

# Report of the Independent Expert

**Report of the Independent Expert on the proposed  
Scheme of Arrangement between holders of certain  
policies in the Liver Ireland Sub-Fund and Royal  
London Insurance DAC**

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# 1 INTRODUCTION

## Background

- 1.1 The Royal London Mutual Insurance Society Limited ("**RLMIS**") is a mutual life insurance company, incorporated and authorised in the United Kingdom ("**UK**").
- 1.2 Royal London Insurance DAC ("**RLI DAC**") is a life insurance company incorporated and authorised in Ireland. RLI DAC is a direct and wholly-owned subsidiary of RLMIS.
- 1.3 RLMIS is conducting a significant project (the "**Legacy Simplification Project**") to rationalise and simplify its fund structure, products, and administration systems to generate operational efficiencies, reduce risk and improve customer outcomes.
- 1.4 The rationalisation of RLMIS's fund structure involves the consolidation into its Royal London Open Fund (the "**RL Open Fund**") of a number of blocks of business, which at the start of the Legacy Simplification Project were managed in separate with-profits funds or sub-funds (the "**Consolidating Funds**").
- 1.5 The Legacy Simplification Project has been ongoing for some time and has already seen a number of the Consolidating Funds moved into the RL Open Fund (none of which had any impact on RLI DAC). It is now proposed that, subject to the necessary approvals, RLMIS's Royal Liver Sub-Fund (the "**Liver Fund**") will be consolidated into the RL Open Fund (the "**Liver Fund Consolidation**").
- 1.6 The proposal to consolidate the Liver Fund into the RL Open Fund has an impact on RLI DAC as, in addition to the Liver Fund's having liabilities in respect of certain UK policyholders of RLMIS, it also has (via inwards reinsurance) liabilities in respect of certain policyholders of RLI DAC. Following the transfer of Royal Liver's Irish policies from RLMIS to RLI DAC in 2019, the liabilities in respect of those policies were reinsured by RLI DAC to RLMIS.
- 1.7 From a legal standpoint, it is proposed that the Liver Fund Consolidation would involve the following:
  - A scheme of arrangement ("**SOA**") in the UK (the "**UK Scheme**"), pursuant to Part 26 of the Companies Act 2006, the purpose of which is to enable the consolidation of the Liver Fund into the RL Open Fund, which would be presented to the High Court of Justice of England and Wales (the "**English High Court**") for sanction;
  - A concurrent SOA in Ireland (the "**Liver Ireland Scheme**" or the "**Scheme**"), pursuant to Part 9 of the Irish Companies Act 2014, in respect of the eligible policyholders in the sub-fund maintained by RLI DAC for its ex-Royal Liver business (the "**Liver Ireland Sub-Fund**"), which would be presented to the High Court in Ireland (the "**Irish High Court**").
- 1.8 For completeness, I note that, in addition to the Liver Fund consolidation, RLMIS also intends to consolidate its Phoenix Life Assurance Limited ("**PLAL**") Sub-fund (the "**PLAL Fund**") into the RL Open Fund by amending the terms of the PLAL Fund's existing sunset provisions.
- 1.9 There would be no change to the current fund structure of RLI DAC as a result of these proposals.
- 1.10 Further background on the proposals can be found in section 5.

## My role as Independent Expert

- 1.11 Although it is not a requirement of the Irish Companies Act 2014, RLI DAC has appointed me, Michael Culligan, a Principal with Milliman Limited ("**Milliman**"), to perform the role of independent expert in relation to the proposed Liver Ireland Scheme ("**Independent Expert**"). I understand that the Central Bank of Ireland ("**CBI**") has indicated to RLI DAC that it has no objection to my appointment.
- 1.12 The terms of my appointment are governed by the engagement letter between Milliman and RLI DAC dated 16 July 2020. In summary, my role as Independent Expert is to consider the proposed Liver Ireland Scheme and its effects on the policyholders of RLI DAC, and whether it meets the overall requirement of being fair and reasonable to those policyholders.
- 1.13 My principal duties as Independent Expert are:
  - to prepare of a report on the terms of the Liver Ireland Scheme (i.e., this report) (the "**Irish IE Report**" or "**this Report**");
  - to prepare a summary of this Report for inclusion in the policyholder communications in relation to the Liver Ireland Scheme; and,

- to prepare any supplemental reports as may be required.

- 1.14 As the UK Scheme and the Liver Ireland Scheme will be co-dependent and, as certain RLI DAC policies are reinsured to RLMIS, I will need, when considering the Liver Ireland Scheme, also to understand and consider the terms of the UK Scheme. In this Report, I use the terms “**the proposed Schemes**” or “**the Schemes**” to cover the two SOAs as a whole.
- 1.15 Separately, RLMIS has appointed my colleague, Nick Dumbreck, from Milliman LLP in the UK to perform the role of independent expert (the “**UK Independent Expert**”) in relation to the proposed UK Scheme and the proposed amendment to the existing Scheme governing its PLAL business. The terms of his appointment are covered under a separate agreement between RLMIS and Milliman LLP.

### My credentials and independence

- 1.16 I am a Fellow of the Society of Actuaries in Ireland (“**SAI**”) and have over 30 years' experience in the Irish life insurance industry. I have served as the Head of Actuarial Function (and, previously, the Appointed Actuary) to a number of Irish insurers. I have also previously fulfilled the role of Independent Actuary on a number of occasions in relation to transfers of long-term insurance business under Section 13 of the Assurance Companies Act 1909 (the “**1909 Act**”) that have been approved by the Irish High Court.
- 1.17 In relation to my independence:
- I am not a member of RLMIS;
  - I do not have any policies with RLI DAC, RLMIS, or any affiliated companies; and,
  - I am not a member of a pension scheme administered by RLI DAC, RLMIS or any affiliated companies.
- 1.18 Milliman has, over the years, undertaken a number of consulting assignments for RLI DAC and its predecessor entities in Ireland. However, these assignments have been small and infrequent, and I do not believe that any work undertaken by Milliman with RLI DAC, or with any of its predecessor entities in Ireland, would create a conflict of interest for me in my role as Independent Expert.
- 1.19 Based on the foregoing I consider that I am in a position to act independently in my assessment of the proposed Scheme.

### This Report

- 1.20 The purpose of this Report is to set out my views on the proposed Liver Ireland Scheme and its likely effect on, and fairness to, all RLI DAC policyholders (including, but not limited to, the RLI DAC policyholders with policies whose benefits are reinsured into the Liver Fund).
- 1.21 In assessing the impact of the implementation of the proposed Liver Ireland Scheme on the policyholders of RLI DAC, and whether those policyholders would be treated fairly and reasonably if the proposed Scheme were to be implemented, I have adopted a number of criteria against which I assess the terms and conduct of the Liver Ireland Scheme, and the fairness and reasonableness of any proposed product changes that may apply.
- 1.22 Further details on my approach to assessing the proposed Scheme are set out in section 8.

### Reliances

- 1.23 In preparing this Report, I have had access to certain documentary evidence provided by RLI DAC and RLMIS, the principal elements of which I list in Appendix A to this Report. In addition, I have had access to, and discussions with, the senior management of both RLI DAC and RLMIS. My conclusions depend on the substantial accuracy of this information, and I have relied on this information without independent verification. There are no documents or other information that I have requested and that have not been provided.
- 1.24 Neither I, nor any member of my team, is a qualified legal or tax expert. In order to get a sound legal understanding of the Schemes I considered it necessary to obtain independent legal advice and I have relied upon the independent legal advice provided to me or the UK Independent Expert by Freshfields Bruckhaus Deringer LLP (“**Freshfields**”) in relation to certain aspects of the Schemes.
- 1.25 RLMIS and RLI DAC have been advised by their own legal advisers, Pinsent Masons LLP (“**Pinsent Masons**” or the “**external legal advisers**”), and, in respect of certain matters, I have reviewed the legal advice provided by Pinsent Masons and have relied on that advice in reaching my conclusions on the basis set out in Section 8. I have described

in Section 8 why I believe it is reasonable to rely on advice given to RLMIS and/or RLI DAC by Pinsent Masons. For the avoidance of doubt, Pinsent Masons has no liability to me in respect of that advice.

- 1.26 RLMIS has conducted a review of the Scheme and the UK Scheme to assess the effect of the Schemes on the UK and Ireland tax liabilities of the Included Policyholders. I am satisfied that RLMIS's in-house tax team has the relevant expertise and that it is therefore reasonable for me to rely on their advice. The report produced by RLMIS's in-house tax team has been shared with me.
- 1.27 I am not an expert in tax matters and hold no qualifications in UK or Ireland tax and have therefore relied on the conclusions of RLMIS's in-house tax team and the external tax experts retained by RLMIS. It should be noted, however, that the external tax experts have not been retained by me and have no liability to me for any advice provided to RLMIS that has been made available to me in my assessment of the Scheme.
- 1.28 This Report is based on the information available to me at, or prior to, 10 June 2022, and takes no account of developments after that date.

### Limitations

- 1.29 This Report, and any extract or summary thereof, has been prepared specifically and solely within the context of the assessment of the terms of the proposed Liver Ireland Scheme. No liability will be accepted by Milliman, or me, for any application of this Report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of this Report (or any summary thereof). Judgments as to the conclusions contained in this Report should be made only after studying the report in its entirety. Furthermore, conclusions reached by the review of a section or sections on an isolated basis may be incorrect. Draft versions of this Report should not be relied upon for any purpose.
- 1.30 This Report is for the exclusive benefit of RLI DAC, the Irish High Court and any other courts to which the Irish IE Report must be submitted to implement the Liver Ireland Scheme. Subject to paragraph 1.32 below, the Irish IE Report may not be disclosed or supplied to any other party without my prior specific written agreement. I do not and will not accept any responsibility, duty of care or liability to any person other than RLI DAC in relation to the Irish IE Report.
- 1.31 I have prepared a summary of this Report which will be provided to the Court and will be included in the Circular that will be sent to the Eligible Policyholders. No other summary of this Report may be made without my written consent and, in particular, no other summary of this Report may be distributed to policyholders without my prior approval.
- 1.32 The Irish IE Report may be made generally available by RLI DAC on its website and filed by RLI DAC with the Irish High Court in connection with the Liver Ireland Scheme. RLI DAC may also circulate copies of the Irish IE Report (together in each case with the summary that I have provided) to:
- those of its policyholders who ask for a copy;
  - the directors of, and professional advisors retained by, RLI DAC, and those employees of RLI DAC or their affiliates who are involved in the development of the Liver Ireland Scheme;
  - the CBI, the Prudential Regulation Authority in the UK, the Financial Conduct Authority in the UK, or any other relevant regulatory authorities;
  - the lawyers and brokers dealing with or representing individual claimants in relation to the RLI DAC business; and,
  - such other persons (including any regulators) who are entitled to receive the Irish IE Report by virtue of any court order or any other requirement of law.
- 1.33 This Report should be read together with the other documents relating to the proposed Liver Ireland Scheme.

### Professional guidance

- 1.34 This Report has been prepared in accordance with the requirements of Actuarial Standard of Practice ("ASP") PA-2 (which covers "General Actuarial Practice") (version 1.2, effective 1 March 2022), issued by the SAI.
- 1.35 Whilst not strictly applicable to my work as Independent Expert, I have also had regard to the provisions of ASP LA-6 (version 2.3, effective 1 September 2021), entitled "Transfer of long-term business of an authorised insurance company – role of the independent actuary" and issued by the SAI.

- 1.36 In addition, ASP PA-2 requires SAI members to consider whether their work requires peer review. In my view this Report does require peer review. To meet this requirement and, in accordance with Milliman quality assurance requirements, this Report has been peer reviewed by a Principal of Milliman LLP in the UK.

### Terminology

- 1.37 This Report contains various technical terms which I need to use in assessing the proposed Scheme. Those terms are written in bold font when first defined in this Report and are also listed in the glossary in Appendix B.

### Structure of this report

- 1.38 The remainder of this Report is structured as follows:
- An Executive Summary is provided in section 2.
  - RLMIS's business is summarised in section 3.
  - Section 4 provides a summary of the business of RLI DAC.
  - Section 5 summarises the proposed Scheme.
  - The process and timetable for the proposed Scheme is set out in section 6.
  - The proposed approach to communicating with policyholders is summarised in section 7.
  - In section 8, I set out the basis on which I will assess the proposed Scheme.
  - My assessment of the proposed Scheme is set out in sections 9 to 15.
  - My conclusions are set out in section 16.
  - Appendix A lists the principal data sources I relied upon in carrying out my work.
  - A glossary of terms is provided in Appendix B.
  - An overview of the regulatory regime applying to the two companies is set out in Appendix C.



## 2 EXECUTIVE SUMMARY

### Background and context

- 2.1 RLMIS is conducting a significant Legacy Simplification Project to rationalise and simplify its fund structure, products, and administration systems to generate operational efficiencies, reduce risk and improve customer outcomes.
- 2.2 As part of that project, RLMIS now proposes to consolidate the Liver Fund into the RL Open Fund.
- 2.3 This would have an impact on RLI DAC as, in addition to its UK business, the Liver Fund also has (via inwards reinsurance) liabilities in respect of certain policyholders of RLI DAC.
- 2.4 From a legal standpoint, it is proposed that the consolidation would involve the following:
  - The UK Scheme, an SOA, the purpose of which is to enable the consolidation of the Liver Fund into the RL Open Fund, which would be presented to the English High Court for sanction;
  - A concurrent SOA in Ireland – the Liver Ireland Scheme – in respect of the eligible policyholders in the Liver Ireland Sub-Fund, which would be presented to the Irish High Court.
- 2.5 In parallel, RLMIS also proposes to amend the existing Scheme governing its PLAL business, to consolidate the PLAL Fund into the RL Open Fund.
- 2.6 There would be no change to the current fund structure of RLI DAC as a result of these proposals.
- 2.7 Further background on the proposals can be found in section 5.

### My role as Independent Expert

- 2.8 RLI DAC has appointed me to act as the Independent Expert in relation to the Liver Ireland Scheme. In summary, my role as Independent Expert is to consider the proposed Liver Ireland Scheme and its effects on the policyholders of RLI DAC, and whether it meets the overall requirement of being fair and reasonable to those policyholders.
- 2.9 In addition to preparing this Report on the terms of the Liver Ireland Scheme, I have also prepared a summary of this Report for inclusion in the policyholder communications in relation to the Liver Ireland Scheme and will also prepare any supplemental reports that may be required.

### Summary of the impact of the proposed Liver Fund Consolidation on RLI DAC

- 2.10 RLI DAC is to enter into a compromise with the Ireland Eligible Policyholders (set out in section 5) through the Liver Ireland Scheme to be sanctioned by the Irish High Court (subject to the vote). This will take effect if both the Irish and UK Schemes are sanctioned.
- 2.11 In summary, the proposals with respect to RLI DAC in relation to the Liver Ireland Business are as follows:
  - The Liver Ireland Sub-Fund will be retained.
  - The Liver Ireland Business would continue to be fully reinsured to RLMIS, with the cover provided by the RL Open Fund rather than the Liver Fund. The reinsurance would continue to support the capital requirements of the Liver Ireland Sub-Fund in line with the internal capital management framework. The reinsurance would continue to be supported by collateral, provided by the RL Open Fund, and the collateral terms would be largely unchanged.
  - RLI DAC will make an offer to eligible Liver Ireland Business policyholders whereby, in return for agreeing to the payment of a Scheme Contribution to the RL Open Fund, they would receive an immediate one-off percentage increase to their prospective benefits.
  - The eligible Liver Ireland Business policies would benefit from the distribution of the Liver Fund Estate in the same way as the eligible UK Liver policyholders (in keeping with the principle of both being treated the same).
  - There would be no change to the bonus setting arrangements, including the ability to apply management actions, currently in operation (although there would be no further estate distributions).
- 2.12 More details on the proposed Scheme are provided in sections 5 and 6.

### Information provided

- 2.13 I have been provided with all of the information I sought to allow me to discharge my role as Independent Expert. This included information on RLMIS and RLI DAC, information on the proposed Schemes, and responses to my questions.
- 2.14 I summarise the information provided on RLMIS in section 3, and the information provided on RLI DAC in section 4. The main aspects of the proposed Schemes are summarised in sections 5 and 6, and the approach to policyholder communications is outlined in section 7. Appendix A contains a list of the principal items of information provided.

### Key assumptions

- 2.15 In assessing and reaching my conclusions on the proposed Scheme, I have assumed that:
- the Liver Reinsurance Agreement ("**LRA**") will remain in place post-Scheme; and,
  - the PLAL Fund will be consolidated into the RL Open Fund on 31 December 2022.
- 2.16 I have disclosed and discussed my assumptions with RLMIS and RLI DAC, and they have not raised any objections. My assessment of the proposed Scheme also includes an assessment of the position should neither of these assumptions prove correct.

### My approach to assessing the proposed Scheme

- 2.17 In section 8, I set out the approach I take in assessing the proposed Scheme.
- 2.18 The purpose of my assessment is to form an opinion on whether the policyholders of RLI DAC are being treated fairly and reasonably as a result of the implementation of the Liver Ireland Scheme.
- 2.19 In assessing the proposed Scheme, I have considered the extent to which the Scheme meets a series of tests which I have adopted and which I term "**Fairness Tests**". Those tests cover the following topics:
- Security of policyholders' benefits;
  - Policyholder outcomes;
  - Adverse scenarios;
  - Policyholder communications
  - Policyholder vote; and,
  - Fair conduct.
- 2.20 The details of the Fairness Tests are set out in section 8 of this Report.
- 2.21 I consider the implications of the proposed Scheme separately for the following groups:
- Ireland Included Policyholders who would remain as policyholders of the Liver Ireland Sub-Fund if the Scheme is implemented;
  - Policyholders of the Liver Ireland Sub-Fund who are not Ireland Included Policyholders, for example holders of heavily-in-the-money policies, non-profit policies (except Contingent Bonus ("**CB**") policies) and unit-linked policies; and,
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.
- 2.22 My assessment of the Scheme against each of the Fairness Tests is set out in sections 9 to 14 of this Report.

### My conclusions

- 2.23 As set out in sections 8 to 15 of this Report, I have considered the effects of the proposed Liver Ireland Scheme on all RLI DAC policyholders, subdivided into the groups set out in 2.21 above.
- 2.24 In summary, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on RLI DAC policyholders with regard to:
- the security of their guaranteed benefits;

- their reasonable benefit expectations; and
- their servicing, administration, management, and governance arrangements.

2.25 I am further satisfied that:

- The Scheme would remain fair and reasonable under a range of circumstances and scenarios.
- The information that has been or is to be provided to RLI DAC policyholders in respect of the Scheme is clear, concise, and of an appropriate level of detail, and has or will have been provided to RLI DAC policyholders with sufficient time for them to assess the proposals and make an informed decision regarding the vote.
- The proposal to include uncontactable policyholders within the scope of the Scheme is appropriate.
- The proposed approach to the policyholder vote is fair and reasonable.
- In respect of the following areas the conduct of RLI DAC in respect of the proposed Liver Ireland Scheme is fair and reasonable to all RLI DAC policyholders:
  - The approach to eligibility for the Offer.
  - The approach to the allocation of the costs of the Scheme and the wider Legacy Simplification Project.
  - The treatment of uncontactable policyholders.
  - The compulsion of non-respondents and those who vote against the Offer.

2.26 I am therefore satisfied that the requirements of the Fairness Tests set out in Section 8 have been met.

2.27 This Report is based on the information available to me at 10 June 2022. I will prepare a Supplementary Report which will provide an update on my conclusions in the light of any significant events or developments that may have occurred since the date of this Report.

2.28 In particular, I will address the following in my Supplementary Report:

- An update on the effect of the implementation of the Schemes based upon more up to date financial information and on any other material developments since the date of this Report.
- The results of the policyholder votes for the UK Scheme and the Liver Ireland Scheme.
- The actual response rates and policyholder comments in relation to the UK Scheme and the Liver Ireland Scheme.
- The communication materials in respect of the Liver Ireland Scheme due to be issued to RLI DAC policyholders after the implementation of the Schemes.
- Consideration of the non-respondents and those who vote against the Offer, and whether these groups of policyholders might be more likely to suffer an adverse outcome as a result of the UK Scheme and the Liver Ireland Scheme.
- Any significant events or market changes that may occur between the finalisation of this Report and the finalisation of my Supplementary Report.

### 3 BACKGROUND TO RLMIS

#### History and background

- 3.1 RLMIS is a mutual life insurance company that is the parent entity of the Royal London Group (“**RLG**”). RLG operates in the protection, retirement, savings, and investments markets, and operates primarily in the UK.
- 3.2 RLMIS has a number of subsidiaries within RLG, including an Irish subsidiary: RLI DAC, which is an insurance company incorporated and authorised in Ireland. Certain business of RLMIS was transferred to RLI DAC with effect from 1 January 2019, and RLI DAC was authorised by the CBI to write new life insurance business with effect from that date. Further details on RLI DAC are provided in section 4.

#### Current fund structure

- 3.3 As a result of its history of mergers and acquisitions and following some recent consolidations (see paragraph 3.61 below), the long-term fund of RLMIS now has four sub-funds.
- 3.4 The principal fund is the RL Open Fund. Following the recent consolidations, the RL Open Fund currently consists of Royal London Ordinary Branch (“**RLOB**”), Royal London Industrial Branch (“**RLIB**”), Police Mutual Assurance Society Limited (“**PMAS**”), Refuge Assurance Ordinary Branch (“**RAOB**”), Refuge Assurance Industrial Branch (“**RAIB**”), United Friendly Industrial Branch (“**UFIB**”), United Friendly Ordinary Branch (“**UFOB**”) and Scottish Life (“**SL**”) with-profits business. There is also non-profit and unit-linked business in the RL Open Fund.
- 3.5 The RL Open Fund is open to new business and the estate<sup>1</sup> is distributed to RLIB, RLOB, RAOB, UFOB and a sub-group of SL with-profits policyholders through “**ProfitShare**” (as defined in paragraph 3.123 below), as well as being used to fund the further expansion of RLMIS.
- 3.6 The other three ring-fenced sub-funds, which are closed to new business (collectively the “**RLMIS Closed Funds**”), are:
- Liver Fund;
  - PLAL Fund; and
  - Royal London (CIS) (“**RLCIS**”) Fund.
- 3.7 The following table provides some overview information on the funds.

**Table 1: Summary information on RLMIS Funds**

	RL Open	Liver	PLAL	RLCIS
Fund size at 31 March 2022	£89,525m	£1,972m	£448m	£28,547m
Open to new business?	Yes	No	No	No
To be consolidated into RL Open Fund?	–	Yes	Yes	No

Source: Information provided by RLMIS

- 3.8 As part of its Legacy Simplification Project, RL is proposing (subject to obtaining the relevant approvals) to consolidate the Liver Fund and PLAL Fund into the RL Open Fund by the end of 2022.
- 3.9 Further information is provided below on each of the four existing funds in turn, starting with the Liver Fund.

<sup>1</sup> The “estate” of a with-profits fund is the excess value of its assets over the value of its liabilities.

## The Liver Fund

### INTRODUCTION

- 3.10 Royal Liver Assurance Limited ("**Royal Liver**") was an incorporated Friendly Society originally established in 1850. Royal Liver was authorised in both the UK and Ireland, having an Irish branch operation, with a mix of ordinary branch and industrial branch business in both jurisdictions.
- 3.11 RLMIS acquired the business of Royal Liver in 2011. On 1 July 2011 the life and pensions business and related assets and liabilities of Royal Liver were transferred into the Liver Fund, by way of a transfer under an Instrument of Transfer ("**IoT**") pursuant to section 86 of the Friendly Societies Act 1992 in the UK. Further details on the IoT are provided below, starting at paragraph 3.23.

### NATURE OF BUSINESS WRITTEN

- 3.12 The nature of the Royal Liver business, i.e. organic growth supplemented by acquisitions, means that there is a wide range of products within the Liver Fund.
- 3.13 The business within the fund includes:
- With-Profits life and pensions business, with a mixture of both Conventional With-Profits ("**CWP**") business (both Industrial Branch ("**IB**") and Ordinary Branch ("**OB**")) and Unitised With-Profits ("**UWP**") business;
  - Non-profit life and pensions business; and,
  - Unit-linked life and pensions business.
- 3.14 Each type of business is spread across a range of originating companies:
- Royal Liver (UK and Ireland)
  - London and Manchester ("**L&M**"), later Friends Provident (UK WP IB only)
  - CSAAS (UK NP only)
  - Caledonian (Ireland only)
  - Irish Life (Ireland IB only)
  - GRELI (Ireland unit-linked only).
- 3.15 In addition to directly-written business, the Liver Fund also contains Irish business reinsured in from RLI DAC (see section 4 for more details).
- 3.16 The main features of each of the product groups may be broadly summarised as follows:

#### With-profits

- 3.17 There is a wide range of with-profits products within the Liver Fund. These include Whole of Life Endowments (Mortgage, Low Cost), With-Profits Bonds, Deferred Annuities, Retirement Annuity Contracts, Personal Pensions and Personal Investment Plans.
- 3.18 Further details on the management of the with-profits business in the Liver Fund are set out below, starting at paragraph 3.40.

#### Non-profit

- 3.19 As for with-profits, there is a wide range of non-profit policies in the Liver Fund. These span both Life and Pensions and include: Annuities, Whole of Life, Term Assurance (including Level, Decreasing and Increasing varieties), Mortgage Protection, Critical Illness, Income Benefit, Pensions Term and Convertible Term Assurance, Death in Service Protection and miscellaneous Rider Benefits.
- 3.20 A special category of the non-profit business is the CB policies. These are IB policies that were written by Royal Liver in both the UK and Ireland and provide a certain fixed payment on death or maturity, and in some cases on a periodic basis. The policies are non-profit in nature but share in the surplus distributions of the estate of the Liver Fund (the "**Liver Fund Estate**") when they are triggered. These surplus distributions can be removed from the policy in certain exceptional circumstances (as is the case for the with-profits policies) but overall increase the fixed payment on death or maturity through a final bonus.

### Unit-linked

- 3.21 The unit-linked business also covers both Life and Pensions and includes: Whole of Life, Personal Pensions, Personal Investment Plans, Stakeholder Pensions, Tax Exempt Bonds, and Flexible Income Benefit (WOL).

### Summary

- 3.22 An overview of the various product groups as at 31 March 2022 is provided in Table 2.

**Table 2: Number of policies in the Liver Fund as at 31 March 2022**

Origin	Product type	Number of policies	
		UK	Ireland
Liver	CWP OB and IB Life	11,113	8,726
	Non-profit CB policies <sup>(1)</sup>	169,569	67,970
	Other non-profit OB and IB Life	470,682	138,772
	Unit-linked Life	3,398	287
	UWP Life	1,127	229
	CWP Pensions <sup>(2)</sup>	333	-
	Non-profit Pensions (annuities)	3,954	575
	Non-profit Pensions(other)	-	-
	Unit linked Pensions	12,043	465
	UWP Pensions	17,342	4,456
	Non-profit OB Life (Progress)	36,970	-
L&M	CWP IB Life <sup>(3)</sup>	20,108	-
	Non-profit IB Life	81,500	-
Caledonian	CWP Life	-	350
	UWP Life	-	1,573
	Non-profit Life	-	31,271
	CWP Pensions	-	1,074
	Non-profit Pensions (annuities)	-	859
	Non-profit Pensions (other)	-	8
GRELI	Unit-linked Investments Bonds and Whole Life	-	113
Irish Life	CWP IB Life	-	29,474
	Non-profit IB Life	-	74,749
<b>Total</b>		<b>828,139</b>	<b>360,951</b>

Source: Information provided by RLMIS

#### Notes:

(1): These are the non-profit CB policies that are entitled to uplifts to their claim amounts when a distribution is made from the Liver Fund Estate, as set out in paragraph 3.20.

(2): Including CSAAS policies.

(3): These are the with-profits policies that do not receive distributions from the Liver Fund Estate, as set out in paragraph 3.40.

## OPERATION

### Instrument of Transfer

- 3.23 The IoT is the legal document which sets out the terms upon which Royal Liver's business was transferred to Royal London. Certain provisions of the IoT were amended and superseded by the RLI DAC Transfer Scheme (described in Section 4) and so together they govern how the business of the Liver Fund is managed. In particular, they include:
- Core Principles of Financial Management ("CPFM") (including bonus setting and estate distribution).

- The establishment of the Liver Supervisory Committee ("**LSC**"), whose responsibility it is to monitor the management of the Liver Fund; to ensure it operates in compliance with the IoT including the CPFM and the Royal Liver Principles and Practices of Financial Management ("**Royal Liver PPFM**").
- Expense provisions under which the Liver Fund paid an amount specified via an expense tariff arrangement (the "**rate card**"), to the RL Open Fund, which was responsible for paying the actual expenses incurred by the Liver Fund. The original unit rates in the rate card expired on 1 December 2021. Since then, the asset shares of the Liver Fund have been charged with the actual expenses plus a margin, in line with the rate card.
- Capital support arrangements for the Liver Fund from the RL Open Fund.
- Minimum service standards for the business of the Liver Fund.
- Provisions for the cessation of the Liver Fund when the total asset shares of with-profits policies in the fund fall below a certain value.

3.24 For the avoidance of doubt, where this Report refers to the IoT governing aspects of the management of the Liver Fund, this includes the provisions of the RLI DAC Transfer Scheme as appropriate.

#### Governance

3.25 As noted above, the LSC was established under the terms of the IoT, with responsibility to monitor the management of the Liver Fund for the benefit of all Liver policies (including those sold in Ireland). The LSC operates in compliance with the IoT including the CPFM, the Royal Liver PPFM and the Liver Ireland Sub-Fund With-Profits Operating Principles ("**Liver Ireland Sub-Fund WPOP**").

#### Rate card

3.26 Until recently, to cover its expenses the Liver Fund paid an amount specified via the rate card, which is set out in the IoT, to the RL Open Fund. The RL Open Fund was responsible for paying the actual expenses incurred in servicing the policies in the Liver Fund.

3.27 The original unit rates in the rate card expired on 1 December 2021. Since then, asset shares of policies allocated to the Liver Fund have been charged with the actual expenses plus a margin (of 7.5%), in line with the rate card. For the allocation of the charges and expenses between policy types beyond what is set out in the rate card, the aim is to ensure that each policy is charged, implicitly or explicitly, an amount which represents a fair proportion of the total charges and expenses incurred, using accepted actuarial techniques (as set out in the Royal Liver PPFM).

3.28 Within 12 months of the expiry of the original unit rates in the rate card (so by 1 December 2022), RLMIS was required to review the charges being made against what would have been charged had the relevant services been provided by a relevant third-party provider. Based on this test, if it was found that services could be provided more cost effectively by a third party, they would either be outsourced, or the charges would be lowered to meet market rates. RLMIS conducted this review shortly after the expiry of the rate card with no changes being required. This is a one-off obligation and there is no legal requirement for RLMIS to review the rate card again after this date.

3.29 As specified in the IoT, the Liver Fund pays to the RL Open Fund a separate investment management charge, expressed as a percentage of the value of all assets held in the Liver Fund. This proportional charge includes a margin over actual investment management expenses incurred.

3.30 As agreed in 2011 when the Royal Liver business was transferred to RLMIS, the charges for administration and investment management services, as set out above, are intended to continue until the Liver Fund is collapsed under the Liver Sunset Clause (described in paragraphs 3.36 to 3.39 below), which is expected to be in 2041. After this point, the Liver Fund policies will be charged 'at cost' for both administration and investment management services, i.e. the 7.5% margin on actual expenses and the margin above cost in the investment management charge will be removed.

3.31 The Conduct of Business Sourcebook ("**COBS**") issued by the Financial Conduct Authority ("**FCA**") in the UK includes a rule (COBS 20.2.23R) that requires firms to only charge costs to a with-profits fund which have been, or will be incurred in operating the with-profits fund. To allow it to apply the agreed terms of the transfer in relation to the level of charges to be levied on the Liver Fund, RLMIS sought a waiver to modify the application of this COBS rule in 2011, which would enable it to charge the Liver Fund amounts in excess of the cost of providing it with administration and investment management services. This waiver was granted by the Financial Services Authority ("**FSA**") (the UK's financial services regulator at that time) to cover the first 20 years of the arrangement. At that time, this was the longest term that the FSA was prepared to grant for a waiver (to any firm).



- 3.32 Therefore, to continue to apply the current charging structure in line with the IoT after 30 June 2031 (the end of the 20-year initial waiver period), RLMIS would need to apply for a new waiver to modify the application of COBS 20.2.23R whilst the Royal Liver business remains in the Liver Fund.

#### Exceptional costs

- 3.33 The IoT allows all exceptional costs, expenses, fees and charges related to the marginal cost of implementing major legislative, regulatory or tax changes that are mandatory and reasonably attributable to the Liver Fund to be met by the Liver Fund Estate. However, the IoT limits the circumstances under which exceptional costs may be attributed to the Liver Fund, and requires RLMIS to use reasonable endeavours to mitigate or minimise any exceptional cost attributable to the Liver Fund.
- 3.34 The allocation of such costs should be on a fair and equitable basis, as determined by the RLMIS Board, having regard to the advice of the RLMIS With-Profits Actuary ("**WPA**") and the RLMIS Chief Actuary, and subject to the approval of the WPA, the With-Profits Committee ("**WPC**") and the LSC.
- 3.35 Any exceptional costs apportioned to the Liver Fund would be charged to the Liver Fund Estate in full (rather than to asset shares), and thus, all else being equal, reduce the potential for future estate distributions to with-profits policies and CB policies.

#### Sunset clause

- 3.36 The Liver Fund is a ring-fenced fund, with policies invested in a pool of assets that is separate from those attributable to RL Open Fund policies. In general, as a ring-fenced fund reduces in size, it becomes increasingly difficult to manage its portfolio of investments and to distribute surpluses fairly and smoothly amongst the remaining policies. In recognition of this the CPFM in the IoT contains a sunset clause (the "**Liver Sunset Clause**").
- 3.37 The IoT prescribes that once the value of the Liver Fund's asset shares falls below two specific trigger limits the Liver Fund *may* (if the higher of the two limits, the "**Liver Sunset May Threshold**", is breached) or *must* (if the lower of the two limits, the "**Liver Sunset Must Threshold**", is breached) be collapsed and on doing so the remaining Liver Fund Estate must be distributed to the asset shares, or claim amounts as applicable, of eligible Liver policies. The IoT also prescribes that the Liver Sunset Clause cannot be operated while the LRA remains in place.
- 3.38 On current projections, it is expected that the Liver Sunset May Threshold will be breached around in or around 2031 and that the Liver Sunset Must Threshold will be breached in or around 2041. In absence of the proposed Scheme, once the sunset clause has been triggered the Liver Fund Estate would be distributed and all policies allocated to, or invested in, the Liver Fund would be consolidated into the RL Open Fund, with the RL Open Fund expected to cover the capital requirements of these policies.
- 3.39 Due to the capital requirements of Solvency II, which were not anticipated in the IoT, the Liver Fund is required to hold a higher level of capital than was the case when the IoT was first implemented. As a result, if the Liver Sunset May Threshold were breached, but the value of the Liver Fund's asset shares was still materially higher than the value required to breach the Liver Sunset Must Threshold, RLMIS would not consolidate the Liver Fund without compensation from the Liver Fund Estate to the RL Open Fund in return for supporting the ongoing capital requirements. Payment of such compensation is not permitted under the IoT and so the Liver Fund would not be collapsed at this time. However, the Liver Fund would be collapsed, and the Liver Fund Estate distributed in full, if the Liver Sunset Must Threshold was breached (without compensation to the RL Open Fund). RLMIS therefore considers the date on which the lower Liver Sunset Must Threshold is breached to be the "**Liver Sunset Point**".

#### Management of the with-profits business

- 3.40 All of the with-profits policies in the Liver Fund (for the avoidance of doubt, both UK and Ireland) are eligible to participate in distributions of the Liver Fund Estate with the exception of the L&M business. This is set out in the IoT.
- 3.41 The Uniform Return Method ("**URM**") is used to calculate the return that is allocated to UK and Ireland policyholders' asset shares in a consistent manner. The primary aim of the URM is to ensure that UK and Ireland policies receive the same absolute rate of return, in local currency terms, without any adverse or beneficial impacts on the Liver Fund Estate.
- 3.42 Bonuses for the UK business are set by RLMIS and those for the Irish business (reinsured into the Liver Fund) are set by RLI DAC. The RLI DAC Board (with advice from the RLI DAC Head of Actuarial Function ("**HoAF**") would generally set bonuses consistent with those set by the RLMIS Board, who will have taken input from RLI DAC and the UK With-Profits Governance Structure.
- 3.43 All of the with-profits policies, including L&M policies, in the Liver Fund can have management actions enforced to reduce their benefits in adverse conditions. To the extent that any management actions have been taken in the past



which have reduced the benefits to the L&M policies, these deductions will be restored ahead of the Liver Fund Estate being distributed to all other Eligible Policies.

- 3.44 Under the terms of the IoT and the Liver Capital Framework (described in paragraphs 3.95 to 3.98), any excess in the Liver Fund Estate above its capital target should be distributed in full through asset share enhancements to with-profits policies (excluding L&M policies) and increases to the claim amounts of CB policies. There would be no distributions from the Liver Fund Estate if the excess capital is below this capital target.
- 3.45 In 2023, the enhancement to asset shares and increase to claim amounts for the eligible policies of the Liver Fund and Liver Ireland Sub-Fund as part of business as usual operations (the "BAU uplift") is expected to be 1.8%. This would be declared based on the financial position of the Liver Fund on 31 December 2022, but applied to eligible policies on 1 July 2023. The BAU uplift in 2022 is 3.6%, which is due to be applied to eligible policies on 1 July 2022.
- 3.46 Within the Liver Fund (including the reinsured Liver Ireland Sub-Fund policies), the amount by which pay-outs on maturity and death vary from one year to the next are smoothed for similar with-profits policies with similar terms. This is done by comparing asset shares to the pay-out on similar policies in the previous year. The size of the Liver Fund Estate, i.e. the strength of the capital position of the Liver Fund, is taken into account when deciding the extent of smoothing of pay-outs.
- 3.47 RLMIS currently maintains a number of annual bonus scales for with-profits policies in the Liver Fund. Final bonuses are added to guaranteed benefits to provide the required total pay-outs as determined using total asset shares, allowing for asset share enhancements from distribution of the Liver Fund Estate. A final bonus scale is determined for each policy term after any smoothing required to avoid anomalies.
- 3.48 As described above, the claim amounts of CB policies are increased whenever a distribution is made from the Liver Fund Estate. These increases are in the form of contingent bonuses. These contingent bonuses can be removed in adverse circumstances, similarly to removal of historical asset share enhancements from distribution of the Liver Fund Estate (as set out in the Liver Capital Framework described in paragraphs 3.95 to 3.98).

## RISK PROFILE

- 3.49 Table 3 below provides a breakdown of the Liver Fund's pre-diversification Solvency Capital Requirement ("SCR"), based on RLMIS's internal view of its financial position, as at 31 December 2021.

**Table 3: Breakdown of the Liver Fund's pre-diversification SCR at 31 December 2021**

Risk category	Percentage breakdown of Internal SCR (pre-diversification)
Longevity	28%
Expense	22%
Market	20%
Other	29%
<b>Total</b>	<b>100%*</b>

\* Sum is less than 100% due to rounding in the presentation shown above.

Source: Information provided by RLMIS

- 3.50 From the breakdown in Table 3, we can see that the main risks are as follows:
- Longevity risk in relation to the non-profit pensions and annuity business.
  - Expense risk in relation to non-profit business as expenses are charged on an actual expense plus profit margin basis in line with the rate card following the expiration of the original unit rates on 1 December 2021.
  - Market risk, which predominantly relates to equity market risk. Equity market risk in the Liver Fund arises in relation to the value of income from charges on unit-linked business, guarantees on with-profits business and the former defined benefit pension schemes (see paragraphs 3.54 to 3.59 below).
  - The 'Other' risk category relates predominantly to the cap on the defined benefit pension schemes as set out in paragraph 3.54 below.

## RISK AND CAPITAL MANAGEMENT

- 3.51 The capital management framework for the Liver Fund is specified in the CPFM in the IoT and is slightly different from the framework that applies to RLMIS's other funds.
- 3.52 The capital management framework for the Liver Fund is discussed further below (starting at paragraph 3.95) alongside the wider RLMIS capital management framework that applies to RLMIS's other funds.

## OTHER

### Service standards

- 3.53 The service standards applicable to policies in the Liver Fund are specified in the IoT. These standards set out the minimum requirements for policy servicing activities such as time taken to process claim payments, policy amendments, etc., the number of calls to the servicing team abandoned and unanswered, and the quality of complaint handling and resolution.

### Pension schemes

- 3.54 The Liver Fund is responsible for providing financial support to the former Royal Liver defined benefit pension schemes (one each for the former UK and Ireland employees of Royal Liver). As a result, any contributions due to those schemes would come from the Liver Fund.
- 3.55 The pension schemes benefit from two guarantees (each) from RLMIS:
- an unconditional guarantee to cover contributions limited to the amount that is recoverable from the Liver Fund, and,
  - a conditional guarantee (requiring that the trustees consult with RLMIS on planned changes to key issues such as investment strategy and funding strategy) which has no upper limit on the amount recoverable from the RL Open Fund.
- 3.56 The pension scheme trustees are given regular updates on the Liver Fund. In addition, they need to be consulted about any material changes to the Liver Fund as creditors of RLMIS (and effectively creditors of the Liver Fund).
- 3.57 The funding levels of the pension schemes (which have been reported as 112% (UK) and 118% (Ireland) at 31 December 2021) provide surpluses of comfortably more than the cost of providing discretionary increases (of broadly Consumer Price Index) in perpetuity, and it is the expectation of both the pension scheme trustees and RLMIS that any future discretionary increases should be funded from surplus, and not from any additional future contributions.
- 3.58 The power to grant discretionary increases rests with RLMIS, and therefore RLMIS can manage its exposure to future contributions being required by controlling the level of future increases in years that they are not affordable. Modelling on the Irish pension scheme, performed on behalf of the Trustees, showed that controlling the level of discretionary increases in years when future increases were not affordable in perpetuity reduced the likelihood of that scheme being in deficit for two or more consecutive years to negligible levels.
- 3.59 Both schemes' trustee boards are currently considering their longer-term strategy and in particular are considering if "buy-in" or "buy-out" might form part of that strategy. However, there is no expectation on the part of the trustees that RLMIS will provide any contributions to fund this, and so they are developing strategies that do not require contributions.

## The RL Open Fund

### INTRODUCTION

- 3.60 All new policies issued by RLMIS, with the exception of increments or options on some existing policies of the closed funds, are written in the RL Open Fund. The estate of the RL Open Fund (the "**RL Open Fund Estate**") provides capital to support the business activities of RLMIS, including writing new business. In return, the RL Open Fund Estate receives profits (or incurs losses) from these business activities.

### RECENT CONSOLIDATIONS AND TRANSFERS

- 3.61 There have been a number of recent transfers and consolidations into the RL Open Fund both through acquisitions and as part of the Legacy Simplification Project.

- 3.62 On 1 October 2020, RLMIS acquired PMAS. The business of PMAS, which includes with-profits (both CWP and UWP), unit-linked and non-profit business, was transferred into the RL Open Fund under section 86 of the Friendly Societies Act 1992.
- 3.63 During 2021, RLMIS consolidated the following four of its closed ring-fenced funds into the RL Open Fund:
- The Refuge Assurance Industrial Branch Sub-Fund (the "**RAIB Sub-Fund**");
  - The United Friendly Industrial Branch Sub-Fund (the "**UFIB Sub-Fund**");
  - The United Friendly Ordinary Branch Sub-Fund (the "**UFOB Sub-Fund**"); and
  - The Scottish Life Fund (the "**SL Fund**").
- 3.64 All of the business of these four funds was written in the UK.
- 3.65 For the RAIB Sub-Fund, during the first half of 2021, RLMIS went through a process to increase the sunset clause threshold for the RAIB Sub-Fund to £200 million with the result that the clause was triggered in 2021. This process was carried out using the existing amendment powers contained in the historical scheme that transferred the business of the RAIB Sub-Fund (as well as the business of the UFIB Sub-Fund and the UFOB Sub-Fund) to RLMIS. This amendment did not require approval by the Court or the UK regulators. This process enabled RLMIS to distribute the estate of the RAIB Sub-Fund (less any deductions deemed to be appropriate) to its with-profits policyholders and to consolidate the RAIB Sub-Fund into the RL Open Fund. This process was implemented on 30 June 2021.
- 3.66 For the remaining three sub-funds, during 2021, RLMIS sought the approval of the English High Court for three separate schemes of arrangement under which the UFIB Sub-Fund, the UFOB Sub-Fund and the SL Fund would be consolidated into the RL Open Fund and, after the deductions deemed to be appropriate, their estates would be distributed to the with-profits policies of the relevant sub-fund. The three schemes were sanctioned by the English High Court on 25 and 26 November 2021 and were implemented on 31 December 2021.
- 3.67 These three schemes of arrangement operated similarly to the Scheme that is the subject of this Report.

## OPERATION

- 3.68 The operation of the RL Open Fund is governed by the RL Long Term Fund PPFM (see paragraph 3.83 below) and the RLMIS Capital Management Framework (see paragraph 3.87 below).

## RISK PROFILE

- 3.69 RLMIS has not written material volumes of CWP business in the RL Open Fund for some time. Therefore, unit-linked with-profits business (i.e. unit-linked business entitled to ProfitShare (see paragraph 3.123 below) and which is sold in material volumes) and non-profit business are becoming more significant in the context of the overall risk profile of the RL Open Fund.
- 3.70 Table 4 below shows a percentage breakdown of the RL Open Fund's pre-diversification SCR, based on RLMIS's internal view of its capital requirements, as at 31 December 2021. This breakdown is shown before allowance for management actions that might be available to mitigate the impact of the stressed scenarios.

**Table 4: Breakdown of pre-diversification components of the RL Open Fund's SCR at 31 December 2021**

Risk category	Percentage breakdown of Internal SCR (pre-diversification)
Market	46%
Persistency	24%
Longevity	11%
Expenses	10%
Operational	6%
Other	2%
<b>Total</b>	<b>100%*</b>

\* Sum is less than 100% due to rounding in the presentation shown above.  
Source: Information provided by RLMIS

- 3.71 Table 4 shows that market risk is a key risk in the RL Open Fund. The RL Open Fund's exposure to market risk is predominantly in relation to equity market risk. Equity market risk in the RL Open Fund arises in relation to the value of income from charges on unit-linked business, guarantees on with-profits business and the staff pension scheme, whose funding is a liability of the RL Open Fund.
- 3.72 Other key risks in the RL Open Fund are:
- Persistency risk in relation to policyholders either transferring or becoming paid up earlier than expected (thus reducing the expected level of future profits) or lapses being lower than expected on older protection policies (thus increasing expected claim outgo) or on with-profits policies with valuable guarantees.
  - Longevity risk. The longevity risk in the RL Open Fund has increased as a result of the consolidation of the SL Fund. The longevity risk from the former SL Fund policies is in relation to the guaranteed annuity rates on pension policies.
  - Expense risk in relation to unit-linked business, whereby an increase in expenses reduces the profit margin of charges levied on policies relative to expenses incurred by the RL Open Fund.
- 3.73 The obligation to meet losses arising as a result of the crystallisation of operational risk in respect of administering the RLMIS Closed Funds (other than the RLCIS Fund) by RLMS primarily sits within the RL Open Fund.

