



The Part VII transfer of the business of AXA Wealth Limited to Phoenix Life Limited

The report of the Independent Expert

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1 INTRODUCTION

Background to the proposed transfer that is the subject of this report

- 1.1 On 1 November 2016, AXA Wealth Limited (“AWL”) was acquired by the Phoenix Group and AWL is currently one of the UK regulated life insurance companies in the Phoenix Group.
- 1.2 The Phoenix Group specialises in the management and acquisition of closed life and pensions funds, and operates primarily in the UK.
- 1.3 It is proposed to transfer all the business of AWL into another regulated life insurance company in the Phoenix Group, Phoenix Life Limited (“Phoenix”) under Part VII of the Financial Services and Markets Act 2000 (“FSMA”).
- 1.4 In order to replicate the economic effects of the proposed transfer, two reinsurance treaties were put in place between AWL and Phoenix and these are collectively referred to as the Intra-Group Reinsurance (“IGR”).
- 1.5 The transfer is expected to be presented to the High Court of Justice of England and Wales (the “Court”) for its Directions Hearing on 24 July 2017 and for a Final Hearing on 21 November 2017.
- 1.6 If approved by the Court, the Scheme will become operative on 8 December 2017 (the “Transfer Date”), at which point the transferring business will legally transfer from AWL to Phoenix. The Scheme provides that it will take effect as between AWL and Phoenix, including for accounting purposes and for determining the levels of policyholder benefits, from 1 October 2017 (the “Effective Date”).

The report of the Independent Expert

- 1.7 When an application is made to the Court for an order to sanction the transfer of insurance or reinsurance business from one insurer to another, the application is subject to Part VII of FSMA and approval by the Court under Section 111 of FSMA.
- 1.8 Section 109 of FSMA requires that the application to Court must be accompanied by a report on the terms of the proposed transfer scheme by an Independent Expert.
- 1.9 I have been appointed by Phoenix and AWL to report, pursuant to Section 109 of FSMA, in the capacity of the Independent Expert, on the terms of the proposed scheme providing for the transfer of the entire business of AWL to Phoenix and my fees will be borne by Phoenix.
- 1.10 The purpose of this report is therefore to review the proposed transfer of the business of AWL to Phoenix and, in particular, to consider the impact of the proposed transfer on the policyholders of AWL and Phoenix.
- 1.11 In this report (“my report”) I refer to the proposed scheme as “the Scheme”, or “this Scheme” and throughout the remainder of this report, these terms are used to cover all the proposals included in the scheme of transfer, including any documents referred to therein relating to the proposed implementation and operation of the scheme of transfer.
- 1.12 The Scheme will be presented to the Court for sanction under Section 111 of FSMA.

The scope of my report

- 1.13 My terms of reference have been reviewed by the Financial Conduct Authority (the “FCA”) and the Prudential Regulation Authority (the “PRA”).
- 1.14 My report has been prepared in accordance with the approach and expectations of the PRA, as set out in “The Prudential Regulation Authority’s approach to insurance business transfers” dated April 2015 (the “PRA Statement of Policy”), as well as Chapter 18 of the Supervision Manual (“SUP 18”) contained in the FCA Handbook.
- 1.15 My report considers the consequences of the Scheme for those policyholders likely to be affected by the implementation of the Scheme: principally the policyholders of AWL and Phoenix.
- 1.16 I understand that an equivalent scheme (the “Guernsey Scheme”) will be presented to the Royal Court of Guernsey in relation to any policies issued by AWL to residents of Guernsey or policies which may otherwise constitute Guernsey long-term insurance business. This report will therefore also be presented to the Royal Court of Guernsey to satisfy the requirement for a report by an independent actuary on the terms of the Guernsey Scheme.

- 1.17 I confirm that the comments and conclusions in this report apply to all policyholders of AWL and Phoenix irrespective of their place of residence and/or the jurisdiction within which the business is said to be carried on or in which their policy was issued. References to the “Scheme” should be taken to include the Guernsey Scheme.
- 1.18 My report will be presented to the Court and will be made available to policyholders via the Phoenix website (www.phoenixlife.co.uk), the SunLife website (www.sunlife.co.uk), and the Phoenix Wealth website (www.phoenixwealth.co.uk). A summary of my report (or, in certain cases, my full report) will be included in the communications pack that is sent to policyholders.
- 1.19 There are no documents or other information that I have requested and that have not been provided. Appendix 4 contains a list of the data upon which I have relied.
- 1.20 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Scheme and in preparing my report, but that nonetheless should be drawn to the attention of policyholders in their consideration of the terms of the Scheme.

Qualifications and disclosures

- 1.21 I am a Fellow of the Institute and Faculty of Actuaries and hold certificates issued by the Institute and Faculty of Actuaries enabling me to act as a Chief Actuary and a With-Profits Actuary.
- 1.22 I am a partner of Milliman LLP (“Milliman”) and I am based in its UK Life Insurance and Financial Services practice. I am an approved person on the Financial Services Register and I currently hold a number of Chief Actuary and With-Profits Actuary roles. I have fulfilled the role of Independent Expert in relation to a number of Part VII transfers that have subsequently been approved by the Court.
- 1.23 My appointment as the Independent Expert was approved by the PRA (after consulting with the FCA) in a letter dated 14 March 2017 to Phoenix.
- 1.24 I submitted a statement of independence to the PRA and FCA for review before my approval and this statement of independence has been approved by the PRA and FCA. In this statement I have set out why I believe I am able to act independently in relation to this assignment. In particular:
- I am not a shareholder in the Phoenix Group, including their subsidiaries. I hold no individual policies issued by either company or their subsidiaries and I am not a member of any of the pension schemes under the management of the Phoenix Group.
 - Work carried out for the Phoenix Group and its subsidiaries worldwide by Milliman represented less than 1% of Milliman’s global revenue between 2014 and 2016 inclusive.
- 1.25 I confirm that neither I nor Milliman LLP have or have had any direct or indirect interest in any of Phoenix, AWL or other related firms that could influence my independence.

The parties for whom the report has been prepared

- 1.26 This report, and any extract or summary thereof has been prepared particularly for the use of:
- The Court;
 - The Royal Court of Guernsey;
 - The Directors and senior management of AWL;
 - The Directors and senior management of Phoenix;
 - The FCA and the PRA, and any governmental department or agency having responsibility for the regulation of insurance companies in the UK;
 - The Guernsey Financial Services Commission;
 - The insurance regulator of any EEA country who requests a copy of the report; and
 - The professional advisers of any of the above.
- 1.27 In accordance with the legal requirements under FSMA, copies of my report may be made available to the policyholders of AWL and Phoenix and to other interested parties.

Limitations

- 1.28 In preparing my report, I have had access to certain documentary evidence provided by AWL and Phoenix, the key elements of which are listed in Appendix 4. I have also had access to, and discussions with, senior management of AWL and Phoenix. My conclusions depend on the substantial accuracy of this information and I have relied on this information without independent verification. I have considered, and am satisfied with, the reasonableness of this information based upon my own experience across the UK life assurance industry.
- 1.29 This report must be considered in its entirety as individual sections, if considered in isolation, may be misleading. Draft versions of this report should not be relied upon for any purpose. I have provided summaries of my report for inclusion in various communications with different groups of policyholders (and, where relevant, distribution to any persons requesting a copy of it). Any other purported summary of my report or elements within my report should not be treated as having been approved or authorised by me.
- 1.30 This report has been prepared on an agreed basis for AWL and Phoenix in the context of the Scheme and must not be relied upon for any other purpose. No liability will be accepted by Milliman, or me, for any application of my report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of the report. In particular, no liability will be accepted by Milliman or me under the terms of the Contracts (Rights of Third Parties) Act 1999.

The Technical Actuarial Standards (“TAS”)

- 1.31 My report has been prepared subject to the terms of the TAS applicable to Insurance transformations (“TAS 200: Insurance”) issued by the Financial Reporting Council. In my opinion, my report complies with the TAS 200: Insurance and is compliant with those elements of the TAS 100: Principles for Technical Actuarial Work that are applicable to transformations. In complying with these requirements, I note that a number of the key documents listed in Appendix 4 have been prepared or reviewed by individuals who were subject to professional standards in undertaking their work, including, where appropriate, TAS requirements.

The Actuarial Profession Standards (“APS”)

- 1.32 APS X2, as issued by the Institute and Faculty of Actuaries, requires members to consider whether their work requires an independent peer review.
- 1.33 In my view this report does require independent peer review and this has been carried out by a senior actuary in Milliman LLP who has not been part of my team working on this assignment.

The structure of my report

- 1.34 Section 2 provides some background information on the regulatory regime in the UK, and Section 3 describes the background on the financial information used in this report.
- 1.35 Section 3 of this report covers the role of the Independent Expert for a Part VII transfer of long-term insurance business in the UK.
- 1.36 Sections 5 and 6 provide background to AWL and Phoenix respectively and Section 7 provides a summary of the key aspects of the Scheme.
- 1.37 The effects of the implementation of the Scheme on the policies of AWL and Phoenix and on the holders of these policies, as well as the effects on other stakeholders, are covered in Sections 8 and 9.
- 1.38 Section 10 contains my considerations in respect of the conduct of insurance business and the treatment of customers, and Section 11 addresses certain other considerations arising from the Scheme.
- 1.39 Section 12 contains my conclusions on the Scheme.

The appendices contain financial information relevant to the companies involved in the Scheme, some relevant background information and, at Appendix 5, a glossary of defined terms and abbreviations used in my report.

2 THE UK LIFE INSURANCE MARKET AND REGULATORY ENVIRONMENT

Introduction

2.1 The regulatory regime to which UK insurers are subject, and the applicable solvency requirements, are relevant to my considerations as Independent Expert and the UK regulatory environment for insurance companies is summarised in this section.

The UK regulators

2.2 Since 1 April 2013, responsibility for the regulation of insurance companies has been split between the PRA and the FCA.

2.3 The PRA is a part of the Bank of England, and carries out the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.

2.4 The PRA has statutory objectives to promote the safety and soundness of the insurers that it regulates, and to contribute to ensuring that policyholders are appropriately protected. More generally, these statutory objectives can be advanced by seeking to ensure that regulated insurers have resilience against failure and that disruption to the stability of the UK financial system from regulated insurers is minimised.

2.5 The FCA regulates the conduct of all financial services firms in relation to consumer protection, market integrity and the promotion of competition in the interests of consumers.

The Financial Services Compensation Scheme (“FSCS”) and Financial Ombudsman Service (“FOS”)

2.6 The FSCS provides compensation to individual holders of long-term insurance policies issued by UK insurers in the UK or another EEA state who are eligible for compensation under the FSCS in the event of the insurer’s default.

2.7 The FOS is an independent public body that aims to resolve disputes between individuals and UK financial services companies, and may make compensation awards in favour of policyholders. Only holders of policies that constitute business carried on in the UK are permitted to bring complaints to the FOS.

The products and long-term insurance business relevant to the proposed Scheme

2.8 AWL and Phoenix have a wide variety of in-force long-term insurance policies.

2.9 Phoenix’s policies include both with-profits and non-profit life and pension policies.

2.10 The transferring AWL policies are all non-profit life and pension policies consisting of:

- Whole of life policies: these provide a guaranteed lump sum upon the death of the policyholder.
- Term assurance policies: these provide a guaranteed lump sum upon the death of the policyholder before the end of a defined term.
- Unit-linked life and pension policies: the policyholders’ investments or premiums buy units whose price rises and falls with the value of the underlying assets.
- Corporate trustee investment plans (“CTIP”): these are unit-linked policies providing fund management for registered pension schemes – the policyholder is the trustees of the pension scheme.

2.11 All transferring policies are non-profit in nature so the benefits payable to policyholders are not eligible to be amended or increased by discretionary bonuses.

The Solvency II regulatory regime

Introduction

2.12 A new regulatory solvency framework for the European Economic Area (“EEA”) insurance and reinsurance industry came into effect on 1 January 2016. This new regime is known as Solvency II and aims to introduce solvency requirements that better reflect the risks that insurers and reinsurers actually face and to introduce consistency

across the EEA. All but the smallest EEA insurance companies are required to adhere to a set of new, risk-based capital requirements and the results will be shared with the public.

2.13 Solvency II is based on three pillars:

- Under Pillar 1, quantitative requirements define a market consistent¹ framework for valuing the company's assets and liabilities, the results of which will be publicly disclosed.
- Under Pillar 2, insurers must meet minimum standards for their corporate governance and their risk and capital management. There is a requirement for permanent internal audit and actuarial functions. Insurers must regularly undertake a forward looking assessment of risks, solvency needs and adequacy of capital resources, called the Own Risk and Solvency Assessment ("ORSA"), and senior management must demonstrate that the ORSA actively informs business planning, management actions and risk mitigation.
- Under Pillar 3, there are explicit requirements governing disclosures to supervisors and policyholders. Firms will produce private reports to supervisors and a public solvency and financial condition report.

The Pillar 1 requirements

- 2.14 The determination of a market consistent value of liabilities under Solvency II requires the insurer to calculate the best estimate liabilities ("BEL"). The expected future obligations of the insurer are projected over the lifetime of the contracts using the most up-to-date financial information and the best estimate actuarial assumptions, and the BEL represents the present value of these projected cash-flows.
- 2.15 Under Solvency II, a company's Pillar 1 liabilities are called the "technical provisions" which consist of the sum of the BEL and the "risk margin". The risk margin is an adjustment designed to bring the technical provisions up to the amount that another insurance or reinsurance undertaking would be expected to require in order to take over and meet the insurance obligations in an arm's length transaction.
- 2.16 Assets are, broadly speaking, reported at market value under Pillar 1.
- 2.17 The Solvency Capital Requirement ("SCR") under Solvency II is the capital requirement under Pillar 1, and is intended to be the amount required to ensure that the firm's assets continue to exceed its technical provisions over a one year time frame with a probability of 99.5%.
- 2.18 The Minimum Capital Requirement ("MCR"), which is lower than the SCR, defines the point of intensive regulatory intervention. The MCR calculation is simpler, more formulaic and less risk-sensitive than the SCR calculation.
- 2.19 In calculating the SCR, it is expected that most firms will use the "Standard Formula", as prescribed by the European Insurance and Occupational Pensions Authority ("EIOPA"). However, Solvency II also permits firms to use their own internal models (or a combination of a "partial internal model" and the Standard Formula) to derive the SCR. These internal models and partial internal models are subject to approval by the relevant regulator: in the UK this is the PRA.
- 2.20 On 9 March 2015, "The Solvency 2 Regulations 2015" were laid before the UK Parliament. These regulations implement, in part, the Solvency II Directive (as amended by the subsequent Omnibus II Directive) into UK law and came into force on 1 January 2016.
- 2.21 The remainder of the Solvency II Directive has been implemented by the FSMA, by rules and binding requirements imposed by the PRA and the FCA, and by directly applicable regulations made by the European Commission. The PRA has issued final statements on the transposition of Solvency II, as amended by the Omnibus II Directive, into the UK national framework. These set out its approach to the prudential regulation, and its expectations, of firms subject to Solvency II.
- 2.22 EIOPA has published the implementing technical standards ("ITS") and guidelines for the new regime and these have been endorsed by the European Commission, are legally binding and apply to all national regulators under the scope of Solvency II.
- 2.23 Many of the technical requirements of Solvency II are contained in Commission Delegated regulation (EU) 2015/35, known as the Delegated Acts, adopted by the European Commission in October 2014.

