Milliman Client Report

The Part VII transfer of some of the business of The Prudential Assurance Company Limited to Prudential International Assurance Plc

The report of the Independent Expert

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1 INTRODUCTION

Background to the firms involved in the proposed transfer

1.1 Prudential plc is an international financial services group with operations principally in Asia, Europe (predominantly the United Kingdom (the "UK")), the United States and Africa and is the holding company of the Prudential group. Prudential plc's European operations are currently split across two companies:

- The Prudential Assurance Company Limited ("PAC"). PAC is a proprietary company domiciled and authorised in the UK whose shares are wholly owned by Prudential plc and whose principal activity is the transaction of long-term business (although PAC also conducts some general insurance business).
- Prudential International Assurance plc ("PIA"). PIA is a proprietary company domiciled and authorised in the Republic of Ireland ("Ireland") whose shares are wholly owned by PAC and whose principal activity is the transaction of long-term business.

1.2 Firms authorised in a member state of the European Economic Area ("EEA") are currently permitted to apply for a 'passport' to provide financial products or services in another country in the EEA without the need to apply for authorisation in each EEA country. Passporting rights allow firms to:

- Establish a branch in an EEA state (an 'establishment' or 'branch' passport); and/or
- Provide cross-border services (a 'services' passport).

1.3 As member states of the European Union ("EU") both the UK and Ireland are members of the EEA and therefore insurers based in these countries can take advantage of the EEA passporting regime.

The EU referendum result – "Brexit"

1.4 In a referendum held in the UK on 23 June 2016, a majority voted for the UK to leave the EU. The subsequent triggering by the UK government of Article 50 of the Treaty on European Union in March 2017 means that as things stand the UK is currently scheduled to leave the EU in March 2019.

1.5 The exit of the UK from the EU could lead to considerable disruption in the market for financial services across Europe and in particular for UK and non-UK companies relying on passporting rights to write business via the EU's freedom of establishment or freedom of service rules into the rest of the EEA or the UK respectively.

1.6 At the time of writing this report, there remains considerable uncertainty as to when the UK will leave the EU and around exactly what form that exit might ultimately take. Therefore I have, in my analysis in this report, made no assumptions about the possible consequences of the UK leaving the EU, but have focussed on the implications of the implementation of the Scheme for the policyholders of PIA and PAC. Therefore if, for whatever reason, the UK's exit from the EU is delayed or cancelled, the analysis contained in this report and the conclusions reached should remain valid. Put another way, the conclusions in this report are independent of whether the UK leaves the EU and of what formal relationships and arrangements may be in place in the event of the UK leaving the EU.

The purpose of this report

1.7 Under UK law a transfer of long-term business must be carried out in accordance with Part VII of the Financial Services and Markets Act 2000 ("FSMA") and an application must be made to the High Court of Justice of England and Wales (the "Court") for approval under Section 111 of FSMA.

1.8 Under Section 109 of FSMA the application to Court for approval must be accompanied by a report (the "Scheme Report") by an Independent Expert on the terms of the proposed transfer scheme.

1.9 The Scheme Report consists of this report and any subsequent supplementary reports.

My appointment as Independent Expert

1.10 I have been appointed by PAC and PIA to report, pursuant to Section 109 of FSMA, in the capacity of the Independent Expert, on the terms of the proposed scheme providing for the transfer to PIA of all of the long-term business of PAC written in Poland, France, Malta, Germany and Ireland.

1.11 I refer to the proposed scheme as "the Scheme" or "this Scheme" and, throughout the remainder of this report, these terms are used to cover all the proposals included in the scheme of transfer.

1.12 I am a Fellow of the Institute and Faculty of Actuaries ("IFoA") and hold certificates issued by the IFoA enabling me to act as a Chief Actuary and a With-Profits Actuary.

1.13 I am a partner of Milliman LLP ("Milliman") and I am based in its London office. I am an approved person on the Financial Services Register and I currently hold a number of Chief Actuary and With-Profits Actuary roles. I have fulfilled the role of Independent Expert in relation to a number of recent Part VII transfers that have subsequently been approved by the Court.

1.14 My appointment was approved by the Prudential Regulation Authority ("PRA") after consultation with the Financial Conduct Authority ("FCA") and was confirmed in a letter dated 13 October 2017 to Prudential plc. My terms of reference have been reviewed by the FCA and the PRA.

1.15 I submitted a statement of independence to the PRA and FCA for review before my approval. I confirm that neither I nor Milliman have or have had any direct or indirect interest in any of PAC, PIA or other related firms that could influence my independence.

1.16 As with other costs of the proposed Scheme, my fees will be borne by PAC and PIA as described in Section 7.33 of this report.

My report as Independent Expert

1.17 My report is produced for the Court to assist in its deliberations in respect of the proposed Scheme. The report and a summary will be made available to policyholders via the Prudential websites www.prudential.co.uk, www.prudential.pl, www.prudential.fr and www.prudential-international.com and the summary of my report will be included in the communications pack that is sent to the appropriate policyholders. The groups of policyholders who will receive a communications pack, and the reasons why, are set out in Section 11 of this report.

1.18 My report has been prepared in accordance with the approach and expectations of the PRA, as set out in "The Prudential Regulation Authority's approach to insurance business transfers" dated April 2015 (the "PRA Statement of Policy"), as well as Chapter 18 of the Supervision Manual ("SUP 18") contained in the FCA Handbook, and the FCA's Guidance Consultation "GC17/5: Proposed guidance on the FCA's approach to the review of Part VII insurance business transfers" dated May 2017 (the "FCA Proposed Guidance").

1.19 I confirm that the comments and conclusions in this report apply to all policyholders of PAC and PIA irrespective of their place of residence and/or the jurisdiction within which the business is said to be carried on or in which their policy was issued.

My Supplementary Report

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

1.21 My Supplementary Report will be available to policyholders via the Prudential websites www.prudential.co.uk, www.prudential.pl, www.prudential.fr and www.prudential-international.com.

The parties for whom my report has been prepared

1.22 This report, and any extract or summary thereof, has been prepared particularly for the use of:

- The Court;
- The policyholders of PAC and PIA;
- The Directors and senior management of PAC;
- The Directors and senior management of PIA;
- The FCA and the PRA, and any governmental department or agency having responsibility for the regulation of insurance companies in the UK;
- The insurance regulator in Ireland: the Central Bank of Ireland (the “CBI”);
- The insurance regulator in Poland: Komisja Nadzoru Finansowego (“KNF”);
- The insurance regulator in France: Authorite Des Marches Financiers (“AMF”);
- The insurance regulator in Malta: Malta Financial Services Authority and the Financial Services Tribunal;
- The insurance regulator of Germany: Bundesanstalt fur Finanzdienstleistungsaufsicht (“BaFin”);
- The insurance regulator of any EEA country who requests a copy of the report; and
- The professional advisers of any of the above.

1.23 In accordance with the legal requirements under FSMA, copies of my report should be made available to the policyholders of PAC and PIA and to other interested parties.

Reliances and limitations

1.24 In preparing my report, I have had access to certain documentary evidence provided by PIA and PAC, the key elements of which are listed in Appendix J. I have also had access to, and discussions with, senior management of PAC and PIA. My conclusions depend on the substantial accuracy of this information and I have relied on this information without independent verification.

1.25 I have relied on the work of the external auditors (KPMG LLP) of PAC and PIA in gaining confidence in the financial information as provided in Appendices A and B of this report.

1.26 Where I have considered it appropriate I have sought legal advice from Hogan Lovells and relied upon that advice and this is set out in Section 4 of this report.

1.27 PAC and PIA have been separately advised by their own legal adviser, Slaughter and May, and in respect of certain matters I have reviewed the legal advice provided by Slaughter and May and have relied on that advice to reach my conclusions on the basis set out in Section 4. I have described in Section 4 why I thought it reasonable to use that advice in that way. For the avoidance of doubt, Slaughter and May has no liability to me in respect of that advice.

1.28 This report must be considered in its entirety as individual sections, if considered in isolation, may be misleading. Draft versions of this report should not be relied upon for any purpose. I have provided a summary of my report for inclusion in various communications with the policyholders (and, where relevant, distribution to any persons requesting a copy of it). Any other purported summary of my report or elements within my report should not be treated as having been approved or authorised by me.

1.29 This report has been prepared for the Court on a basis agreed with the PRA and FCA and must not be relied upon for any other purpose. No liability will be accepted by Milliman, or me, for any application of my report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of the report. In particular, no liability will be accepted by Milliman or me under the terms of the Contracts (Rights of Third Parties) Act 1999.

1.30 There are no documents or other information that I have requested and that have not been provided. Appendix J contains a list of the data upon which I have relied.

1.31 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Scheme and in preparing my report, but that nonetheless should be drawn to the attention of policyholders in their consideration of the terms of the Scheme.

Regulatory and professional guidance

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

1.33 Actuarial Profession Standard ("APS") X2, as issued by the IFoA, requires members to consider whether their work requires an independent peer review.

1.34 In my view this report does require independent peer review and, as the proposed Scheme involves the transfer of long-term business from the UK to Ireland, this report has been peer reviewed by another partner of Milliman LLP with appropriate experience of the UK insurance market and by a senior principal of Milliman in Ireland with appropriate experience of the Irish insurance market.

2 EXECUTIVE SUMMARY

Introduction

2.1 PAC is a proprietary company, whose shares are wholly owned by Prudential plc (an international financial services group) and whose principal activity is long-term insurance business.

2.2 As at 31 December 2017, PAC had over £229 billion of assets under management and over 6.5 million policyholders.

2.3 PAC currently has long-term business across Europe (in addition to its business in the UK):

- Poland: This business is written under a freedom of establishment passport in the PAC Poland Branch.
- France: This business was written under a freedom of establishment passport. The PAC France Branch closed to new business in 2003 but remains open.
- Malta: This business was written by PAC in the PAC Malta Branch whilst operating with authorisation as a third country insurance undertaking in Malta and is currently serviced under a freedom of services passport. The PAC Malta Branch was closed to new business in 1982 but remains open.
- Germany and Ireland: This business was written by the German and Irish branches of The Equitable Life Assurance Society ("ELAS") and was transferred in to PAC in 2007 via a Part VII transfer. It is serviced under a freedom of services passport.

2.4 PIA is a proprietary company, domiciled and authorised in Ireland whose shares are wholly owned by PAC, and whose principal activity is long-term insurance business. PIA has a branch in the UK established in 2014 under the EEA Passporting regime (the "PIA UK Branch").

2.5 As at 31 December 2017, PIA had over £6.5 billion of assets under management and 47,692 policyholders.

2.6 PIA currently has two lines of business:

- Single premium 'off-shore' bonds written through PIA and sold to UK nationals in the UK and Europe which include a with-profits option (if selected by the policyholder) where returns are provided through a reinsurance arrangement with the PAC with-profits funds.
- Single premium 'on-shore' bonds written through the PIA UK Branch to high net worth UK nationals and non-UK nationals seeking the tax and estate planning advantages offered by an on-shore bond.

The proposed Scheme

2.7 In order to allow more efficient operation and to simplify the management of its long-term business across Europe, Prudential plc wishes to consolidate all of its long-term business written in Europe (excluding the UK) into one entity: PIA. Although not a primary motivation, the transfer has been structured so as to ensure that the PAC policies written through establishments in Europe (excluding the UK) can continue lawfully to be administered and serviced in the event that the UK were to leave the EU.

2.8 If the proposed Scheme were to be implemented, the existing PAC long-term business in Poland, France, Malta, Ireland and Germany would be transferred to PIA. This business is collectively known as the "transferring policies" or the "transferring business".

2.9 The total policyholder liabilities proposed to be transferred, amounted to £74 million (as at 31 December 2017, excluding the negative liabilities for Poland).

2.10 With the exception of the PAC Poland business all of the transferring blocks of business are now closed to new business.

2.11 The transfer is expected to be presented to the Court for its Directions Hearing on 9 July 2018 and for a Final Hearing on 11 December 2018. If approved by the Court, the Scheme would become operative on 1 January 2019 (the "Transfer Date").

My considerations with respect to the proposed Scheme

2.12 The key points to consider in respect of each group of policyholders affected by the proposed Scheme are the likely changes (if any) to the following as a result of the implementation of the proposed Scheme:

- **The security of benefits under the policies.**

  This is derived from the financial strength available to provide security for the benefits for each group of policies under the appropriate risk appetite statements and the applicable capital policy and includes the strength provided by the reinsurance arrangements and by the support from the parent company (where relevant).

- **The regulatory regime to which the policies will be subject.**

- **The profile of risks to which the policies are exposed.**

- **The reasonable expectations of the policyholders in respect of their benefits.**

  This includes the likely effects of the Scheme on the standards of administration, service, management and governance applied to each group of policies.

2.13 In my report I consider the effects of the proposed Scheme on the transferring PAC policies in Section 8, on the PIA policies in Section 9, and on the non-transferring PAC policies in Section 10, and I summarise these sections below.

The effects of the proposed Scheme on the transferring policies

The effects of the Scheme on the security of benefits under the transferring policies

2.14 Currently, the transferring policies derive their security of benefits from being part of PAC and the associated financial strength under the PAC risk appetite statements, the strength of PAC's reinsurance arrangements and support provided to PAC from the parent (Prudential plc). In addition, the transferring policyholders are currently protected under the UK's statutory 'fund of last resort' the Financial Services Compensation Scheme (the "FSCS"). In the event that PAC were to become insolvent and unable to meet its obligations to policyholders, 100% of any benefits that would have been claimed from the insurer would be covered under the FSCS.

2.15 The implementation of the proposed Scheme would mean that PAC would cease to have a defined contractual obligation under the transferring policies and that these obligations would be transferred to PIA. As the analysis in Section 8 shows, if the Scheme were to be implemented I am satisfied that:

- There would be no material adverse effect on the security of benefits due to the reliance on the financial strength of PIA (rather than PAC) and the associated risk appetite statements;

- The reinsurance arrangements in place would provide security of benefits by placing contractual obligations on PAC and Swiss Re (the reinsurers of PIA's business if the Scheme were to be implemented) and the termination conditions set out in the reinsurance arrangements mean that policyholders' security would be protected in the event of a subsequent termination of the reinsurance arrangement; and

- Considerable security is derived from having PAC as PIA's parent as in all but the most extreme scenarios PAC would provide support to PIA if and when required.

2.16 If the Scheme were to be implemented, it is likely (although not certain) that the transferring policies would no longer be covered under the FSCS.

2.17 Analysis has been carried out into the likelihood of a scenario where PIA would be unable to meet its obligations to policyholders and this indicates that:

- The likelihood of such a scenario occurring is less than 0.03% over a one year time horizon; and

- The main drivers of such a scenario relate to either the default of PAC in respect of its obligations under the reinsurance arrangements, or the failure of PAC to provide support as the parent of PIA, and the likelihood of these events remains low even over a 10 year time horizon.

2.18 Taking all of this together, in summary, I am satisfied that, if the Scheme were to be implemented:

- There would not be a material adverse effect on the security of the benefits of the transferring policies as a result of their being part of PIA after the Scheme rather than PAC as currently; and
- Although the implementation of the Scheme may mean that the coverage provided by the FSCS would cease, the loss of the FSCS coverage for the transferring policyholders would not lead to a material adverse effect on the security of their benefits.

The effects of the Scheme on the profile of risks to which the transferring policies are exposed

2.19 If the proposed Scheme were to be implemented, the transferring PAC policies would be directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.

2.20 Although implementation of the proposed Scheme would result in a change to the risk exposures of the transferring policies, the types of risk exposures are likely to be similar and it should be noted that:

- The Solvency II regime has been implemented consistently across the UK and Ireland;
- The Solvency Capital Requirement (the “SCR”) calculated in accordance with the Solvency II regime will reflect the risk exposures of the relevant company;
- The capital held in PIA comfortably exceeds the required SCR; and
- The capital held in PIA exceeds the level required under the PIA risk appetite statement (the “PIA RA Statement”).

2.21 I am satisfied that any change in risk profile would not have a material adverse effect on the security of the benefits of the transferring policies.

The effect of the Scheme on the benefit expectations of the transferring policyholders

2.22 If the proposed Scheme were to be implemented, there would be no change to the following:

- The terms and conditions of the transferring policies (except that the policies would become policies of PIA);
- The charges that apply to the transferring policies;
- The operation of the PAC with-profits funds;
- The PAC with-profits fund (the PAC WPSF or the PAC DCPSF) upon which any transferring policy depends for its benefits;
- The derivation of the bonuses granted to, or any Market Value Reduction (“MVR”) to be applied to, the transferring with-profits policies;
- The range of funds to which the transferring unit-linked policies would have access;
- The management of the unit-linked funds in respect of investment objectives, charges taken, the tax charged to the unit funds, and unit pricing; or
- The number of or type of units held by the transferring policyholders as a result of the implementation of the proposed Scheme.

2.23 If the proposed Scheme were to be implemented, reinsurance arrangements would be set up between PIA and PAC in respect of the transferring with-profits business and these reinsurance arrangements would ensure that the transferring with-profits policies would not be treated any differently to the other policies in the PAC with-profits funds and that the declared bonuses and any MVRs will remain subject to the governance and oversight of the PAC With-Profits Actuary (“WPA”) and the PAC With-Profits Committee (“WPC”).