### The other funds of RLMIS

#### THE PLAL FUND

- 3.74 Phoenix Life Assurance Limited was acquired together with the Self Assurance and Pegasus protection business from Scottish Mutual Assurance Limited ("**SMA**") and Scottish Provident Limited ("**SPL**") in August 2008.
- 3.75 In December 2008, the long-term business of Phoenix Life Assurance Limited was transferred to RLMIS by way of a scheme of transfer into the newly established PLAL Fund. The long-term business acquired from SMA and SPL was similarly transferred to RLMIS, into the RL Open Fund, by way of a scheme of transfer.
- 3.76 The PLAL Fund comprises only UWP business, with an approximately equal split of life and pension business. All of the business of the PLAL Fund was written in the UK.
- 3.77 RLMIS intends to go through a process to increase the sunset clause threshold for the PLAL Fund to a level that would allow the clause to be triggered in 2022 (the "**PLAL Fund Consolidation**"). This process is expected to be carried out using the existing amendment powers contained in the historical scheme that transferred the business of the PLAL Fund to RLMIS. This process would be similar to that previously used for the RAIB Sub-Fund with the main difference being that the amendment for the PLAL Fund would require approval by the Court and non-objection from the UK regulators.
- 3.78 If approved, the PLAL Fund Consolidation is expected to be implemented on the same day as the Schemes considered in this Report (31 December 2022), and would result in:
- The consolidation of the PLAL Fund into the RL Open Fund;
  - The distribution of the estate of the PLAL Fund to its with-profits policies through a uniform percentage uplift to asset shares.
- 3.79 In section 15 of this Report I comment on any implications of the PLAL Fund Consolidation for the policies of the Liver Ireland Sub-Fund.

#### THE RLCIS FUND

- 3.80 RLMIS acquired the Co-operative Insurance Society Limited on 31 July 2013, which was subsequently renamed to RLCIS. The long-term business of RLCIS was transferred into the RLCIS Fund in December 2014. The RLCIS Fund contains three segregated sub-funds: the RLCIS Ordinary & Industrial Branch Fund, the RLCIS With-Profits Pension Fund and the RLCIS With-Profits Stakeholder Fund.
- 3.81 The RLCIS Fund comprises a mixture of IB and OB business consisting of:
- CWP business, including whole of life business, endowments, personal pensions, and deferred annuities;
  - UWP business, including funeral plans; and
  - Non-profit business.

### Capital support arrangements

- 3.82 In general, all of the RLMIS Closed Funds are managed in a way that enables them to run off and be funded by their own assets without requiring external support. However, there are certain inter-fund agreements between the RL Open Fund and the RLMIS Closed Funds whereby capital support can be provided between funds if required.
- 3.83 The RL Long Term Fund PPFM covers the RL Open Fund and provides that:
- The RL Open Fund Estate is available in extreme circumstances to provide capital support to the RLMIS Closed Funds should this be required. Any such payment to the RLMIS Closed Funds (other than payments to the Liver Fund and the UFIB Sub-Fund) would be refunded to the RL Open Fund Estate once the support is no longer required.
  - The estates of the RLMIS Closed Funds are available in extreme circumstances to provide capital support to the RL Open Fund should this be required. Any such payment would be refunded to the relevant estate once the support is no longer required.
- 3.84 To date no capital support has been required, or provided, in either direction between the RL Open Fund and the RLMIS Closed Funds.

### Risk and capital management

- 3.85 RLMIS manages the capital in each of its funds on a standalone basis. For the RL Open Fund, PLAL Fund and RLCIS Fund, this is undertaken in line with an overarching framework that sets out how capital is measured, managed, monitored, and reported (the "**RLMIS Capital Framework**").
- 3.86 The Liver Fund is also managed under the RLMIS Capital Framework, but with some additional requirements imposed by the CPFPM (together referred to in this report as the "**Liver Capital Framework**").

### THE RLMIS CAPITAL FRAMEWORK

- 3.87 The RLMIS Capital Framework sets out the capital target for each of the three in-scope funds (i.e. all RLMIS funds other than the Liver Fund). For each of the funds this includes a target range for capital that is set with reference to the need to withstand a 1-in-20-year event over the next year and still have sufficient Internal Own Funds to be able to meet its Internal SCR, where:
- "**Internal Own Funds**" are calculated in a similar way to regulatory Own Funds, except that allowance for the Transitional Measure on Technical Provisions ("**TMTP**") in the PLAL Fund and the RLCIS Fund is assumed to be dynamic over time<sup>2</sup>.
  - The "**Internal SCR**" represents the RLMIS view of the capital required to meet a 1-in-200-year event and is calculated in accordance with the Internal Model developed by RLMIS (the "**RLMIS Internal Model**") and approved by the Prudential Regulation Authority ("**PRA**").
- 3.88 The borders of the capital target ranges for each fund are set with reference to the capital required such that the fund could withstand a 1-in-N year event (with the values of N set out in Table 5) over the next year and to still have sufficient Internal Own Funds to be able to meet its Internal SCR.
- 3.89 The capital target ranges for the PLAL Fund and RLCIS Fund are dynamic and so vary from year to year as they are recalibrated to the required risk level.
- 3.90 For the RL Open Fund, the borders of the capital target ranges are fixed (to a set Internal SCR Cover ratio) to simplify the processes for managing the fund. The capital target ranges are calibrated to approximately the same 1-in-N year levels as used for the PLAL Fund and the RLCIS Fund.
- 3.91 The RLMIS Capital Framework defines a Red-Amber-Green ("**RAG**") status to set out the capital target and trigger levels in respect of the level of capitalisation of each fund. The RAG statuses and trigger levels for all funds, except the Liver Fund, are set out in Table 5 below.

<sup>2</sup> Given the significance of the TMTP to some of the RLMIS Closed Funds, RLMIS's internal basis for these funds assumes that the TMTP is recalculated regularly in line with the BEL and Risk Margin, as opposed to only as part of the regulatory recalculation (every two years).

**Table 5: RLMIS Capital Framework**

RAG Status	Level of available capital
Over Capitalised (Upper Red)	Enough to withstand a 1-in-100-year event
Sub-Optimal+ (Upper Amber)	Enough to withstand between a 1-in-100-year and a 1-in-50-year event
Acceptable Range (Green)	Enough to withstand between a 1-in-50-year and a 1-in-10-year event Within this range there is a narrower Target Range, centred around the level of capital required to withstand a 1-in-20-year event (for the RL Open Fund this is the midpoint of the Target Range and for the RLMIS Closed Funds this is the bottom of the Target Range).
Sub-Optimal- (Lower Amber)	Enough to withstand between a 1-in-10-year and a 1-in-5-year event
Alert (Lower Red)	Less than the level required to withstand a 1-in-5-year event

Source: Information provided by RLMIS

- 3.92 The RLMIS Capital Framework includes "red" and "amber" categories for situations in which a fund is considered either over-capitalised ("upper red/amber") or under-capitalised ("lower red/amber"). For shareholder-backed insurance business it would be typical for a capital framework only to regard an under-capitalised fund as undesirable; however, in the case of a with-profits fund, it is undesirable for the fund to be over-capitalised as this could indicate an over cautious approach to the distribution of the excess surplus to with-profits policyholders.
- 3.93 The Green ranges are split between a target range, which is the optimal capitalisation for the fund, and an acceptable range, which is viewed as an acceptable interim position for the fund.
- 3.94 The RLMIS Capital Framework also sets out the possible additional management responses (beyond those management actions already assumed in the calculation of the Internal SCR) that may be taken should the capital position of the fund move outside of a defined range. The management responses vary between the RL Open Fund, and the PLAL Fund and RLCIS Fund, and include varying the distribution of profits or the funds' estates (including potential removal of historical estate distributions) or engaging in de-risking or re-risking strategies.

#### THE LIVER CAPITAL FRAMEWORK

- 3.95 The Liver Capital Framework follows the same principles as the RLMIS Capital Framework but with some differences (described below) reflecting the specific requirements of the CPFM under the IoT. The Liver Capital Framework sets out the capital target for the Liver Fund, which is set such that the Liver Fund should hold sufficient capital to withstand a 1-in-20-year event over the next year and still meet the Internal SCR for the Liver Fund.
- 3.96 The Liver Capital Framework defines a RAG status to set out the capital target and trigger levels for the Liver Fund in the same way as the RLMIS Capital Framework as outlined above. However, the Liver Capital Framework sets out different management responses that may or should be taken should the capital position of the fund move outside of a defined range.
- 3.97 The key difference between the Liver Capital Framework and the RLMIS Capital Framework is:
- Under the Liver Capital Framework, any excess in the Liver Fund Estate above the 1-in-20-year capital target should be distributed in full through asset share enhancements to with-profits policies (excluding L&M policies) and increases to the claim amounts of CB policies. There would be no distributions from the Liver Fund Estate if the excess capital was below this capital target.
  - Under the RLMIS Capital Framework, which covers the RL Open Fund, the PLAL Fund and the RLCIS Fund, estate distributions can take place in a given fund if that fund is in the Lower Amber range or above (i.e. above the 1-in-5-year level), and so distributions can be made at a lower level of Internal SCR Cover in these funds. Furthermore, estate distributions are accelerated when the fund is in the Upper Amber or Upper Red range (so above the 1-in-50-year level) but there is no requirement, as there is under the Liver Capital Framework, to distribute the entire excess above the 1-in-20-year level.
- 3.98 The Liver Capital Framework means that distributions must be made when they are in excess of the 1-in-20-year capital target but are not allowable below this capital target. It is worth noting that this could lead to more volatile distributions to Liver Fund policyholders as the capital requirements become an increasingly large part of the Liver Fund.



- 3.99 The Liver Capital Framework allows for the presence of the Liver Pension Schemes, including size of the Pension Scheme Cap.

### Investment strategy

- 3.100 For the with-profits liabilities in the Liver Fund (including the with-profits business reinsured in from the Liver Ireland Sub-Fund), the Equity Backing Ratio ("**EBR**") i.e. the proportion of the fund invested in 'risky' asset classes such as equities and property, was 68% as at 31 December 2021. Policies in the UK and Ireland have the same asset mix backing their asset shares, which consequently means that UK policies are backed by a proportion of euro-denominated assets and a proportion of Ireland policies are backed by sterling-denominated assets.
- 3.101 The non-profit business of the Liver Fund (including the CB policies and the non-profit business reinsured in from the Liver Ireland Sub-Fund) is backed by a combination of UK and Euro sovereign and corporate bonds, i.e. it is invested with an EBR of 0%.
- 3.102 The required collateral under the LRA is part of the assets of the Liver Fund but is ring-fenced and takes the form of a complete portfolio of assets, e.g. euro corporate bonds. These assets are available to meet claims arising on the policies of the Liver Ireland Sub-Fund.
- 3.103 The Liver Fund Estate is invested primarily in UK and Euro sovereign and corporate bonds with a proportion held as cash, i.e. it is invested with an EBR of 0%.
- 3.104 The Liver Fund also utilises a series of hedges to manage its capital position against market risks, in particular hedging liabilities in respect of investment guarantees on with-profits policies and expense inflation on both the UK and Ireland business.
- 3.105 The asset share EBR for the RL Open Fund was 68% as at 31 December 2021 but there are some groups of policies, with significant (in terms of the size of the guarantee and/or the amount in the money) guarantees for which the backing assets have been separately assigned, with a lower EBR (including 0%).

### With-profits governance

- 3.106 The governance of the with-profits business within RLMIS principally consists of the WPA, the WPC and the RLMIS Board. Management of the Liver Fund is also overseen by the LSC (see paragraph 3.25 above). The LSC members have regard solely to the interests and reasonable expectations of the policyholders transferred from Royal Liver to RLMIS.
- 3.107 The Principles and Practices of Financial Management ("**PPFM**") applicable to the business in the Liver Fund are set out in the Royal Liver PPFM. In addition, as set out in paragraph 3.23 above, the IoT includes the CPFM, which covers requirements for bonus setting and estate distributions.
- 3.108 The "**RL Long Term Fund PPFM**" covers the business of the RL Open Fund, including the business consolidated into the RL Open Fund through the recent fund consolidations and other business transfer schemes.
- 3.109 There are also separate PPFMs for the other two closed ring-fenced funds of RLMIS (the PLAL Fund and the RLCIS Fund). Those PPFMs set out how the with-profits business within each of the funds will be managed.
- 3.110 The WPA and WPC are responsible for advising the RLMIS Board on managing the with-profits business in line with the PPFMs and, more generally, treating with-profits policyholders fairly. This includes making recommendations to the RLMIS Board on the size of pay-outs to with-profits policyholders, including in respect of final bonus scales and the level of estate distribution.

### Financial condition

#### BASIS OF PREPARATION

- 3.111 The current regulatory solvency framework for the European Economic Area ("**EEA**") insurance and reinsurance industry came into effect on 1 January 2016; this regime is known as Solvency II. The Solvency II regime applied to UK insurers until 31 December 2020, which was the end of the transition period agreed following the UK's exit from the EU (and the EEA). Since 1 January 2021 the UK has been free to determine an appropriate regulatory regime for insurance companies, which I refer to throughout this Report as "**UK Solvency II**".
- 3.112 UK Solvency II is applicable to RLMIS (and Solvency II is applicable to RLI DAC).

- 3.113 As previously noted, RLMIS uses the RLMIS Internal Model for the purposes of calculating its SCR under UK Solvency II. RLMIS uses its Group reporting basis to prepare the balance sheet that it uses for its report and accounts, and this is the basis on which it makes decisions in relation to the RL Open Fund and the RLMIS Closed Funds.
- 3.114 Under the Group basis, the RL Open Fund's financial position is calculated on a "Pillar 1" basis, while the RLMIS Closed Funds' financial positions are calculated on a "Pillar 2" basis. The Pillar 1 and Pillar 2 bases are closely aligned as both are calculated using the RLMIS Internal Model, and both allow for the TMTP. The only difference between the Pillar 1 and Pillar 2 bases is that on a Pillar 1 basis the TMTP is assumed to be fixed at the last calculation date with allowance for run-off, while on a Pillar 2 basis the TMTP is assumed to be dynamic over time.
- 3.115 In this Report I have therefore presented RLMIS's financial position on the Group reporting basis.

#### POSITION AT 31 MARCH 2022

- 3.116 Table 6 shows the UK Solvency II financial position of the Liver Fund and the RL Open Fund on a Group basis, as at 31 March 2022. The assets of the Liver Fund have been adjusted to allow for the release of a small portion of the Liver Fund Estate currently held by RLI DAC to cover the Liver Ireland Sub-Fund capital requirements.

**Table 6: UK Solvency II financial position as at 31 March 2022 (£ millions)**

	Liver Fund	RL Open Fund
Assets (A)	1,987	89,525
Liabilities (B)	1,615	85,467
<i>Of which asset shares</i>	<i>843</i>	<i>11,674</i>
<b>Available capital before adjustments (C = A - B)</b>	<b>373</b>	<b>4,058</b>
Risk Margin (D)	62	1,128
TMTP (E)	67	926
Sub-debt (F)	-	1,446
<b>Internal Own Funds (G = C - D + E + F)</b>	<b>378</b>	<b>5,302</b>
Internal SCR (H)	216	2,452
<b>Excess capital (G - H)</b>	<b>162</b>	<b>2,850</b>
<b>Internal SCR Cover (G / H)</b>	<b>175%</b>	<b>216%</b>

Source: Information provided by RLMIS

- 3.117 Table 6 shows that, as at 31 March 2022:
- The Liver Fund had excess capital of £162 million and an Internal SCR Cover of 175%. This corresponds to Upper Amber (Sub-Optimal+) under the Liver Capital Framework, i.e. the Liver Fund was marginally above its target range. There is a planned enhancement to asset shares and claim amounts on CB policies of 3.6% that will be made on 1 July 2022 as the Internal SCR Cover was above the 1-in-20-year capital target at 31 December 2021, in line with the IoT provisions.
  - The RL Open Fund had excess capital of approximately £2.9 billion and an Internal SCR Cover of 216%. This corresponds to Upper Amber (Sub-Optimal+) under the RLMIS Capital Framework, i.e. the RL Open Fund was marginally above its acceptable range.

#### Other

#### MEMBERSHIP

- 3.118 RLMIS is a mutual life insurance company, owned by its members, with the RLMIS Board having a duty to promote the success of the business for the benefit of its current and future members.



- 3.119 Members are generally policyholders who have purchased policies from RLMIS that allow them the opportunity to participate in the profits of RLMIS.
- 3.120 Policyholders whose policies have been transferred to RLMIS through previous acquisitions and subsequent schemes of transfer have not gained membership. Therefore, none of the policies of the Liver Fund (or the PLAL Fund, the RLCIS Fund or the funds of RLI DAC) confer membership of RLMIS on the holders of these policies.
- 3.121 Members of RLMIS have the right to vote at the Annual General Meeting or an Extraordinary General Meeting of RLMIS. All members have voting rights of one vote per member, all ranking equally.
- 3.122 The rules of membership are contained in the Articles of Association of RLMIS.

#### PROFITSHARE

- 3.123 ProfitShare is a mechanism used by RLMIS to distribute part of the profits emerging in the RL Open Fund to certain policyholders. ProfitShare is currently allocated only to:
- Certain with-profits policies in the RL Open Fund;
  - Unit-linked pensions policies written by RLMIS with an inception date from 2001; and
  - German bond business in RLI DAC via a reinsurance mechanism with RLMIS (the “**German Bond Reinsurance Agreement**”). These are reinsured to the RL Open Fund and are not within the scope of the Liver Fund Consolidation (see section 4 for more details).
- 3.124 ProfitShare is allocated by means of discretionary enhancements to asset share, or an allocation of additional units for unit-linked policies.

## 4 BACKGROUND TO RLI DAC

### History of Royal Liver in Ireland

- 4.1 As previously noted in 3.10 above, Royal Liver was authorised in both the UK and Ireland and wrote a mix of ordinary branch and industrial branch business in both jurisdictions (with the Irish business being written through an Irish branch).
- 4.2 In addition, in 2000 Royal Liver acquired Caledonian Insurance Company ("**Caledonian**") and GRE Life Ireland ("**GRELI**"). GRELI remained a subsidiary of Royal Liver, whereas the business of Caledonian, which ceased trading in 2000, was transferred into Royal Liver. Royal Liver also acquired the industrial branch business written by Irish Life Assurance plc.
- 4.3 Prior to 1 July 2011, Royal Liver wrote new business in Ireland using the brand name Caledonian Life. Almost all new business was ordinary branch protection business sold through the IFA distribution channel.
- 4.4 As noted in 3.11 above, the business of Royal Liver (including its Irish business) was transferred into the Liver Fund on 1 July 2011 by way of a transfer under the IoT.
- 4.5 The business of GRELI was subsequently also transferred to the Liver Fund on 1 July 2012 under a scheme of transfer pursuant to section 13 of the 1909 Act, section 36 of the Insurance Act 1989 and Article 35 of the European Communities (Life Assurance) Framework Regulations 1994.
- 4.6 After the transfer of the Royal Liver business in 2011, RLMIS continued to write new protection business in Ireland, this being written (through RLMIS's Irish Branch) into the RL Open Fund.

### History of RLI DAC

- 4.7 Following the UK's referendum on membership of the EU, and as a mitigation against the UK leaving the EU without the passporting arrangements under which business can be sold and serviced in other EU states being replaced, RLMIS decided to apply for authorisation to establish an insurance subsidiary in Ireland.
- 4.8 The subsidiary, RLI DAC was authorised by the CBI with effect from 1 January 2019. RLMIS made a capital injection of €40 million (€1 million share capital and €39 million capital contribution) to RLI DAC on 17 December 2018 and the subsidiary became fully operational and started selling new business from 7 January 2019.
- 4.9 RLI DAC has three ring-fenced funds:
  - The main fund which is open to new business ("**RLI DAC Open Fund**");
  - The Liver Ireland Sub-Fund, which contains the business originally written in Ireland by Royal Liver, Caledonian Life, Irish Life and GRELI (the "**Liver Ireland Business**"); and,
  - A fund (the "**RLI DAC German Bond Sub-Fund**") for business written in Germany by RLMIS (the "**German Bond Business**").
- 4.10 In parallel with the application to establish RLI DAC, RLMIS developed a scheme of transfer of part of its long-term business to RLI DAC under an insurance business transfer (the "**RLI DAC Transfer Scheme**") under Part VII of the Financial Services and Markets Act 2000 ("**Part VII Transfer**"). The business to be transferred was:
  - (i) Business written in Ireland by RLMIS through its Irish branch since 1 July 2011;
  - (ii) The Liver Ireland Business; and,
  - (iii) The German Bond Business.
- 4.11 The Part VII Transfer was approved by the English High Court and took place on 7 February 2019:
  - Block (i) of business was transferred to the RLI DAC Open Fund;
  - Block (ii) was transferred to the Liver Ireland Sub-Fund; and,
  - Block (iii) was transferred to the RLI DAC German Bond Sub-Fund.
- 4.12 Following the Part VII transfer, the Liver Ireland policyholders are no longer direct policyholders of RLMIS. However, they continue to have access to the Liver Fund and have certain rights to a share in the Liver Fund Estate through the LRA which was put in place on 1 January 2019. The LRA is described further below, starting at paragraph 4.21.

- 4.13 The RLI DAC Transfer Scheme acknowledged that the Part VII Transfer did not prejudice any interest that Liver Ireland Business policyholders may have in the Liver Fund Estate. Furthermore, the RLI DAC Transfer Scheme recognised that, if the LRA was terminated, the Liver Fund Estate would have to be split between RLMIS and RLI DAC and set out a formal arrangement for conducting that split, including the appointment of an independent expert.
- 4.14 Further information on the Liver Ireland Sub-Fund is provided in the following subsection, starting at paragraph 4.18.
- 4.15 The products currently sold by RLI DAC, and written in the RLI DAC Open Fund, are:
- Term Assurance.
  - Specified Serious Illness.
  - Income Protection.
  - Mortgage Protection.
  - Whole of Life cover.
  - Multi-Claim Protection Cover.
- 4.16 The RLI DAC Open Fund comprises only business written in Ireland.
- 4.17 The types of business written are as follows:
- Insurance with-profit participation: This comprises CWP, Deposit administration, UWP, and Accumulating with-profits business.
  - Index-linked and unit-linked business.
  - Health insurance: This comprises Stand-alone critical illness, and Income protection business.
  - Other life insurance: This comprises non-profit business and Accelerated critical illness business. It also includes Index-linked business where the policyholder does not bear the risk, and with-profits business that has been converted to or re-classified as non-profit.

**Table 7: Summary of the business of RLI DAC as at 31 December 2021**

Line of Business	BEL	Risk Margin	TPs calculated as a whole	Total Technical Provisions
Insurance with-profits participation	542.9	1.5	-	544.4
Index-linked and unit-linked insurance	0.0	0.1	17.0	17.0
Health insurance	(23.4)	3.9	-	(19.5)
Other life insurance	235.3	34.6	-	269.9
<b>Total</b>	<b>754.7</b>	<b>40.1</b>	<b>17.0</b>	<b>811.8</b>

Source: RLI DAC Solvency and Financial Condition Report 2021

## Liver Ireland Sub-Fund

### NATURE OF BUSINESS WRITTEN

- 4.18 The main lines of business written in the Liver Ireland Sub-Fund are:
- Conventional life with-profits (both OB and IB).
  - Conventional life non-profit (both OB and IB). This IB business includes the CB policies that share in the surplus distributions of the Liver Fund Estate (through contingent bonuses) when they are triggered.
  - Conventional pensions (both with-profits and non-profit).
  - UWP (both life and pensions).
  - Unit-linked (both life and pensions).
  - Protection.

■ Annuities.

- 4.19 The Liver Ireland Sub-Fund is closed to new business and all the business in the Liver Ireland Sub-Fund was written in Ireland.
- 4.20 The Liver Ireland Business includes a significant proportion of with-profits business which is managed in line with the Liver Ireland Sub-Fund WPOP, the CPFM as defined in the IoT and the PPFM for the Liver Fund. The past practice in relation to the Liver Fund has been to apply a uniform rate of return (as set out in paragraph 3.41), allowing for currency differences, across both Ireland Liver with-profits business and the UK Liver with-profits business. As noted in paragraph 3.42, bonuses for the UK Liver with-profits business are set by RLMIS and those for the Ireland Liver with-profits business are set by RLI DAC.

#### REINSURANCE TO LIVER FUND

- 4.21 To keep the Liver Fund economically intact and enable RLMIS and RLI DAC to maintain the expectations of policyholders under the Royal Liver PPFM and the Liver Ireland Sub-Fund WPOP, the Liver Ireland Business was, from the point of transfer, 100% reinsured back to the Liver Fund in RLMIS under a quota share arrangement (the LRA).
- 4.22 If the reinsurance was not in place, the Liver Fund would need to be split, which would require a once-and-for-all allocation of all the assets in that fund between the Liver Ireland Business and UK Liver business. This would be a complex task which would involve detailed consideration around the fairness to different groups and generations of policyholders with specific requirements detailed in the IoT.
- 4.23 At the time, it was not considered possible to complete this process in a fair and controlled manner ahead of the expected deadline imposed by the UK's exit from the EU. In addition, splitting the fund would mean past management practices, which have worked well, could not be continued and there would be consequences on the covenant available to the staff pension schemes currently supported by the Liver Fund.
- 4.24 The key principle, as outlined in the application to the CBI for the authorisation of RLI DAC, was as follows:  
*"The combination of the Part VII transfer and the reinsurance is designed to minimise the disruption to the operation of the with-profits business in these portfolios. The Royal Liver Fund in RLMIS has a significant block of both Ireland and UK with-profits business which are credited with a uniform rate of return for the purposes of assessing bonuses. The reinsurance is designed to enable that approach to be maintained, allowing the policyholders' expectations to be maintained."*
- 4.25 The initial reinsurance premium was such as to leave sufficient assets in the Liver Ireland Sub-Fund to cover the BEL Counterparty Default Adjustment in respect of the exposure to RLMIS and the Risk Margin, SCR and **"Capital Buffer"** as required under the RLI DAC capital management framework (64% of SCR), all determined allowing for the reinsurance to RLMIS. The ongoing reinsurance premiums would be any regular premiums payable under Liver Ireland Business policies.
- 4.26 The LRA requires RLMIS to post dedicated collateral for the cover provided and to provide a floating charge over certain of the assets of RLMIS to ensure that the Liver Ireland Business policyholders rank the same as direct policyholders of RLMIS in the event of a winding up of RLMIS.
- 4.27 There is one collateral framework agreement and two fixed charge deeds, a first tier and second tier, in respect of the Liver Ireland Business. The fixed charge deeds each provide a fixed charge over sufficient assets of the Liver Fund to enable 50% of the reinsured BEL to be met, so that in total the fixed charges cover 100% of the reinsured BEL. These fixed charges mean that, in the event that a material breach of the LRA occurs, RLI DAC can take control of sufficient assets to meet the reinsured liabilities. The floating charge and the second-tier fixed charges include an "equalisation clause" such that the reinsured policyholders do not receive more than the equivalent direct policyholders in the Liver Fund in the event that there is a shortfall of available assets on the insolvency of RLMIS.
- 4.28 The collateral is ring-fenced and separately identifiable by the custodian. It takes the form of complete portfolios of assets, e.g. euro corporate bonds, which allows the assets to continue to be managed by RLAM to the relevant investment benchmarks. The assets are available to meet claims arising under the reinsured contracts using the monthly settlement arrangements. The value of the collateral relative to the reinsured liabilities is rebalanced as part of the monthly settlement process under the LRA with quarterly restatement based on regulatory reporting figures.
- 4.29 The LRA provides that, in the event of the termination of the LRA as a result of a management decision or another reason which did not involve the insolvency of RLMIS, the two parties will agree a termination payment calculated as the BEL (on an agreed set of assumptions) of the Liver Ireland Business.

## SUNSET CLAUSE

- 4.30 Under the terms of the RLI DAC Transfer Scheme, there are two thresholds that form part of the “**Liver Ireland Sunset Clause**” at which RLI DAC either may or must cease to maintain the Liver Ireland Sub-Fund as a separate sub-fund. These thresholds are referred to respectively as the “**Liver Ireland Sunset Clause May Threshold**” and the “**Liver Ireland Sunset Clause Must Threshold**”
- 4.31 It should be noted that the Liver Ireland Sunset Clause would only be triggered if the LRA was no longer in place, and so at this time it is effectively redundant. I understand that there are currently no plans (from either RLMIS or RLI DAC) to terminate the LRA in the short to medium term.
- 4.32 It should also be noted that the thresholds for the Liver Ireland Sunset Clause are not dependent on the thresholds for the Liver Sunset Clause being reached and vice versa.

### Liver Ireland Sunset Clause May Threshold

- 4.33 RLI DAC *may* cease to maintain the Liver Ireland Sub-Fund when the total asset shares of the Liver Ireland Sub-Fund fall below €334 million indexed with the Irish Consumer Price Index annually from 31 December 2018 (€356 million as at 31 December 2021), or at any time after this threshold is passed. This is expected to be reached in the next few years.
- 4.34 RLI DAC may also cease to maintain the Liver Ireland Sub-Fund when the total asset shares of that sub-fund are higher than the amount set out above, if the RLI DAC Board, having regard to the advice of the RLI DAC HoAF, considers: (i) the continued maintenance of the Liver Ireland Sub-Fund to be materially adverse to the interests of policyholders of any of RLI DAC's funds; and, (ii) the cessation of the Liver Ireland Sub-Fund would not be materially adverse to the interests of policyholders of any other of RLI DAC's funds.

### Liver Ireland Sunset Clause Must Threshold

- 4.35 RLI DAC *must* cease to maintain the Liver Ireland Sub-Fund when the total asset shares of that sub-fund fall below €134 million indexed with the Irish Consumer Price Index annually from 31 December 2018 (€143 million as at 31 December 2021), or at any time after this threshold is passed. This is expected to be reached in 2030.

### Consequence of triggering either Sunset Clause

- 4.36 When RLI DAC ceases to maintain the Liver Ireland Sub-Fund under either of the thresholds above, the RLI DAC Transfer Scheme prescribes that:
- The excess assets of the Liver Ireland Sub-Fund will be allocated as enhancements to the with-profits policies and the CB policies of the fund in a manner determined to be fair by the Board, having regard to the advice of the HoAF; and
  - The Liver Ireland Sub-Fund would be consolidated into the RLI DAC Open Fund.

## EXPENSE ARRANGEMENTS

- 4.37 Following the establishment of RLI DAC and the Part VII Transfer, the rate card was amended so that UK and Irish policyholders continued to benefit from the rate card structure. This resulted in a rate card being introduced for Liver Ireland Business on the same terms as for UK policyholders. The original unit rates in the rate card expired on 1 December 2021. Since then, asset shares of policies allocated to the Liver Fund have been charged with the actual expenses plus a margin, in line with the rate card. See paragraphs 3.26 to 3.32 for more details.

## GOVERNANCE

- 4.38 The Liver Ireland Sub-Fund WPOP sets out the principles by which the Liver Ireland Sub-Fund is managed.
- 4.39 The RLI DAC Board is responsible for determining the manner and timing of any distributions of surplus in respect of RLI DAC policyholders. However, prior to the termination of the LRA, the distribution of the Liver Fund Estate is also subject to the approval of the RLMIS Board. The RLI DAC Board is advised on such matters by the RLI DAC HoAF.
- 4.40 The IoT provided for the establishment of the LSC, whose responsibility it is to monitor the management of the Liver Fund for the benefit of all Liver policies. This responsibility extends to those policies that were transferred to RLI DAC under the RLI DAC Transfer Scheme, taking into account the Liver Ireland Sub-Fund WPOP.
- 4.41 The LSC's remit was also extended to include consideration of compliance with the LRA, the associated collateral agreements and the RLI DAC Transfer Scheme.

### Capital support arrangements

- 4.42 While the LRA is in place, in the event that RLMIS becomes insolvent or fails to meet its key payment obligations under the LRA, the RLI DAC Transfer Scheme sets out the following circumstances in which the RLI DAC Open Fund will provide capital support to the Liver Ireland Sub-Fund:
- If the Liver Ireland Sub-Fund has insufficient assets to cover its BEL plus SCR, then the RLI DAC Open Fund will hold sufficient assets to cover the deficit in the Liver Ireland Sub-Fund, or
  - If the Liver Ireland Sub-Fund has insufficient assets to cover BEL, then the RLI DAC Open Fund will transfer assets to the Liver Ireland Sub-Fund sufficient to eliminate the deficit in the Liver Ireland Sub-Fund.
- 4.43 Equivalent capital support provisions are set out in the RLI DAC Transfer Scheme between the RLI DAC German Bond Sub-Fund and the RLI DAC Open Fund.
- 4.44 There will be no obligation to provide this capital support (to either the Liver Ireland Sub-Fund or the RLI DAC German Bond Sub-Fund) if the RLI DAC Board, having consulted with the RLI DAC HoAF, is of the opinion that the assets of the RLI DAC Open Fund are insufficient to meet the minimum regulatory requirements of the RLI DAC Open Fund.

### Risk and capital management

- 4.45 The capital framework for RLI DAC (the "**RLI DAC Capital Framework**") sets out the capital target each of the in-scope funds. As with the RL Open Fund, the RLI DAC Open Fund has a capital target that requires that the fund be able to withstand a 1-in-20-year event over the next year and to still have sufficient Internal Own Funds to be able to meet its Internal SCR.
- 4.46 The RLI DAC Capital Framework is summarised in the company's Risk Appetite Statement as follows:
- "The Company will hold at all times a Capital Coverage Ratio of at least 164%, representing 100% of the minimum regulatory capital requirements plus an additional buffer of 64% to allow for the potential variability and risks to capital and the expected impact from new and existing Business Plans."*
- 4.47 The RLI DAC Capital Framework defines a RAG status in respect of the RLI DAC Open Fund to set out the capital target and trigger levels in the same way as the RLMIS Capital Framework as outlined in section 3. However, the RLI DAC Capital Framework sets out different management responses for the RLI DAC Open Fund, in particular in relation to the payment of dividends to RLMIS. There is no with-profits business in the RLI DAC Open Fund and so many of the management actions in the RLMIS Capital Framework would not be applicable. The management responses under the RLI DAC Capital Framework are:
- Where the capital levels are categorised as Upper Red or Upper Amber, dividend payments to RLMIS should be accelerated.
  - Where the capital levels are categorised as Green, the normal agreed level of dividend payments should be made to RLMIS.
  - Where the capital levels are categorised as Lower Amber, dividends to RLMIS should be reduced or cancelled.
  - Where the capital levels are categorised as Lower Red dividends to RLMIS should be suspended.
- 4.48 The other key difference between the RLI DAC Capital Framework and the RLMIS Capital Framework is the ability for the RLI DAC Open Fund to consider raising additional capital through a capital injection from RLMIS where the capital falls to a Lower Red level.
- 4.49 The RLI DAC Capital Framework allows for the presence of the two ring-fenced funds of RLI DAC (the RLI DAC German Bond Sub-Fund and the Liver Ireland Sub-Fund). These ring-fenced funds target a capital buffer of a 1-in-20-year level. As previously noted, the business in the ring-fenced funds of RLI DAC is fully reinsured to RLMIS through collateralised agreements. The capital buffer is in place on the ring-fenced funds in case of any risk volatility and between reinsurance true-ups. The experience adjustments under the reinsurance arrangements for the Liver Ireland Sub-Fund and the RLI DAC German Bond Sub-Fund are designed to maintain the capital coverage ratio for these funds at a target ratio aligned with the RLMIS capital framework (currently at 164%).

## Financial condition

### BASIS OF PREPARATION

- 4.50 RLI DAC uses the “**Standard Formula**” (described in paragraph 8.26) to calculate its SCR under Solvency II, and so the Solvency II financial information presented in this Report for RLI DAC (including for the Liver Ireland Sub-Fund) is the Pillar 1 reported information on a Standard Formula basis.

### POSITION AT 31 MARCH 2022

- 4.51 Table 8 below shows the Solvency II Pillar 1 financial position of the three sub-funds and overall RLI DAC position, as at 31 March 2022.

**Table 8: RLI DAC Solvency II Pillar 1 financial position as at 31 March 2022 (€ millions)**

	RLI DAC Open Fund	Liver Ireland Sub-Fund	RLI DAC German Bond Sub- Fund	Total RLI DAC
Assets (A)	129	785	112	1,026
<i>Of which reinsurance asset</i>	46	721	108	875
Liabilities (B)	(56)	772	111	827
<b>Available capital before adjustments (C = A - B)</b>	<b>185</b>	<b>13</b>	<b>1</b>	<b>200</b>
Risk Margin (D)	35	2	0	37
<b>Internal Own Funds (E = C - D)</b>	<b>150</b>	<b>11</b>	<b>1</b>	<b>162</b>
Internal SCR (F)	73	7	1	80
<b>Excess capital (E - F)</b>	<b>77</b>	<b>4</b>	<b>0</b>	<b>82</b>
<b>Internal SCR Cover (E / F)</b>	<b>206%</b>	<b>164%</b>	<b>164%</b>	<b>202%</b>

Source: Information provided by RLI DAC

- 4.52 Table 8 shows that, as at 31 March 2022:
- The RLI DAC Open Fund had excess capital of €77 million and an Internal SCR Cover of 206%. This corresponds to Upper Red status under the RLI DAC Capital Framework.
  - Both the Liver Ireland Sub-Fund and the RLI DAC German Bond Sub-Fund had Internal SCR coverage ratios of 164%. (As noted in paragraph 4.49 above, the reinsurance arrangements are designed to maintain the ratios at that level).



## 5 SUMMARY OF THE PROPOSED OFFER AND SCHEME

### Background

- 5.1 As introduced in section 1, RLMIS is conducting its Legacy Simplification Project to rationalise and simplify its fund structure, products, and administration systems to generate operational efficiencies, reduce risk and improve customer outcomes. This involves consolidating into the RL Open Fund a number of blocks of business currently managed in separate with-profits funds or sub-funds.
- 5.2 The Legacy Simplification Project has been ongoing for some time. In 2021, the RAIB Sub-fund, the UFIB Sub-fund, the UFOB Sub-fund and the SL Fund were consolidated into the RL Open Fund. RLI DAC was not impacted by these consolidations.
- 5.3 The planned actions under the Legacy Simplification Project in 2022 will, subject to the necessary approvals, see the Liver Fund and the PLAL Fund consolidated into the RL Open Fund.
- 5.4 The proposal to consolidate the Liver Fund into the RL Open Fund has an impact on RLI DAC as, in addition to the Liver Fund's having liabilities in respect of certain UK policyholders of RLMIS, it also has (via inwards reinsurance) liabilities in respect of certain policyholders of RLI DAC. Following the transfer of Royal Liver's Irish policies from RLMIS to RLI DAC in 2019, the liabilities in respect of those policies were reinsured by RLI DAC to RLMIS.

### Rationale

- 5.5 The Liver Fund is currently managed on a ring-fenced standalone basis and needs to hold a level of capital appropriate to the level and nature of risks to which the fund is exposed. Due to this ring-fencing, those risks cannot easily be diversified with risks in another RLMIS fund or funds. The current standalone status also leads to the additional overhead of separate accounting and reporting for the fund.
- 5.6 Under the proposed consolidation, the RL Open Fund (including the consolidated business) will benefit from a material reduction in overall capital requirements due to diversification benefits which will accrue from the consolidation.
- 5.7 The With-Profits Actuary of RLMIS has stated that:  
*"Distributing the Liver Estate in the shorter term, as opposed to waiting until the Liver sunset point is reached (which RL estimates will occur in 2041), or at any point in the interim period by way of a scheme of arrangement or other mechanism in the future, would have the following benefits to certain policyholders who are entitled to a share of the Liver Estate:*  
  - (a) *Enabling the accelerated distribution of the Liver Estate by way of uplifts to asset shares, thereby smoothing the potential tontine and leading to more equitable distributions of the Liver Estate;*
  - (b) *Generating additional, material capital diversification benefits that would not otherwise have been realised and that will be shared with the holders of Eligible Policies invested in the Liver Fund through a higher Uplift, if the [UK] Scheme goes ahead.*
- 5.8 The Chief Actuary of RLMIS has also stated that *"[the proposed consolidation] is expected to improve the efficiency of the business, reduce risk exposure through diversification and provide fairer outcomes to policyholders"*.
- 5.9 In terms of timing, the Chief Actuary of RLMIS has stated:  
*"RL intends to implement the Liver Fund Consolidation on 31 December 2022 ... As the Liver Sunset Point is projected to be 2041, consideration should be given as to whether this is an appropriate timescale or whether it would be preferable to delay implementation ...*  
*There are a number of strong arguments in favour of implementing the Liver Fund Consolidation as proposed:*  
  - *Tontine smoothing – as the Liver Fund runs off and its capital requirements reduce, distributions from the Liver Fund Estate are expected to increase. By consolidating sooner rather than later, these distributions can be smoothed more equitably.*
  - *Certainty of distribution – the value of Liver Fund Estate distributions is uncertain and adverse future experience could mean actual future distributions may be less than currently expected. Upon the implementation of the Liver Fund Consolidation, the current value of the Liver Fund Estate will be*



*distributed to Eligible Benefits with certainty. The earlier the consolidation is effected the greater certainty there is for policyholders.*

- *Project cost efficiencies – the natural sunset points for the Consolidating Funds were (where already consolidated) and are (in the case of the Liver Fund and PLAL Sub-fund) expected to be reached at various points over the next 20 or so years. Implementing the Liver Fund Consolidation and the consolidations of the other Consolidating Funds in short order under the Legacy Simplification Project has allowed RL to build up expertise and use lessons learned from the other funds to generate efficiencies which would otherwise have been lost between consolidations. This has facilitated (in the case for funds that have already been consolidated) and will facilitate (for funds yet to be consolidated) savings that can be passed on to policyholders in these funds.*

5.10 I provide my views on these issues in section 10.

### Guiding principles

5.11 Due to the unique nature of the Liver Fund, RLMIS (in conjunction with RLI DAC) developed a set of high level aims for the Liver Fund Consolidation to inform decisions regarding the design of the Schemes:

- With-profits policyholders of the Liver Fund (and Liver Ireland Sub-Fund) should continue to be treated equivalently for bonus purposes following fund consolidation process. This means that both UK and Irish asset shares would receive the same uplift percentage from the Liver Fund Estate and bonuses should continue to be set in line with current methodology.
- Other than the Scheme Contribution, no other deduction will be made from the Liver Fund Estate. The remainder of the Liver Fund Estate will be distributed in its entirety through a combination of an uplift provided to included policyholders (UK and Ireland, as defined later in the section) via the Schemes, and an uplift provided to heavily-in-the-money policyholders (as set out paragraph 5.47 below).
- The uplift to be offered under the Schemes will be guaranteed at the Calculation Date (defined in paragraph 5.25) by the RL Open Fund, in advance of the **"Implementation Date"** of the Schemes. Any costs/profits to the RL Open Fund from providing this guarantee will be settled in full immediately before the Schemes takes effect.
- The compromise(s) offered should be constructed to minimise the risk of a formal fund split being required by one of the Schemes not passing a policyholder vote or obtaining approval of the relevant Court.
- Following the consolidation, the Liver Ireland Business will continue to be reinsured to RLMIS through the LRA, and the Schemes should minimise changes to the LRA. The collateral arrangements will be structured so as to minimise the counterparty default SCR, subject to maintaining the ranking of the Irish policyholders in the event of a winding up of RLMIS, limiting disruption to the assets of the RL Open Fund and avoiding excessive administration requirements.
- The capital requirements, including the capital buffer, for the Liver Ireland Sub-Fund will be met from the RL Open Fund Estate so that the full amount of the Liver Fund Estate (after deduction of the Scheme Contribution) can be distributed to the included policyholders. For clarity the Scheme Contribution (the **"Closed Fund Contribution"** or **"CFC"** in particular) will include allowance for the capital strain of this support being required.
- The reinsurance will be amended so that any cancellation of the arrangement continues to be fair to both the RLMIS and RLI DAC policyholders post implementation of the Schemes.
- The current approach to setting bonuses for RLMIS and RLI DAC will continue (i.e. in respect of RLI DAC, the bonuses on the with-profits business will be set by the RLI DAC Board having taken input and guidance from RLI DAC's HoAF). While the LRA is in place, the RLI DAC Board would generally set bonuses consistent with those set by the RLMIS Board, who will have taken input from RLI DAC and the UK With-Profits Governance Structure. As is currently the case, a dispute resolution process will be followed if agreement cannot be achieved between the two entities.

### Proposal

5.12 The proposal is for the entire business of the Liver Fund to be consolidated into the RL Open Fund. This would see the capital requirements of the Liver Fund transferred to the RL Open Fund, allowing the Liver Fund Estate (after the deduction of certain amounts to be paid by the Liver Fund Estate to the RL Open Fund) to be distributed immediately to the Eligible Policies (as defined below) through an uplift to their Eligible Benefits (the **"Offer Uplift"**). The amount to be paid by the Liver Fund Estate to the RL Open Fund is referred to as the **"Scheme Contribution"** (described in more detail below).

- 5.13 RLMIS proposes that, through the legal mechanism of a scheme of arrangement<sup>3</sup> (see below), it will reallocate the UK Eligible Policies (as defined below) from the Liver Fund to the RL Open Fund. Separately from the SOA, but concomitantly, RLMIS will also reallocate certain other policies currently allocated to the Liver Fund (and all assets, liabilities, rights, powers, benefits and business relating thereto) from the Liver Fund to the RL Open Fund under the Liver Ireland Must Threshold in the IoT. As a consequence, the Liver Fund would be consolidated into the RL Open Fund and no longer exist.
- 5.14 Following the implementation of the proposed Scheme, the Liver Ireland Business policies will continue to be allocated to the Liver Ireland Sub-Fund (albeit that the Liver Ireland Business will now be reinsured into the RL Open Fund, rather than the Liver Fund).