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

Own funds and capital

- 2.24 Under the Solvency II regime, the excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds. Own Funds can be thought of as the capital available in the company to cover capital requirements.
- 2.25 Under Solvency II, companies are required to classify their Own Funds into three tiers, which broadly represent the quality of the Own Funds in relation to their ability to absorb losses. The Own Funds of the highest quality are classified as Tier 1. In order to be classified as Tier 1, Own Funds must exhibit both of the following:
- Permanent availability, i.e. the item is available, or can be called up on demand, to fully absorb losses on a going concern basis, as well as in the case of winding up.
 - Subordination, i.e. in the case of winding up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations towards policyholders and beneficiaries of insurance and reinsurance contracts, have been met.
- 2.26 Own Funds that are classified as Tier 2 or Tier 3 are of a lower quality, with less ability to fully absorb losses.

Approvals required from the PRA

- 2.27 Any UK firms intending to use an internal model, transitional measures, a matching adjustment or a volatility adjustment (as described in the paragraphs below) must apply to the PRA for approval.
- 2.28 Applications have been accepted by the PRA since 1 April 2015 and the outcome of firms' applications for measures to take effect from 1 January 2016 was communicated by the PRA in late 2015.
- 2.29 Under the Solvency II regulations, the PRA has the right to remove approvals for the use of any of these measures, if the firm is found to be in breach of the restrictions and conditions on which the original approval was based.
- 2.30 Firms must apply to the PRA if they wish to make changes to the terms of their existing approvals. For example, firms would seek approval from the PRA to make a major change to their internal model and would not be expected to submit more than one major change application per year. A major change can comprise a single change or an accumulation of minor changes that, in aggregate, comprise a major change.
- 2.31 Additionally, firms are permitted to seek approval to undertake a recalculation of their transitional measure every six months if their risk profile has changed materially since the previous recalculation.

The matching adjustment

- 2.32 In calculating the BEL, the Solvency II rules permit firms to apply to their regulator to make use of the "matching adjustment". The matching adjustment is an increase to the discount rate used in the calculation of the BEL that allows firms to take credit for the additional investment return in excess of the risk free rate (swap rates under Solvency II) that they expect to earn from a "hold to maturity" investment strategy for their less liquid assets, which are used to back their most stable and predictable liabilities, typically non-profit in-payment annuity liabilities.
- 2.33 Firms using the matching adjustment are subject to various restrictions around the types of asset that are permitted to back the relevant liabilities, the circumstances in which the assets may be traded, and the extent to which mismatching of asset and liability cash flows is permitted.

The volatility adjustment

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

The transitional measures

- 2.36 Insurers are also permitted to apply to their regulator (the PRA in the UK) to make use of transitional measures. Transitional measures allow firms to phase in the balance sheet impact of moving from the former Solvency I regulatory regime to the Solvency II regulatory regime. The transitional measures can be applied in one of two ways:

- The Transitional Measure on Technical Provisions (“TMTP”) allows firms to phase in the increase in technical provisions under Solvency II Pillar 1 (in relation to business written prior to 1 January 2016) over a sixteen year period. In the UK, the increase is measured relative to the firm’s Solvency I Pillar II liabilities.
- The Transitional Measure on the Risk-Free Interest Rate allows firms to phase in any reduction in the discount rate used to calculate their liabilities under Solvency II relative to the previous regime over a sixteen year period.

- 2.37 For a given firm, the TMTP is calculated as at the implementation date of Solvency II, i.e. 1 January 2016. The TMTP is calculated as the difference, to the extent that this difference is a positive number, between the firm’s technical provisions under Solvency II and the firm’s insurance liabilities under the previous Pillar II regime.
- 2.38 A further test is then carried out to determine whether deducting the calculated TMTP from the firm’s Solvency II technical provisions at 31 December 2015 would result in a Financial Resources Requirement (“FRR”) under Solvency II that is lower than the firm’s FRR under the previous Pillar I and Pillar II regimes at the same valuation date.
- 2.39 The FRR for a given solvency regime is calculated as the total liabilities plus the firm’s capital requirement under that regime. If the Solvency II FRR after deduction of the TMTP is lower than the FRR under the Solvency I regime (Pillar I and Pillar II) then the calculated TMTP must be reduced to a level that ensures that this is no longer the case. The purpose of the FRR test is to ensure that firms are not able to hold lower amounts of financial resources under Solvency II than under the Solvency I regime as a result of the use of the TMTP.
- 2.40 The final calculated TMTP is deducted from the firm’s technical provisions in its Solvency II balance sheet at 1 January 2016. For valuation dates after 1 January 2016, the TMTP that was calculated at 1 January 2016 is reduced linearly to zero over a sixteen year period.
- 2.41 The PRA has stated publicly² that it regards the financial benefit conferred by the TMTP as Tier 1 capital.
- 2.42 The Solvency II Directive provides for firms’ TMTPs to be subject to recalculation every two years, with more frequent recalculations permitted if the firm’s risk profile has materially changed, as described above.

Ring-fenced funds

- 2.43 Solvency II includes the concept of a ring-fenced fund. This refers to any arrangement where an identified set of assets and liabilities are managed as though they were a separate undertaking, meaning that there are restrictions on the extent to which surplus in the ring-fenced fund may be transferred to shareholders or used to cover losses outside the ring-fenced fund.
- 2.44 In the UK, many firms have set up ring-fenced funds in order to reflect the arrangements applicable to their with-profits funds (as defined under the previous regulatory regime) and the with-profits and non-profit business within the with-profits fund.

The long-term fund and shareholders’ fund

- 2.45 Prior to the implementation of Solvency II, proprietary firms writing long-term insurance business were required to identify the assets attributable to their long-term insurance business and keep those assets separate from shareholder funds in what was referred to as a long-term insurance fund (the “LTF”). The other assets of a proprietary company were typically allocated to the shareholders’ fund (the “SHF”). Under the PRA rules, the assets in the LTF were only available to be used to support the firm’s long-term insurance business and firms were required to maintain assets in the LTF sufficient in value to cover the fund’s mathematical reserves.
- 2.46 Following the implementation of Solvency II, the requirement to maintain a separate LTF has been removed and therefore a firm’s “fund structure” now consists of the ring-fenced funds and the business outside of the ring-fenced funds. This business outside the ring-fenced funds is often called the “non-profit fund” (if it is all long-term business) or the “shareholder backed fund” (this could include short-term or general insurance business) but whatever the name it includes the assets and liabilities of what were, under the previous regime, called the non-profit fund (in the LTF) and the shareholders’ fund (outside of the LTF).
- 2.47 Although not required to do so for regulatory purposes, some firms, including Phoenix, continue to maintain a notional fund for accounting purposes in respect of long-term business outside of the ring-fenced funds. Such a notional fund is sometimes referred to as the non-profit fund.

² <http://www.bankofengland.co.uk/publications/Pages/speeches/2015/829.aspx>

The treatment of the transferring policies under Solvency II

- 2.48 The business being transferred under the Scheme comprises premium-paying whole of life and term assurance policies and unit-linked life and pensions business.
- 2.49 The BEL for the whole of life and term assurance business under Solvency II is calculated as the present value of the expected claim and relevant expense outgo less the present value of expected premium income. This calculation identifies the extent to which assets need to be set aside to cover any excess of future outgo over income.
- 2.50 The AWL whole of life and term assurance business is expected to be profitable under best estimate assumptions as the present value of premiums is expected to exceed the present value of expected claim and expense outgo. This means that the aggregate BEL for these policies is negative and so these policies are treated as an asset rather than a liability.
- 2.51 For the unit-linked life and pensions business, including the CTIPs, the BEL is broadly calculated as the value of policyholders' units, plus any additional "non-unit" reserve required to cover future expenses that cannot be met by income from management charges levied on policyholders' units.
- 2.52 For the AWL transferring unit-linked business the present value of future income from management charges levied on the policyholders' units is expected to exceed the present value of the future expenses and therefore the non-unit reserve for the unit-linked life and pensions business is negative. This is often called a Present Value of Future Profits ("PVFP") item and is a negative contribution to the overall BEL.
- 2.53 For the whole of life, term assurance and the unit-linked transferring business, AWL must hold a risk margin and an SCR, both of which reduce the benefit of the negative contribution of the PVFP to the BEL.

The governance of UK long-term insurers

- 2.54 The Board of Directors of a long-term insurer is normally the firm's governing body, and is ultimately responsible for setting the strategic direction of the firm, overseeing the activities of the firm's day-to-day management and approving the firm's financial statements.
- 2.55 Under Solvency II, all insurers are required to establish the following key functions:
- Actuarial function: This function is required, inter alia, to coordinate the calculation of technical provisions, and to ensure the appropriateness of the methodologies, underlying models and assumptions used in the calculation of technical provisions.
 - Compliance function: This function is required, inter alia, to advise the insurer on compliance with the Solvency II regulations.
 - Internal audit function: This function is required, inter alia, to evaluate the adequacy and effectiveness of the insurer's internal control system and other elements of its system of governance. The Internal Audit Function is required to be objective and independent from the company's operational functions.
 - Risk management function: This function is required, inter alia, to facilitate the implementation of the insurer's risk management system.
- 2.56 These functions are not defined by the Solvency II regulations as being performed by an individual; however, in the UK, the PRA has introduced a new governance regime for UK insurers called the Senior Insurance Managers Regime ("SIMR") which became effective on 7 March 2016, and which defines a set of senior insurance management functions ("SIMF"), including:
- SIMF 1 - Chief Executive Officer ("CEO");
 - SIMF 2 - Chief Financial Officer ("CFO");
 - SIMF 4 - Chief Risk Officer ("CRO");
 - SIMF 20 - Chief Actuary;
 - SIMF 5 - Head of Internal Audit; and
 - SIMF 22 - Chief Underwriting Officer (general insurance firms only).

- 2.57 Under SIMR, the persons having responsibility for the actuarial function, internal audit function and risk management under Solvency II are the Chief Actuary, Head of Internal Audit and Chief Risk Officer respectively, and the individuals responsible for these functions will be subject to PRA approval.
- 2.58 In addition to the roles listed above, those firms with with-profits business must appoint an actuary (or actuaries) to perform the “with-profits actuary function”. This individual is the WPA, and his responsibilities include advising the firm’s management on the key aspects of the discretion to be exercised affecting those classes of the with-profits business of the firm in respect of which he has been appointed. The WPA role is SIMF 21 under SIMR.
- 2.59 Firms with with-profits business must appoint a With-Profits Committee (“WPC”) (or a “with-profits advisory arrangement” if appropriate given the size, nature and complexity of the fund in question) in respect of the with-profits business. The WPC’s role is to advise and provide recommendations to the firm’s governing body on the management of the with-profits business, and to act as a means by which the interests of with-profits policyholders are appropriately considered within a firm’s governance structures.

A firm’s risk appetite and internal capital policy

- 2.60 The Board of a firm is responsible for the management of the company and for its exposure to risk. The Board will typically set out its appetite for risk in a form which references the probability that the Board is willing to accept of not being able to pay policyholder liabilities as they fall due and/or meet regulatory requirements.
- 2.61 In order to ensure that day-to-day fluctuations in markets and experience do not lead to a breach of their risk appetite and regulatory capital requirements, firms usually aim to hold more capital than strictly required to meet the regulatory minimum. The details of the target level of capital buffer are typically set out in the firm’s internal capital policy.
- 2.62 The internal capital policy of a firm is set by and owned by the Board and describes the capital that the Board has determined should be held in the company. Changes to the internal capital policy usually require Board approval and appropriate consultation with the relevant regulator (the PRA in the UK).
- 2.63 The capital policy is typically stated in terms of the capital requirements set down by the relevant regulations. The regulatory capital requirements typically target a particular probability of remaining solvent over a certain time horizon: for example for the Solvency II regulatory regime it is a 99.5% probability of remaining solvent over a one year time horizon. By requiring additional capital to be held on top of the regulatory requirements, the capital policy increases the probability of remaining solvent over a particular timeframe and therefore increases the security of the benefits provided under the policies subject to the capital policy.
- 2.64 The level of capital required may also be driven by the desire of the Board to maintain a certain credit rating with external credit rating agencies.

3 THE ROLE OF THE INDEPENDENT EXPERT

Introduction

- 3.1 The UK legal and regulatory system can be described as providing four main layers of protection for policyholders in relation to insurance business transfers:
- The UK regulators (the PRA and the FCA):
 - Approve the appointment of the Independent Expert and the form of the Scheme Report;
 - Produce their own reports on the Scheme for consideration by the Court;
 - Are entitled to appear in Court; and
 - Approve the form of the notices which are published and sent to policyholders.
 - The Independent Expert: he/she produces the (publicly available) Scheme Report assessing the proposed Scheme and an updated supplementary report for the Final Hearing.
 - Obligations to give notice of the proposed transfer to policyholders and other interested parties, so that any person who considers they may be adversely affected by the proposed Scheme may make a representation to the Court.
 - The Court's review of the proposed Scheme in particular at the Final Hearing where the Court takes into account the views of the regulators, the Independent Expert, various statements by the parties to the transfer, and any objections raised by policyholders and other interested parties.
- 3.2 My role as Independent Expert, as the second layer of protection for policyholders described above, is to assess the proposed Scheme and to report on this via the Scheme Report (this report and any supplemental reports) to the Court. I set out below my significant areas of consideration in discharging this role.

The considerations of the Independent Expert

The regulatory requirements in respect of my role

- 3.3 The requirements in respect of my Scheme report are set out in the PRA Statement of Policy (paragraphs 2.27 to 2.40) and paragraphs 31 to 41 of section 2 of SUP 18, and my report complies with these documents.
- 3.4 In considering the proposed Scheme, the concept of treating customers fairly should be applied. From the policyholders' perspective, the successful implementation of the Scheme must be on the basis that they are treated fairly during the process and will be treated fairly in the future. To ensure that customers are treated fairly in the future, it is necessary to establish the ways in which customers have been treated in the past.
- 3.5 As described in Section 1 of this report, the Scheme concerns two life insurance companies: AWL and Phoenix. I need to consider the terms of the Scheme generally and how the different groups of policyholders of AWL and Phoenix and the different generations of policyholders within the different groups are likely to be affected by the implementation of the proposed Scheme. In particular I need to consider:
- The effect of the implementation of the Scheme on the security of the policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;
 - The effect of the implementation of the Scheme on the reasonable benefit expectations of policyholders; and
 - The effect of the implementation of the Scheme on the standards of service, administration, management and governance applicable to the policies.
- 3.6 My considerations in respect of each of these areas are set out in more detail below.
- 3.7 Although they are not direct policyholders of Phoenix or AWL, I have considered the interests of the members of pension schemes which have taken out policies with Phoenix and AWL and references to policyholders should be construed accordingly.
- 3.8 In this report I have not restricted my assessment of the Scheme to adverse effects.
- 3.9 I am only required to comment on the effects of the implementation of the proposed Scheme on policyholders who

enter into contracts with AWL and Phoenix prior to the Transfer Date of the Scheme. I am not required to consider the effects of the Scheme on new policyholders entering into contracts after this date.

- 3.10 I am not required to consider possible alternative schemes and I have therefore only considered the terms of the Scheme presented to me.

The security of policyholder benefits

- 3.11 As part of my role as Independent Expert for the Scheme, I need to consider the security of policyholder benefits, that is, the effect of the implementation of the Scheme on the likelihood that policyholders will receive their guaranteed benefits when these are due.

- 3.12 In considering and commenting upon policyholder security, I shall consider policyholders' guaranteed benefits, their exposures to different types of risk and, as appropriate, their reasonable benefit expectations.