2.24 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the benefit expectations of the transferring with-profits policies.

2.25 The transferring unit-linked and non-profit business is currently subject to the management and governance of PAC and would, if the Scheme is implemented, be subject to the management and governance of PIA and I am satisfied that the PIA Board has relevant experience and expertise in managing the types of business that make up the transferring unit-linked and non-profit business and that PIA's governance and management guidelines are materially similar to those of PAC.

2.26 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the benefit expectations of the transferring unit-linked and non-profit policies.

2.27 Although the administration and servicing of the transferring policies would be outsourced, under CBI rules, PIA will retain ultimate responsibility for the administration and servicing of the transferring policies.

2.28 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the benefit expectations of the transferring policyholders or on the levels and standards of administration and service that would apply to the transferring policies.

The effects of the proposed Scheme on the existing policies of PIA

The effect of the Scheme on the security of benefits of the existing PIA policies

2.29 As at 31 December 2017 the transferring business consisted of approximately 47,000 policies and £74 million of liabilities and PIA had 47,692 policyholders and over £6.5 billion of assets under management. Therefore at under 1.2% (by liabilities as at 31 December 2017), the business being transferred in to PIA is small compared to the existing business of PIA.

2.30 If the Scheme were to be implemented, the existing PIA policies would continue to be policies of PIA and there would be no change to the structure of PIA, the Solvency II regime, the calculation of the technical provisions and SCR for PIA, or to the PIA risk appetite.

2.31 I am satisfied that the implementation of the proposed Scheme would not lead to a material adverse effect on the security of benefits for the existing PIA policies.

The effect of the Scheme on the profile of risks to which the existing PIA policies are exposed

2.32 If the Scheme were to be implemented, the range of risks to which the existing PIA business would be exposed would change. However it should be noted that the business being transferred in to PIA is small compared to the existing business of PIA, the SCR of PIA would reflect the risk exposures of PIA in accordance with Solvency II, and the risk exposure of PIA would be less concentrated than currently.

2.33 I am satisfied that the change in the profile of risks to which the existing PIA policies are exposed would not have a material adverse effect on the security of the benefits of the existing PIA policies.

The effect of the Scheme on the expectations of the existing PIA policyholders in respect of their benefits

2.34 If the Scheme were to be implemented, there would be no change to the terms and conditions, the governance, the management, the administration, the servicing, or the investment management of the existing PIA policies.

2.35 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable benefit expectations of the existing PIA policyholders or on the standards of administration, service, management and governance that apply to the existing PIA business.

The effects of the proposed Scheme on the non-transferring policies of PAC

The effect of the Scheme on the security of benefits of the non-transferring PAC policies

2.36 As at 31 December 2017, the transferring business consisted of approximately 47,000 policies and £74 million of liabilities and PAC had over 6.5 million policyholders and over £229 billion of assets under management and therefore the business to be transferred out is, at less than 0.05% of the total liabilities, immaterial in the context of the PAC business.

2.37 I am satisfied that the transfer would have no material effect on the security of the remaining business of PAC.

The effect of the Scheme on the profile of risks to which the non-transferring PAC business is exposed

2.38 I am satisfied that the transfer out of less than 0.05% of the liabilities of PAC would not have a material adverse effect on the profile of risks to which the non-transferring PAC policies are exposed.

The effect of the Scheme on the expectations of the non-transferring PAC policyholders in respect of their benefits

2.39 If the Scheme were to be implemented, there would be no change to the terms and conditions, the governance, the management, the administration, the servicing, or the investment management of the non-transferring PAC policies.

2.40 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable benefit expectations of the non-transferring PAC policyholders or on the standards of administration, service, management and governance that apply to the non-transferring PAC business.

The fair treatment of policyholders

2.41 PAC intends to seek waivers from the regulatory requirements to send a written notice to the policyholders of PAC that would not be transferred under the Scheme on the basis that the cost of such a mailing would be disproportionate relative to the benefits to the non-transferring policyholders of PAC.

2.42 I am satisfied that the proposed approach to communication with policyholders, including the application for the waiver, is fair and reasonable, and that the information contained in the notification to policyholders adequately describes the proposals to policyholders.

2.43 The costs of the Scheme would be split between PAC and PIA, with the costs allocated to PAC being divided between the shareholders and the with-profits funds. As the primary motivation for the Scheme is to simplify the management and increase the operational efficiency in respect of the non-UK European operations of Prudential plc and any efficiencies and reductions in ongoing costs would reduce the costs charged to the with-profits funds, I am satisfied that it is reasonable to charge some of the Scheme costs to the PAC with-profits funds and I am satisfied that the approach of PIA and PAC to the allocation of the costs of the Scheme is reasonable.

My other considerations arising from the scheme

The exit of the UK from the EU – "Brexit"

2.44 The exit of the UK from the EU could lead to considerable disruption in the market for financial services across Europe and there remains considerable uncertainty as to exactly what form exit might ultimately take.

2.45 That said, if the Scheme were to be implemented I am satisfied that, in most scenarios where the UK leaves the EU, the transferring business would be in a better position than the scenario where the UK leaves the EU and the Scheme had not been implemented.

The restructuring of Prudential plc and the sale of part of the UK annuity portfolio

2.46 In August 2017, Prudential plc announced that it was combining two businesses within the Prudential group, Prudential UK & Europe and its asset manager, M&G, to form a combined business called M&G Prudential.

2.47 In March 2018, Prudential plc announced a restructuring and a transaction with Rothesay Life plc to transfer a portion of the PAC non-profit annuity business.

2.48 As set out in Section 12 of this report, I am satisfied that neither the restructuring of Prudential plc nor the reinsurance arrangement with Rothesay will have any effect on the conclusions reached.

My conclusions

2.49 I confirm that I have considered the issues affecting the policyholders of PAC and PIA separately, as set out in Sections 8, 9, 10, 11 and 12 of this report, and that I do not consider further subdivisions (other than those in this report) to be necessary.

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

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

2.51 I am satisfied that the Scheme is equitable to all classes and generations of PIA and PAC policyholders.

3 THE INSURANCE MARKET AND REGULATORY ENVIRONMENT RELEVANT TO THE PROPOSED SCHEME

Introduction

3.1 The proposed Scheme concerns the transfer of long-term business from an insurance company (PAC) authorised and regulated in the UK to an insurance company (PIA) authorised and regulated in Ireland.

3.2 This section provides some background on the types of long-term business involved in the transfer, and the solvency and governance requirements of the regulatory regimes in the UK and Ireland. The background provided is done so in the context of this proposed Scheme and is not intended to be a complete description of the products or regulatory environment in the UK and Ireland.

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

3.3 The long-term business involved in the Scheme can be divided into the following three categories: with-profits business, unit-linked business and conventional non-profit business. There is a fuller description in Appendix C of this report but I summarise the key points below:

With-profits business

3.4 With-profits business refers to insurance business where policyholders are entitled to share in the profits of the insurer.

3.5 There are different types of with-profits policies but in general the policyholder pays premiums which usually secure a minimum level of guaranteed benefit. This benefit or policy value is increased periodically through bonuses awarded at the discretion of the insurer depending on the surplus emerging in the relevant insurance fund and, once they have been awarded, bonuses are typically guaranteed. There is often a further bonus (a final or terminal bonus) payable at maturity, death or surrender.

3.6 It is typical for insurers to target policyholder pay-outs to be relatively close to the policy's "asset share", which is a measure of the true value of the policy based on actual investment returns and expenses incurred by the fund.

Unit-linked business

3.7 Unit-linked business is principally a type of investment product where policyholders' premiums are used to buy units in investment funds. The value of the policyholder's units then moves in line with the performance of the investments in the fund. Charges are deducted from policyholders' premiums or from their units. At maturity, policyholders receive the value of their units.

Conventional non-profit business

3.8 Conventional non-profit business refers to insurance business where the benefits received by policyholders are fixed in terms of monetary amount, for example a life insurance policy that pays a fixed death benefit or a pension annuity that pays a fixed annuity amount each year whilst the policyholder is alive.

3.9 The business being transferred under the Scheme comprises a variety of long-term insurance policies and the particular product types are described below:

- With-profits business:
  - With-profits, regular premium endowments;
  - With-profits, regular premium whole of life;
  - With-profits single premium bonds; and
  - With-profits annuities.

- Unit-linked single premium bonds.
- Conventional non-profit business:
  - Standalone term assurance; and
  - Protection rider benefits.

The Solvency II regime requirements in the UK and Ireland

Introduction

3.10 The current regulatory solvency framework for the EEA insurance and reinsurance industry (from 1 January 2016 onwards) is known as Solvency II and all but the smallest EEA insurance companies are required to adhere to the Solvency II regime.

3.11 The Solvency II regime is summarised in Appendix D of this report and I bring out below some of the features of the regime that are particularly important to understand in the context of the proposed transfer.

The Solvency II capital requirements

3.12 Under Solvency II, assets are, broadly speaking, reported at market value.

3.13 A company's liabilities are called the "technical provisions" which consist of the sum of the best estimate liabilities (the "BEL") and the "risk margin":

- The BEL is a market consistent[1] value of liabilities calculated by projecting the expected future obligations of the insurer over the lifetime of the contracts using the most up-to-date financial information and the best estimate actuarial assumptions. The BEL is the present value of these projected cash-flows.
- The risk margin is an adjustment designed to bring the technical provisions up to the amount that another insurance or reinsurance undertaking would be expected to require in order to take over and meet the insurance obligations in an arm's length transaction.

3.14 The excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds. Own Funds can be thought of as the capital available in the company to cover capital requirements.

3.15 The Solvency Capital Requirement ("SCR") is intended to be the amount required to ensure that the firm's assets continue to exceed its technical provisions over a one year time frame with a probability of 99.5%.

3.16 In calculating the SCR, it is expected that most firms will use the "Standard Formula", as prescribed by the European Insurance and Occupational Pensions Authority ("EIOPA"). However, Solvency II also permits firms to use their own internal models (or a combination of a "partial internal model" and the Standard Formula) to derive the SCR. These internal models and partial internal models are subject to approval by the relevant regulator: in the UK this is the PRA and In Ireland this is the CBI.

Regulatory approvals under Solvency II

3.17 Firms intending to use an internal model instead of the Standard Formula must apply to the regulator (the PRA in the UK and the CBI in Ireland) for approval to do so.

3.18 There are other adjustments to the technical provisions that may be made such as transitional measures, a matching adjustment and a volatility adjustment and approval for these must also be sought from the appropriate regulator. These adjustments are described in detail in Appendix D.

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

Ring-fenced funds

3.19 Solvency II includes the concept of a ring-fenced fund. This refers to any arrangement where an identified set of assets and liabilities are managed as though they were a separate undertaking, meaning that there are restrictions on the extent to which surplus in the ring-fenced fund may be transferred to shareholders or used to cover losses outside the ring-fenced fund.

3.20 In the UK, many firms have set up ring-fenced funds in order to reflect the arrangements applicable to their with-profits funds (as defined under the previous regulatory regime) and the with-profits and non-profit business within the with-profits fund.

The regulation of insurance companies in the UK and Ireland

3.21 PAC is authorised by the PRA and regulated by the PRA and FCA in the UK and PIA is authorised and regulated by the CBI in Ireland.

3.22 The roles of the regulators are described in more detail in Appendix E of this report but in summary:

- In the UK:
    - The PRA is a part of the Bank of England, and is responsible for the prudential regulation and supervision in the UK of banks, building societies, credit unions, insurers and major investment firms.
    - The FCA regulates the conduct of all UK financial services firms in relation to consumer protection, market integrity and the promotion of competition in the interests of consumers.

      Although there may be circumstances in which the FCA retains a role, in general conduct of business responsibility for the policies serviced under the EU's passporting regime lies with the host state supervisors.
- In Ireland:
    - The CBI carries out the prudential regulation and supervision in Ireland of banks, building societies, credit unions, insurance intermediaries and investment firms.
    - The CBI also regulates the conduct of all financial services firms in Ireland in relation to consumer protection and conduct of business.

      As with the FCA in the UK, although there may be circumstances in which the CBI retains a role, in general conduct of business responsibility for the policies serviced under the EU's passporting regime lies with the host state supervisors.

3.23 The CBI and the PRA are aligned in their approach to prudential supervision in terms of the adherence to the Solvency II regime, adherence to the appropriate risk appetite statements, and the standards of governance required.

The governance of long-term insurers in the UK and Ireland

3.24 The governance of long-term insurers in the UK and in Ireland is set out in more detail in Appendix E of this report but in summary:

- In both the UK and Ireland, the Board of Directors of a proprietary long-term insurer is the firm's governing body, and is ultimately responsible for setting the strategic direction of the firm, overseeing the activities of the firm's day-to-day management and approving the firm's financial statements.
- Under Solvency II, all insurers are required to establish the following key functions:
    - Actuarial function: This function is required, inter alia, to coordinate the calculation of technical provisions, and to ensure the appropriateness of the methodologies, underlying models and assumptions used in the calculation of technical provisions.

  - Compliance function: This function is required, inter alia, to advise the insurer on compliance with the Solvency II regulations.
  - Internal audit function: This function is required, inter alia, to evaluate the adequacy and effectiveness of the insurer's internal control system and other elements of its system of governance. The internal audit function is required to be objective and independent from the company's operational functions.
  - Risk management function: This function is required, inter alia, to facilitate the implementation of the insurer's risk management system.
- In the UK, in addition to the roles listed above, those firms with with-profits business must:
  - Appoint an actuary (or actuaries) to perform the "with-profits actuary function" (the "WPA"). This individual's responsibilities include advising the firm's management on the discretion to be exercised in respect of the with-profits business of the firm.
  - Appoint a With-Profits Committee ("WPC") (or a "with-profits advisory arrangement" if appropriate given the size, nature and complexity of the fund in question) in respect of the with-profits business. The WPC's role is to advise and provide recommendations to the firm's governing body on the management of the with-profits business, and to act as a means by which the interests of with-profits policyholders are appropriately considered within a firm's governance structures.
- In Ireland, there is no requirement for firms with with-profits business to appoint a WPC or a WPA.

A firm's risk appetite and internal capital policy

3.25 The Board of an insurer is responsible for the management of the company and for its exposure to risk. The Board will typically set out its appetite for risk in a form which references the probability that the Board is willing to accept of not being able to pay policyholder liabilities as they fall due and/or meet regulatory capital requirements.

3.26 In order to ensure that day-to-day fluctuations in markets and experience do not lead to a breach of their risk appetite and regulatory capital requirements, firms usually aim to hold more capital than strictly required to meet the regulatory minimum. The details of the target level of capital buffer are typically set out in the firm's internal capital policy.

3.27 The internal capital policy of a firm is set by and owned by the Board and describes the capital that the Board has determined should be held in the company. Changes to the internal capital policy usually require Board approval and appropriate consultation with the relevant regulator (the PRA in the UK and the CBI in Ireland).

3.28 The capital policy is typically stated in terms of the capital requirements set down by the relevant regulations. The regulatory capital requirements typically target a particular probability of remaining solvent over a certain time horizon: for example for the Solvency II regulatory regime it is a 99.5% probability of remaining solvent over a one year time horizon. By requiring additional capital to be held on top of the regulatory requirements, the capital policy increases the probability of remaining solvent over a particular timeframe and therefore increases the security of the benefits provided under the policies subject to the capital policy.

3.29 The level of capital required may also be driven by the desire of the Board to maintain a particular credit rating with external credit rating agencies.

The Financial Services Compensation Scheme ("FSCS")

3.30 The FSCS provides compensation (100% of the policyholder's entitlement) to individual holders of long-term insurance policies issued by UK insurers (after 2001) in the UK or another EEA state in the event of the insolvency of an insurer (the failure of that insurer to pay benefits). In the event of an insolvency, a call on the FSCS is covered by levies on the insurers in the UK insurance industry.

3.31 There is no equivalent or comparable compensation scheme in Ireland.

3.32 The implications for policyholders of losing the protections conferred by the FSCS as a result of the proposed transfer are covered in Section 8 of this report.

The Financial Ombudsman services in the UK and Ireland

The UK Financial Ombudsman Service ("FOS")

3.33 The FOS is an independent public body that aims to resolve disputes between individuals and UK financial services companies, and may make compensation awards in favour of policyholders. Only holders of policies that constitute business carried on in the UK are permitted to bring complaints to the FOS. The FOS may direct UK financial services companies to pay compensation up to a maximum limit of £150,000.

3.34 The 'Dispute Resolution: Complaints' ("DISP") section of the FCA Handbook sets out the jurisdiction and scope of the FOS in the UK.

The Irish Financial Services Ombudsman ("FSO")

3.35 The FSO is an independent public body that aims to resolve disputes between individuals and Irish financial services providers. Having heard the evidence in each particular case the FSO issues findings which are legally binding on both parties (subject to the right of appeal to the High Court). Holders of policies issued by Irish insurers (such as PIA) are permitted to bring complaints to the FSO. The FSO may direct financial services providers to pay compensation up to a maximum of €52,000 per annum where the subject of the complaint is an annuity, and a maximum of €500,000 for any other complaints.