### Legal mechanism

- 5.15 From a legal standpoint, it is proposed that the consolidation would involve the following:
- A SOA in the UK (the UK Scheme), pursuant to Part 26 of the Companies Act 2006, the purpose of which is to enable the consolidation of the Liver Fund into the RL Open Fund, which would be presented to the English High Court for sanction; and,
  - A concurrent SOA in Ireland (the Liver Ireland Scheme), pursuant to Part 9 of the Irish Companies Act 2014, in respect of the eligible policyholders in the Liver Ireland Sub-Fund, which would be presented to the Irish High Court.
- 5.16 The UK Scheme would allow the UK Included Policyholders to permit RLMIS to: (i) deduct the Scheme Contribution (see below) from the Liver Fund Estate; (ii) apply the Offer Uplift to the asset shares / claim values of the UK Eligible Policies; and, (iii) reallocate the UK Included Policies to the RL Open Fund. The Liver Ireland Scheme would allow the Ireland Included Policyholders (as defined below) to permit RLI DAC to: (i) provide its consent to the UK Scheme; (ii) apply the Offer Uplift to the asset shares / claim values of the Ireland Eligible Policies; and, (iii) amend the LRA so that the RL Open Fund assumes the obligations of the Liver Fund in respect of the operation of the LRA.
- 5.17 A conditional contract will also be entered between RLI DAC and RLMIS and submitted to the English and Irish High Courts under which:
- RLI DAC will confirm that: (i) it will make all necessary payments to Ireland Eligible Policyholders; and, (ii) take all other steps in its power which are required to give effect to the UK Scheme; and,
  - RLMIS will confirm that: (i) it will make all necessary payments to RLI DAC; and, (ii) take all other steps in its power which are required to give effect to the Liver Ireland Scheme.
- 5.18 The two Schemes would be co-dependent, i.e. they would both need to be sanctioned to take effect.
- 5.19 In this Report, unless otherwise stated, references to "**the proposed Schemes**" or "**the Schemes**" should be interpreted as referring collectively to the (effectively identical) UK and Ireland SOAs.

### Scope

- 5.20 Under the proposed UK Scheme, RLMIS will make an offer (the "**UK Offer**") to all UK Eligible Policyholders in the Liver Fund, as defined below. Ireland Eligible Policyholders (defined below) of the Liver Ireland Sub-Fund would receive an offer (the "**Ireland Offer**") that is, in effect, the same as that received by UK Eligible Policyholders under the UK Scheme. In this Report, unless otherwise stated, references to the "**Offer**" should be interpreted as referring collectively to the (effectively identical) UK Offer and Ireland Offer.
- 5.21 Under the Offer, these policyholders will be asked to agree to certain payments (collectively termed the Scheme Contribution) being made from the Liver Fund Estate to the RL Open Fund, with the remainder of the Liver Fund Estate being applied to provide an immediate increase (the Offer Uplift) to their Eligible Benefits (where Eligible Benefits means asset shares for with-profits Eligible Policies and claim amounts for non-profit Eligible Policies).
- 5.22 The Offer will take effect from the Implementation Date, which is expected to be 31 December 2022.
- 5.23 Certain policyholders who hold policies invested in the Liver Fund (including certain policyholders within the Liver Ireland Business) are collectively entitled to a share of the Liver Fund Estate. These policies include the eligible policies as defined below.

<sup>3</sup> In fact, there will be two parallel and co-dependent schemes of arrangement – one in the UK and one in Ireland, as outlined in 5.15.

## Eligible policies

### THE UK SCHEME

- 5.24 Policies of RLMIS that are eligible for the UK Offer are referred to in this Report as "**UK Eligible Policies**" and holders of UK Eligible Policies are referred to as "**UK Eligible Policyholders**".
- 5.25 A UK Eligible Policy is a with-profits or CB policy allocated to the Liver Fund which is not a UK Excluded Policy (see below), and:
- Which will not have reached its scheduled maturity date or retirement date, where applicable, before 31 December 2022;
  - Which has not been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer or death, in each case in accordance with the terms of the policy, as at 31 March 2022 (the "**Calculation Date**") nor as at the date of the UK Scheme Meeting; and
  - In respect of which the UK Eligible Policyholder has not (in accordance with the terms of the policy) ceased to be entitled to receive benefits as at the Calculation Date nor as at the date of the UK Scheme Meeting.
- 5.26 A "**UK Excluded Policy**" means any policy allocated to the Liver Fund which is not eligible for the UK Offer, including:
- Any L&M policy;
  - Any non-with-profits policies of the Liver Fund (other than CB policies); and
  - Any with-profits policy allocated to the Liver Fund immediately prior to the Calculation Date in respect of which, based on the best estimate assumptions applied as at the Calculation Date, the projected value of the benefits payable on the with-profits policy as at the expected date of claim is not expected to be increased by the application of the Offer Uplift and the increase in future premiums, if applicable. Such UK Excluded Policies are referred to as UK heavily-in-the-money ("**UK HITM**") policies.
- 5.27 The holders of UK Excluded Policies are referred to as "**UK Excluded Policyholders**".
- 5.28 If the Scheme were to be implemented, "**UK Included Policies**" would comprise all UK Eligible Policies, which as at 31 December 2022, have not:
- reached their scheduled maturity or retirement date;
  - been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer or death, in each case in accordance with the terms of the policy; and
  - whose policyholders have not ceased to be entitled to receive benefits in accordance with the policy terms;
- 5.29 The holders of UK Included Policies are referred to as "**UK Included Policyholders**".
- 5.30 For the avoidance of doubt, RLI DAC (in its capacity as a policyholder of the Liver Fund by way of the LRA) will not be a UK Eligible (or UK Included) Policyholder under the Scheme.

### THE LIVER IRELAND SCHEME

- 5.31 Policies of RLI DAC that are eligible for the Ireland Offer are referred to in this Report as "**Ireland Eligible Policies**" and holders of Ireland Eligible Policies are referred to as "**Ireland Eligible Policyholders**".
- 5.32 An Ireland Eligible Policy means a with-profits policy or a non-profit CB policy allocated to the Liver Ireland Sub-Fund which is not an Ireland Excluded Policy (see below) and:
- Which will not have reached its scheduled maturity date or retirement date, where applicable, before 31 December 2022;
  - Which has not been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer, or death, in each case in accordance with the terms of the policy, as at the Calculation Date nor as at the date of the Ireland Scheme Meeting; and
  - In respect of which the Ireland Eligible Policyholder has not (in accordance with the terms of the policy) ceased to be entitled to receive benefits as at the Calculation Date nor as at the date of the Ireland Scheme Meeting.
- 5.33 An "**Ireland Excluded Policy**" means any policy allocated to the Liver Ireland Sub-Fund which is not eligible for the Ireland Offer, including:

- Any non-with-profits policies of the Liver Ireland Sub-Fund (other than CB policies); and
- Any with-profits policy allocated to the Liver Ireland Sub-Fund immediately prior to the Calculation Date in respect of which, based on the best estimate assumptions applied as at the Calculation Date, the projected value of the benefits payable on the with-profits policy as at the expected date of claim is not expected to be increased by the application of the Offer Uplift and the increase in future premiums, if applicable. Such Ireland Excluded Policies are referred to as **"Ireland HITM policies"**.

5.34 The holders of the Ireland Excluded Policies are known as **"Ireland Excluded Policyholders"**.

5.35 An **"Ireland Included Policy"** is defined as an Ireland Eligible Policy that continues to be invested in the Liver Ireland Sub-Fund and which, as at 31 December 2022, has not:

- reached its scheduled maturity or retirement date;
- been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer or death, in each case in accordance with the terms of the policy; and,
- In respect of which the Ireland Eligible Policyholder has not ceased to be entitled to receive benefits (in accordance with the terms of the policy),

5.36 The holders of the Ireland Included Policies are known as the **"Ireland Included Policyholders"**.

## THE SCHEMES

5.37 Throughout this Report I collectively refer to:

- The UK Eligible Policies and the Ireland Eligible Policies as the **"Eligible Policies"**;
- The UK Eligible Policyholders and the Ireland Eligible Policyholders as the **"Eligible Policyholders"**;
- The UK Included Policies and the Ireland Included Policies as the **"Included Policies"**;
- The UK Included Policyholders and the Ireland Included Policyholders as the **"Included Policyholders"**; and
- The UK HITM policies and the Ireland HITM policies as the **"HITM policies"**.

## The Offer

5.38 The Offer made to Eligible Policyholders will be as follows:

- To receive an immediate uplift (the Offer Uplift) to their Included Policies on the Implementation Date.  
  
The Offer Uplift percentage (23.1%) would be applied to the asset shares of with-profits Included Policies and to the claim amounts of CB Included Policies. This compares to the expected BAU uplift to asset shares of with-profits policies and claim amounts of CB policies of the Liver Fund and Liver Ireland Sub-Fund in 2023 of 2.7%, although additional enhancements would be expected in future years to with-profits and CB policies that remain in-force, increasing their overall distribution from the estate over time.
- In addition, for with-profits Included Policies where the policyholder is still paying regular premiums (i.e. the policy has not been made paid-up and the policyholder has not reached the fully free-paid age), the Offer Uplift percentage (23.1%) would also be made to the amount allocated to asset share in respect of future premiums as and when those premiums are paid and credited to asset shares.
- The application of the Offer Uplift, combined with the payment of the Scheme Contribution (see below) is, in combination with the uplift provided to HITM, expected to exhaust the Liver Fund Estate and therefore, following the application of the Offer Uplift, the Liver Fund Estate will cease to exist, and Included Policies will not receive any future distributions from the Liver Fund Estate.
- Once transferred into the RL Open Fund, Liver Fund policies would not receive any future distributions from the inherited estate of the RL Open Fund.

5.39 The Offer Uplift percentage of 23.1% (when rounded to the nearest 0.1%) included in the voting packs that would be sent to policyholders was calculated based on the Solvency II balance sheet for the Liver Fund as at 31 March 2022, projected to the Implementation Date of the Scheme, which is expected to be 31 December 2022. The Offer Uplift percentage will be fixed until the Implementation Date.

- 5.40 Although not part of the Offer, it should be noted that holders of policies eligible for distributions of the Liver Fund Estate will also receive (on 1 July 2022) a 3.6% uplift to the asset shares of the with-profits policies and to the claim amounts of CB policies in respect of the excess surplus (above the 1-in20 year capital target from the Liver Capital Framework) in the Liver Fund as at 31 December 2021. This distribution is in line with the Liver IoT and the value has been calculated using the prescribed methodology. The distribution will be applied at 1 July 2022, and the Offer Uplift percentage has been calculated allowing for this distribution.
- 5.41 It should be noted that while the effect of the two Schemes for Ireland Included Policyholders and UK Included Policyholders would be the same (and as set out above), the compromise under the Liver Ireland Scheme differ legally from that under the UK Scheme. For the Liver Ireland Scheme, the Ireland Eligible Policyholders will be asked to permit RLI DAC to consent (as a creditor of RLMIS under the LRA) to the UK Scheme under which the Scheme Contribution will be deducted.
- 5.42 Beyond the changes described above, there would be no further changes to the terms and conditions of any policies of RLMIS or RLI DAC as a result of the Schemes. In particular:
- The UK Included Policies would remain as the same type of policy, either with-profits or non-profit CB, following the application of the Offer Uplift and the consolidation of the business of the Liver Fund into the RL Open Fund;
  - The Ireland Included Policies would remain as the same type of policy, either with-profits or non-profit CB, following the application of the Offer Uplift; and,
  - The Offer would not affect any additional policy benefits.

#### Options available to Eligible Policyholders

- 5.43 Under the Offer, Eligible Policyholders have two options:
- **To vote in favour of or against the Offer:** If the English High Court and Irish High Court were to sanction the Schemes then they would become binding on all Eligible Policies held by Eligible Policyholders that remain in-force at 31 December 2022, the expected Implementation Date of the Schemes, including those who voted against the Offer.
  - **To do nothing:** Eligible Policyholders may decide that they do not wish to respond to the Offer. If the Schemes were to be sanctioned by the English High Court and Irish High Court then they would become binding on all Eligible Policies held by Eligible Policyholders that remain in-force at 31 December 2022 as above, including those who do not respond to the Offer.
- 5.44 If the English High Court or the Irish High Court were to decline to sanction the UK Scheme or the Liver Ireland Scheme respectively, then neither the UK Scheme nor the Liver Ireland Scheme would be implemented, and all of the Eligible Policies would remain unchanged.

#### Scheme implementation conditions

- 5.45 For the Schemes to be implemented the following conditions must be met:
- The proposed UK Scheme must be approved by the necessary majority of UK Eligible Policyholders at the UK Scheme Meeting as set out in the Offer Acceptance Thresholds (described in section 6);
  - The proposed Liver Ireland Scheme must be approved by the necessary majority of Ireland Eligible Policyholders at the Ireland Scheme Meeting as set out in the Offer Acceptance Thresholds (described in section 6);
  - The English High Court must sanction the UK Scheme at the English Sanctions Hearing; and
  - The Irish High Court must sanction the Liver Ireland Scheme at the Ireland Sanctions Hearing.
- 5.46 I refer to these conditions in this Report as the "**Scheme Implementation Conditions**" and, once these conditions are met, the RLMIS Board can choose whether it will resolve to implement the UK Scheme and the RLI DAC Board can choose whether it will resolve to implement the Liver Ireland Scheme, noting that the Schemes are co-dependent so either both or neither of the Schemes must be implemented.

#### The HITM policies

- 5.47 As at 31 March 2022, there were 5,396 policies Ireland HITM policies (with asset shares of approximately £46.3 million) and 713 UK HITM policies (with asset shares of approximately £2.0 million).

- 5.48 HITM policies are not included within the scope of the Schemes and holders of HITM policies will not be asked to vote upon the Schemes. However, if the Schemes are implemented, the HITM policies would receive the Offer Uplift to their asset shares, i.e. the same percentage that applies to Included Policies under the Schemes.
- 5.49 It should be noted that, if the Scheme were to be implemented, while the asset shares of HITM policies would receive the same Offer Uplift, a holder of a HITM policy would only receive a higher pay-out on claim as a result of the Offer Uplift if:
- The holder of the policy elected to access their policy benefits on a date on which their guaranteed benefits did not apply; or
  - Investment returns on assets backing asset shares were to exceed expectations to such a degree that the guaranteed benefits would no longer be in-the-money.
- 5.50 This is because (by definition) for the HITM policies, if the guaranteed benefits remain in-the-money, then the uplifted asset share of the policy would not be relevant in determining the policy's pay-out provided the policy was held to maturity or to a date on which the guaranteed benefits would apply.
- 5.51 As HITM policies would receive the Offer Uplift if the Schemes were implemented (although outside of the Schemes), where I comment in this Report on the impact of the Schemes on Included Policies in the context of receipt of the Offer Uplift, such comments are also applicable to HITM policies unless otherwise stated.

### Scheme contribution

- 5.52 Under the proposed Scheme, the Scheme Contribution will be paid from the Liver Fund Estate to the RL Open Fund.
- 5.53 The Scheme Contribution is the sum of the following:
- The Closed Fund Contribution;
  - The Project Costs Allowance; and,
  - The Premium Uplift Contribution.

### CLOSED FUND CONTRIBUTION (CFC)

- 5.54 Under the proposed Scheme, the Closed Fund Contribution (or CFC) is paid from the Liver Fund Estate to the RL Open Fund to compensate the RL Open Fund for taking on the responsibility for meeting the capital requirements associated with the business being consolidated under the proposed Scheme (i.e. both the directly-written business of the Liver Fund and the business in the Liver Ireland Sub-Fund which is reinsured into the Liver Fund via the LRA, and both Eligible Policies and those that are not Eligible Policies).

### Methodology

- 5.55 The CFC is calculated using a "required return on capital" approach. This approach involves multiplying the projected capital requirement associated with the business at each point in time over the run-off period by a rate representing RLMIS's required rate of return on capital provided (the "**Required Return on Capital**"). The resulting amounts are then discounted to the relevant date of calculation using the risk-free interest rate curve specified under Solvency II (without the volatility adjustment but allowing for the credit risk adjustment) and which RLMIS uses to calculate its Risk Margin for the purpose of UK Solvency II reporting. Summing these discounted amounts provides the CFC.
- 5.56 As can be seen from the description in the previous paragraph, the calculation of the CFC therefore depends on:
- The projected capital requirements;
  - The run-off period;
  - The Required Return on Capital; and,
  - The risk-free interest rate curve.
- 5.57 In the following paragraphs I expand on each of these in turn.
- Projected capital requirements*
- 5.58 RLMIS proposes to use the following definition of capital requirement for the purposes of the CFC calculation:



- The Liver Fund's SCR (excluding all market risk and some counterparty default risks, and net of the value of management actions which apply in the Liver Fund); plus
- The target Capital Buffer under the RLMIS Capital Framework; plus
- The Liver Fund's Risk Margin less any TMTP; less
- The Liver Fund's share of diversification benefit arising from the consolidation; less
- The CFC.

- 5.59 RLMIS terms this amount the net balance sheet strain ("**NBSS**") to the RL Open Fund, i.e. the net reduction in excess capital that results from the RL Open Fund's taking on the Liver Fund. Note that the NBSS at any point in time is floored at zero (i.e. it cannot be a negative amount). Note also that the inclusion of the CFC in the definition of NBSS introduces some circularity into the calculation of the CFC, which means that an iterative (goal-seeking) approach to its calculation is required.
- 5.60 The rationale for excluding the market risk component of the SCR is that, under the Liver Fund Consolidation, the assets of the Liver Fund to be transferred to the RL Open Fund will include an amount equal to the Liver Fund UK Solvency II Best Estimate Liability ("**BEL**"), which is calculated on a basis that is close to market-consistent and includes the cost of guarantees. The assets transferred from the Liver Fund in respect of the cost of guarantees should be sufficient for the RL Open Fund to purchase the necessary hedging assets to remove the vast majority of market risk arising from these guarantees.
- 5.61 The Capital Buffer refers to the additional amount of capital representing the 1-in-20-year buffer above the Internal SCR in line with the capital target under the RLMIS Capital Framework (which is the same Capital Buffer as would apply under the Liver Capital Framework).
- 5.62 Consolidating the Liver Fund into the RL Open Fund will generate material diversification benefits in the calculation of the SCR (i.e. the SCR post-consolidation will be less than the sum of the two standalone SCRs immediately pre-consolidation). This reduction in capital requirements is reflected in the post-Liver Fund Consolidation capital requirements of the RL Open Fund for the purposes of the CFC calculation. RLMIS is proposing that the benefit be shared 50:50 between the RL Open Fund and the Liver Fund (i.e. the element of the NBSS entitled 'the Liver Fund's share of diversification benefit' is taken as 50% of the additional diversification benefit arising in the RL Open Fund capital requirements post-Liver Fund Consolidation relative to the pre-Liver Fund Consolidation capital requirements at each point in time over the run-off period). The CFC is not reduced in respect of any 'extra' diversification benefits arising from implementing the PLAL Fund Consolidation over and above the diversification benefits arising from implementing the two consolidations in isolation.
- 5.63 Currently under the LRA, the Liver Fund Estate supplies the capital to the Liver Ireland Sub-Fund to meet its capital requirements and the Capital Buffer required under the Liver Capital Framework. Following the implementation (and under the amended LRA), the RL Open Fund would provide this capital. As the business in the Liver Ireland Sub-Fund is 100% reinsured to RLMIS under the LRA, the only risks that remain in the fund are counterparty default (in respect of RLMIS) and operational risk (that is broadly a function of the counterparty default risk). Any charge made as part of the CFC for this capital would in effect be RLMIS charging the Included Policies for the risk of RLMIS itself becoming insolvent. It is therefore proposed that the capital required to be held in the Liver Ireland Sub-Fund is not included in the NBSS for calculating the CFC.

- 5.64 I comment on the approach to determining the NBSS in my assessment of the proposed Scheme in section 10.

*Run-off period*

- 5.65 The IoT does not contain extensive detail on how the consolidation of the Liver Fund should be conducted when the Liver Sunset Must Threshold is breached. However, it does not permit a 'charge for the provision of capital support' to be deducted. This is because, at the time the IoT became effective, it would have been anticipated that the additional capital requirements for the RL Open Fund in relation to the business being consolidated once the Liver Sunset Must Threshold has been reached would be immaterial.
- 5.66 However, it is not expected that the additional capital requirements for the RL Open Fund in relation to the business being consolidated would be immaterial in advance of reaching the Liver Sunset Must Threshold. Therefore, it is unlikely that RLMIS would choose to undertake the consolidation early (i.e. at some point after reaching the Liver Sunset May Threshold but in advance of reaching the Liver Sunset Must Threshold) given that no charge could be made under the terms of the IoT to compensate the RL Open Fund for the additional capital requirements it would be taking on.

- 5.67 The proposal under the Schemes is for the Required Return on Capital to be charged up to the estimated Liver Sunset Point (i.e. the point at which RLMIS estimates the Liver Sunset Must Threshold will be reached) but not thereafter. This run-off period therefore aligns with the point at which the RL Open Fund would be obliged to meet the capital requirements without a compensation payment, in line with the terms of the IoT. This is currently projected to be in or around 2041. It should be noted that the NBSS is expected to fall to zero ahead of this point (by around 2039) in the calculation of the CFC, and so in practice this limit does not change the amount of the CFC.

*Required return on capital*

- 5.68 The RL Open Fund needs to consider an investment in the Liver Fund Consolidation relative to other investments it could make. Therefore, in determining an appropriate CFC, the RL Open Fund ought to make a charge for its Required Return on Capital which is consistent with the return that it may aim to make on alternative investments.
- 5.69 Note that, as the RL Open Fund will be able to earn a risk-free return on the capital employed to support the capital requirements of the Liver Fund, the rate charged to the Liver Fund Estate via the CFC would be the margin in excess of this, i.e. a risk premium.
- 5.70 I understand that, in order to arrive at an appropriate rate, RLMIS has considered a number of factors, namely:
- RLMIS's target return for external ventures, which has amongst other factors been informed by past experience of the return sought by other firms in similar conditions, and has been set by the RLMIS Board;
  - Rates applied on precedent schemes of arrangement, e.g. Sun Life of Canada's 2017 scheme of arrangement (11% p.a.); and
  - Rates underlying recent bulk annuity deals (9% p.a.).
- 5.71 In addition, RLMIS argues that from the Liver Fund's perspective, as an alternative to the Liver Fund Consolidation, there is the option of reinsurance to a third-party reinsurer. A reinsurer would be expected to charge for the capital that it needed to cover the SCR (or some multiple of the SCR) in respect of the business that it is reinsuring, which means that the Liver Fund would need to pay a market rate of return on capital to the third-party reinsurer. An analysis of achieved return on equity metrics for reinsurers suggests that this might be broadly of the order of a gross rate of around 12% p.a. However, RL has a more complete knowledge of the business of the Liver Fund than a third-party reinsurer, having been responsible for it since 2001. This would suggest that RL should require a lower risk premium – and therefore a lower overall rate of return – than an external reinsurer.
- 5.72 RLMIS has also taken the view that this risk premium should be reduced to some extent to allow for the fact that, as described in section 5, under the proposed Schemes all project costs associated with the Schemes are to be borne by the Liver Fund.
- 5.73 However, against this, RLMIS notes that it is incurring a significant opportunity cost in seeking to undertake the Liver Fund Consolidation as opposed to investing its resources in alternative value-generating projects which, it argues, suggests that the risk premium charged by the RL Open Fund should be increased to some extent to compensate the RL Open Fund for this opportunity cost, as well as for taking on the risk that the Liver Fund Consolidation is not completed successfully after an extended development period (execution risk). Furthermore, RLMIS notes that one of the material risks in the Liver Fund, longevity risk is not as straightforward to reinsure in the market as other risks and that these factors would tend to support an increase in the RL Open Fund's required rate of return, reflecting the higher charges the Liver Fund would likely incur on reinsuring these risks.
- 5.74 In light of all these considerations, RLMIS has settled on a gross Required Return on Capital that is 9% p.a. in excess of the prevailing risk-free curve specified by UK Solvency II regulations, for the purposes of the calculation of the CFC as at the Calculation Date.
- 5.75 I consider the reasonableness of RLMIS's arguments, its approach to deriving the Required Return on Capital rate, and the fairness of the proposed Required Return on Capital rate from the perspective of policyholders in the Liver Ireland Sub-Fund in section 10.

*Risk-free interest rate curve*

- 5.76 The risk-free interest rate curve used to discount values to the Calculation Date is the GBP SONIA curve as specified by UK Solvency II regulations (without the volatility adjustment but allowing for the credit risk adjustment).

**Amount of the CFC**

- 5.77 If the Schemes are implemented, the CFC payable from the Liver Fund Estate to the RL Open Fund, calculated as described above, is expected to be £43.2 million.



## PROJECT COSTS ALLOWANCE

- 5.78 RLMIS will incur costs in executing the Legacy Simplification Project across the various Consolidating Funds. These costs include the cost of internal resources, the cost of issuing communications to policyholders, fees paid to external advisors, fees paid to independent experts, and the cost of supporting regulatory review. Some of these costs have already been incurred (e.g. a significant portion of the costs in implementing the consolidations in 2021) and are therefore known, whereas others are projected to be incurred in the future.
- 5.79 As at the **"Project Costs Calculation Date"** (31 March 2021), RL estimated the cost of implementing the consolidations (and the associated review of minor product changes to be made in respect of certain of the Consolidating Funds) under the Legacy Simplification Project (the **"Project Costs"**) to be £38.1 million, inclusive of all costs incurred up to that date, and all projected future costs. This estimate was based on RLMIS's experience of undertaking schemes of arrangement and Part VII transfers in the recent past. It also considered cost synergies that RLMIS expected to realise from implementing the Legacy Simplification Project over a short, concentrated period of time utilising largely the same internal and external resources over its course.
- 5.80 RLMIS argues that, were it to implement the consolidation for each Consolidating Fund in isolation as and when each fund reached its natural sunset point, it would be less able to leverage the experience gained from earlier consolidations, owing to the longer period of time that would have elapsed between consolidations. Synergies that would otherwise have been gained from completing consolidations in a single concentrated project would be lost, meaning the overall cost of executing the Legacy Simplification Project would likely be higher. In addition, as a consequence of delaying the completion of the project, there would be fewer closed fund policyholders over which the costs could be distributed.
- 5.81 In terms of the allocation of costs between the Consolidating Funds and the RL Open Fund, RLMIS proposes to charge the estimated Project Costs wholly to the Consolidating Funds. RLMIS argues that this approach is consistent with an arm's length transaction, under which the seller (or cedant) of risk in a reinsurance transaction would be liable for development expenses incurred. I note the RAIB Sub-fund, UFIB Sub-fund, UFOB Sub-fund and SL Fund were consolidated with Project Costs charged on this basis.
- 5.82 RLMIS has stated that it considers that it would be unfair to charge each Consolidating Fund the costs incurred in relation to the consolidation directly affecting that fund, as this would result in funds that were consolidated earlier being charged more than funds that were consolidated later due to the learnings and synergies acquired over time. Instead, RLMIS proposes to allocate the estimated Project Costs across the Consolidating Funds on a pro rata basis according to the value of the total asset share (less, in the case of the Liver Fund, the asset shares of the L&M policies, and with the addition of the BEL for the CB policies) plus the estate value in each Consolidating Fund as at the Calculation Date.
- 5.83 On this basis, the costs allocated to the Liver Fund and the Liver Ireland Sub-Fund (jointly) amounted to £6.9 million.
- 5.84 If the actual costs of the Fund Consolidations were to exceed the expected costs used to derive the project costs allowances that would be charged to the appropriate funds then the excess cost would, in effect, be met by the RL Open Fund and would not be charged back to the funds (or the policies in those funds). If the costs of the Fund Consolidations were to be lower than those expected, the benefit would accrue to the RL Open Fund.
- 5.85 As the RL Open Fund would take on the risk of a cost overrun in relation to the Fund Consolidations, the allocation of the expected cost of the Fund Consolidations that would be charged to the Liver Fund Estate (with reference to the total asset shares of with-profits policies (excluding the L&M policies) plus the BEL for the CB policies plus the Liver Fund Estate) would be increased by an amount intended to represent an **"Indemnity Premium"**.
- 5.86 At the point of calculation (the Project Costs Calculation Date), certain of the costs of the Fund Consolidations were known as they had either already been incurred; or, would be incurred in the future but would be subject to fixed cost contracts and so would not vary from their expected level. An Indemnity Premium would not be charged in respect of such known costs.
- 5.87 The Indemnity Premium was set as a fixed percentage (15%) of the future (at the Project Costs Calculation Date), non-fixed expected costs of the Fund Consolidations.
- 5.88 Overall, the Indemnity Premium attributable to the Liver Fund and the Liver Ireland Sub-Fund is £0.3 million. Adding this to the cost allocation for the funds of £6.9 million gives a total Project Costs Allowance for the Liver Fund and the Liver Ireland Sub-Fund of £7.2 million.
- 5.89 It should be noted that the terms of the IoT only allow for certain exceptional costs to be charged to the Liver Fund Estate and do not allow for any margins to be included. Therefore, this Project Costs Allowance (including the Indemnity Premium) could not be charged to the Liver Fund Estate in the absence of the proposed Schemes.

- 5.90 I consider the fairness of the overall approach to allowing for Project Costs in my assessment of the proposed Schemes in section 10.

#### PREMIUM UPLIFT CONTRIBUTION

- 5.91 I understand that, when designing previous fund consolidations, RLMIS analysed whether policyholders who continue to pay premiums would be detrimentally impacted if the estate was distributed early as opposed to being distributed gradually over time, i.e. the uplift received under the consolidation would gradually reduce against the status quo as additional premiums are received. This led to allowance being made so that future premiums are uplifted as they are credited to asset shares.
- 5.92 It is proposed that the same approach be adopted in this case, with an uplift on the amount applied to asset shares when future contractual premiums are received, in line with the uplift that is granted to asset shares at the consolidation point.
- 5.93 The Offer would involve an immediate distribution of the Liver Fund Estate (less the Scheme Contribution) to Included Policies. For with-profits Included Policies, this distribution would take the form of the uplift that would be applied to the asset shares of the Included Policies on the Implementation Date and to the amount allocated to asset share when future contractual premiums are paid.
- 5.94 In respect of future contractual premiums, the additional uplift to asset shares would take place as and when the premiums are paid and credited to asset shares for those with-profits policies of the Liver Fund (excluding L&M policies) that are still paying regular premiums (i.e. the policy has not been made paid-up and the policyholder has not reached the fully free-paid age).
- 5.95 To avoid the risk of 'carpetbagging' (as described in paragraphs 5.116 and 5.117), the additional uplifts would only apply to regular premiums started on or before 31 December 2021.
- 5.96 The portion of the Liver Fund Estate that would be held back to cover the uplift in respect of future contractual premiums is referred to as the **"Premium Uplift Contribution"**. This contribution is based on a best-estimate assessment of expected future contractual premiums to be paid on with-profits policies of the Liver Fund.
- 5.97 For the avoidance of doubt, the application of the uplift to the amount allocated to asset share when future premiums are paid would not result in an increase to the premiums payable by policyholders.
- 5.98 The Premium Uplift Contribution payable by the Liver Fund under the proposed Scheme is £3.3 million.

#### TOTAL SCHEME CONTRIBUTION

- 5.99 In total, the Scheme Contribution amounts to £53.7 million, as summarised in Table 9 below.

**Table 9: Components of the Scheme Contribution (£ millions)**

Item	
Closed Fund Contribution (CFC)	43.2
Project Costs Allowance	7.2
Premium Uplift Contribution	3.3
<b>Total</b>	<b>53.7</b>

Source: Information provided by RLMIS

#### Distribution of the Liver Fund Estate

- 5.100 Under the proposed Scheme, once the Scheme Contribution has been paid from the Liver Fund Estate to the RL Open Fund, the Liver Fund Estate will be used to uplift the Eligible Benefits of the Included Policies. The Offer Uplift will be applied to the Eligible Benefits of each Included Policy on the Implementation Date, with the monetary amount of this increase being determined as the value of the Eligible Benefits of the Included Policy, multiplied by the Offer Uplift.
- 5.101 In addition, the Offer Uplift will be applied to the Eligible Benefits of the Included Policies (other than CB policies) in respect of any eligible future contractual premiums that are paid into these policies as and when those premiums are paid. This reflects the expectation of the holders of any such policies that their future premiums would share in the distribution of the Liver Fund Estate in the absence of the Scheme. As noted in paragraph 5.117, to avoid the risk of carpetbagging, the future premiums eligible for the Offer Uplift will be limited to regular premiums only, limited to the

level of annual premium being paid as at 31 December 2021 (plus any contractual increases such as by way of indexation). As described above (starting at paragraph 5.91), the overall Scheme Contribution will include a Premium Uplift Contribution to provide for this.

5.102 The Offer Uplift that is intended to apply to the Eligible Benefits of the Included Policies (under the Scheme) and to the Eligible Benefits of the HITM Policies (under the wider Liver Fund Consolidation) is determined as (A) divided by (B), where:

- (A) is the value of the Liver Fund Estate, less the Scheme Contribution; and
- (B) is the value of the Eligible Benefits of the Eligible Policies and HITM Policies,

and (A) and (B) are both calculated as at the Calculation Date of 31 March 2022 and projected to the expected Implementation Date of 31 December 2022.

5.103 The (non-economic) assumptions used to determine the financial position of the Liver Fund for the purpose of determining the value of the Liver Fund Estate and the Eligible Benefits of Eligible Policies and HITM Policies (and therefore the Offer Uplift) as at the expected Implementation Date, based on projections from the Calculation Date, are unchanged from those used for RLMIS's audited UK Solvency II balance sheet as at 31 December 2021, with one exception noted in paragraph 5.104 below. These assumptions reflect RLMIS's best-estimate view of future outcomes. The economic assumptions were updated to reflect market conditions as at the Calculation Date.

5.104 An adjustment has been made to the expense assumptions for the Liver Fund since the audited position at 31 December 2021. The audited position allowed for the margins on the charges for administration and investment management services to continue indefinitely. However, the expense assumptions used for the calculation of the Liver Fund Estate available for distribution, as well as the balance sheets as at 31 March 2022 presented in this Report, allow for the margins on the charges to the Liver Fund being removed after 31 December 2039. This change has been made to account for:

- The profit margin on expenses would only apply until the Liver Fund is collapsed under the Liver Sunset Clause, which is expected to be in 2041. The earlier date of 31 December 2039 has been chosen acknowledging that RLMIS may, for operational reasons, execute the Liver Sunset Clause slightly in advance of the Liver Must Threshold being reached; and
- As set out in paragraphs 3.31 to 3.32, to continue to apply the current charging structure in line with the IoT after 30 June 2031, RLMIS would need to apply for a new waiver to modify the application of COBS 20.2.23R whilst the Royal Liver business remains in the Liver Fund. The FCA has informed RLMIS that it has no objection to RLMIS's assumption, for the purposes of calculating the Liver Fund Estate to be distributed under the Schemes and of determining future charges to asset shares after implementation of the Schemes, that the current charging structure could continue to apply until 31 December 2039.

5.105 The application of the Offer Uplift to the Eligible Benefits of the Included Policies and HITM Policies on the Implementation Date is therefore expected to exhaust the remaining Liver Fund Estate (after the Scheme Contribution has been deducted).

5.106 The Offer Uplift does not vary by policy and is 23.1% (to the nearest 0.1%).

5.107 The Offer Uplift was calculated as at the Calculation Date based on a projection of the expected Implementation Date value of the Liver Fund Estate, with surplus assets in the defined benefit pension schemes having been excluded (as not distributable to Eligible Policies). There is therefore a risk that market movements over the interim period result in the actual supportable uplift at the Implementation Date being different to that originally quoted.

5.108 In principle this would necessitate a recalculation of the Offer Uplift at that point. However, a recalculation would create uncertainty for the Eligible Policyholders who are voting on the Scheme. Therefore, to address this issue the Offer Uplift has instead been guaranteed once calculated at the Calculation Date. The Offer Uplift will be mailed to policyholders prior to the Implementation Date and will not be subject to any subsequent recalculation.

5.109 The cost of providing this guarantee will be met by the RL Open Fund, in effect taking on the nature of the risks that it will inherit from the Implementation Date from a slightly earlier date (the Calculation Date) instead. The exposure to the RL Open Fund from providing the guarantee is broadly symmetrical, i.e. there is a broadly equal probability of recording a similar sized loss or gain depending on which direction markets move in. Given this symmetry, there is no explicit charge made by the RL Open Fund for providing the guarantee in respect of market risks.

5.110 There is also the risk that other (non-market related) assumptions in the projection may prove to be incorrect. In respect of such non-market risks, e.g. differences in the actual versus expected rate of policy run-off, the additional exposure taken on by the RL Open Fund over the period prior to the Implementation Date is allowed for through a

proportionate increase in the CFC, consistent with the methodology employed in respect of the period following the Implementation Date. The CFC includes an amount of £1.3 million in respect of this element.

- 5.111 If the ratio of the value of the assets backing the Liver Fund Estate to the value of the assets backing the Eligible Benefits of the relevant policies changes during the period from the Calculation Date to the Implementation Date (during which the Scheme Contribution and Offer Uplift are guaranteed), the value of the Liver Fund Estate will not precisely cover the cost of the Scheme Contribution and the aggregate value of the uplifts due to be applied on the Implementation Date; i.e. there will be a surplus or a shortfall.
- 5.112 In that eventuality, either:
- Assets would be transferred from the RL Open Fund to the Liver Fund to make good any shortfall in the Liver Fund Estate caused by the ratio above decreasing; or,
  - Assets would be transferred from the Liver Fund to the RL Open Fund to ensure that any increase in the ratio above does not lead to there being residual value in the Liver Fund Estate immediately after the Scheme is implemented.
- 5.113 In either case, RLMIS would process this inter-fund transfer immediately before the Schemes are implemented such that, at the Implementation Date, the value of the Liver Fund Estate exactly matches the cost of the Scheme Contribution and the aggregate value of the uplifts to be applied on the Implementation Date.
- 5.114 In the event that fluctuations in the values of the assets backing the Liver Fund Estate and the assets backing Eligible Benefits between the Calculation Date and the implementation of the Schemes lead to a profit to the RL Open Fund that the With-Profits Actuary considers to be excessive, the RLMIS Board will (on the advice of the With-Profits Actuary) take any necessary steps to address any resulting inequity between policies allocated to the RL Open Fund and policies reallocated to the RL Open Fund by way of the Liver Fund Consolidation. Such steps may include a special distribution of some element of that excess to consolidated policies following the implementation of the Schemes.
- 5.115 I comment further on the proposed approach to the distribution of the Liver Fund Estate, including the determination of the Offer Uplift and the approach to guaranteeing the Offer Uplift in my assessment of the Schemes in section 10.

### Carpetchbagging

- 5.116 The Liver Fund and Liver Ireland Sub-Fund currently allow Liver pension policies to increase existing with-profits premiums and pay new with-profits premiums. Switches from unit-linked to UWP are also allowed for certain pension and life policies. When the Schemes were made public through the “**Appetite Mailing**” (a notification to policyholders about the proposed Schemes) in early 2022, there was a risk that policyholders could artificially pay temporarily high levels of additional premiums purely to exploit the planned Liver Fund Consolidation. This course of action is often referred to as “**carpetchbagging**”.
- 5.117 To address this risk, the Offer Uplift in respect of future premiums will be limited to the level of regular premiums set prior to a certain cut-off date, which both RLMIS and RLI DAC propose to set as 31 December 2021. Any lump sum premiums paid (including switches or transfers-in) or regular premium increases started after that date will not receive the Offer Uplift when they are credited to asset shares.

### Alternatives considered

- 5.118 Alternative approaches were considered, such as splitting the Liver Fund Estate between RLMIS and RLI DAC under the terms of the RLI DAC Transfer Scheme. This approach was envisaged in the RLI DAC Transfer Scheme and might, therefore, be what is expected by the CBI and RLI DAC policyholders, but it was felt that this approach would result in a sub-optimal position for both RLMIS and Liver Ireland Business policyholders compared to the ‘no fund split’ option, as:
- In addition to the extra complexity of conducting the estate split, this would result in it being impossible to comply with the uniform rate of return principle as there would no longer be a common pool of assets.
  - A fund split could make it more difficult to complete the full fund consolidation, particularly in respect of the Irish business, which would need to be consolidated into the RLI DAC Open Fund (which would be unlikely to be able to take on the capital requirements of the business for a CFC). Alternatively, reinsurance could be used to keep the capital risk with RLMIS with the CFC forming part of the premium, although this would require the creation of a new reinsurance arrangement as opposed to an amendment to an existing treaty, which would require approval from the CBI.

- 5.119 The possibility of a single UK Scheme was also explored, but I understand that legal advice indicated that there was a risk that this could be challenged in the Irish High Court by those Irish policyholders whose policies were written under Irish law.

### Pension schemes

- 5.120 The two pension schemes each benefit from two guarantees from RLMIS:
- an unconditional guarantee to cover contributions limited to the amount that is recoverable from the Liver Fund; and,
  - a conditional guarantee from the RL Open Fund which has no upper limit.
- 5.121 These guarantees will be replaced by a single unconditional guarantee from the RL Open Fund. The pension fund risks will be captured in the RL Open Fund SCR, and the CFC allows for those risks (albeit the proposed charge is immaterial).
- 5.122 Any liabilities arising from the Irish pension scheme will not fall to RLI DAC, i.e. the current position in that regard remains unaltered.

### Voting

- 5.123 All with-profits policyholders (apart from the L&M policies) and CB policies in the Liver Fund and Liver Ireland Sub-Fund have entitlement to the Liver Fund Estate. As the interests of these policyholders are aligned, they have been included in a single Voting Class (as defined in section 6) for each of the UK Scheme and the Liver Ireland Scheme.
- 5.124 The L&M policies are not entitled to share in the Liver Fund Estate and are therefore excluded from the UK Scheme. There are no L&M policies in the Liver Ireland Sub-Fund,
- 5.125 Further details on the voting arrangements are provided in section 6.

### Impact on IoT

- 5.126 In advance of the Implementation Date of the Liver Schemes, RLMIS will make an application to the PRA to make amendments to the Liver Sunset Clause in the IoT to allow the sunset provisions to be triggered while the LRA remains in place. This amendment, as well as the other proposed amendments to the IoT set out in paragraph 5.128, would be made under the existing modification provisions in the IoT, and so will be carried out outside of the proposed Schemes.
- 5.127 Following these amendments and following the Liver Ireland Scheme and UK Scheme being implemented, RLMIS intends to operate the Liver Sunset Clause in the IoT to consolidate the Liver Fund into the RL Open Fund. The effect of this would be to reallocate all remaining policies, assets and liabilities from the Liver Fund to the RL Open Fund, and to bring the substantive provisions of the IoT to an end. In particular, the Liver Sunset Clause specifies that many of the provisions of the IoT should fall away following this consolidation, including that the LSC would cease to have a role in monitoring the management of the Liver business.
- 5.128 Notwithstanding this, and having undertaken an analysis of the provisions of the IoT in conjunction with its legal advisers, Pinsent Masons, RLMIS and RLI DAC consider that there is a small number of provisions of the IoT that it is desirable to continue to apply, and such provisions would be included in one of:
- A cut-down revised IoT. Provisions such as those that govern the charges (including in respect of exceptional costs) that may be allocated to Liver policies would be retained here. The application to the PRA described in paragraph 5.126 will allow the relevant provisions to be retained and clarify their ongoing application to the policies of the Liver Ireland Sub-Fund and the policies formerly allocated to the Liver Fund. This includes specifying that the margin on expenses under the rate card will apply until 31 December 2039, at which time charges will revert to an 'actual costs' basis. In the absence of the Schemes, the margin is expected to continue until the consolidation of the Liver Fund into the RL Open Fund, and so 2039 has been chosen acknowledging that RLMIS may, for operational reasons, execute the Liver Sunset Clause slightly in advance of the Liver Sunset Must Threshold being reached (which is expected to happen in 2041).
  - The RL Long Term Fund PPFM. Many of the CPFM in the IoT are already reflected (as either principles or practices) in the Royal Liver PPFM. The principles and practices that are relevant to the management of the Liver business following the implementation of the Schemes would be transferred to the RL Long Term Fund PPFM will be transferred to the RL Long Term Fund PPFM following implementation of the Schemes.



### Impact on RLI DAC Transfer Scheme

- 5.129 The RLI DAC Transfer Scheme would be amended to reflect the consolidation of the Liver Fund into the RL Open Fund. These amendments would be made under the existing modification provisions in the RLI DAC Transfer Scheme, which require a certificate from an independent actuary to the effect that the proposed amendments will not materially adversely affect the security or reasonable expectations of the holders of policies allocated to the Liver Ireland Sub-Fund. I have included the required certificate in Appendix D of this Report.
- 5.130 The amendments to be made include:
- Removing references to estate distribution, as the Liver Fund Estate will have been distributed in full;
  - Changing references to the LSC to refer to the WPC instead, as the LSC would cease to exist following the consolidation of the Liver Fund into the RL Open Fund;
  - Changing references to the CPFPM in the IoT to instead refer to the RL Long Term Fund PPFM, as the surviving principles from the CPFPM would be contained in the RL Long Term Fund PPFM following the consolidation of the Liver Fund; and
  - Amending the provisions that govern the charges that may be allocated to Liver Ireland policies in line with the proposed amendments to the IoT set out in paragraph 5.128.
- 5.131 The application of the uplifts to the asset shares of with-profits Ireland Included Policies under the Liver Ireland Scheme would delay the expected date at which the thresholds of the Liver Ireland Sunset Clause would be met. However, the Liver Ireland Sunset Clause would only be triggered if the LRA was no longer in place, and so at this time it is effectively redundant.

### Impact on LRA

- 5.132 Although both RLMIS and RLI DAC intend for the LRA to remain in place there are a number of consequences from Liver Fund Consolidation that will need to be addressed with regard to the LRA. Namely:
- As the Liver Fund will cease to exist, the source of capital support to the Liver Ireland Sub-Fund will change from the Liver Fund to the RL Open Fund; and,
  - The cancellation terms of the LRA will need to be amended to reflect Liver Fund Consolidation.
- 5.133 The first of these is straightforward as there is no change to the party to the agreement, just to the fund within RLMIS that is used to maintain the capital requirements in the Liver Ireland Sub-Fund. The RL Open Fund should have received sufficient compensation, via the CFC, for taking on the capital support role for the Liver business.
- 5.134 The second issue is more material. The LRA cancellation terms currently specify that the Liver Ireland Sub-Fund policyholders would receive their share of the Liver Fund Estate should the LRA be terminated. However, as the Liver Fund Estate will be distributed in full at the point of consolidation, this will no longer be possible. The Liver Ireland Sub-Fund would, however, receive a rebate on the CFC that will be made in respect of the capital requirements that no longer need to be met from the RL Open Fund.
- 5.135 I understand that there are no plans to terminate the LRA either immediately following the Liver Fund Consolidation or thereafter. However, if at some subsequent point the LRA is terminated, it will be necessary to determine what an appropriate Termination Payment should be. The Scheme Contribution is determined on the assumption that the LRA remains in place throughout the lifetime of the Liver Ireland business. Therefore, if the LRA is cancelled prior to the complete run off of the Liver Ireland business a payment may need to be made in respect of the 'unspent' elements of the Scheme Contribution at that time.
- 5.136 In terms of the collateral that supports the LRA, this will continue to be provided by RLMIS under the terms of the agreement, with the necessary assets provided by the RL Open Fund. As the RL Open Fund is expected to receive sufficient assets from the Liver Fund to meet these collateral requirements (through the transfer of assets equal to the BEL of transferring policies), the Liver Fund Consolidation is not expected to have any impact on RLMIS's ability to provide the necessary collateral.

