, the terms & conditions of the policies not being transferred by the Scheme will remain unaltered post-Scheme.

- 7.11 In the case of Residual Policies, the situation following the end of the Transition Period is currently unclear. While it is possible that the regulators in the EEA states in which the underlying risks for any such Residual Policies are located might permit the continuation of the existing arrangements for servicing and administering the Residual Policies, it is also possible that some might not. In such circumstances, it might not be possible for AGIL and/or LGI to fulfil their obligations to the holders of Residual Policies without a technical breach of authorisation requirements in the relevant EEA state. The risk of this eventuality in respect of all of the Transferring Business is the primary motivation for the Scheme and, as noted above in paragraph 7.2, the Companies shall work towards transferring to AEI any such Residual Policy by novation or by other means. If there are any Residual Policies, the Scheme does not alter in any way the risk of it not being possible, post the Transition Period, for them to be serviced and administered in accordance with local authorisation requirements.

### Conclusion

- 7.12 I am satisfied that the policyholders of AGIL and LGI who are not being transferred by the Scheme will not experience any adverse change in the quality of servicing of their policies or in the terms and conditions of their policies as a result of the Scheme.

### OTHER MATTERS

- 7.13 In the event of the insolvency of AGIL, pre-Scheme, holders of direct policies would rank ahead of holders of inwards reinsurance policies and of unsecured debt in the distribution of the remaining assets of AGIL. This would also be the case were such an insolvency to occur post-Scheme, the differences being that, post-Scheme, the pool of policyholders would be smaller and the proportion of those policyholders who hold inwards reinsurance policies (if any) would be greater, there being no inwards reinsurance business included within the Transferring Business. This would also be the situation in the event of the insolvency, pre or post-Scheme, of LGI. Hence, I conclude that the Scheme does not affect to a material degree the prospects of the remaining policyholders of AGIL or LGI in the event of the post-Scheme insolvency of AGIL or LGI.
- 7.14 The Scheme will not affect the eligibility of remaining policyholders of either AGIL or LGI to seek compensation from the FSCS or to take complaints to the FOS.

### IMPACT WERE THE ASSURANT LIFE SCHEME TO BE DELAYED BEYOND THE EFFECTIVE DATE

- 7.15 If the Assurant Life Scheme were to be delayed beyond the Effective Date then the EEA Creditor Policies would be Residual Policies until such time as the Life Scheme were effected on until another means were arranged to transfer the EEA Creditor Policies to AEI.
- 7.16 Until the transfer of the EEA Creditor Policies to AEI were completed, AGIL would retain the assets and liabilities relating to the AGIL EEA Creditor Policies Business and LGI would retain the assets and liabilities relating to the LGI EEA Creditor Policies Business. This would be neutral in terms of its impact upon the own funds of both AGIL and LGI but would result in their post-Scheme SCR's being higher than would be the case were the Assurant Life Scheme not delayed and were the EEA Creditor policies not to become Residual Policies. The increase in the SCR would be more profound for LGI than for AGIL as LGI has a significantly larger proportion of the liability relating to the EEA Creditor Policies.
- 7.17 This would leave AGIL with a post-Scheme Capital Cover Ratio slightly less than that which it would have been had there been no Residual Policies, but at a higher level than pre-Scheme. Whether or not the Assurant Life Scheme were delayed, Post-Scheme AGIL would be well-capitalised and the position of the non-transferring AGIL policyholders would be unaltered.
- 7.18 In LGI, the dividend payment will reduce LGI's own funds by £25.8 million (and also the market risk element within the SCR). The post-dividend but pre-Scheme Capital Cover Ratio would thus be reduced to a level consistent with being more than sufficiently capitalised. Post-Scheme, most of the LGI Transferring Policies would have become Residual Policies and so the SCR would only have reduced by a small amount, but it would have been sufficient to increase the Capital Cover Ratio to a level at or close to that of a well-capitalised insurer. Therefore, in relative terms, a delay in the Assurant Life Scheme would adversely affect the security of benefits of the non-transferring policyholders in LGI but, as they would continue to be policyholders of a well-capitalised insurer, any adverse impact would not be material.

**CONCLUSION FOR THE POLICYHOLDERS OF AGIL AND LGI NOT TRANSFERRING UNDER THE SCHEME**

- 7.19 I am satisfied that the security of the contractual rights or the standards of policy servicing currently enjoyed by policyholders of AGIL and LGI whose policies will remain with their current insurer post-Scheme will not be adversely affected to a material degree by the Scheme.

## 8. Other considerations

### THOSE ASSETS BEING TRANSFERRED TO AEI AND THOSE ASSETS REMAINING IN AGIL AND LGI

- 8.1 The investment assets that support the liabilities related to the Transferring Policies comprise a portfolio of corporate and government bonds, a small portfolio of equities, and cash. AGIL and LGI each maintains an asset and liability management process whereby, so far as practicable, the duration of assets and the duration of liabilities are matched, and the currencies are matched to the liabilities. Thus, the assets to be transferred will largely match the respective policy liabilities being transferred in both currency and duration and are readily identifiable in the current portfolio. Such assets are effectively segregated from the non-transferring investment portfolio, which is denominated in Sterling (for UK policies) and Swiss Francs (for Swiss policies). The bulk of the Transferring Assets (other than the outwards reinsurance contracts) will be denominated in Euros, with a small proportion in the other EU currencies of relevant territories outside the Eurozone.
- 8.2 I have been told by AEG that the transfer process will be managed to minimise the need for any liquidation of assets outside normal maturity and investment management activities and to minimise or avoid any foreign exchange impacts. Thus, the selection process for the transfer of investment assets will be directed by the current matching of assets and liabilities. The investment strategy of the AEI will be broadly the same as that of the Transferors, and AEI will use the same investment managers. This will facilitate the transfer of ownership of specific assets and assist in minimising any avoidable expense, value fluctuation or other impacts.

### Conclusion regarding the assets being transferred to AEI and those remaining with AGIL and LGI

- 8.3 Currently the assets and liabilities with AGIL and LGI are well matched. According to the process outlined to me by AEG, I believe that the assets transferred to AEI as part of the Transferring Business should be well matched, by duration and currency, to the Transferring Policies. As a corollary, the assets that do not transfer to AEI as part of the Transferring Business should be well matched, by duration and currency, to the policies that remain with AGIL and LGI, post-Scheme.

### OPERATIONAL PLANS AND CHANGES IN ASSETS AND LIABILITIES UP TO THE EFFECTIVE DATE

- 8.4 In this Report, I have shown balance sheet data for AGIL and LGI as at 31 December 2019 (this being the most recent date for which audited financial information is available). I have also shown pro forma balance sheets, which have been based on those actual balance sheets as at 31 December 2019, but which include data, as at 31 December 2019, that relates to the Scheme. Further, I have shown a pro forma balance sheet for AEI, as if the Scheme had taken place as at 31 December 2019.
- 8.5 I expect that the current activities of both AGIL and LGI have continued between 31 December 2019 and the date of this Report, and will continue between the date of this Report and the Effective Date. Both AGIL and LGI have continued, and will continue until the Effective Date, to write new business, and have continued, and will continue until the Effective Date, to settle claims and reassess reserves in the light of experience. I do not consider that any material additional risk to any group of affected policyholders will emerge as a result of the continuation of normal business.
- 8.6 I have considered the business plans and forecast numbers, both for AGIL and LGI and for AEI. Those plans and forecasts give me no cause to reconsider the conclusions that I have derived within this Report that were based on historic information.

### Impact of the COVID-19 Pandemic on the Scheme

- 8.7 I have discussed within paragraphs 4.122-4.125, above, the immediate operational issues created by the COVID-19 pandemic and the possible financial impacts on the Companies.

### *The potential market risk from COVID-19*

- 8.8 In recent weeks, there has been considerable volatility in the financial markets. I have been provided with estimated balance sheet impacts for AGIL, LGI and AEI that take account of the recent market volatility and show the solvency of AGIL, LGI and AEI as at 31 December 2019, assuming that the market volatility had occurred at this time.

- 8.9 In producing the estimated balance sheet impacts, the following assumptions have been made:
- A reduction in market value of assets of 5% for AGIL and 3% for LGI, reflecting the observed movement in assets resulting from COVID-19 and that LGI assets are longer-dated on average than those within AGIL; and
  - An increase in technical provisions of 2% for AGIL and 3% for LGI, reflecting their respective views on the impact of COVID-19 on their portfolios of business in aggregate.
- 8.10 I note that at the time of writing this Report, the volatility caused by COVID-19 is moving on a daily basis and it is therefore difficult to quantify the expected impact at a particular point in time. However, the approach used to determine the assumptions made, as outlined above, appears broadly reasonable.
- 8.11 The balance sheet impacts I have been provided show that AGIL, LGI and AEI all continue to hold capital in excess of their respective target levels, before and after the implementation of the proposed Scheme as at 31 December 2019, assuming the market volatility resulting from COVID-19 had occurred at that time. I have been told that, if it appears likely that the falls in asset values and the increases in the liabilities that have been caused by COVID-19 will be sustained and will make it unlikely that AEI would, post-Scheme, met its Target Capital, then further capital will be injected into AEI from elsewhere in the Assurant Group.
- 8.12 Overall, I am therefore satisfied that the increased volatility in financial markets resulting from COVID-19 is not expected to have a material adverse impact on the security of benefits of policyholders of AGIL, LGI and AEI both before and after the implementation of the proposed Scheme.