3.36 The implications for policyholders of the financial ombudsman changing from the FOS to the FSO as a result of the proposed transfer are covered in Section 8 of this report.

4 THE ROLE OF THE INDEPENDENT EXPERT

Introduction

4.1 Policyholders involved in UK insurance business transfers have four main layers of protection provided by the legal and regulatory system in the UK. These layers of protection are provided by:

- The UK regulators (the PRA and the FCA) as they:
  - Approve the appointment of the Independent Expert and the form of the Scheme Report;
  - Produce their own reports on the Scheme for consideration by the Court;
  - Are entitled to appear in Court; and
  - Approve the form of the notices which are published and sent to policyholders.
- The Independent Expert. He/she produces the (publicly available) Scheme Report assessing the proposed Scheme and an updated Supplementary Report for the Final Hearing.
- The obligations placed on the companies to give notice of the proposed transfer to policyholders and other interested parties. Any person who considers they may be adversely affected by the proposed Scheme may make a representation to the Court.
- The Court. There are two Court Hearings: the Directions Hearing and the Final (or Sanctions) Hearing. The Court reviews the proposed Scheme at the Final Hearing where the Court also takes into account the views of the regulators, the Independent Expert, various statements by the parties to the transfer, and any objections raised by policyholders and other interested parties.

4.2 My role as Independent Expert, as the second layer of protection for policyholders described above, is to assess the proposed Scheme and to report on this via the Scheme Report (this report and any supplemental reports) to the Court. I set out below my significant areas of consideration in discharging this role.

The considerations of the Independent Expert

The regulatory requirements in respect of my role

4.3 The requirements in respect of my Scheme Report are set out in the PRA Statement of Policy (paragraphs 2.27 to 2.40) and paragraphs 31 to 41 of section 2 of SUP 18, and my report complies with these documents.

4.4 In considering the proposed Scheme, the concept of treating customers fairly should be applied. From the policyholders' perspective, the successful implementation of the Scheme must be on the basis that they are treated fairly during the process and will be treated fairly in the future.

4.5 As described in Section 1 of this report, the Scheme concerns two life insurance companies: PAC and PIA. I need to consider the terms of the Scheme generally and how the different groups of policyholders of PAC and PIA and the different generations of policyholders within the different groups are likely to be affected by the implementation of the proposed Scheme. In particular I need to consider:

- The effect of the implementation of the Scheme on the security of the policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;
- The effect of the implementation of the Scheme on the reasonable benefit expectations of policyholders; and
- The effect of the implementation of the Scheme on the standards of service, administration, management and governance applicable to the policies.

4.6 My considerations in respect of each of these areas are set out in more detail below.

4.7 In this report I have not restricted my assessment of the Scheme to adverse effects.

4.8 I am only required to comment on the effects of the implementation of the proposed Scheme on policyholders who enter into contracts with PAC and PIA prior to the Transfer Date of the Scheme. I am not required to consider the effects of the Scheme on new policyholders entering into contracts after this date.

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

The security of policyholder benefits

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

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

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

4.13 The two life insurance companies involved in the Scheme have a different mix of policies and policyholders and the type of policy held by a policyholder will be a key determinant of the risks to which the policyholder is exposed. Other than this, the key determinants of the policyholders' risk exposure will be the characteristics of the company in which the policy is held such as the size of the company, the mix of different types of business, the amount and quality of capital resources available, and the internal capital policy and risk appetite of the company.

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

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

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

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

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

4.17 In particular, Evans-Lombe J. stated in Re AXA Equity & Law that "the court is concerned whether a policyholder, employee or other interested person or any group of them will be adversely affected by the scheme". He went on to state: "That individual policyholders or groups of policyholders may be adversely affected does not mean that the scheme has to be rejected by the court. The fundamental question is whether the scheme as a whole is fair as between the interests of the different classes of persons affected". The most common interpretation of these (and other relevant) statements has been that a conclusion that "no group of policyholders is materially adversely affected by the Scheme" provides a sufficient condition to conclude that the fairness of the Scheme as a whole has been demonstrated.

4.18 As Independent Expert, my assessment of the impact of the implementation of the 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.

4.19 A Scheme may have both positive and negative effects on a group of policies and the existence of detrimental effects should not necessarily imply that the Court should reject the Scheme as the positive effects may outweigh the negative effects or the negative effects may be very small.

4.20 In order to acknowledge this inherent uncertainty, and to be consistent with the statements by the Court noted above, the conclusions of the Independent Expert in relation to transfers of long-term insurance business are usually framed using a materiality threshold. If the potential impact under consideration is very unlikely to happen and does not have a significant impact, or is likely to happen but has a very small impact, then it is not considered to have a material effect on the policies.

4.21 The assessment of materiality will also take into account the nature of the potential impact so that, for example, the materiality threshold for a change that could have a direct financial impact on policyholders' benefits is likely to be lower than the materiality threshold for a change that does not have a direct financial impact.

4.22 This is the framework in which I undertake my consideration of the proposed Scheme.

Reliances of the Independent Expert on the work of others

The financial information in this report

4.23 Appendices A and B show the current and pro-forma Solvency II balance sheets (including the SCR) as at 31 December 2017 for PAC and PIA and this financial information is used in the analysis of the effects of the implementation of the proposed Scheme as set out in Sections 8, 9, 10, 11 and 12.

4.24 I have not carried out an independent review of these Solvency II results but I note that the financial information as at 31 December 2017 for PAC and for PIA has been subject to an external audit by Prudential plc's external auditors (KPMG LLP). The scope of the review by KPMG LLP is in line with the UK regulatory requirements and so the BEL is in scope, but the risk margin and the SCR are out of scope.

4.25 I understand that this audit identified no issues that would have a material adverse effect on the solvency figures that PAC or PIA have provided for inclusion in this report.

4.26 I have carried out a high level reconciliation of the pro-forma post-Scheme balance sheet as at 31 December 2017 back to the published and externally audited financial information as at 31 December 2017.

4.27 In respect of the PAC Solvency II results as at 31 December 2017:

- The SCR has been calculated using PAC's approved internal model the Prudential Group Internal Model or "PGIM";
- The PAC Solvency II results have been approved by the Chief Actuary of PAC, the PAC Audit Committee and the PAC Board; and
- The Transitional Measure on Technical Provisions ("TMTP") has been reviewed internally and signed off/approved by the chairman of the PAC Audit Committee.

4.28 In respect of the PIA Solvency II results as at 31 December 2017:

- The SCR has been calculated using the PGIM; and
- The PIA Solvency II results have been approved by the Head of Actuarial Function of PIA, the PIA Audit Committee and the PIA Board.

4.29 In March 2018 it was announced that PAC had entered into an arrangement to reinsure approximately £12 billion of liabilities (as at 31 December 2017) to Rothesay Life Plc ("Rothesay").

4.30 The financial information in Appendices A and B includes the position of PAC before and after this reinsurance arrangement with Rothesay has been put in place. The analysis in this report has been carried out based on the position of PAC prior to this reinsurance arrangement being implemented for the following reasons:

- The financial information in respect of PAC prior to the implementation of the reinsurance arrangement with Rothesay has been subject to review and external audit as set out above;
- None of the business that would be transferred under the proposed Scheme is covered by the Rothesay reinsurance arrangement;
- The financial strength of PAC both before and after the Scheme is projected to be in excess of the PAC risk appetite statement with or without the impact of the Rothesay reinsurance arrangement and the PAC risk appetite statement is unchanged by the Rothesay reinsurance arrangement;
- The Rothesay reinsurance arrangement has no effect on PIA so the post Scheme position for the transferring business is unaffected by the Rothesay reinsurance arrangement; and
- The Rothesay reinsurance arrangement does not change the effect of the proposed Scheme on either PAC or PIA.

4.31 I am satisfied that carrying out my analysis on the financial information that does not include the effect of the reinsurance arrangement with Rothesay will have no effect on my conclusions.

4.32 Given the level of external audit and internal governance to which the financial information has been subject, I am satisfied that it is appropriate to rely upon these Solvency II results for the purpose of this report.

4.33 My Supplementary Report will contain financial information as at 30 June 2018 and will provide an update on the effect of the implementation of the proposed Scheme based upon these figures.

My reliance on legal advice

4.34 My report is prepared for the Court as part of the process of submission of the Scheme to the Court. I am not an expert in legal matters and hold no qualifications in UK law (insurance regulations or otherwise) and therefore rely on experts in UK insurance law in relation to a number of areas. In particular:

- I rely on a legal review of previous schemes involving PAC and PIA (as described in paragraph 12.16) to ensure that there are no provisions in previous schemes that could, in conjunction with the implementation of the proposed Scheme, result in a material adverse impact on policyholders; and
- I rely on advice given by legal experts in order to ensure that my understanding of the proposed Scheme, and my description of its relevant features in my report, is materially accurate.

4.35 Obtaining information in respect of the operation of the Scheme from the legal experts provides a sound basis from which to carry out my review and analysis using actuarial expertise.

4.36 In order to get a sound understanding of the legal effect of the Scheme I have relied upon advice produced on behalf of PAC and PIA by the legal firm retained by PAC and PIA in respect of this Scheme, namely Slaughter and May, and advice from my own legal adviser, namely Hogan Lovells. Slaughter and May has not been retained by me and Slaughter and May has no liability to anyone other than its client in respect of a particular piece of advice nor any liability for any advice that has been made available to me in order to provide me with information that I consider relevant to my assessment of the effects of the Scheme.

4.37 My reasons for this reliance are:

- Hogan Lovells and Slaughter and May are large international legal firms with a wide range of experience in UK insurance law and Part VII transfers and it is my view that they have the relevant and appropriate qualifications and knowledge of the laws and regulations governing insurance business transfers in the UK.
- The nature of the information and advice from Slaughter and May to its clients upon which I have relied is factual and in particular concerns how a particular aspect of PAC or PIA (pre or post the implementation of the proposed Scheme) works in accordance with UK law.

- Hogan Lovells has been retained by me and has confirmed its independence from PAC and PIA.

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

5 BACKGROUND INFORMATION REGARDING PAC

Introduction

5.1 PAC is a proprietary company, whose shares are wholly owned by Prudential plc.

5.2 Prudential plc is an international financial services group with operations principally in Asia, Europe (predominantly the UK), the United States and Africa and is the holding company of the Prudential group.

5.3 PAC's principal activity is long-term insurance business, although PAC also conducts some general insurance business: between 1919 and 1992 PAC wrote general insurance business in relation to which there remain some contingent liability claims. This general insurance business will not be transferring under the proposed Scheme.

5.4 PAC operates as the main insurance company in the UK and Europe business unit of the Prudential group.

5.5 As at 31 December 2017, PAC had over £229 billion of assets under management and over 6.5 million policyholders.

PAC's current fund structure

5.6 PAC currently has three ring-fenced (with-profits) funds as defined under Solvency II. These are:

- The PAC With-Profits Sub-Fund (the "PAC WPSF");
- The PAC Defined Charge Participating Sub-Fund (the "PAC DCPSF"); and
- The Scottish Amicable Insurance Fund (the "SAIF").

These are referred to collectively as the PAC with-profits funds.

5.7 Capital support arrangements exist between these ring-fenced (with-profits) funds where support is provided to funds in return for charges levied on asset shares. The capital support arrangements between these ring-fenced funds do not affect, nor are they affected by, the Scheme and therefore are not covered in detail in this report.

5.8 As set out in Section 3, under the UK's Solvency II regime, all assets not in a ring-fenced fund must be allocated to either the long-term insurance business or the general insurance business of the company, and there is no required segregation of the long-term insurance business assets between a long-term insurance fund (the "LTF") and a shareholders' fund (the "SHF").

5.9 The business outside the ring-fenced funds is called the "PAC shareholder-backed business" as the capital for such business has been provided by PAC's shareholders. PAC does maintain a division of the shareholder backed business for reporting and management purposes between the PAC Non-Profit Sub-Fund (the "PAC NPSF") and the PAC SHF.

5.10 The PAC shareholder-backed business consists of:

- The PAC long-term shareholder-backed business (the "PAC LT SH business") in the PAC NPSF;
- The PAC short-term shareholder-backed business (the "PAC general insurance business") in the PAC SHF; and
- All other assets and liabilities of PAC outside the PAC ring-fenced funds, including the wholly owned subsidiaries of PAC, in the PAC SHF:
    - Prudential Holborn Life Limited ("PHLL");
    - Prudential Hong Kong Limited ("PHKL");
    - Prudential General Insurance Hong Kong Limited (PG HKL");
    - Prudential Pensions Limited ("PPL"); and
    - PIA.

PAC's non-UK European long-term business (the transferring business)

5.11 PAC has European business that was written outside the UK. This primarily consists of business written out of:

- The PAC Poland Branch;
- The PAC France Branch;
- The PAC Malta Branch; and
- The German and Irish branches of ELAS.

The PAC Poland Branch

5.12 The PAC Poland Branch was set up in 2012 and, as at 31 December 2017, had the following approximate numbers of policies managed on a freedom of establishment basis:

- 17,889 with-profits policies;
- 13,153 non-profit policies; and
- 13,986 Affinity (non-profit) policies.

5.13 As at 31 December 2017, the with-profits business had asset shares of approximately £3 million and the non-profit business had a negative liability of approximately £21 million reflecting the fact that the expected income from the charges on this business is expected to exceed the expected outflow from expenses.

5.14 The with-profits business of the PAC Poland Branch is written in the PAC WPSF and the non-profit business is part of the PAC LT SH business written in the PAC NPSF.

5.15 The Affinity business consists of simple protection products that are sold directly (over the phone) to customers of partner firms (such as telecommunications firms).

5.16 The PAC Poland Branch is currently open to new business and sells business through the following:

- Prudential Polska Sp.z.o.o. ("Prudential Polska"). Prudential Polska acts as an agent for the PAC Poland Branch and manages the tied agency sales force. Prudential Polska is a wholly owned subsidiary of Prudential Financial Services Limited ("PFSL"), itself a wholly owned subsidiary of Prudential plc.

  As at 31 December 2017 there were 22 sales offices and 933 tied agents.
- A multi-agency channel where Prudential's products are sold alongside a variety of products from other insurers.
- A bancassurance channel via relationships with various financial intermediaries that are part of the Getin Noble Bank Group.
- An Affinity channel where simple protection products are sold directly (over the phone) to customers of partner firms (such as telecommunications firms).

5.17 The administration and servicing of the policies of the PAC Poland Branch is currently carried out by the PAC Poland Branch using employees and infrastructure based in Poland.

5.18 Prudential Polska provides administration and service support as its agents are typically the first point of contact for policyholders of business sold through this channel.

5.19 Some IT services are currently provided to the PAC Poland Branch by Prudential Global Data Services Limited ("PGDS").

5.20 The costs associated with the establishment of the PAC Poland Branch were partially met by the estate of the PAC with-profits funds and this funding is recouped by a development recovery charge ("DRC") levied on the asset shares of the PAC Poland Branch with-profits policies.

The PAC France Branch

5.21 The PAC France Branch was set up in 2000 and closed to new business in 2003 but remains open for top-ups to existing business. As at 31 December 2017, the PAC France Branch had 769 single premium bonds with liabilities of £44 million managed on a freedom of services basis. These bonds are invested in a mix of with-profits and unit-linked funds.

5.22 The with-profits business is written in the PAC DCPSF and the non-profit business is part of the PAC LT SH business written in the PAC NPSF.

5.23 The business of the PAC France Branch is currently administered by Prudential Insurance Management Services Limited ("PIMS"), a services company wholly owned by PAC and domiciled in Ireland, with the relevant services provided by Capita Life and Pensions Services (Ireland) Limited ("Capita Ireland") pursuant to an outsourcing arrangement with PIMS.

The PAC Malta business

5.24 PAC established the PAC Malta Branch in 1955 and sold business through a direct sales force. In 1982 the PAC Malta Branch closed to new business but remains open for top-ups to existing business. In 2007, the PAC Malta Branch transferred to a freedom of services basis.

5.25 As at 31 December 2017, PAC had the following numbers of policies in Malta managed on a freedom of services basis:

- 17 whole of life with-profits policies; and
- 4 non-profit whole of life policies.

5.26 The with-profits business is written in the PAC WPSF and the non-profit business is part of the PAC LT SH business written in the PAC NPSF.

5.27 The long-term PAC business in Malta is currently administered by Prudential Distribution Limited ("PDL").

The former ELAS business

5.28 ELAS wrote business through overseas branches in Germany and Ireland and this was transferred to PAC in 2007 (the "ELAS Scheme"). This business is currently managed on a freedom of services basis and, as at 31 December 2017, had the following numbers of policies:

- 439 with-profits annuity contracts written in Germany by ELAS; and
- 237 with-profits annuity contracts written in Ireland by ELAS.

5.29 The with-profits business is contained in the PAC DCPSF.

5.30 PAC does not write new business in Germany and Ireland.

5.31 This business is currently serviced and administered by Equiniti under an outsourcing agreement between PAC and Equiniti.