### Governance

- 5.137 Following the implementation of the Schemes, the governance of the with-profits business would be broadly unchanged and would continue to consist principally of:
- Within RLMIS: the WPA, the WPC and the RLMIS Board; and

- Within RLI DAC: the RLI DAC HoAF and the RLI DAC Board.
- 5.138 The LSC will be disbanded as specified by the provisions of the IoT, with the WPC assuming responsibility for ensuring compliance with the terms of the LRA and the continuing provisions of the IoT.
- 5.139 In respect of the principles and practices for the management of the Liver business following the implementation of the Schemes:
- The Royal Liver PPFM will cease to be applicable to the business after the implementation of the Schemes (and will cease to exist), and the RL Long Term Fund PPFM will govern the ongoing management of the former Liver Fund business;
  - Elements of the Royal Liver PPFM that are not currently covered in the RL Long Term Fund PPFM would be transferred across to the RL Long Term Fund PPFM, with some edits to remove references to principles and practices that would not apply following implementation of the Schemes (such as references to distributions of the Liver Fund Estate);
  - Some amendments would be made to the principles and practices currently in the Royal Liver PPFM to reflect that the Liver Fund business would be transferred to the RL Open Fund and that the Liver Fund would cease to exist, as well as to align some principles and practices between the funds, such as target ranges for pay-outs; and
  - Amendments would be made to the Liver Ireland Sub-Fund WPOP to:
    - Remove references to principles and practices that would not apply following implementation of the Schemes (such as references to distributions of the Liver Fund Estate);
    - Reflect the fact that the LRA means the management of the Liver Ireland Sub-Fund is linked to the management of the RL Open Fund rather than the Liver Fund;
    - Reflect the fact that additional detail and information on the management of the Liver Ireland Sub-Fund can be found in the RL Long Term Fund PPFM rather than the Royal Liver PPFM; and
    - Reflect how exceptional costs will be managed given that there will no longer be a Liver Fund Estate.

### Investment implications

- 5.140 If the Schemes were to be implemented, assets backing the asset shares of the majority of with-profits Included Policies and other with-profits policies in the RL Open Fund would be pooled.
- 5.141 As a result, a uniform asset share EBR would be applied across all of the with-profits business in the RL Open Fund (including the with-profits business reinsured in from the Liver Ireland Sub-Fund) following the implementation of the Schemes, with the exception of the groups of policies in the RL Open Fund with significant guarantees for which the backing assets have been separately assigned. There would be no change to the asset strategies for this business as a result of the proposed Schemes and the backing assets would continue to be separately assigned.
- 5.142 The asset share EBR of the RL Open Fund was 68% as at 31 December 2021. If the Schemes were to be implemented, the EBR for the with-profits Included Policies would be unchanged (68% in both funds).
- 5.143 The Liver Fund Estate is invested primarily in UK and Euro Sovereign and corporate bonds with a proportion held as cash. If the Schemes were to be implemented then, after consolidation, trades to purchase additional equities may be required to ensure an asset share EBR of 68% is achieved following the application of the Offer Uplift to the asset shares of with-profits Included Policies and the subsequent pooling of assets backing asset shares between the Liver Fund and the RL Open Fund. The costs of these trades would be attributed to asset shares in the RL Open Fund.
- 5.144 The non-profit business of the Liver Fund (including the non-profit business reinsured in from the Liver Ireland Sub-Fund) would continue to be backed by a combination of UK and Euro Sovereign and corporate bonds. This includes the CB Included Policies for which the claim amounts would be increased by the application of the Offer Uplift under the Schemes.
- 5.145 The required collateral under the LRA would become part of the assets of the RL Open Fund, but would continue to be ring-fenced and available to meet claims arising on the policies of the Liver Ireland Sub-Fund.
- 5.146 The hedges in place in the Liver Fund to manage its capital position against market risks are expected to be retained following the implementation of the Schemes, and so these would be transferred to the RL Open Fund. These would be reviewed as part of the overall review of the investment strategy of the RL Open Fund following the Schemes.



### Exceptional costs

- 5.147 At present, where exceptional costs occur then, with the approval of the WPA and the WPC of the proposed apportionment between the RL Open Fund and the RLMIS Closed Funds, part of the exceptional costs can be charged to the Liver Fund. Exceptional costs are typically apportioned to the various funds based on the total BEL including any unit reserves within each fund (rather than being allocated based on asset shares).
- 5.148 The IoT limits the circumstances under which exceptional costs may be attributable to the Liver Fund, and requires RLMIS to use reasonable endeavours to mitigate or minimise any exceptional cost attributable to the Liver Fund. In addition, the RLI DAC Transfer Scheme limits the circumstances under which exceptional costs may be attributed to the Liver Ireland Sub-Fund, as well as setting out the process by which allowable exceptional costs may be applied to the Liver Ireland Sub-Fund. These limitations on exceptional costs will be retained in the same documents following the implementation of the Schemes.
- 5.149 Currently any exceptional costs that are attributed to the Liver Fund are met by the Liver Fund Estate.
- 5.150 If the Scheme were to be implemented, there would be no Liver Fund Estate to which to charge any exceptional costs relating to policies transferred from the Liver Fund (and those reinsured from the Liver Ireland Sub-Fund). Instead, the amount that would have been charged to the Liver Fund Estate would either be:
- In most circumstances, met by the RL Open Fund Estate and then recovered over time from the asset shares of policies transferred from the Liver Fund (excluding L&M policies), the asset shares of policies in the Liver Ireland Sub-Fund and the declared contingent bonuses applying to CB policies. The amount of the exceptional cost would be charged over the projected future run-off of these policies. Interest would be charged on these costs at a risk-free interest rate; or
  - In some circumstances (if determined to be fair and reasonable by the RLMIS Board and the WPC), charged directly to the asset shares of policies transferred from the Liver Fund (excluding L&M policies), the asset shares of policies in the Liver Ireland Sub-Fund (if permitted under the terms of the RLI DAC Transfer Scheme, and subject to the agreement of the RLI DAC HoAF) and the declared contingent bonuses applying to CB policies in the form of an immediate, uniform percentage deduction across all such policies in-force at that time. This approach to charging for exceptional expenses is expected to be adopted where all policyholders are expected to benefit equally from the action being taken that has incurred the cost.
- 5.151 Both of the above approaches need to take into account advice from the RLMIS WPA and the RLI DAC HoAF, the rationale for the Scheme and for the calculation of the CFC, and the associated representations made by RLMIS in respect of the Scheme to its policyholders.
- 5.152 For the avoidance of doubt, the circumstances under which exceptional costs may be attributed to the Liver Fund and Liver Ireland Sub-Fund policies would be unchanged from those allowed by the IoT, although, as set out in paragraph 5.126, these circumstances would be set out in a cut-down revised IoT.

### Miscellaneous

#### PROFITSHARE

- 5.153 RLMIS does not generally allocate ProfitShare (as defined in paragraph 3.123 above) to investments in its closed funds as these investments are generally not entitled to distributions of the RL Open Fund Estate. RLMIS considers that the holders of the with-profits policies in the Liver Fund do not have any reasonable expectation of a distribution of ProfitShare as they benefit from distributions of the Liver Fund Estate and do not currently have the option to transfer benefits into the RL Open Fund in order to start receiving ProfitShare. Furthermore, distributing ProfitShare to Liver Fund policyholders would dilute the level of ProfitShare received by the holders of existing with-profits investments in the RL Open Fund. Based on these considerations, RLMIS does not currently expect to distribute ProfitShare to any Liver Fund policies after the Liver Fund Consolidation has been implemented.

#### MEMBERSHIP OF RLMIS

- 5.154 Membership of RLMIS is only available to specific policies written by and remaining with RLMIS, as defined in RLMIS's Articles of Association. None of the policies invested in the Liver Fund or the Liver Ireland Sub-Fund prior to the implementation of the IoT was written by RLMIS. Therefore, none of the policies invested in the Liver Fund or the Liver Ireland Sub-Fund confers membership of RLMIS on the holders of those policies. That position is not affected by the Schemes or the consolidation of the Liver Fund into the RL Open Fund.

## MODIFICATION OR ADDITIONS

- 5.155 RLMIS may consent (for and on behalf of itself and all other persons concerned, other than the relevant UK regulatory authorities) to any modification of or addition to the UK Scheme or to any further condition or provision affecting the UK Scheme which, prior to the sanction of the UK Scheme, the English High Court may approve or impose (without prejudice to the position which the relevant UK regulatory authorities may take in relation to any such modification or addition).
- 5.156 The consent of the English High Court shall not be required in relation to minor and/or technical amendments to the terms of the UK Scheme (including amendments to correct manifest errors), which may be approved by the RLMIS Board having regard to advice from the RLMIS WPA, provided that the relevant UK regulatory authorities have been notified of the terms of the amendment(s) at least 60 days in advance and have not objected (or have confirmed their non-objection sooner).
- 5.157 RLI DAC may consent (for and on behalf of itself and all other persons concerned, other than the CBI) to any modification of or addition to the Liver Ireland Scheme or to any further condition or provision affecting the Liver Ireland Scheme which, prior to the sanction of the Liver Ireland Scheme, the Irish High Court may approve or impose (without prejudice to the position which the CBI may take in relation to any such modification or addition).
- 5.158 The consent of the Irish High Court shall not be required in relation to minor and/or technical amendments to the terms of the Liver Ireland Scheme (including amendments to correct manifest errors), which may be approved by the RLI DAC Board having regard to advice from the RLI DAC HoAF, provided that the CBI has been notified of the terms of the amendment(s) at least 60 days in advance and has not objected (or has confirmed its non-objection sooner).

## IMPACT ON DOCUMENTATION

- 5.159 The consolidation of the Liver Fund into the RL Open Fund will mean that a number of the existing structures will need to be amended. These include:
- The LRA, which will need to be amended to reflect that the Liver Fund will cease to exist, and that, as the Liver Fund Estate has been distributed, the cancellation terms of the reinsurance will need to be refined. The associated collateral and fixed and floating charge documentation will also need to be updated.
  - The RLI DAC Transfer Scheme.
  - The IoT.
  - The RL Long Term Fund PPFM and the Royal Liver PPFM.
  - The Liver Ireland Sub-Fund WPOP.
  - Pension Scheme Guarantees.

## UNCLAIMED RESERVES AND DORMANT ACCOUNTS

- 5.160 For the purposes of its best-estimate valuation of liabilities, RLMIS makes assumptions about policies that are not expected to be claimed by policyholders. This reduces the BEL held in the Liver Fund in respect of its policies, allowing this additional surplus to be distributed back to other policyholders in the Liver Fund (and the Liver Ireland Sub-Fund) rather than being held back and then possibly never claimed. Holders of policies deemed to be “unclaimed” (or their beneficiaries) do not lose their right to make a claim under their policy.
- 5.161 In Ireland, policies that are deemed “dormant policies” (in accordance with the provisions of the Unclaimed Life Assurance Policies Act 2003), and the assets backing those policies, are transferred to the Dormant Accounts Fund (“DAF”), which is managed by the National Treasury Management Agency. However, the holders of these policies (or their beneficiaries) can return to claim these funds at any time. To date, some 21,000 Ireland Eligible Policies have been transferred to the DAF.
- 5.162 Unclaimed and dormant policies which meet the criteria to be classified as Ireland Eligible Policies will receive the Offer Uplift if the Liver Ireland Scheme goes ahead. If a dormant policy subsequently claims from RLI DAC, then RLI DAC will request a refund of the amount previously paid to the DAF. If the amount had been transferred to the DAF after 31 December 2022, then it will have been increased for the Offer Uplift. If, however, the amount was transferred prior to that date, then there would be a shortfall between the claim amount (which would include the Offer Uplift) and the funds received back from the DAF (which would not). The RL Open Fund, through the LRA, is taking on the risk of meeting this shortfall in cases where policies transferred to the DAF prior to end-2022 but subsequently make a claim after that date. Based on past experience and the total amount transferred to the DAF to date, RLI DAC expects this risk to be minimal (less than €100,000 p.a.).

- 5.163 The assumptions that have been made in the calculation of the BEL in relation to unclaimed and dormant policies are set out and discussed in section 10.

**Summary: Impact on RLI DAC**

- 5.164 RLI DAC is to enter into a compromise with the Ireland Eligible Policyholders through the Liver Ireland Scheme to be sanctioned by the Irish High Court (subject to the vote). This will take effect if both the Irish and UK Schemes are sanctioned.
- 5.165 The proposals with respect to RLI DAC in relation to the Liver Ireland Business may be summarised as follows:
- The Liver Ireland Sub-Fund will be retained.
  - The Liver Ireland Business would continue to be fully reinsured to RLMIS, with the cover provided by the RL Open Fund rather than the Liver Fund. The reinsurance would continue to support the capital requirements of the Liver Ireland Sub-Fund in line with the internal capital management framework.
  - The reinsurance would continue to be supported by collateral, provided by the RL Open Fund.
  - RLI DAC will make an offer to eligible Liver Ireland Business policyholders whereby, in return for agreeing to the payment of a Scheme Contribution to the RL Open Fund, they would receive an immediate one-off percentage increase to their benefits.
  - The eligible Liver Ireland Business policies would benefit from the distribution of the Liver Fund Estate in the same way as the eligible UK Liver policyholders (in keeping with the principle of both being treated the same).
  - There would be no change to the bonus setting arrangements currently in operation (although there would be no further estate distributions).
  - The Liver Ireland Business IB business would be moved to a new more modern administration system. (The benefits of moving the OB business, both UK and Irish, is still being considered.)

## 6 THE PROCESS AND TIMETABLE FOR THE PROPOSED SCHEMES

### Overview

- 6.1 In order to implement the Schemes, the Scheme Implementation Conditions (set out in section 5) must be met and the steps undertaken to meet these have been, and will be, as set out in Table 10.

**Table 10: Overview of timetable and process for implementation of the Schemes**

The Appetite Mailing	RLMIS and RLI DAC sent the Appetite Mailing to Eligible Policyholders for whom a validated address was held over a six-week period commencing 14 February 2022. The Appetite Mailing feedback window closed on 29 April 2022.
Determination of Eligible Policies	RLMIS and RLI DAC determined the set of Eligible Policies based on policies that were in-force on 31 March 2022 (the “ <b>Eligibility Date</b> ”) using the criteria set out in Section 5.
Calculation of the Offer Uplift	The Offer Uplift quoted in the Voting Packs was calculated based on the financial position of the Liver Fund as at 31 March 2022. This Offer Uplift percentage is fixed until the Implementation Date of the Scheme, which is expected to be 31 December 2022.
The Convening Hearings	The “ <b>Convening Hearing</b> ” for the Liver Ireland Scheme will take place on 21 June 2022 and this Report will be submitted to the Irish High Court for that hearing. The Convening Hearing for the Liver UK Scheme will take place on 28 and 29 June 2022.
The Policyholder Votes	The Voting Pack will be sent to Eligible Policyholders over a six-week period commencing 17 August 2022. Eligible Policyholders will be able to register their votes on the Scheme by post until midday on 11 November 2022. If RLMIS or RLI DAC has not received an Eligible Policyholder’s vote within four weeks of mailing their Voting Pack, a “ <b>Reminder Mailing</b> ” will be sent to the policyholder.
The Scheme Meetings	The Ireland Scheme Meeting will be held on 1 November 2022 for the Liver Ireland Scheme. A separate UK Scheme Meeting will be held on 15 November 2022) for the UK Scheme. The results of the policyholder votes at the Scheme Meetings constitute the first of the Scheme Implementation Conditions set out in section 5.
The reviews of the Independent Experts	In advance of the Sanction Hearing, I will undertake a final review of the Ireland Offer and write to RLI DAC to give my view on whether the Ireland Offer continues to satisfy the Fairness Tests set out in Section 8 of this Report. The UK Independent Expert will undertake a similar review in respect of the UK Offer.
The Sanction Hearings	The Sanction Hearing for the Liver Ireland Scheme will take place on 29 November 2022 and I will submit a supplementary report to the Irish High Court for that hearing. The Sanction Hearing for the UK Scheme will take place on 5 and 6 December 2022). The UK Independent Expert will submit a supplementary report to the English High Court for that hearing. The Schemes are co-dependent i.e. both the UK Scheme and the Liver Ireland Scheme must be sanctioned in order for both Schemes to progress. The sanction of the Schemes constitutes the second of the Scheme Implementation Conditions set out in section 5.
The Implementation Date	If the Scheme Implementation Conditions are all met, then the Implementation Date of the Schemes is expected to be 31 December 2022 but this can be delayed by RLMIS to no later than 31 March 2023. The two Schemes are expected to be implemented on the same date. The Confirmation Mailing (see paragraph 7.2) would be sent to all Liver Fund and Liver Ireland Sub-Fund policyholders (Included and Excluded) following the Implementation Date, with the wording amended as necessary for each sub-group.

- 6.2 Each of these procedural steps, from the Convening Hearings onwards, is explained in more detail below.

## The Convening Hearings

- 6.3 The main purpose of the Convening Hearings is to ask the respective courts to convene the respective Scheme Meetings. There will be a Convening Hearing in the English High Court to convene the meeting for the UK Scheme. A separate Convening Hearing will be held in the Irish High Court to convene the meeting for the Liver Ireland Scheme.
- 6.4 In considering whether to grant an order convening each Scheme Meeting, the relevant court will consider whether more than one meeting of creditors is required and, if so, the appropriate composition of the meetings.
- 6.5 Since, in respect of each Scheme, RLMIS and RLI DAC propose that the Eligible Policyholders should vote together as a single class at a single meeting in relation to that Scheme (see Voting Classes below), the respective courts would need to be satisfied that this is appropriate, having regard to the rights which the Eligible Policyholders have and the effect of the Offer on those rights. The respective courts would take into account any representations that policyholders may make, particularly in relation to the proposal that there should be a single class and a single Scheme Meeting for each of the Schemes (UK and Ireland).
- 6.6 The respective courts will also consider and be asked to approve the proposed voting arrangements and the approach to determining the result of the relevant policyholder vote.

## The Policyholder Votes

### INTRODUCTION

- 6.7 RLMIS and RLI DAC will communicate the Offer to each Eligible Policyholder in the Voting Pack. In this pack, there will be a decision form to be completed by the policyholder and returned by post. Alternatively, the policyholder may vote on the Offer online, or the policyholder or their nominated proxy may cast their vote in person at the Scheme Meeting (see below).
- 6.8 The voting options available to the Eligible Policyholder will be:
- Vote in favour of the Offer; or,
  - Vote against the Offer.
- 6.9 While eligibility for the Offer was determined at the Eligibility Date for the purpose of receiving a Voting Pack, in order for an Eligible Policyholder to be eligible to cast a vote on the relevant scheme, they must continue to meet the eligibility criteria set out in section 5 at the date of the relevant Scheme Meeting.

### VOTING CLASSES

- 6.10 The subdivision of Eligible Policyholders into different "**Voting Classes**" must be such that the Eligible Policyholders in each Voting Class are not so dissimilar as to make it impossible for them to consult together and to form a common view on account of their common interest.
- 6.11 The external legal advisers of RLMIS and RLI DAC have carried out a due diligence exercise on the policies of the Liver Fund and the Liver Ireland Sub-Fund. This included consideration of the terms and conditions of Eligible Policies, as well as the legal rights of the Eligible Policyholders. One of the primary purposes of this due diligence was to identify any class tensions that might suggest that the Eligible Policyholders should be subdivided into more than one Voting Class.
- 6.12 Following this due diligence exercise, RLMIS has elected to constitute the UK Scheme with a single Voting Class, noting that HITM policies will not be part of the Scheme.
- 6.13 Similar due diligence has been carried on the Eligible Policies in respect of the Liver Ireland Scheme. Following this, RLI DAC has elected to constitute the Liver Ireland Scheme with a single Voting Class, noting that HITM policies will not be part of the Scheme.
- 6.14 In reaching this conclusion RLI DAC has had regard to advice from its external legal advisers, who have conducted an analysis of the Scheme and concluded that the only areas that may give rise to class or fairness tensions under the UK Scheme proposals relate to the outstanding terms of the policies.
- 6.15 The key issues are:
- The holders of policies with short remaining terms are projected to receive a higher distribution of the Liver Fund Estate under the Scheme than they would have received in the absence of the Scheme, with the opposite being

true for holders of policies with long remaining terms, noting that there is significant uncertainty around distributions and pay-outs in the future in the absence of the Scheme.

- In mitigation of this, the external legal advisers have highlighted the importance of ensuring that all relevant fairness considerations are addressed in communications to policyholders and the respective courts.
- There are differences in the certainty provided by the Scheme for the with-profits policies and the CB policies. However, these differences are due to the nature of these policies and their existing rights to distributions from the Liver Fund Estate, and not as a result of any element of the design of the Scheme.

6.16 I cover these issues in detail in section 13 (the Policyholder Vote Test).

#### OFFER ACCEPTANCE THRESHOLDS

6.17 There are two thresholds (the "**Offer Acceptance Thresholds**") set out in respective Companies Acts (Part 26 of the Companies Act 2006 in the UK and Part 9 of the Companies Act 2014 in Ireland). The Offer Acceptance Thresholds are the same in both countries.

6.18 Both of the Offer Acceptance Thresholds have to be met by the result of the vote before RLMIS or RLI DAC may seek the sanction of the Scheme from the respective High Courts.

6.19 The Offer Acceptance Thresholds, which would need to be met are:

- **Threshold 1:** More than 50% of the Eligible Policyholders who vote on the Offer must vote in favour of the Offer; and
- **Threshold 2:** Those Eligible Policyholders who vote in favour of the Offer must represent at least 75% in value (see below) of those voting.

#### THE VOTE VALUE

6.20 For a given Eligible Policyholder, a weighting will be attached to the policyholder's vote (the "**Vote Value**") used in assessing the vote result against Threshold 2. This Vote Value is proposed to be:

- The sum of the amounts payable on a claim under all of the policyholder's Eligible Policies at the Calculation Date; plus
- The sum of future premiums on all of the policyholder's with-profits Eligible Policies as at the Calculation Date until their contractual end point for premiums. The contractual end point is identified as the point at which the policy becomes fully free-paid (if the policy is a whole of life policy), matures (if the policy is an endowment policy), or at which the policyholder will reach the retirement date on the policy (if the policy is a pension policy).

6.21 The amount payable on a claim is defined to be the following as at the Calculation Date:

- For pension policies, the transfer value of the policy;
- For endowment policies, the cash-in value of the policy; and
- For other life policies, the death value of the policy.

#### RESULT OF THE POLICYHOLDER VOTES

6.22 If the result of the policyholder vote meets the Offer Acceptance Thresholds, then all Eligible Policyholders will be bound by the decision of the relevant High Court in relation to each respective Scheme. For the avoidance of doubt this would include:

- Any Eligible Policyholders who voted against the Offer;
- Any Eligible Policyholders who did not respond to the Offer; and
- Any Eligible Policyholders that are uncontactable (Gone-Aways).

6.23 If the necessary conditions were not to hold then RLMIS or RLI DAC, as applicable, would not proceed with the Scheme and all Eligible Policies would be unchanged and the Liver Fund would not be consolidated into the RL Open Fund.



- 6.24 Whilst the court will consider the fairness of the Scheme more widely, the Offer Acceptance Thresholds are the only requirements set out in legislation that the result of the vote itself needs to meet in order that RLMIS and RLI DAC can seek the sanction of the respective High Courts.
- 6.25 However, even in the event that the Offer Acceptance Thresholds are met, both RLMIS and RLI DAC will consider all aspects of the result of the vote carefully before deciding whether to proceed to the Sanction Hearings (see below).
- 6.26 It is important to note that, whilst the meeting of the Offer Acceptance Thresholds is a necessary condition for the Scheme to proceed, it is also necessary for the Scheme to be sanctioned by the respective High Courts.
- 6.27 If the Offer Acceptance Thresholds for the Liver Ireland Scheme were not met and those for the UK Scheme were met, the UK Scheme would not progress to its Sanction Hearing due to the co-dependence of the Schemes. Similarly, if the Offer Acceptance Thresholds for the UK Scheme were not met, but those for the Liver Ireland Scheme were, the Liver Ireland Scheme would not progress to its Sanction Hearing.

### The Scheme Meetings

- 6.28 At the Scheme Meetings (one for the UK Scheme and one for the Liver Ireland Scheme), Eligible Policyholders can discuss the Scheme with members of the RLMIS or RLI DAC management teams (as applicable) and formally cast their votes.
- 6.29 Eligible Policyholders who had chosen to vote by post or online would be counted as having voted by proxy as the Chair of the Scheme Meeting would formally vote on their behalf at the Scheme Meeting unless they were to appoint another person to act as their proxy.
- 6.30 Eligible Policyholders who vote by post or online would not need to attend the Scheme Meeting. However, where policyholders do vote in person or by proxy at the Scheme Meeting, this decision would be counted, and any other votes submitted would be ignored.
- 6.31 I would also attend the Scheme Meeting for the Liver Ireland Scheme and be available to take questions from policyholders. The UK Independent Expert would attend the Scheme Meeting for the UK Scheme.

### The Sanction Hearings

- 6.32 For each Scheme, the sanctioning of the proposed Scheme by the relevant High Court at the relevant Sanction Hearing is a Scheme Implementation Condition as set out in section 5. For each Scheme, if the Offer were to be approved at the relevant Scheme Meeting, the Sanction Hearings for the Liver Ireland Scheme would be expected to take place on 23 November 2022 and the Sanction Hearings for the UK Scheme would be expected to take place on 5 and 6 December 2022.
- 6.33 At the respective Sanction Hearings, the relevant High Court would be asked to make an order approving the Scheme. In considering whether to make such an order, the court will consider four key matters:
- Whether the relevant Companies Act requirements (Part 26 of the Companies Act 2006 in the UK and Part 9 of the Companies Act 2014 in Ireland) have been complied with, including whether the Scheme was approved at the relevant Scheme Meeting by the necessary majorities.
  - Whether the Eligible Policyholders were fairly represented by those who attended the Scheme Meeting (in person or by proxy) and that the statutory majority of policyholders in favour of the Scheme are acting bona fide and not coercing the minority in order to promote interests adverse to those of Eligible Policyholders as a whole.
  - Whether an intelligent and honest person who was an Eligible Policyholder and was acting in his own interest might reasonably approve the Scheme.
  - Whether there is a "blot" on the Scheme, that is, some technical or legal defect that means, for example, that it does not work according to its own terms, or that it would infringe some mandatory provision of law.
- 6.34 In coming to its decision, the court will consider the overall fairness of the Offer and whether it is appropriate for Eligible Policyholders who are uncontactable or decide for any reason not to respond to the Offer to be bound by the decision of the majority. This is likely to involve consideration of whether there are good reasons for the Offer to be made using a scheme of arrangement, and also consideration of matters such as the way in which the Offer has been communicated to policyholders. The court will also consider any benefit to RLMIS and RLI DAC. I consider a number of matters relevant to these wider fairness considerations in sections 9 to 15 of this Report.
- 6.35 Due to the co-dependence of the UK Scheme and the Liver Ireland Scheme both schemes need to be sanctioned in order to meet the necessary conditions for implementation.



### The Implementation Date

- 6.36 The Implementation Date for the UK Scheme is expected to be 31 December 2022, but this can be delayed by RLMIS to no later than 31 March 2023. This is the date on which, provided that both courts have sanctioned the Scheme:
- The Offer Uplift of 23.1% would be applied to the asset shares of Included Policies; and
  - The Liver Fund would be consolidated into the RL Open Fund.
- 6.37 The Liver Ireland Scheme is expected to be implemented on the same date. After this date, the Liver Ireland Sub-Fund would remain as a separate ring-fenced fund of RLI DAC and the LRA would remain in place between RLI DAC and RLMIS. However, internally to RLMIS, the required collateral under the LRA would be provided by the RL Open Fund (as the Liver Fund would no longer exist).

## 7 COMMUNICATIONS

### Communications strategy

- 7.1 RLMIS and RLI DAC have produced a detailed communications strategy for the Schemes that seeks to ensure all Eligible Policyholders are adequately informed of the nature and likely effect of the proposed Schemes. The communications strategy also addresses issues such as vulnerable customers, provision of helplines, and advice and guidance for policyholders. In this section, I summarise the companies' communications strategy and in section 12, I set out my assessment of the communication arrangements.

### COMMUNICATION WITH LIVER FUND AND LIVER IRELAND SUB-FUND POLICYHOLDERS

- 7.2 For the Liver Ireland Sub-Fund, the communications strategy involves issuing four customer mailings to Ireland Eligible Policyholders in relation to the Liver Ireland Scheme.
- A notification pack about the Scheme, which RLI DAC sent to Ireland Eligible Policyholders for whom a validated address was held over a seven-week period commencing 14 February 2022. This pack comprised a covering letter, a booklet providing a high-level guide to the proposed Scheme, a leaflet providing a reminder about how with-profits policies work, a feedback form, and a reply envelope with pre-paid postage.
  - Assuming the Irish High Court grants the necessary permission at the Convening Hearing, RLI DAC will proceed with the Scheme and send the "**Voting Pack**" to Ireland Eligible Policyholders, asking them to vote on the proposed Scheme. The Voting Pack comprises a covering letter, an Explanatory Booklet (split into two parts), a brief summary of this Report, a personalised illustration, a voting form and a reply envelope with pre-paid postage. The Voting Pack also satisfies the requirement to notify the Liver Ireland policyholders of changes to the principles of the Liver Ireland Sub-Fund WPOP used to manage their policies.
  - To promote customer engagement with the Voting Pack and in particular to encourage Ireland Eligible Policyholders to vote on the Scheme, a Reminder Mailing (either a postcard or brief letter referring to the Voting Pack) will be issued during the voting period to an Eligible Policyholder if RLI DAC has not received their vote within four weeks of mailing their Voting Pack.
  - Finally, assuming the required voting thresholds are passed, the Irish High Court sanctions the Scheme at the Sanction Hearing and the Scheme is implemented, RLI DAC will send a letter to the Ireland Included Policyholders shortly after the Implementation Date confirming that the Offer Uplift has been applied to their Ireland Included Policies (the "**Confirmation Mailing**").
- 7.3 I note RLMIS expects to take a similar approach with respect to the Liver UK Scheme. The Voting Pack for the UK Eligible Policyholders includes an explanation of the changes to the principles of the Royal Liver PPFM used to manage their policies and confirms that, from the Implementation Date, their policies will be covered by the RL Long Term Fund PPFM.
- 7.4 Holders of HITM policies will receive a letter after the Implementation Date confirming that their policies' asset shares have been uplifted, along with an explanation that the uplift isn't expected to change their claim value, and confirming that their policies' terms and conditions have not been affected. In addition, holders of UK HITM policies will be informed that their policies have been transferred to the RL Open Fund.

### COMMUNICATION WITH RL OPEN FUND POLICYHOLDERS

- 7.5 RLMIS proposes to notify policyholders in the RL Open Fund of the Legacy Simplification Project (including the proposed fund consolidation activity under the Scheme) in the with-profits annual update statements issued throughout 2022. This will provide advance notice of the proposed changes and the impacts from the wider Legacy Simplification Project in a cost-effective way. For any of these policyholders who do not currently receive regular annual statements, RLMIS intends to issue a brief one-off mailing to notify these policyholders of the Legacy Simplification Project using the same messaging provided in the with-profits annual update statements.

### 'Gone-away' policyholders and unclaimed policies

- 7.6 RLMIS has gone to extensive lengths to minimise the number of Eligible Policyholders that it cannot communicate with i.e., policyholders from whom RLMIS or RLI DAC has had written correspondence returned undelivered. Such policyholders are referred to as "**Gone-Aways**".
- 7.7 In the UK, RLMIS established a centralised process in 2015 with the aim of conducting at least one tracing attempt for every known Gone-Away originally sold in the UK.

- 7.8 However, the same tracing infrastructure does not exist in Ireland as there are no major tracing companies in operation and a postcode system was introduced only relatively recently. Therefore, RLI DAC has not been able to carry out the same tracing as in the UK, either as part of business-as-usual processes or in advance of proposing the Liver Ireland Scheme.
- 7.9 As part of the Communication Strategy for the Schemes, RLMIS and RLI DAC published a significant number of legal notices in newspapers in both the UK and Ireland, to increase the likelihood of Gone-Aways being made aware of the Schemes. RLI DAC has also undertaken some targeted advertising in Ireland where the tracing infrastructure is unavailable, including advertising in local newspapers in regions where a material proportion of the mailing population reside.
- 7.10 Overall, there are 14,000 Eligible Policyholders in the Liver Ireland Sub-Fund that are classed as Gone-Away, as well as a further 1,800 Eligible Policyholders for whom RLI DAC either has no or an incomplete address.
- 7.11 Separately to this, although with some overlap in the groups, 21,000 Eligible Policies have been transferred to the DAF. Of these policies, around 4,400 belong to policyholders marked as Gone-Away and so the holders of the remaining policies would be mailed to inform them of the Scheme.
- 7.12 Any Gone-Away policyholders that are identified and re-engaged during the feedback or voting windows for the Schemes would be provided with a Voting Pack.
- 7.13 Any policies that are classified as “unclaimed” for the purposes of the best-estimate valuation of liabilities (as set out in section 5) would still be Eligible Policies if they meet the criteria for eligibility for the Offer. This includes policies in the Liver Ireland Sub-Fund that have transferred to the DAF.

#### Holders of pensions policies with selected retirement dates prior to 31 December 2022

- 7.14 Any pension policies with a selected retirement date (“SRD”) before 31 December 2022 (the expected Implementation Date of the Schemes) are not eligible for the Offer.
- 7.15 However, holders of pensions policies have the option to defer their SRD, and this typically occurs when RLMIS or RLI DAC send their usual ‘wake up’ packs to policyholders six months before their SRD (and again six weeks before SRD if they did not respond to the first pack). SRD would be deferred if the policyholder either actively requests this (SRD is moved to a new date chosen by the policyholder), or if the policyholder does not respond to the ‘wake up’ pack (SRD is automatically moved on by one year).
- 7.16 Therefore, it is expected that some pensions policies that were not Eligible Policies at the Calculation Date (31 March 2022), due to their SRD being before 31 December 2022, will become Eligible Policies as the holders of these policies defer their SRD following business-as-usual communications.
- 7.17 RLMIS and RLI DAC intend to contact holders of pensions policies with SRDs between 31 March 2022 and 31 December 2022 to inform them that, if they were to defer their SRDs to beyond 31 December 2022, they would benefit from the Offer under the Schemes. However, RLMIS and RLI DAC would not provide formal advice to these policyholders as to whether deferring their SRD to benefit from the Offer is appropriate for their broader retirement plans and personal circumstances.

#### Access to full documentation and reports

- 7.18 For the Liver Ireland Sub-Fund, a full copy of the Liver Ireland Scheme, this Report, the RLI DAC HoAF’s report, all as submitted to the Irish Court, as well as the updated Liver Ireland Sub-Fund WPOP, will be available online (on RLI DAC’s website) or on request (in writing or by telephone), as will the corresponding supplementary reports from me as Independent Expert and the RLI DAC HoAF in due course.
- 7.19 Similarly for the Liver Fund, a full copy of the UK Scheme, the UK IE’s report, the RLMIS Chief Actuary’s report and the RLMIS WPA’s Report, all as submitted to the English Court, as well as the revised RL Long Term Fund PPFM that describes the management of the with-profits business in the enlarged RL Open Fund, will be available online (on RLMIS’s website) or on request (in writing or by telephone) as will the corresponding supplementary reports from the UK Independent Expert, RLMIS Chief Actuary and RLMIS WPA in due course.

## 8 APPROACH TO ASSESSING THE PROPOSED SCHEME

### Introduction

- 8.1 In this section I explain the approach I have adopted in assessing the impact of the proposed Liver Ireland Scheme on the policyholders of RLI DAC.

### Role of the Independent Expert

- 8.2 My role as Independent Expert is to consider the proposed Liver Ireland Scheme and its effects on the policyholders of RLI DAC, and whether it meets the overall requirement of being fair and reasonable to those policyholders.
- 8.3 The role of Independent Expert is not prescribed (or required) by law or regulation. However, I have approached the role in a similar manner to that of the Independent Actuary as set out in the 1909 Act, and accordingly I have proceeded on the basis of an obligation to assist the Irish High Court in its deliberations.

### Context of assessment

- 8.4 My assessment is conducted within the context of the proposed Liver Ireland Scheme, and only the proposed Liver Ireland Scheme, and considers its likely effects on the RLI DAC policyholders. It is not within my remit to consider possible alternative schemes or to form a view as to whether this is the best possible scheme. Due to the linkages and co-dependency between the Liver Ireland Scheme and the UK Scheme, it is sometimes necessary for me to consider aspects of the UK Scheme in the course of my assessing the Liver Ireland Scheme.
- 8.5 My assessment of the impact of the implementation of the proposed Liver Ireland Scheme on the various affected policies is ultimately a matter of expert 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.
- 8.6 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 Irish High Court should reject a scheme as the positive effects may outweigh the negative effects or the negative effects may be very small.
- 8.7 In order to acknowledge this inherent uncertainty, and to be consistent with normal practice in these matters, I have framed my conclusions using a materiality threshold. If the potential issue 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 I do not consider it to have a material effect on the policies. The assessment of materiality will also consider 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' benefits is likely to be lower than the materiality threshold for a change that does not have a direct financial impact.

### Principles of assessment

- 8.8 In assessing the impact of the implementation of the Liver Ireland Scheme on the policyholders of RLI DAC, and whether those policyholders are being treated fairly and reasonably as a result of the implementation of the Liver Ireland Scheme, I have considered the extent to which the Scheme meets a series of tests. These tests – which I have termed “Fairness Tests” – are not prescribed in law or regulation, and, in selecting what I consider to be appropriate fairness tests in this case, I have had regard to examples of such tests from other similar Independent Experts' reports.
- 8.9 I have applied each of the Fairness Tests separately (as appropriate) for the following groups of policyholders:
- Ireland Included Policyholders who would remain as policyholders of the Liver Ireland Sub-Fund if the Liver Ireland Scheme were implemented;
  - Policyholders of the Liver Ireland Sub-Fund who would not be Ireland Included Policyholders, for example holders of Ireland HITM policies, non-profit policies (except CB policies) and unit-linked policies. For the avoidance of doubt, as holders of HITM policies would receive the Offer Uplift (although outside of the Liver Ireland Scheme), where I consider the impact of the Offer Uplift to Ireland Included Policies, my consideration would also be applicable to Ireland HITM policies unless otherwise stated; and,
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.

- 8.10 For the avoidance of doubt, I have not considered the RLMIS policyholders in this Report. Those policyholders will be considered by the RLMIS Chief Actuary, the RLMIS With-Profits Actuary, and the UK Independent Expert as part of the UK Scheme.
- 8.11 The Fairness Tests I have investigated are as follows:

**Table 11: Brief description of the Fairness Tests**

Test No.	Test name	Description
1	Security of policyholders' benefits	<p>This test considers the effect that the implementation of the Liver Ireland Scheme would have on the security of policyholders' guaranteed benefits under their policies with RLI DAC.</p> <p>In order for the proposed Liver Ireland Scheme to pass this test, I would need to be satisfied that the implementation of the Liver Ireland Scheme would not lead to a material adverse effect on the security of the benefits of the RLI DAC policies.</p>
2	Policyholder outcomes	<p>This test considers whether the effects of the proposals are fair and reasonable in respect of outcomes for different groups of policyholders in RLI DAC, focusing on:</p> <ul style="list-style-type: none"> <li>Policyholders' reasonable benefit expectations; and</li> <li>The standards of servicing, administration, management, and governance experienced by the policyholders.</li> </ul> <p>Furthermore, this test involves consideration of the distribution of the effects of the proposed Liver Ireland Scheme on the different groups of policies in RLI DAC given the rights, interests, and expectations of the different groups of policies, as well as the risks and costs posed by the proposals.</p> <p>A key part of the consideration of the effect of the Liver Ireland Scheme on policyholders' reasonable benefit expectations is consideration of the fairness of the Offer Uplift that would be applied to the Ireland Included Policies if the Liver Ireland Scheme were to be implemented. This includes consideration of the fairness of the following:</p> <ul style="list-style-type: none"> <li>The Scheme Contribution; and</li> <li>The distribution of the Liver Fund Estate via the uniform Offer Uplift percentage to the asset share of each with-profits Included Policy and the claim amount of each non-profit CB Included Policy.</li> </ul> <p>This test also includes consideration of:</p> <ul style="list-style-type: none"> <li>The fairness of the allocation of the costs associated with the Scheme between the RLMIS Closed Funds (and so ultimately the allocation to the Liver Fund Estate that will affect the Offer Uplift available for the Ireland Included Policies); and</li> <li>Any amendments made to policy conditions as part of the Liver Ireland Scheme.</li> </ul> <p>In order for the proposed Liver Ireland Scheme to pass this test I would need to be able to conclude that the implementation of the Scheme would not lead to a material adverse effect on policyholder benefit expectations or on the standards of servicing, administration, management, and governance of the RLI DAC policies.</p>
3	Adverse scenarios	<p>This test considers whether my conclusions on the Security of Policyholders' Benefits Test and the Policyholder Outcomes Test would change under different circumstances and scenarios, and hence whether the proposals would remain fair and reasonable under a range of circumstances and scenarios.</p>
4	Policyholder communications	<p>This test considers whether the information provided to Ireland Eligible Policyholders in respect of the Liver Ireland Scheme is clear, concise, and of an appropriate level of detail, and has been provided in good time to allow them to assess the proposals and make an informed decision regarding the policyholder vote on the Liver Ireland Scheme.</p> <p>This test also includes consideration of:</p>

		<ul style="list-style-type: none"> <li>▪ The adequacy of the arrangements for supporting and guiding Ireland Eligible Policyholders through the process.</li> <li>▪ The communications with policyholders of RLI DAC who are not Ireland Eligible Policyholders.</li> </ul>
5	Policyholder vote	<p>This test considers the fairness of the various features of the policyholder vote on the Liver Ireland Scheme, which is required before the Scheme could be sanctioned by the Irish High Court and implemented. These considerations include:</p> <ul style="list-style-type: none"> <li>▪ The number of Voting Classes and the class composition;</li> <li>▪ The requirements for the proposals to be approved and</li> <li>▪ The approach to the calculation of the value given to each vote in the interpretation of the results of the vote.</li> </ul>
6	Fair conduct	<p>This test considers whether the conduct of RLI DAC in relation to the proposed Liver Ireland Scheme is fair and reasonable to all policyholders. This test includes consideration of factors such as:</p> <ul style="list-style-type: none"> <li>▪ The approach to eligibility for the Offer;</li> <li>▪ The approach to eligible investments and future contractual premiums (i.e. “carpetbagging”);</li> <li>▪ The treatment of Gone-Aways; and</li> <li>▪ The compulsion involved if the Scheme is sanctioned; in this case compulsion would apply to non-respondents and those who vote against the Offer.</li> </ul>

#### Items considered in the course of my assessment of the proposed Scheme

- 8.12 In assessing the proposed Scheme, I have had regard to:
- The reports of the Chief Actuary and the With-Profits Actuary of RLMIS on the impact of the implementation of the UK Scheme and the Liver Ireland Scheme.
  - The report of the HoAF of RLI DAC on the impact of the implementation of the Liver Ireland Scheme.
- 8.13 There are no documents or other information that I have requested and that have not been provided.
- 8.14 Appendix A contains a list of the main sources of information upon which I have relied.

#### Reliance on the work of others

##### RELIANCE ON LEGAL ADVICE

- 8.15 My Report has been prepared for the Irish High Court as part of the process of submission of the Liver Ireland Scheme to the Irish High Court. I am not an expert in legal matters and hold no qualifications in Irish law (insurance regulations or otherwise) and therefore I have relied on the conclusions of experts in Irish insurance law in relation to a number of areas.
- 8.16 In the absence of such a legal analysis, it would not be possible for me to provide conclusions on those aspects of the Liver Ireland Scheme that are outside of my expertise and that have an impact on the fairness of the Scheme.
- 8.17 I have received input and advice in legal matters from two sources:
- The external legal advisers of RLI DAC: Pinsent Masons; and
  - My own legal advisers: Freshfields.
- 8.18 The areas where I have relied, either wholly or partially, upon the advice and analysis provided to RLMIS by Pinsent Masons are:

- Advice given to RLI DAC in order to ensure that my understanding of the legal process, the Schemes, and the amendments to be made to the IoT, the RLI DAC Transfer Scheme and the LRA, as well as my description of their relevant features in this Report, is materially accurate; and
  - A review of the status of the provisions of the IoT following the operation of the Liver Sunset Clause and consolidation of the Liver Fund into the RL Open Fund.
- 8.19 It should be noted that Pinsent Masons has not been retained by me and has no liability to me or Milliman for any advice provided by Pinsent Masons to RLI DAC that has been made available to me in my assessment of the Scheme.
- 8.20 The areas where Freshfields has provided me or the UK Independent Expert with information and advice in relation to the Scheme are:
- A review of the advice provided to RLI DAC by Pinsent Masons on the proposed number of Voting Classes and the class composition for the Liver Ireland Scheme;
  - A review of the advice provided to RLI DAC by Pinsent Masons on whether the proposed Scheme could be considered to be a Reattribution of the Inherited Estate as set out in Chapter 20 of the FCA's COBS rules; and
  - A review of the legal due diligence report produced by Pinsent Masons in relation to the proposed Scheme.
- 8.21 I am content to rely upon the advice given to RLI DAC by Pinsent Masons and to me or the UK Independent Expert by Freshfields because:
- Both Pinsent Masons and Freshfields are large international legal firms with wide ranges of experience in Ireland insurance company transactions and it is my view that they have the relevant and appropriate qualifications and knowledge of the laws and regulations governing schemes of arrangement in Ireland; and
  - The nature of the information and advice provided by Pinsent Masons to RLI DAC upon which I have relied is mostly factual in nature and, in particular, concerns how a particular aspect of RLI DAC (pre or post the implementation of the Scheme) works in accordance with Irish law.

#### RELIANCE ON TAX ADVICE

- 8.22 RLMIS has conducted a review of the Scheme on behalf of RLI DAC to assess the effect of the Scheme on the Ireland tax liabilities of the Ireland Included Policyholders. I am satisfied that RLMIS's in-house tax team has the relevant expertise and that it is therefore reasonable for me to rely on their advice. The report produced by RLMIS's in-house tax team has been shared with me.
- 8.23 I am not an expert in tax matters and hold no qualifications in Ireland tax and therefore I have relied on the conclusions of RLMIS's in-house tax team and the external tax experts retained by RLMIS.
- 8.24 It should be noted that the external tax experts have not been retained by me and have no liability to me for any advice provided to RLMIS that has been made available to me in my assessment of the Scheme.