#### *The potential operational disruption from COVID-19*

- 8.13 As previously discussed, AEG has taken a number of steps to minimise the operational disruption from COVID-19. These appear to be working well, such that, while there has been some disruption and reduction in services, these are being minimised and the Companies are continuing to operate largely as normal.
- 8.14 Overall, AEG is taking an aligned approach to dealing with the operation disruption from COVID-19 across all of its entities, which include AGIL, LGI and AEI. Therefore, the measures taken by AGIL and LGI to ensure the continued administration and servicing of its policies in the event of operational disruption are aligned to those that AEI would take in respect of Transferring Policies if the Scheme were to be implemented.
- 8.15 In addition, I concluded in paragraph 6.117, above, that the implementation of the proposed Scheme would not have a material adverse effect on the levels and standards of administration and service that would apply to Transferring Policyholders, as all material aspects of policy administration and servicing will be unchanged by the implementation of the proposed Scheme. Therefore, I would not expect any operational disruption that could arise from COVID-19 to differ materially across AGIL, LGI and AEI in respect of policy servicing and administration.
- 8.16 The steps being taken by AEG in response to the operational disruption from COVID-19 appear to be reasonable and I am therefore satisfied that COVID-19 is not likely to materially change the impacts of the proposed Scheme on administration and service standards if it were to be implemented.

#### *FCA draft guidance*

- 8.17 On 1 May 2020, the FCA issued draft guidance for insurance firms regarding product value and the COVID-19 pandemic. This guidance was then finalised and became effective on 3 June 2020. Under the guidance, insurers are expected to consider whether and how coronavirus may have materially affected the value of their insurance products. Where such material changes are identified, they are further expected to consider the appropriate action to take.
- 8.18 I have been informed by AGIL and LGI that they are aware of the guidance and have discussed this topic and their products with the PRA and FCA during May 2020. They have conducted a review of their entire product base and, while this has yet to be ratified by their respective Boards, their current view is that all of their products continue to provide fair value to their customers and that they do not anticipate making any material changes. As such, AGIL and LGI do not expect that this guidance will affect them commercially to a material extent.

### Conclusion regarding the potential risks from COVID-19

- 8.19 Having taken the above factors into account, I am satisfied that the COVID-19 pandemic does not provide any reason to change my conclusions in this Report. However, given the rapidly developing nature of the COVID-19 outbreak, I will provide an update on the potential risks from COVID-19 in my Supplementary Report, and will also, if necessary, provide an Update Addendum to the Court immediately before the Directions Hearing.
- 8.20 I believe that it is unlikely that any other events that have occurred between 31 December 2019 and the date of this Report, or which is likely to occur between the date of this Report and the Effective Date would affect any conclusion that I have reached based on my review as at 31 December 2019. However, I will consider this further, in the light of emerging experience and of any changes in expectations, in my Supplementary Report.

### THE LIKELY EFFECTS OF THE SCHEME UPON REINSURERS OF THE TRANSFERRING BUSINESS

- 8.21 In accordance with the PRA Statement of Policy and SUP18, I have considered the likely effects of the Scheme on the reinsurers whose reinsurance contracts cover the Transferring Business.
- 8.22 Leaving aside the quota share reinsurance of LGI's business by VSC, most of the reinsurance contracts benefiting the Transferring Business will transfer under the Scheme (it is intended to transfer those not included in the Scheme by consent through contractual novation). As at 31 December 2019, the reinsurers' share of technical provisions amounted to £14.5 million on a UK GAAP basis and £13.5 million on a Solvency II basis.
- 8.23 The amount of the liabilities of each external reinsurer of the Transferring Business will not change as a result of the Scheme.
- 8.24 As noted in paragraph 6.116 (and elsewhere), above, the administration of the Transferring Business will be unaffected by the Scheme. Therefore, I have no reason to expect any change in the standards of claims handling or management. Hence, the magnitude and timing of recoveries claimed against reinsurance contracts relating to the Transferring Business will be unaffected by the Scheme.
- 8.25 I have considered whether the Scheme are likely to lead to any changes in the rights of "set-off"<sup>14</sup> for creditors or debtors of AGIL or LGI. The Transferring Business comprises insurance contracts mitigated by outwards reinsurance contracts. Any mutual debits or mutual credits relating solely to the Transferring Business would be available, post-Scheme, to AEI, but any that existed in AGIL or LGI where one side only related to the Transferring Business would be lost. I have been told that the amount of set-off within either of the Transferors that would be lost as a result of the Scheme is negligible. This would only be an issue were either of the Transferors, post-Scheme, to become insolvent. However, I consider the likelihood of either AGIL or LGI becoming insolvent, post-Scheme, to be remote. As such, I do not believe the right of set-off affects my conclusions on the impact of the Scheme on reinsurers.

### Conclusion for the reinsurers of the Transferring Business

- 8.26 For the reasons discussed above, I am satisfied that the Scheme will not have a materially adverse effect on the reinsurers whose contracts of reinsurance currently benefit the Transferring Business.

### THE APPROACH TO COMMUNICATION WITH POLICYHOLDERS

- 8.27 Regulations made under the FSMA require a communication regarding the proposed Scheme to be sent to every policyholder of the Companies. However, consideration may be given to the practicality and costs of sending notices against the likely benefits for policyholders of receiving such communications. In order to comply with paragraph 2.53 of the Policy Statement, paragraph 2.46G of SUP18 and Sections 7 and 8 of FG18/4, the Companies would be expected to notify the policyholders, or interested persons (which would include those reinsurers of AGIL or LGI whose contacts will be transferred to AEI under the Scheme), at least six weeks before the date of the Court hearing at which the application to sanction the Scheme will be heard.

<sup>14</sup> "Set-off" allows parties to cancel or offset mutual debts with each other by subtracting one from the other, and paying only the balance.

- 8.28 The Companies' approach to communicating the Scheme to affected policyholders is outlined in paragraphs 5.45-5.58, above.
- 8.29 I consider the approach being taken to those Transferring Policyholders that AGIL and LGI intend contacting directly to be reasonable.
- 8.30 I consider it reasonable that the Companies will be applying to the Court for waivers in respect of the requirement to make direct notification to the following groups:
- Transferring Policyholders for whom AGIL, LGI or the relevant distributors/intermediaries hold no valid contact details<sup>15</sup>;
  - Transferring Policyholders whose contracts have expired and for whom there is no on-going period of cover and no known current claims exposure;
  - Those reinsurers of AGIL and LGI whose contracts of reinsurance will not be transferred to AEI under the Scheme; and
  - Those policyholders of AGIL and LGI who are not Transferring Policyholders.
- 8.31 The Transferors are not aware of any substantial proportion of the Transferring Policyholders whose contact details, as held by the Transferors or by the relevant distributors/intermediaries, are incorrect. They consider that, to comply with the requirement to contact directly all Transferring Policyholders including those for whom there are no valid contact details, is impractical and probably impossible. I note that I have concluded earlier in this Report that the Scheme will result in no change to either the benefits or the level of servicing that the Transferring Policyholders can expect to receive, and that the Transferring Policyholders will not be materially adversely affected by the Scheme.
- 8.32 As regards those Transferring Policyholders whose contracts have expired, I note that:
- the nature of the insurance cover provided under the Transferring Policies is inherently "short tail", with any claims notifications tending to follow promptly after an insured event has occurred;
  - claims are triggered by insured events that give rise to financial loss, which will involve loss, breakdown or damage to the insured item (for extended warranty insurance products) or loss of income or loss of capacity to work (for payment protection insurance products). This reduces the latency of unknown claims;
  - the potential for any adverse impact on those Transferring Policyholders with expired policies is mitigated by the existence of consistent claims administration services and contact points post-Scheme through the customer service arrangements that currently exist.
- 8.33 The Transferors does not propose to write to their policyholders who are not Transferring Policyholders on the basis that:
- They consider it unlikely that any such policyholders would be adversely affected by the Scheme and that, therefore, there would be little benefit in notifying directly those policyholders who are not Transferring Policyholders, indeed such notification might give rise to customer confusion;
  - The number of AGIL and LGI policyholders who are not Transferring Policyholders is roughly 10 million. The costs of notifying them all has been estimated to be in excess of £4.5 million and would therefore be disproportionate];
  - There will be indirect publicity for the Scheme, as set out in paragraph 5.56, above; and
  - the key documentation relating to the Scheme will be made available to any and all interested parties, on request or via the Transfer Websites, as described at paragraph 5.57, above.

<sup>15</sup> I have been informed by the Companies that the policyholders for whom they are aware they have no contact details relate primarily to approximately 60,000 warranty insurance policies written by LGI in Spain. These policies were sold through approximately 400 to 500 retail stores affiliated to two Assurant clients in Spain and provided cover on electrical appliances sold by those retail stores. It was not necessary to collect contact details as the receipt provided by the retail store at the point of sale would be sufficient evidence of the policyholder's right to claim under the insurance contract (the policy number is linked to the receipt number). LGI will contact the two Assurant clients and ask them to inform the retail stores of the Scheme. Each retail store will then be asked that, in the event that in the period between the Directions Hearing and the Effective Date a policyholder presents a claim, it informs the policyholder of the proposed Scheme and explains how further information could be obtained.

- 8.34 I have reviewed draft copies of the proposed notices and letters, including the draft summary of the Scheme and of the Report. I am not an expert in such communications. However, I consider the draft notices and letters to be clear and concise, to contain all of the information that I would expect them to contain, to be fair, and to be appropriate for their intended audiences.
- 8.35 I am satisfied that the proposed approach to communication with policyholders in respect of the Scheme is both proportionate and reasonable.
- 8.36 In the Supplementary Report, I shall consider how the proposed communication plan has worked in practice and I shall also consider the responses received (and how the Companies have reacted to those responses). In particular, I shall consider in detail any and all objections raised to the Scheme.