Previous schemes transferring long-term business into PAC

5.32 As well as the business written directly by PAC, and the business reinsured in from other PAC subsidiaries, there have been a number of transfers of long-term insurance business into PAC:

- Non-profit annuity business transferred in from Prudential Retirement Income Limited ("PRIL") on 1 October 2016.
- Non-profit annuity business transferred in from Prudential Annuities Limited ("PAL") on 1 October 2014. All of the long-term business of PAL was transferred into the PAC WPSF.

- Business transferred in from PHLL and from Prudential (AN) Limited ("PANL") on 31 October 2010. All the long-term business of PANL and PHLL was transferred to PAC.
- With-profits annuity business transferred to PAC from ELAS on 31 December 2007 which was principally allocated to the PAC DCPSF. This is mentioned later in this report and is referred to as the ELAS Scheme.
- Business transferred from Scottish Amicable Life plc ("SAL") on 31 December 2002 to PAC.
- Business transferred to PAC from Scottish Amicable Life Assurance ("SALAS") on 30 September 1997 which was principally allocated to a newly created sub-fund, the PAC SAIF.

PAC's reinsurance arrangements

5.33 PAC has a reinsurance arrangement in place with PIA under which 100% of PIA's with-profits business, including the net cost of options and guarantees, is ceded from PIA to PAC (the "PIA PAC reinsurance arrangement"). The investment content of the reinsured business is invested in the PAC DCPSF.

5.34 PAC currently has a quota share reinsurance arrangement in place with Swiss Re (the "PAC Swiss Re quota share arrangement") under which 75% of the risks of the following business of the PAC Poland Branch are ceded:

- The non-profit protection business;
- The non-profit protection riders on the with-profits business; and
- The mortality risk on the with-profits business.

5.35 PAC has other reinsurance arrangements including longevity swaps with several different counterparties that cede a material proportion (approximately £14 billion of liabilities as at 31 December 2017) of the longevity risk in respect of the annuities in the PAC NPSF, but these do not relate to the business to be transferred under the proposed Scheme.

The PAC risk appetite statements

5.36 The PAC Board is responsible for the management of PAC's exposure to risk and in particular:

- Determining PAC's risk appetite and therefore its capacity for risk.
- Managing the overall risk level of the company having regard to the capacity for risk and the internal capital policy.

5.37 The PAC risk appetite statement for its with-profits business defines the level of capital that should be held in terms of the Solvency II Pillar 1 SCR coverage ratio and the Solvency II Pillar 2 risk capital requirements coverage ratio.

5.38 The PAC risk appetite statement for its shareholder-backed business is set out in the Shareholders' Risk Appetite ("SRA") Framework and defines the level of capital that PAC is required to hold in terms of its Solvency II Pillar 1 SCR coverage ratio and its Solvency II Pillar 2 risk capital requirements coverage ratio.

5.39 The PAC SRA Framework also defines a series of thresholds as part of a Solvency Intervention Ladder. When these thresholds are breached a series of management actions are considered to restore the SRA Framework capital buffer. In addition the PAC shareholder backed business must adhere to the risk appetite requirements of the Prudential group which sets a target solvency ratio that is allowed to move in a range through the economic cycle.

5.40 In order to ensure that PAC remains within its risk capacity, the Board manages the type and volume of new business accepted and sets the bonus and investment policy of its with-profits business with regard to the available capital in PAC.

5.41 In this report I refer collectively to the risk appetite statements for with-profits business and for the shareholder backed business as the PAC risk appetite statements.

5.42 The PAC risk appetite statements are confidential and not in the public domain and PAC does not want to put the PAC risk appetite statements in the public domain and so the detail has not been included in this report.

The management of PAC's long-term insurance business

5.43 Under the UK regulations that were in force before Solvency II, UK shareholder-owned life insurance companies typically maintained a LTF and SHF in order to segregate the assets and liabilities attributable to the long-term insurance business and shareholders respectively.

5.44 Under Solvency II the requirement to maintain a separate LTF has been removed but PAC continues to maintain the PAC NPSF separately for accounting purposes to allow PAC to identify the financial resources that are allocated to support its long-term insurance business but that are not allocated to its with-profits funds. There is no legal or regulatory requirement to maintain the PAC NPSF or to separate the business formerly (under Solvency I) allocated to the PAC SHF and it should be noted that:

- There are no regulatory restrictions (such as a requirement to carry out a formal actuarial valuation) on the transfer of assets between the PAC NPSF and the PAC SHF; and
- As there is no legal or regulatory obligation for PAC to maintain this separate identification of the PAC NPSF and the PAC SHF, such a distinction could be removed without breaching any regulatory requirements.

5.45 Therefore, in my appraisal of the proposed Scheme, I can only rely upon the security provided by the fund structure required under the Solvency II regulations rather than that used in the management of the business by PAC.

The PAC Pensions Mis-selling Costs Assurance

5.46 The UK insurance regulator required all UK life insurance companies to review sales of personal pension's policies for potential mis-selling. Offers to all cases were made by 30 June 2002. Costs arising from this review are met by the excess assets of the PAC WPSF and hence have not been charged to the asset shares used in the determination of policyholder bonus rates.

5.47 PAC has given an assurance that these deductions from excess assets will not impact its bonus or investment policy for policies within the with-profits sub-funds that were in force at 31 December 2003. This assurance does not apply to new business since 1 January 2004. In the unlikely event that such deductions would affect the bonus or investment policy for the relevant policies, PAC has stated it would make available support to the sub-fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged.

Support for with-profits sub-funds by shareholders' funds

5.48 PAC is liable to meet its obligations to with-profits policyholders even if the assets of the with-profits sub-funds are insufficient to do so. The assets, represented by the unallocated surplus of the with-profits funds, in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers (the "excess assets") in the with-profits sub-funds could be materially depleted over time by, for example, a significant or sustained equity market downturn, costs of significant fundamental strategic change or a material increase in the pension mis-selling provision.

5.49 In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the ability of the Prudential group to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the with-profits sub-funds to provide financial support.

The restructuring of Prudential plc and the sale of part of the UK annuity portfolio

5.50 In August 2017, Prudential plc announced that it was combining two businesses within the Prudential group, Prudential UK & Europe and its asset manager, M&G, to form a combined business called M&G Prudential.

5.51 In March 2018, Prudential plc announced that:

- M&G Prudential would demerge from the Prudential group, resulting in two separately listed companies; and
- The legal ownership of Prudential plc's Hong Kong insurance subsidiaries would be transferred from PAC to Prudential Corporation Asia Limited ("PCA"), another subsidiary of Prudential plc, by the end of 2019.

5.52 Also in March 2018 it was announced that PAC had entered into a transaction to transfer a portion of the shareholder-backed non-profit annuity business to Rothesay. Under the terms of the agreement, approximately £12 billion of liabilities (as at 31 December 2017) are reinsured to Rothesay, through a collateralised reinsurance arrangement, with the intention that this is followed by a Part VII insurance business transfer of the business by the end of 2019.

6 BACKGROUND INFORMATION REGARDING PIA

Introduction

6.1 PIA was established in Ireland on 29 November 1993 as a private limited company and is a proprietary company, the shares of which are wholly owned by the PAC shareholder-backed business.

6.2 PIA is domiciled and authorised in Ireland and subject to the relevant requirements and guidelines of the CBI. PIA's principal activity is long-term insurance business.

6.3 As at 31 December 2017, PIA had over £6.5 billion of assets under management and 47,692 policyholders.

PIA's current fund structure

6.4 PIA does not have any ring-fenced funds.

PIA's current business

6.5 PIA is authorised by the CBI to write the following classes of long-term business:

- Class I: Life assurance and annuities.
- Class III: Contracts linked to investment funds.
- Class III with connected Class IV (PHI) features.
- Class VI: Capital redemption operations.

6.6 In October 2014, PIA established a branch in the UK under the EEA Passporting regime (the "PIA UK Branch").

6.7 PIA currently has two lines of business:

- Single premium 'off-shore' bonds written through PIA and sold to UK nationals in the UK and Europe.

  These provide a with-profits option (if selected by the policyholder) where returns are provided through a reinsurance arrangement with the PAC DCPSF.

  The majority of this business is written in the UK and there is also business in France, Spain, Malta, Cyprus, Gibraltar and the Crown Dependencies (Guernsey, the Isle of Man and Jersey).

- Single premium 'on-shore' bonds written through the PIA UK Branch to high net worth UK nationals and non-UK nationals seeking the tax and estate planning advantages offered by an on-shore bond.

  For the avoidance of doubt the PIA UK Branch business products do not have with-profits options.

6.8 PIA is currently seeking approval to set up a branch in Poland (the "PIA Poland Branch") under the EU's freedom of establishment passporting rules. Approval for this is expected to be granted by the CBI after consultation with the Polish insurance regulator (the KNF).

6.9 In November 2017, PIA formally requested additional authorisation for Class I with connected Class IV business. This is required so that PIA will be appropriately authorised to sell assurance products with Class IV (Permanent Health Insurance) features, which it intends to offer through the PIA Poland branch.

The PIA PAC reinsurance arrangement

6.10 Under the PIA PAC reinsurance arrangement, 100% of PIA's with-profits participation business, including the net cost of options and guarantees, is ceded to its parent company PAC (to the PAC DCPSF).

6.11 Policyholders under the above arrangement incur only the defined charges stated in the policy. These charges include an annual management charge on the assets held within the DCPSF. The charges accrue to PIA, which bears all of the corresponding expense subject to any additional expense costs that are disclosed at point of sale.

6.12 Bonus smoothing accounts for the reinsured business are maintained in the inherited estate within the WPSF. PIA pays an annual charge to the PAC inherited estate within the WPSF for the use of the economic capital supporting this business.

6.13 The policies subject to the PIA PAC reinsurance arrangement are subject to the PAC Principles and Practices of Financial Management ("PAC PPFM").

6.14 PIA assumes a low probability of default for the PIA PAC reinsurance arrangement due to the high credit rating of PAC, and therefore does not have any material allowance for counterparty risk in relation to this.

6.15 PIA has a 'pari passu' charge over the assets in the PAC DCPSF and PAC WPSF in respect of PAC's obligations under the reinsurance treaty. This means that in the event of insolvency PIA would rank alongside the direct insurance creditors of PAC.

Other PIA reinsurance arrangements

6.16 PIA has in place a number of outwards reinsurance arrangements:

- Swiss Re Life and Health;
- Swiss Re (UK) Ltd;
- Cologne Re (Dublin) Ltd; and
- General Re Corporation.

6.17 For PIA's unit-linked insurance lines of business which have significant death or disability benefits, PIA has in place external reinsurance covering 75% of the mortality and morbidity risks for these products.

The PIA risk appetite and capital management

6.18 The PIA Board is responsible for the governance and management of PIA and this includes setting the risk appetite for PIA and ensuring adherence to this risk appetite:

- Determining PIA's risk appetite and therefore its capacity for risk.
- Managing the overall risk level of PIA having regard to the capacity for risk and the internal capital policy.

6.19 The PIA Risk Appetite Statement (the "PIA RA Statement") includes PIA's internal capital policy and defines risk targets and risk appetite limits based on financial and non-financial requirements. The PIA risk management function monitors the level of risk exposure of PIA on an on-going basis. The PIA RA Statement sets a target operating level of required capital and a minimum level of required capital buffer. The target operating level is a percentage of the PIA SCR and the minimum operating level has been set to be the greater of a fixed nominal amount of capital and a percentage of PIA's SCR.

6.20 The Prudential group's approach to capital management is, where possible, to hold capital in excess of its subsidiaries' regulatory capital requirements at the level of Prudential plc and provide additional capital support to the subsidiaries as required.

6.21 Although PIA is a wholly owned subsidiary of PAC, there is no formal capital support arrangement in place between PAC and PIA.

6.22 In the event that the target or minimum capital buffers are breached, the Chair of the PIA Risk Committee would be informed as soon as practical by the PIA Chief Risk Officer (or in their absence the PIA Managing Director). They would consider the nature of the breach and the proposed corrective action plan. If deemed necessary, the breach would be notified to the CBI, the PIA Board, the PAC Board and to Prudential plc.

6.23 The PIA RA Statement is confidential and PIA does not want to put the PIA RA Statement in the public domain and so the detail has not been included in this report.

The administration and servicing of the PIA policies

6.24 The administration and servicing of PIA's policies is carried out by PIMS, with the relevant services provided by Capita Ireland pursuant to an outsourcing arrangement with PIMS.

Investment management

6.25 The PIA Board is responsible for setting PIA's investment strategy which it does through PIA's investment policy. The investment policy sets out the framework for the management and oversight of investment performance and investment related risk for internally and externally managed funds, both policyholder and shareholder.

6.26 Investments are made in accordance with PIA's investment policy which is set in line with its risk appetite from an investment and credit risk exposure perspective, and is reviewed annually. PIA monitors its exposures on an ongoing basis, highlighting deviations from its risk appetite through its escalation processes.

6.27 Constraints are placed on the credit quality of PIA's assets, and reserves are held to protect the company against the risk of adverse credit experience.

7 THE PROPOSED SCHEME

The motivation for the Scheme

7.1 The management of PAC and PIA have described the motivation for entering into the Scheme as to simplify the management and increase the operational efficiency in respect of the non-UK European operations of Prudential plc that are currently split across two companies: PAC and PIA. After the transfer all long-term insurance business in Europe outside of the UK would be held by PIA.

7.2 Although not a primary motivation for the Scheme, the Scheme has been designed so as to ensure that, in the event that the UK leaves the EU, Prudential plc is able to continue to:

- Service the existing policyholders of the PAC long-term business in Poland, France, Malta, Germany and Ireland; and
- Expand its business in Poland by continuing to sell new business.

7.3 With the Brexit negotiations ongoing at the time of writing this report there is uncertainty surrounding the ability of UK insurance companies like PAC to continue to write and service insurance business in other EEA member states like Poland after the UK leaves the EU.

7.4 PIA is a subsidiary of PAC and is headquartered in Ireland and therefore is not at risk of losing its passporting rights to other EEA member states as a result of the Brexit outcome.

A summary of the Scheme

7.5 If the proposed Scheme were to be implemented, all of the non-UK European long-term business of PAC written through establishments in Poland, France, Malta and the former ELAS business written in Ireland and Germany would be transferred to PIA. This consists of the following (all numbers as at 31 December 2017):

- The business written in the PAC Poland Branch:

  The 17,889 with-profits policies, 13,153 non-profit policies and 13,986 Affinity (non-profit) policies that together constitute regular premium savings policies with optional protection riders and standalone regular premium protection products would transfer to the newly authorised PIA Poland Branch and be managed on a freedom of establishment basis.

- The business written in the PAC France Branch:

  The 769 single premium bonds would transfer to PIA and be managed on a freedom of services basis.

- The PAC business written in Malta:

  The 17 whole of life with-profits policies and 4 whole of life non-profit policies would transfer to PIA and be managed on a freedom of services basis.

- The former ELAS business written by ELAS in Germany:

  The 439 with-profits annuity contracts written in Germany would transfer to PIA and be managed on a freedom of services basis.

- The former ELAS business written by ELAS in Ireland:

  The 237 with-profits annuity contracts written in Ireland would transfer to PIA and be managed under PIA's domestic Irish authorisation.

7.6 The total policyholder liabilities proposed to be transferred amounted to £74 million (as at 31 December 2017, excluding the negative liabilities for Poland).

7.7 With the exception of the PAC Poland business, all of these blocks of business are now closed to new business.

7.8 PAC will transfer assets attributable to the transferring business to PIA including:

- The asset shares and net cost of guarantees and (except in respect of the with-profits PAC Poland business, where smoothing is not applied) smoothing in respect of the transferring with-profits business.
- The Solvency II technical provisions (where positive) held by PAC in respect of any non-profits transferring business of PAC Malta or PAC Poland; and
- The aggregate face value of the units allocated to the transferring unit-linked policies of PAC France.

7.9 In respect of the bonuses and MVRs to apply to the transferring with-profits policies if the Scheme were to be implemented, the obligations of PAC and PIA are set out in the Scheme which requires that:

- PIA would declare bonuses and apply MVRs in accordance with those notified to it by PAC.
- PAC will determine the applicable bonus rates and methodology for calculating MVRs in a manner that is consistent with:
  - The terms and conditions of the transferring policies (as if they applied directly to PAC);
  - The approach PAC has taken before the implementation of the Scheme in respect of the transferred policies so that PIA would receive from PAC the same total claim amounts in respect of the transferring with-profits policies as would have been paid by PAC if the Scheme were not implemented; and
  - Any interest of the transferring policies in the estates of the relevant PAC with-profits funds.

7.10 These requirements reflect the obligations of PAC and PIA under the reinsurance arrangements that would be set up if the Scheme were to be implemented with respect to bonus and MVR declarations. These reinsurance arrangements are described below in paragraph 7.22.

7.11 Under the Scheme, the PAC Swiss Re quota share arrangement (described in Section 5) would be transferred to PIA.

7.12 The Scheme is expected to be presented to the Court for a Directions Hearing on 9 July 2018 and for a Final Hearing on 11 December 2018.

7.13 If approved by the Court, the Scheme will become operative on the Transfer Date (1 January 2019), at which point the transferring business will legally transfer from PAC to PIA.