#### THE FINANCIAL INFORMATION IN THIS REPORT

- 8.25 The financial information used in the analysis of the effects of the Schemes is set out in Section 9. This includes:
- The current (i.e. before the implementation of the Scheme) Solvency II Pillar 1 balance sheet for the Liver Ireland Sub-Fund, the RLI DAC German Bond Sub-Fund and the RLI DAC Open Fund as at 31 March 2022;
  - The pro forma post-Scheme Solvency II Pillar 1 balance sheet for the Liver Ireland Sub-Fund, the RLI DAC German Bond Sub-Fund and the RLI DAC Open Fund as at 31 March 2022 assuming the Schemes had been implemented on that date;
  - The current (i.e. before the implementation of the Schemes) UK Solvency II balance sheet for the Liver Fund as at 31 March 2022;
  - The pro forma post-Scheme UK Solvency II balance sheet for RL Open Fund as at 31 March 2022 assuming the Schemes had been implemented on that date; and
  - The calculation of the Offer Uplift percentage, including the calculation of the CFC, the Premium Uplift Contribution, the Project Cost Allowance and the diversification benefits.
- 8.26 In Ireland and the UK, a firm's SCR can be calculated using:



- A Standard Formula, which is a methodology for calculating a firm's SCR prescribed by the European Insurance and Occupational Pensions Authority (and as currently adopted under the UK Solvency II framework); or
  - An Internal Model, which is subject to approval by the local regulator, in this case the CBI in Ireland and the PRA in the UK.
- 8.27 RLI DAC uses the Standard Formula to calculate its SCR, and so the Solvency II financial information presented in this Report for RLI DAC (including for the Liver Ireland Sub-Fund) is the Pillar 1 reported information on a Standard Formula basis.
- 8.28 The PRA granted approval for RLMIS to use its Internal Model (the RLMIS Internal Model) for Solvency II reporting in 2019 and so the Solvency II financial information presented in this Report for RLMIS (including for the Liver Fund and the RL Open Fund) is based on the RLMIS Internal Model.
- 8.29 In addition to the RLMIS Internal Model, RLMIS maintains an actuarial model which calculates the Solvency II technical provisions for regulatory reporting purposes (the "**RLMIS Cashflow Model**"). I refer to these collectively as the "**RLMIS Actuarial Systems**".
- 8.30 RLMIS uses the UK Solvency II Group reporting basis for its day-to-day management, and this is the basis on which it makes decisions in relation to the RL Open Fund and the RLMIS Closed Funds. Under the Group basis, the RL Open Fund's financial position is calculated on a "Pillar 1" basis, while the RLMIS Closed Funds' financial positions are calculated on a "Pillar 2" basis, as described in paragraph 3.114. I have therefore presented the financial information for RLMIS in this Report on a Group basis, and this is the basis to which I have had principal regard in reaching my conclusions on the Scheme.
- 8.31 As set out in Appendix C to this Report, the UK Government published a full consultation document on proposed UK reforms to Solvency II in April 2022. The proposed reforms include a substantial reduction in the Risk Margin and a change to the treatment of credit risk in the matching adjustment. Considering each of these proposed reforms:
  - The precise impact of the reduction in the Risk Margin on RLMIS's balance sheet is not yet known, but it would increase the Internal SCR Cover for RLMIS's funds. The effect of a reduction in the Risk Margin will be partially offset by a reduction in the TMTP.
  - RLMIS uses the matching adjustment in the RL Open Fund currently for certain non-profit pension annuity liabilities. While the precise impact of the proposed changes is not yet known, the impact would be the same whether the Schemes are implemented or not.
- 8.32 Therefore, I am satisfied that it is appropriate for the financial analysis presented and considered in this Report in respect of RLMIS to focus on the current UK Solvency II requirements.
- 8.33 Furthermore, the proposed reforms would not affect the amount of the Liver Fund Estate available for distribution (and so the Offer Uplift to be applied) under the Schemes, as the size of the Risk Margin does not affect the value of the Liver Fund Estate to be distributed and the matching adjustment is not used in the Liver Fund.
- 8.34 RLMIS was required to put in place strict governance and control processes to ensure that the RLMIS Internal Model would not be materially changed without adherence to the internal checking controls and that for major changes re-approval from the PRA would be required. RLMIS confirmed that it has adhered to these processes and controls.
- 8.35 Further background on the Solvency II (and UK Solvency II) regulatory regime, and the pillars on which it is based, is provided in Appendix C to this Report.
- 8.36 My Supplementary Report will contain more up to date financial information and will provide an update on the effect of the implementation of the Schemes based upon these figures and on any other material developments since the date of this Report.
- 8.37 I have placed reliance on the financial information provided to me. Please refer to paragraph 1.23 to 1.28 for more details.

#### CALCULATION OF THE OFFER UPLIFT PERCENTAGE

- 8.38 The Offer Uplift percentage has been calculated using a model (the "**RLMIS Tactical Model**") that has been built by RLMIS specifically for the Legacy Simplification Project and is separate from the RLMIS Actuarial Systems described in paragraph 8.29 above.
- 8.39 The Offer Uplift percentage that would be applied to Included Policies has been based on calculations as at 31 March 2022 carried out using the RLMIS Tactical Model. The RLMIS Tactical Model uses output from the RLMIS Actuarial Systems, with some adjustments (such as allowing for changes to the EBR in the RL Open Fund and allowing for the

Offer Uplift itself as this changes the cost of guarantees and consequently the value of the Liver Fund Estate available for distribution).

- 8.40 Given the timing of the uplift calculation and these necessary adjustments to the inputs, the output from the RLMIS Actuarial Systems used by the RLMIS Tactical Model to calculate the Offer Uplift was not externally audited. There is, however, a comprehensive framework of internal review and governance within RLMIS in relation to the inputs to the RLMIS Tactical Model.
- 8.41 The RLMIS Tactical Model has been developed, checked, and reviewed within the RLMIS project team as well as being reviewed by the RLMIS Risk Function. RLMIS has also produced a checking tool which shows that the results of the RLMIS Tactical Model behave as would be expected.
- 8.42 As additional assurance RLMIS engaged external actuarial consultants to provide a further review of both the calculations and the inputs to those calculations in the RLMIS Tactical Model. I have been provided with the output of this external review and I understand that no material concerns were raised in the review and that no material changes to the calculated Offer Uplift percentage were required. The UK Independent Expert has also carried out a high-level review of the RLMIS Tactical Model and its outputs and has not identified any material issues.
- 8.43 Given the level of external review and internal checking and governance to which the financial information and Offer Uplift calculations have been subject, I am satisfied that it is appropriate to rely upon the financial information and Offer Uplift calculations for the purpose of this Report.

#### Assumptions made when assessing the proposed Scheme

- 8.44 When considering the implications of the proposed Scheme, I need to make certain assumptions about how RLMIS and RLI DAC will run their respective businesses.
- 8.45 The assumptions I have made include:
- An assumption that the LRA will remain in place post-Scheme.
  - An assumption that the PLAL Fund will be consolidated into the RL Open Fund on 31 December 2022.
- 8.46 My assumptions are based on my understanding of the issues in question and have been shared with the two companies' respective senior management teams for confirmation. I believe, therefore, that it is reasonable to make the assumptions I have made when assessing the implications of the proposed Scheme. My assessment of the proposed Scheme also includes an assessment of the position should neither of these assumptions prove correct.

#### Regulation and professional guidance

- 8.47 As noted above, there are no specific regulations or guidance governing the role of an independent expert appointed to report on the terms of a scheme of arrangement in Ireland. (Indeed, there is no requirement in law to appoint an independent expert in connection with a scheme of arrangement.)
- 8.48 I have, however, had regard to the regulations and guidance applicable to an Independent Actuary who has been appointed to report on the transfer of a portfolio of long-term insurance business under the 1909 Act. In particular, I have had regard to the provisions of ASP LA-6. I have also complied with the requirements of ASP LA-2 (which covers General Actuarial Practice).

## 9 TEST 1: SECURITY OF POLICYHOLDERS' BENEFITS

### Introduction

- 9.1 In this section, I set out my assessment of the proposed Schemes in so far as they may affect the security of policyholders' guaranteed benefits under their policies with RLI DAC.
- 9.2 I have considered this separately for the following groups of existing policyholders of RLI DAC:
- Ireland Included Policyholders, as well as policyholders of the Liver Ireland Sub-Fund who would not be Ireland Included Policyholders, who would all remain as policyholders of the Liver Ireland Sub-Fund if the Schemes were to be implemented; and
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.

### Effect of Schemes on security of guaranteed benefits – Liver Ireland Sub-Fund

#### INTRODUCTION

- 9.3 The policyholders of the Liver Ireland Sub-Fund comprise:
- Ireland Included Policyholders; and
  - Policyholders of the Liver Ireland Sub-Fund who would not be Ireland Included Policyholders, for example holders of HITM policies, non-profit policies (except CB policies) and unit-linked policies.
- 9.4 The implementation of the Schemes would have a different effect on these groups of policyholders and the policies they hold have guaranteed benefits that are different in nature. However, they will all remain as policyholders of the Liver Ireland Sub-Fund in RLI DAC following the implementation of the Schemes and their policies will continue to be covered by the LRA. Therefore, I have considered the security of their guaranteed benefits together in this sub-section.
- 9.5 Currently, the policyholders of the Liver Ireland Sub-Fund derive security for their guaranteed benefits from:
- The LRA between RLMIS and RLI DAC; and
  - The assets of RLI DAC.
- 9.6 I cover the impact of the Schemes on each of these in turn below.

#### THE LRA

- 9.7 At present, although the LRA is between RLMIS and RLI DAC, internally to RLMIS, the required capital and collateral is provided by the Liver Fund.
- 9.8 If the Schemes were to be implemented, the Liver Fund Estate would be distributed in full and the liabilities in respect of the reinsured Liver Ireland Sub-Fund business would be assumed by the RL Open Fund. The LRA would remain in place between RLMIS and RLI DAC but, internally to RLMIS, the required capital and collateral would be provided by the RL Open Fund instead.
- 9.9 Furthermore, the LRA cancellation terms currently specify that the Liver Ireland Sub-Fund policyholders would receive their share of the Liver Fund Estate should the LRA be terminated. However, as the Liver Fund Estate will be distributed in full at the point of consolidation, this will no longer be possible. The Liver Ireland Sub-Fund would, however, receive a rebate on the CFC that will be made in respect of the capital requirements that no longer need to be met from the RL Open Fund.
- 9.10 There would be no other material changes to the LRA, including the collateral framework and the floating and fixed charges, including the equalisation clause set out in Section 4.
- 9.11 In considering the relative security provided by the LRA pre- and post-Schemes, I have therefore considered the financial positions of the Liver Fund and the RL Open Fund below.
- 9.12 Table 12 below shows the pre-Schemes financial position of the Liver Fund, as well as the pro forma post-Schemes financial position of the RL Open Fund, on a UK Solvency II basis at 31 March 2022. The assets of the Liver Fund

pre-Schemes have been adjusted to allow for the release of a small portion of the Liver Fund Estate currently held by RLI DAC to cover the Liver Ireland Sub-Fund capital requirements.

**Table 12: Pre-Schemes and pro-forma post-Schemes financial position (UK Solvency II) as at 31 March 2022 of the relevant RLMIS funds (£ millions)**

	Liver Fund Pre-Schemes	RL Open Fund Post-Schemes
Assets (A)	1,987	91,492
Liabilities (B)	1,615	87,263
<b>Available capital before adjustments (C = A - B)</b>	<b>373</b>	<b>4,229</b>
Risk Margin (D)	62	1,172
TMTF (E)	67	975
Sub-debt (F)	-	1,446
<b>Internal Own Funds (G = C - D + E + F)</b>	<b>378</b>	<b>5,478</b>
Internal SCR (H)	216	2,619
Excess capital (G - H)	162	2,859
<b>Internal SCR Cover (G / H)</b>	<b>175%</b>	<b>209%</b>

Source: Information provided by RLMIS

9.13 Table 12 shows that, as at 31 March 2022:

- The Liver Fund had excess capital of £162 million and an Internal SCR Cover of 175%. This corresponds to Upper Amber (Sub-Optimal+) under the Liver Capital Framework, i.e. the Liver Fund was marginally above its target range.
- If the Schemes had been implemented as at that date, the RL Open Fund would have had excess capital of approximately £2.9 billion and an Internal SCR Cover of 209%. This is within the acceptable range under the RLMIS Capital Framework, and above the target, and so the RL Open Fund is expected to be sufficiently well capitalised following the implementation of the Schemes to support the required collateral under the LRA.

9.14 While the excess asset position of the RL Open Fund following the implementation of the Schemes is useful to understand, RLMIS is free to distribute assets in the RL Open Fund in excess of the buffer required by the RLMIS Capital Framework. Therefore, any excess assets should only be relied on for benefit security to the extent that those assets are required to meet the RLMIS Capital Framework.

9.15 As a result, the key considerations for benefit security are:

- The relative strength of the Liver Capital Framework and the RLMIS Capital Framework, and so whether the fund providing the required capital under the LRA is subject to a materially weaker capital framework than currently;
- The relative risk exposures between the Liver Fund currently and the RL Open Fund following the implementation of the Schemes.

9.16 The Liver Capital Framework and the RLMIS Capital Framework are similarly structured but there are some differences as the Liver Capital Framework is specified in the IoT. The key difference between the Liver Capital Framework and the RLMIS Capital Framework is:

- Under the Liver Capital Framework, any excess in the Liver Fund Estate above the 1-in-20-year capital target should be distributed through asset share enhancements to with-profits policies and increases to the claim amounts of CB policies. There would be no distributions from the Liver Fund Estate if the excess capital was below this capital target.
- Under the RLMIS Capital Framework, distributions of the estate (for the RL Open Fund, in the form of ProfitShare) can take place if the fund is in the Lower Amber range or above (i.e. above the 1-in-5-year level), and so distributions can be made at a lower level of Internal SCR Cover than under the Liver Capital Framework. Furthermore, estate distributions are accelerated when the fund is in the Upper Amber or Upper Red range (so above the 1-in-50-year level) but there is no requirement as under the Liver Capital Framework to distribute the entire excess above the 1-in-20-year level.

9.17 While distributions of the estate could continue to a lower (relative) level of excess capital in the RL Open Fund than would be allowed in the Liver Fund, I understand that in practice if the RL Open Fund's financial position was below

its target range, these distributions would be reduced or stopped in the RL Open Fund to bring the Internal SCR Cover back up to the target range. Furthermore, the middle of the target range under the RLMIS Capital Framework is the 1-in-20-year level, which is the same level as the capital target under the Liver Capital Framework.

- 9.18 I am therefore satisfied that the differences in the capital frameworks would not have a material adverse effect on the security of guaranteed benefits for the policyholders of the Liver Ireland Sub-Fund.
- 9.19 The RL Open Fund is a significantly larger fund than the Liver Fund and is exposed to a more diverse range of risks. However, the RL Open Fund holds capital in accordance with the RLMIS Capital Framework, which provides a buffer against the risks to which it is exposed. The Internal SCR and the capital buffer reflect both the quantum of the various risks and the level of diversification of risk that results from having a range of risks within the fund.
- 9.20 Therefore, while the policyholders of the Liver Ireland Sub-Fund would be exposed (indirectly through the LRA) to a different risk profile following the implementation of the Schemes, the capital held by the RL Open Fund would ensure that their guaranteed benefits were subject to a reasonable level of security through the LRA.
- 9.21 Furthermore, the required collateral under the LRA would become part of the assets of the RL Open Fund following the implementation of the Schemes, but would continue to be ring-fenced and available to meet claims arising on the policies of the Liver Ireland Sub-Fund.
- 9.22 Therefore, I am satisfied that the changes to the LRA as a result of the implementation of the Schemes would not have a material adverse effect on the security of the guaranteed benefits for the policyholders of the Liver Ireland Sub-Fund while the LRA remains in place. However, I must also consider the possibility of the LRA being terminated in the future and the impact that may have, which I have set out in paragraphs 9.30 to 9.42 below.

#### THE ASSETS OF RLI DAC

- 9.23 The assets of RLI DAC of relevance to the security of guaranteed benefits for the policyholders of the Liver Ireland Sub-Fund are:
- The assets held in the Liver Ireland Sub-Fund, including the reinsurance asset; and
  - The assets of the RLI DAC Open Fund that provide additional security through the capital support arrangements set out in the RLI DAC Transfer Scheme.
- 9.24 Table 13 below shows the pre-Schemes financial position of the Liver Ireland Sub-Fund, as well as the pro forma post-Schemes financial position of the Liver Ireland Sub-Fund, on a Solvency II Pillar 1 basis at 31 March 2022.

**Table 13: Pre-Schemes and pro-forma post-Schemes financial position (Solvency II Pillar 1) as at 31 March 2022 of the Liver Ireland Sub-Fund**

€million	Liver Ireland Sub-Fund	
	Pre-Schemes	Post-Schemes
Assets (A)	785	983
<i>Of which reinsurance asset</i>	721	917
Liabilities (B)	772	968
<b>Available capital before adjustments (C = A - B)</b>	<b>13</b>	<b>15</b>
Risk Margin (D)	2	2
<b>Own Funds (E = C - D)</b>	<b>11</b>	<b>13</b>
SCR (F)	7	8
Excess capital (E - F)	4	5
<b>SCR Cover (E / F)</b>	<b>164%</b>	<b>164%</b>

Source: Information provided by RLI DAC

- 9.25 Table 13 shows that, following the implementation of the Schemes:
- The liabilities of the Liver Ireland Sub-Fund would increase to reflect the uplifts applied to the Ireland Included Policies;
  - The SCR of the Liver Ireland Sub-Fund (and so the Risk Margin) would increase to reflect the increased liabilities of the fund; and

- The assets of the Liver Ireland Sub-Fund would be correspondingly increased through the LRA with RLMIS such that the Liver Ireland Sub-Fund would continue to cover the Counterparty Default Adjustment<sup>4</sup> in respect of the Liver Ireland Sub-Fund's exposure to RLMIS, the Risk Margin, the SCR and a capital buffer as required under the RLI DAC capital management framework (64%).

- 9.26 Therefore, there would be no change to the SCR Cover of the Liver Ireland Sub-Fund as a result of the Liver Ireland Scheme.
- 9.27 Following the implementation of the Schemes, there would be no change to the capital support arrangements set out in the RLI DAC Transfer Scheme, under which the RLI DAC Open Fund would provide capital support to the Liver Ireland Sub-Fund should this be required.
- 9.28 Furthermore, the implementation of the Schemes would not transfer any assets or liabilities into or out of the RLI DAC Open Fund and so the Schemes would have no impact on the financial strength of this fund.
- 9.29 Therefore, I am satisfied that security provided by the assets of RLI DAC for the guaranteed benefits of the policyholders of the Liver Ireland Sub-Fund would not be materially adversely affected by the implementation of the Schemes.

#### TERMINATION OF LRA

- 9.30 The preceding analysis assumes the continuation of the LRA.
- 9.31 If the LRA were to be terminated prior to the implementation of the Schemes, the Liver Fund Estate would have to be split between RLMIS and RLI DAC. However, as the Liver Fund Estate will be distributed in full at the point of consolidation following implementation of the Schemes, this will no longer be possible. The Liver Ireland Sub-Fund would, however, receive a rebate on the CFC that will be made in respect of the capital requirements that no longer need to be met from the RL Open Fund.
- 9.32 The CFC rebate amount would be determined on a "mutually agreed basis" between RLI DAC and RLMIS. If the Schemes are implemented, the LRA would be amended to ensure the definition of a "mutually agreed basis" is appropriate and legally sound, but not overly prescriptive so as to lock either party into a calculation that would not be appropriate. Furthermore, within the LRA more widely there are protections that would be invoked in the case of a dispute over the calculation, such as appointing an independent expert.
- 9.33 That being said, the CFC has been determined on the assumption that the LRA remains in place throughout the lifetime of the Liver Ireland business. Therefore, RLI DAC does not anticipate that the rebated amount would be sufficient to cover the capital requirements of the Liver Ireland Sub-Fund, and so termination of the LRA would leave RLI DAC in a materially worse position than would otherwise be the case.
- 9.34 I therefore need to consider the circumstances in which the LRA could be terminated. The LRA allows the parties (RLI DAC and RLMIS) to terminate the agreement through mutual consent but also specifies the situations and conditions in which either party may terminate the agreement unilaterally.
- RLI DAC may terminate the LRA in certain specific circumstances, such as if RLMIS defaults on its obligations under the LRA or becomes insolvent. However, it would not be in RLI DAC's best interests to choose to terminate the LRA, due to the capital strains that this would place on RLI DAC. It is reasonable to assume, therefore, that RLI DAC would act rationally and would not voluntarily terminate the agreement.
  - The conditions under which RLMIS may terminate the LRA are:
    - if either RLMIS or RLI DAC is prevented from fulfilling its obligations under the LRA because of a law or regulation;
    - if either RLMIS or RLI DAC ceases to hold registration, permission, authorisation, consent or licence that therefore prevents it from fulfilling its obligations under the LRA;
    - if RLI DAC fails to pay amounts due under the LRA;
    - if RLI DAC is in material breach of the LRA where this has not been remedied within a specific timeline;
    - if RLI DAC disposes of a material proportion of the Liver Ireland Sub-Fund Policies;

<sup>4</sup> The Counterparty Default Adjustment is an adjustment that is applied to the BEL to take account of the expected losses due to the default of the RLMIS after the LRA was effected.



- if RLI DAC ceases to maintain the Liver Ireland Sub-Fund as a separate fund; and
- if RLI DAC becomes insolvent.

- 9.35 The first two situations above seem to me to be extremely remote possibilities.
- 9.36 In relation to the third situation above, the payments from RLI DAC to RLMIS under the LRA are in respect of either the receipt of regular premiums from policyholders (so there is an incoming cash-flow to RLI DAC for every outgoing cash-flow due) or when the Liver Ireland Sub-Fund has excess capital that needs to be transferred to RLMIS. Therefore, it seems very unlikely to me that RLI DAC would fail to make the payment due under the LRA.
- 9.37 The other conditions in the list above are primarily within RLI DAC's control subject to remaining well capitalised (as is currently the case and as is expected to remain the case following the Scheme). As it is not in RLI DAC's best interests to allow the termination of the LRA (due to the negative impact that would have on its solvency position as set out below), I consider it highly unlikely that these conditions will occur.
- 9.38 I have been provided with projections of RLI DAC's future solvency development on a number of scenarios<sup>5</sup>, including a scenario where the LRA is terminated post-Scheme. The results of these projections are set out in Table 14 below.

**Table 14: Projected development of RLI DAC's solvency coverage ratio under a range of scenarios**

Scenario description	YE2022	YE2023	YE2024	YE2025	YE2026
Scheme not implemented	206%	191%	180%	172%	164%
Scheme implemented	206%	191%	180%	172%	164%
LRA ceases (no Scheme)	192%	182%	175%	169%	163%
LRA ceases (post Scheme)	137%	139%	141%	143%	143%
RLMIS defaults (no Scheme)	99%	104%	108%	113%	116%
RLMIS defaults (post Scheme)	90%	96%	101%	107%	111%

Source: Information provided by RLI DAC

- 9.39 RLI DAC aims to keep its capital coverage ratio above the target of 164% which has been calibrated to a '1-in-20' risk event. The table above shows that the LRA ceasing immediately after the Scheme is implemented would cause RLI DAC's solvency coverage to drop below its target level. However, RLI DAC's solvency coverage is projected to remain above the statutory minimum required level (i.e. at least 100% coverage) throughout the projection period and is projected to recover over time, albeit that it remains below the 164% target level over the period shown. Both of the RLMIS default scenarios are projected to result in an immediate and very substantial reduction in solvency coverage, with coverage dipping below the statutory 100% minimum (which would trigger a requirement for RLI DAC to submit a plan to the CBI to restore its solvency position). The fact that the immediate impact is similar in both of the default scenarios (i.e. both with and without the implementation of the Scheme) indicates that it is not a consequence of the Scheme, although it is the case that the impact is somewhat more severe and prolonged in the scenario where the Scheme is implemented.
- 9.40 Overall, in the event that the LRA was terminated for whatever reason, I expect that RLI DAC would be in a materially worse position than if it were kept in place. It is not in RLI DAC's best interests to choose to terminate the LRA, so I believe that it is reasonable to assume that RLI DAC would act rationally and would not terminate voluntarily.
- 9.41 In summary, I believe it is crucial that the LRA remains in place in order to protect the security of benefits of the policyholders of the Liver Ireland Sub-Fund as otherwise there would potentially be a materially adverse impact on their benefit security. However, as the Scheme envisages the continuation of the LRA and as it is very unlikely that the LRA would subsequently be terminated, I am satisfied that the implementation of the Schemes does not have a

<sup>5</sup> Note that these projections were produced before the adjustment noted in paragraph 5.104 was made. Based on information provided to me, I estimate that the impact of making that adjustment would be to reduce the projected YE2022 solvency ratio by a low single digit number of percentage points, with a smaller impact at later dates. Therefore, I consider the projections in Table 14 to provide a sound basis for assessing the projected solvency position of RLI DAC.



material adverse impact (as per my reasoning in paragraph 8.7) on the security of the benefits of the policyholders of the Liver Ireland Sub-Fund.

## CONCLUSION

- 9.42 Taking all of the above into account, I am satisfied that the implementation of the Schemes would not have a material adverse effect on the security of the guaranteed benefits for the policyholders of the Liver Ireland Sub-Fund.

### Effect of Schemes on security of guaranteed benefits – Other RLI DAC funds

- 9.43 The policyholders of the other funds of RLI DAC are those with policies in either the RLI DAC Open Fund or the RLI DAC German Bond Sub-Fund, and these funds are not in the scope of the Schemes.
- 9.44 If the Schemes were to be implemented, there would be no change to the assets and capital support arrangements that currently provide security for the guaranteed benefits of the policyholders of the other funds of RLI DAC.
- 9.45 From the perspective of the policyholders with policies in the other funds of RLI DAC, the implementation of the Schemes would only have an effect on the security of guaranteed benefits if it were to have a material effect on:
- The German Bond Reinsurance Agreement between RLMIS and RLI DAC; or
  - The financial strength of the RLI DAC Open Fund, which provides capital support to the RLI DAC German Bond Sub-Fund.
- 9.46 Taking each of these in turn:
- The implementation of the Schemes would have no direct effect on the German Bond Reinsurance Agreement, and the required capital and collateral would continue to be provided by the RL Open Fund.
- As set out in paragraph 9.13, if the Schemes had been implemented on 31 March 2022, following implementation the Internal SCR Cover of the RL Open Fund would have been within the acceptable range, and above the target, of the RLMIS Capital Framework. Furthermore, the Liver Fund is small in relation to the size of the RL Open Fund and therefore its consolidation into the RL Open Fund would not result in a material change to the risk profile of the RL Open Fund.
- Therefore, the implementation of the Schemes would not have a material adverse effect on the RL Open Fund's ability to provide the required capital and collateral under the German Bond Reinsurance Agreement.
- The implementation of the Schemes would not transfer any assets or liabilities into or out of the RLI DAC Open Fund and so the Schemes would have no impact on the financial strength of this fund.
- Therefore, the implementation of the Schemes would not lead to a material reduction in the security of benefits for the policyholders of the RLI DAC Open Fund nor would it materially reduce the strength of the capital support arrangements whereby the RLI DAC Open Fund would provide capital support to the RLI DAC German Bond Sub-Fund should this be required.
- 9.47 Furthermore, the implementation of the Schemes would not transfer any assets or liabilities into or out of the RLI DAC German Bond Sub-Fund and so would have no impact on the financial strength of this fund.
- 9.48 However, the RLI DAC Open Fund (and indirectly the RLI DAC German Bond Sub-Fund) would be impacted if the LRA were to be terminated in the future for whatever reason. This is because RLI DAC becomes responsible for the gross capital requirements of the Liver Ireland Sub-Fund. To the extent that the Liver Ireland Sub-Fund requires capital support, this will need to come from the RLI DAC Open Fund. The assessment above regarding security of benefits if the LRA were to cease is therefore relevant to the RLI DAC Open Fund policyholders and RLI DAC German Bond Sub-Fund policyholders as their security of benefits could be potentially adversely impacted were the LRA to terminate.
- 9.49 Therefore, subject to the assumption that the LRA remains in place (and, as discussed above, I conclude that it is very unlikely that the LRA would be terminated), I am satisfied that the implementation of the Schemes would not have a material effect on the security of guaranteed benefits of the policyholders of the other funds of RLI DAC.

## Summary & Conclusions

- 9.50 In summary, the implementation of the Schemes would have no material adverse effect on the security of guaranteed benefits of any of the policies of RLI DAC.

9.51 I am therefore satisfied that the requirements of the Security of Benefits test have been met.

## 10 TEST 2: POLICYHOLDER OUTCOMES

### Introduction

- 10.1 In this section, I set out my assessment of the proposed Schemes in so far as it may affect policyholders' reasonable benefit expectations under their policies with RLI DAC.
- 10.2 I have considered this separately for the following groups of existing policyholders of RLI DAC:
- Ireland Included Policyholders, whose Ireland Included Policies would be uplifted by the Offer Uplift if the Schemes were to be implemented;
  - Policyholders of the Liver Ireland Sub-Fund who would not be Ireland Included Policyholders; and
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.

### Effect of Schemes on reasonable benefit expectations – Ireland Included Policyholders

#### INTRODUCTION

- 10.3 The current reasonable benefit expectations of the Ireland Included Policyholders should be that (in line with their policy terms and conditions) they would receive:
- Their guaranteed benefits:
    - For CWP business, this would be the sum assured plus any attaching annual bonuses declared to date;
    - For UWP business, this would be their total premiums paid to date plus any attaching annual bonuses declared to date; or
    - For CB business, this would be the sum assured.
  - For with-profits Ireland Included Policyholders, future annual bonuses that are yet to be declared.
  - A final bonus that, if higher than 0%, would increase their pay-outs upon claim. This would be expected to reflect:
    - For with-profits Ireland Included Policyholders, the asset share underlying their policy including any historical enhancements to asset share in respect of the distribution of the Liver Fund Estate; or
    - For CB Ireland Included Policyholders, the historical allocations to their policies in respect of the distribution of the Liver Fund Estate.
  - Their additional guaranteed benefits, such as guaranteed annuity rates or guaranteed cash rates, where relevant.
- 10.4 Ireland Included Policyholders are likely to have an additional reasonable expectation, based on the recent practice of RLI DAC (as set out in the Liver WPOP), that their policy will be allocated a fair proportion of the remaining Liver Fund Estate.
- 10.5 Following the implementation of the proposed Schemes, the reasonable benefit expectations of the Ireland Included Policyholders will be broadly unchanged, other than that their asset shares (for with-profits policyholders) or their expected claim amounts (for CB policyholders) already include their full allocation of the Liver Fund Estate and so would not be increased further. In practice, this means:
- For with-profits Ireland Included Policyholders, their annual and final bonuses would be determined as currently but these would be based on asset shares allowing for the certain distribution of the Liver Fund Estate under the Schemes rather than an uncertain pattern of future enhancements; and
  - For CB Ireland Included Policyholders, their final bonuses would be determined as currently, but these would be based on a certain distribution of the Liver Fund Estate under the Schemes rather than an uncertain pattern of future enhancements.
- 10.6 Therefore, when considering the effect of the Schemes on the Ireland Included Policyholders in respect of their reasonable benefit expectations, I have considered the following:
- The calculated size of the Liver Fund Estate to be distributed under the Offers, noting this is dependent on assumptions made about the value of liabilities of the Liver Fund and the Liver Ireland Sub-Fund;

- The deductions being made to the Liver Fund Estate under the Schemes through the Scheme Contribution, as this reduces the amount available to distribute to the Ireland Included Policies (and the UK Included Policies) in aggregate;
- The Offer Uplift to be applied under the Schemes compared with the expected pattern of future enhancements to asset shares and CB claim amounts in the absence of the Scheme;
- The expected investment return and volatility of the investment return earned by the assets backing the asset shares of the with-profits Ireland Included Policies;
- The expenses that would be charged to the asset shares of the with-profits Ireland Included Policies (either in the normal course of business or in exceptional circumstances) and the exceptional costs that may reduce the contingent bonuses on CB Ireland Included Policies;
- Other aspects of the operation of the with-profits Ireland Included Policies, such as future management actions, the smoothing of pay-out values, and future annual and final bonuses that would be declared on these policies.

10.7 I consider each of these areas in turn below.

#### THE CALCULATED SIZE OF THE LIVER FUND ESTATE

- 10.8 The Liver Fund Estate is equal to (broadly speaking) the assets of Liver Fund less the liabilities of the Liver Fund (excluding the surplus in the staff pension schemes), including the BEL of the directly held policies and those reinsured in from the Liver Ireland Sub-Fund. The BEL is valued using assumptions about the future, informed by experience data and expert judgement. The size of the Liver Fund Estate therefore depends on these assumptions.
- 10.9 In the normal course of managing the Liver Fund, as the liabilities run-off, these assumptions would be adjusted (for example to reflect changing experience) so that the amount of the Liver Fund Estate available for distribution to policyholders eligible for distributions of the Liver Fund Estate will vary with experience over time.
- 10.10 If the Schemes were to be implemented, the value of the Liver Fund Estate would be locked in at the point of calculation of the Offer Uplift (the Calculation Date) based on assumptions made at that time about the future. It is important that the assumptions represent a best estimate view of future experience so that the size of the Liver Fund Estate is not materially overvalued or undervalued when calculating the Offer Uplift percentage that will be applied to the Included Policies because, after the implementation of the Schemes, the RL Open Fund Estate would benefit from any undervaluation of the Liver Fund Estate or would be required to make up any shortfall because of overvaluation of the Liver Fund Estate.
- 10.11 Given the timing of the Offer Uplift calculation and some necessary adjustments to the inputs, the output from the RLMIS Actuarial Systems used by the RLMIS Tactical Model to calculate the Offer Uplift has not been externally audited. However, the (non-economic) assumptions used to calculate the BEL for the purposes of determining the value of the Liver Fund Estate (and so the Offer Uplift) as at 31 December 2022, based on projections from 31 March 2022, were unchanged from those used for the audited UK Solvency II balance sheet as at 31 December 2021, with one exception in respect of expense assumptions, described in paragraph 5.104. These assumptions reflect RLMIS's best estimate view of future outcomes. The economic assumptions were updated to reflect market conditions as at the Calculation Date.
- 10.12 I have reviewed RLMIS's approach to setting these assumptions, as well as the best-estimate assumptions themselves at a high level, and I am satisfied that they are reasonable. I am also satisfied it is reasonable to make the adjustment to the expense assumptions when calculating the size of the Liver Fund Estate available for distribution.
- 10.13 One of the key areas of uncertainty in the assumptions is in respect of uncontactable policyholders (Gone-Aways) and the likelihood that they will make a claim under their policy in the future. Any assets that are not expected to be claimed by policyholders in the future ("**unclaimed assets**") would be recycled back into the Liver Fund for distribution to the other policyholders eligible for distributions of the Liver Fund Estate. An allowance for some proportion of the unclaimed assets to be included in the value of the Liver Fund Estate would increase the Offer Uplift percentage proposed to Eligible Policyholders under the Schemes.
- 10.14 A reduction in the number of Gone-Aways would reduce the materiality of the assumption in respect of how many of these policyholders will re-establish contact with RLI DAC or RLMIS to claim on their policies, as this would reduce the volume of unclaimed assets. As set out in Section 7, RLMIS has taken significant steps to trace its Gone-Aways in the Liver Fund as part of its ongoing centralised tracing process. RLI DAC has not been able to carry out the same tracing as in the UK as the same infrastructure does not exist in Ireland.

- 10.15 For those policyholders that remain uncontactable, RLI DAC has made assumptions about the number of these policyholders that will eventually make a claim on their policies as part of its BAU assumption setting process and has considered these assumptions with increased scrutiny ahead of commencing the Simplification Programme.
- 10.16 For both the Liver Ireland Sub-Fund and the Liver Fund, there remains a significant volume of Gone-Aways (even following the tracing activities undertaken by RLMIS in the UK. RLMIS's claims experience for these policies is that a reasonable proportion of these Gone-Aways (or their dependents) will not re-establish contact with RLMIS or RLI DAC to make a claim on their policies.
- 10.17 These Gone-Aways arise primarily from two sources:
- Non-computerised records, where policies are only held on paper files. Given the nature of the records, there is no substantial claims experience information available for these policies. However, the latest any of these policies paid a premium was in the early 1980s.
  - Waived premium policies for which premiums were waived in 2008.
- 10.18 The BEL in respect of these policies (in both cases) in the Liver Fund is reduced over time in line with experience for other policies held by RLMIS that have been paid up for a similar period of time. That is, an adjustment has been made to the BEL for the Liver Fund to allow for the expectation that a proportion of these policies would not be claimed in the future. This adjustment was made as part of BAU processes before commencing the Schemes and so some of the unclaimed assets have already been distributed to policyholders through historical distributions of the Liver Fund Estate.
- 10.19 In Ireland, policies that are deemed "dormant policies" (in accordance with the provisions of the Unclaimed Life Assurance Policies Act 2003), and the assets backing those policies, are transferred to the DAF. RLI DAC therefore considers that no reduction can be made to the BEL in respect of the Gone-Aways in the Liver Ireland Sub-Fund as the full value of these policies would need to be transferred to the DAF once these policies are deemed to be "dormant". Therefore, although there is a substantial number of policies in the Liver Ireland Sub-Fund that are not expected to be claimed by the holders of these policies (or their beneficiaries), their unclaimed assets cannot be distributed to the remaining policyholders in the Liver Ireland Sub-Fund (and the Liver Fund). Furthermore, where these Gone-Aways are also Ireland Included Policies, the full policy value would include the application of the Offer Uplift under the Schemes.
- 10.20 I am satisfied that the assumptions made in respect of Gone-Aways and future unclaimed assets are reasonable.
- 10.21 For the avoidance of doubt, Gone-Aways who re-establish contact with RLI DAC (or RLMIS) to make a claim under their policy would be able to do so and would receive the Offer Uplift under the Schemes on their policy if it would otherwise have been an Included Policy (i.e. regardless of the uncontactable status). As noted in paragraph 5.162, this exposes the RL Open Fund, through the LRA, to the risk of meeting this shortfall in cases where policies transferred to the DAF prior to end-2022 but subsequently make a claim after that date. However, based on past experience and the total amount transferred to the DAF to date, RLI DAC expects this risk to be minimal.
- 10.22 The inclusion of Gone-Aways in the scope of the Schemes and the consequent binding of them by the decision of the relevant High Court in relation to each Scheme is covered in section 13.23.
- 10.23 It should be noted that applying the Offer Uplift to the claim amounts of the CB Eligible Policies would increase the cost of guarantees for the Liver Ireland Sub-Fund, thus reducing the size of the Liver Fund Estate available for distribution under the Scheme. However, this is in line with current practice when making distributions of the Liver Fund Estate and so is not a change in practice introduced by the Scheme.
- 10.24 The calculated size of the Liver Fund Estate also allows for the margin under the rate card (for charges for both administration and investment management services) applying to (but not beyond) 31 December 2039, as described in paragraph 5.128. I am satisfied this is reasonable as this is in line with the expected treatment of the charges to the Liver Fund Estate in the absence of the Schemes, and is aligned with the proposed amendments to the IoT.
- 10.25 Overall, I am satisfied that the size of the Liver Fund Estate used to determine the Offer Uplift percentage for the Schemes has been calculated based on a reasonable set of assumptions that reflect RLI DAC's best estimate view of future outcomes.

#### THE DEDUCTION TO THE LIVER FUND ESTATE THROUGH THE SCHEME CONTRIBUTION

- 10.26 If the Schemes were to be implemented, the Scheme Contribution would be deducted from the value of the Liver Fund Estate before calculating the Offer Uplift percentage to be applied to Included Policies.
- 10.27 As set out in Section 5, the Scheme Contribution comprises:

- The CFC;
- The Project Costs Allowance; and
- The Premium Uplift Contribution.

10.28 I cover each of these in turn below, as well as my considerations in respect of the total Scheme Contribution.

#### The CFC

10.29 As set out in Section 5, if the Schemes were to be implemented, the RL Open Fund would take on the capital requirements of the Liver Fund (including the capital requirements in respect of the reinsured in Liver Ireland Sub-Fund). This would create a balance sheet strain for the RL Open Fund through the increased SCR, capital buffer under the RLMIS Capital Framework and the Risk Margin, partially offset by the increased TMTP and the CFC payment itself.

10.30 To compensate the RL Open Fund for the net balance sheet strain, a payment (the CFC) would be made from the Liver Fund Estate to the RL Open Fund, calculated on the basis of a Required Return on Capital rate consistent with returns the RL Open Fund would expect to achieve on other investments.

10.31 The balance sheet strain for the RL Open Fund has been adjusted for the purposes of calculating the CFC as follows:

- The removal of market risk.

Some of the balance sheet strain would be in respect of the capital requirements held against market risk inherent in the Liver Fund. It would be possible for RLMIS to reduce the current level of market risk (in theory at least) to an immaterial level by entering into suitable hedging arrangements. Therefore, the CFC would be based on the balance sheet strain assuming no capital requirements are held in relation to market risk.

- Sharing of diversification benefits from the consolidation of the Liver Fund into the RL Open Fund.

The diversification benefits would be shared between the RL Open Fund and the Liver Fund implicitly via the CFC calculation, effectively reducing the CFC payment from the Liver Fund Estate.

- The removal of counterparty default capital held by RLI DAC in respect of the LRA.

The balance sheet strain calculation is intended to compensate the RL Open Fund for taking on coverage of the capital requirements of the Liver Fund, including the Liver Ireland Sub-Fund through the LRA. RLI DAC only holds capital in the Liver Ireland Sub-Fund in respect of operational risk and reinsurance counterparty default risk, i.e. the risk that RLMIS is unable to meet its obligations under the LRA, but the CFC would be based on a balance sheet strain assuming no capital requirements are held in RLI DAC in relation to counterparty default.

10.32 I am satisfied it is reasonable to charge an amount to the Liver Fund Estate as compensation for the RL Open Fund taking on the capital requirements of the Liver Fund, and in particular I am satisfied that:

- The calculation of the net balance sheet strain is reasonable. In particular, it seems appropriate to allow for the SCR on a Pillar 2 basis and to include the target level capital buffer under the RLMIS Capital Framework, as this is the way the Liver Fund is managed currently and the way the business would continue to be managed following the consolidation into the RL Open Fund.
- It is appropriate to allow for potential management actions in the calculation of the SCR included in the net balance sheet strain, such as increasing guarantee charges or reducing the asset share EBR. These actions will continue to be available following the implementation of the Schemes and so it is appropriate to allow for these in the SCR, which would in turn reduce the CFC payable under the Schemes. I note there are more extreme management actions, such as removing asset share enhancements, that are not allowed for in the SCR and so in the CFC calculation, but I am satisfied it is appropriate not to include these as these are only available in extreme circumstances, and not allowing for these additional management actions is consistent with the approach to determining the SCR in RLMIS's reported balance sheets.
- Adjusting the balance sheet strain to remove the component of the capital requirements relating to market risk is reasonable as this risk could be materially removed by the RL Open Fund through hedging activities should RLMIS wish to do so.
- The sharing of diversification benefits equally between the Liver Fund and the RL Open Fund in the calculation of the CFC is reasonable as neither of the funds are being forced into the transaction, and the diversification benefit can only be achieved by combining two funds so neither fund is 'contributing' more to the diversification of risks. It should be noted that while the diversification benefits are shared equally between the funds in calculating the



CFC (by adjusting the balance sheet strain upon which the amount will be charged), the diversification benefit that would have been achieved by the RL Open Fund if the funds were consolidated on 31 March 2022 was £48 million, while the Eligible Policyholders would benefit from a reduction in the CFC payment of £14.5 million. I comment further on this point in paragraph 10.37 below.

- It is appropriate not to include the counterparty default capital held by RLI DAC in the balance sheet strain when calculating the CFC. Inclusion of this risk in the balance sheet strain calculation would mean that, in effect, RLMIS would be charging the Liver Fund Estate for the risk that RLMIS itself becomes insolvent in the future. Furthermore, none of the other historical closed funds of RLMIS that have been included in the wider Simplification Programme have been charged for this risk.

10.33 I note, however, that any potential future reduction in the Risk Margin arising from a review of the UK's implementation of the Solvency II regime has not been factored into the calculation of the CFC. Although there is no guarantee that such a reduction will arise, both HM Treasury and the PRA have given a strong indication that the Risk Margin requirements will be relaxed in the coming years. Whilst both the timing and the extent of any reduction are uncertain at the time of finalising this Report, I think it is reasonable to conclude that some allowance should in principle be made in the calculation of the CFC for the potential future reduction in the Risk Margin. I consider this further in paragraphs 10.38 and 10.39.

10.34 The CFC has been calculated to cover the period from the Calculation Date to the Liver Sunset Must Threshold. I am satisfied it is reasonable for an amount to be charged:

- For the period between the Calculation Date and the expected Implementation Date of the Schemes (31 December 2022).

The Offer Uplift percentage will be fixed as 23.1% based on the financial position of the Liver Fund on the Calculation Date (as projected to 31 December 2022) and so the RL Open Fund is, in effect, taking on the risks of the Liver Fund from the Calculation Date. It should be noted the CFC would not be paid if the Schemes were not implemented, but in this case the RL Open Fund also would not have to guarantee the Offer Uplift and so there would be no transfer of risk to be compensated for.

- For the period up to the Liver Sunset Must Threshold (expected to be reached in 2041).

The Liver Sunset Must Threshold was set at a level where the cost to the RL Open Fund of meeting the capital requirements of the Liver Fund at that point would be expected to be immaterial. Therefore, although the IoT is not explicit on the matter, it does not seem likely that it was intended that a "charge for providing capital support" payment would be payable upon the natural reaching of the Liver Sunset Must Threshold. Therefore it seems reasonable to not charge for the period after this point, noting that as NBSS is expected to reach zero ahead of 2041, this limit does not change the CFC amount calculated in practice.

However the cost to the RL Open Fund of meeting the capital requirements of the Liver Fund at the Liver Sunset May Threshold (expected to be reached in 2031) would not be immaterial. In order for the Liver Fund to be consolidated under this May Threshold, it is likely that some sort of charge for providing capital support would be required to be paid to the RL Open Fund from the Liver Fund Estate, but this would not be permitted under the terms of the IoT. Therefore, it seems reasonable that the CFC should charge an amount beyond the Liver Sunset May Threshold through to the Liver Sunset Must Threshold.

10.35 In section 5, I have set out RLMIS's and RLI DAC's rationale for choosing a Required Return on Capital rate of 9% p.a. above risk-free. My considerations in respect of this choice of rate for calculating the CFC are:

- While the policyholders of the RL Open Fund are not within the scope of my role as Independent Expert for the Liver Ireland Scheme, any payment from the Liver Fund to the RL Open Fund needs to balance the interests of the policyholders in each fund (including those policyholders reinsured into the Liver Fund from the Liver Ireland Sub-Fund).
- Therefore, when determining the Required Return on Capital rate, it is reasonable to have regard to the rate of return the RL Open Fund would expect to achieve on other comparable investments, as opposed to a lower rate such as a cost of capital rate (i.e. allowing for the cost of borrowing). As a starting point, RLMIS's target rate of return for external ventures (as set by the RLMIS Board) provides an obvious starting reference point.
- That being said, I am satisfied it is reasonable to charge a lower rate than this target return as RLMIS is familiar with the Liver business having administered this business for around 10 years, and so taking on this business is less risky than other return-seeking ventures the RL Open Fund may choose to invest in. However, this is balanced to some extent with the RL Open Fund taking on the full suite of risks of the Liver business through the capital requirements for the closed funds.