## THE RECENT JUDGMENT ON THE PRUDENTIAL/ROTHESAY SCHEME

### Introduction

- 8.37 On 16 August 2019, the Court declined to sanction the transfer of a £12 billion portfolio of annuities from Prudential Assurance Company Limited (“**Prudential**”) to Rothesay Life Limited (“**Rothesay**”). Prudential and Rothesay had sought to effect the transfer of the portfolio pursuant to Part VII of FSMA.
- 8.38 I have considered the Scheme in the context of the Court’s decision in respect of that proposed transfer of an annuity portfolio (the “**Prudential/Rothesay Scheme**”). I am not an expert in either matters relating to life assurance or, as I noted in paragraph 1.55, legal matters. Nevertheless, based on my understanding of the judgment and my reasoning as set out below, I am satisfied that the conclusions in this Report are unaffected by the judgment in the Prudential/Rothesay Scheme.
- 8.39 I have summarised my understanding of the reasons cited by the presiding judge for his decision into the following subsections:
- The policy types (annuities) that were to be transferred under the Prudential Rothesay Scheme
  - The reasonable expectations of policyholders
  - The security of the benefits under the policies affected by the Scheme
  - 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
- 8.40 I provide further details on each of these areas, below, along with my views on the relevance to the proposed Scheme of each such area.

### The policies to be transferred under the Scheme

- 8.41 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 that these annuities paid an income to customers in retirement, it was likely that if the provider were to fail, however remote the possibility, then the result would be catastrophic for policyholders.
- 8.42 There are no annuities in the Transferring Business. The Transferring Business is very different from the business within the Prudential/Rothesay Scheme. In particular, it is short term in nature and it does not form a significant part of the wealth of the Transferring Policyholders.

8.43 Consequently, I am satisfied that the Transferring Policyholders would be less vulnerable to the type of catastrophic consequences of insurance company failure that was envisaged by the presiding judge in respect of the Prudential/Rothsay Scheme, particularly as it is an intragroup transfer.

#### The reasonable expectations of policyholders

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

8.45 For the Prudential/Rothsay Scheme, the presiding judge considered there to be merit in the arguments from policyholders that they had reasonable expectations that Prudential would not transfer its obligations under the their respective policies to another company. In forming this view, he 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.

8.46 The first of these bullet points in paragraph 8.45, above, may apply to an extent to the Transferring Policies. However, as I have explained in this Report, I am satisfied that the proposed Scheme will not materially disadvantage the Transferring Policyholders. Indeed, as explained in paragraph 8.74, below, the Transferring Policyholders might be materially disadvantaged if the proposed Scheme does not proceed.

8.47 As regards the second of these bullet points, I am unaware of any statements made for marketing purposes by either AGIL or LGI that emphasise particular characteristics (such as longevity or trustworthiness) that would not apply to AEI, seeing that AGIL, LGI and AEI are all members of the Assurant Group.

8.48 I have no reason to suspect that policyholders' (reasonable) expectations would be adversely affected to a material extent.

#### The security of benefits under the policies affected by the Scheme

8.49 The presiding judge in respect of the Prudential/Rothsay Scheme highlighted the potential differences in the availability of financial resources between Prudential and Rothsay. In particular, it was his view that Prudential's parent provided greater security to Prudential than Rothsay's parent companies did for Rothsay because he felt that Rothsay's three main shareholders could more easily distance themselves from their subsidiary should they wish to do so.

8.50 I deal with the impact of the Scheme upon the security of benefits for the Transferring Policyholders in Section 6, above, of this Report. 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.

8.51 Therefore, the security of benefits to the Transferring Policyholders is provided:

- Pre-Scheme by the financial strength of AGIL and LGI and any support from being subsidiaries of the Assurant Group; and
- Post-Scheme by the financial strength of AEI and any support from being a subsidiary of the Assurant Group.

8.52 In this case, as this is an intra-group transfer, the parental support available to the protect the benefits of the Transferring Business is identical post-Scheme to that available pre-Scheme, and the presiding judge's concerns in this respect in relation to the Prudential/Rothsay Scheme do not apply.

8.53 I also note that the Prudential/Rothsay Scheme was concerned with annuity policies, for which, in general, the period to expiry of liability would be expected to be considerably longer than that in respect of the Transferring Policies.

### The age and reputation of the firms involved in the Scheme

- 8.54 For the Prudential/Rothesay Scheme, the presiding judge 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.
- 8.55 In the proposed Scheme, the transfer is between subsidiaries of the same group, the Assurant Group. LGI was established in 1984 and has traded under its current name since 1985; AGIL was established in 1989 and has traded under its current name since 2007; AEI is a new company. In addition, I note that most of AGIL and LGI's insurance business has been written under the brand of their clients, and therefore awareness of the Assurant Group is likely to be low for most Transferring Policyholders. I do not believe that there are significant differences between the age and reputation for the Assurant Group entities involved in the scheme.
- 8.56 I am satisfied that if the proposed Scheme were to be implemented and the Transferred Policies were to transfer from AGIL and LGI to AEI, the difference between the respective ages and reputations of the companies would not lead to a material adverse effect on the Transferred Policies.

### The balance between the interests of the policyholders and those of the commercial parties to the transfer

- 8.57 I understand that the Prudential/Rothesay Scheme was partly motivated by the desire of Prudential to release solvency capital. In his judgment on the Prudential/Rothesay Scheme, the presiding judge noted that most of the economic benefits of the transaction had already been achieved via the 100% quota share reinsurance arrangement that had been put in place between the two firms in respect of the Transferred Business. He considered that, whereas Prudential and Rothesay had already largely achieved their business purpose, the implementation of the Prudential/Rothesay Scheme would lead to a "fundamental change" for the transferring annuitants. Thus, he saw an imbalance between the interests of the policyholders and those of the commercial parties to the Scheme.
- 8.58 As stated in Section 5, above, the reason for the proposed Scheme results from the decision of the UK to leave the EU and the Assurant Group's desire to continue to be able to service the business relating to its EEA risks while retaining regulatory compliance post the Transition Period. That aim cannot be satisfied without the Scheme being effected. The reinsurance arrangement between Prudential and Rothesay was effectively a portfolio transfer of the economic risk relating to the transferring annuitants, with the Prudential/Rothesay Scheme then intended to transfer to Rothesay the legal risk relating to the transferring annuitants, thus giving Prudential finality in respect of the transferring business. In this Scheme, there are no reinsurance arrangements between the Transferors and the Transferee – all of the existing reinsurance arrangements relating to the Transferring Business are with third party providers and all will be transferred to AEI by the Scheme – and thus no risk, either economic or legal, has been transferred or will be transferred from AGIL or LGI to AEI prior to the Effective Date.
- 8.59 Consequently, as the reasons for the proposed Scheme are essentially legal and regulatory, in nature I am happy that it strikes a reasonable balance between the interests of the policyholders and the commercial interests of the Assurant Group and its subsidiaries involved in the transfer.

### The number of complaints about, and objections to, the Scheme

- 8.60 Under the Prudential/Rothesay Scheme, around 1,000 of the responses received could be classified as objections. This was considered a significant level of objections from policyholders, even though it only amounted to around 0.4% of the total communications packs sent to policyholders.
- 8.61 As of the date of this Report, the policyholder communication process has not begun. I will comment in my Supplementary Report on the level of responses and on any significant policyholder objections that are received.

### Overall conclusions regarding the recent judgment on the Prudential Rothesay Scheme

- 8.62 Only a few of the factors that influenced the judgment on the Prudential/Rothesay Scheme are relevant to the Scheme and, in my view, none applies to the Scheme to the same extent as to the Prudential/Rothesay Scheme.
- 8.63 I am satisfied that the conclusions in this Report are unaffected by the judgment in the Prudential/Rothesay Scheme.

- 8.64 I have been informed that Prudential and Rothesay may be appealing the decision. If the outcome of any appeal is known by the time of the Sanction Hearing then I will address any points raised by it in my Supplementary Report.

#### CHANGE IN REGULATION

- 8.65 For the policyholders of AGIL and LGI who are not being transferred by the Scheme, there will be no change to the supervisory authorities as a result of the Scheme; they will remain the PRA and FCA. Thus, the Scheme will cause no adverse regulatory impact on such policyholders. Moreover, because there will be no change to the terms and conditions of the Transferring Policies, they will be subject post-Scheme to the same laws as they were pre-Scheme.
- 8.66 The Transferring Policyholders will experience a change in the supervisor as a result of the Scheme. Pre-Scheme, the prudential supervision of their insurers was undertaken by the PRA, while, post-Scheme, the prudential supervision of their insurer will be undertaken by the DNB.
- 8.67 I note that Solvency II has essentially harmonised prudential supervision across the EU. As such, I consider that the prudential regulatory regime in the Netherlands to be substantively similar to that operating in the UK (through to the end of the Transition Period).
- 8.68 In general, conduct regulation is performed by a combination of the regulator of the home state of the insurer and the regulator of the host state in which the risk is located. In the case of Transferring Policyholders, although the location of the risk is not changing, the home state and hence the primary regulator will change from the UK to the Netherlands. However, any regulated activity carried out within one of the other EEA states will continue to be regulated by the local conduct regulator, in combination with the Netherlands regulator.
- 8.69 Thus, in cases where a Transferring Policy is currently administered and serviced by a UK-regulated entity, post-Scheme it will be subject to the Dutch conduct regime, and oversight would be provided by the AFM rather than the FCA.
- 8.70 The Dutch Corporate Governance Code contains principles and best practices relating to the governance of companies, which the DNB and AFM apply to Dutch insurers. Further, the DNB and AFM are both members of EIOPA and operate within a significant and sophisticated insurance market, and there is therefore no reason to believe that the oversight standards would be any lower than those applied within the UK. Finally, AEI is wholly owned by TWGE, a company that is regulated by the PRA and the FCA in the UK.
- 8.71 As such, I do not consider that the Transferring Policyholders are likely to be materially adversely affected by any change in the conduct regime as a result of the Scheme.
- 8.72 Thus, I have concluded that, while Transferring Policyholders will experience a change in the prudential supervision of their insurer as a result of the Scheme, the effects of any of these changes are unlikely to affect adversely the Transferring Policyholders to a material degree. I have further concluded that, while Transferring Policyholders will experience a change in the conduct regulation of their insurer (and possibly of the entities that administer and service their policies) as a result of the Scheme, the effects of any of these changes are unlikely to affect adversely the Transferring Policyholders to a material degree.

