

**Supplementary Report of the Independent Expert on  
the proposed Scheme to transfer a block of the  
European International Life Insurance Business of  
Scottish Widows Limited to Scottish Widows Europe  
SA**

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# 1 Executive summary

## Background

- 1.1 Scottish Widows Limited (SWL) is a private limited company incorporated in England and Wales and domiciled in the UK. It is a life insurance subsidiary of Scottish Widows Group (SWG), which is a subsidiary of Lloyds Banking Group plc (LBG or Group), the ultimate parent company. Under European Union (EU) regulations, UK insurance companies can sell policies and service business written in the European Economic Area (EEA) countries on a Freedom of Services or a Freedom of Establishment basis (commonly referred to as “EU passporting rights”). SWL has previously written life insurance and pensions business, primarily in Germany, Austria and Italy under EU passporting rights.
- 1.2 On 23 June 2016, the UK voted to leave the EU and on 29 March 2017, the UK government officially notified the European Commission of its intention to withdraw from the EU (Brexit). Brexit is expected to take effect on 29 March 2019. It is uncertain whether UK insurance companies will continue to be able to sell policies and service business (including the collection of premiums and payment of claims) written in EEA countries outside of the UK, under EU passporting rights, after 29 March 2019. Therefore, unless suitable transitional or grandfathering arrangements between the UK and the EU are agreed prior to 29 March 2019, it is expected that it will become illegal for SWL to continue to service the policies written under EU passporting rights.
- 1.3 SWL has established a new wholly-owned subsidiary in Luxembourg, Scottish Widows Europe SA (SWE), which was authorised by the Luxembourg Insurance Supervisory Authority, Commissariat aux Assurances (CAA) and Ministry of Finance as a life insurance company on 1 February 2019. Following authorisation, the CAA gave notice to the regulators of the EEA countries in which, SWE will service insurance policies under EU passporting rights. SWE has received approval from the CAA for setting up branch offices in Germany and Italy; it has also received a response from the German regulator BaFin acknowledging the set-up of the branch office in Germany. SWE is expecting to receive a response or no objection from the Italian regulator for setting up a branch office in Italy in early March 2019.
- 1.4 SWL intends to transfer the policies written under EU passporting rights to SWE so that it can be certain that it will be able to service this business following Brexit. This transfer will be carried out using a legal process known as a Part VII transfer of insurance business (under the Financial Services and Market Act 2000 as amended) (FSMA). The terms of the transfer are set out in a document known as the Scheme. The Scheme provides certainty that SWL will be able to lawfully service the business written under EU passporting rights post-Brexit. The Part VII transfer of these policies from SWL to SWE (Transferring Policies), together with the associated reinsurance agreement, charge agreement, unit linked servicing agreement and the indemnity agreement that sit alongside the Scheme, are referred to as the Transfer.
- 1.5 I have classified the Transferring Business into two main groups unitised with-profits business (Transferring UWP Business) and unit-linked business (Transferring UL Business).
- 1.6 Immediately following the transfer, the Transferring UWP Business will be reinsured back to SWL through a reinsurance agreement (the Reinsurance Agreement), which will also create the associated collateral arrangements known as the funds withheld (FWH). To provide further security for the Transferring Business, SWL will enter into a floating charge agreement (the Charge Agreement) with SWE. The Transferring UL Business will remain with SWE, but to ensure that the operations of the Transferring UL Business remain unchanged, SWE will enter into a service agreement with Lloyds Bank Plc (LB) to enable them to provide support for the back office management tasks related to the Transferring UL Business (Unit Linked Service Agreement), as happens at present for SWL. SWE will also enter into a service agreement with Lloyds Bank GmbH (LB Europe) relating to HR and payroll services.

- 1.7 Additionally, to provide protection for SWE against any litigation claims resulting from SWL's actions prior to the transfer of business to SWE, SWL will enter into an indemnity agreement (the Indemnity Agreement) with SWE. The Charge Agreement will also cover the obligations of SWL under the Indemnity Agreement.
- 1.8 I prepared a previous report dated 14 November 2018 (the Report) in my capacity as Independent Expert in which I considered the impact of the proposed Scheme on policyholders and other affected parties.
- 1.9 The purpose of this report (the Supplementary Report) is to provide the Court with an updated assessment of the likely effect of the proposed Transfer and to consider whether or not the conclusions reached in my Report remain unchanged after taking into account any financial and non-financial developments since the publication of the Report and of any objections received in relation to the proposed Transfer.
- 1.10 This Supplementary Report should be read in conjunction with the Report. For the avoidance of doubt, capitalised terms used in this Supplementary Report shall have the same meaning as in the Report.
- 1.11 Details of the scope of my appointment, my qualifications, limitations and reliances are contained in the Report. The additional information that I have relied on in preparing this Supplementary Report is set out in Appendix A.

## Update on Brexit negotiations

- 1.12 There have been no developments within the public domain regarding the Brexit negotiations that provide any certainty over whether or not SWL will be allowed to continue to service business written under EU passporting rights after 29 March 2019. I understand that Germany, Italy and Austria have issued draft legislations which allow the UK insurers and reinsurers a transitional period until December 2020 to continue to service the business sold in these countries under EU passporting rights in case of hard Brexit (ie an exit with no deal), however there is no certainty beyond this point.
- 1.13 I considered these draft transitional arrangements and discussed them with SWL. SWL remains of the view that the Scheme is necessary as the proposals by Germany, Italy and Austria are only for a transitional period, they are currently not finalised, and they are not at an EU level (ie as a result the implementation would not be consistent across the EU).
- 1.14 I am satisfied that it is reasonable for SWL to proceed with the Scheme given that these draft arrangements are for a transitional period only with no certainty beyond December 2020, that they are not finalised and that the Scheme continues to provide SWL with certainty that the Transferring Business can continue to be lawfully serviced post-Brexit.

## Update on FSCS protection

- 1.15 In the Report, I pointed out that the holders of the Transferring Policies who currently have FSCS protection are expected to lose FSCS protection in respect of acts or omissions arising after the Effective Date as a result of the Transfer. I have discussed issues related to FSCS protection with SWL and its legal advisers and reviewed a note prepared by SWL's legal advisers on the impact of the Transfer on FSCS protection including the implications of the CP 26/18 published by the PRA.
- 1.16 I understand that claims related to acts or omissions by SWL that occur prior to the Effective Date will be covered by FSCS. The acts or omissions under a contract of insurance would cover protection in respect of insurance claims that have arisen under the policy terms and conditions before the Effective Date. However, as SWE will not be a 'relevant person' (as defined under FSMA), I understand that any acts or omissions by SWE occurring after the Effective Date will not be covered by FSCS.
- 1.17 I have discussed with SWL whether FSCS protection for those Transferring Policyholders, who will lose this protection as a result of the Transfer, could be maintained, if SWE were to either obtain passporting

rights to service business within the UK or set up a third country branch in the UK. I agree with SWL that transferring the Transferring Policies to SWE is required to ensure that SWL is allowed to continue to service business written under EU passporting rights after Brexit, and that these other options either do not provide the certainty required or are not necessary for SWE to carry out its day-to-day activities as explained in paragraphs 3.18 and 3.19.

- 1.18 Furthermore, the FSCS only provides protection to covered policyholders following an insolvency or default event. Given that SWE is well capitalised, is required to comply with Solvency II regulations and SWE's Capital Management Framework requires it to hold a capital buffer in excess of that required by Solvency II, the likelihood of default or insolvency of SWE, is in my opinion, remote and the conclusions stated in the Report regarding the loss of the FSCS protection are unchanged.

#### Change to business covered by FSCS

- 1.19 In the Report, I stated that all of the Transferring Business is currently covered by FSCS protection. Since the Report SWL has performed further analysis and identified an estimated 228 policies that are currently not covered by FSCS and this will continue to be the case after the Transfer.
- 1.20 I confirm that the conclusions detailed in my Report for these policies related to the policyholder benefit expectations, security of benefits or governance under the Transfer remain unchanged since the only update for these policies is the change in current status in relation to FSCS.

#### Updated financial information

- 1.21 I have reviewed the financial information for SWL and pro forma financials for SWE as at 30 June 2018, which is the most recent date that this information is available. In Section 3, I provide my opinions on how this updated financial information impacts the conclusions detailed in my Report. In particular, I have reviewed the updated SCR Cover Ratio figures calculated assuming the Transfer had taken place on 30 June 2018.
- 1.22 I have also seen estimated financials up to 31 December 2018 for SWL and SWE and reviewed the estimated changes in the financial position since 31 December 2018. I am satisfied that the conclusions in my Report still hold as the solvency position for SWL is within the Green zone<sup>1</sup> based on its risk appetite as defined within its Capital Management Plan (CMP) and for SWE it is at or above its capital policy.

#### Updated key dependencies

- 1.23 The analysis contained in the Report was prepared on the basis that a number of actions would take place in advance of the Effective Date. These key dependencies were:
- SWE receiving authorisation from the CAA (and in addition, receiving approval from the CAA to service insurance policies in the relevant EEA countries outside of the UK under EU passporting rights and receiving approval from the CAA (and a response or no objection from the local regulators) for setting up branch offices in Germany and Italy)
  - SWE receiving an initial capital injection from SWL that is expected to be sufficient to capitalise SWE at its target level

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<sup>1</sup> Capital levels above the target SCR Cover Ratio as defined within the Capital Management Plan, (ie enough capital to cover the regulatory capital requirements as well as the firm's internal capital requirement) is considered to be within the Green zone.

- SWE and SWL entering into the Associated Arrangements, namely the Reinsurance Agreement, Charge Agreement, Unit Linked Service Agreement and Indemnity Agreement, to be effective immediately following the Effective Date.
- 1.24 Paragraphs 3.35 to 3.38 provide an update on these key dependencies. All of the key dependencies have either been completed or are on track to be completed in advance of the Effective Date.

## Updated non-financial information

- 1.25 Within Section 3 I also provide updates on:
- UK COBS protection
  - the overall purpose, structure and scope of the Scheme and the Associated Arrangements including the update on the transfer of FWH to SWE
  - the composition of the SWE Board
  - SWE set-up, operations including the branch offices, governance
  - requirement of a UK Branch for SWE
  - the Tied Assets arrangements as required by the Luxembourg regulations
  - policyholder taxation
  - tax clearances and tax due to Transfer pricing adjustment
  - risk mitigation plans
  - Italian surrender rights.
- 1.26 I have reviewed each of the developments and I am satisfied that these do not change the conclusions in my Report.
- 1.27 I also confirm that the change in the Effective Date for the Scheme from 28 March 2019 to 29 March 2019 does not change my conclusions with regards to the Transfer as the amendment was made for practical reasons relating to the implementation of the Transfer; it does not impact the operation of the Scheme and it has no impact on the benefits or contractual rights of Transferring Policyholders or Non-transferring Policyholders. I am also satisfied that the plan to provide an undertaking to the Court to enable the Transferring UWP Policyholders and the Non-transferring Policyholders in the CM WPF the right to enforce the conditions in relation to the termination of the Reinsurance Agreement provides additional protection to these policyholders and is consistent with the approach taken on other similar Schemes.

## Updated impact on policyholders and reinsurers

- 1.28 In Section 4, I confirm that there have been no changes to any of my opinions set out in the Report. Overall, it remains my opinion that the implementation of the proposed Scheme and the Associated Arrangements at the Effective Date will not have a material adverse effect on the security of benefits or the future benefit expectations of the Transferring Policyholders and Non-transferring Policyholders of SWL. It is also my opinion that the Transfer will have no material adverse impact on the governance or service standards experienced by the Transferring Policyholders and Non-transferring Policyholders of SWL.
- 1.29 Further, I remain satisfied that there is no material adverse effect on Transferring Policyholders caused by the loss of FSCS protection as a result of the Transfer.
- 1.30 It remains my opinion that the Transfer will have no material adverse impact on the current external reinsurer of SWL whose contracts of reinsurance cover the Transferring Policyholders.

## Policyholder communications and objections received

1.31 In Section 5, I provide an update on the policyholder communication process and respond to the objections raised. The objections can be summarised into the following categories:

- loss of FSCS protection and concerns over security of benefits
- withholding tax for policyholders in Germany
- concerns related to the Transfer
- clarity in my Report
- request for surrender value and compensation
- other
- no reason provided.

1.32 Overall, I am satisfied that the communication process, for informing Transferring Policyholders and Non-transferring Policyholders of the Transfer, has met the requirements of the Directions Order and the policyholders have been given sufficient details and notice of the proposed Scheme. Further, I am satisfied that, at the time of writing this Supplementary Report, SWL is recording the objections received from policyholders appropriately, and that policyholders have not raised any issues that were not considered in the work leading up to the Report except those related to tax exempt status in Germany. As I explain in Sections 3 and 4 the Transfer will not affect the tax exempt status of the policyholders. Given that no other new issues were raised, I am satisfied that there are no reasons to change the conclusions in my Report.

## Revised certification of changes to the 2015 Scheme

1.33 I describe in paragraph 3.47 how it was necessary to make changes to the wording of my certification of the changes to the 2015 Scheme. An amended certification is provided in Appendix B.

## Conclusions

1.34 I confirm that, overall, I am satisfied that Transfer will not have a material adverse effect on the security of benefits or future benefit expectations of the Transferring Policyholders and the Non-transferring Policyholders. It is also my opinion that the Transfer will have no material adverse effect on the governance or service standards experienced by the Transferring Policyholders and the Non-transferring Policyholders. In addition, I am satisfied that the Transfer will not materially adversely affect the reinsurer of the Transferring Business.