- 3.13 The regulations require insurance companies to hold a minimum amount of capital in addition to the assets backing a realistic estimate of their liabilities to policyholders. Insurance companies must also demonstrate that they can fulfil their regulatory requirements and meet policyholder claims as they become due in adverse scenarios.

- 3.14 Therefore, the amount by which the assets available to support the long-term insurance business exceed the long-term liabilities provides security for the guaranteed benefits and security is also provided by other capital resources in the insurance company.

- 3.15 The two life insurance companies involved in the Scheme have a different mix of policies and policyholders and the type of policy held by a policyholder will be a key determinant of the risks to which the policyholder is exposed. Other than this, the key determinants of the policyholder's risk exposure will be the characteristics of the company in which the policy is held, for example:

- The size of the company;
- The amount and quality of capital resources available, other calls on those capital resources and capital support currently available to the company;
- The internal capital policy and risk appetite of the company;
- The investment strategy of the company;
- The mix of business of the company;
- The company's strategy, and governance around its objectives and strategy: for example, its acquisition and new business strategy; and
- Other factors, such as operational risks faced by the company, reinsurance agreements of the company, the company's governance framework and its tax position.

- 3.16 Some of these risks are company-specific, for example risks arising from the particular mix of business written or from the company's strategy, and some are common to various different groups of policyholders across the companies subject to the Scheme.

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

- 3.17 As Independent Expert, I also need to consider the proposals in the context of the FCA's regulatory objectives and, in particular, the effect of the implementation of the Scheme on policyholders' reasonable expectations in respect of their benefits and their levels of administration, servicing, management and governance in respect of their policies.

- 3.18 This includes considering the effect of the implementation of the Scheme on areas where discretion is involved on behalf of the relevant insurance company with regard to the charges applied to a policy and the benefits (including with-profits bonuses) granted to the policyholder.

The framework for the Independent Expert's consideration of the proposed Scheme

- 3.19 The framework for my conclusions is a consequence of the Court's consideration of prior schemes. In particular, principles stated by Evans-Lombe J. in *Re Axa Equity & Law Life Assurance Society plc* and *AXA Sun Life plc* (2001) (based on principles outlined by Hoffman J. in *Re London Life Association Ltd* (1989)) are often used as the

basis for the consideration of insurance business transfers by the Independent Expert and by the Court.

- 3.20 In particular, Evans-Lombe J. stated in *Re AXA Equity & Law* that “the court is concerned whether a policyholder, employee or other interested person or any group of them will be adversely affected by the scheme”. He went on to state: “That individual policyholders or groups of policyholders may be adversely affected does not mean that the scheme has to be rejected by the court. The fundamental question is whether the scheme as a whole is fair as between the interests of the different classes of persons affected”. The most common interpretation of these (and other relevant) statements has been that a conclusion that “no group of policyholders is materially adversely affected by the Scheme” provides a sufficient condition to conclude that the fairness of the Scheme as a whole has been demonstrated.
- 3.21 As Independent Expert, my assessment of the impact of the implementation of the Scheme on the various affected policies is ultimately a matter of actuarial judgement regarding the likelihood and impact of future possible events. Given the inherent uncertainty of the outcome of such future events and that the effects may differ across different groups of policies, it is not possible to be certain of the effect on the policies.
- 3.22 A Scheme may have both positive and negative effects on a group of policies and the existence of detrimental effects should not necessarily imply that the Court should reject the Scheme as the positive effects may outweigh the negative effects or the negative effects may be very small.
- 3.23 In order to acknowledge this inherent uncertainty, and to be consistent with the statements by the Court noted above, the conclusions of the Independent Expert in relation to transfers of long-term insurance business are usually framed using a materiality threshold. If the potential impact under consideration is very unlikely to happen and does not have a significant impact, or is likely to happen but has a very small impact, then it is not considered to have a material effect on the policies.
- 3.24 The assessment of materiality will also take into account the nature of the potential impact so that, for example, the materiality threshold for a change that could have a direct financial impact on policyholders’ guaranteed benefits is likely to be lower than the materiality threshold for a change that does not have a direct financial impact.
- 3.25 This is the framework in which I undertake my consideration of the proposed Scheme.

My reliance on legal advice

- 3.26 My report is prepared for the Court as part of the process of submission of the Scheme to the Court. I am not an expert in legal matters and hold no qualifications in UK law (insurance regulations or otherwise) and therefore rely on input from experts in UK insurance law in relation to a number of areas. In particular:
- I rely on a legal review of previous schemes to ensure that there are no provisions in previous schemes that could, in conjunction with the implementation of the proposed Scheme, result in a material adverse impact on policyholders; and
 - I rely on input from legal experts in order to ensure that my understanding of the proposed Scheme, and my description of its relevant features in my report, is accurate.
- 3.27 Obtaining the facts in respect of the operation of the Scheme from the legal experts provides a sound basis from which to carry out my review and analysis using actuarial expertise.
- 3.28 In order to get a sound legal understanding of the Scheme the options available to me are to retain my own legal adviser to carry out the relevant legal review, or to rely upon the advice and input of the legal firm retained by Phoenix in respect of this Scheme, namely Hogan Lovells International LLP (“Hogan Lovells”). In this case, I consider that it is not necessary for me to obtain independent legal advice, and that it is appropriate for me to rely upon the advice provided by Hogan Lovells. Hogan Lovells has not been retained by me and Hogan Lovells has no liability for any advice that they have provided that has been made available to me.
- 3.29 My reasons for this reliance are;
- Hogan Lovells is a large international legal firm with a wide range of experience in UK insurance law and Part VII transfers and it is my view that they have the relevant and appropriate qualifications and knowledge of the laws and regulations governing insurance business transfers in the UK.
 - The nature of the information and advice from Hogan Lovells upon which I have relied is factual and in particular concerns how a particular aspect of Phoenix or AWL (pre or post the implementation of the proposed Scheme) works in accordance with UK law. As such, I am satisfied that the advice or information given by Hogan Lovells would not be different if they were retained directly by me in respect of the proposed Scheme.

- For the same reason, I consider it unlikely that I would receive a different answer from a different (but similarly qualified) legal expert.

3.30 I am therefore comfortable that it is appropriate for me to rely on the conclusions of Hogan Lovells in forming my view on the Scheme.

My Supplementary Report

3.31 I will prepare a further report (the “Supplementary Report”) prior to the final Court Hearing to provide an update for the Court on my conclusions in respect of the effect of the proposed transfer on the different groups of policyholders in light of any significant events subsequent to the date of the finalisation of my main report.

3.32 My Supplementary Report will be available to policyholders on the Phoenix website (www.phoenixlife.co.uk), the SunLife website (www.Sunlife.co.uk), and the Phoenix Wealth website (www.phoenixwealth.co.uk).

4 THE FINANCIAL INFORMATION IN THIS REPORT

- 4.1 During 2015, the PRA granted approval to Phoenix to use the TMTP, the matching adjustment, and its internal model for Solvency II reporting.
- 4.2 Phoenix has, subsequent to the implementation of Solvency II, received approval from the PRA for three recalculations of its TMTP and for an extension to its matching adjustment.
- 4.3 The acquisition of AWL and the reinsurance of the AWL business to Phoenix under the IGR led to a reapplication to the PRA for approval for the AWL business to be included in the internal model. Following the PRA's approval in March 2017, the Phoenix Group's internal model (the "PGIM") is used for all of Phoenix's and AWL's business, including that reinsured into Phoenix from AWL under the IGR.
- 4.4 For this version of my Report, Appendices 1 and 2 show the Solvency II balance sheets as at 31 March 2017 for AWL and Phoenix, adjusted to reflect:
- The approval (granted in March 2017) from the PRA to use the PGIM to calculate the SCR (with a consequent impact on the risk margin) for the AWL business; in respect of both the business reinsured into Phoenix and of AWL as a solo entity; and
 - Dividends of £160 million and £5 million paid from Phoenix and AWL respectively.
- 4.5 The financial information used in the analysis of the effects of the implementation of the proposed Scheme as set out in Sections 8 and 9 is derived from the Solvency II information shown in Appendices 1 and 2.
- 4.6 I have not carried out an independent review of these Solvency II results as at 31 March 2017.
- 4.7 In respect of the Phoenix Solvency II results as at 31 March 2017:
- The SCR has been calculated using Phoenix's approved internal model (the PGIM);
 - The Phoenix Solvency II results as at 31 March 2017 have been approved by the Chief Actuary of Phoenix, the Phoenix Audit Committee and the Phoenix Board; and
 - The TMTP has been reviewed internally and signed off/approved by the chairman of the Phoenix Audit Committee.
- 4.8 In respect of the AWL Solvency II results as at 31 March 2017:
- The SCR has been calculated using the PGIM; and
 - The AWL Solvency II results as at 31 March 2017 have been approved by the Chief Actuary of AWL, the AWL Audit Committee and the AWL Board.
- 4.9 Given the level of external audit and internal governance to which the financial information has been subject, I am satisfied that it is appropriate to rely upon these Solvency II results for the purpose of this report.
- 4.10 My Supplementary Report will contain Solvency II numbers as at 30 June 2017 and will provide an update on the effect of the implementation of the proposed Scheme based upon these figures.

5 INFORMATION REGARDING AWL

Introduction

- 5.1 AWL is one of the UK regulated life companies in the Phoenix Group.
- 5.2 The Phoenix Group specialises in the management and acquisition of closed life and pensions funds, and operates primarily in the UK.
- 5.3 AWL is authorised under the terms of FSMA to undertake long term insurance business falling in Classes I - IV, VI and VII.

The history of AWL

- 5.4 AWL was originally known as Colonial Mutual Life (Pension Annuities) Limited and was established in 1975. Its name was changed to Colonial Pension Funds (UK) Limited in 1996. It was acquired by Winterthur in 2000 and renamed as Winterthur Pension Funds UK Limited. Winterthur was subsequently acquired by AXA.
- 5.5 The name of the company was changed to AXA Wealth Limited in September 2010. During 2011, AWL recommenced writing new business in the form of simple non-profit products sold under the SunLife brand, unit-linked life and pension business, including CTIP business.
- 5.6 During 2011, AWL was also party to two Part VII schemes (the "AWL Schemes"). Under the first of these, certain traditional life and pensions business of AWL was transferred to Winterthur Life UK Limited ("WLUK"), and some of the business of WLUK was transferred to AWL. Under the second of these, some of the business of Friends Life Company Limited was transferred to AWL.
- 5.7 The reason for the AWL Schemes was that AXA had sold the bulk of its UK life and pensions business to Friends Provident Holdings ("FPH") and the schemes enabled AXA to move all of its retained business into one company (namely AWL) and to move business that was being sold to FPH out of AWL.
- 5.8 On 1 November 2016, AWL was acquired by the Phoenix Group.

The AWL structure

- 5.9 AWL has no ring-fenced funds as defined by the Solvency II regulations.
- 5.10 Under Solvency II, all assets not in a ring-fenced fund must be allocated to either the long-term insurance business or the general insurance business of the company. AWL has no general insurance business.

The AWL products

- 5.11 AWL has the following in-force products (all figures as at 31 March 2017):
- Approximately 919,000 guaranteed non-profit whole of life and term assurance policies sold to the over 50s under the SunLife brand. The majority of these policies are whole of life, and are principally used to fund funeral costs. The average sum insured is approximately £3,300 and the average monthly premium is £16.
 - Approximately 39,000 unit-linked life and pension policies, supported by funds under management of approximately £4.4 billion (including £0.4 billion of accepted reinsurance).
 - Approximately 70 CTIPs, providing fund management for registered pension schemes. These are supported by approximately £8.5 billion of funds under management.
- 5.12 AWL's internal unit-linked funds in respect of the unit-linked individual and CTIP business invest in external unit-linked funds. Some of these arrangements are directly invested in external funds and some are structured as reinsurance between AWL and the provider of the external unit-linked funds. As at 31 March 2017:
- Approximately £6.0 billion was directly invested in external unit-linked funds:
 - £2.2 billion is CTIP business; and
 - £3.8 billion is individual unit-linked business.

- Approximately £7.0 billion was structured as reinsurance between AWL and the provider of the external unit-linked funds:
 - £6.3 billion is CTIP business; and
 - £0.6 billion is individual unit-linked business.

5.13 AWL is open to new business.

Recent relevant events

The acquisition of AWL by the Phoenix Group

5.14 On 1 November 2016, AWL was acquired by the Phoenix Group.

The Intra-Group Reinsurance treaties

5.15 Following the acquisition of AWL by Phoenix Group, two reinsurance treaties were put in place between AWL and Phoenix.

5.16 Under one of these, Phoenix paid a sum to AWL in return for receiving all future premiums and paying all future claims and expenses in relation to the SunLife business. Under the other treaty, Phoenix paid a sum to AWL in return for receiving any policyholder premiums not allocated to units and deductions from units, and paying expenses, in relation to individual and CTIP unit-linked business.

5.17 In this report, I refer to these treaties collectively as the IGR.

Reinsurance arrangements

5.18 Aside from the IGR treaties described above, AWL's conventional term assurance business is subject to external reinsurance of 90% of the mortality risk with Munich Re and PartnerRe.

5.19 As described above, the policyholder units in the AWL internal unit-linked funds in respect of the unit-linked individual and CTIP business are invested in external unit-linked funds and, as at 31 March 2017 approximately £7.0 billion was structured as reinsurance between AWL and the provider of the external funds. Of this:

- £6.3 billion is CTIP business. For most (approximately 99%) of the reinsured CTIP business, in the event of the insolvency of a provider of an external unit-linked fund, any losses are borne by the policyholder and AWL would not be required to reinstate the relevant policyholder units and associated liabilities.
- £0.6 billion is individual unit-linked business.

Solvency II for AWL

5.20 In March 2017, AWL received approval from the PRA to use the PGIM for the calculation of its Solvency II SCR and the PGIM was also approved for use by Phoenix in relation to the business reinsured in from AWL under the IGR.

5.21 Due to the presence of the IGR, AWL's SCR (as calculated using the PGIM) does not include any significant capital requirements in relation to the demographic risks underlying AWL's business. AWL's residual SCR principally reflects the risk of default of its counterparties, together with a capital requirement in relation to operational risk and the market risk associated with the non-linked assets that remain in AWL. The counterparty default risk and operational risk components of AWL's SCR are deemed to be non-hedgeable, and therefore also contribute to AWL's risk margin.

The AWL capital policy

5.22 In November 2016, the AWL Board approved a new capital policy for AWL (the "AWL Capital Policy" or "ACP").

5.23 The ACP specifies that AWL's risk appetite compels it to hold capital resources sufficient to be able to meet its SCR after a 1-in-10 year all risk event. The SCR referred to in the ACP is an SCR calculated using the PGIM, which was approved for use by AWL in March 2017.

- 5.24 AWL's analysis indicates that a buffer of £12 million would be sufficient to remain within this risk appetite, and therefore £12 million was set as the amount to be held under the ACP. AWL's analysis also indicates that the £12 million buffer would be sufficient to remain able to cover its standard formula SCR following a 1-in-10 year event.
- 5.25 At 31 March 2016, the ACP capital buffer of £12 million was equivalent to approximately 43% of AWL's SCR.
- 5.26 In order to ensure that AWL retains sufficient liquidity to execute trades in relation to its unit-linked funds, AWL must hold £40 million of its assets in liquid form.