#### WHAT WOULD HAPPEN WERE THE SCHEME NOT TO PROCEED?

- 8.73 In the event that the Scheme does not proceed, the AGIL Transferring Policyholders would continue to be policyholders of AGIL, and would continue to benefit from the financial strength afforded by a more than sufficiently capitalised company. Similarly, the LGI Transferring Policyholders would continue to be policyholders of LGI, and would continue to benefit from the financial strength afforded by a well-capitalised company.
- 8.74 In the short term, should the Scheme does not proceed, the Transferring Policyholders would continue to enjoy the same level of service that they have always enjoyed. However, as explained in paragraphs 3.27-3.31, above, there is a material risk that, after the end of the Transition Period, regulations in one or more EEA state would prevent the Transferors from servicing their respective Transferring Policies in such states or providing the Transferring Policyholders with the benefits to which their policies entitle them.

## LEGAL JURISDICTION

- 8.75 I understand that, prior to the end of the Transition Period, an insurance business transfer scheme as defined in Section 105 of FSMA would be effective as a result of the Court Order sanctioning the business transfers for all policies governed by the law of an EEA member state. However, there is no obligation on the courts of non-EEA states to recognise automatically the ability of the Court to transfer a policy governed by non-EEA state laws. Thus, it may be possible for policyholders with non-EEA policies to challenge the validity of a sanctioned transfer subsequent to its effective date.
- 8.76 I have been told that none of the Transferring Policies is governed by laws other than those of one of the EEA states. Therefore, I conclude that there is no risk that such a challenge might reasonably be made in respect of the Scheme, providing that it is sanctioned by the Court prior to the end of the Transition Period.

## TAX

- 8.77 The Scheme will create no change in the tax liability of policyholders. Policyholders are taxed for the insurance services bought at the point of sale, through Insurance Premium Tax (“IPT”), and not at the delivery of those services (i.e. there is no tax on claim payment). IPT is due and payable based on where the risk is located. For the type of risks underwritten by AGIL and LGI, this is deemed to be the country of residence of the policyholder. Therefore, the domicile of the insurance company underwriting the risks and whether those risks are written via a branch (freedom of establishment) or under freedom of services rules.
- 8.78 The Scheme transfers to AEI from AGIL and LGI existing insurance liabilities arising from business already written, together with suitable supporting investment assets of the same value. There will be nil net gain in either AGIL or LGI as a result of this transfer and hence no additional tax payment would be due in the UK.
- 8.79 Additional assets (including goodwill) have been and will be transferred to the AEI to enable AEI to write future business within the EEA (subject to AEI having obtained appropriate permissions). Such transfers might give rise to taxable gains.
- 8.80 Tax professionals within AEG have provided me with their initial valuations of the tax implications of the Scheme for AGIL and for LGI. I am not an expert on tax but the costs involved are less than £1 million for each entity.
- 8.81 Therefore, I conclude that no material tax issues or liabilities associated with the Scheme that would affect either the Transferring Policyholders or those remaining within LGI or AGIL.

## COSTS

- 8.82 I have been told by AEG that the total costs of the Scheme will be split between Assurant, AGIL, LGI and AEI, with the majority being met by Assurant. The costs of the Scheme will not be met by any policyholders of AGIL or LGI.
- 8.83 As at the date of this Report, I had not been provided with an estimate of the cost of the Scheme or of how much of that cost would be carried by AGIL and by LGI. However, based on other Part VII schemes in which I have been involved, I consider it unlikely that the cost would be such that the post-Scheme Capital Cover Ratios of either AGIL or LGI would be reduced materially from the levels indicated earlier in this Report. In the very unlikely event that costs associated with the proposed Scheme threaten to breach the target solvency cover of either AGIL or LGI, AGIL and LGI will take steps to ensure that their respective target solvency covers are maintained in accordance with their capital management policies.
- 8.84 I am satisfied that the allocation of costs as described above is reasonable, but I will comment on it further in the Supplementary Report, by which time I would expect that a cost estimate would have been made.

## 9. Conclusions

9.1 In summary, in my opinion, provided the proposed Scheme operates as intended, and I have no grounds for believing that it will not do so, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on:

- The benefit expectations of the Transferring Policyholders under the Transferring Policies;
- The security of the benefits under the Transferring Policies;
- The level and standards of administration and service that would apply to the Transferring Policies;
- The benefit expectations of the policyholders of AGIL and LGI whose policies will not be transferred to AEI under the Scheme;
- The security of the benefits of the policyholders of AGIL and LGI whose policies will not be transferred to AEI under the Scheme;
- The level and standards of administration and service that would apply to the policies of AGIL and LGI that will not be transferred to AEI under the Scheme.

9.2 In reaching this opinion I have applied the following principles:

- I have considered which parties might be affected by the Scheme and in what way. I have documented my findings.
- I have not performed my own modelling, rather I have relied on the results of models developed and operated within AGIL, LGI and AEI. I have reviewed documentation describing the models, describing and justifying the assumptions underlying those models, and explaining the derivation of the data underlying the models and assumptions, in particular explaining how its accuracy, completeness and relevance has been verified.
- To the best of my knowledge, there are no groups of policyholders for whom the impact of the Scheme has not been considered.
- I have considered how the Scheme might lead to any changes in the material risks to the benefits of the different interested parties.
- I have considered the impact on the actuarial information provided to me of AGIL, LGI and AEI having adopted alternative plausible assumptions.
- I have considered the impact on the Companies of COVID-19.
- I have not considered alternative arrangements.



Derek Newton / 19 June 2020

Fellow of the Institute and Faculty of Actuaries

## Appendix A Definitions

TERM	DEFINITION
<b>Accident year</b>	The year in which an incident that gives rise to an insurance claim occurs.
<b>ABE</b>	Actuarial best estimate.
<b>AEG</b>	Assurant Europe Group, a group of indirect subsidiaries of Assurant, Inc.
<b>AEI</b>	Assurant Europe Insurance N.V.
<b>AEL</b>	Assurant Europe Life Insurance N.V.
<b>AES</b>	Assurant Europe Services B.V.
<b>AFM</b>	The Netherlands Authority for the Financial Markets.
<b>AFR</b>	Actuarial Function Report, a report prepared at least annually by the Actuarial Function for the Board of the relevant insurer.
<b>AGIL</b>	Assurant General Insurance Limited.
<b>AGL</b>	Assurant Group Limited.
<b>ALL</b>	Assurant Life Limited.
<b>Assurant</b>	Assurant, Inc.
<b>Assurant Creditor Policies</b>	Policies written by AGIL or LGI that cover one or more of the following insurance risks: death, disability, sickness and unemployment.
<b>Assurant Europe</b>	Collectively, AEI, AEL and AES.
<b>Assurant Group</b>	The group of companies comprising Assurant and its direct and indirect subsidiaries (including AGIL, LGI and AEI).
<b>Assurant Life Scheme</b>	A Part VII transfer that is intended to run parallel to the Scheme, whereby the long-term insurance business of ALL and of LGL that relates to risks situated in an EEA Member State will be transferred to AEL.
<b>Available Capital</b>	Capital available to meet solvency capital requirements.
<b>BBNI</b>	Bound But Not Incepted.
<b>Best estimate</b>	This term is used in this Report in reference to an estimate of outstanding claim amounts and is intended to represent an expected value over a reasonable range of estimates. As such, a “best estimate” is not deliberately biased upwards or downwards, and does not include any margins. However, the limitations of actuarial projection methods mean that a “best estimate” is not a statistically rigorous estimate of the mean of the underlying distribution of all possible outcomes.
<b>B-F</b>	The Bornhuetter-Ferguson method, which is a commonly used actuarial method for estimating claim reserves.
<b>Brexit</b>	“Brexit” refers to the exit of the UK from the European Union on 31 January 2020, following the referendum on continuing membership held in the UK in June 2016. As at the time of drafting this Report, the future relationship between the UK and the EU, including the regulatory environment for insurers operating across UK/EEA borders, was being negotiated. Until the completion of the transition period (currently scheduled to finish on 31 December 2020) the regulatory environment for insurers remains unaltered from its pre-Brexit state.
<b>Capital Cover Ratio</b>	The ratio of Available Capital to Required Capital. This is a measure of the capital strength of the insurer – the higher the ratio, the stronger the company.
<b>CL</b>	Chain ladder, a commonly used actuarial method for estimating claim reserves.
<b>Companies</b>	The collective term for AGIL, LGI and AEI.
<b>Correlation</b>	Correlation (in the context of this Report) is a number that describes the statistical relationship between two variables (e.g. equity prices and interest rates).
<b>Court</b>	The High Court of Justice of England and Wales.