1.35 Given my conclusions outlined above, I see no reason why the Transfer should not proceed.

## 2 Introduction

### Background to the Scheme

- 2.1 Scottish Widows Limited (SWL) is a private limited company incorporated in England and Wales and domiciled in the UK. It is a life insurance subsidiary of Scottish Widows Group (SWG), which is a subsidiary of Lloyds Banking Group plc (LBG or Group), the ultimate parent company. SWL was formed when all of the UK life insurance business written by SWG's insurance subsidiaries was transferred into one company on 31 December 2015. The principal activity of SWL is the transaction of long-term insurance business. SWL has unit-linked, non-profit and with-profits business and primarily writes pensions, bonds and protection business.
- 2.2 Under European Union (EU) regulations, United Kingdom (UK) insurance companies can sell policies and service business including the collection of premiums and payment of claims, written in the European Economic Area ("EEA") countries on a Freedom of Services or a Freedom of Establishment basis (commonly referred to as "EU passporting rights"). Scottish Widows Limited (SWL or Transferor) has previously written life insurance and pensions business, primarily in Germany, Austria and Italy, under EU passporting rights.
- 2.3 On 23 June 2016, the UK voted to leave the EU and on 29 March 2017, the UK officially notified the European Commission of its intention to withdraw from the EU (Brexit). Brexit is expected to take effect on 29 March 2019. It is uncertain whether UK insurance companies will continue to be able to sell policies and service business written in EEA countries outside of the UK, under EU passporting rights, after 29 March 2019. Therefore, unless suitable transitional or grandfathering arrangements between the UK and the EU are agreed prior to 29 March 2019, it is expected that it will become illegal for SWL to continue to service the policies written under EU passporting rights.
- 2.4 SWL established a new wholly-owned subsidiary in Luxembourg, Scottish Widows Europe SA (SWE). The Luxembourg Insurance Supervisory Authority, Commissariat aux Assurances (CAA) provided authorisation for SWE's licence application on 22 January 2019; SWE's authorisation as a life assurance company was then approved by the Luxembourg Ministry of Finance on 1 February 2019. SWL will transfer its existing business that was originally written in EU countries outside of UK (Transferring Business) to this subsidiary on the Effective Date. Following authorisation, the CAA gave notice to the regulators of the EEA countries in which, SWE will service insurance policies under EU passporting rights. SWE has received approval from the CAA for setting up branch offices in Germany and Italy; it has also received a response from the German regulator BaFin acknowledging the set-up of the branch office in Germany. SWE is expecting to receive a response or no objection from the Italian regulator for setting up a branch office in Italy in early March 2019.
- 2.5 The proposed transfer of these policies will be carried out using a legal process known as a Part VII transfer under the Financial Services and Market Act 2000 (as amended) (FSMA). The terms of the proposed transfer are set out in a document known as the Scheme. The Scheme provides certainty that SWL will be able to lawfully service the business written under EU passporting rights post-Brexit. The Part VII transfer of these policies from SWL to SWE (Transferring Policies), together with the associated reinsurance agreement, charge agreement, unit linked servicing agreement and the indemnity agreement that sit alongside the Scheme, are referred to as the Transfer.
- 2.6 I have classified the Transferring Business into two main groups:
- Transferring unitised with-profits business (Transferring UWP Business) including vested annuities – business currently invested in Guaranteed Growth Funds (GGFs) which reside in SWL's Clerical Medical (CM) with-profits fund (WPF) (CM WPF), written primarily in Germany, Austria and Italy under EU passporting rights.

- Transferring unit-linked business (Transferring UL Business) – business currently invested in unit-linked (UL) funds that reside in SWL Combined Fund, written primarily in Germany, Austria and Italy under EU passporting rights. These unit-linked funds are exclusive for policies of the Transferring UL Business (Transferring UL Policies).
- 2.7 Immediately following the Transfer, the Transferring UWP Business will be reinsured back to SWL through a reinsurance agreement (the Reinsurance Agreement), which will also create the associated collateral arrangements known as the funds withheld (FWH). To provide further security for the Transferring Business, SWL will enter into a floating charge agreement (the Charge Agreement) with SWE. The Transferring UL Business will remain with SWE, but to ensure that the operations of the Transferring UL Business remain unchanged, SWE will enter into a service agreement with Lloyds Bank Plc (LB) to enable them to provide support for the back office management tasks related to the Transferring UL Business (Unit Linked Service Agreement), as happens at present for SWL. SWE will also enter into a service agreement with Lloyds Bank GmbH (LB Europe) relating to HR and payroll services.
- 2.8 Additionally, to provide protection for SWE against any litigation claims resulting from SWL's actions prior to the transfer of business to SWE, SWL will enter into an indemnity agreement (the Indemnity Agreement) with SWE. The Charge Agreement will also cover the obligations of SWL under the Indemnity Agreement.

## Purpose of the Supplementary Report

- 2.9 I prepared a previous report dated 14 November 2018 (the Report) in my capacity as Independent Expert in which I considered the impact on policyholders and other affected parties of the proposed Scheme to transfer certain life insurance and pensions business written in non-UK territories from SWL to SWE.
- 2.10 The purpose of this report (the Supplementary Report) is to provide the Court with an updated assessment of the likely effect of the proposed Transfer and to consider whether or not the conclusions reached in my Report remain unchanged after taking into account the most recent financial information for both SWL and SWE that has been made available to me. I have also taken into account any other significant relevant developments since writing the Report, including any objections received in relation to the proposed Transfer.
- 2.11 This Supplementary Report should be read in conjunction with the Report. For the avoidance of doubt, capitalised terms used in this Supplementary Report shall have the same meanings as in the Report. These terms can also be found in the Glossary in Appendix C.
- 2.12 The Supplementary Report will be available to the Court and published on websites [www.scottishwidows.co.uk](http://www.scottishwidows.co.uk), [www.clericalmedical.com/de/index.asp](http://www.clericalmedical.com/de/index.asp), [www.clericalmedical.com/austria/index.asp](http://www.clericalmedical.com/austria/index.asp) and [www.clericalmedical.com/it/index.asp](http://www.clericalmedical.com/it/index.asp) prior to the Court hearing to sanction the Scheme which is scheduled for 14 March 2019.
- 2.13 Details of the scope of my appointment, my qualifications, limitations and reliances are contained in the Report. The additional information that I have relied on in preparing this Supplementary Report is set out in Appendix A.
- 2.14 My independence has remained unchanged since the preparation of the Report.

## Regulatory and professional guidance

- 2.15 The Supplementary Report has been prepared in accordance with guidance contained in SUP 18 and the Statement of Policy: The PRA's approach to insurance business transfers. I have also paid regard to the FCA's guidance FG18/4: The FCA's approach to the review of Part VII insurance business transfers.

- 2.16 The FRC has issued standards which apply to certain types of actuarial work. I have prepared this Supplementary Report, with the intention that it, and the work underlying it, should meet the requirements of Technical Actuarial Standards TAS 100 (Principles for Technical Actuarial Work) and TAS 200 (Insurance). I believe that this Supplementary Report and my work underlying it does so in all material respects.
- 2.17 I confirm that I have also complied with the Actuarial Practice Standard X2: Review of actuarial work and considered APS L1: Duties and Responsibilities of Life Assurance Actuaries, issued by the Institute and Faculty of Actuaries.

### Duty to the Court

- 2.18 I confirm that I am aware of the requirements of Part 35 of the Civil Procedure Rules and the relevant Practice Direction, and the Guidance for the Instruction of Experts in Civil Claims.
- 2.19 In reporting on the Scheme as the Independent Expert, I recognise that I owe a duty to the Court to assist on matters within my expertise. This duty overrides any obligation to SWL or SWE. I confirm that I have complied with this duty.

### Statement of truth

- 2.20 I confirm that I have made clear which facts and matters referred to in this Supplementary 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.
- 2.21 This Supplementary Report has been peer reviewed by a fellow Actuary at Grant Thornton, Derek Smith, who has over 25 years of experience in the insurance industry and specialises in reviewing insurance transactions.
- 2.22 Finally, SWL has seen my Supplementary Report and has agreed that it is factually correct in relation to the references to SWL, SWE and the Transfer.

## 3 Updated information

- 3.1 This section of the Supplementary Report updates the financial and non-financial information that was presented in the Report. I also provide an update on the latest relevant Brexit negotiations, FSCS protection and key dependencies. I provide my opinions on how this updated information impacts my conclusions about the impact of the Transfer on Transferring Policyholders, the Non-transferring Policyholders and the reinsurer of the Transferring Business in Section 4.

### Update on Brexit negotiations

- 3.2 Since my Report, there have been no developments within the public domain regarding the Brexit negotiations that provide any certainty over whether or not SWL will be allowed to continue to service business written under EU passporting rights after 29 March 2019. I understand that Germany, Italy and Austria have issued draft legislations<sup>2</sup> which allow the UK insurers and reinsurers a transitional period until December 2020 to continue to service the business already sold in these countries under EU passporting rights in case of hard Brexit (ie an exit with no deal) however there is no certainty beyond this point.
- 3.3 I considered these draft transitional arrangements and discussed them with SWL. SWL remains of the view that the Scheme is necessary as the proposals by Germany, Italy and Austria are only for a transitional period, they are currently not finalised and they are not at an EU level (ie as a result the implementation would not be consistent across the EU).
- 3.4 I am satisfied that it is reasonable for SWL to proceed with the Scheme given that these draft arrangements are for a transitional period only with no certainty beyond December 2020, that they are not finalised and that the Scheme continues to provide SWL with certainty that the Transferring Business can continue to be lawfully serviced post-Brexit.

### Update on FSCS protection

- 3.5 In the Report, I stated that all of the Transferring Business is covered by the FSCS. However, since the Report SWL has performed further analysis and identified an estimated 228 policies which they believe are currently not covered by the FSCS. These include:
- policyholders who took out policies from Clerical Medical Investment Group (CMIG, which was renamed to “SWL” as part of the 2015 Scheme) that were subject to the law of EEA countries who are believed to have been habitually resident outside the EEA at the time the policies were sold (estimated to be 165 such policies). As these policies are believed to have been issued to policyholders who were habitually resident outside the EEA at the time that they took out their policy, they are not covered by the FSCS.

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<sup>2</sup> The link to the draft legislation in Germany :

[https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze\\_Gesetzesvorhaben/Abteilungen/Abteilung\\_IV/19\\_Legislaturperiode/Gesetze\\_Verordnungen/Brexit-StBG/0-Gesetz.html](https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze_Gesetzesvorhaben/Abteilungen/Abteilung_IV/19_Legislaturperiode/Gesetze_Verordnungen/Brexit-StBG/0-Gesetz.html)

The link to the draft legislation in Italy: [http://www.mef.gov.it/ufficio-stampa/comunicati/2019/comunicato\\_0015.html](http://www.mef.gov.it/ufficio-stampa/comunicati/2019/comunicato_0015.html)

The link to the draft legislation in Austria: [https://www.parlament.gv.at/PAKT/VHG/XXVI/ME/ME\\_00113/index.shtml](https://www.parlament.gv.at/PAKT/VHG/XXVI/ME/ME_00113/index.shtml)

- policies sold by CMI Insurance (Luxembourg) S.A. (CMIL) that were transferred to SWL at 31 December 2015 by a Ministerial Decree (63 such policies now remaining in-force). As these policies were sold by a non-UK insurer they are not covered by the FSCS.
- 3.6 Given that these policyholders currently do not have FSCS protection as advised by SWL, the Transfer does not change this position.
- 3.7 At 31 December 2018, there were 80,729 Transferring Policies. I have been advised by SWL that all of these policies except those referred to in paragraph 3.5, currently benefit from the FSCS protection. In the Report, I explained that holders of these policies are expected to lose FSCS protection (although claims related to acts or omissions that occur prior to the Transfer would still be covered by FSCS).
- 3.8 In the PRA's consultation paper "CP 26/18 – UK withdrawal from the EU: Changes to the PRA Rulebook and onshored Binding Technical Standards" (dated October 2018), the PRA stated that where a UK insurer transfers its insurance liabilities to an insurer without UK authorisation, existing PRA rules provide FSCS protection only to acts or omissions that arose before the transfer to the 'successor' (as defined by the PRA Rulebook). SWE is the 'successor' in this Transfer and examples of acts and omissions are provided in paragraph 3.13. The consultation paper also proposed that if the 'successor' to which the policies are transferred is a 'relevant person' (as defined under FSMA) ie a firm authorised by the UK regulator, FSCS will continue to apply to protected claims in respect of acts or omissions which have occurred before Brexit until risks are run off as long as the insurer remains a 'relevant person'.
- 3.9 I have discussed the sections of CP26/18 relating to FSCS protection, in relation to this Transfer, with SWL and its legal advisers. SWL has taken legal advice in relation to FSCS protection and the implications of this Transfer on this protection for Transferring Policyholders, and a note was prepared by the legal advisers summarising this advice. This note has been shared with me and I have had an opportunity to discuss and explore this note with SWL's legal advisers and to establish the basis and logical flow of the legal advice. I am not an expert in legal matters and therefore, in forming my conclusions related to the loss of FSCS protection for those Transferring Policyholders who are currently protected by the FSCS, I have given consideration to my discussions with SWL's legal advisers and the legal advice prepared on this topic.
- 3.10 I do not believe it is necessary to seek independent legal advice in relation to the loss of FSCS for those Transferring Policyholders who are currently covered by this protection as:
- in forming my views on FSCS cover I have taken into consideration my interpretation of the FSCS rules, as set out in the PRA Handbook
  - as a result of my analysis, whether Transferring Policyholders will have FSCS protection in relation to acts or omissions occurring after the Effective Date is a relatively clear-cut matter and I do not expect that seeking independent legal advice would result in a different conclusion and would result in unnecessary additional costs
  - the discussions with SWL's legal advisers and the legal advice note prepared by SWL with regards the loss of FSCS protection for those Transferring Policyholders currently protected is consistent with what I have seen elsewhere on similar corporate restructuring projects. I have considered the logical basis of the note and legal advice provided by SWL's legal advisers and it is consistent with my own understanding, based on over 20 years' experience of advising on acquisitions and restructuring, including cross border transactions
  - in my opinion, it is reasonable to rely on the discussions related to FSCS provided by SWL's legal advisers as they are a respected law firm with significant experience in insurance regulation including FSCS, Part VII transfers, including cross-border transfers, and are well experienced in advising on such matters.

