Supplementary Report of the Chief Actuary of Utmost Life and Pensions Limited on the proposed transfer of business from Equitable Life Assurance Society

Rob Kerry, Chief Actuary

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1. INTRODUCTION

1.1. SCOPE AND PURPOSE OF THE REPORT

In July 2019 I prepared a report ("the Report") for the Board on the proposed transfer of the business of Equitable Life Assurance Society ("ELAS") to Utmost Life and Pensions Limited ("ULP") under Part VII of the Financial Services and Markets Act 2000 ("the Transfer Scheme"), with the exception of policies written under Irish or German law which will be excluded from the Transfer Scheme and remain in ELAS. That report detailed my assessment of the impact of the Transfer Scheme on the financial security of ULP policyholders and their benefit expectations.

This report, my "Supplementary Report", is written for ULP's Board ("the Board") in my capacity as Chief Actuary of ULP. Its purpose is to provide the Board of ULP with an update on my assessment of the impact of the Transfer of the business of ELAS to ULP taking into account the responses from EEA regulators, from customers in response to the policyholder communication and for events, including the updated financial position, since my Report. I am a Fellow of the Institute and Faculty of Actuaries and was appointed as Chief Actuary of ULP on 13th December 2018.

The report may be used by the following in support of their assessments of the impact of the Transfer Scheme:

- the Chief Actuary ("CA") and With-Profits Actuary ("WPA") of ELAS;
- the WPA of ULP
- the Independent Expert ("IE") for the Transfer Scheme
- the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA"), together referred to as the "Regulators"; and
- the Court(s), to assist with the sanctioning of the Transfer Scheme

In particular, I have considered an updated analysis of the impact of the Transfer Scheme on the financial security of ULP policyholders (section 5) and their benefit expectations (section 6). In section 7 I have also considered non-financial aspects, such as the likely impact on service standards, which ensure that policyholders are treated fairly. This Supplementary Report compares the position following the Transfer with the current position and considers the situation if the Transfer does not proceed.

The impact on the policyholders of ELAS is outside the scope of this report.

1.2. REGULATORY AND PROFESSIONAL GUIDANCE

In preparing this report I have taken account of relevant professional standards and Technical Actuarial Standards as published by the Actuarial Profession and the Financial Reporting Council, in particular: APS L1: Duties and Responsibilities of Life Assurance Actuaries, APS X2: Review of Actuarial Work, TAS 100 (Principles for Technical Actuarial Work and TAS 200 (Insurance). I do not believe there have been any departures from these standards in performing this work. This report has been peer reviewed for the purposes of APSX2 by Feryal Nadeem, the Chief Risk Officer of ULP.

1.3. RELIANCES AND LIMITATIONS

In preparing this report I have relied on the accuracy and completeness of data and information provided to me, both written and oral, by ELAS and the Utmost Group of Companies. My report also relies on analysis that has been carried out internally on the effect of the Transfer on the capital position of ULP. I have relied on these being materially correct given the reliance on information provided by ELAS.

2. SUMMARY OF CONCLUSIONS

2.1. RESPONSES FROM POLICYHOLDERS AND EEA REGULATORS

I have considered the responses from existing policyholders of ULP received up to the date of this report and have not identified any concerns that would lead me to change my conclusions.

Since the date of my Report, ULP has been granted passport authorisations on a freedom of services basis into France, the Republic of Ireland and Denmark.

2.2. SECURITY OF POLICYHOLDER BENEFITS

I have considered the security of the existing ULP policyholders before and after the Transfer and am satisfied that the level of capital coverage will be maintained at a level sufficient to provide adequate security for policyholder benefits.

2.3. POLICYHOLDER BENEFIT EXPECTATIONS

I am satisfied that the Transfer Scheme does not change the level of expected benefits for the existing ULP policyholders. In particular the terms of the policies remain unaltered by the Transfer Scheme, including any options or guarantees included in the contracts as well as the benefits payable on surrender, maturity, or any other insured event occurring.