<b>DNB</b>	The Dutch Central Bank (De Nederlandsche Bank).
<b>Dutch Act on Financial Supervision</b>	In Dutch, <i>Wet op het financieel toezicht</i> . Under this Act the DNB exercises its responsibility for the prudential supervision of Dutch insurance companies.
<b>EEA</b>	The European Economic Area (“EEA”) was established by the EEA Agreement on 1 January 1994. The EEA unites the 27 EU member states with Iceland, Liechtenstein, and Norway into an internal market governed by the same basic rules. These rules aim to enable goods, services, capital, and persons to move freely about the EEA in an open and competitive environment, a concept referred to as the four freedoms.
<b>Effective Date</b>	The date on and from which the Scheme shall become effective, which is expected to be 2 November 2020.
<b>EIOPA</b>	The European Insurance and Occupational Pensions Authority (“EIOPA”) was established in consequence of the reforms to the structure of supervision of the financial sector in the European Union, with the goals of: better protecting consumers and rebuilding trust in the financial system; ensuring a high, effective and consistent level of regulation and supervision taking account of the varying interests of all Member States and the different nature of financial institutions; greater harmonisation and coherent application of rules for financial institutions & markets across the European Union; strengthening oversight of cross-border groups; and promoting coordinated European Union supervisory responses.
<b>ENID</b>	In estimating the technical provisions under Solvency II, insurers must make allowance for events not in data (“ENID”), i.e. those possible future events or developments that have not been seen in the historic claims experience of the insurer.
<b>EU</b>	European Union.
<b>FCA</b>	The Financial Conduct Authority (“FCA”) is the UK regulatory agency that focuses on the regulation of conduct by retail and wholesale financial services firms. The FCA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
<b>FG18/4</b>	Guidance published by the FCA in May 2018 relating to Part VII insurance business transfers.
<b>FIN-NET</b>	An international partnership of financial complaint institutes of which KiFiD is a member
<b>FOS</b>	Set up by the UK Parliament, the Financial Ombudsman Service (“FOS”) is the UK’s official expert in sorting out problems with financial services.
<b>FSCS</b>	The Financial Services Compensation Scheme (“FSCS”) is the compensation fund of last resort for customers of UK authorised financial services firms.
<b>FSMA</b>	Financial Services and Markets Act 2000, the legislation under which Part VII governs the transfer of (re)insurance business between (re)insurance undertakings.
<b>GAAP</b>	Generally accepted accounting principles (“GAAP”) form the standard framework of guidelines for financial accounting used in any given jurisdiction.
<b>GMT</b>	Greenwich Mean Time.
<b>IBNR reserves</b>	These are reserves in respect of claims that relate to claim events that have occurred before the valuation date but which were still to be reported to the insurer as at that date. For the purposes of this Report they also include reserves in respect of any perceived shortfall between the projected ultimate costs and the case estimates for claims already notified.
<b>IDD</b>	The Insurance Distribution Directive, which has applied in the UK (and in all other EU Member States) with effect from 1 October 2018.
<b>IFoA</b>	The Institute and Faculty of Actuaries, the professional body for actuaries in the UK.

<b>IFRS</b>	International Financial Reporting Standards (“IFRS”) form a common global language for business affairs so that company accounts are understandable and comparable across international boundaries.
<b>Independent Expert</b>	The Independent Expert prepares the Scheme Report and provides it to the Court in order that it may properly assess the impact of the proposed transfer, including the likely effects on the policyholders of the insurance companies in question. In the case of the Scheme, I have been appointed as the Independent Expert.
<b>Independent Peer Review</b>	Work Review undertaken by one or more individual(s) who is, or are, not otherwise involved in the work in question and who would have had the appropriate experience and expertise to take responsibility for the work themselves.
<b>IPT</b>	Insurance Premium Tax.
<b>KiFiD</b>	The Dutch Financial Services Complaints Institute (Klachteninstituut Financiële Dienstverlening).
<b>LGI</b>	London General Insurance Company Limited.
<b>LGI EEA Creditor Policies</b>	Those Creditor Policies that were written by LGI, that are linked to policies within LGL (i.e. co-issued by LGI and LGL) and that are included within the Transferring Business.
<b>LGL</b>	London General Life Company Limited.
<b>MCR</b>	The Solvency II Minimum Capital Requirement (“MCR”) is lower than the SCR, and defines the point of intensive regulatory intervention. The MCR calculation is less risk sensitive than the SCR calculation and is calibrated to a confidence level of 85% over one year (compared to 99.5% for the SCR).
<b>Milliman</b>	Milliman LLP, a member of the Milliman Group.
<b>The Milliman Group</b>	The group of entities whose ultimate parent is Milliman, Inc.
<b>NL ARCC</b>	The Audit, Risk and Compliance Committee for Assurant Europe.
<b>NLMB</b>	Management Board – each of the companies within Assurant Europe has its own NLMB
<b>NLSB</b>	Supervisory Board – each of the companies within Assurant Europe has its own NLSB.
<b>ORSA</b>	The Own Risk Solvency Assessment (“ORSA”) is a fundamental set of processes under Solvency II constituting a tool for decision-making and strategic analysis. It aims to assess, in a continuous and prospective way, the overall solvency needs related to the specific risk profile of the insurance company.
<b>Own Funds</b>	In Solvency II terminology, the amount of capital or excess assets of an insurance company. Own funds are divided into basic own funds and ancillary own funds (e.g. additional premiums from members), which require regulatory approval.
<b>PAD</b>	Provision for Adverse Deviation, a margin within the reserves held by AGIL and by LGI (and to be held by AEI) above the ABE.
<b>Part VII transfer</b>	A transfer of insurance business between one company and another pursuant to Part VII of FSMA.
<b>The Policy Statement</b>	The Statement of Policy issued by the PRA entitled The Prudential Regulation Authority’s approach to insurance business transfers, issued in April 2015.
<b>PRA</b>	The Prudential Regulation Authority (“PRA”) is part of the Bank of England and carries out the prudential regulation of financial firms in the UK, including banks, investment banks, building societies and insurance companies. The PRA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
<b>Prudential</b>	Prudential Assurance Company Limited.
<b>Prudential/Rothesay Scheme</b>	A proposed Part VII transfer of a portfolio of annuities from Prudential to Rothesay. The Court declined to sanction the Scheme on 16 August 2019.

<b>QRTs</b>	Quantitative Reporting Templates, which must be completed by insurers and submitted to the regulator on a regular basis in accordance with Solvency II. The QRTs cover a wide range of quantitative financial information about the insurer including details of its balance sheet, capital requirements and reserves.
<b>Required Capital</b>	The amount of capital an insurer must hold in order to meet its regulatory capital requirements (for example the SCR).
<b>Reinsurance</b>	An arrangement with another insurer whereby risks are shared (or passed on). If reinsurance is termed as being “inwards” then the reinsurer in question has accepted risk from an(other) (re)insurer; if reinsurance is termed as being “outwards” then the (re)insurer in question has passed risk to a(nother) reinsurer.
<b>Report</b>	References to the “Report” refer to this report, which is the Scheme Report relating to the Scheme.
<b>Report Summary</b>	The summary of this Report, prepared specifically to be included in a document that also summarises the Scheme and which will be made available to policyholders of the Companies and to others who might be affected by the Scheme.
<b>Residual Policy</b>	A contract of insurance (if any) written or assumed by AGIL or LGI under which any liability remains unsatisfied or outstanding as at the Effective Date and which would have formed part of the Transferring Business but which, for any reason, is not transferred by order of the Court on the Effective Date pursuant to the Scheme.
<b>Rothesay</b>	Rothesay Life Limited.
<b>RPPD</b>	The Responsibilities of Providers and Distributors for the Fair Treatment of Customers, a guidance document published by the FCA in January 2018.
<b>Scheme</b>	In the context of this Report, the proposal that the transferring business of AGIL and of LGI be transferred to AEI as a Part VII transfer.
<b>Scheme Document</b>	The document that sets out the terms of the Scheme.
<b>Scheme Report</b>	A report on the terms of a Part VII transfer, to be prepared by an independent person. The Scheme Report is required in order that the Court may properly assess the impact of the proposed transfer, including the effect on the policyholders of the insurance companies in question.
<b>SCR</b>	The Solvency Capital Requirement (“SCR”) under Solvency II is the amount of capital required to ensure continued solvency over a one-year trading time-frame with a likelihood of 99.5%.
<b>SFCR</b>	Each insurer is expected to publish a Solvency and Financial Condition Report (“SFCR”) annually, which will contain certain qualitative and quantitative information, the quantitative information being in the format of certain prescribed QRTs.
<b>Solvency II</b>	The system for establishing (among other things) minimum capital requirements for EU (re)insurers under the Solvency II Directive 2009/138/EC.
<b>SUP18</b>	Section 18 of the FCA Supervision Manual.
<b>Supplementary Report</b>	A report I will prepare in advance of the Court hearing to sanction the Scheme covering any relevant matters that might have arisen since the date of this Report.
<b>TCF</b>	The TCF (“treating customers fairly”) principles aim to raise standards in the way firms carry on their business by introducing changes that will benefit consumers and increase their confidence in the financial services industry. Specifically, TCF aims to: help customers fully understand the features, benefits, risks and costs of the financial products they buy; and minimise the sale of unsuitable products by encouraging best practice before, during and after a sale.
<b>Technical Provisions</b>	Liabilities determined for regulatory purposes. In particular, the provisions for the ultimate costs of settling all claims arising from events that have occurred up to the balance sheet date, including provision for claims incurred but not yet reported, less any amounts paid in respect of these claims; plus the provisions for future claims (and premiums) arising on unexpired periods of risk (see Appendix H for further details).

<b>TPs</b>	Technical provisions as calculated for Solvency II purposes. As such, they differ from technical provisions calculated on an IFRS basis.
<b>Transfer Websites</b>	www.assurant.co.uk, www.thewarrantygroup.eu and https://assurantnederland.nl, on which key documents relating to the Scheme will be made available free of charge.
<b>Transferee</b>	The entity to which business is being transferred – in the case of the Scheme, this is AEI.
<b>Transferor</b>	The entity from which business is being transferred – in the case of the Scheme, there are two Transferors: AGIL and LGI.
<b>Transferring Assets</b>	The assets of AGIL and of LGI that are included within the Transferring Business. Those that relate specifically to AGIL are referred to as AGIL Transferring Assets; those that relate specifically to LGI are referred to as LGI Transferring Assets.
<b>Transferring Business</b>	The business of AGIL and of LGI that is to be transferred to AEI under the Scheme.
<b>Transferring Policies</b>	The policies of AGIL and LGI that are included within the Transferring Business. Those that relate specifically to AGIL are referred to as AGIL Transferring Policies; those that relate specifically to LGI are referred to as LGI Transferring Policies.
<b>Transferring Policyholders</b>	The policyholders of the Transferring Business.
<b>Transition Period</b>	The period between the date on which the UK formally left the EU (31 January 2020) and 31 December 2020, during which period the existing trading relationships will continue unaltered and the future relationship between the UK and the EU will be negotiated. It is possible that the Transition Period may be extended to either 31 December 2021 or 31 December 2022, subject to the mutual agreement of the EU and UK, that agreement to be reached by 1 July 2020.
<b>TWGE</b>	The Warranty Group Europe, the parent company of LGI, LGL, AEI, AEL and AES.
<b>TWGS</b>	TWG Services Limited.
<b>UK ARCC</b>	The Audit, Risk and Compliance Committee for AEG's UK operations.
<b>ULAE</b>	Unallocated loss adjustment expenses, i.e. claim-related costs that cannot be allocated specifically to individual claims, such as the costs of running a claims team.
<b>Update Addendum</b>	The Update Addendum would provide an update to this Report in the event that there were developments relating to COVID-19 that were pertinent to the Scheme and which occurred shortly before the date of the Directions Hearing. If there were no such developments then no Update Addendum would be produced.
<b>UPR</b>	Unearned premium reserve.
<b>VSC</b>	Virginia Surety Company, Inc.
<b>Work Review</b>	Process by which a piece of actuarial work is considered by at least one other individual for the purpose of providing assurance as to the quality of the work in question.