7.14 The PAC general insurance business will not be subject to the Scheme and will remain with PAC.

7.15 There are not expected to be any policies in the blocks listed above in paragraph 7.5 that would be excluded from the transfer.

The effect of the Scheme on the reinsurance arrangements currently in place

7.16 Under the PAC Swiss Re quota share arrangement, 75% of the mortality risk in respect of the non-profit protection business of the PAC Poland Branch, and the non-profit riders and mortality risk on the with-profits business of the PAC Poland Branch, is reinsured to Swiss Re.

7.17 If the Scheme were to be implemented:

- The PAC Swiss Re quota share arrangement would be transferred to PIA with no other changes to the terms and conditions, and the corresponding reinsurance asset would be allocated to PIA; and
- Immediately after the implementation of the Scheme, the part of the arrangement in respect of the mortality risk on the with-profits business of the PAC Poland Branch would be novated back to PAC (together with the reinsurance assets in respect of mortality risk only) as the risk would remain with PAC by virtue of the reinsurance arrangements that would be in place between PIA and PAC as described below in paragraph 7.22.

7.18 The reinsurance arrangements between each of PAC and PIA and Swiss Re would continue to cover future new business written in the PIA Poland Branch in accordance with the terms of the current arrangement between PAC and Swiss Re in respect of the PAC Poland Branch business. This is not part of the Scheme as it would only impact future policyholders.

7.19 Two high value with-profit whole of life policies written by PAC in Malta are currently reinsured with Swiss Re under a separate reinsurance arrangement. If the Scheme were to be implemented the PAC Malta business would be transferred to PIA and reinsured to PAC and so this reinsurance arrangement would remain with PAC.

7.20 All other reinsurance arrangements to which PAC and/or PIA are party would remain unchanged by the implementation of the proposed Scheme.

7.21 I cover the effects of the changing reinsurance arrangements in respect of the transferring policyholders and the non-transferring policyholders of PIA and PAC in Sections 8, 9 and 10 respectively.

The reinsurance arrangements set up as a result of the Scheme

7.22 If the Scheme were to be implemented then reinsurance arrangements would be set up between PIA and PAC to replicate the economic effects of the current treatment of the transferring with-profits business and under these arrangements:

- The asset shares and net cost of guarantees and (where applicable) smoothing of the transferring with-profits business would be paid by PIA to PAC as part of the initial reinsurance premium and thereby into the relevant with-profits fund in PAC.
- The policyholder premiums paid to PIA would be passed to PAC.
- PAC would pay amounts to PIA to cover claims and the relevant expenses.
- There are limited circumstances under which the reinsurance arrangements can be terminated, namely that:
    - Performance of the reinsurance arrangements becomes illegal or otherwise impossible;
    - Either party fails to fulfil its payments obligations under the terms of the treaty (subject to the decision of an umpire after non-payment has exceeded six months);
    - By PIA if PAC becomes insolvent; or
    - By mutual consent.

  Except in the case of termination due to the insolvency of PAC, termination can only be carried out with agreement from the PAC WPC and from an independent actuary that such termination would not have a material adverse effect on the transferring with-profits policies.
- In respect of the bonuses and MVRs to apply to the transferring with-profits policies, the obligations of PAC and PIA set out in the Scheme are also set out in the reinsurance treaty as described above at paragraph 7.9.

The effect of the Scheme and the reinsurance arrangements set up as a result of the Scheme

7.23 The implementation of the proposed Scheme and the reinsurance arrangements set out above would ensure that:

- In respect of each with-profits fund, PAC would not distinguish between business reinsured into the with-profits fund and business written directly in that fund. This would include the setting of bonuses and MVRs and therefore any interest in the estate of that fund.
- PIA would declare bonuses and apply MVRs in accordance with those notified to it by PAC and PIA would receive from PAC the same total claim amounts in respect of the transferring with-profits policies as would have been paid by PAC if the Scheme were not to be implemented.

7.24 In addition, PIA would be granted a pari passu charge such that, in the event of PAC becoming insolvent, PIA would rank alongside the direct insurance creditors of PAC.

7.25 The conditions under which the reinsurance arrangements can be terminated, in particular the requirement for review and approval from the PAC WPC and an independent actuary, mean that any such termination would not have a material adverse effect on the future discretionary benefits, and any interest in the estates of the with-profits funds of PAC, of the transferring with-profits policyholders.

The administration and servicing arrangements currently in place

7.26 The current administration and servicing arrangements for the transferring business are set out in Section 5.

7.27 If the Scheme were to be implemented there would be the following effects on the transferring business:

- A PIA Poland Branch would be set up and the PAC Poland Branch business would be transferred to it.
- The PIA Poland Branch would administer the business transferred from the PAC Poland Branch and any new business written in Poland with the administration and servicing carried out by the staff and infrastructure transferred across from the PAC Poland Branch.
- The ownership of Prudential Polska would transfer from PFSL to PIMS (by way of a separate agreement between PFSL and PIMS) and Prudential Polska would become a tied agent of the PIA Poland Branch. The level and standard of the administration and servicing provided by Prudential Polska in respect of the transferring business would be unchanged.
- The existing arrangement between PAC and PIMS in respect of the long-term PAC business written in France would transfer to PIA but would, in substance, be otherwise unchanged.
- The policies of the PAC Malta business would be covered by the scope and terms of the existing PIA/PIMS outsourcing arrangement. Given the nominal number of policies, there would be no separate outsourcing agreement between PIMS and Capita Ireland to cover this business and PIMS will administer the business as, post Scheme, it would have the required regulatory authorisation to do so.
- The existing arrangement between PAC and Equiniti in respect of the former ELAS business would remain in place and the arrangement between PAC and Equiniti would not transfer to become an arrangement between PIA and Equiniti. PAC would be responsible to PIA for the administration and servicing of this business through PAC's agreement with Equiniti.

7.28 Although the administration and servicing of the transferring business would be outsourced as described above, PIA would retain ultimate responsibility for the administration and servicing of the transferred business.

7.29 The implementation of the proposed Scheme would have no effect on the administration and servicing arrangements for the non-transferring PAC business or the existing PIA business.

7.30 I cover the effects of the proposed Scheme on the administration and servicing arrangements in place in respect of the transferring policyholders of PAC, the non-transferring policyholders of PIA, and the non-transferring policyholders of PAC in Sections 8, 9 and 10 respectively.

Amendment of PAC and PIA's Investment Management Agreements (IMAs)

7.31 For the PAC France unit-linked business, a fund account is currently in place with Carmignac and Vega to allow access to the corresponding unit-linked funds. PIA will arrange with Carmignac and with Vega for the fund accounts to be transferred to PIA with effect from the Scheme Transfer Date.

7.32 There are no other investment management agreements in place that would be affected by the Scheme.

The costs of the Scheme

7.33 The total costs of the proposed Scheme have been split between PAC and PIA in the following way:

- The costs of the Part VII transfer in relation to the PAC Poland Branch and the closure of the PAC Poland Branch to new business would be entirely allocated to the PAC Poland Branch and split between the PAC

WPSF and the PAC NPSF in accordance with the approved cost allocation methodology annually approved by the PAC Cost Allocation Steering Committee (the "PAC CASC"). The element of the costs allocated to the PAC WPSF will be recouped through the development recovery charge (described in Section 5) applied to the PAC Poland with-profits policies.

- The costs for setting up the PIA Poland Branch would be split between PIA and the new PIA Poland Branch. The costs incurred by the PIA Poland Branch would be allocated between the PAC WPSF and the PAC NPSF in the same manner as for the PAC Poland costs.
- The costs for the transfer of the non-Polish business to PIA would be entirely allocated to the PAC NPSF.

The structure after the implementation of the Scheme

7.34 If the Scheme were to be implemented, all of the PAC non-UK European long-term business written through establishments in Poland, France, Malta, and the former ELAS business would be part of PIA and it is expected that the PAC Poland Branch, the PAC France Branch, and the PAC Malta Branch would cease to transact insurance business. The PAC Poland Branch would not be closed as it may be necessary for it to remain open as a shared services centre.

7.35 If the Scheme were to be implemented:

- PIA would remain without any ring-fenced funds separating any of its business, whether with-profits, unit-linked or non-profit.
- PIA would have the following types of business and is authorised for all of them:
  - With-profits business and non-profit business (Class I & Class III with connected Class IV) in Poland on a freedom of establishment basis;
  - With-profits business and unit-linked business (Class I and Class III) in France on a freedom of services basis;
  - With-profits business and non-profit business (Class I) in Malta on a freedom of services basis;
  - Annuity business (Class I) in Germany (written by ELAS and transferred to PAC in 2007) on a freedom of services basis; and
  - Annuity business (Class I) in Ireland (written by ELAS and transferred to PAC in 2007).
- From 1 January 2019 all new business written in Poland would be written by PIA from the PIA Poland branch (assuming authorisation by the CBI).
- Reinsurance arrangements would be set up between PIA and PAC to enable the with-profits transferring business to maintain its links with the PAC WPSF and the PAC DCPSF, as currently:
  - The with-profits business transferring from the PAC Poland Branch was written in the PAC WPSF.
  - The with-profits business transferring from the PAC France Branch was written in the PAC DCPSF.
  - The with-profits business transferring from the PAC Malta Branch was written in the PAC WPSF.
  - The former ELAS business written in Germany and Ireland was allocated to the PAC DCPSF.

7.36 I cover the effects of the changing reinsurance arrangements in respect of the transferring policyholders and the non-transferring policyholders of PIA and PAC in Sections 8, 9 and 10 respectively.

8 THE EFFECT OF THE SCHEME ON THE TRANSFERRING POLICIES

Introduction

8.1 If the proposed Scheme were to be approved by the Court, all of the PAC long-term business of Poland, France, Malta, Germany and Ireland would be transferred to PIA with the business of the PAC Poland Branch being transferred into the PIA Poland Branch. These policies are collectively the "transferring policies" or the "transferring business".

8.2 In this section of my report I consider the likely effects on the transferring policies of the implementation of the proposed Scheme. The key points to consider in respect of the transferring PAC policies are the likely changes in the following due to the transfer:

- **The security of benefits under the transferring policies.**

  This is derived from the financial strength available to provide security for the benefits under the transferring policies under the appropriate risk appetite statements and capital policy applicable and includes the strength provided by the reinsurance arrangements and by the support from PAC as the parent of PIA.

  This is covered in paragraphs 8.4 to 8.55.

- **The regulatory regime that will apply to the transferring policies.**

  If the Scheme were to be implemented, the transferring policies would move from being subject to the laws and regulations of the UK to those of Ireland.

  This is covered in paragraphs 8.56 to 8.72.

- **The profile of risks to which the transferring policies are exposed.**

  If the Scheme were to be implemented, the transferring PAC policies would become direct policies of PIA and directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.

  This is covered in paragraphs 8.73 to 8.81.

- **The reasonable expectations of the transferring policyholders in respect of their benefits.**

  This includes the likely effects of the transfer on the standards of administration, service, management and governance applied to the transferring policies.

  This is covered in paragraphs 8.82 to 8.100.

8.3 These are considered in turn in this section.

The effect of the Scheme on the security of benefits under the transferring policies

Introduction

8.4 Currently, the transferring policies derive their security of benefits from being part of PAC and the associated financial strength under the PAC risk appetite statements, the strength of PAC's reinsurance arrangements and support provided to PAC from the parent (Prudential plc). In addition, in the extreme scenario of PAC becoming unable to pay policyholder benefits the transferring policyholders are currently protected under the FSCS (as described in Section 3 of this report).

8.5 The implementation of the proposed Scheme would mean that PAC would cease to have a defined contractual obligation to the transferring policyholders and that these obligations would be transferred to PIA. Therefore, after the implementation of the proposed Scheme, the transferring policies would derive their security of benefits from being part of PIA and the associated financial strength under the PIA RA statement, the strength of PIA's reinsurance arrangements, and the support provided to PIA from its parent (PAC).

8.6 In considering the effects of the Scheme on the security of benefits under the transferring policies, I therefore need to consider the effects on the security of the benefits under the transferring policies of:

- The change of applicable risk appetite statements from the PAC risk appetite statements to the PIA RA Statement;
- The transfer to be in PIA after the Scheme as compared to PAC currently: this will include consideration of the changes to the:
  - Financial strength provided by PIA;
  - Applicable reinsurance arrangements; and
  - Support from the parent;
- The loss of the protections conferred by the FSCS.

8.7 These are covered in order below.

The effects on the security of benefits of a change in the applicable risk appetite statements and capital policies

8.8 The risk appetite and capital policies for PAC and PIA are described in Section 5 and Section 6 and the proposed transfer will not lead to any change to either of the risk appetite statements.

8.9 The capital policy in respect of a company specifies the capital that a company is committed to hold in respect of its business and is typically stated in terms of the capital required by the relevant regulations. By requiring additional capital to be held on top of the regulatory requirements, the capital policy increases the probability of remaining solvent over a particular timeframe and therefore increases the security of the policies within the business covered by the capital policy.

8.10 When considering the financial strength available to provide the security of the benefits of a particular group of policies, reliance should only be placed upon the assets held in accordance with the capital policy, as assets in excess of capital policy requirements need not be kept in the company and could, subject to appropriate governance procedures, be transferred out of the company.

8.11 The strength of a risk appetite statement is derived from both the relative level of capital required and the qualitative aspects such as the governance surrounding changes to the risk appetite and the required response of management to a breach. The level of capital required by the risk appetite statement can usually be approximated by a statement that at this level of capital the company has a 1 in X chance of not meeting its regulatory capital requirements over a certain time horizon.

8.12 A comparison of the PIA RA Statement and the PAC risk appetite statements has been carried out together with an analysis of the differences and I am satisfied that, by moving from the coverage required under the PAC risk appetite statements to the coverage required under the PIA RA Statement, there would be no material adverse effect on the security of the benefits under the transferring policies.

8.13 The management actions available to respond to breaches of risk appetite in PAC are different to those available in PIA. These differences reflect the differences between the two companies in size, type of business written and risk exposures, and hence it is not useful to compare the two sets of available management actions.

8.14 That said, a comparison of the governance around the risk appetite statements of the two companies is useful in considering whether there would be differences in the response of the two companies to a breach of risk appetite.

8.15 The governance around the PIA RA Statement appears to be of similar strength to that around the PAC risk appetite statements, and in particular:

- The governance processes that are required when amending the PIA RA Statement and the PAC risk appetite statements are similar:
  - The changes must be approved by the appropriate Board; and

  - If the changes are material then the proposed changes must be sent to the appropriate regulator (the PRA for PAC and the CBI for PIA) for non-objection before being implemented.

- The required actions and management responses of the companies to a breach of the required capital levels set out in the relevant risk appetite statements are similar:

  - Dividends may not be paid while the policy is breached; and

  - A plan must be presented to the relevant Board regarding the restoration of the solvency level to comply with the relevant risk appetite.

8.16 I am satisfied that there is no material adverse effect on the security of benefits from being subject to the PIA RA Statement as compared to the PAC risk appetite statements.

The effects on the security of benefits due to being part of PIA after the Scheme compared to PAC currently

Introduction

8.17 If the Scheme were to be implemented then the transferring policies would be transferred from PAC to PIA and reinsurance arrangements would be set up between PIA and PAC in respect of the transferring with-profits policies as set out in Section 7. The transferring policies would derive their security of benefits from:

- The financial strength of PIA as provided by the assets backing the technical provisions and SCR as required by the Solvency II regulations and the excess assets up to the level of the requirements of the PIA RA Statement;

- The reinsurance arrangements (both new and existing arrangements) of PIA after the implementation of the Scheme; and

- The support from PAC as the parent of PIA.

The financial strength of PIA

8.18 If the Scheme were to be implemented, the financial strength of PIA would be provided by:

- The assets backing the technical provisions and SCR as required by the Solvency II regulations. In respect of these I note that:

  - Both PAC and PIA are currently subject to the Solvency II regime and the technical provisions and SCR of PIA, including those in respect of the transferring policies, would continue to be calculated in accordance with the Solvency II regulations;

  - The Solvency II regulations around the calculation of the technical provisions and the SCR are consistent between the UK and Ireland;

  - The Scheme would not lead to any change to the PGIM which will still be used to calculate the SCR and risk margin for PIA; and

  - The Scheme would not change the Solvency II Standard Formula as set by EIOPA (this may be used to calculate the SCR for the transferring business).

- The excess assets (in excess of total technical provisions and SCR) in PIA up to the level of the requirements of the PIA RA Statement.

8.19 The pro-forma financial information in Appendix B shows that, if the Scheme were to be implemented, it is expected that PIA, the PAC with-profits funds and PAC itself would all exceed the requirements of their respective risk appetite statements. Furthermore, as stated above, I am satisfied that there would be no material adverse effect on the security of benefits due to the transferring policies being subject to the PIA RA Statement rather than the PAC risk appetite statements.