2.4. GOVERNANCE AND SERVICE STANDARDS

I have considered the Company's plans for the integration of ULP and ELAS, and in particular the Company's plans to maintain the service provided to ULP's existing customers. I am satisfied that these plans and the Transfer Scheme does not adversely affect the level of oversight and governance of the fair treatment of ULP policyholders. The existing Service Standards for ULP will continue to apply after the transfer.

3. CHANGES TO THE TRANSFER SCHEME

3.1. EFFECT AND PURPOSE

The effect of the Transfer Scheme is to transfer the business of ELAS to ULP, except for policies written under Irish or German law which will be excluded from the Transfer Scheme and remain in ELAS. The Transfer Scheme also transfers the investment management, reinsurance and administration contracts that support the management of the transferring business. The Transfer Scheme is expected to take effect from 1 January 2020. The Transfer Scheme cannot proceed unless the Scheme of Arrangement also proceeds and the two schemes are expected to be implemented on the same date.

Following the majority vote by the members on 1 November 2019, the court sanction of the Scheme of Arrangement will mean that ULP will become the sole member of ELAS, effectively making ELAS a subsidiary of ULP.

3.2. CHANGES SINCE MY REPORT

Since my report, there has been a change made to the Order for the Transfer Scheme to make it explicit that prior to the Transfer being implemented, ULP will have Eligible Own Funds of at least 150% of its estimated Solvency Capital Requirement ('SCR') immediately after the effective date of the Scheme. Further, if following calculation of the actual Solvency II balance sheet immediately after the effective time of the Transfer, it is determined that the Eligible Own Funds were not at least equal to 150% of the SCR then further additional capital will be provided such that the Eligible Own Funds are at least equal to 150% of the SCR at the Effective Time.

It should be noted that this does not provide a guarantee that the Eligible Own Funds of ULP will be at least 150% of the SCR after that date. After the effective date of the Scheme, the capital position of ULP will be managed in line with its existing capital policy as set out in section 6. of my Report.

4. FINANCIAL IMPACT OF THE TRANSFER SCHEME

4.1. ESTIMATED BALANCE SHEETS

Estimated balance sheets for ULP showing the solvency position on a Solvency II basis pre and post Transfer are shown below. These values are estimates and the final position will be dependent on many factors, including the development of both the ELAS and ULP business until the transfer date, the implementation of the ELAS Scheme of Arrangement and economic factors up to the implementation date.

4.1.1. ULP PRE TRANSFER BALANCE SHEET

Table 4.1 shows the base balance sheet for ULP before the Transfer. This is based on the 30 June 2019 Solvency II results.

Table 4.1 ULP balance sheet as at 30 June 2019 before Transfer

30 June 2019 £m	NPF	WPSF1	WPSF2	WPSF4	WPSF6	Total
Assets	1,410.8	30.9	12.8	118.6	102.9	1676.1
Reinsurance	-12.2	0.0	0.0	-6.3	0.0	-18.5
Assets	**1,398.6**	**30.9**	**12.8**	**112.3**	**102.9**	**1,657.5**
Best Estimate Liability						
BEL (excl. FDB)	1,285.4	6.1	6.0	86.2	80.4	1,464.2
Future Discretionary Benefits (FDB)	0.0	7.1	6.8	26.1	22.5	62.5
Risk Margin	31.0	0.0	0.0	0.3	0.3	31.6
Transitional Deduction (TD)	-30.6	0.0	0.0	-0.3	-0.3	-31.2
Technical Provisions (Post - TD)	**1,285.8**	**13.2**	**12.8**	**112.4**	**102.9**	**1,527.0**
Own Funds	**112.8**	**17.7**	**0.0**	**0.0**	**0.0**	**130.5**
Ring Fenced Fund Restriction	0.0	-17.7	0.0	0.0	0.0	-17.7
Tier 2 Capital Restriction	-2.1	0	0	0	0	-2.1
Eligible Own Funds	**110.7**	**0.0**	**0.0**	**0.0**	**0.0**	**110.7**
Solvency Capital Requirement	**64.8**	**0.1**	**0.1**	**0.5**	**0.4**	**65.8**
Solvency Coverage Ratio						**168%**

The Solvency Coverage ratio as at 30 September 2019 was 151%, mainly due to a fall in risk free interest rates between June and September. At the time of writing, risk free rates have risen, which would be expected to lead to an improvement in the solvency coverage position.