## Appendix B CV for Derek Newton

- B.1 Derek Newton is a principal and actuarial consultant in Milliman's London office. He is leader of Milliman's UK General Insurance practice. He joined the firm in 2003.
- B.2 Derek started his actuarial career in 1983. Since 1994 he has worked exclusively within General Insurance, where he has experience with reserving, mergers and acquisitions (M&A) activity, portfolio transfers, Solvency II, the underwriting process, management reporting, designing and evaluating risk transfer mechanisms, premium rating, risk modelling, and capital and solvency evaluation. His experience includes:
- B.2.3 Leading teams reviewing reserves (and the internal reserving processes) for various insurers and reinsurers, including, where relevant providing statements of actuarial opinion for Lloyd's, for the Central Bank of Ireland, for the Bermudan Monetary Authority and for the relevant US insurance departments.
  - B.2.4 Assisting insurers with the preparation of solvency capital assessments, both internal and in accordance with prevailing regulatory requirements.
  - B.2.5 Leading assignments to review the underwriting effectiveness of several insurance operations, both commercial and personal lines, resulting in improved efficiency and additional profits to the insurers.
  - B.2.6 Providing independent expert support to insurers arranging transfers of business between themselves (see below).
  - B.2.7 Providing Actuarial Function support to several insurers.
  - B.2.8 Leading the evaluation of the reinsurance strategy and reinsurance programme for a major insurer.
  - B.2.9 Leading the review of various European insurers as part of due diligence assignments
- B.3 Of particular relevance in this context, Derek acted as the independent expert in respect of the following Part VII transfers:
- B.3.10 The transfer of the general insurance business of RL(CIS) Limited to CIS General Insurance Limited, a transfer that was sanctioned in 2014;
  - B.3.11 The transfer of general insurance business relating to the Tower pool from Royal & Sun Alliance Insurance PLC to Knapton Insurance Limited, a transfer that was sanctioned in 2015;
  - B.3.12 The transfer of the general insurance business of Dowa Insurance Company (Europe) Limited to Aioi Nissay Dowa Insurance Company of Europe Limited, a transfer that was sanctioned in 2016;
  - B.3.13 The transfer of general insurance business relating to the Ridgwell, Fox & Partners pool from QBE Insurance (Europe) Limited and from Moorgate Insurance Company Limited to Bothnia International Insurance Company Limited, a transfer that was sanctioned in 2017;
  - B.3.14 The transfer of general insurance business from Royal & Sun Alliance Insurance PLC and from The Marine Insurance Company Limited to AEI Indemnity Company Limited, a transfer that was sanctioned in 2019.
- B.4 In addition, Derek has been peer reviewer to the Independent Expert in the following transfers.
- B.4.15 the general insurance business of various UK-regulated subsidiaries of the Royal Sun Alliance Insurance Group to a smaller number of UK-regulated subsidiaries of Royal Sun Alliance Insurance Group. The transfers were approved by the Court on 12 December 2011;
  - B.4.16 the general insurance business of PA(GI) Limited to Royal Sun Alliance Insurance and to Marine Insurance Company Limited. The transfers were approved by the Court on 12 December 2011;
  - B.4.17 certain general insurance business of the Italian branch of Sampo Japan Insurance Company of Europe Limited to Berkshire Hathaway International Insurance Limited. The transfer was effective 31 March 2013;

- B.4.18 the general insurance business of Chevanstell Limited to R&Q Insurance (Malta) Limited. The transfer was effective 31 December 2013;
- B.4.19 the European branch general insurance business of Mitsui Sumitomo Insurance Company (Europe) Limited to MSIG Insurance Europe AG. The transfer was effective 31 December 2013;
- B.4.20 the EEA general insurance businesses of Sompo Japan Nipponkoa Insurance Company of Europe Limited and Endurance Worldwide Insurance Limited to SI Insurance (Europe), SA and the non-EEA business of Sompo Japan Nipponkoa Insurance Company of Europe Limited to Endurance Worldwide Insurance Limited. The transfer was effective 31 December 2018;
- B.4.21 the business of the Irish, Dutch, French and German branches of Travelers Insurance Company Limited to Travelers Insurance DAC. The transfer was effective 1 October 2019.
- B.5 Before joining Milliman, Derek was:
- A director of Heath Lambert's ART division (2002-2003)
  - A partner within Ernst & Young's UK property & casualty consulting practice (1998-2001)
  - In a variety of roles within Prudential plc (1983-1998), culminating in finance director and actuary for Prudential's UK general insurance operation.
- B.6 Derek was awarded Fellowship of the Institute of Actuaries in 1988. He was a member of the General Insurance Board of the Institute & Faculty of Actuaries (2002-2014) and chaired the Board 2005-2007. He also served on the Council of the Institute of Actuaries (2005-2010). He has chaired various actuarial working parties and authored or co-authored several papers. In 2013, Derek received a special award from the profession to mark his Outstanding Contribution to General Insurance Research.

## Appendix C Scope of the work of the Independent Expert in relation to the Scheme

The following was included within the letter of engagement that was agreed between the Companies, Milliman and me, and which was shown to the PRA prior to the approval by the PRA and FCA of my appointment as the Independent Expert in respect of the Scheme. As such, the following constitutes my terms of reference in respect of this assignment.

*“My report is to consider the terms of the Scheme generally and the effect that the Scheme will have on the Companies’ different groups of policyholders, including, for the avoidance of doubt, the policyholders of AGIL, LGI and AEI.*

*In particular, my report will consider the following specific matters in both such scenarios:*

- The impact of the Scheme on the security of benefits of policyholders, and on the risks to which policyholders will be exposed;*
- The impact of the Scheme on the benefit expectations of policyholders;*
- How the application of any management discretion that is embedded in the current policies would be affected by the transfer; and,*
- The impact of the Scheme on existing service levels and agreements.*

*The review and report will address generally the way in which the Companies have conducted their business but taking into account the particular circumstances of each class of insurance business to be transferred. It will deal inter alia with the following aspects:*

- Reserving, capital and security;*
- The terms of the respective policies issued by the Companies;*
- The Companies’ respective reinsurance agreements;*
- Any service, or other relevant, agreements with intra-group companies;*
- The regulatory regime, financial ombudsman scheme (or equivalent) and financial services compensation scheme (or equivalent) that policyholders of the transferor and transferee are subject to;*
- The existing and proposed internal working arrangements relating to the financial management of the business funds, including the operational and administrative arrangements which will apply to the business to be transferred under the terms of the insurance scheme;*
- The terms and conditions expected to be imposed by the Scheme to be presented to the Court;*
- The views expressed by the governing bodies or management of the Companies with respect to the Scheme;*
- The terms of any previous Scheme of transfer concerning the policyholders of the Companies; and*
- The assessment of any adverse effect of a conduct nature, such as those effects that might arise from changes to the product terms and conditions, service and administration, and the relative governance arrangements between the firms.*

*The above list is not intended to be exclusive to any other aspects which may be identified during the completion of the project and which are considered to be relevant.*

*I shall not be directly involved in the formulation of the proposed transfer although I should expect to give guidance (to both the transferor and transferee) during the evolution of the detailed proposals on those issues which concern me, or which I consider unsatisfactory.*

*The Scheme Report will be prepared in accordance with the form approved by the PRA pursuant to section 109(3) of the Act and will comply with all lawful requirements of the PRA and in particular those requirements set out in the PRA’s Statement of Policy, The Prudential Regulation Authority’s approach to insurance business transfers (the “PRA Statement of Policy”), and Chapter 18 of the Supervision Manual (“SUP 18”) contained in the FCA Handbook.*

*The Scheme Report will consider the consequences of the Scheme for those policyholders likely to be affected by the implementation of the Scheme.*

*The Scheme Report (and any supplemental Scheme Report in relation to the Scheme) will comply with relevant Technical Actuarial Standards issued by the Financial Reporting Council and/or any relevant Actuarial Profession Standards issued by the Institute and Faculty of Actuaries.*

*If the PRA lawfully requires the form and content of the Scheme Report to include matters not set out in [this Appendix C], such matters will be deemed to be included in [this Appendix C] for the purposes of this Agreement. In preparing the Scheme Report, the Independent Expert will give due consideration to all material facts and take proper care to ensure that the Scheme Report will, in its final form, accurately represent his opinion, honestly held, on the matters set out in [this Appendix C] and be limited to the matters of opinion which fall within his area of expertise.*

## Appendix D General considerations of the Independent Expert in relation to the Scheme

### INTRODUCTION

- D.1 I have compiled my Report in accordance with the Policy Statement and with SUP18.
- D.2 Under FSMA, the concept of TCF must be applied. To help ensure that customers are treated fairly in the future it is necessary to understand how they have been treated in the past. From the policyholders' perspective, the acceptability of the Scheme must be on the basis that it will not have a materially adverse effect on their benefits or fair treatment.
- D.3 In order to fulfil my obligations as Independent Expert I have considered the terms of the Scheme generally and how the different groups of policyholders are likely to be affected by the Scheme. In particular, I have considered:
- The likely effects of the Scheme on the security of the policyholders' benefits, including the likelihood and potential effects of the insolvency of the insurer; and
  - The likely effects of the Scheme on policyholder servicing levels (e.g. claims handling).