8.20 The financial information in Appendix A and Appendix B shows that, as at 31 December 2017:

- In respect of the PAC shareholder backed business, the capital resources covered the SCR with excess capital of £6.1 billion. This corresponds to a solvency ratio of 178% which is in excess of that required by the regulations and by the PAC SRA Framework.
- If the Scheme had been implemented on this date, the pro-forma financial information shows that PIA's capital resources would have covered its SCR with excess capital of £68 million. This corresponds to a solvency ratio of 147% which would be in excess of that required by the regulations and of the level required by the PIA RA Statement.

8.21 This projected decrease in the SCR coverage ratio that would be experienced by the transferring policies as a result of the Scheme might, in isolation, be taken to imply a negative impact on the security of the transferring policies. However, the SCR coverage ratios are indicators of, or proxies for, financial strength and a decrease in the coverage ratio does not necessarily indicate a significant or material reduction in security.

8.22 In particular, when considering the solvency coverage, one should only take into account the capital resources that the firm is required to hold up to the level required according to its risk appetite statement and capital policy because capital resources in excess of this may be transferred out.

8.23 The pro-forma financial information in Appendix B shows that if the Scheme had been implemented on 31 December 2017, PIA's financial strength would have been 147% which is materially above the regulatory required level of 100% and above the level required to satisfy the PIA RA Statement and indicates that, if the Scheme had been implemented on 31 December 2017, PIA would have been sufficiently well capitalised to withstand a wide range of adverse stress events.

8.24 I have been provided with some projections, on realistic best estimate assumptions, showing the expected path for the PIA SCR coverage if the proposed Scheme were to be implemented. These projections show that, in the near term, the SCR coverage ratio is initially below the target operating level set out in the PIA RA Statement but:

- The coverage remains strong relative to the regulatory intervention level of 100% of SCR;
- It remains higher than the target operating level required under the PIA RA Statement; and
- It quickly (within one year) recovers above the target operating level and then exceeds this level for the rest of the projection period.

8.25 These projections assume expected growth of PIA's future sales of new business and improvements in the firm's solvency position as a result of capital optimisation plans and plans to reduce unit costs. In order to analyse the effects of these assumptions I have been provided with projections showing the sensitivity of the projections of the PIA SCR coverage (excluding the transferring business) on the following bases:

- Assuming no capital optimisation benefits;
- Assuming no reduction in unit costs;
- Assuming no growth in new business from the 2018 level; and
- A combination of the three above scenarios.

8.26 In each of these scenarios the solvency coverage remained in excess of that required by the PIA RA Statement.

8.27 Therefore I am satisfied that reliance on the financial strength of PIA if the Scheme were to be implemented would not lead to a material adverse effect on the security of benefits under the transferring policies.

The reinsurance arrangements of PIA after the implementation of the Scheme:

8.28 If the Scheme were to be implemented, the reinsurance arrangements of PIA would be as follows:

- Reinsurance arrangements would be set up in respect of the transferring with-profits business:

Reinsurance arrangements would be set up between PIA and PAC to reinsure the transferring with-profits policies from PIA to the relevant with-profits sub-fund in PAC. PAC must meet its obligations under these reinsurance arrangements and if it does not, PIA would be able to initiate proceedings to compel PAC to do so.

In the extreme scenario where PIA were to become insolvent, the failure of PAC to meet its obligations under the reinsurance arrangements would mean that the appointed liquidator would be expected to initiate legal proceedings against PAC.

- The existing quota share arrangement currently between PAC and Swiss Re would be transferred to PIA with no other changes to the terms and conditions, and the corresponding reinsurance asset would be allocated to PIA.

  Immediately after the Scheme becomes effective, the part of the arrangement in respect of the mortality risk on the with-profits business of the PAC Poland Branch would be novated back to PAC (together with the reinsurance assets in respect of mortality risk only) as the risk would remain with PAC by virtue of the reinsurance arrangements that would be in place between PIA and PAC as described above.

- The existing reinsurance arrangement with Swiss Re in respect of two high value with-profit whole of life policies written by PAC in Malta would remain with PAC.

- All other existing reinsurance arrangements to which PIA is a party, including those in respect of PIA's existing with-profits business, would be unaffected by the implementation of the proposed Scheme.

8.29 As set out in paragraphs 7.22 to 7.25, there are various safeguards in place in the event that the reinsurance arrangements between PIA and PAC were to be terminated. In particular, with the exception of termination due to the insolvency of PAC, a review by the WPC and an independent actuary would be required to confirm that policyholders would not be materially adversely affected by the proposed arrangements following such a termination. This would include consideration of future discretionary benefits and the policyholders' interests in any estate in the with-profits funds of PAC.

8.30 I am satisfied that the reinsurance arrangements that would be in place if the Scheme were to be implemented would provide security for the transferring policies by placing contractual obligations on PAC and Swiss Re and that the termination conditions set out in the reinsurance arrangements mean that policyholders' security would be protected in the event of a subsequent termination.

The support for PIA from PAC as the parent of PIA:

8.31 There is no formal capital support arrangement between PIA and PAC and therefore, as PAC's interest in PIA is limited to owning the entire issued share capital of PIA, all of which is fully paid-up, as a matter of company law, PAC is not under any legal obligation to provide capital support to PIA.

8.32 However, PAC is subject to a number of contractual and regulatory obligations which link PAC's financial position to that of PIA and which, in my view, limit PAC's ability to walk away from PIA to all but the most extreme scenarios when PAC itself is at risk of not being able to meet its own claims:

- PAC's status as the shareholder of PIA means that PIA is integrated into the Prudential management and oversight framework. PAC's Solvency II and internal economic capital results incorporate the financial position of its subsidiaries including PIA. The financial position of PIA would therefore affect PAC's financial position and the failure of PIA to meet its SCR would be expected to lead to regulatory intervention by the CBI, and these could ultimately lead to a constraint on PAC's ability to pay a dividend.

- PAC cannot freely sell its shares in PIA to a third party without the prior approval of the CBI to the change in control over PIA and this approval would only be given if the CBI was satisfied with the suitability of the acquirer and financial soundness of the acquisition.

- PIA and PAC are both members of the Prudential group, and the policies they sell are marketed under the Prudential brand name. Given the number of policyholders of PIA and the nature of its insurance business, any attempt by PAC to walk away from PIA would be likely to result in significant adverse publicity that the Prudential group would be unlikely to sanction.

8.33 Therefore, although there is no formal capital support arrangement in place with PAC, PIA can derive considerable security from having PAC as its parent as in all but the most extreme scenarios PAC would provide support to PIA if and when required.

Additional security for the transferring policies

8.34 Under the regulatory regime in Ireland, in the extreme scenario of PIA becoming insolvent, the PIA policies would, with the exception of expenses arising out of winding up proceedings (where these cannot be met by PIA's other assets) and certain other limited exceptions, have a priority claim on the assets of PIA backing the Solvency II technical provisions.

8.35 This would apply to all PIA policies (without exception) and they would rank pari passu as regards all the assets held against the technical provisions. This provides additional security for the benefits under the PIA policies including those that would be transferred from PAC under the Scheme.

8.36 Under the UK regulatory regime the position is different. Insurance claims take precedence over any other claims, with the exception of:

- Claims by employees;
- Claims by public bodies on taxes;
- Claims by social security systems; and
- Claims on assets subject to rights in rem (i.e. subject to rights someone might have in the asset itself).

Summary and conclusion

8.37 As set out above, if the Scheme were to be implemented, the transferring policies would be transferred to be part of PIA rather than PAC, and I am satisfied that:

- There would be no material adverse effect on the security of benefits under the transferring policies due to the reliance on the financial strength of PIA rather than PAC;
- The reinsurance arrangements that would be in place would provide security for the transferring policies by placing contractual obligations on PAC and Swiss Re and the termination conditions set out in the reinsurance arrangements mean that policyholders' security would be protected in the event of a subsequent termination; and
- PIA would derive considerable security from having PAC as its parent as in all but the most extreme scenarios PAC would provide support to PIA if and when required.

8.38 Therefore I am satisfied that, if the proposed Scheme were to be implemented there would not be a material adverse effect on the security of the benefits of the transferring policies as a result of their being part of PIA after the Scheme rather than PAC as currently.

8.39 I consider below in paragraphs 8.40 to 8.53 the effect on the transferring policyholders of no longer having the cover provided by the FSCS.

The effects on the security of benefits of losing the protection conferred by the FSCS

Introduction

8.40 Currently the transferring policyholders are covered under the UK's statutory 'fund of last resort', the FSCS. In the event that PAC were to become insolvent, any benefits that would have been claimed from the insurer would be covered under the FSCS. For long-term insurance benefits 100% of the benefits are protected and the coverage is automatic for policyholders of UK authorised insurers and is funded by levies on firms authorised by the PRA and FCA.

8.41 If the Scheme were to be implemented, it is likely (although not certain) that the transferring policies would no longer be covered under the FSCS. I therefore need to consider whether the potential loss of the protections conferred by the FSCS has a material adverse effect on the transferring policies.

8.42 Although it is uncertain whether or not, in the event the Scheme is implemented, FSCS coverage would be lost, the analysis below is based on the assumption that it is lost as then it can only be to the advantage of the transferring policies if this coverage is maintained at some level.

8.43 As stated in Section 1 of this report, there remains considerable uncertainty as to when (and even if) the UK's exit from the EU will take place and around what form that exit might ultimately take and I have therefore made no assumptions about the possible consequences of the UK leaving the EU on either access to the FSCS or PAC's ability to service the non-UK European long-term business if and when the UK leaves the EU.

The effect of the loss of FSCS coverage

8.44 As the FSCS cover would only provide a benefit in the extreme event where the firm is unable to meet its obligations to policyholders, PIA has carried out analysis to consider the likelihood of such extreme events and therefore the value of the FSCS protections to the transferring policyholders.

8.45 PIA's analysis was carried out as follows:

- Generating 100,000 economic scenarios;
- Using the PGIM and the year-end 2017 data to analyse the solvency of PIA in each of these scenarios; and
- Identifying the scenarios where PIA was expected to be insolvent and unable to pay its benefits and therefore where the FSCS coverage would be of value to policyholders.

8.46 The modelling showed that there were very few scenarios (fewer than 30 scenarios out of the 100,000 scenarios which is less than 0.03%) where PIA was projected to be unable to meet its obligations and that, in these scenarios, the most material driver of PIA being unable to meet its obligations was PAC being unable to fulfil its obligations under the reinsurance arrangements between PIA and PAC.

8.47 I have conducted a high-level review of the analysis carried out by PIA in relation to the FSCS and believe it is reasonable for the following reasons:

- The PGIM model is a PRA approved internal model and has been approved by the CBI for use in the calculation of the PIA Solvency II SCR;
- The risk profile of PIA is not expected to change in the near future, and any material change in risk profile would require notification to the CBI per PIA's authorisation letter from the CBI in 2016;
- The methodology has been approved by the Prudential Group Technical Actuarial Committee; and
- The methodology is consistent with that used for Prudential plc and has been reviewed by the PRA.

8.48 As a further piece of analysis in relation to the likelihood of the transferring PAC policies suffering material detriment as a result of the loss of the FSCS coverage, the likelihood of PIA being unable to meet its obligations over a longer time horizon has also been considered.

8.49 Over a longer time horizon, the most significant threats to the solvency of PIA, and therefore that the transferring PAC policyholders suffer a detriment if they do not have access to the FSCS, remain the following:

- The default of PAC on its obligations under the reinsurance arrangements between PIA and PAC; and
- The failure of PAC to provide support as the parent of PIA.

8.50 In order to cover the first of these, an investigation into the likelihood of PAC defaulting over a 10 year time horizon was undertaken using underlying data on default rates and recovery rates obtained from one of the major ratings agencies (Moody's). This indicates that the financial strength of PAC is such that the likelihood of default remains low (significantly below 1%) even over a 10 year time horizon.

8.51 In respect of the second of these, and as set out above in paragraphs 8.31 to 8.33, I am satisfied that although there is no formal capital support arrangement in place with PAC, PIA can derive considerable security from having PAC as its parent as in all but the most extreme scenarios PAC would provide support to PIA if and when required.

8.52 The governance around changes to the PIA RA Statement is set out above in paragraphs 8.8 to 8.16 and this will expose any proposed changes to the PIA RA Statement to appropriate scrutiny in future.

8.53 I am satisfied that the loss of the FSCS coverage for the transferring policyholders would not lead to a material adverse effect on the security of their benefits.

Conclusion on the security of benefits of the transferring policies

8.54 In summary, I am satisfied that, if the Scheme were to be implemented:

- There would not be a material adverse effect on the security of the benefits of the transferring policies as a result of their being part of PIA after the Scheme rather than PAC as currently; and
- Although the implementation of the Scheme may mean that the coverage provided by the FSCS would cease, the loss of the FSCS coverage for the transferring policyholders would not lead to a material adverse effect on the security of their benefits.

8.55 Therefore, in conclusion, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on the security of the benefits under the transferring policies.

The effects on the transferring policies of the change in regulatory regime from the UK to Ireland

Introduction

8.56 If the Scheme were to be implemented then the transferring policies would become protected by the regulatory environment in Ireland rather than that in the UK as currently. This would involve a change to:

- The supervisory body responsible for prudential regulation. The supervisors are the PRA in the UK and the CBI in Ireland;
- The access of policyholders to the services of an industry ombudsman service to opine on alleged cases of policyholder mistreatment. This role is currently fulfilled by the FOS in the UK and the FSO in Ireland; and
- Access to the FSCS.

Regulation in respect of the conduct of business

8.57 Although there may be circumstances in which the FCA retains a role, in general conduct of business responsibility for the policies serviced under the EU's passporting regime lies with the host state supervisors.

8.58 Therefore, the transferring business which was written in Poland, France, Malta, Germany and Ireland currently falls under the regulatory responsibility for conduct of business of the relevant authority in Poland (the KNF), France (the AMF), Malta (the MFSA) , Germany (BaFin) and Ireland (the CBI) respectively. This would not change if the proposed Scheme were to be implemented.

8.59 The Conduct of Business Sourcebook ("COBS") section of the FCA Handbook applies to firms with respect to certain activities carried on in the UK. These COBS rules and the principles set out in the PAC PPFM are applied by PAC in the management of the PAC with-profits funds and therefore, as the transferring business is currently part of the PAC with-profits funds, the COBS rules and principles in the PPFM are currently applied to the transferring business.

8.60 This would continue to be the case if the Scheme were to be implemented as the transferred policies would be reinsured into the PAC with-profits funds and PAC would continue to adhere to the COBS rules in its management of its with-profits funds.

8.61 Also, if the Scheme were to be implemented, although there may be circumstances in which the CBI has a role, in general, conduct of business responsibility would remain with the host state supervisors.

8.62 However, the CBI has issued principles of best practice for the distribution of products in other EU member states and third countries. Although not binding, the principles note that they may reflect binding requirements, and have been implemented by PIA in full. Amongst other things, the principles address:

- Confining target markets to consumers for which products are suitable;
- Checking whether the product continues to meet the general needs of its target market;
- Ensuring that information provided to intermediaries is clear, accurate and not misleading;
- Appropriately addressing errors, complaints and policyholder communications; and
- Relationships with intermediaries.

8.63 I am satisfied that, in terms of conduct of business regulation, the implementation of the proposed Scheme would not have a material adverse effect on the transferring policies.

Regulation in respect of prudential supervision

8.64 If the Scheme were to be implemented there would be a change in the regulator responsible for prudential supervision from the PRA to the CBI.

8.65 There is a high degree of alignment between the regulatory regimes in the UK and in Ireland and the change in responsibility for prudential regulatory supervision from the PRA to the CBI would have a material adverse effect on:

- The Solvency II regulations that would apply to the transferring business;
- The adherence to the Solvency II regulations in relation to the methodologies and assumptions used to calculate the Solvency II balance sheet (in particular the technical provisions and the SCR);
- The adherence to the appropriate risk appetite statements; and/or
- The governance, management (including risk management) and servicing standards that apply to the transferring policies.

8.66 Therefore, I am satisfied that the change in regulatory oversight in respect of prudential supervision from the PRA to the CBI would not have a material adverse effect on the security of the benefits under the transferring policies.

The access of policyholders to the services of an industry ombudsman

8.67 If the Scheme were to be implemented, the transferring policyholders would no longer have access to the FOS and the provisions of the DISP (Dispute Resolution: Complaints) section of the FCA Handbook would no longer apply. Nevertheless, PIA has agreed to:

- Continue to apply the provisions of DISP as such rules apply on the Transfer Date, and to the extent that such rules are compatible with applicable Irish rules or regulations, to:
    - Claims commenced prior to the Transfer Date but not yet settled; and
    - Claims brought after the Transfer Date in respect of acts or omissions of PAC before the Transfer Date.

- Comply with any valid ruling of the UK FOS given in respect of the transferring business.

8.68 In respect of acts and omissions subsequent to the implementation of the Scheme, the policyholders would no longer have access to the FOS but would be able to pursue complaints against the insurer through the FSO. In circumstances where PAC currently refers policyholders to the FOS, PIA would refer those policyholders to the FSO.

8.69 The complaints procedures for both the FOS and the FSO are broadly similar. Both organisations have the powers to make legally binding rulings on individual disputes. However, for FOS the limit to the amount it can make a business pay an individual is £150,000. By contrast the limit for the FSO is €52,000 per annum where the subject of the complaint is an annuity, and a maximum of €500,000 for any other complaints.