- 3.11 Based on my own analysis and these discussions I have concluded that following the Transfer, only claims in respect of acts or omissions of SWL prior to the Effective Date will continue to be covered by FSCS.
- 3.12 The Scheme transfers the Transferring Policies to SWE, an insurer based in Luxembourg. As SWE is not a 'relevant person' under FSMA, in accordance with the guidance detailed in paragraph 3.8 and following the discussions detailed in paragraph 3.9, I have concluded that irrespective of the outcome of Brexit negotiations, acts or omissions occurring after the Effective Date, will not be covered by FSCS protection.
- 3.13 The table below provides examples of acts or omissions for different policy types:

Policy type	Example of an act or omission <sup>3</sup>
<b>Protection</b>	Valid claims under the insurance policy for insured events where the insured event occurs prior to the Effective Date eg death claims
<b>Annuity</b>	Valid claims under the insurance policy for insured events where the insured event occurs prior to the Effective Date eg annuity payments up to the Effective Date
<b>Savings/Pensions</b>	Valid claims under the insurance policy for insured events where the insured event occurs prior to the Effective Date eg annuity payments up to the Effective Date and maturity claims

- 3.14 I have discussed with SWL and its legal advisers if the German business litigation claims would be covered by FSCS protection under acts or omissions of a contract of insurance. I understand that the eligibility of these claims under FSCS depends on specific circumstances of each individual claim and a definitive view can only be reached in the event of a claim under FSCS.
- 3.15 Furthermore, the FSCS only provides protection to covered policyholders following an insolvency or default event. Given that SWE is well capitalised, is required to comply with Solvency II regulations and SWE's Capital Management Framework requires it to hold a capital buffer in excess of that required by Solvency II, the likelihood of default or insolvency of SWE, is in my opinion, remote.

### Conclusion

- 3.16 For the purpose of this Supplementary Report I have considered the impact of CP 26/18, discussed this paper with SWL and its legal advisers and considered the latest Brexit negotiations. It remains, as stated in the Report, that Transferring Policyholders who currently benefit from FSCS protection will lose this protection in relation to acts or omissions occurring after the Effective Date as a result of the Transfer. Claims related to acts and omissions that occur prior to the Effective Date will be covered by FSCS. The conclusions detailed in my Report, related to the loss of FSCS, therefore remain unchanged.
- 3.17 I note that, as at 1 March 2019 SWL has received 81 written objections and three verbal objections in relation to the loss of FSCS protection for Transferring Policyholders. I discuss these further in Section 5.

### Alternative operating models considered to mitigate the loss of FSCS protection

- 3.18 As mentioned in my Report, I have discussed with SWL whether a possible mitigant against the loss of FSCS protection is for SWE to set up a third country branch in the UK. If SWE were to establish a UK

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<sup>3</sup> I have been advised by SWL and its legal advisors that under some circumstances claims or litigation relating to mis-selling or mal-administration occurring prior to the Effective Date may also be covered under FSCS.

branch, this would make SWE a 'relevant person' in the UK and would mean FSCS protection would be retained for those Transferring Policies, which currently benefit from FSCS protection. However, for reasons set out in paragraph 11.43 of my Report and outlined below, SWL has not pursued such an option because:

- SWE does not require a third country branch in the UK in order to carry out its day to day operations
- the PRA expressed (in Supervisory Statement SS2/18) that EU insurers would not generally be permitted to have UK branches larger than £500m, a figure exceeded by the Transferring Business.

3.19 I have also discussed with SWL whether FSCS protection could be maintained following the Transfer if SWE were to have passporting rights to service the business within the UK. At the present time SWL has no intention of applying for passporting rights to write business within the UK, because SWL is already authorised in the UK. SWL is not pursuing such an option as:

- SWE does not require UK passporting rights in order to carry out its day to day operations
- passporting rights are only likely to be available in the event that a transitional period is agreed and only for the transitional period.

### Conclusion

3.20 Having considered the alternative operating models available to SWL to mitigate the loss of FSCS for those Transferring Policies which currently have it (detailed in paragraph 3.7), I believe proceeding with the transfer of the Transferring Policies to SWE, without implementing either of the potential mitigants identified is a reasonable approach as:

- setting up a third country branch in the UK is not necessary for SWE to carry out its day-to-day activities
- obtaining passporting rights in the UK does not provide certainty as to continuation of FSCS protection as uncertainty remains over whether passporting to the UK will still be possible post-Brexit. Even if it is possible it is likely that this would be for a transitional period only and in any case, SWE does not require passporting rights in the UK to carry out its day-to-day activities.

## Updated financial information

### Volume of Transferring Business

- 3.21 The table below provides an update on the policy count and the Best Estimate Liabilities (BEL) for the Transferring Business as at 31 December 2018 compared to 31 December 2017.

	31/12/2017			31/12/2018		
	Number of Policies	BEL (Investment element only) (£m)	Total BEL* <sup>4</sup> (£m)	Number of Policies	BEL (Investment element only) (£m)	Total BEL* (£m)
<b>Transferring UWP Business</b>	61,408	1,766	1,753	56,807	1,571	1,600
<b>Transferring UL Business</b>	26,995	318	360	23,922	301	342
<b>Total</b>	88,403	2,084	2,113	80,729	1,872	1,942

*All numbers in the above table are rounded to the nearest whole number.*

*\* BEL is based on the Solvency II basis and the post-Transfer position in SWE.*

- 3.22 At 31 December 2018, the Transferring Business had 9% fewer policies and the BEL had reduced by 8% compared to the figures as at 31 December 2017. The reduction in policies and BEL is as a result of exits (surrenders, deaths, expiries and maturities). The reduction in BEL caused by these exits is partially offset by the investment return earned and premiums paid during the year.

### Conclusion

- 3.23 Following my review of the number of Transferring Policyholders and level of Transferring Business as at 31 December 2018, I am satisfied that the movement can be explained by policy exits.

### Pre and post-Transfer SCR Cover

- 3.24 The table below shows the Solvency II SCR Cover Ratios for SWL and SWE both pre and post Transfer as stated in the Report, assuming the Transfer took place on 31 December 2017. I have reviewed the Solvency II results for SWL before and after the Transfer and SWE after the Transfer assuming the Transfer took place on 30 June 2018. I can confirm that these results do not change my conclusions related to the financial strength of SWL and SWE in my Report. I am unable to quote the latest figures within this Supplementary Report as the results for SWL as at 30 June 2018 are not publicly available.

31 December 2017 (£m)	SWL Pre-Transfer	SWL Post-Transfer	SWE Post-Transfer
<b>Own Funds</b>	8,412	8,244	175
<b>SCR</b>	6,014	6,050	125
<b>Excess Capital over SCR</b>	2,398	2,194	50
<b>Solvency Cover Ratio</b>	140%	136%	140%

*All numbers in the above table are rounded to the nearest whole number.*

- 3.25 There will be an increase in operating expenses as a result of the creation of a new subsidiary to service the Transferring Business. SWL has performed a review of expenses and the expected increase is

<sup>4</sup> BEL is based on the Solvency II basis and the post-Transfer position in SWE not "Luxembourg Generally Accepted Accounting Principles (GAAP) basis" as it was stated in the footnote of the table as at 31 December 2017 used in paragraphs 1.6 and 2.9 of the Report.

reflected in the Solvency II results which I reviewed as at 30 June 2018. However, there is limited scope for charges to policyholders to change and this could only happen with sufficient governance and, as a result, the increase in ongoing expenses will be met by the shareholders of SWE and not by policyholders. The one-off costs of implementing the Scheme will be met by the shareholders of SWL.

- 3.26 In addition to the above, I have had sight of the estimated Solvency II results for SWL and SWE as at 31 December 2018. This information indicates that the solvency position of SWL both before and after the Transfer is within the Green zone<sup>5</sup> based on its risk appetite as defined within its Capital Management Plan (CMP). The pro forma financial position for SWE is at or above its capital policy.
- 3.27 I have also reviewed the output of SWL's solvency monitoring process and SWE's estimated solvency position since 31 December 2018. I remain satisfied that SWL's solvency position is within the Green zone based on its risk appetite as defined within its CMP and for SWE it is at or above its capital policy. In my opinion it is reasonable to rely on the Solvency Monitoring Report. The solvency estimates take account of up to date market conditions on equity markets, interest rates and bond spreads and reflect the impact these conditions have on the risks within the portfolio and the expected movements in liabilities. The results are subject to the review processes in place within SWL's finance department. I have reviewed the solvency results and had the opportunity to ask SWL questions on the results, which have been answered adequately.
- 3.28 I will continue to monitor market conditions up to the date of the Sanctions Hearing on 14 March 2019 with a view to determining whether these will have any impact on my conclusions. If, after the finalisation of this Supplementary Report, there is any material adverse change to market conditions which would alter the conclusions of this Supplementary Report I will prepare a note to the Court, which will include updated analysis and conclusions on the impact of the Transfer.
- 3.29 In my Report I stated the credit ratings of SWL as A from Standard and Poor and a credit rating of A2 from Moody's. The credit ratings have not been updated by the credit agencies since the completion of the Report.

### Conclusion

- 3.30 Given the above, I am satisfied that the solvency positions of SWL and the pro forma position for SWE, as at 30 June 2018 do not change my conclusions related to the financial strength of SWL and SWE in my Report. Additionally, having reviewed the estimated financial position for SWL and SWE at 31 December 2018 and the results of the solvency monitoring process since 31 December 2018, I am satisfied that the solvency position for SWL is within the Green zone based on its risk appetite as defined within its CMP and for SWE it is at or above its capital policy.

### Update on ORSA

- 3.31 An updated version of SWL's ORSA is not available at the time of writing this Supplementary Report. I am satisfied that it is reasonable to rely on the results of the SWL ORSA prepared in March 2018 which includes projections from 2017 year end. I am satisfied that the risks modelled, the stresses and scenarios tested and the management actions assumed in this ORSA are still the most relevant ones for SWL. The ORSA work is subject to SWL's review process.
- 3.32 A separate ORSA has not been prepared for SWE and it is not expected to be produced until later in the year. I was provided with a separate Stress and Scenario Testing analysis for the Transferring Business which included the risks relevant for this business. Additional stresses and scenarios on Transferring

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<sup>5</sup> Capital levels above the target SCR Cover Ratio as defined within the Capital Management Plan, (ie enough capital to cover the regulatory capital requirements as well as the firm's internal capital requirement) is considered to be within the Green zone.

Business were also provided on my request. I relied on this analysis for my Report. No further analysis has been repeated since then. I am satisfied that the risks assessed and the stress and scenario analysis performed and management actions assumed are still the most relevant ones for Transferring Business for the purposes of the Supplementary Report. SWL confirmed that the analysis was subject to SWL's review processes.

### Conclusion

- 3.33 I am satisfied that, it is reasonable for the purposes of the Supplementary Report to rely on the results of the ORSA prepared in March 2018 for SWL and the Stress and Scenario Testing analysis provided for SWE; as the risks modelled, the stresses and scenarios tested and the management actions assumed are still the most relevant for SWL and SWE.

### Update on key dependencies

- 3.34 In the Report, I stated that my conclusions were dependent on a number of actions taking place before the Effective Date. I provide an update on each of these below.

### Update on authorisation of SWE by CAA

- 3.35 The CAA provided authorisation for SWE's licence application on 22 January 2019; SWE's authorisation as a life insurance company was then approved by the Luxembourg Ministry of Finance on 1 February 2019. Following authorisation, the CAA gave notice to the regulators of the EEA countries in which, SWE will service insurance policies under EU passporting rights. SWE has received approval from the CAA for setting up branch offices in Germany and Italy; it has also received a response from the German regulator BaFin acknowledging the set-up of the branch office in Germany. SWE is expecting to receive a response or no objection from the Italian regulator for setting up a branch office in Italy in early March 2019.

### Update on initial capital injection

- 3.36 In Section 6 of the Report, I provided SWE's estimated Solvency II balance sheet immediately after the Transfer, assuming the Transfer occurred on 31 December 2017.
- 3.37 SWE received an initial capital injection of c€6m on 21 January 2019 to meet its enhanced MCR as required by CAA for its authorisation. A further capital injection of €75m was made on 26 February 2019 to capitalise SWE to its target capital level<sup>6</sup>. A certificate of solvency is expected to be provided by the CAA by the date of the Sanction Hearing.

### Update on the Associated Arrangements

- 3.38 SWE and SWL will enter into the Associated Arrangements, namely the Reinsurance Agreement, Charge Agreement, Unit Linked Service Agreement and Indemnity Agreement, prior to the Effective Date. The Witness Statement shows intention to sign these agreements in early March 2019 (except the Unit Linked Service Agreement which will be signed before the Effective Date), however the provisions of such agreements will be conditional on the Scheme taking effect.

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<sup>6</sup> Based on the estimated position of SWE at 31 December 2018 assuming that the Scheme had been implemented at that date

## Conclusion

- 3.39 All of these key dependencies have either been completed or are on track to be completed in advance of the Effective Date.

## Updated non-financial information

- 3.40 Below, I provide updates on a number of non-financial considerations for Transferring Policyholders and Non-transferring Policyholders in relation to the Transfer, being:
- update on UK COBS protection
  - the overall purpose, structure and scope of the Scheme and the Associated Arrangements including the transfer of FWH to SWE
  - the composition of the SWE Board
  - SWE set-up, operations and governance
  - update on requirement of a UK branch for SWE
  - the Tied Assets arrangement as required by the Luxembourg regulations
  - policyholder taxation
  - tax clearances and tax due to Transfer pricing adjustment
  - risk mitigation plans
  - Italian surrender rights.
- 3.41 I have identified no other major developments since the publication of the Report that will impact the Transfer or my opinion of whether any policyholders or reinsurers are materially adversely affected by it.

## Update on UK COBS protection

- 3.42 As a result of the Transfer, the Transferring Policyholders will no longer have direct access to the protections provided by the UK COBS. I described how the Reinsurance Agreement will enable the Transferring UWP Policyholders to continue to indirectly benefit from the UK COBS and the protections provided by the Luxembourg regulations in Section 9 and 11 of the Report.
- 3.43 SWL conforms to the relevant LBG policies, procedures and systems and controls framework, which reflect and facilitate compliance with the UK COBS requirements. SWL has performed a high-level gap analysis to assess its compliance with the governance outlined in UK COBS and any additional requirements resulting from the conduct of business regulations in Luxembourg where SWE will be based, and Austria, Germany and Italy where the business had been sold. Based on the analysis, SWL concluded that the existing LBG risk and control framework meets the conduct of business requirements in the UK and the additional conduct of business requirements in Luxembourg, Germany, Austria and Italy are not material.
- 3.44 I reviewed a high level summary of the analysis and discussed the findings with SWL. Although the analysis is limited in scope, it did not identify material gaps. As the analysis did not indicate material gaps and SWE will comply with LBG's risk and control framework (policies and procedures, systems and controls) my conclusions set out in Section 11 of the Report remain unchanged; and I am satisfied that although the equivalent of the UK COBS does not exist in Luxembourg, the Transferring Policyholders will not be materially adversely affected by the Transfer.