- I have also reviewed RLMIS's analysis of achieved return on equity metrics for reinsurers, which should be indicative of the return on capital reinsurers would expect to receive in any transactions, as well as recent rates applied in recent schemes of arrangements in the UK. I am therefore satisfied that the Required Return on Capital rate of 9% p.a. is within a reasonable expected range of rates charged by reinsurers and on similar schemes of arrangement.
- I also note that, in my experience, a net return on capital of 9.0% p.a. is broadly consistent with the return that a participant in an arm's length transaction would expect to achieve when accepting a transfer of UK insurance risks in a pension scheme buyout.

- 10.36 Considering the above, I am satisfied that using a Required Return of Capital Rate of 9.0% p.a. (above the risk-free rate) to calculate the CFC is reasonable.
- 10.37 However, it should be noted that, only allowing for 50% of the diversification benefits of consolidation to be reflected in the CFC results in higher capital requirements in the CFC than if the full diversification benefit were to be allowed for. Therefore, in the calculation of the CFC, the required return on capital rate is applied to higher capital requirements than the actual increase in capital requirements in the RL Open Fund that would result from the implementation of the Scheme. This would increase the effective rate of return on the actual NBSS arising in the RL Open Fund from the implementation of the Scheme.
- 10.38 The expected reduction in the Solvency II Risk Margin in the UK would increase this further. This would result in a relatively high rate of return for a transaction of this nature and, in particular, higher than the minimum return that RLMIS would expect to achieve on an external transaction. However, against this, there are some mitigating factors which I set out below.
- 10.39 In particular, the fact that the net balance sheet strain is reduced by virtue of the fact that the CFC is treated as additional available capital (i.e. is netted off the NBSS) provides a substantial mitigation, offsetting the impact of the relatively high rate of return. The magnitude of this reduction can be gauged by reference to the UK Solvency II Risk Margin for the Liver Fund. The Risk Margin at 31 March 2022, adjusted to exclude any contribution stemming from projected capital requirements after the date at which the Liver Sunset Must Threshold is projected to be reached, and further adjusted to reflect 50% of the diversification benefits of the proposed transaction, is £36 million. This compares to a CFC of £43.2 million at that date. Adjusting the CFC to allow for capital requirements at the level of 100% of the SCR (in line with the approach in the Risk Margin) rather than the SCR plus the capital target, would reduce the CFC figure to £25.6 million. Therefore, when calculated on a like-for-like basis, the CFC is roughly 70% of the Risk Margin (£25.6 million versus £36 million). As the Risk Margin is calculated using a prescribed cost of capital rate of 6% p.a., this implies that the effective rate of return on capital implied by the calculated CFC is much lower than the headline rate of 9% p.a.
- 10.40 Further to the above, I have also considered the sensitivity of the CFC to a range of rates to understand the materiality of this assumption for the Included Policyholders. As set out in paragraph 5.58, the CFC itself is netted off the NBSS when calculating the CFC, and so the Offer Uplift percentage that can be offered to policyholders is not particularly sensitive to the choice of Required Return on Capital rate. These sensitivities have been set out in the table below.
- 10.41 This table shows the sensitivity of the Offer Uplift calculated as at 31 March 2022, and so differs from the projected Offer Uplift to the Implementation Date of 31 December 2022. This also does not allow for the 3.6% estate distribution to be applied on 1 July 2022, and so the uplifts shown are higher than the Offer Uplift percentage.

**Table 15: Sensitivity of CFC and Offer Uplift to choice of Required Return on Capital rate**

	Required Return on Capital (above risk-free)		
	6% p.a.	9% p.a.	12% p.a.
CFC (£m)	36.6	43.2	47.9
Offer Uplift	26.2%	25.3%	24.6%

Source: RLMIS Chief Actuary report

- 10.42 In summary, in addition to considering the individual assumptions in the calculation of the CFC set out above, I have also considered the overall appropriateness of the value of the CFC payable by the Liver Fund to the RL Open Fund. While there are some aspects of the calculation that appear relatively onerous for a transaction of this nature, the impact of reducing the NBSS used in the calculation of the CFC to allow for the available capital provided by the CFC

itself is substantial, and in my view this aspect of the methodology offsets the impact of the relatively high Required Return of Capital Rate.

- 10.43 Overall, therefore, having considered all of the components of the calculation of the CFC, I am satisfied that the methodology used to calculate the CFC and the assumptions underlying this calculation are reasonable when taken in the round.

### **The Project Costs Allowance**

- 10.44 As set out in Section 5, if the Scheme were to be implemented, a deduction (the Project Costs Allowance) would be made from the Liver Fund Estate to cover the Liver Fund's (including the Liver Ireland Sub-Fund's) share of the costs of the fund consolidations under the Simplification Programme.
- 10.45 The aggregate costs of the fund consolidations and each fund's share of these costs were fixed as at 31 March 2021, which was the date on which the uplifts for the UFIB Sub-Fund Consolidation, the UFOB Sub-Fund Consolidation and the SL Fund Consolidation were locked in. Nevertheless, I have reviewed the appropriateness of the Project Costs Allowance to be charged to the Liver Fund Estate to ensure it is reasonable from the perspective of the Ireland Included Policyholders.
- 10.46 In assessing the Project Costs Allowance for the Liver Fund, I have considered:
- The aggregate costs of the fund consolidations;
  - The method of apportioning the costs between the in-scope funds; and
  - The size of the indemnity premium applied to the non-fixed costs expected to be incurred from 31 March 2021.
- 10.47 I have reviewed a breakdown of the aggregate costs of the fund consolidations incurred to 31 March 2021 and the expected future costs at that time in respect of the costs incurred to that date, I take comfort that the costs were overseen throughout the course of the project by the RLMIS Board, the RLMIS WPA, the RLMIS WPC and (in the case of certain funds) the relevant supervisory committee, such as the LSC in respect of the Liver Fund.
- 10.48 The expected future costs were assessed based on RLMIS's experience of similar projects and I am satisfied that, at the time this was calculated, the estimate was based on reasonable assumptions and was a true 'best estimate' such that it was considered equally likely that the total cost would be above or below the estimate. I note that, since 31 March 2021, there have been some overruns in project costs relative to the best estimate view, although these overruns to date are more than covered by the aggregate indemnity premium paid across the fund consolidations.
- 10.49 The aggregate costs were apportioned between the in-scope funds in proportion to asset shares plus the estates of those funds (plus in the case of the Liver Fund, the BEL of the CB policies), all as at 31 March 2021. I am satisfied this is a reasonable metric by which to apportion the costs as it is a measure of the post-uplift asset shares of each of the funds (and benefits for CB policies in the Liver Fund and the Liver Ireland Sub-Fund) and therefore a proxy for the value of the Eligible Policies and for the extent to which the policies of the fund would benefit from the fund consolidations.
- 10.50 I am also satisfied that the costs of the fund consolidations should be met by the in-scope closed funds, with no allocation to the RL Open Fund (on a best estimate basis, noting that in practice the RL Open Fund would meet any cost overruns), as:
- The principal benefits of the fund consolidations are to allow a fairer distribution of the estates of the closed funds to their policyholders and to provide certainty of these distributions, neither of which benefit the existing RL Open Fund policyholders.
  - The costs of the eventual fund consolidations under each funds sunset provisions would be (in most circumstances) expected to be met by the closed funds themselves. However, it should be noted that this is necessarily the case for the Liver Fund given the restrictions in the IoT, and the wording is open to interpretation and judgement. That being said, the Schemes are being undertaken to remove a tontine risk expected to arise in the UK and Ireland Liver Funds in advance of the sunset thresholds being reached, and so it seems reasonable for the Liver Fund to meet these costs in this case.
- 10.51 The Indemnity Premium has been set as a fixed percentage (15%) of the future (as at 31 March 2021), non-fixed expected costs of the fund consolidations. In assessing the reasonableness of the Indemnity Premium percentage, I have taken into account:
- RLMIS's analysis of premiums typically charged by external suppliers when RLMIS has sought fixed price contracts indicated that a premium of 10% to 30% would be typical, depending on duration of, and the level of certainty and control, around the activity.

- The fund consolidations under the Simplification Programme are a complex programme with multiple workstreams and so may be expected to attract a higher indemnity premium.
  - General market practice for with-profits funds to arrange fixed expense deals whereby a premium is paid in return for certainty in respect of the future expenses that would be charged to the fund. Such expense deals vary considerably between funds in terms of their duration and the allowance for inflation but an increase to current costs of 5% to 15% would be typical.
- 10.52 Overall I am satisfied that a 15% Indemnity Premium percentage is reasonable for the fund consolidations.
- 10.53 Furthermore, I note that at the time the aggregate costs were locked in (31 March 2021), the future, non-fixed costs represented a small proportion of the aggregate costs (£12.0 million of the aggregate costs of £38.1 million) and so the additional total costs split between all in-scope funds as a result of the indemnity premium is £1.8 million.
- 10.54 The Liver Fund's share of this total Indemnity Premium (£0.3 million) is relatively small in the context of the Liver Fund Estate, and this Indemnity Premium provides protection for the Liver Fund against cost overruns for the fund consolidations.
- 10.55 For the avoidance of doubt, in the event that the overall costs of the fund consolidations were to be lower than expected, it is not proposed that the RL Open Fund should refund any of the payments to the in-scope funds. As set out in paragraph 10.48, the costs will be higher than expected, but funded by the aggregate indemnity premium.
- 10.56 In assessing the reasonableness of the Project Costs Allowance (£7.2 million) allocated to the Liver Fund and the Liver Ireland Sub-Fund (jointly), I have considered the costs of alternative courses of action that may be taken as follows:
- If schemes of arrangement in respect of the Liver Fund and the Liver Ireland Sub-Fund were proposed at a later date (i.e. outside of the current Simplification Programme), the project cost efficiencies gained by completing all of the fund consolidations under one project would be lost. The Liver Fund consolidation is also more complex than some of the other fund consolidations; for example, owing to the LRA and the need for co-dependent schemes of arrangement in the UK and Ireland. The costs of undertaking these Schemes at a later date are therefore be expected to be greater than £7.2 million, and would be spread over a smaller number of policies, given the Liver Fund and the Liver Ireland Sub-Fund are closed to new business.
  - If no action were to be taken and the Liver Fund was consolidated under the Liver Sunset Clause, it is likely that the costs of consolidation would be lower than undertaking the schemes of arrangement, given certain actions would not be required on natural closure, such as the policyholder vote (and associated costs from mailings, helplines, etc.). The IoT is also silent on whether any costs of closure could be charged to the Liver Fund at this time and so it is not clear to what extent the IoT would allow the costs of this consolidation to be charged to the Liver policies rather than being met by the RL Open Fund. There is therefore a potential cost saving to the RL Open Fund from bringing forward the consolidation, which has not been reflected in the Project Costs Allowance (i.e. through a reduction to this amount). That being said:
    - There is significant uncertainty regarding the costs that may be incurred at the Liver Sunset Clause and regarding the extent to which such costs could reasonably be charged to the Liver Fund at that time. However, if the Liver Fund were to be consolidated at the Liver Sunset Must Threshold, which is expected to be met in 2041 when only around 20% of policies are expected to be in-force, in most circumstances the consolidation is likely to be more expensive on a per-policy basis than under the proposed Schemes if at that time it was deemed appropriate to charge all or some of the costs to the Liver Fund.
    - It is unlikely the Liver Fund would be consolidated at the Liver Sunset May Threshold (or any time much in advance of the Liver Sunset Must Threshold) as the risks remaining in the Liver Fund and the Liver Ireland Sub-Fund at this time would likely still be too significant for the RL Open Fund to take on without the payment of a capital charge (like the CFC). A capital charge would not be possible without utilising schemes of arrangement (or something similar) and so the project costs in this case would be higher.
    - Given the uncertainty and the relatively low materiality of the potential cost saving to the RL Open Fund, I am satisfied that I take this into account in my overall assessment of the terms of the Schemes (and the costs relative to the benefits to Included Policyholders) rather than as a standalone issue.
- 10.57 Taking all of the above into account, I am satisfied that the methodology used to calculate the Project Costs Allowance and the assumptions underlying this calculation are appropriate, and that the Project Costs Allowance allocated to the Liver Fund and the Liver Ireland Sub-Fund is reasonable.
- 10.58 If the Scheme were not to be implemented, the costs deemed to be attributable to the Liver Fund and incurred up until the point of abandonment would be shared between the RL Open Fund and the Liver Fund Estate in line with the

IoT, with the final allocation of costs being subject to review by the WPC and the LSC. I consider it reasonable to allocate a proportion of these costs to the Liver Fund Estate given the volume of feedback received by RLMIS and RLI DAC from Eligible Policyholders and the high proportion of responses supportive of the Schemes.

### **The Premium Uplift Contribution**

- 10.59 Currently, the Liver Fund Estate is being distributed through enhancements to asset share whenever the Liver Fund has excess capital above the 1-in-20-year capital target. This means the enhancements would apply throughout the term of a given with-profits policy at different points where different amounts of the premiums under the contract would have been paid.
- 10.60 If the Schemes were to be implemented, the Liver Fund Estate would be distributed through an immediate, single enhancement to asset share, and this would not be applied to premiums yet to be paid.
- 10.61 As holders of with-profits policies in the Liver Fund and the Liver Ireland Sub-Fund are contractually entitled to continue paying premiums at a certain level into the future, it seems reasonable that these should also benefit from the Offer Uplift as and when they are paid so they are not unfairly disadvantaged by the immediate distribution of the Liver Fund Estate under the Schemes.
- 10.62 The Premium Uplift Contribution deducted from the Liver Fund Estate under the Schemes is therefore intended to cover the amount required to uplift the amount allocated to asset share in respect of contractual future premiums payable by premium-paying with-profits policies.
- 10.63 As the pattern of future premiums is uncertain, the Premium Uplift Contribution has been calculated based on best-estimate assumptions of future contractual premium payments, i.e. allowing for expected decrements. The RL Open Fund Estate would be responsible for meeting the uplifts to asset share in respect of future premiums and so would have to fund any deficit resulting from an under-estimation at the Calculation Date of future premiums payable, or would make a 'profit' from any over-estimation of the future premiums.
- 10.64 If future experience is in line with these best-estimate assumptions, the whole of the Premium Uplift Contribution would be returned to policyholders of the Liver Fund and Liver Ireland Sub-Fund.
- 10.65 I am satisfied that the assumptions used in calculating the Premium Uplift Calculation represent a best-estimate view of future premium payments for the with-profits Included Policies.
- 10.66 It should be further noted that contractual future premiums only apply to those that had commenced on or prior to 31 December 2021, before details of the Schemes were made public through the Appetite Mailing. This approach was chosen to prevent policyholders from increasing their current or contractual future investments in the Liver Fund in order to benefit unfairly from the Offer Uplift under the Schemes (i.e. disadvantaging other policyholders of the Liver Fund and the Liver Ireland Sub-Fund). I am satisfied this is reasonable.
- 10.67 For the avoidance of doubt, future premiums on CB Ireland Included Policies would not lead to any enhancement to the sums assured or declared contingent bonuses on these policies as these sums assured already implicitly allow for all future contractual premiums being paid.
- 10.68 Overall, I am satisfied that it is reasonable to extend the uplift to the amount allocated to asset share in respect of future premiums as set out above and that the Premium Uplift Contribution represents a fair amount to deduct from the Liver Fund Estate to cover these future uplifts.

### **The Scheme Contribution overall**

- 10.69 The total Scheme Contribution payable from the Liver Fund Estate is £53.7 million and I note this is around a quarter of the value of the Liver Fund Estate at 31 December 2022, projected from 31 March 2022.
- 10.70 Of this £53.7 million, £3.3 million relates to the Premium Uplift Contribution, which will ultimately be returned to policyholders (under the best estimate view of future premium payments) through uplifts to asset shares as and when future premiums are credited to asset share.
- 10.71 However, the £50.5 million covering the CFC (£43.2 million) and the Project Costs Allowance (£7.2 million) still remains a significant deduction from the Liver Fund Estate. In respect of this large proportionate deduction, I note that:
- I have concluded in the sub-sections above that, when considered in the round, the methodology and assumptions used to calculate the CFC and Project Costs Allowance are reasonable, and therefore the calculated amounts are direct outputs from an approach that I consider to be fair.
  - In respect of the CFC, I note that:



- The Liver Fund and the Liver Ireland Sub-Fund contain significant long-tailed risks, predominantly in respect of longevity and expense risk on the non-profit policies in the funds. This means the capital requirements and risks in the funds are expected to persist for a long time, making them costly to transfer away from the Liver Fund Estate to the RL Open Fund.
  - As these risks are long-tailed, the capital charge is expected to remain at this level (as a proportion of the size of the Liver Fund Estate) in the medium-term and so it would not necessarily be less costly (proportionately) to undertake a similar exercise in the future.
  - For this reason, RLMIS has stated it is unlikely the RL Open Fund would elect to take on these risks without a capital charge at the Liver Sunset May Threshold. Schemes of arrangement (or similar) would need to be utilised at this time, with likely a higher total cost or per-policy cost (or both) through a similar scheme contribution given the long-tailed risks of the fund.
  - There would, however, be no capital charge on reaching the Liver Sunset Must Threshold under the terms of the IoT. That being said, RLMIS and RLI DAC have indicated that it is likely some other action would need to be taken ahead of this point to address the tontine risk in the fund, and such action taken would likely have a cost associated with it.
  - In respect of the Project Costs Allowance, the IoT is silent on whether any costs of closure could be charged to the Liver Fund if it were to be consolidated under the Liver Sunset Clause and so there is significant uncertainty in the comparison of the Project Costs Allowance with the costs of consolidation at the Liver Sunset Clause. However, as set out in paragraph 10.56, the aggregate charge to the Liver Fund and the Liver Ireland Sub-Fund in the future may be higher or lower than the proposed Project Costs Allowance depending on timing and the mechanism for the consolidation, but in most circumstances the consolidation is likely to be more expensive on a per-policy basis than under these proposed Schemes if at that time it was deemed appropriate to charge all or some of the costs to the Liver Fund.
  - Further to the above, any delay in taking action would mean that fewer policyholders would benefit from the action taken. For example, as shown in Figure 16 below, those policyholders who claim in the short-term would receive a lower distribution from the Liver Fund Estate than would be the case if the Schemes were implemented, and those who claim in the longer-term would have more uncertainty around their distribution from the Liver Fund Estate. The relative benefits of the proposed Schemes for different groups of Included Policyholders are covered in paragraphs 10.75 to 10.96.
- 10.72 Taking all of the above into account, I am satisfied that the size of the Scheme Contribution is reasonable in the context of the effect of the Schemes, and therefore that it is reasonable to propose the Schemes to Eligible Policyholders to vote on.
- 10.73 Whether the Schemes are implemented will then depend on the risk appetite of Eligible Policyholders, and to what extent they value the certainty of their distribution from the Liver Fund Estate. I have set out my consideration of the differences between the Offer Uplift under the Schemes and the current expected pattern of estate distributions in the sub-section below.
- 10.74 Furthermore, I am satisfied that the details of the compromise, and in particular the materiality of the Scheme Contribution being given up in exchange for certainty, have been set out clearly in the Appetite Mailing and Voting Packs so that Eligible Policyholders can make an informed decision on how to vote. I have set out my views on the communications with Eligible Policyholders in Section 12.

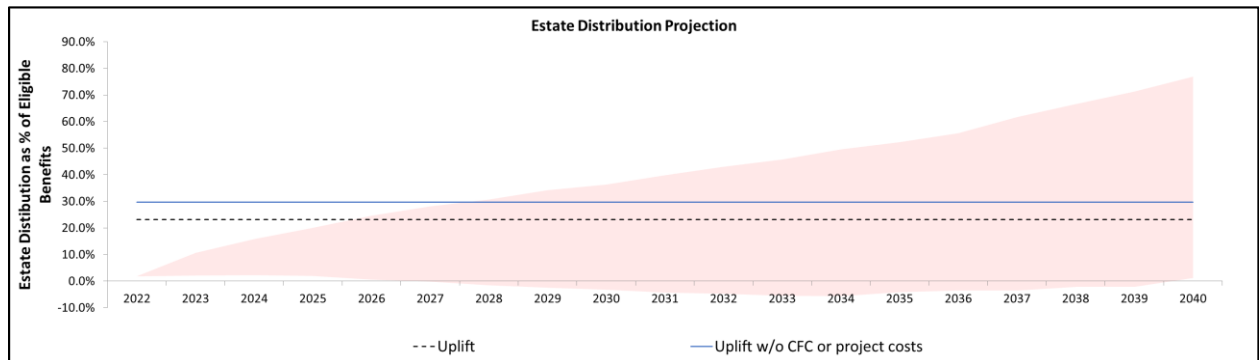
#### COMPARISON OF OFFER UPLIFT AND THE CURRENT EXPECTED PATTERN OF ESTATE DISTRIBUTIONS

- 10.75 If the Schemes were to be implemented, the Offer Uplift would be applied as an immediate (i.e. at the Implementation Date of the Scheme) uplift to the asset shares backing the with-profits Included Policies and to the claim amounts of the CB Included Policies.
- 10.76 The Offer Uplift would be structured as a fixed percentage uplift for all Included Policies (set as 23.1% based on financial information as at 31 March 2022, projected to 31 December 2022), together with the same percentage uplift to the amount allocated to asset share in respect of future premiums on premium-paying with-profits Included Policies as and when those premiums are credited to asset shares.
- 10.77 For those policies where, after the uplift, the value of guaranteed benefits would continue to exceed the uplifted asset share, the Schemes would have no immediate effect on the benefits paid. Eventual benefits paid on these policies on claim would depend on future investment returns and whether these are sufficiently high for the uplifted asset share to exceed the guaranteed benefits.



- 10.78 The implementation of the Schemes would therefore result in a different allocation of the Liver Fund Estate across the Included Policies than would be the case under the future distribution of the Liver Fund Estate in the absence of the Schemes. Some groups of policies would receive a higher allocation as a result of the Schemes, and some would receive a lower allocation.
- 10.79 Figure 16 below shows the comparison of the Offer Uplift percentage with the expected pattern of Liver Fund Estate distribution in the absence of the Schemes over the period to the Liver Sunset Must Threshold (expected to be reached in 2041).

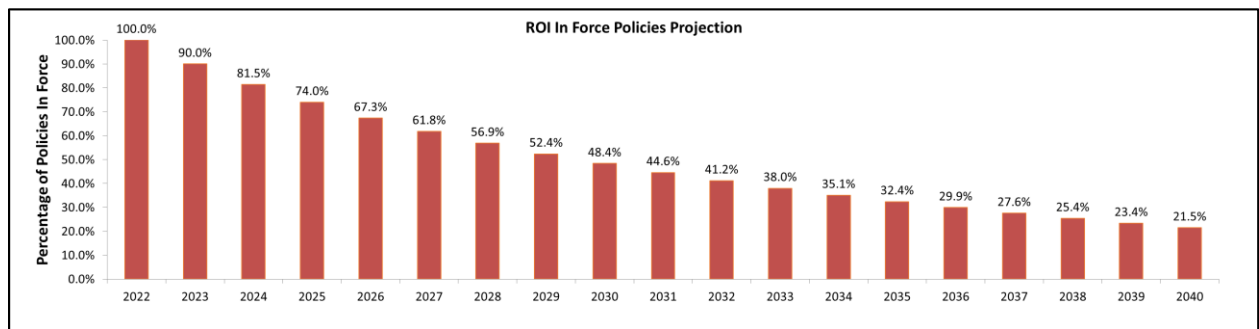
**Figure 16: Comparison of the Offer Uplift percentage with the expected pattern of Liver Fund Estate distribution in the absence of the Schemes**



Source: Information provided by RLMIS

- 10.80 In Figure 16, the Offer Uplift percentage (23.1%) is shown by the black dotted line.
- 10.81 The blue solid line shows the potential uniform uplift in the absence of the CFC and Project Costs Allowance elements of the Scheme Contribution (29.6%). As previously described, the Liver Fund Estate would be reduced by the Scheme Contribution prior to calculating the Offer Uplift percentage under the Schemes and so the total amount distributed to policyholders if the Schemes were to be implemented would (under best estimate assumptions) be lower than the total amount distributed in the absence of the Schemes. However, as concluded in the previous subsection, I am satisfied it is appropriate to deduct a Scheme Contribution from the Liver Fund Estate and that the size of the Scheme Contribution is reasonable.
- 10.82 The pattern of estate distribution in the absence of the Schemes reflects the enhancements to the asset shares of with-profits policies and to the sums assured of CB policies over the run-off of the Liver Fund whenever the fund has an excess above the 1-in-20-year capital buffer, as prescribed in the IoT. The estate distributions are therefore limited by the capital requirements and capital buffer required to be held in the Liver Fund.
- 10.83 Under best estimate assumptions, it would be expected that these capital requirements and the capital buffer could be released over time for distribution to policyholders. The central estimate of the aggregate distribution in the absence of the Schemes therefore increases over time for those policies in the fund the longest.
- 10.84 However, as this projection is based on best estimate assumptions, there is also some uncertainty in how the distributions will change over time. The pink shaded area of Figure 16 therefore shows the 90% confidence interval for the (uncertain) pattern of distributions in the absence of the Scheme.
- 10.85 It should be noted that the pink shaded area of Figure 16 shows the cumulative distributions that could be paid for policies exiting after the following mid-year in line with the IoT, e.g. the 2025 cumulative distribution would apply to asset shares and CB claim values for policies exiting from 1 July 2026.
- 10.86 Figure 16 shows the comparison of the uplift with the Schemes and in the absence of the Scheme for all Included Policies, both UK and Ireland. In my consideration of the Liver Ireland Scheme applying to the Ireland Included Policyholders, I need to consider the expected run-off profile of the Ireland Included Policies to understand the different sub-groups that would receive a higher or lower allocation of the Liver Fund Estate as a result of the Schemes.
- 10.87 Figure 17 shows the expected run-off of the Ireland Included Policies in the Liver Ireland Sub-Fund based on best estimate assumptions of future decrements. The percentage of policies in-force is shown as at the year-end for the labelled year.

Figure 17: Expected pattern of run-off of Ireland Included Policies



Source: Information provided by RLI DAC

- 10.88 I note the pattern of run-off of the Ireland Included Policies is broadly aligned with the pattern of run-off for the UK Included Policies.
- 10.89 Considering both Figure 16 and Figure 17, if the Schemes were to be implemented:
- Policyholders exiting the Liver Ireland Sub-Fund up to mid-year 2036 are expected (under best estimate assumptions) to receive a higher allocation of the Liver Fund Estate as a result of the Schemes. This corresponds to approximately 70% of Ireland Included Policies.
  - Policyholders exiting the Liver Ireland Sub-Fund from mid-year 2036 onwards are expected (under best estimate assumptions) to receive a lower allocation of the Liver Fund Estate as a result of the Schemes. This corresponds to approximately 30% of Ireland Included Policies.
- 10.90 However, in the absence of the Schemes, those policyholders exiting the Liver Ireland Sub-Fund later are expected to benefit from a tontine due to the large capital requirements of the Liver Fund that would be released over time under best estimate assumptions. The increased distribution for these policyholders may also be thought of as a 'reward' for bearing the additional risks of the Liver Fund in run-off; that is, that the best estimate assumptions are not borne out in practice. The increased distribution is not certain, as can be seen from the pink shaded area of Figure 16.
- 10.91 If the Schemes were to be implemented, this risk would be passed to the RL Open Fund and so would no longer be borne by the with-profits and CB policyholders of the Liver Ireland Sub-Fund. Therefore, it seems reasonable that those policyholders invested in the fund the longest would equally no longer benefit from an increased estate distribution relative to those exiting in the shorter term.
- 10.92 Furthermore, in my view the expectation to receive a tontine should not form part of policyholders' reasonable benefit expectations. This view is shared by the FCA in the UK and backed up by a recent UK ruling on a scheme of arrangement involving The Equitable Life Assurance Society where Zacaroli J stated that:
- "I consider that Equitable is indeed facing a problem that requires a solution – namely the emergence of a tontine which can properly be characterised as leading to an unfair distribution of capital among remaining policyholders. The FCA, whose statutory objectives include securing an appropriate degree of protection for consumers and ensuring that the relevant markets function well, is of the view that a tontine is not a desirable outcome and should not form part of policyholders' reasonable expectations."*
- 10.93 For the uplifts applied to the asset share in respect of future contractual premiums:
- Currently enhancements are applied over time to the asset share, where this asset share includes premiums paid to the date of the enhancement but not future premiums.
  - If the Schemes are implemented, all future contractual premiums would receive the full Offer Uplift (to the asset share allocated when those premiums are paid).
- 10.94 The approach to distributing the Liver Fund Estate under the Schemes may therefore be seen as more favourable to the premium-paying with-profits Included Policyholders. However, given the practical desirability of having a single Offer Uplift percentage, the choice in respect of future contractual premiums is whether to apply that Offer Uplift percentage to all future contractual premiums or to apply it to none. In my view, the former is the preferable approach, even if it does result in a somewhat more favourable outcome for premium-paying policies. Therefore, on balance, I do not view the change in the premiums to which an uplift would apply to be a material change in policyholder expectations, or to be overly favourable to premium-paying policyholders.

- 10.95 Considering the wider expectations of holders of policies of different terms, the with-profits Included Policies would remain as with-profits and so the investment returns on the asset share underlying their policies would continue to reflect the term of their policy, and the sums assured on the CB Included Policies would be unchanged by the Schemes (and so reflecting the term originally chosen). Only the additional return from the distribution of the estate would be altered by the Schemes.
- 10.96 I am satisfied that the change in the pattern of estate distribution as a result of the implementation of the Schemes would not have a material adverse effect on the reasonable benefit expectations of the Ireland Included Policyholders.

#### INVESTMENT RETURNS

- 10.97 If the Schemes were to be implemented, assets backing the asset shares of the majority of with-profits Included Policies and other with-profits policies in the RL Open Fund would be pooled. As a result, a uniform asset share EBR would be applied across the majority of the with-profits business in the RL Open Fund, including the with-profits business reinsured in from the Liver Ireland Sub-Fund.
- 10.98 The exception to this is the groups of with-profits policies in the RL Open Fund with significant guarantees for which the backing assets have been separately assigned. There would be no change to the asset strategies for this business as a result of the proposed Schemes.
- 10.99 The current asset share EBRs of the Liver Fund and the RL Open Fund are both 68%. If the Schemes were to be implemented, the EBR for the with-profits Included Policies would therefore be unchanged.
- 10.100 The Liver Fund Estate is invested primarily in UK and Euro Sovereign and corporate bonds with a proportion held as cash. If the Schemes were to be implemented then, after consolidation, trades to purchase additional equities may be required to ensure an asset share EBR of 68% is achieved following the application of the Offer Uplift to the asset shares of with-profits Included Policies and the subsequent pooling of assets backing asset shares between the Liver Fund and the RL Open Fund. The costs of any such trades would be attributed to asset shares in the RL Open Fund.
- 10.101 Therefore, I am satisfied that the implementation of the Schemes would not have a material effect on the expected return or volatility of investment returns for the with-profits Ireland Included Policies.
- 10.102 The benefits payable on the CB Ireland Included Policies are not linked to the investment returns on the assets backing them, and so the investment strategy following the implementation of the Schemes would not affect the reasonable benefit expectations of the CB Ireland Included Policyholders.

#### EXPENSES TO BE CHARGED TO ASSET SHARES AND EXCEPTIONAL COSTS

- 10.103 Following the expiration of the original unit rates in the rate card in the IoT on 1 December 2021, the with-profits policies of the Liver Fund are now charged (in line with this rate card):
- The 'actual cost' plus a profit margin, charged on a per-policy and percentage of premium basis; and
  - A proportional charge in relation to investment expenses, charged to all assets held by the Liver Fund with the exception of those in respect of the liabilities for the Liver Pension Schemes.
- 10.104 Within twelve months of the expiry of the rate card (so by 1 December 2022), RLMIS was required to carry out a review of the amounts being charged to the Liver Fund, by comparing them to those that would have been charged had the required services been provided by a relevant third-party provider. If the outcome of this review was that the required services could be provided at more cost-effective rates by a third party, the services would have either been outsourced to a relevant provider, or the amounts being charged to the Liver Fund would have been lowered in line with market rates. RLMIS conducted this review shortly after the expiry of the rate card with no changes being required. This is a one-off obligation and there is no legal requirement for RLMIS to review the rate card again after this date.
- 10.105 Although not a consequence of the Schemes, RLMIS intends to amend the IoT to include an ongoing obligation for a comparable review to be undertaken at least every three years. This change will align the processes for the business of the Liver Fund and Liver Ireland Sub-Fund with that of other funds that have previously been consolidated into the RL Open Fund.
- 10.106 However, the charges to the asset shares of with-profits policies would not be changed as a direct result of the implementation of the Schemes.

- 10.107 The benefits payable on the CB Ireland Included Policies are not affected by either of these expenses and so any changes to these following the implementation of the Schemes would not affect the reasonable benefit expectations of the CB Ireland Included Policyholders.
- 10.108 It is currently the case that where exceptional costs occur then, part of the exceptional costs can be charged to the Liver Fund. The IoT limits the circumstances under which exceptional costs may be attributable to the Liver Fund and requires RLMIS to use reasonable endeavours to mitigate or minimise any exceptional cost attributable to the Liver Fund. These provisions would be retained in the cut-down IoT following the implementation of the Schemes and the operation of the Liver Sunset Clause.
- 10.109 Currently any exceptional costs that are attributed to the Liver Fund are met by the Liver Fund Estate.
- 10.110 If the Schemes were to be implemented, there would be no Liver Fund Estate to which to charge any exceptional costs relating to policies transferred to the RL Open Fund from the Liver Fund (and those reinsured from the Liver Ireland Sub-Fund). Instead, the amount that would have been charged to the Liver Fund Estate would, depending on the nature of the exceptional cost, either be:
- In most circumstances, met by the RL Open Fund Estate and then recovered over time from the asset shares of the remaining with-profits Included Policies and from the declared contingent bonuses of the remaining CB Included Policies. The amount of the exceptional cost would be charged over the projected future run-off of these policies. Interest would be charged on these costs at a risk-free interest rate; or
  - In some circumstances (if determined to be fair and reasonable by the RLMIS Board and the RLMIS WPC), charged directly to the asset shares of the remaining with-profits Included Policies and from the declared contingent bonuses of the remaining CB Included Policies in the form of an immediate, uniform percentage deduction across all such policies in-force at that time.
- 10.111 Both of the above approaches need to take into account advice from the RLMIS WPA, the rationale for the Scheme and for the calculation of the CFC, and the associated representations made by RLMIS in respect of the Scheme to its policyholders.
- 10.112 The first proposed approach of spreading the exceptional costs over the future run-off of the former Liver Fund policies would allow for a greater proportion of these exceptional costs to be charged to those policies that remain in-force for longer. This approach would be consistent with the distribution of costs between generations of Liver Fund policies under the current approach and is expected to be used in most circumstances.
- 10.113 Furthermore, I consider it appropriate to charge interest on the costs to compensate the RL Open Fund for meeting the costs upfront. The change in approach to charging for exceptional costs is a consequence of the Schemes rather than an intentional change for the benefit of the Included Policyholders, and so I consider a risk-free rate to be appropriate to not unduly penalise those policyholders.
- 10.114 The second approach would only be adopted where all policyholders would be expected to benefit equally from the action being taken that has incurred the cost. Therefore, it would be reasonable in these circumstances to apply an equal charge to all remaining Included Policies.
- 10.115 I consider the proposed approach to charging for exceptional costs following the implementation of the Schemes to be reasonable.
- 10.116 Overall, I am satisfied that the implementation of the Schemes would not have a material adverse effect on the expenses that are charged to the asset shares of the with-profits Ireland Included Policies and, in the case of exceptional costs only, to the contingent bonuses for the CB Ireland Included Policies.

#### OTHER ASPECTS OF THE OPERATION OF THE WITH-PROFITS BUSINESS

- 10.117 Currently, the Liver Fund Estate meets the costs of smoothing the pay-outs in Liver Fund and, if the Schemes were to be implemented, these costs would instead be met by the RL Open Fund. However, the implementation of the Schemes would not result in any change to the smoothing practices applied to with-profits Included Policies.
- 10.118 The exception to this is in the first year following the implementation of the Schemes. For the first year, the smoothing approach would be applied to the claim value before the addition of the asset share uplift. This approach is taken to avoid the distributions under the Scheme being reduced by the effects of smoothing due to the increase in asset shares following the application of the Offer Uplift.
- 10.119 I am satisfied that this approach to smoothing in the first year following the Schemes is reasonable.

- 10.120 The implementation of the Schemes would not directly result in any changes to the process for setting annual or final bonuses for with-profits Included Policies. However, bonuses would be set with reference to the uplifted asset shares of the with-Profits Included Policies following the implementation of the Schemes.
- 10.121 The current target ranges for pay-outs on UK and Ireland with-profits Liver policies are that bonus rates are set such that at least 90% of pay-outs fall between 80% and 120% of asset share. Following the implementation of the Schemes, these target ranges will be aligned with the current target ranges in the RL Long Term Fund PPFM, which indicates that pay-outs for most policies should fall within 80% to 130% of asset share for CWP business, and 75% to 125% of asset share for UWP business.
- 10.122 Although the revised target ranges are wider than currently, the change is primarily to monitoring of pay-outs, and in practice bonuses would still be set in the same way as currently, targeting 100% of asset share. That being said, if pay-outs were not falling within these target ranges, the bonuses applying to Included Policies would be reviewed by RLMIS and RLI DAC with the aim of bringing pay-outs within the target range. There is therefore the possibility that the widening of the target range could result in a greater range of pay-outs for Included Policies.
- 10.123 The annual target range compliance reviews for the UK and Ireland Liver Funds show that the current target ranges have been met for the past five years. This provides some comfort that there have not historically been outliers in pay-outs that may have been affected by a slightly wider target range.
- 10.124 Following the implementation of the Schemes, the CB Included Policies would not receive any future contingent bonuses as the Liver Fund Estate (less the Scheme Contribution) would have been fully distributed.
- 10.125 Overall I am satisfied that the implementation of the Schemes would not have a material adverse effect on the reasonable benefit expectations of Ireland Included Policyholders through the changes to these aspects of the operation of the with-profits business (and bonuses for CB Ireland Included Policyholders).

#### CONCLUSION FOR THE IRELAND INCLUDED POLICYHOLDERS

- 10.126 Taking into account all of the above, I am satisfied that the implementation of the Schemes would not have a material adverse effect on the reasonable benefit expectations of Ireland Included Policyholders.

#### Effect of Schemes on reasonable benefit expectations – other RLI DAC policyholders

- 10.127 The remaining policyholders of RLI DAC are:
- Policyholders of the Liver Ireland Sub-Fund who would not be Ireland Included Policyholders; and
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.
- 10.128 I have considered these policyholders together in respect of their reasonable benefit expectations as the implementation of the Scheme would not change:
- The terms and conditions of the remaining policies of RLI DAC;
  - The charges that apply to the remaining policies of RLI DAC;
  - The capital management policy to which the funds in which the remaining policies of RLI DAC are held are managed; or
  - Any other aspect of the operation of the funds in which the remaining policies of RLI DAC are held.
- 10.129 Furthermore, in respect of the remaining with-profits policies of RLI DAC (namely those in the RLI DAC German Bond Sub-Fund), the implementation of the Scheme would not change:
- The principles and practices used in the management of the RLI DAC German Bond Sub-Fund;
  - The methodology used to calculate asset shares and surrender values of the with-profits policies of the RLI DAC German Bond Sub-Fund; or
  - The bonus and pay-out policies applied to the with-profits policies of the RLI DAC German Bond Sub-Fund.
- 10.130 Therefore, I am satisfied that the implementation of the Schemes would not have a material adverse effect on the reasonable benefit expectations of Ireland Included Policyholders.

## Standards of administration, servicing, management, and governance in RLI DAC

- 10.131 The implementation of the Scheme would not have any direct effect on:
- The systems on which the RLI DAC policies are stored and administered (although it should be noted that the wider consolidation programme is expected to bring changes in this regard);
  - The processes by which the RLI DAC policies are serviced;
  - The personnel in the RLI DAC teams that currently administer the policies;
  - The standards and levels of service that RLI DAC requires; or
  - The metrics against which RLI DAC measures its success or otherwise in customer servicing.
- 10.132 As set out in section 5, once the Schemes have been implemented and the Liver Sunset Clause has been operated to effect the consolidation of the Liver Fund into the RL Open Fund, the IoT specifies that the LSC would cease to exist.
- 10.133 The IoT as currently drafted:
- Sets out the terms of reference for the LSC, which include monitoring the operation and compliance with the IoT, the LRA and the RLI DAC Transfer Scheme; and
  - Specifies that the Liver Sunset Clause cannot be operated while the LRA remains in place, and so the LSC would continue to oversee the Liver business at least until the LRA is terminated.
- 10.134 However, the IoT will be amended (by application to the PRA in the UK) to allow the Liver Sunset Clause to be operated while the LRA remains in place. The Liver business would therefore lose the oversight of the LSC sooner than envisaged, and while the LRA, the RLI DAC Transfer Scheme and a cut-down IoT remain in-force.
- 10.135 Considering the LSC's primary objectives:
- The LSC monitors whether the management of the business of the Liver Fund and Liver Ireland Sub-Fund is in line with the IoT.  
  
Only a small number of provisions of the IoT would be maintained following the operation of the Liver Sunset Clause, as set out in the revised cut-down version of the IoT.
  - The LSC considers compliance with the RLI DAC Transfer Scheme, as well as the LRA and the associated collateral agreements.  
  
Both the LRA and the RLI DAC Transfer Scheme would remain in place following the implementation of the Schemes.  
  
RLMIS has informed me that, at the time of amending the IoT to allow for the RLI DAC Transfer Scheme in 2019, it was envisaged that the Liver Fund Estate would be divided between the Liver Fund and the Liver Ireland Sub-Fund before consolidating the Liver Fund into the RL Open Fund, and so the LRA would be terminated. However, as part of the current proposals, RLMIS and RLI DAC have agreed that retaining the LRA is preferable, and so the amendment to the Liver Sunset Clause to allow it to be operated while the LRA remains in place is required to achieve the desired outcomes under the Schemes.  
  
The RLI DAC Transfer Scheme would be amended solely to reflect the operational changes resulting from the Schemes.
- 10.136 Furthermore, the business of the Liver Ireland Sub-Fund would continue to be governed by the RLI DAC HoAF and the RLI DAC Board, and I am satisfied that this governance would be suitable for monitoring the operation of these continuing provisions. Therefore, I am satisfied that there would not be a material loss of policyholder protection from the LSC being disbanded.
- 10.137 There is a small number of provisions of the IoT that RLMIS considers it desirable to continue to apply, with these provisions remaining in either a cut-down revised IoT or the RL Long Term Fund PPFM, as set out in paragraph 5.128.
- 10.138 The additional provisions to be retained in the IoT are those that govern the charges (including in respect of exceptional costs) that may be charged to former Liver policies. This will ensure the current restrictions on charges to the Liver policies will be retained in the IoT following the consolidation of the Liver Fund into the RL Open Fund. However:



- As the Liver Fund Estate will be distributed in full, there will be some modifications to the provisions to clarify that charges that would have been made to the Liver Fund Estate will be made instead to asset shares; and
  - The provisions would be updated to specify that the margin on expenses under the rate card will apply until 31 December 2039, at which time charges will revert to an 'actual costs' basis. Currently the margin would apply until the Liver Fund is consolidated into the RL Open Fund, but this consolidation will be brought forward following the implementation of the Schemes. 2039 has been chosen acknowledging that RLMIS may, for operational reasons, execute the Liver Sunset Clause slightly in advance of the Liver Sunset Must Threshold being reached (which is expected to happen in 2041).
- 10.139 I am satisfied that both of these amendments are reasonable and are intended to ensure the provisions governing the management of the Liver policies are in line with current practice (in the absence of the Schemes).
- 10.140 Furthermore, within twelve months of the expiry of the rate card (so by 1 December 2022), RLMIS was required under the Liver IoT to carry out a review of the amounts being charged to the Liver Fund by comparing them to market rates, and will make any necessary adjustments as outlined in paragraph 3.28. This review was conducted shortly after the expiry of the rate card, with no changes required. There is no ongoing obligation for RLMIS to review the rate card again after this date. Although not a consequence of the Schemes, RLMIS intends to amend the IoT to include an ongoing obligation for a comparable review to be undertaken at least every three years. This change will align the position of the business of the Liver Fund (and the Liver Ireland Sub-Fund) with that of other funds that have previously been consolidated into the RL Open Fund, and provide an additional layer of protection to the with-profits policyholders of these funds.
- 10.141 In respect of the CPFM, the Liver Sunset Clause does not require these to be retained once the Liver Fund has been consolidated into the RL Open Fund, and RLMIS does not propose any amendments to retain these CPFM in the revised IoT. However, the CPFM are broadly captured in the Royal Liver PPFM currently; that is, while the CPFM are not exactly replicated in the Royal Liver PPFM, the intentions of these CPFM are included, as either principles or practices. Following the implementation of the Schemes, those principles and practices that have continuing relevance to the management of the Liver business would be transferred from the Royal Liver PPFM to the RL Long Term Fund PPFM.
- 10.142 Therefore, following the implementation of the Schemes, the CPFM would no longer be included in a legal document (the IoT), and would instead be included (broadly) in the RL Long Term Fund PPFM. Furthermore, certain CPFM would be included as practices rather than principles, with practices being easier to change than principles. This could be viewed as a weakening of the core principles by which the Liver business is currently managed. The RLMIS WPA has confirmed that any future changes to the principles and practices in the RL Long Term Fund PPFM will take account of the protections previously provided by the IoT, and these will be maintained wherever possible.
- 10.143 Having reviewed the terminating and continuing provisions of the IoT, I am satisfied that implementation of the Schemes would not have a material adverse effect on the protections provided to policyholders of the Liver Ireland Sub-Fund by the IoT.
- 10.144 The WPOP for the Liver Ireland Sub-Fund would be materially unchanged, other than amendments to reflect the implementation of the Scheme, such as removing references to future distributions of the Liver Fund Estate and reflecting that the LRA means the management of the Liver Ireland Sub-Fund is linked to the management of the RL Open Fund rather than the Liver Fund.
- 10.145 For the holders of policies in the RLI DAC German Bond Sub-Fund, there would be no changes to the WPOP governing the management of this business.
- 10.146 Taking into account all of the above, I am satisfied that the implementation of the Schemes would not have a material adverse effect on the standards of administration, servicing, management, and governance applying to the policies of RLI DAC, including the Ireland Included Policyholders.