4.1.2. ULP POST TRANSFER BALANCE SHEET

Table 4.2 shows the estimated balance sheet of ULP, assuming the Transfer occurred at 30 June 2019.

ULP's capital policy requires the SCR coverage of ULP to be at least 150% as at the Effective Date and a capital injection from the Utmost Group of Companies into ULP to achieve this level of coverage has been included in the assets of NPF post-transfer.

Table 4.2 ULP estimated balance sheet as at 30 June 2019 post Transfer.

30 June 2019 £m	NPF	WPSF1	WPSF2	WPSF4	WPSF6	Total
Assets	7,616.1	30.9	12.8	118.6	102.9	7,881.3
Reinsurance	356.9			-6.3		350.6
Assets	**7,973.0**	**30.9**	**12.8**	**112.3**	**102.9**	**8,231.9**
Best Estimate Liability						
BEL (excl. FDB)	7,610.6	6.1	6.0	86.2	80.4	7,798.3
Future Discretionary Benefits (FDB)		7.1	6.8	26.1	22.5	62.5
Risk Margin	84.4					84.4
Technical Provisions (Post - TD)	**7,694.9**	**13.2**	**12.8**	**112.3**	**102.9**	**7,936.1**
Own Funds	**278.1**	**17.7**	**0.0**	**0.0**	**0.0**	**295.8**
Ring Fenced Fund Restriction		-17.7				-17.7
Eligible Own Funds	**278.1**	**0.0**	**0.0**	**0.0**	**0.0**	**278.1**
Solvency Capital Requirement	**184.3**	**0.1**	**0.1**	**0.5**	**0.4**	**185.4**
Solvency Coverage Ratio						**150%**

It should be noted that the estimated post transfer balance sheet allows for ULP to be capitalised to give a Solvency Coverage Ratio of 150% at the date of the transfer.

The Transfer Scheme would trigger a recalculation of the Transitional Deduction. I expect that following a recalculation ULP would be unable to recognise a Transitional Deduction. The table above therefore shows the capital position of ULP post transfer with no Transitional Deduction.

4.1.3. KEY IMPACTS

SCR Coverage

The Capital Policy SCR coverage illustrates the continued security for policyholders as a result of the injection of assets to a coverage level of 150%, as required by ULP's Capital Policy. An initial injection of capital will be received in advance of the Implementation Date based on the estimated Solvency Capital Requirement and, if required, additional capital will be received in early 2020. The capital injection required to achieve a coverage level of 150% has been guaranteed by Oaktree.

There is no impact on the coverage for benefits in the with-profits sub-funds. These continue to have their own ring fenced assets which are not affected by the Transfer. These funds do however benefit from the security provided by the company level SCR coverage and capital support from the Non Profit Fund.

Capital Policy of ULP compared to ELAS

The capital policy of ULP remains to seek to maintain a capital ratio (Eligible Own Funds / SCR) in excess of 135% at all times. In practice, in order to ensure that this level is not breached, ULP aims to have a Capital Coverage Ratio of 150% immediately after the payment of any dividends (or loan repayments).

Similarly, interest on regulatory debt would only be paid if this would not result in the capital ratio falling below 150%. If paying interest would result in the capital ratio falling below 150% then the interest would be accrued until such time as it could be paid without resulting in the capital ratio falling below 150%.

In the unlikely event of solvency failing to satisfy its minimum capital ratio of 135% SCR, ULP will need to consider the appropriate actions to take to ensure a recovery to this level of solvency within no more than six months.

If the solvency ratio was not expected to recover organically within six months, ULP would need to implement management actions to reduce the required recovery period to six months or less. Such management actions could include raising additional capital from investors in order to immediately recapitalise ULP to at least a 135% SCR ratio.