## Update on the Scheme and the Associated Arrangements

- 3.45 I provided a description of the Scheme in Section 7 of the Report, and a description of the Associated Arrangements in Section 9 of the Report. There have been no changes to the purpose, terms or operation of the Scheme or the Associated Arrangements except for the amendment mentioned in paragraph 3.48 below since they were presented to the Court at the Directions Hearing on 26 November 2018, and they remain applicable to the same group of policyholders that they did when I considered in the Report.
- 3.46 Clause 4.4 of the Scheme requires compliance with dispute resolution rules of the FCA with regards to the Transferring Business in relation to disputes that are not settled before the Effective Date and disputes related to acts or omissions of SWL prior to the Effective Date as long as these are compatible with any rules or regulations issued by the CAA. As requested by the FCA, the CAA has provided a letter confirming that the CAA commits to take into account the decisions given by the UK FOS (in relation to Clause 4.4 of the Scheme).
- 3.47 Within the Report, I described how some changes are required to the 2015 Scheme to enable the transfer of assets out of the CM WPF under the Scheme. My certification for these changes to the 2015 Scheme was in Appendix F of the Report. Since the publication of the Report, I have amended the wording in my certification to more accurately reflect the requirement in the 2015 Scheme. The revised certification is attached in Appendix B of this Supplementary Report.
- 3.48 As described in Section 9 of the Report, the Charge is a floating charge over all the assets of SWL (excluding assets of the SWL WPF and any asset subject to security other than a pari passu floating charge, including where prior consent would be required). Since the Report, an amendment has been made in the Charge Agreement to comply with COBS 20.1A.11A and ensure that the portion of the Charge relating to Indemnity does not include the assets of CM WPF. In my opinion this amendment does not have an adverse impact on the Transferring Policyholders as the assets covered by the Charge are likely to be more than sufficient to pay SWE the amount it is entitled to on the winding-up of SWL, had SWE been an ordinary direct policyholder of SWL. I am satisfied that the amendment does not alter the ranking between SWE and the Non-transferring Policyholders, as the provisions under the Charge Agreement still have the effect of aligning SWE and the Non-transferring Policyholders in relation to the distribution of the assets of SWL in the event of SWL being insolvent.
- 3.49 Based on the Witness Statements I understand SWL plans to give the Court at the Sanctions Hearing an undertaking which gives the Transferring UWP Policyholders and the Non-transferring Policyholders in CM WPF the right to enforce the termination conditions set out in clauses 21.1, 21.2 and 22.5.2 of the Reinsurance Agreement. I described these conditions in paragraph 9.41 of the Report. This provides policyholders additional protection on the termination of the Reinsurance Agreement and is consistent with the approach taken on other similar Schemes.

## Update on the Effective Date

- 3.50 The Effective Date for the Scheme has changed from 00.01 GMT on 28 March 2019 to 22.59 GMT on 29 March 2019. The Scheme document has been updated to reflect this amendment. I confirm that this does not change my conclusions with regards to the Transfer as the amendment was made for practical reasons relating to the implementation of the Transfer, it does not impact the operation of the Scheme and it has no impact on the benefits or contractual rights of Transferring Policyholders or Non-transferring Policyholders.

## Update on the transfer of FWH to SWE

- 3.51 Under the Scheme, the assets backing the FWH will be transferred to SWE on the Effective Date. There have been no changes to the purpose and operation of FWH in SWE that would affect my conclusions set out in the Report regarding its impact on Transferring Policyholders and Non-transferring Policyholders.

### Conclusion

- 3.52 Following my review of the above amendments, I am satisfied that they are not material and do not alter the purpose or operation of the Scheme and Associated Arrangements.

### Update on the composition of the SWE Board

- 3.53 In addition to the three Board members originally planned as stated in the Report, the CAA has stated that they will require a fourth Board member to be appointed to ensure that the Board has the required knowledge of financial reporting and accounting. The CAA has approved three members of the SWE Board. The subsequent formal appointment of the Board is in progress and will be completed in March 2019. The recruitment of the fourth Board member is in progress and they are expected to be appointed before the Effective Date.

### Conclusion

- 3.54 I am satisfied that the recruitment process for the Board is progressing well and that the appointment of the fourth Board member will be completed before the Effective Date.

### Update on SWE set-up, operations and governance

- 3.55 I provided a description of the arrangements for SWE's company operations and governance (including company governance, with-profits and unit-linked business governance) in Section 6 of the Report. There has been no change to the planned operations of SWE and the progress that has been made since the publication of the Report has been summarised in this section.

### Recruitment

- 3.56 Recruitment for the CEO and the direct reporting key function holders was substantially finalised subject to signing of contracts which is expected to be in early March 2019. The CEO has been approved by the CAA and will start in March 2019. The key function holders excluding the SWE Chief Actuary (who will also act as the Chief Risk Officer (CRO)) will start in March 2019 following their approval by the CAA which is expected in March 2019. The SWE Chief Actuary is expected to start after the Effective Date; an interim appointment, subject to CAA approval, will be made prior to the Effective Date to cover any period between the Effective Date and the SWE Chief Actuary commencing his appointment.
- 3.57 The majority of other employees are already in place as part of the existing operation of the Transferring Business.
- 3.58 The process of the recruitment of branch managers was substantially completed in February 2019, subject to final formalisation and signing of agreements. They are expected to start in mid-March 2019.

### Governance

- 3.59 Being part of SWG, SWE is expected to comply with all relevant Group policies with immediate effect from authorisation. At the first meeting of SWE Board in March 2019, the Board will discuss any additional policies required under Luxembourg regulations.
- 3.60 The Transferring UWP Business will continue to be managed in line with the CM WPF's PPFM. The CM WPF PPFM has been amended for the Transfer to state that the Transferring UWP Policies will be invested through reinsurance rather than as direct policies of SWL. There have been no further amendments as part of the Transfer.

### Transfer of existing external reinsurance treaties

- 3.61 SWL informed Swiss Re in relation to its reinsurance treaties for the Transferring Business. In the communications they have had, Swiss Re have not indicated that they have an objection. The treaties will be transferred to SWE from the Effective Date.

### Service agreements with outsource providers

- 3.62 SWL has been in contact with the three outsource providers for the policy administration of the Transferring Policies, and they have each agreed to transfer the administration agreements to SWE from the Effective Date.

### Service agreements with LB

- 3.63 I mentioned in Section 6 of my Report that SWE will have service agreements with LB to provide support on internal audit, risk, data privacy, actuarial and finance functions and also the UL Service Agreement specifically for the operation of the Transferring UL Business. SWE is also in the process of establishing a service agreement with LB Europe for HR and payroll services. I understand the execution of these agreements will take place before the Effective Date as stated in the Witness Statements.

### Conclusions

- 3.64 Based on my review I am satisfied that the recruitment process for senior management is on track, and I expect that the service agreements, and the operational and governance requirements for SWE will be completed before the Effective Date.

### Update on requirement of a UK branch for SWE

- 3.65 SWL has considered whether the level and nature of the activities that will be performed on behalf of SWE from the UK would require SWE to seek authorisation in the UK as a third country branch post-Brexit, and has sought legal advice on the issue from its legal advisers. A note was prepared by the legal advisers summarising this advice. This note has been shared with me and I have had an opportunity to discuss and explore this note with SWL's legal advisers to establish the basis and logical flow of the legal advice. I am not an expert in legal matters and therefore I have relied on my discussions with SWL's legal advisers and the legal advice prepared on this topic.
- 3.66 I understand that the activities performed in the UK on behalf of SWE will not trigger a UK Branch as:
- the service agreements for the back office services provided to the Transferring UL Business will include provisions to ensure LB will not provide services that would constitute regulated activity under Part IV of FSMA. As the services are provided by a bank they do not fall within the internal contagion rules that govern insurance entities
  - given SWL has genuine ongoing interest for the decisions made under the terms of the Reinsurance Agreement and the Indemnity Agreement these would be permitted by the internal contagion rules (ie the rule set out in Rule 9.1 of the Conditions Governing Business part of the PRA Rulebook which prohibits an insurer from carrying on any commercial business other than insurance business and activities directly arising from that business).
- 3.67 Overall, the legal advice SWL received indicates the services that will be provided in the UK for Transferring Business would not result in a legal requirement for SWE to seek authorisation as a third country branch within the UK. As such, it is my opinion that SWL has properly considered whether SWE will require a UK branch.

## Update on the Tied Assets

- 3.68 In line with the Luxembourg regulations as described in Section 3 of the Report, a tripartite custodian agreement with the CAA will be required. The Tied Assets backing the greater of Luxembourg GAAP reserves and Solvency II Technical Provisions for both Transferring UWP Policies and Transferring UL Policies will be deposited with the custodian on the Effective Date.
- 3.69 In the unlikely event of SWE's insolvency, the Transferring Policyholders will have priority ranking on the Tied Assets under Luxembourg winding up rules. Further, if the Tied Assets are insufficient to meet policyholder liabilities, the Transferring Policyholders will have preferential rights on the remaining assets of SWE.
- 3.70 In the Report, I gave consideration to these arrangements. In paragraphs 3.47 to 3.54 of the Report I describe the rights of policyholders in case of insolvency of the insurer. In paragraph 3.49 of the Report I mentioned that "Policyholders have super preferential rights on these Tied Assets which ensures that they receive their guaranteed benefits", I would like to clarify that the requirement to hold Tied Assets ensures that policyholders will have access to these assets before other creditors under winding up of SWE due to insolvency. However, there might be circumstances where the Tied Assets may not be sufficient to cover all the insurance claims in their entirety; in this case the policyholders would have a preferential right on the assets of the insurance company as I explained in paragraphs 3.53 and 3.54 of the Report.
- 3.71 Overall, I remain satisfied that the Luxembourg winding up rules provide at least as much protection to policyholder benefits under winding up due to insolvency, as those provided by UK winding up regulations.

## Update on policyholder taxation

- 3.72 In Section 7 of the Report I outlined that the Transfer would result in a difference in timing of the payment of policyholder tax in Germany. The tax on policy payouts (investment income as defined in section 20 of the German Income Tax Code) will be withheld by SWE rather than policyholders having to pay the tax via their tax returns.
- 3.73 Since the Report I have been informed that policyholders who have tax exemption status at the time of the payment of policy payments will not be charged withholding tax; and in case they are charged, they can claim the refund on the withholding tax in their tax returns.
- 3.74 I note that SWL received 56 written objections and one verbal objection as at 1 March 2019 regarding the withholding tax on claim payments in Germany.

## Update on tax clearances and tax due to Transfer pricing adjustment

- 3.75 Since the Report SWL has successfully obtained the required clearances and confirmations from HMRC. A VAT tax clearance is not required by the Luxembourg tax authorities as the Transfer of business qualifies as a "transfer of going concern". This is based on the advice provided by SWL's tax advisers. I consulted Grant Thornton's internal tax adviser, who also confirmed that if the transfer qualifies as a Transfer of Going Concern, no VAT will arise on the transaction.
- 3.76 I mentioned in Section 7 of the Report that there would potentially be transfer pricing adjustment on corporation tax. The work to finalise the transfer pricing is in progress and is expected to be finalised in March. Although this could result in a transfer pricing adjustment, it is not expected to be material and only impacts the corporation tax position of SWL. The corporation tax position of SWL and SWE does not affect the Transferring Policyholders and Non-Transferring Policyholders because it is met by the shareholders.

### **Update on risk mitigation plans**

- 3.77 In Section 10 of my Report I described the key risks to SWE's solvency position and the potential mitigation actions identified to mitigate these risks. These actions include inflation and equity hedges. Until the Transfer the inflation and the equity exposure of the Transferring Business is managed along with the Non-transferring Business through SWL's derivative strategy. Management are aware of the risks that SWE is exposed to and intend to investigate this more closely soon after the authorisation of SWE. They intend to carry out the analysis of risk exposure, measure the extent of the risk and decide on the level of hedges and when to implement it taking into account SWE's risk appetite. This position has not changed since my Report.

### **Update on Italian surrender rights**

- 3.78 As I described in Section 6 of the Report, Transferring Policyholders domiciled in Italy have additional revocation rights under Italian laws that give the policyholders the option to surrender their policies with no surrender penalties if a material aspect of their policies change. The Transfer will trigger this option because the change of domicile of a policy will count as a material change. Policyholders will have 60 days after the Transfer in which to exercise this option.
- 3.79 An updated analysis indicates the cost of Italian policyholders exercising this option to SWE would be c£20m. This will be borne by the shareholders of SWE and it will be included in the amount that will be transferred to SWE.

## 4 Updated impact of the Transfer on policyholders and reinsurers

- 4.1 Within this section, I set out whether the developments described in Section 3 change the opinions that I provided on the likely impact of the Transfer on policyholders and the external reinsurer in the Report.

### The impact of the Transfer on the Transferring Policyholders

- 4.2 Below I consider whether my overall opinion on the likely impact of the Transfer on Transferring Policyholders has changed as a result of the developments described in Section 3.

### Security of policyholder benefits

- 4.3 The developments that could impact on the security of benefits for Transferring Policyholders are:

- changes in market conditions
- the updated financial positions of SWL and SWE before and after the Transfer
- changes in the mitigating actions that SWE might be able to take to manage its risks, particularly its expense and counterparty default stresses.

- 4.4 With regard to security of benefits, I have received the following updated information as discussed in Section 3:

- the financial information based on the transfer occurring on 30 June 2018
- the estimated financial information up to 31 December 2018
- the outputs of SWL's solvency monitoring process and SWE's estimated solvency position since 31 December 2018.