8.70 In addition:

- The policyholders of the PIA Poland Branch would continue to have access to the Polish Financial Ombudsman (the "PFO") and this has been the preferred route for any enquiries from the PAC Poland Branch policyholders to date. The PFO carries out a similar function to the FOS and FSO.

  While firms are not formally obliged to comply with the recommendation of the PFO, if the firm does not comply with the PFO recommendation, a legal opinion is sent by the PFO to the complainant that may be used as evidence in any future court proceedings.

- Policyholders of the PAC Malta business would also be able to contact the Arbiter for Financial Services which fulfils a similar function to the FOS and the FSO.

- Policyholders of PAC in Germany would also be able to make complaints to BaFin which fulfil similar functions to the FOS and the FSO.

- Policyholders of PAC France would also continue to have access to the French ombudsman, La Médiation de l'Assurance which fulfils a similar function to the FOS and the FSO.

8.71 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the rights of the transferring policyholders in relation to their access to the services of a financial ombudsman.

The access of policyholders to the FSCS

8.72 The implications of the loss of protection from the FSCS are dealt with in paragraphs 8.40 to 8.53 of this report.

The effect of the Scheme on the profile of risks to which the transferring policies are exposed

8.73 If the proposed Scheme were to be implemented, the transferring PAC policies would be direct policies of PIA and directly exposed to the risk profile of a different company that has written different business, through different distribution channels, to policyholders with different demographic profiles.

8.74 PAC has a large variety of in-force business that exposes it to a range of different risk types, including insurance risks (such as mortality risk, longevity risk and persistency risk), market risks, and credit and counterparty risks.

8.75 By contrast, PIA is exposed to a narrower set of risks. These are principally market risk, persistency risk, and expense risk in relation to both its non-linked and its unit-linked business and counterparty risk as a result of the reinsurance arrangements.

8.76 As stated above, PIA derives security from the fact that PAC is its parent and would be expected to provide support in all but the most extreme circumstances and therefore, PIA has an exposure to the risks that affect PAC's ability to provide that support.

8.77 Alongside the different in-force business, PIA and PAC hold different portfolios of assets and have different exposures to liquidity risk. The same liquidity risk policy applies to both PIA and PAC and is set by the Chief Risk and Compliance Officer of Prudential UK & Europe Insurance and approved by the Board. The current version was finalised in September 2017 and is due to be reviewed in September 2018.

8.78 As at 31 December 2017, both PIA and PAC adhered to this liquidity risk policy and therefore I am satisfied that, although the implementation of the Scheme may change the exposure of the transferring policies to liquidity risk, this will not result in a material adverse effect on the security of the benefits under these policies.

8.79 If the Scheme were to be implemented, the presence of the reinsurance arrangements with PAC would expose the transferring business to counterparty and operational risks. These would be mitigated as described below:

- The counterparty risk would be that of a default by PAC of its obligations under the reinsurance arrangement. This could be due to the insolvency of PAC or the voluntary termination of the arrangement by PAC:
  - The risk of default due to the insolvency of PAC is mitigated by the financial strength of PAC as described in paragraphs 8.17 to 8.27.
  - As set out in paragraphs 7.22 to 7.25, there are various safeguards in place in respect of the termination of the reinsurance arrangements between PIA and PAC. In particular, with the exception of termination due to the insolvency of PAC, a review by the WPC and an independent actuary would be required to confirm that policyholders would not be materially adversely affected by the proposed arrangements following such a termination. This would include consideration of future discretionary benefits and the policyholders' interests in any estate in the with-profits funds of PAC.
- The operational risks would be mitigated by governance and processes that already exist in respect of the risk exposures from the existing reinsurance arrangements between PIA and PAC. These include:
  - An annual review by PIA management of the operation and experience under the reinsurance arrangements;
  - Periodic reviews by the PIA risk function, actuarial function and the internal audit team;
  - Clearly defined roles and responsibilities for managing reinsurance arrangements; and
  - Periodic spot checks for risk premium and claim calculations.

8.80 Therefore, whilst the implementation of the Scheme would result in a change to the risk exposures of the transferring policies, the types of risk exposures are likely to be similar and it should be noted that:

- The Solvency II regime has been implemented consistently across the UK and Ireland;
- The SCR calculated in accordance with the Solvency II regime will reflect the risk exposures of the relevant company;
- The capital held in PIA comfortably exceeds the required SCR; and
- The capital held in PIA exceeds the level required under the PIA RA Statement.

8.81 I am satisfied that any change in risk profile would not have a material adverse effect on the security of the benefits of the transferring policies.

The effect of the Scheme on the benefit expectations of the transferring policyholders

Introduction

8.82 The transferring PAC business consists of with-profits business (single premium bonds and whole of life contracts), non-profit and unit-linked business. For these types of business, policyholders' expectations in respect of their benefits are that:

- They receive their benefits as guaranteed under the policy, on the dates and in the contingencies specified in the terms and conditions;

- The management, governance, administration, and servicing of the policies after implementation of the Scheme are in line with what they have had up until the point of implementation;
- In respect of with-profits policies, that the Scheme does not have a material adverse effect on:
    - The level of discretionary benefits (i.e. declared bonuses) applied to their policies;
    - The charges taken are as specified in the policy conditions; and
    - The level of bonuses received reflect the investment performance of the appropriate with-profits fund (i.e. the WPSF or DCPSF as relevant) with appropriate levels of smoothing (where relevant) applied.
- In respect of unit-linked policies that the Scheme does not have a material adverse effect on:
    - The range of funds available, the management of those funds, the investment objectives applied to those funds, the charges applied to those funds or the pricing of those funds;
    - The benefits received by the policyholders as these should continue to reflect the investment performance of the assets in which their units are invested and the contractual charges payable under the policies; or
    - The assets in which the units under unit-linked policies are invested as these should continue to be materially in line with the target investment allocation in the relevant fund literature.
- In respect of non-profit policies that the Scheme does not have a material adverse effect on:
    - The likelihood that they receive their benefits when due; or
    - The size or frequency of those benefits.

8.83 In the following sections I cover the effect that the implementation of the proposed Scheme would have on the benefit expectations of policyholders in respect of the with-profits, unit-linked and non-profit transferring business respectively and I conclude with a section considering the likely effects of the proposed Scheme on the administration and servicing of the transferring policies.

The benefit expectations of the transferring with-profits policyholders

8.84 If the proposed Scheme were to be implemented, there would be no change to:

- The terms and conditions of the transferring policies (except that the policies would become policies of PIA);
- The charges that apply to the transferring policies;
- The operation of the PAC with-profits funds;
- The PAC with-profits fund (the PAC WPSF or the PAC DCPSF) upon which any transferring policy depends for its benefits;
- The basis upon which the with-profits policies participate in profits;
- The derivation of the bonuses granted to the transferring with-profits policies: PAC would determine these in accordance with the policy conditions, the approach it has previously taken in respect of these policies, and the PPFM (where relevant as described in 8.60 - 8.63), and this would be subject to the governance and oversight of the WPC and WPA; or
- The derivation of any MVR to be applied to any with-profits policy: PAC would determine these in accordance with the policy conditions, the approach it has previously taken in respect of these policies, and the PPFM (where relevant as described in 8.60 - 8.63), and these would be subject to the governance and oversight of the WPC and the WPA.

8.85 If the proposed Scheme were to be implemented, reinsurance arrangements would be set up between PIA and PAC in respect of the transferring with-profits business and these reinsurance arrangements would ensure that PIA would declare bonuses and apply MVRs in accordance with those notified to it by PAC and PIA would have a claim against PAC for the same total claim amounts in respect of the transferring with-profits policies as would have been paid by PAC if the Scheme were not to be implemented.

8.86 In addition, it is set out in the Scheme that PIA must declare and apply bonuses in accordance with notification from PAC and that PIA apply the MVRs in accordance with the amounts notified to it by PAC.

8.87 This means that, the transferring with-profits policies will not be treated any differently to the other policies in the PAC DCPSF or the PAC WPSF in terms of the bonuses and MVRs declared, or in terms of any interest in the estates of these with-profits funds, and the declared bonuses and MVRs will remain subject to the governance and oversight of the PAC WPA and the PAC WPC.

8.88 In addition, PIA would be granted a pari passu charge on the assets of PAC such that, in the event of the statutory insolvency of PAC where the separation between the different PAC sub-funds would break down, the PIA policies would rank equally with the direct written policies of PAC.

8.89 I have reviewed the reinsurance arrangements that would be put in place if the Scheme were to be implemented and I have discussed these reinsurance arrangements with both the legal advisors retained by the firm and my own independent legal advisors and I am satisfied that the description of the reinsurance arrangements set out above is accurate.

8.90 The WPA of PAC is satisfied that, if the Scheme were to be implemented, the bonuses and any MVRs determined in respect of the transferring policies would be no less favourable than they would have been if the policies had remained in PAC and that PIA is committed to declare the bonuses, and apply the MVRs, in respect of the transferring policies in accordance with the bonus rates and MVRs determined by PAC.

8.91 It is also the case that, if the Scheme were to be implemented, to the extent they are currently, the transferring with-profits policies would:

- Be subject to the governance and oversight of the relevant WPC and WPA; and
- Benefit from the protections conferred by the COBS rules and the PPFM.

8.92 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the bonuses and MVRs applied to the transferring with-profits policies or on any other aspects of the benefit expectations of the transferring with-profits policies.

The benefit expectations of the transferring unit-linked and non-profit business

8.93 If the proposed Scheme were to be implemented, then:

- There would be no change to the terms and conditions of the transferring policies (except that the policies would become policies of PIA) or to the charges that apply to the transferring policies.
- There would be a full transfer of arrangements in respect of the existing providers of funds to the transferring unit-linked policies to ensure that:
  - Transferring unit-linked policies would have access to the same range of funds; and
  - The funds would be managed in the same way as currently in respect of investment objectives, charges taken, the tax charged to the unit funds, and unit pricing.
- There would be no change to the number of or type of units held by the transferring policyholders as a result of the implementation of the proposed Scheme.

8.94 The transferring unit-linked and non-profit business is currently subject to the management and governance of PAC and would, if the Scheme is implemented, be subject to the management and governance of PIA and I note the following in respect of the planned management of the transferring unit-linked and non-profit business after the transfer:

- The PIA Board would replace the PAC Board as the governing body with responsibility for the non-profit and unit-linked business that is being transferred.
- The PIA Board has relevant experience and expertise in managing the types of business that make up the transferring unit-linked and non-profit business.
- A new management committee would be set up to oversee the PIA Poland Branch and would report to the PIA Board.
- The non-linked assets backing the transferring non-profit business would be managed in accordance with PIA's governance and management guidelines. These are materially similar to those of PAC and there would not be a material adverse effect on the security of policies as a result of this change.
- The pro-forma financial information shown in Appendix B shows that there is not expected to be a material increase in the likelihood that policyholders would not receive their benefits.

8.95 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the benefit expectations of the transferring unit-linked and non-profit policies.

The effect of the Scheme on the administration and servicing of the transferring policies

8.96 Currently, the transferring policies are administered and serviced as follows:

- The PAC Poland Branch business is currently administered and serviced by the PAC Poland Branch itself. Prudential Polska provides administration and service support as its agents are typically the first point of contact for policyholders of this channel. Some IT services are currently provided by PGDS.
- The PAC France Branch business is currently administered by PIMS, with the relevant services provided by Capita Ireland pursuant to an outsourcing arrangement with PIMS. PAC has 100% interest in PIMS and the Managing Director of PIA currently exercises delegated authority from PAC over the French business.
- The PAC Malta business is currently administered by PDL. The Managing Director of PIA currently exercises delegated authority from PAC over the Maltese business.
- The transferring former ELAS business (Germany and Ireland) is currently administered and serviced by Equiniti under an outsourcing agreement between PAC and Equiniti.

8.97 If the Scheme were to be implemented then this business would be administered and serviced as follows:

- The PAC Poland Branch business would be transferred to PIA and would continue to be administered and serviced by the staff and infrastructure that would have been transferred to the PIA Poland Branch under the Scheme. IT services would be provided by PGDS via a contract between Prudential Distribution Ltd ("PDL") and PGDS (so PDL acts as an intermediary).
- The ownership of Prudential Polska would transfer from PFSL to PIMS (by way of a separate agreement between PFSL and PIMS) and Prudential Polska would become a tied agent of the PIA Poland Branch. There would be a change to the charge made by Prudential Polska to the PIA Poland Branch compared to that currently charged to PAC Poland Branch, but the level and standard of the administration and servicing provided by Prudential Polska to the transferring policies would be unchanged.
- The existing arrangements between PAC and PIMS in respect of the long-term PAC business written in France would transfer to PIA and PIMS but would in substance otherwise be unchanged.
- The policies of the PAC Malta business would be covered by the scope and terms of the existing PIA/PIMS outsourcing arrangement. Given the nominal number of policies, there would be no separate outsourcing agreement between PIMS and Capita Ireland to cover this business and PIMS would administer the business as, post Scheme, it will have the required regulatory authorisation to do so.

- The existing arrangement between PAC and Equiniti in respect of the former ELAS business would remain in place and the arrangement between PAC and Equiniti would not transfer to become an arrangement between PIA and Equiniti. PAC would be responsible to PIA for the administration and servicing of this business through PAC's agreement with Equiniti.

8.98 Although the administration and servicing of the transferring policies would be outsourced as described above, PIA will retain ultimate responsibility for the administration and servicing of the transferring policies.

8.99 The implementation of the proposed Scheme would have no effect on the administration and servicing arrangements for the non-transferring PAC business or the existing PIA business.

8.100 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the levels and standards of administration and service that would apply to the transferring policies.

Conclusion for the effect of the proposed Scheme on the transferring policies

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

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

9 THE EFFECT OF THE SCHEME ON THE EXISTING PIA POLICIES

Introduction

9.1 If the proposed Scheme were to be approved by the Court, all of the PAC long-term business of Poland, France, Malta, Germany and Ireland would be transferred into PIA with the business of the PAC Poland Branch being transferred into the PIA Poland Branch. These policies are collectively the "transferring policies" or the "transferring business".

9.2 In my consideration of the proposed Scheme, the key points in respect of the existing PIA policies are the likely effects of the transfer of the transferring policies into PIA on the following:

- The security of benefits under the existing PIA policies. This is derived from:
  - The financial strength available to provide security for the benefits under the existing PIA policies; and
  - The strength of the PIA RA Statement and the associated capital requirements.
- The profile of risks to which the existing PIA policies are exposed.
- The reasonable expectations of the existing PIA policyholders in respect of their benefits including the standards of administration, service, management and governance applied to their policies.

9.3 These are considered in turn below.

The effect of the scheme on the security of benefits of the existing PIA policies

9.4 As at 31 December 2017, the transferring business consisted of approximately 47,000 policies and £74 million of liabilities and PIA had 47,692 policyholders and over £6.5 billion of assets under management and therefore at under 1.5% (by liabilities as at 31 December 2017) the business being transferred in to PIA is small compared to the existing business of PIA.

9.5 PIA currently has no ring-fenced funds and all the business, whether with-profits, unit-linked or non-profit, is written, in effect, in one fund. The security of the benefits of the existing PIA business is currently provided by:

- The financial strength required by the Solvency II regulations for PIA;
- The financial strength required by the PIA RA Statement; and
- The strength of the governance around the PIA RA Statement.

9.6 If the Scheme were to be implemented, the existing PIA policies would continue to be policies of PIA and:

- The implementation of the Scheme would not lead to the introduction of any ring-fenced funds;
- There would be no change to the Solvency II regime as a result of the Scheme and the technical provisions and SCR for PIA would remain calculated in accordance with the Solvency II regime;
- The approval for the use of the PGIM would not change as a result of the Scheme and the risk margin and SCR for the existing PIA policies would continue to be calculated using the PGIM; and
- There would be no change to the PIA RA Statement as a result of the implementation of the Scheme.

9.7 Given the above, I need to consider the effect of the proposed Scheme on the financial strength available to provide security of benefits for the existing PIA policies.

9.8 Based on the financial information as at 31 December 2017 shown in Appendices A and B of this report:

- The capital resources of PIA covered its SCR with a ratio of 157% and with excess capital of £74 million. This was in excess of the requirements of the PIA RA Statement.

- If the Scheme had been implemented on this date, the capital resources of PIA would have covered its SCR with a ratio of 147% and excess capital (above the SCR) of £68 million.

9.9 This projected decrease in the SCR coverage ratio as a result of the Scheme might, in isolation, be taken to imply a negative impact on the security of the existing PIA policies. However, the SCR coverage ratios are indicators of, or proxies for, financial strength and a decrease in the coverage ratio does not necessarily indicate a significant or material reduction in security. In particular one should note:

- If the Scheme were to be implemented, the projected PIA financial strength of 147% would indicate a position of considerable strength as it is materially above both the required regulatory level of 100% and the level required to satisfy the PIA RA Statement.
- I have been provided with some projections, on realistic best estimate assumptions, showing the expected path for the PIA SCR coverage if the proposed transfer were to go ahead. These projections show that, in the near term, the SCR coverage ratio is initially below the target level set out in the PIA RA Statement but:
  - The coverage remains strong relative to the regulatory intervention level of 100% of SCR;
  - It remains higher than the level required under the PIA RA Statement; and
  - It quickly (within one year) recovers above the target level and is then projected to exceed the target level and required level for the rest of the projection period.