For the purpose of calculating coverage ratios under the capital policy, the own funds restriction on ring fenced funds will be applied at the level of the capital coverage of ULP in its entirety, rather than 100% of (notional) SCR.

Any capital in excess of the level required to cover 150% SCR would be available to pay interest on the regulatory debt or to pay dividends (subject to maintaining an appropriate level of liquidity). To the extent that the company does not have sufficient distributable reserves to pay dividends consistent with the capital policy, ULP would seek to lend the excess amount up to a parent company pending the creation of additional distributable reserves through either organic means or from a capital reduction process.

In contrast, the existing capital policy of ELAS is

- "*To maintain a reasonable margin over the assessed level, the Society expects the ratio of the available capital to the required capital on both measures to exceed 120%.*
- *To enable timely action if this limit is in danger of being breached, if either ratio fell below 150%, consideration would be given to reducing Policy Values and the Capital Distribution Amount to restore the solvency position.*
- *Should either ratio fall below 120%, such action would be almost certain. These parameters may be amended by the Society if that is considered appropriate.*"

ELAS considers its capital policy on both a regulatory basis and on its own internal assessments. As I have only been provided with information on the regulatory basis, I am only able to make a comparison of the capital policy on this basis.

In essence, although both companies aim to have a level of SCR cover at 150%, ELAS's initial action available is to reduce the capital distribution to customers, which it will consider if the coverage falls below 150%. Other actions are also considered and once a SCR coverage of 120% is reached it is almost certain that the capital distribution would have been reduced. The ELAS capital policy also does not include a view as to how long it is expected to take to restore the solvency coverage. As a mutual, ELAS also does not have the ability to raise additional capital from investors. In contrast, ULP aims to maintain a level of solvency coverage after the payment of a dividend in excess of 150%, and considers actions to maintain solvency coverage above 135%, with the aim of restoring that coverage within 6 months. On this basis, ULP takes management actions to maintain solvency coverage at a higher level than ELAS.

In conclusion I am satisfied that as this policy will continue, there will be no adverse impact on policyholder security as a result of the Transfer.

4.1.4. BREXIT

There has been continued uncertainty about the UK's exit from the European Union. This has resulted in significant volatility in interest rates, and the reduction in interest rates to 30 June 2019 is the main factor behind the change in the Company's solvency coverage rate since the end of 2018. I continue to monitor the capital position of the company and the impact it has on the capital injection required to achieve a coverage level of 150% at the effective date of the Transfer.

5. IMPACT ON SECURITY OF POLICYHOLDER BENEFITS

5.1. CAPITAL COVERAGE

The primary indicator of security of benefits under the ULP policies after the Transfer is the financial strength of ULP and this is derived principally from the level of assets held to back the liabilities and the capital held in ULP. This is illustrated by the SCR coverage figures shown in Section 4.1. Under its existing capital policy, ULP could pay a dividend provided that the solvency coverage level remains above 150% after payment. The change in the capital coverage for ULP from 168% to 150% does not therefore represent a materially adverse change in the security of policyholder benefits.

The security of benefits is also affected by the risk profile of the company. The table below compares the top 5 risks before and after the transfer, and the percentage of the total undiversified risk capital. The nature of the top 5 risks is unchanged, although there is greater exposure to lapse, equity and expense risk after the transfer arising from the greater concentration of unit-linked business. After the transfer, the risks are more diverse, with a lower proportionate exposure to spread risk. This change in the risk profile is reflected in the SCR and is therefore recognised in the extent of capital that is held to cover these risks.

Before Transfer	After Transfer
Spread (48%)	Lapse (27%)
Expense (18%)	Equity (21%)
Equity (16%)	Spread (19%)
Longevity (15%)	Expense (19%)
Lapse (14%)	Longevity (8%)

In addition, financial strength (and therefore security of benefits) is also affected by the options available to a company to increase its SCR coverage following adverse experience. These options include the ability to take management actions (for example hedging the risks from exposure to volatile assets such as equities) or to raise additional capital. These are not changed as a result of the Transfer.