- 4.5 Based on my review of the above information I can confirm that:

- the solvency position of SWL is not materially different from that in the Report both before and after the Transfer assuming the Transfer had taken place on 30 June 2018. The pro forma financial position for SWE as at 30 June 2018 is at or above its capital policy
- I have reviewed the estimates of SWL's solvency as at 31 December 2018 and am satisfied that solvency position of SWL is within Green zone based on its risk appetite as defined within its CMP. The pro forma financial position for SWE as at 31 December 2018 is at or above its capital policy
- I have also reviewed the output of SWL's and SWE's solvency monitoring process since 31 December 2018. I remain satisfied that SWL's solvency position is within Green zone based on its risk appetite as defined within its CMP and the pro forma financial position for SWE is at or above its capital policy. The stress and scenario analysis for SWE has not been updated since my Report but I am satisfied that these continue to cover the main risks to which SWE is exposed, and that the management actions SWE can use to control its solvency in adverse conditions remain appropriate.

- 4.6 Given the above, my conclusions within the Report regarding the security of benefits remain unchanged and I continue to be satisfied that there will be no material adverse effect on the security of the benefits of the Transferring Policyholders as a result of the Transfer.

### Policyholder benefit expectations and contractual rights

- 4.7 There have been no developments since the Report that impact the expected policyholder benefits and contractual rights of the Transferring Policyholders.

- 4.8 My conclusions, as I set out in paragraph 11.41 of the Report for Transferring UWP Policyholders and paragraph 11.103 of the Report for Transferring UL Policyholders, regarding the policyholder benefits and contractual rights remain unchanged since the Report. I am satisfied that there is no material adverse effect on the fund management and application of discretion with regard to the Transferring Business as a result of the Transfer.

### **External bodies providing further policyholder protection**

- 4.9 As explained in paragraph 3.7 above, most of the Transferring Policyholders except those in paragraph 3.5, currently benefit from FSCS<sup>7</sup>.
- 4.10 As I explained in paragraph 3.2, there have been no developments within the Brexit negotiations that provide any certainty over whether SWL will be able to continue to lawfully service business written under EU passporting rights after 29 March 2019. In paragraph 3.4 I mention that although Germany, Italy and Austria have issued draft legislations which allow UK insurers and reinsurers a transitional period until December 2020 to continue to service the business sold in these countries under EU passporting rights in case of hard Brexit, these are temporary solutions without any certainty beyond December 2020 and not finalised yet. These are also not at an EU level (ie the implementation would not be consistent across the EU). Therefore, SWL remains of the view that the Scheme is necessary in order to have certainty that the Transferring Business can continue to be lawfully serviced after Brexit. As a result of the Transfer, Transferring Policyholders who currently benefit from FSCS protection, as set out within the Report, will lose this protection (although claims related to acts or omissions that occur prior to the Transfer would still be covered by FSCS).
- 4.11 My conclusion regarding the loss of FSCS protection for certain Transferring Policyholders remains unchanged from that presented in the Report. That is, I remain satisfied that there is no material adverse effect on policyholder protection for Transferring Policyholders as a result of the Transfer because SWE will be maintaining strong SCR Cover, will be required to comply with Solvency II EU law, and will have a capital management plan which requires a target SCR cover to meet its Pillar 2 capital requirement following a 1-in-10 year stress event, consequently the likelihood of SWE becoming insolvent is remote. Therefore, in my opinion, the likelihood of the protection provided by the FSCS being required is remote.
- 4.12 As I mentioned in paragraph 3.46, the CAA has provided a letter, as requested by the FCA, committing to take into account the decisions given by the UK FOS for the disputes that are not settled before the Effective Date and those related to acts or omissions of SWL prior to the Effective Date. My conclusions with regards to the additional forms of external policyholder protection outlined in the Report, including ombudsman services and conduct of business regulations remain unchanged.
- 4.13 Overall, I am satisfied that, with regard to external bodies providing policyholder protection, there will be no material adverse effect on the Transferring Policyholders as a result of the Transfer.

### **Governance arrangements**

- 4.14 The developments since the Report relating to governance arrangements for the Transferring Policyholders are as stated in paragraphs 3.53 to 3.64.
- 4.15 These developments indicate that the plan for the governance arrangements described in Section 6 of the Report is being executed. None of the above developments adversely impact the Transferring Policyholders. I therefore remain satisfied that there are no material differences in the company

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<sup>7</sup> The note provided by SWL's legal advisers, HSF considers that policies issued prior to the introduction of FSCS on 1 December 2001 meet the definition of a "United Kingdom policy" for the purposes of the Policyholders Protection Act 1975 and as such are assumed to be covered by FSCS.

governance arrangements of SWE and SWL that adversely affect the Transferring Policyholders as stated in the Report (paragraph 11.62 for Transferring UWP Policyholders and paragraph 11.121 for Transferring UL Policyholders).

### **Associated arrangements**

- 4.16 As explained in paragraphs 3.45 to 3.50 above, there have been no material amendments that change the purpose or structure of the Scheme or the Associated Arrangements since writing the Report except for the amendment explained in paragraph 3.48, the plan to provide an undertaking to the Court in relation to the Reinsurance Agreement as stated in paragraph 3.49 and the amendment in the Scheme document to change the Effective Date as stated in paragraph 3.50.
- 4.17 The amendment which was made in the Charge Agreement was to comply with COBS 20.1A.11A and ensure that the portion of the Charge relating to the Indemnity does not include the assets of CM WPF. This amendment does not have an adverse impact on Transferring Policyholders and it does not alter the ranking between SWE and Non-transferring Policyholders. The undertaking provides additional protection to the Transferring UWP Policyholders as it gives them the right to enforce the termination conditions set out in the Reinsurance Agreement. Given these, and having considered the developments in Section 3, my conclusion regarding the Associated Arrangements remains unchanged, and I am satisfied that they will not have a material adverse effect on the interests of Transferring Policyholders.
- 4.18 The change in the Effective date from 28 March 2019 to 29 March 2019 does not change my conclusions with regards to the Transfer.

### **Vesting annuities**

- 4.19 As there have been no developments since the Report that directly impact vesting annuitants, my opinion that the vesting annuitants would not be materially adversely affected by the Transfer remains unchanged.

### **Tax implications**

- 4.20 The tax developments since the Report are as follows:
- As explained in paragraph 3.73, SWL provided further information confirming that the Transfer itself does not affect the tax exempt status of the German tax resident policyholders. Policyholders who have tax exemption status at the time of the policy payments will not be charged withholding tax. In case they are charged withholding tax, they can claim the refund on this tax in their tax returns.
  - As explained in paragraph 3.75, the required clearances and confirmations have been successfully obtained from HMRC. A tax clearance is not required by the Luxembourg tax authorities as the Transfer of business qualifies as a “transfer of going concern”.
- 4.21 The work to quantify a possible Transfer pricing adjustment on corporation tax is in progress and is expected to be finalised in March. Any adjustment to corporation tax is expected to be immaterial and will be borne by the shareholders of SWL.
- 4.22 None of these developments adversely affect the Transferring Business and my opinion that there will be no material adverse tax implications for the Transferring Business as a result of the Transfer remains unchanged.

### **Costs of the Transfer and incremental ongoing expenses**

- 4.23 As I mentioned in paragraph 3.25, SWL performed a review of expenses and the expected increase is reflected in the Solvency II results which I reviewed as at 30 June 2018. My conclusions regarding the

impact of the treatment of expenses and charges on the Transferring Policyholders remain unchanged, as the one-off costs of implementing the Scheme will be met by the shareholders of SWL; the increase in ongoing expenses will be met by the shareholders of SWE and not by policyholders. Also, there is limited scope to change the charge for policyholders and this could only happen with sufficient governance as I explained in paragraphs 6.49 to 6.53 of the Report. I am satisfied that the expense review performed does not change my conclusion in the Report (paragraphs 11.88 and 11.89 for Transferring UWP Policyholders; paragraphs 11.144 and 11.145 for Transferring UL Policyholders).

### **Administration and service standards**

- 4.24 The developments since the Report that could impact on administration and service standards for Transferring Policies are described in paragraphs 3.57, 3.62 and 3.63.
- 4.25 These developments indicate that the plan for the administration and service standards as set out in the Report is being executed and does not adversely impact the Transferring Policyholders. Therefore, with regard to the administration and service standards experienced by Transferring Policyholders, I remain satisfied that there will be no material adverse effect on the administration and service standards experienced by Transferring Policyholders as stated in the Report (paragraph 11.93 for Transferring UWP Policyholders, paragraph 11.150 for Transferring UL Policyholders).

### **Conclusion**

- 4.26 Overall, having considered all the developments within Section 3, I have concluded that my opinion in the Report remains unchanged: the Transferring Policyholders will not be materially adversely affected by the Transfer.

## **The impact of the Transfer on the Non-transferring Policyholders of SWL**

- 4.27 Below I consider whether my overall opinion on the impact of the Transfer on Non-transferring Policyholders has changed as a result of the developments described in Section 3.

### **Security of policyholder benefits**

- 4.28 The developments that could impact on the security of benefits for Non-transferring Policyholders are:
- changes in market conditions
  - the updated financial position of SWL before and after the Transfer
  - the updated information on SWL's projected future solvency
- 4.29 With regard to security of benefits, I have received the following updated information as discussed in Section 3:
- the financial information based on the transfer occurring on 30 June 2018
  - the estimated financial information up to 31 December 2018
  - the outputs of SWL's solvency monitoring process since 31 December 2018.
- 4.30 Based on my review of the above information I can confirm that the solvency position of SWL is not materially different from that in the Report both before and after the Transfer assuming the Transfer had taken place on 30 June 2018.
- 4.31 I have reviewed estimates of SWL's solvency as at 31 December 2018 and am satisfied that the solvency position of SWL is within Green zone based on its risk appetite as defined within its CMP. The projections within the SWL ORSA have not been updated however I am satisfied that the ORSA

remains relevant as the risks covered remain unchanged and that SWL's solvency position over the projection period is stable.

- 4.32 Given the above, my conclusions within the Report regarding the security of benefits remain unchanged and I continue to be satisfied that there will be no material adverse effect on the security of the benefits of the Non-transferring Policyholders as a result of the Transfer.

### **Policyholder benefit expectations and contractual rights**

- 4.33 There have been no developments since the Report that could impact on the policyholder benefits and contractual rights of the Non-transferring Policyholders so my opinion, as set out in paragraph 12.9 and 12.13 of the Report, remains unchanged. I remain satisfied that the Transfer will have no material effect on either the policyholder benefits or contractual rights for the Non-transferring Policyholders.

### **External bodies providing further policyholder protection**

- 4.34 As outlined in the Report, there will be no change to the availability of FSCS protection, or any other external policyholder protection services for the Non-transferring Policyholders, as a result of the Transfer.
- 4.35 Because nothing has changed since the Report, my conclusions with regard to external bodies providing further policyholder protection for the Non-transferring Policyholders remain unchanged. I remain satisfied that the Transfer will have no impact on the protection of Non-transferring Policyholders.

### **Governance arrangements**

- 4.36 As there has been no developments to the governance arrangements since the Report that would change my opinion, I remain satisfied that there will be no material adverse effect on the company level governance arrangements for Non-transferring Policyholders as a result of the Transfer.

### **Associated arrangements**

- 4.37 As explained in paragraphs 3.45 to 3.52, there have been no material amendments that change the purpose or structure of the Scheme or the Associated Arrangements since writing the Report except for the amendment explained in paragraph 3.48, the plan to provide an undertaking to the Court in relation to the Reinsurance Agreement as stated in paragraph 3.49 and the amendment in the Scheme document to change the Effective Date as stated in paragraph 3.50.
- 4.38 The amendment which was made in the Charge Agreement was to comply with COBS 20.1A.11A and ensure that the portion of the Charge relating to the Indemnity does not include the assets of CM WPF. This amendment does not have an adverse impact on Non-transferring Policyholders and it does not alter the ranking between SWE and Non-transferring Policyholders. The undertaking provides additional protection to the Non-transferring Policyholders in the CM WPF as it gives them the right to enforce the termination conditions set out in the Reinsurance Agreement. Given these, and having considered the developments in Section 3, my conclusion regarding the Associated Arrangements remains unchanged, and I am satisfied that they will not have a material adverse effect on the interests of Non-transferring Policyholders.
- 4.39 The change in the Effective date from 28 March 2019 to 29 March 2019 does not change my conclusions with regards to the Transfer.

### **Tax implications**

- 4.40 The work to quantify a possible Transfer pricing adjustment on corporation tax is in progress and will be finalised in March. Any adjustment to corporation tax is expected to be immaterial and will be borne by SWL shareholders.

- 4.41 All tax implications of the Transfer for Non-transferring Policyholders remain unchanged since writing the Report.

#### Tax clearances

- 4.42 All tax clearances relevant to the Non-transferring Policyholders have been obtained.

#### Costs of the Transfer and incremental ongoing expenses

- 4.43 As I mentioned in paragraph 3.25, SWL performed review of expenses and the expected increase is reflected in the Solvency II results which I reviewed as at 30 June 2018. My conclusions regarding the impact of the treatment of expenses and charges on the Non-transferring Policyholders remain unchanged, as the one-off costs of implementing the Scheme will be met by the shareholders of SWL and the increase in ongoing expenses will be met by the shareholders of SWE and not by policyholders.

#### Administration and service standards

- 4.44 As there are no anticipated changes to the administration and services standards, I remain satisfied that there will be no material adverse effect of Non-transferring Policyholders as a result of the Transfer.

#### Conclusion

- 4.45 Overall, having considered all the developments within Section 3, I have concluded that my opinion in the Report remains unchanged: the Non-transferring Policyholders will not be materially adversely affected by the Transfer.

#### The impact of the Transfer on reinsurers of the Transferring Business

- 4.46 Given that there will be no change to the external reinsurance contract besides the requirement to reflect the change of party following the Transfer, I am satisfied that there will be no material effect of the Transfer on the external reinsurers of the Transferring Policies.
- 4.47 SWL has been in contact with Swiss Re in relation to its reinsurance treaties for the Transferring Business, and they have not raised any objection. The treaties will be transferred to SWE from the Effective Date.