### MATERIALITY

- D.4 After considering the effects of the Scheme on each of the different groups of policyholders affected by the Scheme (as identified in paragraph 5.13, above), I have drawn conclusions as to whether I believe the Scheme will materially adversely affect that group of policyholders. It should be recognised that the Scheme will affect different policyholders in different ways, and, for any one group of policyholders, there may be some effects of the Scheme that are positive, and others that are adverse. If some effects of the Scheme are adverse, that does not necessarily mean that the Scheme is unreasonable or unfair, as those adverse effects may be insignificant or they may be outweighed by positive effects.
- D.5 In order to determine whether any effects of the Scheme on any group of policyholders are *materially* adverse it has been necessary for me to exercise my professional judgement in the light of the information that I have reviewed.
- D.6 When assessing the financial security of policyholders, I have looked at the solvency position of the companies involved in the Scheme, on both pre- and post-transfer bases, relative to regulatory solvency requirements, and also at the nature of the assets that constitute each company's capital and surplus. It should be noted that a company may have capital considerably in excess of its regulatory requirements, but that the directors of a company could legitimately reduce that level of capital (for example through the payment of dividends) and still leave the company appropriately capitalised. In circumstances where the Scheme has adversely affected the financial security of a group of policyholders, in order to determine whether that impact is material, I have considered whether the level of financial security projected to be in place after the transfer would have been acceptable and permissible before the transfer had taken place. I would determine that any adverse impact to a particular group of policyholders is material if the level of financial security afforded to them after the transfer would not have been acceptable under the normal constraints under which the company's capital position was managed before the transfer.

### SECURITY OF POLICYHOLDER BENEFITS

- D.7 As noted above, I need to consider the security of policyholder benefits, i.e. the likelihood that policyholders will receive their benefits when due.
- D.8 In considering and commenting upon policyholder security I shall consider the financial strength of each entity. Financial strength is provided by the margins for prudence in the assumptions used to calculate the technical provisions, by the shareholder capital and by any specific arrangements for the provision of financial support. In considering policyholder security it is also necessary to take into account the potential variability of future experience (including claim frequency and severity). Security is also affected by the nature and volume of future new business.

- D.9 The main factors that determine the risks to which a policyholder is exposed are:
- Size of company;
  - Amount of capital held, other calls on that capital and capital support currently available to the company;
  - Reserve strength;
  - Mix of business written; and
  - Company strategy – for example, whether it is open or closed to new business.
- D.10 I also need to consider the impact on policyholders' security in the event of the default of an insurer (e.g. the role of the FSCS).

#### **TREATING CUSTOMERS FAIRLY**

- D.11 As Independent Expert I also need to consider the impact of the Scheme on levels of service provided to policyholders, including those resulting from changes in administration, claims handling and expense levels.
- D.12 Further, I have considered the proposals in the context of applicable conduct rules/regulation, e.g. the fair resolution of complaints between an insurer and its customers (policyholders).

#### **OTHER CONSIDERATIONS**

- D.13 Paragraph 2.34(4)(b) of the Policy Statement and paragraph 2.36 of SUP18 both require me, as Independent Expert, to consider the likely effects of the Scheme on matters such as investment management, new business, administration, expense levels and valuation bases insofar as they might impact on levels of service to policyholders or on the security of policyholders' benefits.
- D.14 I am also required to consider the cost of the Scheme and the tax effects of the Scheme insofar as they might impact on the security of policyholders' benefits.

## Appendix E Compliance with the PRA Policy Statement

The table below indicates how I have complied with the provisions of the PRA Policy Statement (“*The Prudential Regulation Authority’s approach to insurance business transfers*”, dated April 2015) that pertain to the form of the Report. I have not included references to paragraphs in the Executive Summary of this Report; there should be nothing in the Executive Summary that has not been stated or explained in other parts of the Report.

I note that, in preparing this Report, I have also been mindful of the contents of SUP18 and FG18/4.

PRA Policy Statement Reference	Requirement	Scheme Report paragraph reference
2.30 (1)	Who appointed the Independent Expert and who is bearing the costs of that appointment	1.16, 1.23, 8.82-8.84
2.30 (2)	Confirmation that the independent expert has been approved or nominated by the appropriate regulator	1.3, 1.16
2.30 (3)	A statement of the independent expert’s professional qualifications and (where appropriate) descriptions of the experience that fits him for the role	1.17, Appendix B
2.30 (4)	Whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties that might be thought to influence his independence, and details of any such interest	1.18-1.21
2.30 (5)	The scope of the report	1.24-1.39
2.30 (6)	The purpose of the Scheme(s)	5.11-5.12
2.30 (7)	A summary of the terms of the scheme in so far as they are relevant to the report	5.1-5.10
2.30 (8)	What documents, reports and other material information the independent expert has considered in preparing his report and whether any information that he requested has not been provided	Appendix F
2.30 (9)	The extent to which the independent expert has relied on: (a) information provided by others; and (b) the judgement of others	1.42, 9.2
2.30 (10)	The people on whom the independent expert has relied and why, in his opinion, such reliance is reasonable	1.42, 1.55-1.62
2.30 (11)	His opinion of the likely effects of the scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee	Section 6 Section 7 Not applicable
2.30 (12)	His opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme	8.21-8.26
2.30 (13)	What matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in his opinion, be relevant to policyholders’ consideration of the scheme	As stated in 1.30, there are none of which I am aware

2.30 (14)	For each opinion that the independent expert expresses in the report, an outline of his reasons	6.22, 6.35, 6.48, 6.61, 6.84, 6.98, 6.105, 6.109, 6.113, 6.115, 6.117, 6.119, 6.123, 6.134, 6.139, 7.9, 7.12, 7.13, 7.19, 8.19, 8.26, Section 9
2.32 (1)	The summary of the terms of the scheme should include a description of any reinsurance agreements that it is proposed should pass to the transferee under the scheme	5.1-5.10
2.32 (2)	The summary of the terms of the scheme should include a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred	Not applicable
2.33 (1)	The independent expert's opinion of the likely effects of the scheme on policyholders should include a comparison of the likely effects if it is or is not implemented	8.73-8.74
2.33 (2)	The independent expert's opinion of the likely effects of the scheme on policyholders should state whether he considered alternative arrangements and, if so, what	1.25
2.33 (3)	The independent expert's opinion of the likely effects of the scheme on policyholders should, where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences he considers may be material to the policyholders	5.13, Section 6, Section 7
2.33 (4)	The independent expert's opinion of the likely effects of the scheme on policyholders should include his views on: (a) the effect of the scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer; (b) the likely effects of the scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect: (i) the security of policyholders' contractual rights; (ii) levels of service provided to policyholders; or (iii) for long-term insurance business, the reasonable expectations of policyholders; and (c) the cost and tax effects of the scheme, in so far as they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations	6.109, 6.123, 6.139, 7.9, 7.19, 8.12, 9.1  6.110, 6.117, 6.119, 6.134, 6.139, 7.12, 9.1  1.23, 8.82-8.84
2.35 (1)	For any mutual company involved in the scheme, the report should describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes that could affect their entitlements as policyholders	Not applicable
2.35 (2)	For any mutual company involved in the scheme, the report should state whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights	Not applicable

2.35 (3)	For any mutual company involved in the scheme, the report should comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without	Not applicable
2.36 (1)	For a scheme involving long-term insurance business, the report should describe the effect of the scheme on the nature and value of any rights of policyholders to participate in profits	Not applicable
2.36 (2)	For a scheme involving long-term insurance business, the report should, if any such rights will be diluted by the scheme, how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders	Not applicable
2.36 (3)	For a scheme involving long-term insurance business, the report should describe the likely effect of the scheme on the approach used to determine: (a) the amounts of any non-guaranteed benefits such as bonuses and surrender values; and (b) the levels of any discretionary charges	Not applicable
2.36 (4)	For a scheme involving long-term insurance business, the report should describe what safeguards are provided by the scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm	Not applicable
2.36 (5)	For a scheme involving long-term insurance business, the report should include the independent expert's overall assessment of the likely effects of the scheme on the reasonable expectations of long-term insurance business policyholders	Not applicable
2.36 (6)	For a scheme involving long-term insurance business, the report should state whether the independent expert is satisfied that for each firm the scheme is equitable to all classes and generations of its policyholders	Not applicable
2.36 (7)	For a scheme involving long-term insurance business, the report should state whether, in the independent expert's opinion, for each relevant firm the scheme has sufficient safeguards (such as principles of financial management or certification by a with-profits actuary or actuarial function holder) to ensure that the scheme operates as presented	Not applicable

## Appendix F Key sources of relevant information

F.1 In writing this Report, I relied upon the accuracy of certain documents provided by AGIL, LGI and AEI. These included, but were not limited to, the following:

### Background

- Financial Statements for AGIL as at 31 December 2019
- Financial Statements for LGI as at 31 December 2019

### Scheme and Restructuring

- Scheme Document
- First Witness Statement by Claude Kwasi Sarfo-Agyare.
- First Witness Statement by Ingo Martijn Alexander Soesman.