### Summary & Conclusions

- 10.147 In summary, the implementation of the Schemes would have no material adverse effect on:
- The reasonable benefit expectations of the policies of RLI DAC; or
  - The standards of administration, servicing, management, and governance applying to the policies of RLI DAC.
- 10.148 I am therefore satisfied that the requirements of the Policyholder Outcomes test have been met.

## 11 TEST 3: ADVERSE SCENARIOS

### Introduction

- 11.1 In this section, I set out my assessment of whether my conclusions on the Security of Policyholders' Benefits test and the Policyholder Outcomes test would change under different circumstances and scenarios, and hence whether the proposals would remain fair and reasonable under a range of circumstances and scenarios.
- 11.2 The final Offer Uplift percentage has been calculated based on the Solvency II balance sheet for the Liver Fund as at 31 March 2022 (the Calculation Date), projected forward to the expected Implementation Date of the Scheme (31 December 2022), and will be fixed until the Implementation Date.
- 11.3 Therefore, under the Adverse Scenarios Test, I have considered whether events and scenarios that could occur between the Calculation Date and the date on which the Offer Uplift would be applied to the Ireland Included Policies (the Implementation Date), and whether they would lead to a material adverse effect on outcomes for policyholders.
- 11.4 For the Ireland Included Policyholders, the possible adverse effect over this period would be if the (theoretical) offer uplift percentage calculated at the Implementation Date is higher than the Offer Uplift percentage calculated on the Calculation Date, and as a result the Ireland Included Policyholders are worse off owing to the Offer Uplift percentage being fixed on the Calculation Date.
- 11.5 I have therefore considered the conditions that could have a material effect on the offer uplift percentage as follows:
- A change to investment conditions, including the levels of equity markets or interest rates; and
  - Differences in actual policy run-off patterns for policies of the Liver Ireland Sub-Fund and the Liver Fund compared with those expected and used in the calculation of the Offer Uplift percentage.
- 11.6 For the avoidance of doubt, these scenarios would not directly affect the remaining policyholders of RLI DAC (in relation to the proposed Scheme), and so the analysis in this section only considers the impact on the Ireland Included Policyholders.

### Analysis of the effects of changes to investment conditions

- 11.7 RLMIS and RLI DAC have carried out some analysis of the possible changes in investment conditions that could occur in the period between the Calculation Date and the Implementation Date. In each such investment scenario an offer uplift percentage has been calculated as at the Implementation Date and compared with the actual Offer Uplift percentage that was calculated as at the Calculation Date.
- 11.8 Analysis of these scenarios assumed to occur between the Calculation Date and the Implementation Date shows that the offer uplift percentage that would be calculated at the Implementation Date would be:
- 5.2 percentage points higher following a twenty percent fall in the value of equities (so an offer uplift percentage in this scenario of 28.3% which is 5.2 percentage points more than the Offer Uplift percentage of 23.1%); and
  - 3.9 percentage points higher following a one percent decrease in interest rates (so an offer uplift percentage in this scenario of 27.0%).
- 11.9 In summary, this analysis shows the maximum uplift that the Ireland Included Policyholders could have received if the Offer Uplift percentage had not been locked in (for the market changes set out above) would be around 28.3%, or an additional 5.2% increase to the asset shares of with-profits Ireland Included Policies or claim amounts on CB Ireland Included Policies.
- 11.10 While this potential increase is not insignificant, policyholders would also be protected from the risk of the value of equities or interest rates increasing (and so reducing the theoretical offer uplift percentage) and would benefit from certainty of the Offer, which I cover in paragraphs 11.14 to 11.17 below.

### Analysis of the effects of changes to the expected run-off pattern of policies of the Liver Ireland Sub-Fund and the Liver Fund

- 11.11 RLMIS and RLI DAC have carried out some analysis of the possible changes in the run-off pattern of policies of the Liver Ireland Sub-Fund and the Liver Fund that could occur in the period between the Calculation Date and the Implementation Date.
- 11.12 The business of the Liver Ireland Sub-Fund and the Liver Fund is expected to run-off at around 10% p.a. under best-estimate assumptions. If this run-off pattern were to increase by 50% (so a 15% p.a. policy run-off over the period

between the Calculation Date and the Implementation Date), the offer uplift percentage calculated at the Implementation Date would be 1.0 percentage points higher (so an offer uplift percentage in this scenario of 24.1%).

- 11.13 I note that a 50% increase in the run-off profile for the funds is an extreme scenario, and so the more plausible variations in the run-off profile over this period would be smaller and have a lesser effect on the potential offer uplift percentage.

#### **The reduction in volatility provided by Scheme**

- 11.14 In the absence of the Scheme, volatility in the value of the Liver Fund Estate would affect the estate distributions that policyholders eligible for these distributions would receive. Such volatility could be due to changes in investment conditions or to changes in the run-off of the policies in the Liver Ireland Sub-Fund and the Liver Fund.
- 11.15 If the Scheme were to be implemented, the Offer Uplift percentage would be fixed at the Calculation Date, thus providing Ireland Included Policyholders with certainty in terms of what they would receive under the proposed Offer, and removing their exposure to volatility in the value of the Liver Fund Estate between the Calculation Date and the Implementation Date. The existence of the guarantee would provide protection for Ireland Included Policyholders against the potential downsides from adverse scenarios.
- 11.16 The compensation paid for this certainty is that the potential upside, where conditions change and the theoretical offer uplift percentage as at the Implementation Date would be higher than the actual Offer Uplift percentage, is given away. While the extent of such potential upside in plausible scenarios over the period between the Calculation Date and the Implementation Date (as set out in the sub-sections above) is not insignificant, in my view these impacts are not so material as to make the Offer to be presented to Ireland Eligible Policyholders unreasonable.
- 11.17 Furthermore, based on RLMS's experience of previous schemes of arrangement in the UK, such certainty would be viewed as a positive policyholder outcome.

#### **Summary & Conclusions**

- 11.18 Taking the above into account, I am satisfied that my conclusions in relation to the Security of Policyholders' Benefits test and the Policyholder Outcomes test would not be affected by foreseeable circumstances and scenarios occurring between the Calculation Date of the Offer Uplift percentage that will be quoted in the Voting Packs and the Implementation Date.
- 11.19 I am therefore satisfied that the requirements of the Adverse Scenarios test have been met.

## 12 TEST 4: POLICYHOLDER COMMUNICATIONS

### Introduction

- 12.1 In this section, I set out my assessment of whether the information provided to Ireland Eligible Policyholders in respect of the Scheme is clear, concise, and of an appropriate level of detail, and has been provided in good time to allow them to assess the proposals and make an informed decision regarding the policyholder vote.
- 12.2 My assessment includes consideration of:
- The adequacy of the arrangements for supporting and guiding Ireland Eligible Policyholders through the process.
  - The communications with policyholders of RLI DAC who would not be Ireland Eligible Policyholders.

### Communications sent to Ireland Eligible Policyholders in respect of the Scheme

#### THE APPETITE MAILING

- 12.3 The Appetite Mailing was sent to policyholders that were expected to be Ireland Eligible Policyholders over a six-week period commencing 14 February 2022. Sample copies of the Appetite Mailing were made available on RLI DAC's website.
- 12.4 I reviewed working versions of the Appetite Mailing and provided challenge and feedback to RLI DAC in respect of these. I am satisfied that this challenge and feedback was appropriately addressed in the final versions sent to policyholders.
- 12.5 The outcome of the Appetite Mailing for the Scheme was that, as at 4 May 2022, 12% of those mailed responded and, of these, 85% (by number) and 88% (by value) were in favour of RLI DAC proceeding to make an offer.
- 12.6 The 12% response rate is broadly in line with those observed on previous schemes of arrangement undertaken by RLMIS.
- 12.7 The feedback received included 15 objections and 7 complaints across the Schemes. I have reviewed these objections and complaints, as well as RLI DAC's and RLMIS's responses to the policyholders raising them, and I confirm that the objections and complaints received from policyholders have not changed my conclusions in respect of the Fairness Tests or the Scheme overall.
- 12.8 Based on the responses to the Appetite Mailings, I am satisfied that it is reasonable for RLI DAC to proceed with the Scheme and the offer to Ireland Eligible Policyholders.

#### THE VOTING PACKS

- 12.9 If the Irish High Court grants an order to convene the Convening Hearing for the Liver Ireland Scheme, the Voting Packs will be sent to Ireland Eligible Policyholders over a six-week period commencing 17 August 2022.
- 12.10 I have reviewed working versions of the Voting Packs and provided challenge and feedback to RLI DAC in respect of these. I am satisfied that this challenge and feedback was appropriately addressed in the final versions sent to policyholders. In particular, I am satisfied that the details of the compromise, and in particular the materiality of the Scheme Contribution being given up in exchange for certainty, have been set out clearly in the Voting Packs so that Eligible Policyholders can make an informed decision on how to vote.
- 12.11 While the policyholder communications are quite lengthy, this reflects the complexity of the Schemes and associated changes, and I do not consider that any unnecessary detail has been included. Accordingly, I am comfortable to conclude that the information that has been provided (in the Appetite Mailing) and is to be provided (in the Voting Packs) to policyholders in respect of the Ireland Scheme may be regarded as concise as well as clear and of an appropriate level of detail.

#### THE CONFIRMATION MAILING

- 12.12 I have not yet seen a working version of the Confirmation Letter that RLI DAC would send to the Ireland Included Policyholders shortly after the Implementation Date confirming that the uplift has been applied to their Ireland Included Policies if the Scheme is implemented. I will provide an update on my review of the Confirmation Letter in my Supplementary Report.

## The arrangement for supporting and guiding Ireland Eligible Policyholders through the process

### THE ROUTE FOR POLICYHOLDER RESPONSES, ENQUIRIES AND OBJECTIONS

- 12.13 RLMIS has an established support team in the UK to deal with policyholder queries, particularly over the phone, from its previous schemes under the Legacy Simplification Project, and will continue to use this team in relation to the UK Scheme. However, RLI DAC has received legal advice that it cannot service calls from Ireland Eligible Policyholders using the UK support team.
- 12.14 RLI DAC's existing customer support team (for business-as-usual activities) does not have capacity to support the responses from Ireland Eligible Policyholders in relation to the Scheme, and the experience from RLMIS in recruiting the UK team is that it would be difficult to recruit enough sufficiently qualified team members into RLI DAC on short-term contracts.
- 12.15 Therefore, RLI DAC has established a team of 10 outsourced qualified experienced call handlers to provide support to the Ireland Eligible Policyholders and has ensured they are sufficiently trained on the Scheme and the relevant products in advance of the Appetite Mailing. The number of call handlers required has been determined by reference to:
- The volume of mailing packs sent out in relation to the Scheme;
  - The expected propensity of policyholders to seek information over the phone; and
  - RLMIS's experience from previous schemes of arrangement (including those under the Legacy Simplification Project) and from Part VII transfers. RLI DAC has taken this experience into account when considering the likely response rate to the Voting Packs and the likely average length of calls.
- 12.16 RLMIS has experience from a number of previous schemes of arrangement and from Part VII transfers that it believes provide a reasonable indication of the likely response rate to the communications packs and the likely average length of calls.
- 12.17 I have reviewed the analysis carried out by RLMIS and RLI DAC around the resources likely to be required to support policyholder queries, and I am satisfied that reasonable provision is being made for this, and that resource requirements will be able to adapt to any higher-than-expected demand.
- 12.18 Further to the above, I have reviewed working versions of the telephone helpline scripts, the guidance framework and the training materials provided to the RLI DAC outsourced call handlers.

### SUPPORT FOR VULNERABLE POLICYHOLDERS

- 12.19 RLMIS (including RLI DAC) has an established Vulnerable Policyholders Policy setting out the standards required to identify and support policyholders it considers to be vulnerable. In relation to the Schemes, RLMIS and RLI DAC will undertake further activities to facilitate the identification and support of vulnerable policyholders affected by the Schemes, including (but not limited to):
- Supporting vulnerable policyholders to articulate their needs and what adjustments would help them, for example by asking questions about needs and preferences in any contact RLMIS or RLI DAC has with them;
  - Ensuring all communications are made available in alternative formats (e.g. large print, braille, audio);
  - Engaging directly with a policyholder's representative, e.g. person appointed under a Power of Attorney where RLMIS or RLI DAC has been instructed to do so;
  - Ensuring inbound response management personnel have received the necessary training to identify vulnerability and the processes to be followed in response to this;
  - Making policyholders aware of the options available to them for help, e.g. third-party support, and representation (i.e. Power of Attorney);
  - Tailoring communications, where proportionate to do so, to meet the specific needs of vulnerable policyholders;
  - Using multiple channels to ensure, where appropriate, vulnerable policyholders have a choice on how to access the information;
  - Establishing quality assurance processes that identify areas that require improvement; and
  - Producing, and regularly reviewing, management information regarding the outcomes for vulnerable policyholders.

- 12.20 Where possible RLMIS and RLI DAC will ensure vulnerable policyholders are prioritised in the mailing dispatch schedule to maximise the time these policyholders have to consider the proposals and to decide how to vote.
- 12.21 Overall I am satisfied that the arrangements in place should ensure vulnerable policyholders are adequately supported throughout the process for the Scheme.

#### ADVICE AND GUIDANCE

- 12.22 RLI DAC has not established a formal guidance or advice proposition for Ireland Eligible Policyholders affected by the Scheme.
- 12.23 RLI DAC has provided me with information on the likely costs of providing formal advice and guidance for the Scheme for each Eligible Policyholder, and this would be a material proportion of the average uplift a with-profits Eligible Policy would receive under the Offer, and higher than the average uplift a CB Eligible Policy would receive under the Offer. Although only a proportion of Eligible Policyholders would take up the offer of advice and guidance, these costs would be met by the Liver Fund Estate, which would reduce the Offer Uplift available to all Eligible Policyholders.
- 12.24 As set out above, I have reviewed the communications strategy and policyholder communications for the Scheme, and I am satisfied that the information provided to Ireland Eligible Policyholders, in conjunction with the access to further information or assistance available over the phone, on request by post and on the RLI DAC website, would be sufficient to ensure that Ireland Eligible Policyholders have access to an appropriate level of support when making a decision on how whether to vote in favour or against the Offer.
- 12.25 I further note that under the Scheme, policyholders are making a decision about the certainty of their share of the Liver Fund Estate, but policyholders are not being asked to give up anything (e.g. guarantees on their policies) in exchange for the Offer Uplift.
- 12.26 I therefore consider that the costs of providing formal advice and guidance to be disproportionate to the additional benefits it would bring to Ireland Eligible Policyholders, particularly as these costs would reduce the Offer Uplift available to Ireland Eligible Policyholders. I am therefore satisfied it is appropriate for RLI DAC not to provide formal advice and guidance on the proposed Scheme.

#### Communications with holders of pensions policies with selected retirement dates prior to 31 December 2022

- 12.27 As set out in section 7, holders of pensions policies with SRDs between 31 March 2022 and 31 December 2022 would not automatically be Ireland Eligible Policyholders, but could become Ireland Eligible Policyholders if they chose to defer their SRD to on or after 31 December 2022. RLI DAC intends to these policyholders to inform them that, if they were to defer their SRDs to beyond 31 December 2022, they would benefit from the Offer under the Scheme.
- 12.28 The Offer Uplift calculated at the Calculation Date (31 March 2022) based on the expected position of the Liver Ireland Sub-Fund (and the Liver Fund) as at 31 December 2022 takes account of expected deferrals based on business-as-usual experience, i.e. an allowance is made for those who would be expected to defer their SRD in the normal course of business through the 'wake up' packs (or non-response to these packs).
- 12.29 However, there is a risk that the specific communications sent to these policyholders in relation to the Scheme encourage more policyholders to defer their SRD that would typically be the case. This risk is borne by the RL Open Fund, which is acting as the guarantor for the Offer from the Calculation Date (when the Offer was locked in).
- 12.30 If all pensions policyholders deferred their SRDs to benefit from the Offer under the Scheme, the expected cost to the RL Open fund is around £7.9 million. If this was allowed for in the calculation of the Offer Uplift, it would have reduced the Offer Uplift by around 1 percentage point.
- 12.31 However:
- While considering the impact on the RL Open Fund policyholders is not within my remit, I note that the Independent Expert for the UK Scheme has concluded that this approach is consistent with the approach taken for earlier schemes under RLMIS's Legacy Simplification Project, and the experience on these schemes was that the additional deferrals (beyond those assumed under business-as-usual assumptions) were trivial. He further concluded that there is a risk that the experience on this Scheme would be different, but the impact on the RL Open Fund is limited to the £7.9 million listed above, which is relatively small compared with the size of the RL Open Fund.



- Some pensions policyholders may hear about the Scheme in any case, through word of mouth, looking at the RLI DAC website or through the extensive press advertising planned to promote the Scheme and to re-engage Gone-Aways. It therefore seems appropriate to give all policyholders (as far as possible) equal information.
- 12.32 On balance, it seems reasonable to notify these policyholders that they could benefit from the Offer under the Scheme.
- 12.33 There is also the question of whether the cut-off date of 31 March 2022 is the appropriate one, i.e. any pensions policyholders with SRDs before 31 March 2022 would not be informed of the Scheme. There could be an argument to have informed those with SRDs in the first quarter of 2022 (or even earlier) of the plans for the Scheme. However, I note that a cut-off date must be chosen somewhere and the date at which wider eligibility for the Offer is set seems a reasonable choice.
- 12.34 In line with the broader proposal not to provide advice and guidance to Ireland Eligible Policyholders, RLI DAC does not intend to provide formal advice to these pensions policyholders as to whether deferring their SRD to benefit from the Offer is appropriate for their broader retirement plans and personal circumstances. I have reviewed the planned communications with these policyholders and I am satisfied that these are clear and unbiased, and set out that policyholders should consider their own personal circumstances when making a decision as to whether to defer their SRD.
- 12.35 Overall, I am satisfied that the proposed communication strategy with holders of pensions policies with SRDs prior to 31 December 2022 is fair and reasonable.

#### Communications with policyholders who would not be Ireland Eligible Policyholders

- 12.36 Policyholders of the Liver Ireland Sub-Fund who are not Ireland Eligible Policyholders (consisting of holders of Ireland HITM policies and non-with-profits policies other than CB policies) would not receive any communications about the proposed Scheme in advance of its implementation.
- 12.37 If the Scheme is implemented, these policyholders will receive a notification mailing that:
  - Explains the changes to the LRA and RLI DAC Transfer Scheme as a result of the Scheme; and
  - In the case of holders of Ireland HITM policies, confirms that their policies' asset shares have been uplifted, and explains that the uplift isn't expected to change their claim value.
- 12.38 Given that these are the only impacts of the Scheme on these policyholders, and these impacts do not require any decisions from these policyholders, I am satisfied that it is reasonable to notify these policyholders only after the implementation of the Scheme.
- 12.39 The remaining policyholders of RLI DAC (i.e. policyholders of the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund) would not receive communications specifically related to the Scheme because:
  - There will be no changes to the RLI DAC Open Fund or the RLI DAC German Bond Sub-Fund as a result of the Scheme; and
  - The LRA will remain in place, although amended to change the cancellation terms to reflect distribution of the Liver Fund Estate under the Scheme. I have confirmed in section 9 that, subject to the assumption that the LRA remains in place, I am satisfied that the implementation of the Schemes would not have a material effect on the security of guaranteed benefits of the policyholders of the remaining funds of RLI DAC, and it is very unlikely that the LRA would be terminated.
- 12.40 I am satisfied that this approach to the remaining policyholders of RLI DAC is reasonable.

#### Summary & Conclusions

- 12.41 I am satisfied that:
  - The information provided to Ireland Eligible Policyholders in respect of the Liver Ireland Scheme is clear, concise, and of an appropriate level of detail, and has been provided in good time to allow them to assess the proposals and make an informed decision regarding the policyholder vote on the Liver Ireland Scheme;
  - There are suitable arrangements in place for supporting and guiding Ireland Eligible Policyholders through the process; and
  - The approach to communications with policyholders of RLI DAC who are not Ireland Eligible Policyholders is reasonable.

12.42 I am therefore satisfied that the requirements of the Policyholder Communications test have been met.

## 13 TEST 5: POLICYHOLDER VOTE

### Introduction

- 13.1 In this section, I set out my assessment of whether the various features of the policyholder vote, which is required before the Liver Ireland Scheme could be sanctioned by the Irish High Court and implemented, are fair and reasonable to the Ireland Eligible Policyholders. In particular, I have considered the following:
- The number of Voting Classes and the class composition;
  - The requirements for the proposals to be approved; and
  - The approach to the calculation of the value given to each vote in the interpretation of the results of the vote.
- 13.2 In this section I have only considered the Ireland Eligible Policyholders as the remaining policyholders of RLI DAC would not take part in the policyholder vote.

### The number of Voting Classes and class composition

- 13.3 As described in section 6, RLI DAC has concluded that a single Voting Class is appropriate for the Scheme.
- 13.4 The external legal advisers of RLMIS and RLI DAC have carried out a due diligence exercise on the policies of the Liver Fund and the Liver Ireland Sub-Fund. This included consideration of the terms and conditions of Ireland Eligible Policies, as well as the legal rights of the Ireland Eligible Policyholders. One of the primary purposes of this due diligence was to identify any tensions between different groups of Ireland Eligible Policyholders that might suggest that the Ireland Eligible Policyholders should be subdivided into more than one Voting Class, i.e. if there are any aspects of the Scheme and/or the Liver Ireland Sub-Fund that might make it more difficult for Ireland Eligible Policyholders to consult together with a view to their common interest.
- 13.5 The key areas identified by the external legal advisers that could cause a potential class or fairness tension under the Scheme issue are:

- **The change in the pattern of estate distributions to policies of different terms**

As shown in section 10 of this Report, the holders of policies with short remaining terms are projected to receive a higher distribution of the Liver Fund Estate under the Scheme than they would have received in the absence of the Scheme, with the opposite being true for holders of policies with long remaining terms, noting that there is significant uncertainty around distributions and pay-outs in the future in the absence of the Scheme.

The external legal advisers have concluded that it is reasonable for these policyholders to vote together on the Scheme, but have highlighted the importance of ensuring that all relevant fairness considerations are addressed in communications to policyholders. I have commented on the Voting Packs in Section 12 of this Report.

- **The presence of both with-profit and CB Eligible Policies**

The key difference in the effect of the Scheme on these different policy types are that:

- For with-profits Eligible Policies, the Offer Uplift would apply to their underlying asset share, which would be used as a guide when determining pay-outs on claim but the asset share is not necessarily the exact amount a policyholder would receive.
- For CB Eligible Policies, the Offer Uplift would be applied to their sum assured and then this uplifted sum assured would be the exact amount paid out on claim (subject to any future exceptional costs as set out below).

The effect of the Scheme for the CB Eligible Policies is therefore more certain than for the with-profits Eligible Policies. However, the external legal advisers have concluded that it is reasonable for these policyholders to vote together on the Scheme as:

- Their current rights to estate distributions are the same and so these two groups have a common interest in the Liver Fund Estate;
- The Offer Uplift under the Schemes will be calculated and applied consistently between the two groups of policies;
- Future deductions for exceptional costs will be applied equally between the two groups following the implementation of the Schemes (as deductions to asset shares for with-profits policies and as deductions to

contingent bonuses, i.e. the estate distributions, for the CB policies), and so the two groups will not be treated differently once the Liver Fund Estate has been distributed and is no longer able to meet these exceptional costs; and

- Under the two Offer Acceptance Thresholds for the policyholder vote to pass, the CB Eligible Policies outweigh the with-profits Eligible Policies under the first test (by policy count), while the with-profits Eligible Policies outweigh the CB Eligible Policies under the second test (by Vote Value), and so neither can dominate the results of the policyholder vote.

13.6 The other areas considered by the external legal advisers in relation to class and fairness tensions are set out below, noting that in all cases the external legal advisers concluded that these areas would not lead to class or fairness tensions:

- The presence of both life and pension Eligible Policies;
- The periodic payments on some CB Eligible Policies;
- The presence of both CWP and UWP Eligible Policies;
- The presence of guaranteed annuity rates and guaranteed cash rates;
- The presence of “in-the-money” guarantees on certain Eligible Policies that are not classified as HITM and so remain within the scope of the Scheme;
- Entitlement to bonuses;
- The presence of Gone-Away Eligible Policyholders;
- Differing circumstances of policyholders;
- The presence of policy loans for certain Eligible Policyholders;
- The presence of HITM policies in the Liver Ireland Sub-Fund;
- The Premium Uplift Contribution;
- Differences in Vote Value approach;
- Some different characteristics of the Liver Ireland Sub-Fund life products; and
- Some different characteristics of the Liver Ireland Sub-Fund pension products.

13.7 In my view, the matter of Voting Classes is predominantly a legal issue and I sought the opinion of my legal adviser (Freshfields) to also consider this point. On the basis of the information provided by Pinsent Masons and RLMIS, Freshfields have not identified any potential issues around a single Voting Class.

13.8 Having considered both sets of advice I am satisfied that it is reasonable to provide for a single Voting Class.

#### The requirements for the proposals to be approved

13.9 The Offer Acceptance Thresholds that must be passed before the Scheme can be sanctioned are:

- **Threshold 1:** More than 50% of the Ireland Eligible Policyholders who vote on the Offer must vote in favour of the Offer; and
- **Threshold 2:** Those Ireland Eligible Policyholders who vote in favour of the Offer must represent at least 75% of the Vote Value of those voting.

13.10 The above thresholds are legal requirements for schemes of arrangement. While RLI DAC has no discretion in relation to Threshold 1, which requires a majority (by number) of the voting Ireland Eligible Policyholders to approve the Offer, RLI DAC does have an element of discretion in relation to Threshold 2 in terms of the approach it uses to determine the Vote Value.

13.11 I have set out my considerations and conclusions on the approach used to determine the Vote Value for the purposes of Threshold 2 in the sub-section below.

13.12 Once the results of the vote are known, it will be important that RLI DAC can demonstrate to the Irish High Court why it is appropriate for the Irish High Court to sanction the Scheme in light of the results of the vote. In particular, in deciding whether to sanction the Scheme, the Irish High Court will give consideration to whether:

- The firm has complied with the requirements of the Irish Companies Act 2014;
  - The Ireland Eligible Policyholders were fairly represented by those who voted, and those who voted in favour of the Scheme are acting without the intention of promoting interests that are adverse to the group of Ireland Eligible Policyholders overall;
  - Whether an intelligent (or informed) and honest person, as a member of the group of Ireland Eligible Policyholders and acting in respect of his own interest, might reasonably approve the Scheme; and
  - Whether there is any technical or legal defect in the Scheme.
- 13.13 The UK Scheme (the concurrent scheme of arrangement in the UK for the UK Eligible Policyholders of the Liver Fund) and this Scheme (the Liver Ireland Scheme) are co-dependent, and so both Schemes would need to be sanctioned for either to take effect. The UK Scheme has the same Offer Acceptance Thresholds and considerations of the English High Court to be sanctioned.
- 13.14 I will provide my assessment of the results of the vote, as well as the results of co-dependent UK Scheme, in my Supplementary Report.

### The approach to the calculation of the Vote Values

- 13.15 The weighting that will be attached to an Ireland Eligible Policyholder's vote (i.e. the Vote Value) used in assessing the vote result under Threshold 2 set out above would be:
- The sum of the amounts payable on a claim across all of the policyholder's Ireland Eligible Policies at the Calculation Date; plus
  - For with-profits Ireland Eligible Policies only (i.e. not CB), the sum of future premiums on all of the policyholder's Ireland Eligible Policies from the Calculation Date until their contractual end-point. These future premiums are limited to regular premiums only, limited to the level of annual premium being paid as at 31 December 2021 (as set out in paragraph 5.101).
- The amount payable on a claim is defined as follows:
- For pension policies: the transfer value of the policy as at the Calculation Date.
  - For life policies:
    - For endowments, the cash-in value of the policy as at the Calculation Date; and
    - For whole of life policies, the death value of the policy as the Calculation Date.
- 13.16 The use of the amounts payable on a claim would ensure consistency of the Vote Value with the Ireland Eligible Policyholder's interest in the Liver Fund (as the Vote Value is summed across all of their Ireland Eligible Policies).
- 13.17 The amounts payable on a claim do not allow for the Offer Uplift to Ireland Included Policies as a result of the Scheme and so these amounts do not directly represent the benefit of the Scheme for each Ireland Eligible Policy. However, as the Offer Uplift is structured as a uniform percentage increase to the Ireland Included Policies, these values should be a reasonable proxy for benefit of the Scheme for each Ireland Eligible Policy. Furthermore, these values should be understood and recognisable by Ireland Eligible Policyholders.
- 13.18 Including an allowance for future premiums in the Vote Value would reflect the additional interest that premium-paying with-profits Ireland Eligible Policyholders have in the Scheme. This additional interest arises because future premiums on Ireland Included Policies would receive the uplift (of the same percentage as is applied to asset shares) on the amount credited to asset shares when these future premiums are paid.
- 13.19 The amount payable on claim could have been chosen to be different values to those set out above. For example:
- The transfer or cash-in value could have been used for all policy types, i.e. including non-endowment life policies. However, holders of these policies will be more familiar with the death value and it is not expected that the death value and cash-in value would be materially different for these policies in the future.
  - As the intended benefit for a pension policy it is an amount payable on retirement, or equivalently for an endowment it is a maturity pay-out, these retirement or maturity claim values could have been used instead. However, as the voting values allow for future contractual premiums and do not allow for any early exit penalties, it is not expected that using the transfer or cash-in value would have a material impact on the outcome.

- 13.20 Overall, I am satisfied that approach to the calculation of the value given to each vote in the interpretation of the results of the vote set out above is reasonable.

### Summary & Conclusions

- 13.21 I am satisfied that the various features of the policyholder vote, which is required before the Liver Ireland Scheme could be sanctioned by the Irish High Court and implemented, are fair and reasonable to the Ireland Eligible Policyholders.
- 13.22 I am therefore satisfied that the requirements of the Policyholder Vote test have been met.
- 13.23 I will continue to review the arrangements for, and conduct of, the policyholder vote and will provide my views on these aspects in my Supplementary Report.



## 14 TEST 6: FAIR CONDUCT

### Introduction

- 14.1 In this section, I set out my assessment of whether the conduct of RLI DAC in respect of the proposed Liver Ireland Scheme is fair and reasonable to all RLI DAC policyholders. In particular, I have considered the following:
- The approach to eligibility for the Offer;
  - The approach to eligible investments and future contractual premiums (i.e. “carpetbagging”);
  - The treatment of Gone-Aways; and
  - The compulsion involved if the Scheme is sanctioned; in this case compulsion would apply to non-respondents and those who vote against the Offer.

- 14.2 I cover each of these in turn below.

### The approach to eligibility for the Offer

- 14.3 The Liver Ireland Sub-Fund policies are a mixture of with-profits and non-profit policies. Under the Scheme, the Ireland Eligible Policies would be with-profits policies and non-profit CB policies, subject to the following categories of policies being excluded from being Ireland Eligible Policies:
- Policies that will have reached their scheduled maturity or retirement date, where applicable, before 31 December 2022;
  - Policies classified as HITM; or
  - Policies that had been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer or death, or otherwise ceased to be entitled to receive benefits in accordance with the policy terms as at the Calculation Date. Those policies that have been claimed in full (or come into payment in full) on maturity, retirement, surrender, transfer or death, or that have otherwise ceased to be entitled to receive benefits in accordance with the policy terms as at 31 December 2022 would not become Ireland Included Policyholders (to receive the Offer).
- 14.4 The remaining policies of the Liver Ireland Sub-Fund would not be Ireland Eligible Policies.
- 14.5 Only policies that are currently eligible for distributions of the Liver Fund Estate would be eligible to receive the Offer Uplift if the Scheme were to proceed, and I am satisfied this is reasonable.
- 14.6 In the absence of the Scheme, policies exiting the Liver Ireland Sub-Fund before 31 December 2022 (the expected Implementation Date of the Scheme), through maturity, retirement or otherwise ceasing to be entitled to receive benefits in accordance with the policy terms, would not receive any further distributions of the Liver Fund Estate after exiting and, in particular, after 31 December 2022. Therefore, it seems reasonable that these policies should not benefit from the Offer Uplift under the Scheme.
- 14.7 That being said, holders of pensions policies have the option to defer their SRD, and so holders of pensions policies with an SRD prior to 31 December 2022 (and so are not eligible for the Offer) could become eligible if they elected to defer their SRD to after 31 December 2022. RLI DAC intends to contact holders of pensions policies with SRDs between 31 March 2022 and 31 December 2022 to inform them that, if they were to defer their SRDs to beyond 31 December 2022, they would benefit from the Offer under the Scheme.
- 14.8 As set out in section 12, in my view it is reasonable to notify these policyholders that they could benefit from the Offer under the Scheme. Therefore, if these policyholders choose to defer their SRD to after 31 December 2022, I am satisfied that it is reasonable for them to be eligible for the Offer.
- 14.9 In respect of Ireland HITM policies, these policies are not included within the scope of the Scheme and holders of Ireland HITM policies will not be asked to vote upon the Scheme. However, if the Scheme were to be implemented, the Ireland HITM policies would receive the Offer Uplift to their asset shares, i.e. the same percentage applied to Ireland Included Policies under the Scheme.
- 14.10 The external legal advisers have considered the proposed exclusion of Ireland HITM policies and consider that the exclusion of these policies from the scope of the Scheme is reasonable from a legal perspective.
- 14.11 From a fair conduct perspective, in my view it is reasonable to exclude the Ireland HITM policies from the scope of the Scheme for the following reasons:

- If the Scheme were to be implemented, other than in the relatively limited circumstances set out in section 5, the benefits payable to holders of Ireland HITM policies on claim would be unchanged by the Scheme and so giving up the Scheme Contribution would not directly affect these policyholders;
- The asset shares of the Ireland HITM policies would still receive the Offer Uplift (outside of the provisions of the Scheme) and therefore they would not be treated differently under the Scheme than they would in the case of estate distributions in the absence of the Scheme; and
- The effort involved in understanding and reaching a decision on the Scheme and its proposals for Ireland Eligible Policyholders is likely to be significant and it is difficult to justify providing the holders of Ireland HITM policies with significant volumes of communications on the Scheme when there is unlikely to be a material effect on their benefits.

14.12 In addition, I am satisfied that the approach taken by RLI DAC to classify policies as Ireland HITM policies is reasonable.

14.13 Overall, I am satisfied that the approach to eligibility for the Offer is reasonable.

#### **The approach to eligible investments and future contractual premiums**

14.14 As set out in paragraphs 5.116 to 5.117, the Liver Fund and Liver Ireland Sub-Fund currently allow Liver pension policies to increase existing with-profits premiums and pay new with-profits premiums. Switches from unit-linked to UWP are also allowed for certain pension and life policies. When the Schemes were made public through the Appetite Mailing in early 2022, there was a risk that policyholders could artificially pay temporarily high levels of additional premiums purely to exploit the planned Liver Fund Consolidation ("carpetbagging").

14.15 To address this risk, the Offer Uplift in respect of future premiums will be limited to the level of regular premiums set prior to a certain cut-off date, which both RLMIS and RLI DAC propose to set as 31 December 2021. Any lump sum premiums paid (including switches or transfers-in) or regular premium increases started after that date will not receive the Offer Uplift when they are credited to asset shares.

14.16 I am satisfied that it is reasonable to set a cut-off date (31 December 2021) for eligibility for the Offer Uplift for the following reasons:

- The cut-off date (prior to details of the proposals being made public) will prevent individual policyholders from increasing their investments in the Liver Fund or Liver Ireland Sub-Fund to the detriment of the remaining policyholders; and
- Although there would no longer be a share of the Liver Fund Estate available, policyholders' right to switch or make new with-profits investments will be unaffected by the Schemes.

#### **The treatment of Gone-Aways**

14.17 As set out in section 7, while RLMIS has gone to extensive lengths to trace Gone-Aways in the UK, the same tracing infrastructure does not exist in Ireland as there are no major tracing companies in operation and a postcode system is not well established in Ireland. Therefore, RLI DAC has not been able to carry out the same tracing as in the UK, either as part of business-as-usual processes or in advance of proposing the Liver Ireland Scheme.

14.18 RLMIS and RLI DAC have published a significant number of legal notices in newspapers in both the UK and Ireland, to increase the likelihood of Gone-Aways being made aware of the Schemes. RLI DAC has also undertaken some targeted advertising in Ireland where the tracing infrastructure is unavailable, including advertising in local newspapers in regions where a material proportion of the mailing population reside.

14.19 I have reviewed RLI DAC's strategy for re-engaging with Gone-Aways and, although activities are necessarily more limited in Ireland than in the UK for the concurrent UK Scheme, I am satisfied that the steps that have been taken to minimise the number of Gone-Away Ireland Eligible Policyholders are reasonable.

14.20 Overall, there are 14,000 Ireland Eligible Policyholders in the Liver Ireland Sub-Fund that are classed as Gone-Aways, as well as a further 1,800 Eligible Policyholders for whom RLI DAC either has no or an incomplete address.

14.21 In respect of the approach to ensuring that Gone-Aways are treated fairly under the Scheme, I note that:

- Based on my assessments under the Fairness Tests, I am satisfied that the Scheme would be fair and reasonable overall and that the Offer should be attractive to a large number of Ireland Eligible Policyholders.

- The majority of Gone-Aways in the Liver Ireland Sub-Fund are holders of whole of life IB policies for which no computerised records are held. The latest premiums paid on these policies were in the early 1980s and so it is likely that a material proportion of these policyholders are either already deceased but their policy has not been claimed, or are of a very advanced age and so a claim on their policy might be expected in the short to medium term (if at all given claim experience on these policies is low). As set out in Section 10, policyholders exiting the Liver Ireland Sub-Fund before 2035 are expected (under best estimate assumptions) to receive a higher allocation of the Liver Fund Estate as a result of the Schemes. Therefore, if a claim is made on their policies, the pay-out on policies held by these uncontactable policyholders would therefore be expected to be higher if the Schemes were to be implemented.
- For the remaining Gone-Aways, there is no reason to conclude that the benefits of the Scheme for them would be any different than for other Ireland Eligible Policyholders and therefore there is no reason to believe that Gone-Aways would vote any differently to the Ireland Eligible Policyholders who elect to vote on the Scheme.

14.22 I therefore consider it appropriate for RLI DAC to include Gone-Aways within the scope of the Scheme and that Gone-Aways would be bound by the decision of the Irish High Court in relation to the Scheme.

#### The compulsion of non-respondents and those who vote against the Offer

14.23 Under the Scheme, those Ireland Eligible Policyholders who:

- Do not respond to the notice of the Scheme or vote in the Scheme Meeting (in person or by proxy) ("**non-respondents**"); or
- Vote against the Offer, either by post or at the Scheme Meeting (in person or by proxy).

would be bound by the Scheme if it were to be implemented.

14.24 It should be noted that in my considerations in respect of the Fairness Tests in Sections 7 to 18 I have taken account of the type of policy held by the policyholder and I have not taken any account of whether or not a policyholder might respond to the Offer or how the policyholder might vote. This being the case, my analysis in Sections 7 to 18 holds in respect of non-respondents and those who vote against the Offer.

14.25 In addition, I have considered alternatives to the Offer/Scheme approach, such as:

- Including an opt-out mechanism in the Scheme; or
- Requiring Ireland Eligible Policyholders to opt into the Scheme (which would not require a SOA).

14.26 An alternative approach, such as those listed above, would allow for the possibility of a proportion of the policies in the Liver Ireland Sub-Fund not accepting the deductions to the Liver Fund Estate through the Scheme Contribution or receiving the Offer Uplift under the Scheme. This would mean that the Liver Fund Estate would need to be split between those who opt into and out of the Scheme, which would also have implications on the relative size of the Scheme Contribution for those who opted into (or did not opt out of) the Scheme. These are therefore not practical alternatives.

14.27 Based on my assessments under the Fairness Tests, I am satisfied that the Scheme is fair and reasonable overall and that the Offer should be attractive to a large number of Ireland Eligible Policyholders.

14.28 As described in Section 10, the pattern of expected distributions of the Liver Fund Estate would be different in the absence of the Scheme from that if the Scheme were to be implemented.

14.29 In particular, Ireland Included Policies with shorter durations until their expected claim dates would be the ones most likely to benefit from the implementation of the Scheme in terms of a comparison of the Offer Uplift with their estimated estate allocation in the absence of the Scheme. By contrast, Ireland Included Policies with a longer duration until their expected claim dates would be the ones most likely to receive a lower pay-out as a result of the implementation of the Scheme.

14.30 In respect of Ireland Eligible Policyholders who do not vote on the Scheme, it is possible that this group of Ireland Eligible Policyholders contains a disproportionate number of policyholders who are less likely to be in a position to engage fully with the Scheme (for a number of reasons, such as policyholders of higher ages or vulnerable policyholders). In relation to this group, I note the following:

- For life policies, policyholders of higher ages would be more likely to claim in the near term and so would be more likely to receive a higher pay-out as a result of the implementation of the Scheme.

- For pension policies the policyholders are not likely to be elderly as the pension policies within the Eligible Policies are intended to be pre-retirement savings vehicles. However, I would expect that holders of pensions policies would be more likely to engage with the Scheme as these policies will be key to their financial planning for retirement.
- I have explained in Section 10 why, in my view, the impact of the Scheme on the pattern of distributions of the Liver Fund Estate does not constitute a material adverse change to the reasonable benefit expectations of Ireland Included Policyholders.
- For vulnerable policyholders, I have set out in Section 12 the additional steps taken by RLI DAC to support such policyholders and, having reviewed these arrangements, I am satisfied that these are sufficient to ensure that vulnerable policyholders will be adequately supported throughout the process and will not be less well informed or unfairly disadvantaged as a result of their personal circumstances.

- 14.31 I am therefore satisfied that the Eligible Policyholders who are uncontactable or who otherwise do not vote on the Scheme would not be bound by a Scheme that is inherently unfair to them.
- 14.32 There are two Offer Acceptance Thresholds that would need to be met by the result of the vote before RLI DAC could seek the sanction of the Scheme from the Irish High Court. However, even in the event that the Offer Acceptance Thresholds are met, RLI DAC would consider all aspects of the result of the policyholder vote carefully before deciding whether to proceed to the Sanction Hearing. This would include consideration of the non-respondents and those who vote against the Offer, and whether these groups of policyholders might be more likely to suffer an adverse outcome as a result of the Scheme. I will also provide my conclusions in this regard in my Supplementary Report.
- 14.33 I do not see any reason to conclude that the benefits of the Scheme for non-respondents would be systematically any different than for other Ireland Eligible Policyholders, and therefore no reason to conclude that respondents' and non-respondents' interests are not aligned.
- 14.34 Furthermore, I am satisfied that RLI DAC has taken reasonable steps to engage as many Ireland Eligible Policyholders as possible in relation to the Offer and the associated risks, and the action that they need to take. In particular, the draft communications I have seen make it clear that the information is important, and that action is required.
- 14.35 I am therefore satisfied that it is appropriate for non-respondents and those who voted against the Offer to be bound by the decision of the Irish High Court in relation to the Scheme.

### Summary & Conclusions

- 14.36 I am satisfied that the conduct of RLI DAC in respect of the proposed Scheme has been fair and reasonable to all RLI DAC policyholders.
- 14.37 I am therefore satisfied that the requirements of the Fair Conduct test have been met.

## 15 ADDITIONAL CONSIDERATIONS

### Introduction

- 15.1 In this section I consider areas that are not covered by my Fairness Tests but that might nonetheless have a bearing on the Liver Ireland Scheme and its impact on the RLI DAC policyholders.

### Reattribution

- 15.2 In the UK, Chapter 20 of the FCA's COBS rules ("**COBS 20**") defines a reattribution of a with-profits fund's inherited estate as:

*"the process under which a firm which carries on with-profits business seeks to redefine the rights and interests that the with-profits policyholders have over the inherited estate."*

- 15.3 COBS 20 sets out a process that firms seeking to effect a reattribution should follow, including but not limited to:
- The appointment (and regulatory approval) of a "policyholder advocate" to negotiate with the firm on behalf of relevant with-profits policyholders;
  - The appointment of a "reattribution expert" to undertake an objective assessment of the reattribution proposals (this is not required if an independent expert has already been appointed in relation to the reattribution process or to a wider process that includes the reattribution process, such as a scheme of arrangement); and
  - Allowing with-profits policyholders to either individually accept or reject the reattribution proposals, or vote on whether the firm should go ahead with the proposals (in which case the majority would bind the minority if the legal process followed allowed this).
- 15.4 If the Schemes were to be implemented, then on the Implementation Date:
- The Scheme Contribution would be paid to the RL Open Fund from the Liver Fund Estate;
  - The Liver Fund Estate (after deduction of the Scheme Contribution) would be transferred to the RL Open Fund in return for an uplift of a fixed percentage (determined as at the Calculation Date) to the asset shares of the with-profits Included Policies and the claim values of the CB Included Policies invested in the Liver Fund (including those reinsured from the Liver Ireland Sub-Fund under the LRA) and to future regular premiums payable by with-profits Included Policies.
- 15.5 As the actions described above involve a change to the current approach taken to managing the Liver Fund Estate, it is relevant to consider whether these actions, individually or taken together, constitute a reattribution of the Liver Fund Estate pursuant to COBS 20.
- 15.6 For the avoidance of doubt, there are no equivalent rules to these reattribution rules in Ireland. However, given the UK Scheme and Liver Ireland Scheme are co-dependent, I consider the reattribution rules in the UK relevant to my assessment of the Liver Ireland Scheme.
- 15.7 RLMIS has received advice from its legal advisers, Pinsent Masons, that neither of the two actions described in paragraph 15.4 constitutes a reattribution for the purposes of COBS 20 for a number of reasons which I have attempted to summarise as follows:
- The Scheme Contribution does not constitute a redefinition of with-profits or CB policyholders' rights, interests and entitlements to the inherited estate or the manner in which it may be used for the following reasons:
    - The Scheme Contribution is another mechanism used to implement actions that RLMIS might otherwise have taken to mitigate and manage the risks to which the inherited estate is already exposed;
    - It is not unusual for with-profits funds' estates to be used to cover the risks of the fund;
    - Although there is no explicit provision in the Liver IoT for a Scheme Contribution, the Liver IoT does not preclude a Scheme Contribution payment; and
    - It is reasonable for part of the inherited estate to be used to mitigate these risks given the fairness issues that would otherwise arise for policyholders of the RL Open Fund;
  - The allocation of the inherited estate is not a redefinition or reallocation of policyholders' rights and interests as it is intended to distribute that inherited estate in accordance with those rights.