## 5 Consideration of the policyholder communication process and objections and representations received

- 5.1 At the Directions Hearing on 26 November 2018, the Court agreed SWL's proposed plans for policyholder communication in respect of the Scheme.
- 5.2 All Transferring Policyholders, except those subject to the waivers, were to be sent a Policyholder Pack by SWL by post. The packs were to include:
- a brief notification letter called the Policyholder Letter
  - an important information sheet
  - a more detailed Planholder Guide.
- 5.3 SWL has confirmed to me that it has carried out its communications with the Transferring Policyholders in line with the Directions Order<sup>8</sup> and this has been confirmed in the Witness Statements I have seen. I note that the mailing to Transferring Policyholders was completed by 11 January 2019 which is approximately nine weeks prior to the Sanctions Hearing and in line with the requirement under the FCA and PRA's guidance. I have also discussed with SWL the progress of communications on a weekly basis.
- 5.4 SWL also confirmed that they published a notice in the London, Edinburgh and Belfast Gazettes. In addition, it advertised in five national newspapers circulated in the UK (also the EU edition of one of these), two national newspapers in Austria, Germany, Italy and three national newspapers in Luxembourg.
- 5.5 SWL also confirmed that out of the 87,097 communication packs sent out only 964 (ie approximately 1%) were returned as at 1 March 2019. SWL has been working on identifying new addresses for the returned packs and to send the communication packs to correct addresses. SWL identified new addresses for 527 of the returned communication packs and resent the packs to the new addresses identified.
- 5.6 Overall, I am satisfied that the communication process has met the requirements of the Directions Order and the policyholders have been given sufficient details and notice of the proposed Scheme.
- 5.7 At regular intervals, I have been provided with all the objections received from policyholders relating to the Scheme as a result of the policyholder communications. I have also been provided with summarised technical queries. The correspondence in relation to objections, and summarised technical queries including SWL's responses to these have been translated into English by a dedicated translations team in SWL. I have relied on these translations while performing my review.
- 5.8 SWL has confirmed that as at 1 March 2019 it had received 1,365 letters/telephone calls from Transferring Policyholders relating to the Scheme of which 128 were confirmed as written objections.
- 5.9 SWL has corresponded with these policyholders by letter and also by telephone. I have been provided with the written correspondence with policyholders translated into English up to 1 March 2019.
- 5.10 All of the call handlers taking calls related to the Transfer have been through specific training. This training included the definition of objection; process flows indicating the process that needs to be

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<sup>8</sup> An order was made by Deputy ICC Judge Middleton in the High Court of Justice ((Insolvency and Companies List (ChD)) on 26 November 2018 (the Directions Order) upon the Claim Form dated 19 November 2018.

followed to classify the call, provide the response if it is a general query or escalate to the technical team if it is a technical query and the response is not in the response library. The technical team contains representatives from legal, actuarial, tax, risk, customer services, project communications team and other areas if required.

- 5.11 An objection has been defined as any written expression and whether justified or not from or on behalf of an eligible customer who states that they do not wish the Part VII transfer to proceed. SWL received 128 written objections as at 1 March 2019.
- 5.12 In addition, SWL has classified objections raised over the phone as verbal objections. SWL did not treat verbal objections as formal objections, however, their concerns have been recorded and classified separately. As at 1 March 2019 there were five verbal objections. Two of these policyholders were informed to provide their objections in writing to be counted as objections. In my analysis I treated verbal objections as objections, so I have considered the five verbal objections received as at 1 March 2019 and included them into the categorization of objections set out below.
- 5.13 I have reviewed how SWL defines objections and the controls it has in place to ensure that objections are identified and recorded under this definition. I have held calls with SWL specifically on this topic to better understand the process and I have reviewed the training pack that has been given to call handlers regarding how to identify objections.
- 5.14 I have reviewed all correspondence relating to the written objections (and summary of available correspondence relating to the verbal objections) and discussed both written and verbal objections during regular calls with SWL. I have also reviewed correspondence received by SWL for a sample of technical queries. For the technical queries, I have considered whether, in my view, they should instead be classified as objections and held discussions with SWL to understand further the reasoning for certain categorisations.
- 5.15 Overall, I am satisfied that the processes SWL have in place are robust and that objections have been identified correctly. Although SWL did not treat the verbal objections as objections, it recorded those policyholders' concerns and classified them separately.
- 5.16 In addition, I have checked that the Scottish Widows websites ([www.scottishwidows.co.uk](http://www.scottishwidows.co.uk), [www.clericalmedical.com/de/index.asp](http://www.clericalmedical.com/de/index.asp), [www.clericalmedical.com/austria/index.asp](http://www.clericalmedical.com/austria/index.asp) and [www.clericalmedical.com/it/index.asp](http://www.clericalmedical.com/it/index.asp)) have published the following policyholder communications:
- Scheme
  - Independent Expert's Report
  - The Summary Report – an abridged version of the Report
  - Chief Actuary's Report on the Scheme
  - With-Profits Actuary's Report on the Scheme
  - Policyholder Pack
  - Legal Notice of the Scheme.
- 5.17 I am aware that the PRA has notified the supervisory authorities in all EEA states in respect of the Scheme in order to initiate the EEA regulator consultation. At the time of writing this report, there have been no objections from supervisory authorities.

## Objections

- 5.18 Based on my analysis of the objections received by SWL, the objections raised can be summarised into the following categories:
- loss of FSCS protection and concerns over security of benefits

- withholding tax for policyholders in Germany
- concerns related to the Transfer
- clarity in my Report
- request for surrender value and compensation
- other
- no reason provided.

5.19 The categorisation of objections is based on my analysis and the numbers may differ from those presented in the Witness Statements which are based on the analysis undertaken by SWL and its outsource partners. I have considered each of these types of objections below.

### Loss of FSCS protection and concerns over future security of benefits

5.20 SWL received 81 written and three verbal objections as at 1 March 2019 concerning the loss of FSCS protection on their policies. Three refer to the German compensation scheme Protektor as a comparable protection to FSCS in the UK. All policyholders raising these objections currently benefit from FSCS protection.

5.21 SWL has performed an analysis of the types of policyholders that raised written objections relating to the loss of FSCS. This is summarised in the following table:

Product	Number of objections relating to loss of FSCS
Life Savings	64
Pensions and Annuities	17

5.22 As I explained in Section 3 of the Report, the FSCS provides protection to policyholders in an insolvency event. I am satisfied that the insolvency of SWE would be a remote event because SWE will be appropriately capitalised immediately after the Transfer as I explained in Section 10 of the Report. SWE is required to comply with Solvency II rules under which SWE is required to hold capital to cover an SCR for 1 in 200 year adverse risk events. SWE's Capital Management Framework (as described in Section 6 of the Report) sets the Target SCR Cover as an amount sufficient to withstand 1-in-10 year event and still meet its Pillar 2 capital requirements, which is in excess of the amount of capital SWE is required to hold under Solvency II. Therefore, in my opinion the likelihood of FSCS protection being required is remote and I do not consider the loss of FSCS protection to have a material adverse effect on the Transferring Policyholders that currently have FSCS protection for the reasons set out above.

5.23 Further, as stated in paragraphs 3.18 and 3.19, I have discussed with SWL alternative approaches to addressing the loss of FSCS for policyholders. The alternative approaches included consideration of a third country branch of SWE in the UK and SWE establishing passporting rights to service business within the UK. Neither of these alternatives were regarded as appropriate by SWL as setting up a third country branch in the UK is not necessary for SWE to carry out its day to day activities and uncertainty remains over whether passporting in the UK will still be possible post-Brexit. I agree with SWL's view and believe proceeding with the Transfer without implementing these mitigants is reasonable to ensure that SWL is allowed to continue to service business written under EU passporting rights after Brexit.

5.24 The German protection scheme Protektor is only available to a company incorporated in Germany. As SWE is based in Luxembourg it cannot take advantage of it. As I explain in paragraphs 5.33 to 5.37, SWL considered a number of jurisdictions before choosing Luxembourg. I have discussed its reasons with SWL and their legal advisers and I am satisfied that, it is reasonable for the Transferring Business to move to a company incorporated in Luxembourg to ensure servicing of policies sold under EU passporting rights after Brexit.

- 5.25 SWL received a further 11 objections as at 1 March 2019 expressing concerns about the future security of their benefits including the financial strength of SWE. I have reviewed the financial strength of SWE in my Report and the updated position in Section 3 of this document and am satisfied that SWE holds sufficient capital under its Capital Management Framework and my conclusions regarding the security of benefit for the Transferring Policyholders remains unchanged. I remain satisfied that there would be no material adverse effect on the security of the benefits of the Transferring Policyholders as a result of the Transfer.

### **Withholding tax for policyholders in Germany**

- 5.26 SWL received 56 written objections and one verbal objection as at 1 March 2019 where policyholders had concerns that their investment income will be subject to withholding tax in Germany. 23 of these policyholders objected on the basis that they had purchased the policies before the changes in German tax rules as at 31 December 2004 and their policies should be exempt from tax.
- 5.27 As I explained in Sections 7 and 11 of my Report, and in paragraph 3.72 based on the advice SWL received from external and internal tax advisers, German resident taxpayers will be subject to a withholding tax deduction on policy payments (investment income as defined in section 20 of the German Income Tax Code) they receive. This will create a timing difference in when tax payments are made rather than introducing a new taxation or changing the amount of tax actually paid. The tax on claim payments will be withheld by SWE rather than paid through the mechanism of the policyholder's tax return.
- 5.28 I understand there are policies which were purchased before the change of tax rules in Germany that qualify for exemption from the tax on policy payments (investment income as defined in section 20 of the German Income Tax Code) subject to meeting certain requirements. I understand that these policyholders who have tax exempt status at the time of the policy payments will not be charged withholding tax. In case they are charged, they can claim the refund on the withholding tax in their tax returns.
- 5.29 Furthermore, there might be policyholders who do not pay tax due to their personal circumstances, such as their income status. If policyholders provide SWE with an exemption certificate tax will not to be withheld. In the absence of the certificate they can claim the refund on the withholding tax in their tax returns.
- 5.30 Based on the advice I have received from SWL's tax advisers which was reviewed by Grant Thornton's tax specialist, I do not expect any adverse impact to the tax on policy payments of policyholders or any change in the amount of tax that will be paid on the payments. The only impact will be on the timing of the policyholder tax payment. The Transfer will not change the tax exempt status of the policyholders. The policyholders who qualify for tax exempt status at the time of policy payments will be exempted from the withholding tax. In case they are charged, they can claim the refund on the withholding tax in their tax returns.

### **Concerns related to the Transfer**

- 5.31 SWL received a number of objections related to concerns over the Transfer which I have combined under this theme. I summarise the different concerns under the subheadings below and give my opinion for each.

#### **Concerns over the Transfer to Luxembourg based company**

- 5.32 SWL received five objections as at 1 March 2019 against transferring the business to a company incorporated in Luxembourg and the related security of their policies.

- 5.33 SWL considered a number of jurisdictions for the Transfer before choosing Luxembourg. I have discussed the reasons for choosing Luxembourg with SWL and its legal advisers, including the level of policyholder protection the Luxembourg regulations provide.
- 5.34 SWE will be authorised by the Luxembourg insurance regulator, CAA and the Ministry of Finance and regulated by the CAA. Luxembourg regulations operate a risk-based solvency regime based on Solvency II, which requires SWE to hold capital required under a 1-in-200 year adverse scenario. SWE will hold capital in line with its target SCR Cover Ratio, which is in excess of this regulatory minimum.
- 5.35 As described in paragraph 3.69, Luxembourg regulations require insurers to deposit Tied Assets with a custodian bank and these assets are required to be segregated from other assets and liabilities in SWE. In the unlikely event of SWE's insolvency, the Transferring Policyholders (ie the policyholders of SWE) will have priority ranking on the Tied Assets under Luxembourg winding up rules. Further, if the Tied Assets are insufficient to meet policyholder liabilities, the Transferring Policyholders will have preferential rights on the remaining assets of SWE. These provisions provide security to meet SWE's policyholder liabilities in the unlikely event of SWE's insolvency.
- 5.36 SWG has experience in operating in Luxembourg as they had a subsidiary company there in the past.
- 5.37 Given the above, I remain satisfied that, it is reasonable for Transferring Business to move to a company incorporated in Luxembourg to ensure servicing of policies sold under EU passporting rights after Brexit. Like the UK, Luxembourg has a solvency regime based on Solvency II. The Luxembourg winding up rules provide at least as much protection to policyholder benefits under winding up due to insolvency, as those provided by UK winding up regulations.

#### Governing law and jurisdiction for legal disputes and court cases

- 5.38 SWL received 44 objections as at 1 March 2019 regarding the governing law and jurisdiction for legal disputes and court cases. 34 of these objections as at 1 March 2019 asked for German law to apply to their policies and requested the courts and jurisdiction of their country of residence (ie Germany) to apply to any lawsuits. Nine of these as at 1 March 2019 objected due to concerns over language differences and travel expenses of having to travel to Luxembourg should there be a legal dispute.
- 5.39 Based on the advice from SWL's internal legal advisers, I understand the law governing the terms and conditions of the policies will remain the governing law that is stated in the policy documentation. For policies written under German law, German law will continue to apply in relation to disputes about the policy terms and conditions. However, I understand, there are circumstances where the insurance law in the jurisdiction of the country where the policyholder lives may also apply.
- 5.40 As I pointed out in Section 11 of the Report, the Transferring Policyholders will continue to have access to their local systems of complaints handling including approaching the Court. Given policyholders can access their local systems of complaints handling there should be no concerns over language differences and travel expenses to Luxembourg. For policies sold on Freedom of Service basis in addition to their local system of complaints handling they will have access to the Luxembourg Ombudsman Service (LOS) (which offers services in different languages) and Courts in Luxembourg if they wish to do so.
- 5.41 Given the above, I am satisfied that the Transferring Policyholders will not be materially adversely affected by the Transfer with regards to the governing law of their policies or access to local systems of complaints handling.

#### Loss of access to the FOS

- 5.42 SWL received four objections as at 1 March 2019 concerning the loss of FOS protection stating that the FSCS and the FOS were the main reasons why they chose to purchase policies in the UK.