### Reserving

- Assurant Europe Q4 reserving report, dated December 2019
- Assurant Europe Reserving Policy, v.1.0, dated January 2020
- Assurant Europe Q3 Reserving Sensitivities v.0.5, dated January 2020
- AGIL and LGI technical provisions as at 31 December 2019
- Stochastic Reserving Analysis Report v.0.5, dated November 2019

### Risks and Solvency Capital

- Assurant Europe ORSA updated for April 2019 business plan
- Assurant Group Limited 2019 ORSA Supervisory Report, dated May 2019
- TWG Europe Limited 2019 ORSA Supervisory Report, dated May 2019
- Assurant Group Limited SFCR as at 31 December 2018, dated May 2019
- TWG Europe Limited SFCR as at 31 December 2018, dated May 2019
- Assurant Group Limited Risk Management Framework v.4.0, dated March 2018
- Assurant Group Limited Risk Appetite Statement v4.0, dated March 2018
- Assurant Group Limited Capital management Policy v.2.0, dated January 2016
- Assurant Europe Risk Policy v.0.1 – draft
- Assurant Europe Group Operational Risk Policy v.1.0, dated October 2019
- Assurant Europe Capital Management Policy, v.1.1 – draft
- TWG Europe Risk Policy v.5.1, dated February 2017
- TWG Europe Capital Management Policy v.6.3
- Report to Assurant European Audit, Risk & Compliance Committee, Actuarial Reporting, dated April 2020
- Actuarial Function Report 2019
- Actuarial Function Component Report, Technical Provisions and SCR Results as at 31 December 2019
- Actuarial Function Component Report, Solvency II Assumptions as at 31 December 2019
- Assurant General Insurance Ltd SFCR (English language) Public QRTS as at 31 December 2019, dated 26 March 2020
- London General Insurance Company Limited Public QRT (English language) as at 31 December 2019, dated 26 March\_2020

- Q4 2019 GAAP and Solvency II balance sheets as well as pro forma balance sheets post transfer provided by the Actuarial team at Assurant, dated 13 April 2020
- Pro forma MCR post transfer for each of AGIL, LGI and AEI as at 31 December, dated 15 April 2020

#### **Reinsurance and Guarantees**

- Assurant Europe Reinsurance Policy, v.1.0, dated October 2019

#### **Governance**

- Corporate Outsourcing Policy and related framework, dated September 2019
- Assurant Europe Group Governance Framework Diagram

#### **Other**

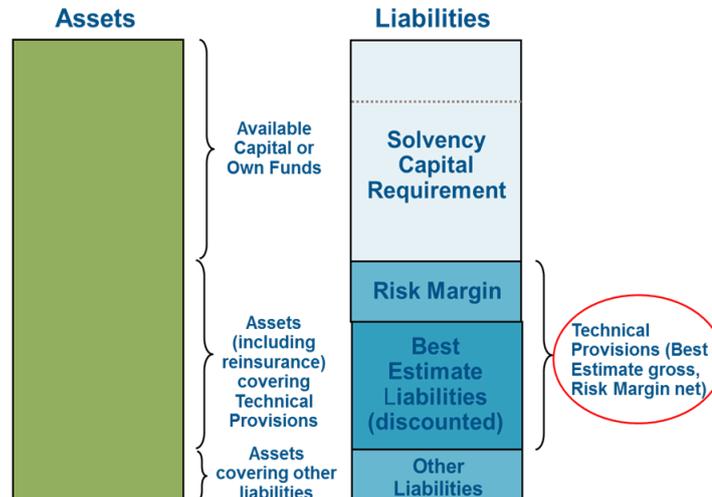
- Assurant Europe Group – COVID 19 Response Board Update Memo, dated 27 March 2020
- AGIL and LGI Part VII Transfer Communications Strategy, dated 3 April 2020

F.2 Information relating to the items listed above was also gathered during discussions with Assurant Group staff members.

## Appendix G Solvency II balance sheet

G.1 A simplified illustration of a Solvency II balance sheet is shown in Figure G.1, below.

FIGURE G.1 SOLVENCY II BALANCE SHEET

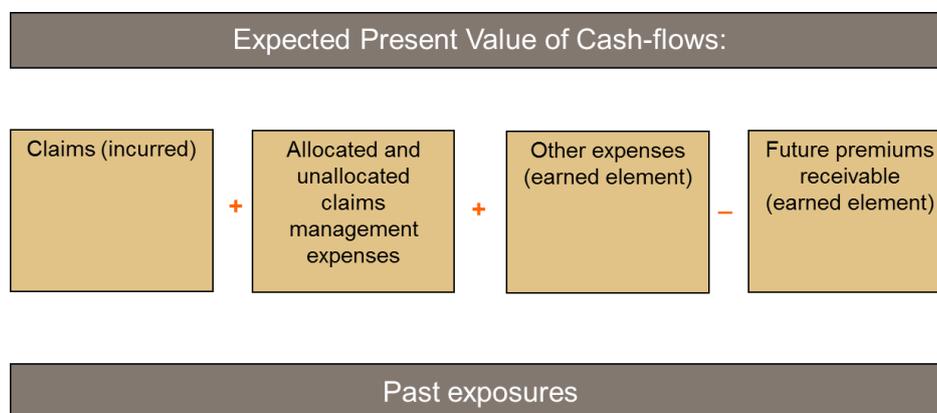


- G.2 The Solvency II balance sheet is intended to be a tool for management to assess an entity's solvency and hence an important consideration for significant decisions. It is also a tool for regulators to assess the solvency of an insurer.
- G.3 A key consideration for management in making significant decisions will be the excess of assets over TPs, other liabilities and the Solvency Capital Requirement (SCR). This excess of Own Funds over the SCR will determine whether the entity can expand existing business, move in to new areas, undertake mergers/acquisitions (with less capital rich entities) etc. or whether they need to consider reducing business volumes, moving out of capital intensive lines of business, purchasing additional reinsurance and so on. The level of Own Funds will also likely impact the credit rating of an entity.
- G.4 The TPs are a direct input to the balance sheet, and are therefore a fundamental input in to the SCR calculation that models the potential movement in the balance sheet over a one-year time horizon.
- G.5 Solvency II requires the TPs (as at the valuation date) to be determined using a market consistent valuation of the liabilities relating to insurance contracts. In practice, a market consistent liability valuation cannot be calculated by reference to market prices, because such prices are not (for practical purposes) available. Therefore TPs are presently estimated on a proxy to a market value basis, i.e. a 'best estimate' of the liabilities relating to insurance contracts allowing (i.e. discounting) for the time value of money supplemented by a risk margin. More specifically the TPs are made up as follows:

Claims provision + Premium provision + Risk margin

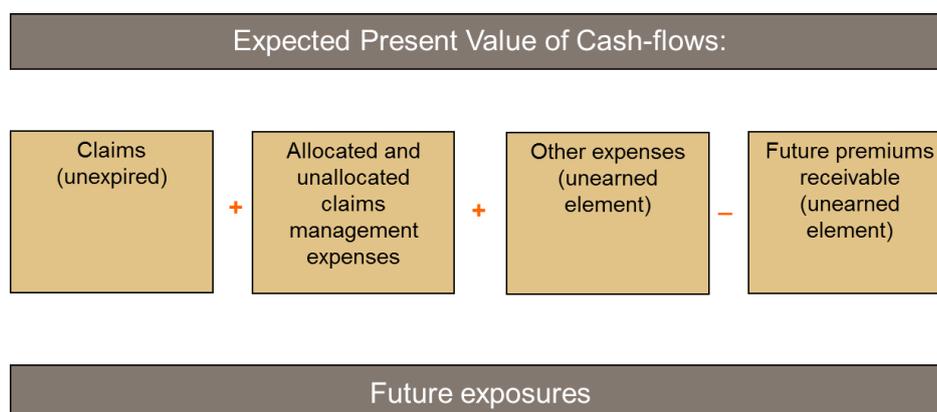
G.6 The claims provision is the expected present value/discouted 'best estimate' of all future cash-flows (claim payments, expenses and future premiums due) relating to claim events prior to the valuation date. G.2, below, illustrates the components of the claims provision calculation.

FIGURE G.2 CLAIMS PROVISION



G.7 The premium provision is the expected present value/discouted 'best estimate' of all future cash-flows (claim payments, expenses and future premiums due) relating to future exposures arising from policies that the insurer is obligated to at the valuation date. Figure G.3, below, illustrates the components of the premium provision calculation.

FIGURE G.3 PREMIUM PROVISION



G.8 The risk margin ("RM") is intended to be the balance that another (re)insurer taking on the liabilities at the valuation date would require over and above the discounted 'best estimate'. Under Solvency II, the RM is calculated using a cost-of-capital ("CoC") approach (presently employing a 6% CoC parameter as provided by EIOPA). More specifically, the calculation is as follows:

$$RM = CoC \times \sum_{t \geq 0} \frac{SCR(t)}{(1 + r_{t+1})^{t+1}}$$

where:

- SCR(t) as employed for the RM formula consists of underwriting risk (with respect to existing business); counterparty risk (e.g. reinsurance); operational risk; and market risk (if unavoidable, i.e. not hedgeable); and
- $r_t$  is the risk-free discount rate(s) at time  $t$ , as provided by EIOPA for all major currencies.

## Appendix H Key differences between IFRS and Solvency II Technical Provisions

H.1 A summary of the key differences between IFRS reserves and Solvency II TPs is set out in the table below:

Area of change	UK GAAP Reserves	Solvency II Technical Provisions	Balance sheet impact
<b>Earned business</b>	Claims reserve = point estimate within a reasonable range (“not insufficient”)	Claims provision = probability weighted average of future cash-flows	Reduces liabilities (removes margins)
<b>Unearned business</b>	Unearned premium reserve, net of Deferred Acquisition Costs	Premium provision = probability weighted average of future cash-flows	Reduces liability (expected profit)
<b>Risk Margin</b>	n/a	Explicit item, based on cost of capital approach	Increases liabilities
<b>Discounting</b>	Undiscounted	Discounted cash-flows	Reduces liabilities
<b>Contract recognition</b>	Policies written	Policies written and legally bound Unaccepted policies (“BBNI” policies’)	Reduces liabilities (due to expected profit on BBNI policies)
<b>Expenses</b>	Claims handling expense reserve	More explicit treatment of expenses	Increases liabilities
<b>Events Not In Data (“ENIDs”)</b>	Limited allowance for contingent liabilities	New concept allowance for extreme outcomes (which are “not in the data” used for reserving)	Increase liabilities
<b>Reinsurance Bad Debt Provision</b>	n/a	Explicit provision required for reinsurer bad debt	Increases liabilities