- The fixed percentage uplift approach to allocating the inherited estate does not constitute a redefinition of with-profits or CB policyholders' rights, interests and entitlements to the inherited estate and it is the view of RLMIS that the uniform uplift represents a more equitable distribution of the Liver Fund Estate. Neither the Liver PPFM nor the Liver IoT creates a reasonable expectation of a tontine, and the terms and conditions do not restrict the ability of RLMIS to apply a fixed percentage uplift.
  - The fixing of the percentage uplift at the Calculation Date rather than the Implementation Date does not constitute a redefinition of with-profits or CB policyholders' rights, but instead represents a transaction entered into between the Liver Fund and the RL Open Fund that is:
    - Ultimately for the benefit of the Included Policyholders (i.e. to implement the approach to uplifting the asset shares of the with-profits Included Policies and the claim values of the CB Included Policies and any future contractual premiums payable); and
    - Designed to address a specific risk to which Included Policyholders will be exposed (i.e. the risk that the Liver Fund Estate less the Scheme Contribution is not sufficient to provide for the uplift at the Implementation Date), and which if not addressed would necessarily create uncertainty or otherwise impede the distribution of the Liver Fund Estate by way of the Schemes.
- 15.8 My legal advisers, Freshfields, have reviewed the legal advice produced by Pinsent Masons and concluded that it provides a sufficiently robust and reasonable basis for RLMIS to proceed on the basis that no reattribution arises in relation to the aspects of the Schemes considered by it.
- 15.9 I am satisfied that given the advice received from Freshfields and the advice received by RLMIS from Pinsent Masons that the implementation of the Schemes would not constitute a reattribution.
- 15.10 While the question of reattribution is a legal one, from the perspective of fairness to Included Policyholders, I have also considered whether the actions taken by, and the process being followed by, RLI DAC and RLMIS are adequate to ensure that the proposals are fair and reasonable for Included Policyholders. In forming a view on this, I have had regard to the following:
- The proposed changes could be made at the time the relevant Sunset Clause Thresholds were met;
  - The Liver Ireland Scheme has been reviewed by the RLI DAC HoAF, and the UK Scheme has been reviewed by the RLMIS WPC and the RLMIS WPA;
  - RLI DAC has appointed me to form a view on whether the Liver Ireland Scheme is fair and reasonable in the capacity of Independent Expert, and equivalently RLMIS has appointed Nick Dumbreck to form a view on whether the UK Scheme is fair and reasonable in the capacity of Independent Expert;
  - The Liver Ireland Scheme has been subject to the scrutiny of the CBI, and the UK Scheme has been subject to the scrutiny of the FCA and the PRA;
  - The Liver Ireland Scheme and UK Scheme will be subject to the scrutiny and sanction of the Irish High Court and English High Court, respectively.
- 15.11 In my view these factors indicate that sufficient processes are in place in relation to the Scheme to ensure that the actions described in paragraph 15.4 are fair and reasonable to the Included Policyholders.

### PLAL Fund Consolidation

- 15.12 As set out in Section 3, RLMIS intends to go through a process to increase the sunset clause threshold for the PLAL Fund to a level that would allow the clause to be triggered in 2022. If approved, the PLAL Fund Consolidation is expected to be implemented on the same date as the Schemes considered in this Report (31 December 2022), and would result in:
- The consolidation of the PLAL Fund into the RL Open Fund;
  - The distribution of the estate of the PLAL Fund to its with-profits policies through a uniform percentage uplift to asset shares.
- 15.13 Throughout Sections 9 to 14 of this Report, including in the financial information presented, I have considered the effects of the implementation of the Schemes in isolation, assuming that the PLAL Fund Consolidation has not occurred and that the PLAL Fund remains as one of the RLMIS Closed Funds.
- 15.14 In this sub-section I consider the effects of the implementation of the Schemes on the RLI DAC policies in the scenario where the PLAL Fund Consolidation is also implemented.



- 15.15 For the RLI DAC policyholders, the principal consideration is the impact of the PLAL Fund Consolidation on the financial position of the RL Open Fund, and whether this would have a material adverse impact on the security of guaranteed benefits for the RLI DAC policyholders owing to the LRA between RLMIS and RLI DAC. If the Schemes were to be implemented, the LRA would remain in place between RLMIS and RLI DAC but, internally to RLMIS, the required capital and collateral would be provided by the RL Open Fund.
- 15.16 As described in Section 9, if the Schemes had been implemented on 31 March 2022, the RL Open Fund would have had excess capital of approximately £2.9 billion and an Internal SCR Cover of 209%. This is within the acceptable range under the RLMIS Capital Framework, and above the target, and so the RL Open Fund is expected to be sufficiently well capitalised following the implementation of the Schemes to support the required collateral under the LRA.
- 15.17 In the event that the PLAL Fund Consolidation were also implemented at the same time as the Schemes, the RL Open Fund's financial position and its Internal SCR Cover would not have been materially different to the impact of the implementation of the Schemes in isolation. The RL Open Fund would have remained within the acceptable range under the RLMIS Capital Framework.
- 15.18 Therefore, I am satisfied that the security provided by the LRA, and so the security of the guaranteed benefits for the policyholders of the Liver Ireland Sub-Fund (as well as the remaining policyholders of RLI DAC), would not be materially adversely affected by the PLAL Fund Consolidation.
- 15.19 I am therefore satisfied that the implementation of the PLAL Fund Consolidation alongside the Schemes would not have any effect on my conclusions under the Security of Policyholders' Benefits Test in respect of the RLI DAC policies.
- 15.20 The PLAL Fund Consolidation would not have any other effects on RLI DAC, the RLI DAC policies or the proposed Schemes. Therefore, overall I am satisfied that the implementation of the PLAL Fund Consolidation would not affect my conclusions set out in Sections 9 to 14 of this Report that if the proposed Schemes were to be implemented the requirements of all the Fairness Tests would be met.

#### Impact on previous schemes

- 15.21 The impact of the Schemes on the IoT and the RLI DAC Transfer Scheme have been set out in section 5.
- 15.22 There are no other schemes relevant to the policies of RLI DAC to be considered.
- 15.23 While there are other previous schemes applicable to the business of RLMIS, RLMIS has not undertaken detailed reviews of any interaction between the Schemes and other previous schemes to which RLMIS is party as it does not expect there to be any issues that have a bearing on these Schemes.

#### Emerging risks

- 15.24 When considering the impact of the implementation of the Schemes, I have continued to review emerging risks in the wider operating environment and whether these affect my conclusions in relation to the Schemes. In light of recent and ongoing events, such as the COVID-19 pandemic and the war in Ukraine, I have considered a range of scenarios that, in my view, are the most plausible and relevant to the Schemes, including:
- The potential for further volatility in financial markets;
  - The potential operational disruption within RLI DAC or RLMIS;
  - The potential disruption to third parties that play a role in the implementation of the Schemes; and
  - The wider societal impacts that may affect policyholders' ability to engage with the Schemes.
- 15.25 In the event that I considered that any emerging risks were to render it inappropriate for RLI DAC and RLMIS to proceed with the Schemes within the planned timeframes, I would make my views on this known to RLI DAC. Based on current conditions, in my view it remains appropriate for RLI DAC and RLMIS to continue to pursue the Schemes. However, I will continue to monitor this and I will provide an update in my Supplementary Report.

#### Tax

- 15.26 The implementation of the Liver Ireland Scheme is not expected to affect the Irish tax liabilities of any Ireland Included Policies. In particular, RLI DAC has received written confirmation from the Irish Revenue that Ireland Included Policies with tax efficient treatment (namely so-called 'Section 60' life assurance policies and Revenue-approved

pension policies) will continue to benefit from the same treatment following the implementation of the Liver Ireland Scheme.


15.27 RLI DAC has confirmed to me that a non-statutory business clearance request has been made in respect of corporation tax, which has been agreed by the Irish Revenue Commissioner.

15.28 In accordance with RLMIS's Tax Strategy, RLI DAC has submitted a full explanation of the transaction and associated Ireland tax consequences to the Irish Revenue Commissioners.

## 16 CONCLUSIONS ON THE PROPOSED SCHEME

- 16.1 I confirm that, as set out in sections 8 to 15 of this Report, I have considered the effects of the proposed Liver Ireland Scheme on all RLI DAC policyholders, subdivided as follows:
- Ireland Included Policyholders who would remain as policyholders of the Liver Ireland Sub-Fund if the Scheme is implemented;
  - Policyholders of the Liver Ireland Sub-Fund who are not Ireland Included Policyholders, for example holders of HITM policies, non-profit policies (except CB policies) and unit-linked policies; and
  - Policyholders of the other funds of RLI DAC, namely the RLI DAC Open Fund and the RLI DAC German Bond Sub-Fund.
- 16.2 I further confirm that I do not consider further subdivisions to be necessary.
- 16.3 For the avoidance of doubt, I have not considered the RLMIS policyholders in this Report. Those policyholders will be considered by the RLMIS Chief Actuary, the RLMIS With-Profits Actuary, and the UK Independent Expert as part of the UK Scheme.
- 16.4 In summary, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on RLI DAC policyholders with regard to:
- the security of their guaranteed benefits;
  - their reasonable benefit expectations; and
  - their servicing, administration, management, and governance arrangements.
- 16.5 I am further satisfied that:
- The Scheme would remain fair and reasonable under a range of circumstances and scenarios.
  - The information that has been or is to be provided to RLI DAC policyholders in respect of the Scheme is clear, concise, and of an appropriate level of detail, and will have been provided to RLI DAC policyholders with sufficient time for them to assess the proposals and make an informed decision regarding the vote.
  - The proposal to include Gone-Aways within the scope of the Scheme is appropriate.
  - The proposed approach to the policyholder vote is fair and reasonable.
  - In respect of the following areas the conduct of RLI DAC in respect of the proposed Liver Ireland Scheme is fair and reasonable to all RLI DAC policyholders:
    - The approach to eligibility for the Offer.
    - The approach to the allocation of the costs of the Scheme and the wider Legacy Simplification Project.
    - The treatment of Gone-Aways.
    - The compulsion of non-respondents and those who vote against the Offer.
- 16.6 I am therefore satisfied that the requirements of the Fairness Tests set out in Section 8 have been met.
- 16.7 I am satisfied that these conclusions would hold whether or not the PLAL Fund Consolidation were to proceed.
- 16.8 I will address the following in my Supplementary Report:
- An update on the effect of the implementation of the Schemes based upon more up to date financial information and on any other material developments since the date of this Report.
  - The results of the policyholder votes for the UK Scheme and the Liver Ireland Scheme.
  - The actual response rates and policyholder comments in relation to the UK Scheme and the Liver Ireland Scheme.
  - The communication materials in respect of the Liver Ireland Scheme due to be issued to RLI DAC policyholders after the implementation of the Schemes.

- Consideration of the non-respondents and those who vote against the Offer, and whether these groups of policyholders might be more likely to suffer an adverse outcome as a result of the UK Scheme and the Liver Ireland Scheme.
- Any significant events or market changes that may occur between the finalisation of this Report and the finalisation of my Supplementary Report.



**Michael Culligan**  
Fellow of the Society of Actuaries in Ireland

**10 June 2022**

## 17 APPENDIX A: LIST OF PRINCIPAL DATA SOURCES

17.1 In carrying out my work and producing this Report, reliance has been placed upon, but not limited to, the following information. All items have been provided directly to me by either RLI DAC or RLMIS unless otherwise noted.

### Legal documents

- The Ireland Liver Scheme Document
- The UK Scheme Document
- RLI DAC Due Diligence Report
- Ireland Liver Scheme Class Composition paper
- Reattribution advice from Pinsent Masons
- Liver Instrument of Transfer
- Proposed amendments to the Instrument of Transfer following implementation of the Schemes
- RLI DAC Transfer Scheme Document
- Proposed amendments to the RLI DAC Transfer Scheme following implementation of the Schemes
- Implementation Deed between RLI DAC and RLMIS

### Actuarial reports

- Report of the RLI DAC HoAF on the Ireland Liver Scheme
- Report of the RLMIS WPA on the UK Scheme
- Report of the RLMIS Chief Actuary on the UK Scheme

### Reinsurance

- Liver Reinsurance Agreement
- Proposed amendments to the Liver Reinsurance Agreement following the implementation of the Schemes

### Financial

- The RLMIS Tactical Model
- Pre-Schemes and pro-forma post-Schemes balance sheets for RLI DAC and RLMIS
- Risk appetite frameworks
- Breakdown of risk profile of RLI DAC and RLMIS

### Other

- Current WPOP and PPFMs
- Proposed amendments to the WPOP and PPFMs

### Correspondence

- Responses to queries in the query log between RLI DAC, RLMIS and the Independent Expert

## 18 APPENDIX B: GLOSSARY OF TERMS

18.1 A glossary of terms and abbreviations used throughout the report is provided below.

Term	Definition
1909 Act	Assurance Companies Act 1909.
Appetite Mailing	A notification about the Schemes sent to Eligible Policyholders prior to the Convening Hearing.
ASP	Actuarial Standard of Practice.
BAU Uplift	The enhancements to asset shares and increases to claim amounts for the policies of the Liver Fund and Liver Ireland Sub-Fund eligible for estate distribution as part of business as usual operations.
BEL	Best Estimate Liability. One of the components of the technical provisions under Solvency II. The BEL is calculated by projecting the expected future obligations of the insurer over the lifetime of the insurance contracts using the most up-to-date financial information and best-estimate actuarial assumptions. The BEL represents the present value of those projected cash-flows
Calculation Date	The date at which RLMIS calculated the Offer Uplift. This is 31 March 2022.
Caledonian	Caledonian Insurance Company, a subsidiary of Royal Liver.
Capital Buffer	The target excess Own Funds over the SCR under RLMIS's and RLI DAC's internal capital management frameworks.
Carpetbagging	Policyholders artificially paying high levels of additional premiums purely to exploit the planned actions of a firm.
CB	Contingent Bonus. A CB policy is non-profit but is entitled to share in distributions of the Liver Fund Estate when they are declared.
CBI	The Central Bank of Ireland, which is the supervisory authority with responsibility for the prudential supervision of insurance companies in Ireland
CFC	Closed Fund Contribution. A payment made from the Liver Fund Estate to the RL Open Fund under the Schemes. The payment is intended to compensate the RL Open Fund for taking on the responsibility for meeting the capital requirements associated with the business being transferred from the Liver Fund under the Liver Fund Consolidation.
COBS	The FCA's Conduct of Business Sourcebook rules.
COBS 20	Chapter 20 of the FCA's COBS rules, which focuses on the management of with-profits business.
Confirmation Mailing	If the required voting thresholds are passed, the Courts sanction the Schemes at the Sanction Hearings and the Schemes are implemented on the Implementation Date, RLMIS and RLI DAC will send letters (the Confirmation Mailing) to the holder of each policy of the Liver Fund and Liver Ireland Sub-Fund (whether Included or Excluded).
Consolidating Funds	The Consolidating Funds are the Liver Fund and the PLAL Fund (both due to be consolidated on 31 December 2022), as well as the RAIB Sub-Fund, UFIB Sub-Fund, the UFOB Sub-Fund and the SL Fund (all of which were consolidated during 2021).
Convening Hearing	A Court hearing at which RLMIS / RLI DAC seeks permission to convene the Scheme Meeting to allow the relevant Eligible Policyholders to vote on the relevant Scheme.
CPFM	Core Principles of Financial Management as set out in the IoT.
CWP	Conventional With-Profits. CWP business typically refers to policies where policyholders' premiums are fixed, and they have a benefit that is guaranteed at the outset in monetary terms if the policy is held to maturity. This benefit can subsequently be increased by annual bonuses that are awarded at the discretion of the insurer, depending upon the amount of surplus emerging in the insurance fund in which the policies are invested. Once they have been awarded, bonuses are typically guaranteed, and the insurer is not able to take them away. A final bonus may also be awarded at maturity.



DAF	Dormant Accounts Fund. In Ireland, policies that are deemed “dormant policies” (in accordance with the provisions of the Unclaimed Life Assurance Policies Act 2003), and the assets backing those policies, are transferred to the DAF, which is managed by the National Treasury Management Agency.
EBR	Equity Backing Ratio. The ratio of the value of equity and property investments to the total value of the investments.
EEA	The European Economic Area. The EEA comprises the EU together with Iceland, Liechtenstein and Norway.
Eligibility Date	The date on which RLMIS and RLI DAC determined the set of Eligible Policies based on policies that were in-force on that date (31 March 2022).
Eligible Policy	Either an Ireland Eligible Policy or a UK Eligible Policy.
Eligible Policyholder	A person who is a creditor for the purposes of the Companies Act in respect of an Eligible Policy. Either an Ireland Eligible Policyholder or a UK Eligible Policyholder.
English High Court	The High Court of Justice of England and Wales
EU	The European Union.
Fairness Test	Has the meaning given in paragraphs 8.8 to 8.11 of this Report.
FCA	Financial Conduct Authority, the conduct regulator for financial services firms and financial markets in the UK.
Freshfields	Freshfields Bruckhaus Deringer LLP, the independent legal adviser to the Independent Experts for the Schemes.
FSA	Financial Services Authority, the regulator for financial services firms and markets in the UK prior to the establishment of the PRA and the FCA.
FSAI	Fellow of the Society of Actuaries in Ireland.
German Bond Business	Business written by RLMIS in Germany that is now held in the RLI DAC German Bond Sub-Fund.
German Bond Reinsurance Agreement	The reinsurance agreement entered into between RLMIS (as reinsurer) and RLI DAC (as cedant) on 1 January 2019, in relation to the 100% quota share reinsurance by RLMIS of the policies transferred to the RLI DAC German Bond Sub-Fund under the RLI DAC Transfer Scheme.
Gone-Aways	Policyholders that RLMIS and RLI DAC cannot communicate with, i.e. RLMIS or RLI DAC has had a letter returned undelivered.
GRELI	GRE Life Ireland, a subsidiary of Royal Liver.
HITM Policy	A Heavily-In-The-Money Policy. A with-profits policy is a Heavily-In-The-Money Policy if, based on RLMIS's or RLI DAC's best-estimate assumptions applied as at the Calculation Date, the projected value of the benefits payable under the policy as at the expected date of claim is not expected to be increased by the application of the Offer Uplift to asset share proposed under the Scheme.
HoAF	Head of Actuarial Function. For an Irish insurance company subject to Solvency II, the person, as nominated by the company's board of directors and approved by the CBI, with overall responsibility for the tasks designated for the actuarial function under Solvency II and the additional responsibilities introduced by the CBI.
IB	Industrial Branch. This business was sold through IB channels with premiums typically paid to a collector who called at policyholders' homes. Premiums are no longer paid by policyholders in this way; they have been updated to be paid by standing order, direct debit or via the Post Office.
Implementation Date	The date on which the Schemes will be implemented (expected to be 31 December 2022). This is also the date on which RLMIS intends to implement the wider Liver Fund Consolidation.
Included Policy	Either an Ireland Included Policy or a UK Included Policy.
Included Policyholder	Any person who is a creditor for the purposes of the Companies Act in respect of an Included Policy. Either an Ireland Included Policyholder or a UK Included Policyholder.
Indemnity Premium	A premium charged in addition to the best estimate Project Costs as compensation for the RL Open Fund for taking on the risk of a cost overrun in relation to the Fund Consolidations.

Independent Expert	I, Michael Culligan, a Fellow of the Society of Actuaries in Ireland and a Principal with Milliman, a firm of actuaries and consultants.
Internal Model	A customised (company-specific) model for determining the SCR, which must meet certain specified standards and be approved by the regulator. Insurers are required to calculate their SCR using either the Standard Formula or an approved Internal Model.
IoT	The Instrument of Transfer, the legal document that led to the creation of the Liver Fund and governs the management of the fund.
Ireland Eligible Policy	Policies of RLI DAC that are eligible for the Ireland Offer, as defined in paragraph 5.32 of this Report.
Ireland Eligible Policyholder	Any person who is a creditor for the purposes of the Companies Act in respect of an Ireland Eligible Policy.
Ireland Excluded Policy	Policies of the Liver Ireland Sub-Fund that are not eligible for the Ireland Offer, as defined in paragraph 5.33 of this Report.
Ireland Excluded Policyholder	Holder of an Ireland Excluded Policy.
Ireland HITM Policy	A HITM Policy in the Liver Ireland Sub-Fund.
Ireland Included Policy	Policies of RLI DAC that are eligible for the Ireland Offer and remain in-force at the Implementation Date, as defined in paragraph 5.35 of this Report.
Ireland Included Policyholder	Any person who is a creditor for the purposes of the Companies Act in respect of an Ireland Included Policy.
Ireland Offer	The offer that RLI DAC is making to Ireland Eligible Policyholders regarding the terms of the Ireland Scheme.
Irish High Court	The High Court in Ireland.
Irish IE Report	This Report on the terms of the Liver Ireland Scheme, prepared by the Independent Expert.
L&M	London and Manchester, later Friends Provident.
Legacy Simplification Project	A major legacy simplification project conducted by RLMIS to rationalise and simplify its fund structure, products and administration systems in order to generate operational efficiencies, reduce risk and improve outcomes for longstanding customers.
Liver Capital Framework	The framework under which the capital of the Liver Fund is measured, managed, monitored, and reported.
Liver Fund	The Royal Liver Sub-Fund, a closed ring-fenced fund of RLMIS which holds the portion of business transferred to RLMIS from Royal Liver on 1 July 2011 and from GRELI on 1 July 2012 that was not subsequently transferred to RLI DAC on 7 February 2019. It also holds the business reinsured into the Liver Fund under the LRA.
Liver Fund Consolidation	The combination of the Scheme and the other steps involved in the consolidation of the Liver Fund into the RL Open Fund.
Liver Fund Estate	The estate of the Liver Fund. The estate is the excess of the assets over the liabilities of a given with-profits fund.
Liver Ireland Business	The business of the Liver Ireland Sub-Fund.
Liver Ireland Scheme	The Scheme; a scheme of arrangement in Ireland pursuant to Part 9 of the Irish Companies Act 2014, in respect of the eligible policyholders in the Liver Ireland Sub-Fund, which would be presented to the Irish High Court.
Liver Ireland Sub-Fund	The Liver Ireland Sub-fund is a closed ring-fenced fund of RLI DAC, which holds the business transferred in relation to the policies written in Ireland from RLMIS to RLI DAC on 7 February 2019.
Liver Ireland Sub-Fund WPOP	The WPOP pursuant to which with-profits business invested in the Liver Ireland Sub-Fund is managed.
Liver Ireland Sunset Clause	The provision in the RLI DAC Transfer Scheme prescribing the conditions under which the Liver Ireland Sub-Fund may or must be maintained as a separate sub-fund of RLI DAC.

Liver Ireland Sunset May Threshold	The level of total asset shares within the Liver Ireland Sub-Fund under which the Liver Ireland Sunset May Clause may be invoked (€334 million indexed with the Irish Consumer Price Index annually from 31 December 2018, i.e. €356 million as at 31 December 2021).
Liver Ireland Sunset Must Threshold	The level of total asset shares within the Liver Ireland Sub-Fund under which the Liver Ireland Sunset Must Clause is automatically triggered (€134 million indexed with the Irish Consumer Price Index annually from 31 December 2018, i.e. €143 million as at 31 December 2021).
Liver Sunset Clause	The provision in the Liver IoT prescribing the conditions under which the Liver Fund may or must be merged with the RL Open Fund and the Liver Fund Estate may or must be distributed.
Liver Sunset May Threshold	The level of total with-profits assets within the Liver Fund under which the Liver Sunset May Clause may be invoked (£296 million indexed with Retail Prices Index annually from 31 December 2018, i.e. £337 million as at 31 December 2021).
Liver Sunset Must Threshold	The level of total with-profits assets within the Liver Fund under which the Liver Sunset Must Clause is automatically triggered (£118 million indexed with Retail Prices Index annually from 31 December 2018, i.e. £135 million as at 31 December 2021).
Liver Sunset Point	The date at which the Liver Fund is projected to trigger the Liver Sunset Must Threshold set out in the Liver Sunset Must Clause.
LRA	The Liver Reinsurance Arrangement. The reinsurance agreement entered into between RLMIS (as reinsurer) and RLI DAC (as cedant) on 1 January 2019, in relation to the 100% quota share reinsurance by RLMIS of the policies transferred to the Liver Ireland Sub-Fund under the RLI DAC Transfer Scheme.
LSC	Liver Supervisory Committee. A committee established under the terms of the IoT, with responsibility to monitor the management of the Liver Fund for the benefit of all Liver policies (including those sold in Ireland). The LSC operates in compliance with the IoT including the CPFM, the Royal Liver PPFM and the Liver Ireland Sub-Fund WPOP.
MCR	Minimum Capital Requirement. Relative to the SCR, a second lower level of regulatory capital requirement under Solvency II, which is intended to represent the amount of capital required to ensure continued solvency in one year's time with a probability of at least 85%.
Milliman	Milliman Ltd., Consultants & Actuaries, 7 Grand Canal Street Lower, Dublin 2
NBSS	Net Balance Sheet Strain, i.e. the net reduction in the excess capital of the RL Open Fund that results from taking on the Liver Fund at each point in time over the run-off.
Non-respondents	Eligible Policyholders who do not respond to the notice of the Schemes or vote in the Scheme Meetings (in person or by proxy).
OB	Ordinary Branch. Business that is not classed as Industrial Branch.
Offer	Collectively, the (effectively identical) UK Offer and Ireland Offer.
Offer Acceptance Thresholds	The two thresholds set out in respective Companies Acts (Part 26 of the Companies Act 2006 in the UK and Part 9 of the Companies Act 2014 in Ireland). The Offer Acceptance Thresholds are the same in both countries and are set out in paragraph 6.19 of this Report.
Offer Uplift	The percentage increase that RLMIS and RLI DAC will apply to the Eligible Benefits of the Included Policies under the Schemes.
Own Funds	Broadly speaking, the excess of an insurer's assets over its liabilities on a Solvency II basis.
Part VII Transfer	A transfer of business undertakings under Part VII of the Financial Services and Markets Act 2000.
Pinsent Masons	Pinsent Masons LLP, RLMIS and RLI DAC's external legal advisers.
PLAL	Phoenix Life Assurance Limited.
PLAL Fund	PLAL With-Profits Fund, a closed ring-fenced fund of RLMIS which holds the investment element of the former PLAL unitised with-profits business which was transferred to RLMIS on 29 December 2008.
PLAL Fund Consolidation	RLMIS intends to go through a process to increase the sunset clause threshold for the PLAL Fund to a level that would allow the clause to be triggered in 2022, with the PLAL Fund being consolidated into the RL Open Fund on 31 December 2022 (the same date as the Implementation Date of the proposed Schemes).

PMAS	Police Mutual Assurance Society Limited. The business of PMAS was transferred into the RL Open Fund under section 86 of the Friendly Societies Act 1992 on 1 October 2020.
PPFM	The Principles and Practices of Financial Management pursuant to which with-profits business invested in a with-profits fund is managed in the UK.
PRA	Prudential Regulation Authority, responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms in the UK.
Premium Uplift Contribution	The best-estimate present value of the uplifts that will be made to the asset shares of the Included Policies under the Schemes in respect of any future contractual premiums (commenced on or before 31 December 2021) paid into Included Policies after the Implementation Date (assuming the Schemes are implemented).
ProfitShare	ProfitShare is the mechanism that RLMIS uses to distribute part of its operating profit by means of discretionary enhancements to the asset shares and unit fund values of the policies that qualify for ProfitShare. ProfitShare is allocated at the sole discretion of the RLMIS Board.
Project Costs	The cost of implementing the consolidations (and the associated review of minor product changes to be made in respect of certain of the Consolidating Funds) under the Legacy Simplification Project.
Project Costs Allowance	The amount that RLMIS proposes to charge each Consolidating Fund in respect of the costs of implementing the consolidations (and the associated review of minor product changes to be made in respect of certain of the Consolidating Funds) that RLMIS intends to implement under the Legacy Simplification Project. This amount varies by Consolidating Fund.
Project Costs Calculation Date	The date at which the Project Costs (both incurred and future expected) were fixed (31 March 2021).
QRT	Quantitative Reporting Template. The private reporting to the supervisor includes quarterly financial and other quantitative information, which is provided in defined formats.
RAG	Red-Amber-Green.
RAIB	Refuge Assurance Industrial Branch.
RAIB Sub-Fund	The Refuge Assurance IB Sub-fund, a former closed ring-fenced fund of RLMIS which held the RAIB business transferred on 1 January 2001 and as consolidated into the RL Open Fund on 30th June 2021.
RAOB	Refuge Assurance Ordinary Branch.
Rate Card	An expense tariff arrangement between the Liver Fund and the RL Open Fund.
Reminder Mailing	To promote customer engagement with the Voting Pack and in particular to encourage Eligible Policyholders to vote on the Schemes, a reminder mailing (postcard or brief letter referring to the Voting Pack) will be issued during the voting period to an Eligible Policyholder if RLMIS or RLI DAC have not received their vote within four weeks of mailing their Voting Pack.
Required Return on Capital	The return required by the RL Open Fund to compensate it for taking on the capital requirements associated with the business transferring from the Liver Fund under the Liver Fund Consolidation.
Risk Margin	The Risk Margin is an amount, in addition to the BEL, designed to bring the Solvency II technical provisions up to the amount that another insurer (or reinsurer) would be expected to require in order to take over and discharge the insurance liabilities in an arm's length transaction
RL Long Term Fund PPFM	The PPFM pursuant to which with-profits business invested in the RL Open Fund is managed.
RL Open Fund	The principal fund of RLMIS, which holds RLMIS's IB and OB business apart from that allocated to the Other Closed Funds. The fund remains open to new OB business.
RL Open Fund Estate	The estate of the RL Open Fund. The estate is the excess of the assets over the liabilities of a given with-profits fund.
RLCIS Fund	Royal London (CIS) Fund, a closed ring-fenced fund of RLMIS which holds the business transferred to RLMIS from Royal London (CIS) Limited on 30 December 2014.
RLG	Royal London Group. The group for which RLMIS is the parent entity and including a number of subsidiaries of RLMIS, such as RLI DAC.

RLI DAC	Royal London Insurance Designated Activity Company. A designated activity company incorporated in Ireland with registered number 630146 Ireland, whose registered office is at 47-49 St Stephens Green, Dublin 2 Ireland.
RLI DAC Capital Framework	The framework under which the capital of RLI DAC's funds are measured, managed, monitored, and reported.
RLI DAC German Bond Sub-Fund	The RLI DAC German Bond Sub-Fund is a closed ring-fenced fund of RLI DAC, which holds the business transferred in relation to the policies written in Germany from RLMIS to RLI DAC on 7 February 2019.
RLI DAC Open Fund	The main fund of RLI DAC, which is open to new business.
RLI DAC Transfer Scheme	The Part VII Transfer Scheme that transferred the business held in the Liver Fund that was written in Ireland from RLMIS to RLI DAC with effect from 1 January 2019, as part of RLMIS's response to the UK's exit from the EU.
RLIB	Royal London Industrial Branch.
RLMIS	The Royal London Mutual Insurance Society Limited, a company limited by guarantee and not having a share capital and incorporated in England and Wales with registered number 99064, whose registered office is at 55 Gracechurch Street, London EC3V 0RL.
RLMIS Actuarial Systems	Collectively, the RLMIS Cashflow Model and the RLMIS Internal Model.
RLMIS Capital Framework	The framework under which the capital of RLMIS's funds are measured, managed, monitored, and reported.
RLMIS Cashflow Model	The actuarial model which calculates the Solvency II technical provisions for regulatory reporting purposes for RLMIS.
RLMIS Closed Funds	The Liver Fund, the PLAL Fund and the RLCIS Fund.
RLMIS Internal Model	The Internal Model developed by RLMIS (and approved by the PRA) to calculate its SCR.
RLMIS Tactical Model	The financial model built by RLMIS specifically for the Legacy Simplification Project to calculate the Offer Uplift percentage.
RLOB	Royal London Ordinary Branch.
Royal Liver	Royal Liver Assurance Limited.
Royal Liver PPFM	The PPFM pursuant to which with-profits business invested in the Liver Fund is managed.
SAI	The Society of Actuaries in Ireland.
Sanction Hearing	A Court hearing at which RLMIS / RLI DAC will request that the relevant Court sanctions the relevant Scheme once the Schemes has been approved by the requisite majority of the relevant Eligible Policyholders.
Scheme	The Liver Ireland Scheme.
Scheme Contribution	A deduction made from the Liver Fund Estate under the UK Scheme. The Scheme Contribution comprises the CFC, the Project Costs Allowance and the Premium Uplift Contribution.
Scheme Implementation Conditions	The conditions that need to be met for the Schemes to be implemented, as set out in paragraph 5.45 of this Report.
Scheme Meeting	The meeting at which Eligible Policyholders can vote on the Scheme.
Schemes	The Liver Ireland Scheme and the UK Scheme.
SCR	Solvency Capital Requirement. One of the regulatory capital requirements under Solvency II. Intended to represent the amount required to ensure that an insurer's assets continue to exceed its liabilities over a one-year time frame with a probability of 99.5%.
SL	Scottish Life.
SL Fund	The Scottish Life Fund, a closed ring-fenced fund of RLMIS which holds the SL business transferred on 1 July 2001 and was consolidated into the RL Open Fund on 31 December 2021.
SMA	Scottish Mutual Assurance Limited, the business of which was transferred to RLMIS in 2008.
SOA	Scheme of Arrangement. A compromise or arrangement between a company and its creditors (for the proposed Schemes, these creditors are the Eligible Policyholders).

Solvency II	The regulatory regime for insurers which came into force on 1 January 2016 aimed at harmonising insurance regulation across all EEA countries.
SPL	Scottish Provident Limited, the business of which was transferred to RLMIS in 2008.
SRD	Selected Retirement Date for a pensions policy.
Standard Formula	A standardised calculation method for determining the SCR. Insurers are required to calculate their SCR using either the Standard Formula or an approved Internal Model
Supplementary Report	The follow-up report written by the Independent Expert and presented at the Sanction Hearing.
Technical provisions	The value of the insurance liabilities of an insurer, as determined for regulatory purposes. Under Solvency II, the Technical Provisions comprise the BEL and the Risk Margin.
TMTF	Transitional Measures on Technical Provisions. Insurers are permitted to apply to their regulator (the PRA in the UK) to make use of the TMTF, which allows firms to phase in the increase in Technical Provisions under UK Solvency II Pillar 1 (in relation to business written prior to 1 January 2016) over a sixteen-year period.
UFIB	United Friendly Industrial Branch.
UFIB Sub-Fund	The United Friendly IB Sub-fund, a closed ring-fenced fund of RLMIS which holds the UFIB business transferred on 1 January 2001 and was consolidated into the RL Open Fund on 31 December 2021.
UFOB	United Friendly Ordinary Branch.
UFOB Sub-Fund	The United Friendly OB Sub-fund, a closed ring-fenced fund of RLMIS which holds the UFOB business transferred on 1 January 2001 and was consolidated into the RL Open Fund on 31 December 2021.
UK	The United Kingdom of Great Britain and Northern Ireland.
UK Eligible Policy	Policies of RLMIS that are eligible for the UK Offer, as defined in paragraph 5.25 of this Report.
UK Eligible Policyholder	Any person who is a creditor for the purposes of the Companies Act in respect of a UK Eligible Policy.
UK Excluded Policy	Policies of the Liver Fund that are not eligible for the UK Offer, as defined in paragraph 5.26 of this Report.
UK Excluded Policyholder	Holder of an UK Excluded Policy.
UK HITM Policy	A HITM Policy in the Liver Fund.
UK Included Policy	Policies of RLMIS that are eligible for the UK Offer and remain in-force at the Implementation Date, as defined in paragraph 5.28 of this Report.
UK Included Policyholder	Any person who is a creditor for the purposes of the Companies Act in respect of a UK Included Policy.
UK Independent Expert	Mr Nick Dumbreck, a Fellow of the Institute of Actuaries in the UK and a Principal with Milliman LLP, a firm of actuaries and consultants in the UK. Mr Dumbreck is the Independent Expert for the UK Scheme.
UK Offer	The offer that RLMIS is making to UK Eligible Policyholders regarding the terms of the UK Scheme.
UK Regulators	The PRA and the FCA.
UK Scheme	A scheme of arrangement in the UK, concurrent with the Ireland Scheme and pursuant to Part 26 of the Companies Act 2006, the purpose of which is to enable the consolidation of the Liver Fund into the RL Open Fund, which would be presented to the English High Court for sanction.
UK Solvency II	The Solvency II regime applied to UK insurers until 31 December 2020, which was the end of the transition period agreed following the UK's exit from the EU (and the EEA). Since 1 January 2021 the UK has been free to determine an appropriate regulatory regime for insurance companies, which is referred to in this Report as UK Solvency II.
Unclaimed Assets	Any assets that are not expected to be claimed by policyholders in the future.
URM	Uniform Return Method. It is used to calculate the return that is allocated to UK and Ireland policyholders' asset shares in a consistent manner.



UWP	Unitised With-Profits. UWP business typically refers to policies where policyholders' premiums are used to buy units whose value is then increased through bonuses that are awarded at the discretion of the insurer, again depending on the surplus emerging in the relevant insurance fund. At maturity, policyholders typically receive the value of their units, which again may be adjusted by a final bonus amount or a Market Value Reduction.
Voting Class	A sufficiently homogeneous class of creditors such that the rights of all creditors against RLMIS or RLI DAC within a particular class are sufficiently similar: (i) compared with the rights of other creditors within the same class and (ii) in terms of the impact of the Schemes on such rights.
Voting Pack	After the court orders are granted, Eligible Policyholders will be sent or otherwise provided with a letter, a booklet which sets out key aspects of the proposed Schemes, a personalised illustration and a decision form that allows the individual policyholder to vote on the Schemes (together the Voting Pack).
Vote Value	The weighting attached to an Eligible Policyholder's vote used in assessing the vote result. The Vote Values are set out in paragraph 6.20 of this Report.
WPA	With-Profits Actuary. A regulated role in the UK with a responsibility for advising a firm's Board on the key areas of discretion exercised in managing its with-profits business.
WPC	With-Profits Committee. The role of the WPC is to act in an advisory capacity to a firm's Board on decisions affecting with-profits policyholders, to ensure the interests of with-profits policyholders are appropriately considered within a firm's governance structures.
WPOP	The With-Profits Operating Principles pursuant to which with-profits business invested in a with-profits fund is managed in Ireland.

## 19 APPENDIX C: OVERVIEW OF THE REGULATORY REGIME FOR INSURERS

### Introduction

- 19.1 RLMIS is a UK-authorized insurer and RLI DAC is an Irish-authorized insurer. However, although authorized and regulated in two different countries, when it comes to prudential regulation both companies are subject to very similar regulatory regimes as both countries adopted the EU-wide Solvency II regime in 2016 (at which time the UK was still a Member State of the EU).
- 19.2 The Solvency II regime applied to UK insurers until 31 December 2020, which was the end of the transition period agreed following the UK's exit from the EU (and the EEA). Since 1 January 2021 the UK has been free to determine an appropriate regulatory regime for insurance companies, which is referred to in this Report as "UK Solvency II". A limited number of changes have been made to date to the Solvency II regime as it is applied to the UK, including a change to the yield curves used to discount the components of the Solvency II balance sheet, which came into force during 2021.
- 19.3 The UK Government published a full consultation document on proposed UK reforms to Solvency II in April 2022, and the PRA published a statement in response and an accompanying discussion paper setting out the PRA's views on key aspects of the consultation. The proposed reforms include a substantial reduction in the Risk Margin and a change to the treatment of credit risk in the matching adjustment.
- 19.4 In contrast with the situation that pertains to prudential regulation, the regulation and supervision of conduct of business risk depends largely on the rules in the territory where the insurer has written the business in question.

### Prudential regulation

- 19.5 Solvency II is the name given to the prudential regime for insurers (and reinsurers) across the European Union ("EU"). Introduced in 2016, it is based on the following so-called three pillar approach:
- Pillar 1: Quantitative requirements.
  - Pillar 2: Governance and risk management.
  - Pillar 3: Supervisory reporting and public disclosure.
- 19.6 Taken together, the three pillars are intended to form a coherent overall approach which incentivises the understanding and management of risks across the insurance sector.
- 19.7 Some of the key features of the Solvency II regulatory framework are:
- Risk-based: Higher risks will lead to higher capital requirements to cover for unexpected losses. Appropriate credit is given for risk mitigation strategies through reduced capital requirements.
  - Market consistent: Assets and liabilities are valued at market value (or a proxy if no direct market price exists).
  - Proportionate: The requirements are intended to be applied in a way that is proportionate to the nature, scale and complexity of the risks inherent in an insurer's business.
- 19.8 The EU Solvency II Directive was implemented in national law in both Ireland and the UK (as well as all other EU Member States), supplemented by EU-wide Delegated Regulations and additional requirements and guidelines issued by national regulators.
- 19.9 In the following paragraphs, I provide a summary of the main relevant features of the Solvency II framework. The descriptions and explanations are necessarily high-level in places and should not be taken as exhaustive. They should, however, help to introduce some of the concepts that I refer to in this Report – in particular when discussing the financial condition of the two companies.

### PILLAR 1

- 19.10 Pillar 1 sets out the rules for the valuation of insurers' assets and liabilities and the rules for determining the risk-based capital requirements.
- 19.11 In summary, the Solvency II Regulations require insurers to value their assets and liabilities at market value, but in most cases liabilities to policyholders are determined on a best estimate basis with the addition of an explicit Risk Margin, reflecting the lack of a market "price" for insurance liabilities. The policyholder liabilities are valued using

best-estimate assumptions, with the projected future cash-flows discounted using risk-free rates (with some adjustments).

- 19.12 Together, the BEL and Risk Margin form the technical provisions which sit on the liability side of the Solvency II balance sheet. To the extent that any business is outwardly reinsured, there will be an offset to the BEL which sits on the asset side of the balance sheet. The terms “net” and “gross” are sometimes used in the context of the BEL or technical provisions to denote the position with or without allowance for reinsurance respectively.
- 19.13 The Solvency II balance sheet provides the measure of the amount by which an insurer’s assets exceed its liabilities (termed the insurer’s “**own funds**”). There can be some further adjustments needed to arrive at the “eligible own funds”, which are the own funds eligible to be counted towards meeting the regulatory capital requirements.
- 19.14 The eligible own funds are then compared with a regulatory capital requirement termed the SCR, which is a risk-based capital requirement, intended to represent the amount of capital that an insurer needs to hold to ensure that it will still be solvent (i.e. that its assets will exceed its liabilities, measured according to Solvency II valuation rules) in one year’s time with a probability of at least 99.5%. Insurance companies must therefore ensure that they have sufficient available capital resources (i.e. “eligible own funds”) to cover the SCR.
- 19.15 The SCR must cover a prescribed list of various types of risk:
  - underwriting risks (life / non-life / health);
  - (financial) market risks;
  - counterparty default risk; and,
  - operational risk.
- 19.16 Insurers may calculate their SCR using standard prescribed stress tests or factors for the various types of risk, which are then aggregated using prescribed correlation matrices. This approach is known as the Standard Formula. Alternatively, the SCR may be calculated using an Internal Model, which is based on the insurer’s internally-derived assessment of appropriate capital requirements, provided it has first been approved by the insurer’s regulator and, in doing so, must meet a number of prescribed standards.
- 19.17 The benefits of risk mitigation techniques (e.g. reinsurance of underwriting risks; hedging of market risks) can be recognised in the calculation of the SCR, subject to certain conditions being met.
- 19.18 RLMIS uses an Internal Model, whereas RLI DAC uses the Standard Formula approach, when determining their respective SCRs.
- 19.19 In addition to the SCR as described above, there is also a second, lower, level of regulatory capital requirement under Solvency II, known as the Minimum Capital Requirement (“**MCR**”) which is intended to represent the amount of capital required to ensure continued solvency in one year’s time with a probability of at least 85%.
- 19.20 The two capital requirements – SCR and MCR – define two rungs on the so-called “ladder of supervisory intervention”, under which increasingly severe actions will be taken by an insurer’s regulator if its level of available capital falls below the SCR (the first point of regulatory intervention)<sup>6</sup> and approaches the MCR. The MCR is the ultimate point of supervisory intervention, below which the company would lose its authorisation.

## PILLAR 2

- 19.21 In addition, under Pillar 2, insurers are required to adopt risk management policies, capital management policies, and risk appetite statements (amongst other things), all of which aim to contribute to effective risk and capital management.
- 19.22 Furthermore, every insurer is required to conduct an Own Risk and Solvency Assessment on at least an annual basis and to report the findings to the Board and the supervisory authority. An Own Risk and Solvency Assessment must also be carried out whenever there is a material change in risk profile.

## PILLAR 3

- 19.23 Pillar 3 imposes reporting requirements on insurers – both private reporting to the supervisor and public reporting.

<sup>6</sup> Although, legally, the supervisory authorities can only first intervene when an insurer’s available capital falls below the level of its SCR (i.e. an SCR coverage ratio of less than 100%), in practice supervisors expect insurers to manage their businesses to a higher level of coverage.

- 19.24 The private reporting to the supervisor includes quarterly financial and other quantitative information, which is provided in defined formats (termed Quantitative Reporting Templates or “**QRTs**”), as well as a more comprehensive suite of annual QRTs and a periodic narrative report (the Regular Supervisory Report).
- 19.25 In terms of public reporting, every insurer is also required to publish detailed information on its recent performance and solvency position in its annual Solvency and Financial Condition Report, which also includes a subset of the annual QRTs.

#### **Conduct of business regulation**

- 19.26 As noted above, when it comes to the regulation and supervision of conduct of business matters, these are largely the domain of the territory in which the business is written. The relevant conduct of business regulations vary from one territory to the next but both RLMIS and RLI DAC are required to comply with them on a territory-by-territory basis.

## 20 APPENDIX D: CERTIFICATE

**Certificate under Clause 44.2 of the RLI DAC Transfer Scheme under which part of the long-term business of RLMIS was transferred to RLI DAC under Part VII of the Financial Services and Markets Act 2000 as sanctioned by the English High Court on 7 February 2019.**

I certify that, in my opinion, the proposed amendments to the RLI DAC Transfer Scheme will not materially adversely affect the security or reasonable expectations of the holders of policies allocated to the Liver Ireland Sub-Fund. In coming to this opinion I have taken account of the proposals as a whole and their impact on holders of policies in the Liver Ireland Sub-Fund as a whole.

I note that Clause 44.2 requires the independent actuary to additionally consider:

1. The holders of policies allocated to the Liver Fund of RLMIS, if the RLMIS Board considers that the amendments may materially adversely affect the security or materially adversely affect the reasonable expectations of the holders of policies allocated to the Liver Fund, or adversely impact on RLMIS's rights and obligations under the LRA; and/or
2. The holders of policies allocated to the RL Open Fund of RLMIS, if the RLMIS Board considers that the amendments may materially adversely affect the security or materially adversely affect the reasonable expectations of the holders of policies allocated to the RL Open Fund, or adversely impact on RLMIS's rights and obligations under the German Bond Reinsurance Agreement.

RLMIS has confirmed to me that the RLMIS Board does not consider that the conditions listed above apply, and so I have not considered the impact of the proposed amendments to the RLI DAC Transfer Scheme on the holders of policies allocated to the Liver Fund or the RL Open Fund of RLMIS.



Michael Culligan

Independent Expert appointed by RLI DAC

10 June 2022