The administration and servicing of the AWL policies

- 5.27 The administration and servicing of the AWL policies is carried out by Capita Life & Pensions Services Limited ("Capita") (for SunLife business) and by AXA Sun Life Direct Limited ("ASDL") (for the unit-linked business). Investment Accounting & unit-pricing services are currently provided by ASDL.
- 5.28 Phoenix has an ongoing project to integrate the AWL business (the AXA integration project) with the Phoenix business and as part of this:
- SunLife policy administration will be supplied to Phoenix by Phoenix Group Services ("PGS") who will outsource the work to Diligenta under the existing arrangement between PGS and Diligenta.
 - Unit-linked policy administration will be supplied to Phoenix by PGS who will outsource the work to Diligenta (as above).
 - Investment Accounting & unit-pricing services will be supplied to Phoenix by Phoenix Group Management Services Limited ("PGMS").
- 5.29 The effect of these changes on the level of service that policyholders experience, for example, the speed and quality of response to enquiries, the provision of annual statements and online services, is considered in Section 8.
- 5.30 There is not expected to be any change to premium collection dates and drawdown payment dates.

6 INFORMATION REGARDING PHOENIX

Introduction

- 6.1 The Phoenix Group has a number of active UK regulated life insurance companies: the largest are Phoenix and Phoenix Life Assurance Limited (“PLAL”). Phoenix Life Holdings Limited (“PLHL”) is the senior UK and European Community insurance holding company in the Group. Phoenix Group Holdings, which is listed on the London Stock Exchange and is a FTSE 250 company, is the ultimate parent.
- 6.2 The Phoenix Group specialises in the management and acquisition of closed life and pensions funds, and operates primarily in the UK.
- 6.3 Phoenix is authorised under the terms of FSMA to undertake long term insurance business falling in Classes I - IV, VI and VII.

The history of Phoenix

- 6.4 Phoenix Group can trace its origins back to 1782 with the establishment of Phoenix Assurance. Its evolution since then is complex and further details of the Phoenix Group’s and Phoenix’s history can be found on the Group’s website.
- 6.5 Phoenix was incorporated in England and Wales on 30 June 1971 under the Companies Acts 1948 to 1967 as a private limited company and it closed to new business in 2002, except in respect of increments and options under existing policies. Since 2002, Phoenix has grown in size as a result of a number of insurance business transfers and has approximately £39 billion of assets under management as at 31 March 2017.

The Phoenix structure and products

- 6.6 Phoenix has ten ring-fenced funds as defined under Solvency II. Outside of the ring-fenced funds, Phoenix has non-profit long-term business.
- 6.7 As discussed in Section 3, the requirement to segregate the assets of a non-profit fund and a shareholders’ fund is no longer in place under Solvency II. As noted in Section 2, Phoenix chooses to maintain a notional fund for accounting purposes to identify its long-term insurance business which is not allocated to its ring-fenced funds.
- 6.8 In this report the business outside of the ring-fenced funds is referred to as the Phoenix Non Ring-Fenced Fund (“PNRFF”) business. For the avoidance of doubt, the PNRFF includes the assets and liabilities of what were, prior to the implementation of Solvency II, the Phoenix NPF and the Phoenix SHF.

The PNRFF

- 6.9 The PNRFF comprises all business outside of Phoenix’s ring-fenced funds.
- 6.10 Annuities arising from policies in the ring-fenced funds and policies in the PNRFF are written in the PNRFF, as are contracts required to honour policy options under existing contracts. The PNRFF also accepts new contracts as they are written in AWL due to the IGR³.
- 6.11 The PNRFF includes business originally written by Phoenix as well as business transferred in as a result of a number of Part VII transfers. The PNRFF business principally comprises:
- Unit-linked regular and single premium life and pension policies;
 - Immediate and deferred annuities;
 - Term assurance, critical illness and income protection policies written on both guaranteed and reviewable premium bases; and
 - The inwards reinsurance of the AWL business.

³ Following the implementation of the Scheme, the PNRFF will write new business for the product lines currently sold by AWL

The Phoenix ring-fenced funds

6.12 The ring-fenced funds in Phoenix, are as follows:

- The Alba WPF;
- The SAL WPF;
- The Phoenix WPF;
- The 100% WPF;
- The 90% WPF;
- The Britannic Industrial Branch Fund;
- The Britannic WPF;
- The NPI WPF;
- The Scottish Mutual WPF; and
- The SPI WPF.

Recent relevant events*The acquisition of AWL and the setting up of the IGR*

6.13 On 1 November 2016, AWL was acquired by the Phoenix Group and two reinsurance treaties were put in place between AWL and Phoenix as described in Section 5. These two treaties are collectively referred to as the IGR.

The Phoenix- ReAssure Scheme

6.14 On 31 December 2016, approximately 58,000 in-payment pension annuities were transferred from three of the Phoenix ring-fenced funds (the Alba WPF, the SAL WPF and the Phoenix WPF) to ReAssure Limited under an insurance business transfer scheme made under Part VII of FSMA.

The Phoenix capital policy

6.15 In October 2016, the Phoenix Board approved a new Phoenix Capital Policy ("PCP") to reflect the transition to Solvency II. Phoenix has received non-objection from the PRA to this capital policy under which a capital buffer equal to 28% of the SCR should be held. For ring-fenced funds that do not require financial support from the PNRFF, this capital buffer may be met by surplus within the relevant ring-fenced fund and allowance is made for management actions permitted within the PPFM.

6.16 The percentage is broadly equivalent to a 1-in-10 level of confidence of 100% SCR coverage over a one year period, after allowing for one year of expected surplus emerging.

6.17 The percentage will be reviewed from time to time to ensure that the PCP continues to meet its objective. The percentage may therefore change without affecting the strength of the capital policy.

6.18 Any assets in excess of the PCP requirements in the PNRFF may be distributed to Phoenix's shareholders or used to finance other strategic initiatives.

6.19 Under the PCP, large deficits relative to the PCP will require consideration of corrective action. However, small deficits relative to the PCP do not require immediate corrective action, although no capital may be released (for example via the payment of dividends) until the deficit has been eliminated.

The reinsurance agreements of Phoenix

6.20 Aside from the IGR treaties described above and in Section 5, Phoenix has a number of external reinsurance agreements (where Phoenix is the cedant) in place with XL Re Limited, American International Reinsurance Company Limited, Munich Re Group, SCOR Global Life SE, Hannover Rück SE, Swiss Re Europe Holdings SA, Pacific Life Re, UNUM Limited, General Reinsurance SE, Legal and General Assurance Society Limited, and RGA International Reinsurance Company Limited.

- 6.21 In addition, the PNRFF and NPI With-Profits Fund of Phoenix reinsure certain elements connected with the business of NPI Limited (which was transferred to Phoenix in 2012) to PLAL. Phoenix accepts the reinsurance of the investment element and certain expense liabilities on unit-linked business from the National Provident Life With-Profits Fund within PLAL.

The administration and servicing of the Phoenix policies

- 6.22 The administration and servicing of the Phoenix policies is carried out by Pearl Group Management Services Limited (“PGMS”), another Phoenix Group company. Fees under this arrangement are based on unit charges and policy volumes, with the unit charges subject to annual increases linked to an external index.
- 6.23 PGMS, in turn, outsources the policy administration to a number of administration providers including Diligenta Limited and Capita Life & Pensions Services Limited, the companies relevant to the policies affected by the proposed Scheme.
- 6.24 Assets are mostly managed by Ignis Asset Management (“IAM”) part of the Standard Life Investment group, in return for fees which vary by asset class and fund.

7 THE PROPOSED SCHEME

The motivation for the Scheme

- 7.1 The senior management of Phoenix has described the motivation for entering into the Scheme as to:
- Improve capital efficiency by:
 - Increasing diversification benefits;
 - Removing the duplication of counterparty risk;
 - Realising synergies in relation to capital policies; and
 - Releasing the liquidity buffer in AWL.
 - Reduce costs by removing the need to operate the IGR.
 - Improve operational efficiency through the reduction in the number of regulated insurance companies and through increased consistency of management practices and principles. This should result in efficiencies in governance, financial reporting, management information and administration.
- 7.2 From the perspective of AWL, the additional motivation for entering into the Scheme is the transfer of its business into a well-capitalised and well diversified insurance company.

A summary of the Scheme

- 7.3 The Scheme is expected to be presented to the Court for a Directions Hearing on 24 July 2017 and for a Final Hearing on 21 November 2017.
- 7.4 If approved by the Court, the Scheme will become operative on the Transfer Date, at which point the transferring business will legally transfer from AWL to Phoenix. The Scheme provides that it will take effect as between AWL and Phoenix, including for accounting purposes, from 1 October 2017 (the "Effective Date").
- 7.5 These provisions will avoid the need for Phoenix and AWL to carry out a separate valuation of the transferring business as at the Transfer Date, and mean that they can instead use the valuation carried out immediately prior to the Effective Date. However, these provisions will not affect the rights of any policyholders or third parties in relation to the transferring business, which will continue to be against AWL up to the Transfer Date and Phoenix thereafter.
- 7.6 If the Scheme is approved by the Court, then on the Transfer Date the business of AWL will be allocated to the PNRFF.
- 7.7 Following the implementation of the Scheme, the IGR will cease to apply as all of the ceded business will have been transferred into Phoenix. Phoenix will become the cedant in all external reinsurance treaties for which AWL is currently the cedant. The operation of these latter treaties will continue unchanged in all other respects.
- 7.8 The implementation of the Scheme will have no effect on the terms and conditions of the transferring policies.

Transferring assets and liabilities

- 7.9 Under the Scheme it is proposed that the entire business of AWL will be allocated to the PNRFF.
- 7.10 The Scheme will transfer AWL's rights and obligations in respect of the transferring policies to Phoenix.
- 7.11 Using figures as at 31 March 2017, the number of policies to be transferred is approximately 958,000, constituting approximately £6,010 million of BEL. This will increase the PNRFF's BEL from £ 19,121 million to £25,131 million.
- 7.12 The assets of AWL, with the exception of those required to meet AWL's MCR, will be transferred to the PNRFF. The remaining assets and any associated investment income and tax liabilities will be transferred to the PNRFF once AWL has been de-authorised as an insurance company.

Management of unit-linked funds

- 7.13 Under the Scheme, new unit-linked funds will be created in Phoenix corresponding to the AWL internal unit-linked funds.
- 7.14 These new unit-linked funds will receive the assets of the corresponding funds in AWL at the Transfer Date and will have the same charges, pricing practices and investment objectives as the current corresponding funds in AWL. The relevant transferring policies will be allocated the same number and value of units as were comprised in the corresponding unit-linked funds immediately prior to the Transfer Date.
- 7.15 The AWL Schemes include certain provisions regarding the future management of AWL's unit-linked funds, including provisions enabling AWL (subject always to applicable legislation and policy terms and conditions) to close, divide or wind up its unit-linked funds or change their investment objectives, and provisions designed to ensure appropriate treatment of policyholders in these circumstances. In order to ensure that there are no changes to the basis on which the transferring policies or their unit-linked funds are managed, equivalent provisions have been incorporated into the Scheme, including the same protections for policyholders in the event that Phoenix chooses to make any such changes to the former AWL unit-linked funds at a future date.
- 7.16 There are no current plans for harmonisation of the unit-linked funds after the transfer.

Administration and investment management

- 7.17 The administrative arrangements and investment management agreements in respect of the transferring policies will not change as a result of the implementation of the Scheme.
- 7.18 However, Phoenix intends to make changes to the administration of the AWL policies at or around the Transfer Date, whether or not the Scheme is implemented.

The costs of the Scheme

- 7.19 The costs of the Scheme will be borne by the PNRFF.

The effect on the AWL Schemes

- 7.20 The Scheme will not change or otherwise affect the operation of the AWL Schemes, which will continue in full force and effect as though Phoenix is a party to the AWL Schemes in place of AWL.

Excluded Policies

- 7.21 An "Excluded Policy" is defined in the Scheme as an AWL policy that cannot be transferred under the Scheme (or the Guernsey Scheme) pursuant to section 111 of FSMA at the Transfer Date due to a legal or regulatory impediment or that:
- Was concluded in an EEA State other than the United Kingdom and the PRA has not prior to the making of the Order by which the Court sanctions the Scheme provided the certificate referred to in paragraph 3A of Schedule 12 to FSMA with respect to the relevant EEA State;
 - Are Guernsey Policies (to the extent that, and for so long only as, the Guernsey Scheme has not yet received the requisite court approval and become effective in accordance with its terms); or
 - Is a policy issued by AWL pursuant to the exercise of any right or option under any such Excluded Policy.
- 7.22 Under the Scheme, any Excluded Policies would be reinsured into Phoenix through an Excluded Policies Reassurance Arrangement from the Transfer Date on a basis intended to replicate the financial effects of a transfer of such policies to Phoenix. This Excluded Policies Reassurance Arrangement is set out in the Scheme.
- 7.23 Any Excluded Policies would be:
- Managed by Phoenix in the same way as if they had been transferred under the Scheme;
 - Subject to the governance of Phoenix; and

- The administration and servicing arrangements for Excluded Policies would be the same as for transferring policies.

7.24 Subject to obtaining the necessary certificates from the PRA in relation to each EEA State and the sanction of the separate Guernsey scheme, there are not expected to be any Excluded Policies.

The structure after the implementation of the Scheme

7.25 After the implementation of the Scheme, the liabilities and most of the assets of AWL will have been transferred to the PNRFF.

7.26 There will be no change to the ring-fenced funds of Phoenix.

My report on the Scheme

7.27 In order to cover the potential effects of the implementation of the Scheme on the affected policies I have divided the affected policies into the following groups for consideration in this report:

- The policies of AWL (Section 8); and
- The policies of Phoenix (Section 9):
 - The policies of the PNRFF; and
 - The other policies of Phoenix outside the PNRFF.

7.28 Sections 8 and 9 cover these sub-divisions of policies and Sections 10 and 11 cover some general points in respect of the Scheme.

8 THE EFFECT OF THE SCHEME ON THE AWL POLICIES

Introduction

- 8.1 As described in Section 7, under the proposed Scheme, all of the AWL business will be transferred to Phoenix (with the exception of any Excluded Policies). This transferring business consists of whole life, term assurance and unit-linked life and pension business.
- 8.2 Under the IGR, the non-linked cash flows of the AWL policies are currently 100% reinsured to Phoenix.
- 8.3 If the Scheme is approved by the Court, the transferring policies will transfer into and become direct policies of the PNRFF. Therefore, the key points to consider are:
- The financial strength available to provide security for the benefits under the AWL policies after the implementation of the Scheme compared to that currently available;
 - Any change to the profile of risks to which the AWL policies will be exposed as a result of the implementation of the Scheme;
 - The effect of the implementation of the Scheme on the reasonable expectations of the AWL policyholders in respect of their benefits; and
 - The effect of the implementation of the Scheme on the standards of administration, service, management and governance applied to the AWL policies.
- 8.4 These are considered in turn in this section.