I have also considered the projected capital position of ULP under a range of more extreme adverse scenarios. These include; the effect of an increase in the number of customers taking their benefits, both in the short term following the Scheme of Arrangement and over the longer term; the effect of a very significant fall in equity and property markets; and increase in expenses; falls in interest rates; and combinations of the above. Some of these scenarios are more extreme than the 1-in-200 stresses that are used to determine the Solvency Capital Requirement. In all these scenarios ULP continues to able to cover its Solvency Capital Requirement after the adverse event and in the scenarios where the solvency coverage ratio falls below 150% the projections show that the coverage ratio recovers so that ULP is able to cover its capital policy.

6. IMPACT ON POLICYHOLDER BENEFIT EXPECTATIONS

My analysis of the impact on benefit expectations relies on the following two key policies, the policy for the management of non-profit discretion and the PPFM. There have been no changes to these for the existing ULP business since my Report.

7. ONGOING MANAGEMENT OF THE BUSINESS

7.1. GOVERNANCE

There have been no changes to the governance arrangements for ULP since my Report.

7.2. INVESTMENT MANAGEMENT

Since my Report, and separately to the Transfer, the Company has negotiated a reduction in the investment management fees. This reduction in costs reduces the expense risk to which the company is exposed.

7.3. SERVICE STANDARDS

The Company is planning to integrate the services provided to both the existing ULP customers and the transferring ELAS customers. The existing administration systems and service standards for ULP customers will be maintained as part of that integration and plans are in place to ensure adequate staffing levels during the integration in order to maintain service levels during that period. Consequently, I am satisfied that there should be no materially adverse impact on service standards as a result of the Transfer.

Conclusion

I am satisfied that there is are no adverse impacts on policyholders as a result of the Transfer.

8. COMMUNICATION WITH POLICYHOLDERS

8.1. RESPONSES FROM POLICYHOLDERS

ULP has written to all contactable policyholders as described in my Report. Of the total number of policyholders, to the date of this Supplementary Report only 1,111 letters have been returned as "gone aways" (1.5%) of the total number mailed.

So far a total of 522 enquiries have been received from existing ULP customers, either by phone or in writing. 416 of these have been 'business as usual' enquiries or complaints.

The 106 enquiries that relate to the transfer have been categorised as;

- 52 policyholders wanted to know why ULP had written to them. We explained that this was because of the transfer of the ELAS business.
- 26 policyholders asked what would happen to their policy. It was explained to them that their policy would continue with Utmost with no changes.
- 12 policyholders want to know if they needed to do anything. They were advised to study the material available and advised that if they felt they were adversely affected they had the right to raise an objection.
- 6 policyholders requested copies of the documentation. This was provided to them.
- 4 policyholders asked if they were materially adversely affected by the transfer. They were referred to the report of the Independent Expert and my Report and advised that if they felt they were adversely affected they had the right to raise an objection.
- 2 policyholders asked if they would receive a payment on completion of the Transfer; they will not.
- 1 policyholder asked which fund the transferring ELAS policies would be held in. He was informed that they will be held in the non-profit fund.
- 1 policyholder asked about the timeline for the completion of the Transfer, and he was advised that it is expected to complete on 1 January 2020.
- 1 policyholder asked if the administration of their policy would continue to be based in Tunbridge Wells, and was advised that there would be no change and he would be able to contact ULP using the same telephone numbers and address as before
- 1 policyholder asked about the timeline for the completion of the transfer, and was advised that this was 1 January 2020, and that any changes to this date would be posted on the ULP website.

To the date or writing, no objections have been received from ULP policyholders.

Conclusion

I am satisfied that the responses from customers do not raise any concerns or issues that affect my conclusions.

APPENDIX A – GLOSSARY

Within this report and other Appendices I have used the following terms.