- 5.43 As I explained in Section 3 and 11 of my Report that the Transferring Policyholders who currently have access to the UK FOS will lose this access, other than in respect of pre-transfer acts or omissions, as a result of the Transfer. The policyholders will continue to benefit from their local systems of complaints handling and policies sold on Freedom of Service basis will also be able to approach the Luxembourg Ombudsman Service (LOS) post Transfer. My conclusion that the Transferring Policyholders will not be adversely affected by any loss of policyholder protection with respect to the UK FOS remains unchanged. Although the ombudsman services in Luxembourg and the other EU countries, from which the policies were purchased, are not binding in the same way as in the UK, I am satisfied that there are sufficient complaints mechanisms available to the policyholders.
- 5.44 I have been informed by SWL that in practice the Transferring Policyholders always raised their disputes through their local system of complaints handling rather than the UK FOS. This indicates that they might not look to use the UK FOS in the future and, as such, are unlikely to suffer detriment from the withdrawal of this service.

#### Concerns over why the Transfer is needed

- 5.45 SWL received four objections as at 1 March 2019 where policyholders have questioned the need for the Transfer.
- 5.46 As I explained in my Report and also in Section 1 and 3, Brexit is expected to take effect on 29 March 2019, resulting in uncertainty as to whether UK insurance companies will continue to be able to service business written in EEA countries outside of the UK, under EU passporting rights, after 29 March 2019. This would include the collection of premiums and payment of claims. Therefore, unless suitable transitional or grandfathering arrangements between the UK and the EU are agreed prior to the 29 March 2019, it is expected that it will become illegal for SWL to continue to service the policies written under EU passporting rights. So far, there have been no developments in Brexit negotiations that provide this certainty over whether SWL will be allowed to continue to service business written under EU passporting rights after 29 March 2019. As I explained in paragraphs 3.2 to 3.4, there are draft legislations that have been put forward by Germany, Italy and Austria for a transitional arrangement in case of hard Brexit, however these are only temporary solutions, they are not yet finalised and they are not at an EU level (ie as a result the implementation would not be consistent across the EU). The Scheme continues to provide SWL with certainty that the Transferring Business can continue to be lawfully serviced post-Brexit.
- 5.47 Given the above, I am satisfied that the Transfer provides SWL with certainty that it will be able to lawfully service the Transferring Business post-Brexit.

#### Concerns over who meets the costs of Transfer and SWE

- 5.48 SWL received 15 objections as at 1 March 2019 relating to concerns that the costs of Transfer and setting up SWE would be borne by the policyholders and the increased costs would adversely impact the performance of their policy. One further objection suggested that, the profits to the policyholder should rise considering SWE will not be paying levy for FSCS to cover Transferring Policies.
- 5.49 As I explained in my Report, the costs of the Transfer and setting up SWE will be met by shareholders of SWL and not the policyholders. There will be an increase in ongoing costs due to the inefficiencies caused by transferring the business into a subsidiary and operating a separate company, however, these additional ongoing costs will also be met by the shareholders and not the Transferring Policyholders.
- 5.50 There is limited scope to increase policyholder charges in the event that expense increase in the future. Any proposed change in charges would need to be in line with the terms and conditions of the policies as set out in product literature and be in line with policyholders' reasonable expectations. Any decision on changing charges would be made by the SWE Board after receiving appropriate advice. Any expenses in excess of charges will be met by the shareholders of SWE.

- 5.51 After the Transfer, SWE will not be paying a levy for the FSCS to cover the Transferring Policies. However, this will not result in a decrease in policy charges as this cost is borne by SWL shareholders and not the policyholders. Given the above, I am satisfied that the costs of the Transfer and setting up of SWE will not affect the performance of the policies or the Transferring Policyholders.

#### Concern over any change in terms, conditions and management of their policies

- 5.52 SWL received three objections as at 1 March 2019 regarding concerns that the Transfer could change the terms and conditions and management of their policies and that the access to with-profit benefits will become more complex and non-transparent after the Transfer. One policyholder raised concerns over the Charge Agreement.
- 5.53 As I explained in Section 11 of the Report, SWE will take on all existing rights and obligations of SWL in relation to the Transferring Policyholders.
- 5.54 While the Transferring UWP Policyholders will become direct policyholders of SWE rather than SWL, the Reinsurance Agreement ensures that these policies will be maintained in the same way before and after the Transfer. There will be no material change to investment strategy and no material change to the governance around bonus distribution (as I explained paragraphs 6.44 to 6.47 in the Report). The with-profit communications will not be altered as a result of the Transfer, the only change will be that the communications will be issued by SWE rather than SWL.
- 5.55 The Transferring UL Policyholders will become direct policyholders of SWE rather than SWL, however, the Unit Linked Service Agreement will ensure that the operation of the unit-linked funds remains the same before and after the Transfer albeit under the control of SWE rather than SWL. There will be no material change to the investment management as a result of the Transfer. The governance around the use of discretion for the Transferring UL Business will be similar to that under SWL; the SWE Chief Actuary will advise the SWE Board on the management of Transferring UL Business for actuarial matters under the Luxembourg regulations. SWE is also expected to comply with Group level policies such as the Customer Treatment Policy.
- 5.56 The Charge Agreement aims to provide protection to SWE in the event of SWL's insolvency against exposure to the Reinsurance Agreement (for amounts in excess of the funds withheld) and the indemnity agreement, enabling SWE to have the same ranking as direct policyholders of SWL.
- 5.57 Based on my analysis I am satisfied that there will be no material changes to the terms and conditions of these policies as a result of the Transfer, and therefore no material impact on the contractual rights of these policyholders. I remain satisfied that the Charge Agreement ensures that in case of SWL's insolvency SWE would have the same ranking as the direct policyholders of SWL.

#### Concerns over difference in treatment for Transferring and Non-transferring Policyholders

- 5.58 One policyholder as at 1 March 2019 who has a with-profits policy has raised concerns that the Transfer results in the Transferring and Non-transferring Policyholders being treated unequally.
- 5.59 As I explained in Section 9, 11 and 12 of the Report for the Transferring UWP Policies, the Reinsurance Agreement aims to allow the Transferring UWP Business to be managed in the same way before and after the Transfer together with the Non-Transferring WP Policyholders in the same fund, CM WPF in SWL.
- 5.60 The main objective of my assessment of the Transfer is to ensure that there is no material disadvantage to either the Transferring or Non-transferring Policyholders. In Section 11 and 12 of the Report I set out my opinion on the impacts of the Transfer on different groups of Transferring and Non-transferring Policyholders respectively. In Section 4 of this report I review the impact of the Transfer on the Transferring and Non-transferring Policyholders since my Report. I confirm that my conclusions since the Report are unchanged. I am satisfied that the implementation of the proposed Transfer will not have

a material adverse effect on the security of benefits or future benefit expectations, governance or service standards experienced by the Transferring Policyholders or the Non-transferring Policyholders.

## **My Report**

- 5.61 SWL received nine objections as at 1 March 2019 relating to the Independent Expert Report, two of these questioning the quality of the Report given the Independent Expert has carried out assessments for multiple Brexit related Part VII transfers. Seven of these objections raised concerns relating to the language used in expressing the Independent Expert's opinion. I understand that expressions such as "materially adverse" are not well understood.
- 5.62 As I explained in Section 2 of my Report, my appointment as Independent Expert for this Transfer was approved by the PRA after their assessment in consultation with the FCA. Their assessment included consideration to my ability to perform the role, my other commitments and independence from SWL.
- 5.63 Although I have been the Independent Expert for a number of Part VII transfers, I work with a large department of actuarial and risk professionals including those who have expertise on Part VII transfers and restructuring of insurance businesses. We have controls on allocation of teams and I have separate teams working on the analysis of each transfer under my supervision. My team and I have performed the necessary analysis with respect to the Scottish Widows Scheme to support my conclusions. We also have internal conflicts arrangements to ensure independence in respect of the Scottish Widows Scheme.
- 5.64 With regards to the objections regarding the level of analysis and clarity in my Report, my Report was prepared in line with the requirements set out in Part VII of FSMA and the guidance issued by the PRA and the FCA (the UK regulators). My Report was also reviewed by the PRA and the FCA and I addressed their comments in my Report. In addition, the PRA and FCA make an independent assessment of the transfer which is submitted to the Court.
- 5.65 As I point out in paragraph 2.10, I further provide this Supplementary Report to give an updated assessment of the likely effect of the proposed Transfer and to consider whether or not the conclusions reached in my Report remain unchanged, after taking into account the most recent financial information for SWL and SWE that has been made available to me and any other significant developments including any objections received.
- 5.66 The expression "materially adverse" is standard wording commonly used for Independent Expert reports as defined in paragraph 2.32 of my Report. As an Independent Expert I am restricted by the information provided to me and can only express my opinion based on this information. I am required to consider factors that could materially impact the various stakeholders (different groups of policyholders and reinsurers) involved with the Transfer. It is inevitable that any transaction has both upsides and downsides. My aim is to investigate whether this Transfer will have unfavourable consequences for any of the policyholder groups or reinsurers involved with the Transfer. Assessments of future events are subject to many assumptions which cannot be forecast with 100% accuracy. Therefore, where I have relied on information concerning the future, I have assessed the reasonableness of the assumptions and considered whether or not stakeholders will be adversely impacted and whether this impact may be material.

## **Request for surrender value and compensation**

- 5.67 As at 1 March 2019 there are 73 policyholders who objected in writing, and one who objected verbally to the Transfer requesting to terminate their policies including requests for surrender value, surrender value with no surrender penalties, return of premiums, return of premiums with interest and other forms of compensation. A further eight policyholders as at 1 March 2019 requested information on their surrender value to consider termination.

- 5.68 I understand that if the policyholders choose to terminate their policies due to the Transfer, a surrender value based on the terms and conditions of their policies will be paid, after the allowance of a surrender penalty, where applicable, as defined in their policy conditions, through the company's normal surrender process. No additional payment will be made to those terminating their policies due to the proposed Transfer.
- 5.69 It is my opinion that it is fair and reasonable to pay the policyholders who choose to terminate their policies surrender values based on the terms and conditions of their policies. This is because, as I conclude in Section 6 below, I remain satisfied that the proposed Transfer will not have a material adverse effect on the security of benefits, future benefit expectations of the Transferring Policyholders and Non-transferring Policyholders and governance or service standards experienced by the Transferring Policyholders and Non-transferring Policyholders.

### **Other**

- 5.70 SWL received one objection as at 1 March 2019 from an intermediary regarding concerns over future commission payments after the Transfer.
- 5.71 I understand that commission payments to the agents and brokers will continue to be made after the Transfer, however not by SWL but by SWE. Therefore, I am satisfied that there will be no change to the commission payment as a result of the Transfer.

### **No reason provided**

- 5.72 SWL received 15 written objections and one verbal objection as at 1 March 2019 where policyholders have objected to the Transfer but have not specified a reason or basis for their dissatisfaction of the proposed Scheme. I have reviewed the written objections and confirm that the policyholders who objected did not state a specific reason for their objection.

### **Conclusion**

- 5.73 Overall, I am satisfied that at the time of writing this Supplementary Report, SWL is recording the objections received appropriately. The policyholders have not raised any issues that were not considered in the work leading up to the Report except those related to tax exempt status in Germany. As I explained in Sections 3, 4 and in this section above I conclude that the Transfer will not affect the tax exempt status of the policyholders. Given that no other new issues were raised, I am satisfied that there are no reasons to change the conclusions in my Report.

## 6 Conclusion

- 6.1 I confirm that, overall, I am satisfied that the implementation of the proposed Scheme and the Associated Arrangements will not have a material adverse effect on the security of benefits or future benefit expectations of the Transferring Policyholders or the Non-transferring Policyholders. It is also my opinion that the Transfer will not have a material adverse effect on the governance or service standards experienced by the Transferring Policyholders or the Non-transferring Policyholders. In addition, I am satisfied that the Transfer will not materially adversely affect the reinsurers of the Transferring Business.
- 6.2 Given my conclusions outlined above, I see no reason why the Transfer should not proceed.



Tim Roff FIA  
Partner  
Grant Thornton UK LLP

6 March 2019.

## A Information/Documents reviewed/relied on

The table below sets out the key additional documents I have relied on in preparing this Supplementary Report. Some of this information is company confidential and is not publicly available. In addition to the listed documents, I have also relied on discussions (both orally and electronically) with senior management and staff at SWL.

Document	Source
<b>Scheme (5 March 2019)</b>	HSF
<b>Reinsurance Agreement (5 March 2019)</b>	HSF
<b>Deed of Charge (5 March 2019)</b>	HSF
<b>Deed of Indemnity (5 March 2019)</b>	HSF
<b>Witness Statements (4 March 2019):</b> <ul style="list-style-type: none"> <li>– Second Transferor Witness Statement</li> <li>– Third Transferee Witness Statement</li> <li>– HLSM Witness Statement</li> <li>- PAM Witness Statement</li> <li>– ITO Witness Statement</li> </ul>	HSF
<b>Report of the Chief Actuary (5 March 2019)</b>	SWL Chief Actuary
<b>Report of the With-Profits Actuary (5 March 2019)</b>	SWL WPA
<b>Communications MI</b>	Deputy SWL Chief Actuary
<b>Communications Training Pack</b>	Deputy SWL Chief Actuary
<b>Detailed objections logs</b>	Deputy SWL Chief Actuary
<b>Query and objections response library</b>	Deputy SWL Chief Actuary
<b>Financials as at 30 June 2018</b>	Deputy SWL Chief Actuary
<b>Estimated Financials as at 31 December 2018</b>	Deputy SWL Chief Actuary
<b>Solvency Monitoring as at 31 January 2019</b>	Deputy SWL Chief Actuary
<b>SWE Luxembourg GAAP Assumptions document (18 January 2019)</b>	Deputy SWL Chief Actuary
<b>Legal advice on Cross Border Business After Brexit</b>	HSF
<b>Legal advice on Scope of the FSCS protection – Independent Expert’s queries</b>	HSF
<b>Amended CM WPF PPFM</b>	Deputy SWL Chief Actuary
<b>COBS Review (20 February 2019)</b>	Deputy SWL Chief Actuary
<b>COBS EY Regulatory Report (20 February 2019)</b>	Deputy SWL Chief Actuary
<b>CAA authorisation letter for SWE (1 February 2019)</b>	Deputy SWL Chief Actuary
<b>CAA authorisation letter for the CEO of SWE (1 February 2019)</b>	Deputy SWL Chief Actuary

<b>CAA letter on UK FOS decisions as requested by FCA (12 February 2019)</b>	Deputy SWL Chief Actuary
<b>SWE Board Meeting Agenda</b>	Deputy SWL Chief Actuary

I have checked that the information listed above has been audited or supplied by an Approved Person or by a person appropriately qualified to provide such information and I am satisfied that it is reasonable for me to rely on this information.