The financial strength available to provide security of benefits

Introduction

- 8.5 Although the IGR has been set up to replicate the economic effects of the proposed Scheme and the risks under the AWL policies are currently reinsured to the PNRFF, AWL remains contractually liable to its policyholders to pay the amounts due under their policies. AWL is exposed to the risk of Phoenix not fulfilling its obligations under the IGR.
- 8.6 The legal consequence of the implementation of the proposed Scheme is that AWL will be released from its obligations to its policyholders and these obligations will be placed on Phoenix.
- 8.7 When a claim arises under one of the AWL policies, AWL is responsible for paying the benefits due and subsequently recovering an appropriate amount from Phoenix or offsetting the benefit against any payments due to be paid to Phoenix under the IGR.
- 8.8 Therefore, the AWL policies currently achieve security for their guaranteed benefits from the assets in AWL and from the assets and strength of Phoenix via the IGR. The strength of AWL and Phoenix includes any rights that AWL and Phoenix have under reinsurance treaties with external reinsurers.
- 8.9 The financial strength available to provide support for guaranteed benefits must be considered in the context of the restrictions that are in place in respect of changing that financial strength through, for example, making dividend payments. For AWL and Phoenix, such restrictions are set out in the ACP and the PCP respectively, as described in Sections 5 and 6.
- 8.10 In addition to the level of capital required under each relevant capital policy, consideration should be given to the governance around changes to the policy and the response of the firm to breaches of the capital policy.
- 8.11 Therefore, the AWL transferring policies currently achieve security for their guaranteed benefits from:
- The financial strength required under the Solvency II regulations for AWL:
 - Assets backing the technical provisions of the AWL policies; and
 - The assets backing AWL's SCR.
 - The financial strength required by the ACP:

- The ACP capital buffer; and
 - The strength of governance around the ACP.
- 8.12 For the non-unit linked AWL policies future premium income is expected to be more than sufficient to meet future claim and expense outgo and so the (gross of reinsurance) technical provisions of these AWL policies are currently negative. However, the technical provisions of these AWL policies may become positive in an adverse scenario and are expected to become positive in the future.
- 8.13 The ability of Phoenix to fulfil its obligations under the IGR contributes to the financial strength of AWL, and therefore the security of the AWL transferring policies.
- 8.14 In addition, AWL has reinsured certain liabilities associated with its term assurance business to third party reinsurers. Under these agreements the reinsurers reimburse AWL for benefit payments in relation to the AWL policies covered by the agreement. The ability of these reinsurers to fulfil their obligations is therefore relevant to the security of the transferring AWL policies.
- 8.15 Appendix 1 shows the current financial positions of AWL and Phoenix.
- 8.16 If the Scheme is approved by the Court then, after its implementation, the security of the benefits under the transferring policies will be provided by:
- The financial strength required under the Solvency II regulations for the PNRFF:
 - Assets backing the technical provisions of the policies in the PNRFF; and
 - Assets backing the PNRFF SCR.
 - The financial strength required by the PCP:
 - The PCP capital buffer; and
 - The strength of governance around the PCP.
- 8.17 In the following paragraphs of this section, I consider the relative financial strength available to provide security for the AWL policies before and after the implementation of the Scheme by considering the bullets above in turn.

The financial strength required under Solvency II for AWL and Phoenix

- 8.18 Under Solvency II the assets held in respect of a policy or group of policies should cover the technical provisions (consisting of the BEL and risk margin and adjusted by the TMTP if appropriate) and the SCR. This amount is then increased in accordance with the firm's capital policy: the PCP for Phoenix and the ACP for AWL.
- 8.19 Currently:
- The technical provisions and SCR for AWL and Phoenix are calculated in accordance with the Solvency II regulations.
 - Phoenix's financial position includes a £1.9 billion TMTP benefit as at 31 March 2017, AWL does not have a TMTP.
 - AWL and Phoenix have approval to use the PGIM for the calculation of their respective SCRs under Solvency II, and therefore both firms use the PGIM to determine their SCR.
 - The technical provisions and SCR in respect of the transferring AWL business are held:
 - In the PNRFF in respect of the non-linked business and the non-unit cash flows of the unit-linked business due to the IGR; and
 - In AWL in respect of the unit-linked business.
 - The capital resources of Phoenix covered its SCR (excluding unsupported with-profits funds – see 8.33 below) with a ratio of 136%, with excess capital (after dividends and using the PGIM for the AWL business) of £591 million, which is sufficient to meet the requirements of the PCP. These figures are shown in Appendix 1.

- The capital resources of AWL covered its SCR with a ratio of 163%, with excess capital (after capital requirements, dividends and using the PGIM) of £17 million.
- 8.20 Following the implementation of the proposed Scheme, the transferring AWL policies will be policies of Phoenix and:
- The Solvency II regime will not change as a result of the Scheme and the technical provisions and SCR for Phoenix will remain calculated in accordance with the Solvency II regime.
 - There will be no change to Phoenix's TMTP due to the Scheme, as the transfer of the AWL business would not constitute a material change in risk profile for Phoenix.
 - There will be no change to the quality of the Phoenix capital – 93% is currently Tier 1 capital. This includes the TMTP and the PRA has stated publicly⁴ that it regards the financial benefit conferred by the TMTP as Tier 1 capital.
 - The approval for the use of the PGIM will not change as a result of the Scheme and so the Phoenix SCR will continue to be calculated on the PGIM.
 - The technical provisions and the SCR in relation to the transferring AWL policies will be held in the PNRFF in Phoenix. Based on figures as at 31 March 2017 (net of reinsurance) the technical provisions of the PNRFF are projected to increase by £6.0 billion (32%) and the SCR of the PNRFF is projected to increase by £10.0 million (0.8%).
 - The capital resources of Phoenix are projected to cover its SCR (excluding the supported with-profits funds) with a ratio of 137%, with excess capital (after dividends and using the PGIM for the AWL business) of £624 million, which is sufficient to meet the requirements of the PCP, as shown in Appendix 2.
 - AWL will have no policies in-force and will have a de minimis capital requirement required to be held by all authorised insurance companies. At 31 March 2017, this amount was €3.7 million. The assets of AWL, other than those required to meet AWL's de minimis capital requirement, will transfer to the PNRFF. Once AWL is de-authorised the requirement to hold this capital requirement will fall away.
- 8.21 As stated above, based on the financial information as at 31 March 2017 shown in Appendices 1 and 2 of this report, the coverage of the Solvency II SCR in AWL is currently 163% and this coverage percentage is projected to be 137% in Phoenix after the Scheme is implemented.
- 8.22 This projected decrease in the SCR coverage ratio might, in isolation, be taken to imply an adverse impact on the security of the transferring AWL policies. However, the SCR coverage ratios are indicators or proxies of financial strength and a decrease in the coverage ratio does not necessarily indicate a significant or material reduction in security. In particular:
- The Phoenix coverage ratio of 137% indicates significant strength and the probability of Phoenix being unable to pay its claims as they fall due is sufficiently remote for there to be no material change in the security of benefits under the transferring AWL policies.
 - Phoenix is many times larger than AWL and its excess assets are, in absolute terms, much bigger: the financial information as at 31 March 2017 shows that Phoenix would have had a large amount of Own Funds (£3.4 billion) and excess capital (£624 million) available to provide security to the AWL policies if the Scheme had been implemented on this date.
 - AWL's small size and lower risk diversification mean that its capital position could be subject to a greater level of volatility than that of Phoenix and thus AWL should require a higher percentage of additional capital for a similar level of assurance.
 - AWL is currently dependent on Phoenix for security due to the IGR and after the Scheme the total assets of Phoenix will be the sum of the assets of Phoenix and AWL before the implementation of the Scheme.
 - Although the coverage ratio (as at 31 March 2017) in AWL is high at 163% of the SCR, this is in excess of the regulatory requirements and the requirements set out in the ACP. There is no obligation for this level of capital to be maintained in AWL and this excess could be paid out.

⁴ <http://www.bankofengland.co.uk/publications/Pages/speeches/2015/829.aspx>

8.23 I am satisfied that although the SCR coverage ratio is projected to be lower in Phoenix after the implementation of the Scheme than currently in AWL there will not be a material adverse effect on the security of benefits for the transferring AWL policies.

The run off of the TMTP

8.24 The projected post-Scheme Phoenix solvency coverage of 137% includes allowance for the TMTP. As discussed in Section 2 the TMTP can be considered Tier 1 capital but is reduced to zero over 16 years in line with the Solvency II rules.

8.25 All else being equal the run off of the TMTP would decrease the solvency coverage and the natural emergence of surplus on the closed Phoenix business will assist with the management of this run off as, in each year, the surplus is projected to comfortably cover the amortisation of the TMTP in that year.

8.26 The Phoenix TMTP run-off plan shows the projected progression of the Solvency coverage ratio as the TMTP runs off and shows that, in each future year, Phoenix is projected to exceed the requirements of the PCP. Therefore, I am satisfied that there will not be a material adverse effect on the security of benefits of the transferring AWL policies due to the run-off of the TMTP in future.

The financial strength provided by the AWL and Phoenix capital policies

8.27 When considering the financial strength available to provide the security of the benefits of a particular group of policies, reliance should only be placed upon the assets held in accordance with the capital policy, as assets in excess of capital policy requirements could be paid out as dividends or invested in business ventures.

8.28 The security of the benefits under the AWL policies currently depends upon the assets of AWL held in accordance with the ACP as set out in Section 5, as well as the assets of Phoenix held in accordance with the PCP.

8.29 Following the implementation of the Scheme, the transferring business and most residual assets attributed to it will be transferred into the PNRFF and the security of the benefits of the AWL policies will be solely provided by the assets of Phoenix held in accordance with the PCP as set out in Section 6.

8.30 The proposed transfer will not change the risk appetite or capital policy of Phoenix and I must consider a comparison of the relative strengths of the capital policies of AWL and Phoenix as part of my considerations in respect of the effect of the proposed Scheme on the benefit security of the transferring policies. This should be a comparison of both the relative levels of capital required under the two policies, and the qualitative aspects of the capital policies such as the governance surrounding each capital policy and the required response of management to a breach of the capital policy, and these are covered in turn below.

The relative strengths of the current capital policies

8.31 The PCP currently provides for a capital buffer of 28% of the SCR. The PNRFF must hold this buffer for its own business and for any supported with-profits funds. A buffer does not need to be held in the PNRFF in relation to the unsupported with-profits funds as these funds are able to meet their capital requirements from their own resources.

8.32 This capital buffer broadly corresponds to Phoenix being able to continue to meet its capital requirements following a 1-in-10 year adverse event, after allowing for one year of expected surplus emerging.

8.33 As a percentage of its total SCR, Phoenix's excess assets are 122%. However, excluding the SCR of those with-profits funds that are able to cover their capital requirements from their own resources gives excess assets sufficient to cover 136% of the SCR.

8.34 Under the PCP, Phoenix must not pay a dividend if the PCP requirements are not being met prior to the payment, or if the payment of the dividend would result in a breach of the PCP.

8.35 Although the ACP also provides for a capital buffer such that it can continue to meet its capital requirements following a 1-in-10 year adverse event, the ACP provides for a fixed capital buffer of £12 million, which was equivalent to 43% of AWL's SCR at 31 March 2017.

8.36 However, although the ACP provides for a higher capital buffer percentage than the PCP, it should be noted that:

- Many of the risks to which the AWL policies are exposed are reinsured to Phoenix under the IGR, and these risks are therefore reflected in the calculation of the PCP capital buffer rather than that of the ACP;

- AWL's small size and lower risk diversification mean that its capital position could be subject to a greater level of year-on-year volatility than Phoenix's thus AWL is likely to require a higher percentage of additional capital for the same level of assurance;
- Despite the differences in the percentages of the SCR, the PCP and the ACP are both derived so as to be broadly equivalent to ensuring the SCR is covered after a 1-in-10 year event;
- In absolute terms, the buffer required by the PCP (post-Scheme) is much larger than the (pre-Scheme) buffer required by the ACP (£414 million vs £12 million at 31 March 2017); and
- Whether viewed as covering capital requirements after a 1 in 10 year event or a 128% capital buffer, this provides a high level of security above the Solvency II SCR which itself requires capital sufficient to meet a 1 in 200 year event and is not out of line with what I have seen in the UK insurance market.

8.37 Therefore, whilst the ACP provides for a higher capital buffer in percentage terms, I do not consider this to provide a materially better level of security than the PCP and it will be to the advantage of the transferring policyholders that they would be transferring into a company with a capital requirement that is less volatile and much larger in absolute terms.

8.38 I am satisfied that differences between the strength of the ACP and the PCP would have no material adverse effect on the security of benefits of the transferring policies.

The governance processes required when amending the capital policies

8.39 There are no material differences between AWL and Phoenix in the governance processes that are required when amending the capital policies. The changes must be approved by the respective Boards and sent to the PRA for non-objection before being implemented.

8.40 The management and operation of Phoenix is subject to the terms of a Part VII scheme that was approved in 2009, which sets out the basic terms of Phoenix's capital policy and how it can be changed.

8.41 The ACP is not subject to any requirements or obligations set out in previous schemes of transfer.

The monitoring of the capital policies

8.42 Phoenix's capital position is calculated daily.

8.43 AWL's capital position is determined on a quarterly basis and, following the implementation of the IGR reinsuring most risks to Phoenix, is expected to be stable over time. Between quarter ends, management regularly monitors the remaining drivers of the AWL capital position and, in the event of significant changes and/or material movements would update the solvency position appropriately.

The required response of management to a breach of the capital policies

8.44 The required response of AWL to a breach in the ACP is broadly aligned with the required response of Phoenix to a breach in the PCP, and therefore the implementation of the Scheme will not result in a material change in the required response to a capital policy breach.

Conclusion on the security of benefits in respect of the differences between the PCP and the ACP

8.45 There are some differences between the ACP and the PCP but, as set out above I do not consider these to be material and the key considerations for the transferring policyholders are as follows:

- Following the implementation of the Scheme, the AWL policyholders will derive their security of benefits from a much larger and better diversified company;
- Changes to the PCP would, in practice, be subject to the non-objection of the PRA;
- The position of Phoenix against the PCP is monitored daily; and
- Phoenix is not permitted to pay dividends when in breach of its capital policy.

8.46 I am satisfied that the security that will be provided to the transferring policyholders by the PCP is sufficiently strong for there to be no material adverse effect on the security of the benefits under the transferring policies as a result of the change from the ACP to the PCP.

Liquidity considerations

8.47 In companies where significant proportions of the business have a negative BEL, liquidity may be an issue because a proportion of the company's own funds is supported by the value of future premiums, which is not a liquid asset. Therefore it is important to check whether, although the company is solvent, it also has sufficient liquid assets to meet its shorter term outflows, including policyholder claims.

8.48 After the implementation of the Scheme, the transferring AWL policies will be in the PNRFF and the liquidity needs will be met by the assets in the PNRFF (which is projected to have own funds of £1.5 billion). Therefore the possibility of not being able to meet the short term needs of the AWL policies is reduced and I am satisfied that the implementation of the Scheme will not adversely affect the liquid assets available to support benefit payments under the AWL policies.

Conclusion on the financial strength available to provide security of benefits

8.49 In conclusion I am satisfied that:

- The implementation of the Scheme will not change the Solvency II regime or the calculation of AWL's technical provisions and SCR (which will continue to be calculated using the PGIM).
- Although the SCR coverage ratio is projected to be lower in Phoenix after the implementation of the Scheme than currently in AWL there will not be a material adverse effect on the security of benefits for the transferring AWL policies.
- The projected financial strength of Phoenix after the implementation of the Scheme is sufficient to provide a level of security for the transferring business that is not materially adverse relative to that prior to the implementation of the Scheme; and
- Although the implementation of the Scheme will lead to a change for the transferring policies such that the capital policy to which they are subject will change from the ACP to the PCP, overall this change will not have a material effect on the security of benefits for the transferring business.

8.50 Therefore I am satisfied that the implementation of the proposed Scheme will not have a material adverse effect on the security of the benefits under the transferring AWL policies.

The security provided by the IGR

8.51 The IGR currently provides security for the AWL policies and after the implementation of the Scheme, the IGR will cease and the AWL policies will be direct policies of the PNRFF.