AMC	Annual Management Charge
BEL	Best estimate liability
CA	Chief Actuary
Criterion	Criterion Life Assurance Ltd
Effective Date	The date on which the Transfer Scheme will take effect, expected to be 1 January 2020.
EIOPA	European Insurance and Occupational Pensions Authority
ELAS	The Equitable Life Assurance Society
Eurolife	Eurolife Assurance Company Ltd
Family Assurance	Family Assurance Friendly Society
FCA	Financial Conduct Authority
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
HOFS	Hearts of Oak Friendly Society
IE	Independent Expert to the Transfer Scheme, Richard Baddon of Deloitte
Industrial Branch	Insurance business, either endowments or whole of life contracts, originally sold by door-to-door collectors
Utmost Group of Companies	A specialist European life assurance group founded with the aim of acquiring and managing life insurance businesses across the UK and Europe.
MA	Matching Adjustment
Mutual	A mutual insurance company is one that is owned by its members
Non-Profit	Policies where benefit payments are not linked to performance of a with-profits fund
NPF	The non-profit fund of ULP.
Oaktree	Oaktree Capital Management
Ordinary Branch	Insurance business that is not Industrial Branch, including savings, pension, annuity, protection and whole of life contracts.
Own Funds	The excess of assets over Technical Provisions under Solvency II. Where own funds are within a ring-fenced fund, amounts in excess of the notional SCR for that ring-fenced fund are ignored at a company level for solvency purposes
PPFM	Principles and Practices of Financial Management, regulations require a PPFM document to be maintained in respect of With-Profits funds.
PRA	Prudential Regulation Authority
RAO	Regulated Activities Order for the purposes of FSMA 2000

Regulators	The PRA, FCA and equivalent regulators in other jurisdictions. Key regulators in other jurisdictions are the Jersey Financial Services Commission and the Guernsey Financial Services Commission who will consider the Channel Island Schemes
Ring-fenced	A set of assets and liabilities where there are restrictions over the use of the assets elsewhere in the business
Risk Margin	Part of Technical Provisions under Solvency II intended to represent the cost of holding SCR in respect of non-hedgeable risks
RL Services	RL Services Ltd (UK). The service company which employs the current employees and services the ULP business.
RMIS	Reliance Mutual Insurance Society Limited or RMIS (RTW). The name was changed to RMIS (RTW) following the transfer to ULP.
RMLA	RM Life Assurance Ltd, previously SEB Trygg Life (UK) Assurance Company Ltd
SCR	Solvency Capital Requirement under Solvency II regulations
SCR Coverage	The ratio of Own Funds to SCR. For the purpose of the ULP capital policy, this is calculated assuming the restriction on own funds within a ring-fenced fund applies at the level of the SCR coverage for the company
Technical Provisions	Amounts to cover insurance liabilities under Solvency II. This includes the best estimate liabilities and risk margin
the Arrangement	This proposed Scheme of Arrangement under Part 26 of FSMA for the creditors of ELAS that must proceed for the Transfer Scheme to proceed and vice versa.
the Board	The Board of Directors of Utmost Life and Pensions Limited
the Transfer	This proposed transfer of all the business of ELAS to Utmost Life and Pensions Limited.
the Transfer Scheme	The legal document setting out the terms for the Transfer.
TMTP or TD	Transitional Measures on Technical Provisions is a transitional measure allowed under the Solvency II Regulations. It allows companies to transition the impact of certain some elements of the new Solvency II measures in over a period of time, subject to regulatory approval.
ULAS	University Life Assurance Society
ULP	Utmost Life and Pensions Limited.
Unit-Linked	Policies where benefit payments are linked to performance of one or more underlying investment funds
With-Profits	Policies where benefit payments are increased by bonuses reflecting the underlying performance of a with-profits fund. Changes in bonus rates are often smoothed.
WPA	With-Profits Actuary
WPC	With-Profits Committee
WPSF	With-Profits sub-fund

WPSF SCR Coverage	Measure used to assess the financial strength of a with-profits sub fund. It is defined as the surplus funds plus any loss absorbing capacity of technical provisions as a percentage of the basic notional SCR of the sub fund. The basic notional SCR is the SCR for that fund on a standalone basis, before operational risk and loss absorbing capacity of technical provisions and deferred tax is applied