## B Certification for changes to the 2015 Scheme

Certificate for the amendments made to the 2015 Scheme under which all UK life insurance and pensions business of LBG including those from SW were consolidated into CMIG via a Part VII Transfer as sanctioned by the High Court with effect from 31 December 2015.

I certify that, in my opinion, the proposed amendments to the 2015 Scheme will not have a material adverse effect on the security or benefit expectations of the policyholders of SWL. This includes reinsured policyholders. In coming to this opinion, I have taken account of the proposals as a whole and their impact on the Non-transferring Policies and Transferring Policies as a whole.

This certification replaces that in Appendix F of the Report.

A handwritten signature in black ink, appearing to read 'TR', is positioned above the typed name 'Tim Roff'.

Tim Roff

Independent Expert appointed by Scottish Widows Plc

06 March 2019

## C Glossary

Term	Definition
<b>2015 Scheme</b>	The Part VII Transfer undertaken in 2015 by Lloyds Banking Group to consolidate all UK life insurance and pensions business into Clerical Medical Investment Group (which was then renamed Scottish Widows Limited)
<b>APS</b>	Actuarial Practice Standards
<b>Asset</b>	Generally, any item of property whether tangible or intangible, that has financial or monetary value
<b>Associated Arrangements</b>	Together the Reinsurance Agreement, Charge Agreement, Unit Linked Service Agreement and Indemnity Agreement.
<b>BEL</b>	Best Estimate Liabilities
<b>Board</b>	The Board of Directors, which is a governing body of an entity.
<b>Brexit</b>	The term used to describe the UK's exit from the EU, following the vote taken in the EU referendum on 23 June 2016
<b>CAA</b>	Insurance Commission (Commissariat aux Assurances). The regulator responsible for the supervision of the insurance sector in Luxembourg.
<b>Capital requirements</b>	The level of funds that an insurance or reinsurance undertaking is required to hold in excess of its liabilities.
<b>CEO</b>	Chief Executive Officer
<b>Charge Agreement</b>	The floating charge agreement between SWL and SWE, to allow the Transferring Policyholders similar rights to Non-Transferring Policyholders upon the insolvency of SWL.
<b>CM</b>	Clerical Medical
<b>CM WPF</b>	CM With-Profits Fund. This is one of two ring-fenced funds for with-profits policies within SWL. See WPF for further details.
<b>CM WPF PPFM</b>	CM WPF Principles and Practices of Financial Management. The specific Principles and Practices of Financial Management for the CM WPF. See PPFM for further details.
<b>CMIG</b>	Clerical Medical Investment Group. In 2015, CMIG was renamed Scottish Widows Limited (SWL).
<b>CMIL</b>	CMI Insurance (Luxembourg) S.A. A previous Luxembourg subsidiary of SWG. All of CMIL's policies were transferred to CMIG (now SWL) on 31 December 2015 by Ministerial Decree.

<b>CMP</b>	Capital Management Plan
<b>COBS</b>	Conduct of Business Sourcebook. This details the FCA's requirements with regard to the conduct of UK insurance companies (among other entities).
<b>Combined fund</b>	That part of SWL's insurance funds not represented by the CM WPF and SW WPF. Whereas most of the profits made within the CM WPF and SW WPF are allocated to policyholders, all of the profits made within the Combined Fund belong to shareholders.
<b>Credit rating</b>	A measure of the financial security of a company provided by a third party agency
<b>CRO</b>	Chief Risk Officer
<b>Customer Treatment Policy</b>	This policy outlines the appropriate treatment of customers within all LBG operations.
<b>EEA</b>	European Economic Area
<b>Estate</b>	Difference between the value of the assets within a with-profits fund and the best estimate liabilities of the fund
<b>EU</b>	European Union
<b>EU passporting rights</b>	The collective term for Freedom of Establishment and Freedom of Services.
<b>FCA</b>	Financial Conduct Authority. The FCA's responsibilities include the regulation of conduct of UK insurers.
<b>FOS</b>	Financial Ombudsman Service. An independent body set up to deal with individual complaints that consumers and financial businesses are not able to resolve themselves
<b>FRC</b>	Financial Reporting Council
<b>Freedom of Establishment</b>	The right of an insurer located in one EEA member state to underwrite a risk located in another EEA member state by establishing a permanent presence in that EEA member state. This permanent presence can be in the form of a local branch or agency. Freedom of Establishment business is business underwritten under a full binding authority where the policyholder and the risk are located in the same EEA member state outside the UK.
<b>Freedom of Services</b>	The right to provide business services on a cross-border basis within the EEA. For insurance contracts, this means that the contract can be underwritten in an EEA member state that is different from the member state where the risk is located. Freedom of Services business consists of open market business written from the UK (with or without the involvement of a local intermediary), business written under a full binding authority where the policyholder is located in a different member state from

	where the risk is located and business that is written under a prior submit binding authority agreement.
<b>FSCS</b>	Financial Services Compensation Scheme. FSCS is a statutory “fund of last resort” which provides compensation in the event of the insolvency of a financial services firm authorised by the PRA or FCA. Insurance protection exists for private policyholders and small businesses (those with an annual turnover of less than £1,000,000) in the situation when an insurer is unable to meet fully its liabilities. For long term insurance policies, the FSCS will pay 100% of any eligible claim. The FSCS is funded by levies on firms authorised by the PRA and FCA.
<b>FSMA</b>	Financial Services and Markets Act 2000 (as amended)
<b>FWH</b>	Funds Withheld. When SWE reinsures the investment element of the Transferring UWP Policies and with-profits annuities, it holds back the reinsurance premium as FWH. The FWH provides security for SWE against the possibility of SWL becoming insolvent and defaulting on reinsurance claims owed to SWE.
<b>GAAP</b>	Generally Accepted Account Principles. This is a collection of commonly-followed accounting rules and standards for financial reporting.
<b>German business litigation claims</b>	The outstanding and potential claims relating to certain (Transferring) policies sold by independent intermediaries in Germany prior to the Transfer.
<b>GGF</b>	Guaranteed Growth Funds. The funds that UWP Transferring Policyholders invested in: these funds currently form part of the CM WPF.
<b>Grant Thornton</b>	Grant Thornton UK LLP
<b>Green zone</b>	Capital levels above the target SCR Cover Ratio as defined within the Capital Management Plan, (ie enough capital to cover the regulatory capital requirements as well as the firm’s internal capital requirement) is considered to be within the Green zone.
<b>Group</b>	Lloyds Banking Group plc (LBG)
<b>Indemnity Agreement</b>	The agreement entered into between SWE and SWL in relation to litigation claims against SWL prior to the Transfer.
<b>Independent Expert</b>	Tim Roff FIA
<b>Insurance Group</b>	Scottish Widows Group (SWG)
<b>Insurance Board</b>	SWG’s insurance Board, also known as SWG Board
<b>Internal contagion rules</b>	The rule set out in Rule 9.1 of the Conditions Governing Business part of the PRA Rulebook which prohibits an insurer from carrying on any commercial business other

	than insurance business and activities directly arising from that business
<b>LBG</b>	Lloyds Banking Group plc, also known as the Group
<b>LB</b>	Lloyds Bank plc
<b>LB Europe</b>	Lloyds Bank GmbH
<b>LOS</b>	Luxembourg Ombudsman Service. A collective name (within this report) for NCOS, ACA and CAA mediation services.
<b>Liability</b>	A claim against the assets, or legal obligations of a person or organisation, arising out of past or current transactions or actions
<b>Material adverse impact</b>	A negative change that is considered to have a material impact on policyholders. For any group of policyholders, there may be some changes for the better and some for the worse. If there are some changes for the worse this does not necessarily mean that the Transfer is unfair or unreasonable, as they might be either outweighed by other benefits, or they might be extremely small. Where there are adverse changes this report attempts to give some context as to their size or likelihood of occurring. If a potential effect is very unlikely to happen and does not have a large impact, or if it is likely to happen but has a very small impact, it is not considered to be material.
<b>Non-transferring Business/Policies/Policyholders</b>	Business/policies/policyholders of SWL that will remain with SWL and not transfer to SWE as a result of the Scheme.
<b>NPF</b>	Non-Profit Fund. That part of a life insurer's insurance funds not represented by WPFs. SWL's NPF is known as the Combined Fund.
<b>ORSA</b>	Own Risk and Solvency Assessment. An internal risk management tool/process/report to assess the overall solvency needs of the firm taking into account the firm's own assessment of its specific risk profile. The ORSA is often referred to as Pillar 2 of the Solvency II regime.
<b>Own Funds</b>	The excess of an insurer's admissible assets over its liabilities on a Solvency II basis
<b>Parent</b>	An enterprise that controls another through ownership of 50 percent or more of its voting stock.
<b>PPFM</b>	Principles and Practices of Financial Management. In managing with-profits business firms rely on their use of discretion. The PPFM explains the nature and extent of discretion available and how this discretion will be applied across different groups and generations of with-profits policyholders

<b>PRA</b>	Prudential Regulation Authority. The PRA's responsibilities include the prudential regulation of UK insurers, ie regulation relating to the ongoing solvency of UK insurers.
<b>Reinsurance</b>	An arrangement with another insurer or reinsurer whereby risks are shared (or passed on) to the reinsurer.
<b>Reinsurance Agreement</b>	The reinsurance agreement between SWL and SWE as a part of the transfer of business from SWL to SWE. The Reinsurance Agreement reinsures the investment element of the Transferring UWP Business from SWE back to SWL and with-profits annuities (both the small number of vested annuities as at 31 December 2017 and any future vesting with-profits annuities on the Transferring Business).
<b>Relevant Person</b>	Firms authorised by the PRA which are participant firms in FSCS
<b>Run-off</b>	The remaining lifetime of a block of insurance business that still needs servicing despite gradually declining in size as a result of no new business being written.
<b>SCR</b>	Solvency Capital Requirement. The capital regulatory requirement under Pillar 1 of the Solvency II regime. The SCR can be calculated using the Standard Formula or using a firm's own Internal Model.
<b>SCR Cover Ratio</b>	The ratio of Own Funds to SCR.
<b>Solvency I</b>	Solvency I was the regulatory regime for insurance companies in the UK that was superseded by Solvency II.
<b>Solvency II</b>	A new regulatory regime for insurers which came into force on 1 January 2016 aimed at harmonising regulation across all EU and EEA countries
<b>Subsidiary</b>	An enterprise controlled by another (called the parent) through the ownership of greater than 50 percent of its voting stock
<b>Successor</b>	A firm who has assumed liabilities from a UK authorised insurer including acts or omissions under those liabilities
<b>SUP 18</b>	Chapter 18 of the Supervision Manual of the FCA's Handbook of Rules and Guidance
<b>Supplementary Report</b>	An additional report produced by the Independent Expert to reflect any updated financial information or any other matter which has come to light since the issue of the Report.
<b>SW</b>	Scottish Widows
<b>SW WPF</b>	Scottish Widows' With-Profits Fund
<b>SWE</b>	Scottish Widows Europe SA

<b>SWG</b>	Scottish Widows Group, also known as the Insurance Group
<b>SWG Board</b>	The Board of SWG, also known as Insurance Board
<b>SWL</b>	Scottish Widows Limited
<b>TAS</b>	Technical Actuarial Standards. TAS 100 covers Principles for Technical Actuarial Work, TAS 200 is for Insurance
<b>Technical provisions</b>	The insurance liabilities of an insurer, as determined for regulatory purposes. These are calculated as the provisions for the ultimate costs of settling all claims arising from events which 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 claims arising on unexpired periods of exposure less any premium in respect of the business written that has not yet been received
<b>Terms of Reference</b>	Sets out the scope and limitations of an agreement.
<b>The Effective Date</b>	29 March 2019 or such other time and date as SWL and SWE may agree, being a date and time after the making of the Order sanctioning the Scheme
<b>The High Court</b>	The High Court of Justice of England and Wales
<b>The Report</b>	The report from the Independent Expert
<b>The Scheme</b>	The legal document that sets the terms of transfer of insurance business from SWL to SWE.
<b>The Transfer</b>	The Scheme, the Reinsurance Agreement, the Charge Agreement, the Unit Linked Service Agreement and the Indemnity Agreement.
<b>Tied Assets</b>	Tied Assets are a requirement under Luxembourg regulation. These assets are required to be deposited into a custodian bank following a tripartite custodian agreement with the CAA. The amount of assets deposited is equal to the greater of the Solvency II technical provisions and the reserves under Luxembourg GAAP.
<b>Transferor</b>	Scottish Widows Limited
<b>Transferring Business</b>	Existing business originally written in EU countries that will be transferred to Scottish Widows Europe SA, a new subsidiary established by Scottish Widows Limited, once authorised.
<b>Transferring Business/Policies/Policyholders</b>	Business/Policies/Policyholders who will be transferred as a result of the Scheme.
<b>Transferring UL Business/Policies/Policyholders</b>	Unit-linked business within the Transferring Business/Policies/Policyholders

<b>Transferring UWP Business/Policies/Policyholders</b>	Unitised with-profits business within the Transferring Business/Policies/Policyholders. This includes Business/Policies/Policyholders currently invested in Guaranteed Growth Funds (GGFs) which reside in SWL's Clerical Medical with-profits fund (CM WPF) This group includes with-profits annuities (both the small number of vested annuities as at 31 December 2017 and any future vesting with-profits annuities on the Transferring Business).
<b>UK</b>	United Kingdom
<b>The UK Regulators</b>	The PRA and the FCA
<b>UL</b>	Unit-Linked.
<b>Unit Linked Service Agreement</b>	The agreements between SWE and LB to enable the operations of the Transferring UL Business to be managed in the same way before and after the Transfer.
<b>UWP</b>	Unitised With-Profits.
<b>WPF</b>	With-profits Fund. A segregated fund within an entity's insurance fund and the fund within which most (or all) of the profits are distributed to with-profits policyholders



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