8.52 Currently:

- AWL ranks below the direct Phoenix policies in the event of wind-up but additional security is provided to AWL by the collateral requirements of the IGR (when the BEL is positive); and
- AWL has the option to terminate the IGR in certain, very unlikely, circumstances (for example Phoenix is unable to cover its MCR).

8.53 After the implementation of the Scheme,

- The AWL policies will be direct policies of Phoenix and will rank equally with the other direct Phoenix policies in the event of wind up;
- The IGR will cease (so there will be no collateral requirements); and
- There will no longer be a 'termination option'.

8.54 I am satisfied that the transfer of the AWL policies to become direct policies of Phoenix will not have a material adverse effect on their security of benefits.

- 8.55 AWL is currently only able to exercise its option to terminate the IGR in very unlikely circumstances and, even if it were able, would either need to replace the reinsurance cover or recapitalise – both at uncertain cost. Therefore, the option to terminate the IGR does not currently provide material security to the AWL policies and so its removal will not have a material adverse effect on the security of the AWL policies.
- 8.56 I am satisfied that the cessation of the IGR as a result of the implementation of the Scheme will not lead to a material adverse effect on the security of the benefits under the AWL policies.

The profile of risks to which the AWL policies are exposed

- 8.57 After the implementation of the Scheme, the transferring AWL policies will be direct policies of Phoenix and therefore directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.
- 8.58 Phoenix has a large variety of in-force business that exposes it to a range of different risk types, including insurance risks (such as mortality risk, longevity risk and persistency risk) and market risks. There are also risks associated with Phoenix's with-profits funds, particularly those that currently require shareholder support to meet their capital requirements.
- 8.59 By contrast, the AWL policies imply exposure to a narrower set of risks: principally market risk, persistency risk, and mortality risk in relation to both its non-linked and its linked business. The presence of the IGR means that the AWL policies are already exposed to a significant degree to the risks of Phoenix as AWL is reliant upon Phoenix to fulfil its obligations under the IGR.
- 8.60 Therefore, the implementation of the Scheme will not have a material effect on the range of risks to which the transferring AWL policies are exposed and to the extent that the exposure of the AWL policies to the risks associated with Phoenix does increase:
- The exposure to a wider range of risks results in a greater level of diversification in the risk exposures; and
 - The Phoenix capital requirement calculation reflects the full range of risks to which Phoenix is exposed and Phoenix more than covers this capital requirement as required by the PCP.
- 8.61 I am satisfied that any change in risk profile will not have a material adverse effect on the security of the benefits of the transferring AWL policies.

The management and governance of the AWL policies

- 8.62 The transferring business is currently managed by, and subject to the governance of, the Board of AWL and, following the implementation of the Scheme, the transferring business will be subject to the governance of the Board of Phoenix and:
- The members of the Boards of AWL and Phoenix are the same;
 - The Board of Phoenix is already responsible for overseeing the reinsured business from AWL; and
 - Phoenix has a wide variety of in-force business, including products that are similar in nature to the products of AWL, and therefore the Phoenix Board is experienced in the management of this type of business. In particular, at 31 March 2017 the PNRFF had whole life business with £21 million of annualised premiums in force, along with approximately £10 billion of unit-linked liabilities.
- 8.63 I am satisfied that the implementation of the Scheme will not have a material adverse effect on the standards of management and governance that apply to the transferring AWL policies.

The standards of administration and service applied to the AWL policies

- 8.64 The administration and servicing of the AWL policies is currently carried out by Capita (for SunLife business) and ASDL (for the unit-linked business).
- 8.65 The AXA integration project and the changes to the administration arrangements are not dependent on the Scheme and these changes will take place whether or not the Scheme is implemented.

- 8.66 The changes will be as follows:
- SunLife policy administration will be supplied to Phoenix by Diligenta under the outsourcing arrangement between PGS and Diligenta. The SunLife product suite is straightforward and the system development work required for Diligenta to administer this business is underway. It is anticipated that these products will be administered and serviced from existing (established) Diligenta sites.
 - Unit-linked policy administration will be supplied to Phoenix by Diligenta. The service will continue to be supplied from Basingstoke utilising staff who will transfer to Diligenta.
 - Investment accounting & unit-pricing services will be supplied to Phoenix by PGMS. The service will continue to be supplied from Basingstoke utilising staff who will transfer to PGMS.
- 8.67 Diligenta already carries out administration for the Phoenix business. Diligenta is a UK-based FCA-regulated company specialising in of business process services (BPS) for the life and pensions industry, providing services to four UK insurance companies and administering over 6.5 million policies in force.
- 8.68 Phoenix will put in place service level agreements in the context of the new arrangements and there is not expected to be any reduction in the level of service that policyholders experience, for example, the speed and quality of response to enquiries, the provision of annual statements and online services. Diligenta has undertaken that, at a minimum, they will supply the same level of services as currently, even if that is better than it provides to Phoenix on other blocks of business. Diligenta has spent the last few months designing the additional functionality that will be needed to support the SunLife and unit-linked products.
- 8.69 Phoenix will continue to be responsible for the quality of customer service and, as it does on all its existing outsourcing arrangements, Phoenix will maintain close oversight of the outsourcer and the customer service it provides especially during the period of change as Diligenta implements and embeds the new services outlined above in paragraph 8.66.
- 8.70 There is not expected to be any change to premium collection dates and drawdown payment dates.
- 8.71 I am satisfied that the implementation of the Scheme will not have a material impact on the standards of administration and service applied to the transferring policies.
- 8.72 I will review the administration and service standards again in my Supplementary Report in light of any developments subsequent to this report.

The reasonable expectations of the AWL policyholders in respect of their benefits

- 8.73 The transferring AWL business consists of non-profit unit-linked and non-linked business. For this type of business, policyholders' expectations in respect of their benefits are that:
- They receive their benefits as guaranteed under the policy, on the dates and in the contingencies specified in the terms and conditions;
 - For unit-linked policies:
 - The benefits received reflect the investment performance of the assets in which their units are invested, net of contractual charges payable under the policies; and
 - The assets in which their units are invested are materially in line with the target investment allocation in the relevant fund literature.
 - The administration, servicing, management, and governance of the policies are in line with the contractual terms under the policies; and
 - The standards of service are at least as good as those they currently receive.
- 8.74 The implementation of the proposed Scheme will not change:
- The terms and conditions of the AWL policies (except that the policies will become policies of Phoenix);
 - The investment objectives of the unit-linked funds;
 - The pricing of the unit-linked funds or the charges that apply to the AWL policies; or

- The outsourcing and asset management arrangements for the AWL policies.

8.75 In addition, new unit-linked funds will be created in Phoenix corresponding to the AWL internal unit-linked funds. These new unit-linked funds will receive the assets of the corresponding funds in AWL at the Transfer Date, and the relevant transferring policies will be allocated the same number and value of units as were comprised in the corresponding unit-linked funds immediately prior to the Transfer Date.

8.76 As discussed above, I am also satisfied that:

- The implementation of the Scheme will not have a material adverse effect on the security of the guaranteed benefits of the AWL policies;
- The implementation of the Scheme will not affect the standards of administration and service that apply to the AWL policies; and
- The implementation of the Scheme will not have a material adverse effect on the management or the governance of the AWL policies.

8.77 Therefore, I am satisfied that the implementation of the Scheme will not have a material adverse effect on the reasonable benefit expectations of the transferring AWL policyholders or on the standards of administration, service, management and governance that apply to the transferring AWL business.

Conclusion for the AWL policies

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

- The security of benefits under the AWL policies;
- The reasonable expectations of the AWL policyholders in respect of their benefits; or
- The standards of service and governance that apply to the AWL policies.

9 THE EFFECT OF THE SCHEME ON THE PHOENIX POLICIES

Introduction

- 9.1 In this section I consider the effect of the implementation of the Scheme on the Phoenix policies, which can be divided into the following groups:
- The PNRFF business; and
 - The policies in the Phoenix ring-fenced funds.
- 9.2 If the Scheme is approved by the Court, the transferring policies will transfer from AWL to the PNRFF, and therefore the key points to consider in respect of the Phoenix policies are:
- The financial strength available to provide security for the benefits under the Phoenix policies after the implementation of the Scheme compared to that currently available;
 - Any change to the profile of risks to which the Phoenix policies will be exposed as a result of the implementation of the Scheme; and
 - The effect of the implementation of the Scheme on the reasonable expectations of the Phoenix policyholders in respect of their benefits and the standards of administration, service, management and governance that apply to the Phoenix policies.
- 9.3 These are considered in turn below for each group of Phoenix policies.

The PNRFF business

Introduction

- 9.4 Currently the transferring business is reinsured from AWL to the PNRFF under the IGR. If the Scheme is implemented, the transferring policies will be transferred to the PNRFF and the IGR will be terminated.

The financial strength available to provide security of benefits

- 9.5 Currently, the security of the guaranteed benefits of the PNRFF business is provided by:
- The financial strength required under the Solvency II regulations for the PNRFF policies:
 - Assets backing the technical provisions of the PNRFF policies; and
 - The assets backing the PNRFF SCR.
 - The financial strength required by the PCP:
 - The PCP capital buffer; and
 - The strength of governance around the PCP.
 - Assets elsewhere in Phoenix.
- 9.6 Appendix 1 shows the current financial position of Phoenix.
- 9.7 If the Scheme is approved by the Court then, after its implementation, the security of the benefits under the transferring policies will be provided by the same constituents but the AWL policies will have been transferred into the PNRFF.
- 9.8 As described in Section 8, when considering the financial strength available to provide the security of the benefits of a particular group of policies, reliance should only be placed upon the assets held in accordance with the capital policy, as assets in excess of capital policy requirements could be paid out as dividends or invested in business ventures.

- 9.9 In addition to the level of capital required under the relevant capital policy, consideration must also be given to the governance around changes to the policy and the response of the firm to breaches of the capital policy.
- 9.10 Clearly the Solvency II regime will not change as a result of the Scheme and so the financial strength and security provided by the Solvency II regime will be the same for the Phoenix policies before and after the implementation of the Scheme.
- 9.11 The proposed Scheme will not change the risk appetite or capital policy in accordance with which the PNRFF is managed and the figures in Appendix 2 show that the PNRFF's compliance with the PCP will not be changed as a result of the implementation of the Scheme. As the PCP requires the PNRFF to hold capital in excess of regulatory capital requirements, policyholders in the PNRFF will continue to be afforded a greater level of security than that required under the PRA's rules.
- 9.12 After the implementation of the Scheme, the security of the guaranteed benefits of the PNRFF business will continue to be provided by the same elements listed above. In particular:
- The implementation of the Scheme will have no effect on the technical provisions held in relation to the current PNRFF business.
 - The tables in Appendices 1 and 2 show the current and the projected post-Scheme Solvency II financial strength of Phoenix as at 31 March 2017 and show that:
 - Prior to the implementation of the Scheme:
 - The capital resources of Phoenix covered its SCR with a ratio of 136%; and
 - The excess capital (after capital requirements and PRA approvals) in Phoenix was £591 million.
 - If the Scheme had been implemented on 31 March 2017:
 - The capital resources of Phoenix would have covered its SCR with a ratio of 137%; and
 - The excess capital (after capital requirements and PRA approvals) of Phoenix would have been £624 million.
- 9.13 The Solvency II financial information shows that the implementation of the Scheme is not expected to materially affect the Solvency II position of Phoenix and that Phoenix is projected to be compliant with the requirements of the PCP both before and after the implementation of the Scheme. The implementation of the Scheme will have no effect on the PCP or on the governance around the PCP.
- 9.14 The PNRFF's SCR will increase as a result of the business being transferred. As there is a greater diversification benefit available in Phoenix, the increase in the SCR will be less than the SCR held by AWL before the transfer and therefore, as AWL more than covered this SCR with assets, and all the assets of AWL will be transferred to the PNRFF, this will be to the benefit of the PNRFF.
- 9.15 Furthermore, the implementation of the Scheme will have no effect on:
- The existing reinsurance agreements except for the IGR;
 - The ring-fenced funds of Phoenix; or
 - The potential support that could be provided by the ring-fenced funds in the extreme scenario where the resources of the PNRFF are insufficient to meet its liabilities and the restrictions on the ring-fenced funds break down.

Conclusions regarding financial strength

- 9.16 I am satisfied that the implementation of the Scheme will not have a material adverse effect on the financial strength available to support the security of the PNRFF policyholders' benefits.

The profile of risks to which the PNRFF business is exposed

- 9.17 As set out in Section 8, the PNRFF is exposed to a range of different risk types, including insurance risks and market risks. There are also risks associated with Phoenix's ring-fenced funds, particularly those that currently require shareholder support to meet their capital requirements.

- 9.18 Under the IGR, the transferring business is reinsured to Phoenix, and so the PNRFF is currently exposed to the majority of the risks of the transferring business. AWL retained the following risks under the IGR:
- Counterparty exposure for the pre-existing external reinsurance arrangements;
 - Market and credit risks for the assets backing the capital held in AWL; and
 - Operational risks associated with the above and with past product mis-selling.
- 9.19 The PNRFF will be exposed to these additional risks from the transferring portfolio after the Transfer Date. These risks are similar in nature to risks that the PNRFF is already exposed to and therefore will not change the profile of risks of the PNRFF materially.
- 9.20 I am satisfied that the implementation of the Scheme will not have a material effect on the profile of risks to which the existing PNRFF business policyholders are exposed.

The reasonable expectations of the PNRFF policyholders

- 9.21 The PNRFF business is non-profit or unit-linked in nature and, as such, policyholders' expectations in respect of their benefits are that:
- They receive their contractual benefits as set out under the policy;
 - The policies are operated in accordance with their contractual terms, including the level of charges for unit-linked policies;
 - The administration, servicing, management, and governance of the policies are in line with the contractual terms under the policies and do not deteriorate as a result of the transfer.
- 9.22 The implementation of the proposed Scheme will not change:
- The terms and conditions of the existing PNRFF policies;
 - The methodology used to calculate the surrender values of the PNRFF policies;
 - The charges that apply to the PNRFF policies;
 - The exercise of discretion in respect of the management of the unit-linked funds;
 - The operation of Phoenix, the ring-fenced funds or the PNRFF;
 - The outsourcing and asset management arrangements for the policies of Phoenix and the governance around these, including the performance standards of Phoenix to which these outsourcing and asset management arrangements are held;
 - The management and governance of the PNRFF policies, which will continue to be the responsibility of the Phoenix Board; or
 - The risk appetite to which the PNRFF is managed.
- 9.23 Phoenix management has discretion with regard to the level of charges on existing unit-linked PNRFF business. The extent of this discretion will not be affected by the Scheme.
- 9.24 PGMS provides the administration and servicing of existing Phoenix policies; the terms on which the services are provided will continue to apply to the existing business of Phoenix after the Transfer Date. Separate arrangements will apply to the transferring policies.
- 9.25 I am therefore satisfied that the implementation of the Scheme will not have a material adverse effect on the reasonable benefit expectations of the policyholders of the PNRFF business or on the standards of administration, service, management and governance that apply to the PNRFF business.

Conclusions for the PNRFF business

- 9.26 I am satisfied that the implementation of the Scheme will not have a material adverse effect on:
- The security of benefits of the PNRFF policyholders;
 - The reasonable expectations of the PNRFF policyholders in respect of their benefits; or

- The standards of administration, service, management and governance that apply to the PNRFF policies.

The policies of the Phoenix ring-fenced funds

The security of benefits of the policies of the Phoenix ring-fenced funds

- 9.27 Under the Scheme, there will be no business transferred into or out of the Phoenix ring-fenced funds and no change to the financial strength of these ring-fenced funds.
- 9.28 The unsupported ring-fenced funds do not rely on shareholder support to meet their capital requirements and capital buffer as these are met by surplus within the relevant ring-fenced funds. Currently, there are two supported ring-fenced funds, the Alba WPF and the SAL WPF, which rely on support from the PNRFF to meet their respective capital requirements and capital buffers under the PCP.
- 9.29 Under the Scheme, the AWL business will be transferred into the PNRFF and therefore I need to consider whether the transfer will lead to extra calls on the capital in the PNRFF because this could result in a subsequent restriction of the capital available to support the ring-fenced funds if and when required.
- 9.30 The tables in Appendices 1 and 2, as described in paragraph 9.12, show that the implementation of the Scheme is not expected to have a material effect on the financial strength of the PNRFF and therefore no material impact on the likelihood of extra calls on the capital in the PNRFF or on the capital available if the ring-fenced funds require it.
- 9.31 I am satisfied that the implementation of the Scheme will not have a material adverse effect on the security of the benefits of the policyholders within the ring-fenced funds.

The reasonable expectations of the policyholders of the ring-fenced funds

- 9.32 The implementation of the proposed Scheme will not change:
- The terms and conditions of the existing policies of the Phoenix ring-fenced funds;
 - The principles and practices used in the management of the Phoenix ring-fenced funds;
 - The rights of the Phoenix policies to any future distributions from the inherited estates;
 - The methodology used to calculate asset shares and surrender values of Phoenix with-profits policies;
 - The bonus and pay-out policies applied to Phoenix with-profits policies;
 - The charges that apply to the existing policies of the Phoenix ring-fenced funds;
 - The operation of Phoenix, the ring-fenced funds or the PNRFF;
 - The outsourcing and asset management arrangements for the policies of Phoenix and the governance around these, including the performance standards of Phoenix to which these outsourcing and asset management arrangements are held;
 - The management and governance of the existing policies of the Phoenix ring-fenced funds; or
 - The risk appetite to which Phoenix is managed.
- 9.33 Taking all this into consideration, I am satisfied that the implementation of the Scheme will not have a material adverse effect on the reasonable benefit expectations of the policyholders of the Phoenix ring-fenced funds or on the standards of administration, service, management and governance that apply to the policies of the Phoenix ring-fenced funds.

Conclusions for the policies of the Phoenix ring-fenced funds

- 9.34 I am satisfied that the implementation of the Scheme will not have a material adverse effect on:
- The security of benefits of the policies of the Phoenix ring-fenced funds;
 - The reasonable expectations of the policyholders of the Phoenix ring-fenced funds in respect of their benefits; or

- The standards of administration, service, management and governance that apply to the policies of the Phoenix ring-fenced funds.

Conclusions for the existing Phoenix policies

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

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

10 MY CONSIDERATIONS IN RESPECT OF THE FAIR TREATMENT OF CUSTOMERS

The approach to communication with policyholders

- 10.1 Regulations made under FSMA require a communication regarding the proposed transfer to be sent to every policyholder of the parties under the Scheme. However, this requirement may be waived at the discretion of the Court which will give consideration to issues such as the practicality and costs of sending notices relative to the likely benefits for policyholders of receiving such communications. In order to comply with paragraph 2.53 of the PRA's policy statement on insurance business transfers, the companies would be expected to notify the policyholders, or interested persons, at least six weeks before the date of the Court hearing at which the application to sanction the Scheme will be heard.
- 10.2 All AWL policyholders for whom AWL holds a valid name and address in its database will be sent a mailing about the Scheme prior to the Court hearing. Different communication strategies and mailing packs will be used for the following:
- SunLife policyholders;
 - Individual unit-linked policyholders; and
 - CTIP trustees.
- 10.3 AWL also intends to send mailing packs to Independent Financial Adviser Firms connected with transferring policies and the employee benefit consultants of the CTIP trustees, and to write to any funeral plan providers with an interest in any of the SunLife policies.
- 10.4 The mailing pack for Sun Life policyholders will include a letter which addresses key questions that policyholders may have, a short guide to the Scheme and a summary of the IE's report. A more detailed set of questions and answers will be available on the SunLife website.
- 10.5 The mailing pack for individual unit-linked policyholders will include a covering letter, a Scheme guide and a Questions and Answers leaflet.
- 10.6 For the CTIP business, I understand that AWL and Phoenix will engage with the trustees and their advisers through their business as usual relationship team, providing a guide to the Scheme and a full copy of this report. Where requested, more detailed information about the Scheme will be provided.
- 10.7 AWL and Phoenix will publish a notice in a form approved by the PRA in the following national newspapers in the UK: The Times, The Daily Telegraph, The Sun, The Daily Mirror and The Daily Mail.
- 10.8 AWL and Phoenix propose that the Scheme be notified to the supervisory authorities in all EEA States, and Phoenix intends to request this from the PRA. The transfer will not be advertised in EEA States, as the number of policyholders resident in any EEA state is small (fewer than 150) and they will be contacted as part of the mailing described above.
- 10.9 Phoenix intends to seek waivers from the requirement to send a written notice to the existing policyholders of Phoenix as it believes it would be disproportionate to do so given that:
- There will be no change to the terms and conditions of any Phoenix policies;
 - As described in earlier sections of this report, in my view there will be no material adverse effect on:
 - The security of benefits under any such policies;
 - The governance, servicing and administration arrangements applicable to such policies; and
 - The reasonable benefit expectations under any such policies.
 - The cost of mailing such policyholders is considered disproportionate relative to the benefits to the policyholders that would result from any such mailing.
- 10.10 Assuming the application for the waivers is successful, the existing policyholders of Phoenix will be notified via newspaper advertisements and via the Phoenix website where a scheme guide will be available.
- 10.11 The Chief Actuary of AWL has confirmed that in his view the information contained in notification to policyholders adequately describes the proposals to policyholders.

- 10.12 The Chief Actuary of Phoenix has confirmed that in his view it is reasonable and proportionate that the policyholders holding Phoenix policies will not receive a direct communication in respect of the Scheme.
- 10.13 I am satisfied that the proposed approach to communication with policyholders, including the application for the waiver, is fair and reasonable.

The standards of administration and servicing

- 10.14 Phoenix has an ongoing project (the AXA integration project) to integrate the AWL business with the Phoenix business and, as part of this intends to make changes to the administration of the transferring policies at or soon after the Transfer Date but will seek to maintain the same service levels.
- 10.15 I have discussed this in Sections 5, 6, 7, 8 and 9.
- 10.16 If the changes to the administration systems for the transferring AWL policies are not complete by the Transfer Date then the current arrangements will continue with the current administration systems amended to reflect the change of company.
- 10.17 Phoenix has compiled a list of the changes that would be required to be made to the current administration systems used for the AWL policies and this been sent to AXA Tech who maintains the code for Capita (in respect of the SunLife policies) and ASDL (in respect of the individual and CTIP unit-linked policies). This contingency plan will continue in parallel with the AXA integration project.
- 10.18 I am satisfied that this contingency plan is reasonable and should ensure that the transferring policies do not experience any change to their service levels in the event that the AXA integration project is not complete by the Transfer Date.

The costs of the Scheme

- 10.19 The costs of the Scheme will be borne by the PNRFF. The PNRFF will pay the costs and expenses in relation to the negotiation, preparation, execution, carrying into effect and potential termination of the Scheme. The costs will not be borne by policyholders.
- 10.20 I am satisfied this is reasonable.

Other creditors

- 10.21 AWL and Phoenix have confirmed that there are no bondholders or third parties to securitisation arrangements or any other creditors of either company who would be affected by the proposed Scheme.

The FSCS and the FOS

- 10.22 Implementation of the Scheme will not adversely affect eligibility for compensation from the FSCS for either transferring AWL policyholders or the existing Phoenix policyholders.
- 10.23 In circumstances where AWL currently refers policyholders to the FOS, Phoenix will continue to do so following implementation of the Scheme.
- 10.24 I am satisfied that the implementation of the Scheme will have no impact on the rights of the policyholders of AWL or Phoenix in relation to the FSCS or FOS.

11 MY OTHER CONSIDERATIONS ARISING FROM THE SCHEME

The future operation of the Scheme

- 11.1 If the Scheme is approved by the Court (and subject to any subsequent amendment of the Scheme, as considered below), the Directors of AWL and Phoenix are committed to implementing the Scheme as set out in the Scheme document (and reflected in this report) in accordance with their fiduciary responsibilities under UK company law.
- 11.2 At any time after the Court's sanction of the Scheme, Phoenix and (where applicable) AWL must apply to the Court for sanction of any amendments to it, except where the amendment is considered to be minor or technical, in which case Phoenix must notify the PRA and FCA.
- 11.3 The published financial position of Phoenix will be calculated by the firm's actuaries and accountants and will be subject to external audit. The business being transferred consists of non-profit business and therefore the most important aspect is that Phoenix will continue to meet any guaranteed liabilities and that sufficient resources are put aside to enable this.
- 11.4 In my opinion there are reasonable safeguards in place to ensure that, if approved by the Court, the Scheme will be operated as presented to the Court.

What happens if the Scheme is not implemented?

- 11.5 If the Scheme does not proceed for any reason, then the transferring AWL policies will not become policies of Phoenix and will remain within AWL. In this situation the IGR agreements between AWL and Phoenix will remain in place.

The tax implications of the Scheme

Introduction

- 11.6 In addition to two reports produced by the tax experts within Phoenix, Phoenix has retained one of the big four accounting firms (the "external tax expert") to provide a report to identify significant tax issues arising from the proposed Scheme. I have seen the final version of this report dated 12 July 2017 and have relied, in forming my view on the proposed Scheme, on this report and those produced by the Phoenix staff, as expert opinion on the tax implications of the proposed Scheme.
- 11.7 If the proposed Scheme is implemented:
- There will be no change to the terms and conditions of any of the AWL policies or the AWL registered pension schemes ("RPS") (except for a change to the names of schemes' administrators and product provider to Phoenix), or pensions in payment;
 - No assets will be transferred into or out of any pensions contracts; and
 - Contributions and premiums to, and benefits arising from, the AWL life assurance and pensions contracts will be unchanged.
- 11.8 No formal tax clearances are required from HMRC for the transfer of the AWL life or pensions business but confirmations of understanding are sought from HMRC in order to provide assurance that the tax statuses of the policies, policyholders and RPS are unaffected by the implementation of the proposed Scheme. I understand that such confirmations are not conditions precedent for the Scheme to proceed.

AWL life assurance business

- 11.9 None of the transferring AWL policies are qualifying in the sense defined in Schedule 15 of the Income and Corporation Taxes Act 1988 and so no formal clearances or confirmations are required from HMRC in respect of the AWL transferring life assurance business.

AWL pensions business

- 11.10 No formal clearances are required from HMRC for the transfer of the AWL pensions business and the following confirmations have been sought:
- Section 158, Finance Act 2004: that the statuses of the RPS are unaffected by the transfer;
 - Section 192, Finance Act 2004: that the entitlement to tax relief on contributions to RPS is unaffected by the transfer;
 - Section 164, Finance Act 2004: that no unauthorised payments arise from the transfer; and
 - Section 58, Finance Act 2012: that there is continuity of treatment as pensions business after the transfer.
- 11.11 In addition to these confirmations, Phoenix will also seek clearance from HMRC that the proposed Scheme does not fall under the provisions of the following (these HMRC clearances are not required for the Scheme to proceed):
- Section 132, FA 2012: Transfers of long-term business: anti-avoidance.
 - Section 748, FA2010: Transactions in securities: clearance procedure.
- 11.12 The anti-avoidance provision can apply if the main purpose, or one of the main purposes, of the transfer is an “unallowable” purpose (as defined in Section 132 of FA 2012).
- 11.13 HMRC clearance will be required to make sure the transactions in securities provisions do not apply to the transfer to Phoenix of securities within the AWL unit-linked funds.
- 11.14 As there is not expected to be any tax arising on the transfer and the Part VII is being effected for (in its view) bona fide commercial reasons, based on the information about the reasons for the transaction in the public domain and provided to the external tax expert by Phoenix, the external tax expert has confirmed that it expects the confirmations and clearances to be provided by HMRC.

Value added tax (“VAT”)

- 11.15 Phoenix and AWL are part of the same VAT group and therefore no VAT will be payable as a direct result of the transfer.

Overseas residents

- 11.16 The external tax expert has confirmed that the proposed Scheme is not expected to change the UK tax status of the transferring AWL policies or the tax status of policies where the holders of those policies are resident outside the UK.

Conclusion

- 11.17 I am satisfied that the proposed Scheme will not have adverse tax implications for any policyholders.

The UK referendum on 23 June 2016

- 11.18 In a referendum held on 23 June 2016, a majority voted for the UK to leave the European Union which has led to considerable political upheaval in the UK and significant turbulence in both UK and global financial markets.
- 11.19 Although in the time since June 2016, markets have calmed somewhat, there remains considerable political uncertainty and it is not possible to know at this point what the long-term effects of this referendum result might be for the UK in general and Phoenix in particular.
- 11.20 Sections 8, 9, 10 and 11 show that the implementation of the Scheme is not expected to have a material adverse effect on the financial strength available to provide security to each group of policies nor on the benefit expectations associated with those policies.
- 11.21 Although the referendum result may in time have an effect on the financial strength of Phoenix there is currently no reason to believe that there would not be a similar effect on AWL or that my conclusions regarding the effect of the implementation of the proposed Scheme would be changed materially.
- 11.22 I will cover any further developments in the implications of the referendum result in my Supplementary Report.

The effect of the Scheme on reinsurance counterparties

- 11.23 As noted in Section 5, the conventional term assurance business of AWL is subject to external reinsurance. I understand that these arrangements will continue after the Transfer Date, with Phoenix being the party to the treaties instead of AWL. Therefore the reinsurance counterparties will be subject to default risk in relation to Phoenix, rather than AWL, after the Transfer Date.
- 11.24 Some of the investments of the AWL internal unit-linked funds in external unit-linked funds are structured as reinsurance, and these reinsurance arrangements will continue after the Transfer Date with Phoenix being the party to the arrangements rather than AWL.
- 11.25 AWL and Phoenix will engage with these reinsurance counterparties to give them notice of the Court hearing and to answer any questions they may have regarding the Scheme.
- 11.26 The IGR will terminate as a result of the Scheme.
- 11.27 I am satisfied that the implementation of the Scheme will not materially adversely affect the external reinsurance counterparties of AWL.

The effect of the proposed Scheme on previous schemes

- 11.28 Hogan Lovells, the legal firm retained by AWL and Phoenix in respect of the Scheme has carried out legal reviews of the AWL Schemes and is satisfied that any relevant protections for AWL policyholders have been incorporated into the terms of the new Scheme. Phoenix has also reviewed the terms of the previous schemes to which Phoenix is party and is satisfied that the implementation of the Scheme will not have a material effect on any of these schemes.
- 11.29 As discussed in Section 3, I am satisfied that it is appropriate for me to rely on the conclusions of Hogan Lovells in relation to the Scheme.

The ORSA

- 11.30 The risk profile of Phoenix is not expected to change materially as a result of the implementation of the Scheme.

Approvals under Solvency II

- 11.31 The transferring business will not form part of Phoenix's matching adjustment portfolio and the matching adjustment is unaffected.
- 11.32 The main risks associated with the AWL business are currently reinsured to Phoenix and are included in PGIM and AWL's other risks are similar to the ones to which Phoenix is already exposed.
- 11.33 The changes to the PGIM have been through the appropriate governance procedures in Phoenix. These governance procedures are consistent with those approved by the PRA as part of the PGIM approval process. In particular the changes to the PGIM as a result of the proposed Scheme have been classified by the Actuarial Technical Committee as a "Sub Minor Change" and therefore will not require the approval of the PRA.
- 11.34 The transfer will not trigger a full recalculation of the TMTP and I note that there will be a regular recalculation of the TMTP at 31 December 2017.
- 11.35 I am satisfied that the Scheme will not have a material impact on the PRA approvals granted to Phoenix.

The quality of own funds capital

- 11.36 It is important to assess the extent to which a scheme of transfer affects the quality of Own Funds available to absorb losses and meet unexpected obligations to policyholders.
- 11.37 AWL's Own Funds are entirely comprised of Tier 1 items, i.e. the highest quality in terms of loss absorbency.
- 11.38 Phoenix's Own Funds are approximately 93% Tier 1 items and 7% Tier 2 capital (subordinated loan notes) with an insignificant amount of Tier 3 items.

- 11.39 Following the implementation of the Scheme, Phoenix's own funds will continue to be mainly comprised of Tier 1 items.
- 11.40 Therefore I am satisfied that the implementation of the Scheme will not lead to a material adverse effect on the quality of Phoenix's Own Funds and that any changes in the capital items that constitute Phoenix's Own Funds will not have a material adverse effect on the existing policyholders of Phoenix or the transferring policyholders of AWL.

Developments for Phoenix from 31 March 2017

- 11.41 Since 31 March 2017, there have been a number of actions and events that have affected the financial position of Phoenix. The most significant of these to 30 June 2017 are as follows:
- Management Actions: A number of management actions undertaken by Phoenix have increased the excess of adjusted own funds by c£55m.
 - Valuation Assumptions: A reserving and reporting exercise will be undertaken for Phoenix as at 30 June 2017 and therefore, in line with established practice, the assumptions and methodologies have been reviewed in preparation for that valuation. These changes have been approved by the Board and are estimated to increase the excess of adjusted own funds by c£50m.
 - The payment of a dividend: at its meeting in June 2017, the Phoenix Board approved a dividend payment of £155m, which will reduce the own funds and excess assets by this amount.
 - Changes in market conditions. In particular, since 31 March 2017:
 - Yields in general (and in particular the EIOPA curve) have risen which would be expected to increase solvency;
 - Credit spreads have narrowed, which would be expected to increase solvency; and
 - Equity markets have not moved significantly (and Phoenix is largely protected from equity movements by various hedging strategies) which would not be expected to have a significant effect on solvency.
 - The run-off of the Phoenix business and resulting surplus arising (including the release of capital).
- 11.42 Taking into account all of the above, as at 30 June 2017, Phoenix met its regulatory capital requirements and the more onerous requirements of the PCP. Whilst the solvency position of Phoenix will have been affected by these developments since 31 March 2017, there is no reason to believe that the effect of the Scheme will appear any different based on the results as at 30 June 2017 and therefore no reason to doubt that my conclusions would hold as at 30 June 2017.
- 11.43 In my Supplementary Report, I will provide financial information as at 30 June 2017 and provide more detailed commentary on the effects of the implementation of the proposed Scheme based on the financial information as at 30 June 2017.

12 MY CONCLUSIONS

- 12.1 I confirm that I have considered the issues affecting the policyholders of AWL, and of Phoenix separately (as set out in Sections 8, 9, 10 and 11) and that I do not consider further subdivisions (other than those in this report) to be necessary.
- 12.2 I am satisfied that the implementation of the Scheme will not have a material adverse effect on:
- The security of benefits of the policyholders of AWL and Phoenix;
 - The reasonable expectations of the policyholders of AWL and Phoenix with respect to their benefits; or
 - The standards of administration, service, management and governance applicable to the AWL and Phoenix policies.
- 12.3 I am satisfied that the Scheme is equitable to all classes and generations of AWL and Phoenix policyholders.



Oliver Gillespie

14 July 2017

Fellow of the Institute and Faculty of Actuaries

APPENDIX 1: SELECTED FINANCIAL INFORMATION BEFORE THE IMPLEMENTATION OF THE SCHEME

Solvency II financial information as at 31 March 2017

AWL

£ million	
Assets	6,066
BEL	6,010
Risk Margin	12
TMP	-
Technical provisions	6,021
Own Funds (post TMP)	45
SCR	28
Excess Assets after SCR	17
Capital policy requirement	12
Excess assets after capital policy	5
Solvency coverage (SCR)	163%

Notes:

- 1) The SCR has been produced using the PGIM.
- 2) The results allow for the £5 million dividend payment in the first quarter of 2017.
- 3) The BEL is shown net of reinsurance.

Phoenix

£ million	Unsupported RFFs	Supported RFFs	PNRFF	Total
Assets	13,092	5,414	20,338	38,844
BEL	12,055	5,163	19,121	36,339
Risk Margin	199	177	684	1,059
TMTF	518	372	982	1,873
Technical provisions	11,736	4,968	18,823	35,526
Own Funds (post TMTF)	1,357	446	1,515	3,318
SCR	1,066	401	1,261	2,727
Excess Assets after SCR	290	46	254	591
Capital policy requirement	-	112	302	414
Excess assets after capital policy	290	66	47	177
Solvency coverage ratio	127%	111%	120%	122%
Solvency coverage ratio (excl. unsupported RFFs)				136%

Notes:

- 1) The SCR has been produced using the PGIM.
- 2) The results allow for the £160 million dividend payment in the first quarter of 2017.

APPENDIX 2: SELECTED FINANCIAL INFORMATION AFTER THE IMPLEMENTATION OF THE SCHEME

Solvency II financial information as at 31 March 2017

Phoenix

£ million	Unsupported RFFs	Supported RFFs	PNRFF	Total
Assets	13,092	5,414	26,397	44,903
BEL	12,055	5,163	25,131	42,349
Risk Margin	199	177	689	1,065
TMTF	518	372	982	1,873
Technical provisions	11,736	4,968	24,838	41,541
Own Funds (post TMTF)	1,357	446	1,559	3,362
SCR	1,066	401	1,271	2,737
Excess Assets after SCR	290	46	288	624
Capital policy requirement	-	112	305	417
Excess assets after capital policy	290	66	17	208
Solvency coverage ratio	127%	111%	123%	123%
Solvency coverage ratio (excl. unsupported RFFs)				137%

Notes:

- 1) The SCR has been produced using the PGIM.
- 2) The results allow for the £160 million dividend payment paid in the first quarter of 2017.

APPENDIX 3: CERTIFICATE OF COMPLIANCE

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

I confirm that I am aware of, and have complied with, the requirements applicable to experts set out in Part 35 of the Civil Procedure Rules, Practice Direction 35 and Guidance for the instruction of Experts in Civil Claims 2014. As required by rule 35.10(2) of Part 35 of the Civil Procedure Rules and by paragraph 3.2(9)(b) of Practice Direction 35, I hereby confirm that I have understood, and have complied with, my duty to the Court.

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

APPENDIX 4: DATA RELIED UPON

In addition to discussions (both orally and electronically) with Phoenix staff, I have relied upon the public and non-public information shown in the table below in formulating my conclusions:

Document	Date of document
Scheme of transfer	7 July 2017
Capital policy of Phoenix	4 October 2016
Capital policy of AWL	8 November 2016
Report of the Chief Actuary of Phoenix on the Scheme	13 July 2017
Report of the Chief Actuary of AWL on the Scheme	13 July 2017
Pre- and post-Scheme financial information as at end 2016 for AWL	21 April 2017
Pre- and post-Scheme financial information as at end 2016 for Phoenix	21 April 2017
Pre- and post-Scheme financial information as at end March 2017 for AWL	5 July 2017
Pre- and post-Scheme financial information as at end March 2017 for Phoenix	5 July 2017
The ORSA of Phoenix	6 December 2016
Solvency II Pillar 1 (Internal Model) Entity Report for PLL – 31 December 2016	13 March 2017
The reinsurance treaties between AWL and Phoenix	9 November 2016
The report of the Independent Tax Expert on the tax implications of the Scheme	12 July 2017
First witness statement of Andrew Moss	24 April 2017

APPENDIX 5: GLOSSARY OF TERMS

A glossary of abbreviations used throughout the report is given below.

A	
APS	Actuarial Profession Standards
Asset share	A measure of a policy's value in the absence of guarantees, defined as the total premiums paid by policyholders, accumulated by actual investment returns, less attributable expenses, benefits paid and other relevant deductions.
B	
BAU	Business as usual
BEL	The best estimate liability under Solvency II
C	
CA	Chief Actuary
Capita	Capita Life & Pensions Services Limited
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CRO	Chief Risk Officer
CTIP	Corporate Trustee Investment Plans
D	
Diligenta	Diligenta Limited
E	
EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
Excluded Policies	AWL policies that cannot be transferred to Phoenix
F	
FA	Finance Act (followed by the year of that Act – e.g. 2004, 2010 or 2012)
FCA	Financial Conduct Authority
FOS	Financial Ombudsman Service
FPH	Friends Provident Holdings
FRR	Financial Resources Requirement
FSA	Financial Services Authority
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
FTSE	Financial Times Stock Exchange

H

HMRC	HM Revenue & Customs
Hogan Lovells	Hogan Lovells International LLP

I

IE	Independent Expert
IGR	Intra-Group Reinsurance
ITS	Implementing Technical Standards

L

LTF	The long-term insurance Fund
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M

MA	Matching Adjustment
MAP	Matching Adjustment Portfolio
MCR	Minimum Capital Requirement

N

NPF	Non-profit Fund
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O

ORSA	Own Risk and Solvency Assessment
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P

PCP	The Phoenix Capital Policy
PGIM	The Phoenix Group internal model
PGMS	Pearl Group Management Services
Phoenix	Phoenix Life Limited
PLAL	Phoenix Life Assurance Limited
PLHL	Phoenix Life Holdings Limited
PNRFF	The Phoenix Non Ring-Fenced Fund
PRA	The Prudential Regulation Authority

R

RFF	Ring-fenced funds
RPI	Retail Price Index
RPS	Registered pension scheme
RTI	Real Time Information

S

SCR	Solvency Capital Requirement
SHF	Shareholders' Fund
SIMF	Senior Insurance Management Functions
SIMR	The PRA's Senior Insurance Managers Regime

T

TAS	Technical Actuarial Standards
TCF	Treating Customers Fairly
TMTP	Transitional Measure on Technical Provisions
Transfer Date	The date on which the transfer is effected (expected to be 8 December 2017)

V

VA	Volatility Adjustment
VAP	Volatility adjustment portfolio

W

WPA	With-Profits Actuary
WPC	With-Profits Committee
WPF	With-Profits Fund

APPENDIX 6: COMPLIANCE WITH THE PRA POLICY STATEMENT

The table below indicates how I have complied with the provisions of the PRA Policy Statement (“The Prudential Regulation Authority’s approach to insurance business transfers”, dated April 2015) that pertain to the form of the Scheme Report.

PRA Policy Statement reference	Requirement	Scheme Report paragraph reference
2.30 (1)	Who appointed the Independent Expert and who is bearing the costs of that appointment	1.9
2.30 (2)	Confirmation that the independent expert has been approved or nominated by the appropriate regulator.	1.23
2.30 (3)	A statement of the independent expert's professional qualifications and (where appropriate) descriptions of the experience that fits him for the role	1.21 - 1.22
2.30 (4)	Whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest	1.24 - 1.25
2.30 (5)	The scope of the report	1.13 - 1.20
2.30 (6)	The purpose of the scheme	7.1 - 7.2
2.30 (7)	A summary of the terms of the scheme in so far as they are relevant to the report	7.3 - 7.23
2.30 (8)	What documents, reports and other material information the independent expert has considered in preparing his report and whether any information that he requested has not been provided	Section 1, Appendix 3
2.30 (9)	The extent to which the independent expert has relied on: (a) information provided by others; and (b) the judgment of others	Section 1, Section 3, Appendix 3
2.30 (10)	The people on whom the independent expert has relied and why, in his opinion, such reliance is reasonable	1.28
2.30 (11)	His opinion of the likely effects of the scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee	8.78 Not applicable 9.26, 9.34
2.30 (12)	His opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme	Section 11
2.30 (13)	What matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in his opinion, be relevant to policyholders' consideration of the scheme	1.20
2.30 (14)	For each opinion that the independent expert expresses in the report, an outline of his reasons.	Sections 8, 9, 10 and 11
2.32 (1)	The summary of the terms of the scheme should include a description of any reinsurance agreements that it is proposed should pass to the transferee under the scheme	7.7

2.32 (2)	The summary of the terms of the scheme should include a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred	Not applicable
2.33 (1)	The independent expert's opinion of the likely effects of the scheme on policyholders should include a comparison of the likely effects if it is or is not implemented	Sections 8, 9, 10 and 11
2.33 (2)	The independent expert's opinion of the likely effects of the scheme on policyholders should state whether he considered alternative arrangements and, if so, what	Section 2
2.33 (3)	The independent expert's opinion of the likely effects of the scheme on policyholders should, where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences he considers may be material to the policyholders	Sections 8, 9, 10 and 11
2.33 (4)	<p>The independent expert's opinion of the likely effects of the scheme on policyholders should include his views on:</p> <p>(a) the effect of the scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;</p> <p>(b) the likely effects of the scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect:</p> <p>(i) the security of policyholders' contractual rights;</p> <p>(ii) levels of service provided to policyholders; or</p> <p>(iii) for long-term insurance business, the reasonable expectations of policyholders; and</p> <p>(c) the cost and tax effects of the scheme, in so far as they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations</p>	Sections 8, 9, 10 and 11
2.35 (1)	For any mutual company involved in the scheme, the report should describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders	Not applicable
2.35 (2)	For any mutual company involved in the scheme, the report should state whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights	Not applicable
2.35 (3)	For any mutual company involved in the scheme, the report should comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without.	Not applicable
2.36 (1)	For a scheme involving long-term insurance business, the report should describe the effect of the scheme on the nature and value of any rights of policyholders to participate in profits	9.32
2.36 (2)	For a scheme involving long-term insurance business, the report should, if any such rights will be diluted by the scheme, how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders;	Not applicable
2.36 (3)	For a scheme involving long-term insurance business, the report should describe the likely effect of the scheme on the approach used to determine:	9.22, 9.32, 9.33

	(a) the amounts of any non-guaranteed benefits such as bonuses and surrender values; and	
	(b) the levels of any discretionary charges	
2.36 (4)	For a scheme involving long-term insurance business, the report should describe what safeguards are provided by the scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm	Section 11
2.36 (5)	For a scheme involving long-term insurance business, the report should include the independent expert's overall assessment of the likely effects of the scheme on the reasonable expectations of long-term insurance business policyholders	8.1 - 8.78
2.36 (6)	For a scheme involving long-term insurance business, the report should state whether the independent expert is satisfied that for each firm the scheme is equitable to all classes and generations of its policyholders	12.2
2.36 (7)	For a scheme involving long-term insurance business, the report should state whether, in the independent expert's opinion, for each relevant firm the scheme has sufficient safeguards (such as principles of financial management or certification by a with-profits actuary or actuarial function holder) to ensure that the scheme operates as presented.	Section 11