9.10 Therefore, I am satisfied that the implementation of the proposed Scheme would not lead to a material adverse effect on the security of benefits for the existing PIA policies.

The effect of the Scheme on the profile of risks to which the existing PIA policies are exposed

9.11 PIA currently writes unit-linked business and some policies have the option of a with-profits link where the with-profits returns are provided by the PAC with-profits funds through reinsurance arrangements.

9.12 The risk exposures of PIA are currently principally market risk, persistency risk, and expense risk in relation to its non-linked and unit-linked business, and counterparty risk through the reinsurance arrangements and the support received from the parent (PAC).

9.13 The PIA PAC reinsurance arrangement in respect of the with-profits business means that PIA is not significantly exposed to the risks associated with its with-profits business and, if the Scheme were to be implemented, the introduction of the reinsurance arrangements between PIA and PAC in respect of the transferring business will mean that this continues to be the case. The reinsurance arrangements expose PIA to counterparty and operational risks and, given the size of the transferring business relative to the existing PIA business, I am satisfied that the new reinsurance arrangement will not materially change the risk exposures of the existing PIA business.

9.14 If the Scheme were to be implemented, the business that would be transferred into PIA would consist of with-profits single premium bonds, whole of life contracts and annuities, and non-profit term assurance policies. These would increase the risk exposures of the existing PIA business to mortality risk and longevity risk. In addition, the transferring business was written in France, Germany, Ireland, Malta and Poland whereas the existing PIA business was written in Ireland and the UK.

9.15 Therefore, if the Scheme were to be implemented, the range of risks to which the existing PIA business would be exposed would change. However it should be noted that:

- At under 1.5% (by liabilities as at 31 December 2017) the business being transferred in to PIA is small compared to the existing business of PIA;
- The SCR of PIA would be (with the exception of the business transferred in from the PAC Poland Branch), as currently, calculated using the PGIM in accordance with the Solvency II regime, and would reflect the risk exposures of PIA after the implementation of the Scheme;
- The increased range of risk exposures would mean that the risk exposure of PIA would be less concentrated than currently – that is there would be an increased diversification of risk exposures; and

- The pro-forma financial information in Appendix B shows that, if the Scheme were to be implemented, the capital held in PIA would be in excess of the required SCR and the level required under the PIA RA Statement.

9.16 I am satisfied that the change in the range of risks to which the existing PIA business is exposed would not have a material adverse effect on the security of the benefits of the transferring policies.

The effect of the Scheme on the expectations of the existing PIA policyholders in respect of their benefits

9.17 If the Scheme were to be implemented, there would be no change to:

- The terms and conditions of the existing PIA policies;
- The governance or management of the existing PIA with-profits business; or
- The governance or management of the existing PIA non-profit and unit-linked business.

9.18 In terms of the administration, servicing and investment management arrangements for the existing PIA policies, these would be unchanged by the implementation of the Scheme and PIA intends to hire additional staff where required to oversee the business being transferred in so PIA policyholders should not experience any adverse effects on their standards of administration and servicing after the implementation of the proposed Scheme.

9.19 I am satisfied that the implementation of the Scheme would not have a material adverse effect on the reasonable benefit expectations of the existing PIA policyholders or on the standards of administration, service, management and governance that apply to the existing PIA business.

Conclusion for the existing PIA policies

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

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

10 THE EFFECT OF THE SCHEME ON THE NON-TRANSFERRING PAC POLICIES

Introduction

10.1 If the proposed Scheme were to be approved by the Court, all of the PAC long-term business of Poland, France, Malta, Germany and Ireland would be transferred into PIA with the business of the PAC Poland Branch being transferred into the PIA Poland Branch. These policies are collectively the “transferring policies” or the “transferring business”.

10.2 Therefore, in my consideration of the proposed Scheme, the key points in respect of the non-transferring PAC policies are the likely effects of the transfer of the transferring policies out of PAC on the following:

- The security of benefits under the non-transferring PAC policies. This is derived from:
    - The financial strength available to provide security for the benefits under the non-transferring policies; and
    - The strength of the PAC SRA Framework and the associated capital requirements.
- The profile of risks to which the non-transferring PAC policies are exposed.
- The reasonable expectations of the non-transferring PAC policyholders in respect of their benefits including the standards of administration, service, management and governance applied to their policies.

10.3 These are considered in turn in this section.

The effect of the Scheme on the security of benefits under the non-transferring policies

10.4 The transferring business consists of approximately 47,000 policies and £74 million of liabilities (as at 31 December 2017).

10.5 PAC currently has 6.6 million policyholders and over £229 billion of assets under management (as at 31 December 2017).

10.6 The Scheme would have no effect on the PAC risk appetite statements for either the with-profits or the shareholder backed business.

10.7 The business to be transferred out is immaterial in the context of the with-profits business and the shareholder backed business at less than 0.05% of the total liabilities (as at 31 December 2017) and I am satisfied that the transfer would have no material effect on the security of the remaining business of PAC.

The effect of the Scheme on the profile of risks to which the non-transferring business is exposed

10.8 As the transferring business is small compared to the remaining PAC business, I am satisfied that the transfer out of less than 0.05% of the liabilities of PAC would not have a material adverse effect on the profile of risks to which the non-transferring PAC policies are exposed.

The effect of the Scheme on the expectations of the non-transferring PAC policyholders in respect of their benefits

10.9 The implementation of the proposed Scheme would not change:

- The terms and conditions of the non-transferring PAC policies;
- The governance or management of the PAC with-profits business;
- The governance or management of the PAC non-profit and unit-linked business; and
- The administration, servicing and asset management arrangements for the non-transferring PAC policies.

10.10 The transferring with-profits business is immaterial in the context of the with-profits business of PAC held in the PAC DCPSF, the PAC WPSF and the SAIF, and would be reinsured into the relevant PAC with-profits fund, and therefore I am satisfied that the transfer of this business to PIA would not have a material adverse effect on the future performance of the PAC with-profits funds, or the returns attributable to the with-profits policies.

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

Conclusion for the non-transferring PAC policies

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

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

11 MY CONSIDERATIONS IN RESPECT OF THE FAIR TREATMENT OF CUSTOMERS

The approach to communication with policyholders

Introduction

11.1 Regulations made under FSMA require a communication regarding the proposed transfer to be sent to every policyholder of the parties under the Scheme. However, this requirement may be waived at the discretion of the Court which will give consideration to issues such as the practicality and costs of sending notices relative to the likely benefits for policyholders of receiving such communications.

The proposed 'waiver' applications

11.2 PAC intends to seek waivers from the regulatory requirements to send a written notice to the policyholders of PAC that would not be transferred if the Scheme were to be implemented.

11.3 The cost of mailing these existing policyholders of PAC has been estimated to be approximately £3.4 million (which I have reviewed and am satisfied is a reasonable estimate) and therefore the cost of mailing such policyholders is considered disproportionate relative to the benefits to the policyholders that would result from any such mailing given that:

- There would be no change to the terms and conditions of any non-transferring PAC policies.
- The financial impact of the Scheme on the non-transferring PAC policyholders is not material as the transferring policies represent a small proportion (less than 0.1% by liabilities as at 31 December 2017) of PAC's balance sheet.
- As described in earlier sections of this report, in my view there would be no material adverse effect on:
  - The security of benefits under any such policies;
  - The governance, administration and servicing arrangements applicable to such policies; and
  - The reasonable benefit expectations under any such policies.
- There will be press advertising for the Scheme to comply with the advertising requirements.

11.4 I am satisfied that the application for a waiver from the regulatory requirements to send a written notice to the non-transferring policyholders of PAC is reasonable.

The mailing pack

11.5 Both the PRA Statement of Policy and the FCA Proposed Guidance state that, in respect of insurance business transfers, companies are required to notify the policyholders, or interested persons, at least six weeks before the date of the Court hearing at which the application to sanction the Scheme will be heard.

11.6 The following will be sent a mailing pack about the Scheme prior to the Court hearing to enable them to make representations to the Court if they feel they may be disadvantaged by the proposals:

- All the transferring policyholders for whom PAC holds a name and address on its computerised databases, except for those populations where a mailing waiver has been granted by Court; and
- Policyholders of PIA for whom PIA holds a name and current address on its database.

11.7 The mailing pack will be translated into the language in which the original policy was written and will contain:

- A covering letter; and
- The Policyholder Information Booklet, which will contain:

- A summary of the Scheme and a summary of this report;
- Questions & Answers; and
- A copy of the legal notice.

The Affinity policyholders

11.8 Since inception, PAC Poland has sold policies through two affinity partners, both telecommunications companies: P4 Sp. z o.o. and Orange S.A. PIA has discussed the proposed communication with these companies who have confirmed that they predominantly use digital means to contact their customers and that in their view it would be more effective and consistent with their customers' expectations if the method of communication were to be digital rather than mailing a pack of documents.

11.9 Therefore, with regard to the PAC Poland Branch policyholders of the Affinity business (as described in Section 5) PIA intends to seek approval from the Court to contact these policyholders of PAC Poland by digital methods.

11.10 The digital communication to Affinity policyholders will be in the form of an SMS text to all policyholders including a link to the website which holds all relevant documentation of the Scheme. Where Affinity policyholders have provided an email address, the mailing pack would also be sent to that email address.

11.11 The products in the Affinity channel are sold as an addition to mobile phone contracts offered by the Affinity partners and so sending the SMS messages to the mobile phone numbers connected with these contracts should minimise the number that do not reach the intended recipient.

11.12 I am satisfied that this proposal to contact Affinity business policyholders via digital methods is reasonable because it would be consistent with the way they took out the policy and therefore it is likely that the policyholders will take notice of information which arrives via the expected method of communication. I have reviewed the proposed text of the SMS text message for the Affinity policyholders and I am satisfied that it is reasonable.

Further publication of the Scheme and distribution of information in respect of the Scheme

11.13 The Prudential websites www.prudential.co.uk, www.prudential.co.fr, www.prudential.pl and www.prudential-international.com will contain the following information:

- All policyholder mailing pack documents;
- My report (this report) and any supplementary reports;
- The reports from the PAC and PIA Chief Actuaries and the PAC WPA, plus any supplementary reports; and
- The full Scheme document.

11.14 PAC and PIA will publish a notice in a form approved by the PRA in the following publications in the UK:

- The London Gazette;
- The Edinburgh Gazette;
- The Belfast Gazette; and
- The Times, The Financial Times, The Daily Telegraph, The Sun, The Daily Mirror, and The Daily Mail.

11.15 Subject to any waiver granted by the Court this will also be published in two national newspapers in each EEA State of the commitment for any policy included in the transfer, namely:

- Gazeta Wyborcza and Dziennik Gazeta Prawna in Poland.
- Les Echos, Le Monde and the French Legal Gazette (Journal Officiel) in France.
- Times of Malta and In-Nazzjon in Malta.
- Der Tagesspiegel, and Frankfurt Allgemeine Zeitung in Germany.
- The Irish Times, The Irish Independent and the Irish Gazette (Iris Oifigiúil) in Ireland.

Conclusion

11.16 The Managing Director of PIA, the Chief Actuary of PAC and the Head of Actuarial Function of PIA have confirmed that in their view the proposed approach to communication with policyholders is fair and reasonable and that the information contained in the notification to policyholders adequately describes the proposals to policyholders.

11.17 I am satisfied that the proposed approach to communication with policyholders, including the application for the waiver, is fair and reasonable, and that the information contained in the notification to policyholders adequately describes the proposals to policyholders.

The effects of the Scheme on access to a financial ombudsman's service

11.18 If the Scheme were to be implemented, the transferring policyholders would no longer have access to the FOS and the provisions of the DISP (Dispute Resolution: Complaints) section of the FCA Handbook would no longer apply. Nevertheless, PIA has agreed to:

- Continue to apply the provisions of DISP as such rules apply on the Transfer Date to:
    - claims commenced prior to the Transfer Date but not yet settled; and
    - claims brought after the Transfer Date in respect of acts or omissions of PAC before the Transfer Date,

    In each case to the extent that such rules are compatible with applicable Irish rules or regulations; and

- Comply with any valid ruling of the UK FOS given in respect of the transferring business.

11.19 In addition, the transferring policyholders would have access to the services of a financial ombudsman as follows:

- In respect of acts and omissions subsequent to the implementation of the Scheme, the policyholders would no longer have access to the FOS but would be able to pursue complaints against the insurer through the FSO. In circumstances where PAC currently refers policyholders to the FOS, PIA would refer those policyholders to the FSO and the complaints procedures in the FSO are broadly similar to those for the FOS.
- Policyholders of PIA Poland would continue to have access to the PFO on the same rules as currently. The PFO carries out a similar function to the FOS and FSO.
- Policyholders of the PAC Malta business would also be able to contact the Arbiter for Financial Services which fulfils a similar function to the FOS and the FSO.
- Policyholders of PAC in Germany would also be able to make complaints to BaFin which fulfils a similar function to the FOS and the FSO.
- Policyholders of PAC France would also continue to have access to the French ombudsman, La Médiation de l'Assurance, which fulfils a similar function to the FOS and the FSO.

11.20 I am satisfied that the transfer would have no material adverse effect on the rights of the transferring policyholders in relation to their access to the services of a financial ombudsman.

11.21 There would be no effect on the rights of either the non-transferring PAC policyholders or the existing PIA policyholders in relation to their access to the FOS or FSO.

The costs of the Scheme

11.22 The costs of the Scheme would be split between PIA, the PAC WPSF and the PAC NPSF as described in Section 7, with the majority of the costs being allocated to the PAC WPSF.

11.23 The element of the Scheme costs allocated to the PAC WPSF will be recouped through the development recovery charge (described in Sections 5 and 7) applied to the PAC Poland with-profits policies. Existing policyholders currently pay the same development recovery charge throughout the lifetime of their policies and these charges would be unaffected if the Scheme were to be implemented.

11.24 As stated in Section 7, the primary motivation for the Scheme is to simplify the management and increase the operational efficiency in respect of the non-UK European operations of Prudential plc.

11.25 Currently, PAC Poland meets all the costs associated with administering the PAC Poland Business and thus the WPSF bears a proportion of these. If the Scheme were to be implemented, any efficiencies and reductions in ongoing costs associated with the PAC Poland business would, through the reinsurance arrangements, reduce the costs charged to the PAC WPSF.

11.26 The PAC WPA is satisfied that the allocation of costs to the PAC with-profits funds that arises from the approach of PIA and PAC to the allocation of the costs of the Scheme is reasonable and fair.

11.27 I am satisfied that it is reasonable to charge some of the costs to the PAC WPSF and I am satisfied that the approach of PIA and PAC to the allocation of the costs of the Scheme is reasonable.

Conduct and mis-selling risk in the future

11.28 As described in Section 5, the PAC Poland Branch currently sells business via tied agents (through Prudential Polska), agents who also work for other firms (multi-agents), a bancassurance channel, and via affinity arrangements with partner firms.

11.29 This increased range of distribution channels would lead to an increase to the advice risk exposure of PIA after the transfer.

11.30 This would be reflected in an increased requirement for operational risk capital as reflected in the Standard Formula SCR. This risk is mitigated by the existing and proposed governance arrangements in PIA after the implementation of the proposed Scheme.

11.31 These include:

- The creation of a new management committee for the PIA Poland Branch; and
- Ensuring that PIA's existing advisory committees include appropriate Polish representation.

11.32 To the extent that any mis-selling risks transfer from PAC to PIA in relation to the former ELAS business these would be covered by ELAS under the conditions set out in the Part VII transfer of the ELAS business to PAC. Therefore, PAC will indemnify PIA in respect of any such claims.

11.33 All the mis-selling and conduct of business liabilities comprised in or attributable to the non-ELAS transferring business would be transferred to PIA. This would include the conduct of business liabilities directly related to the transferring business but not any wider PAC conduct of business liabilities.

11.34 If the Scheme were to be implemented and any such mis-selling costs arise on the transferring business, they would be met by PIA. For the avoidance of doubt they would not be charged to the PAC with-profits funds.

Other creditors

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

Tax in respect of policyholders of the PAC France Branch

11.36 If the Scheme were to be implemented, the policies of the PAC France Branch would be transferred to PIA and it is proposed that the PAC France Branch would subsequently be closed. PIA would not be required to comply with the tax filing and payment obligations to which PAC is currently subject under French law which could present an issue for some of the affected policyholders.

11.37 I understand that PAC and PIA have taken advice from their French legal advisors on this matter and that PIA will seek a mandate from the policyholders of the PAC France Branch to handle their tax filing and payment obligations.

11.38 This mandate will allow PIA to deduct the relevant tax at source and will be issued to the policyholders of the PAC France Branch at the same time as the policyholder mailing.

11.39 I am satisfied that this is reasonable and that there will be no material adverse effect on the PAC France policyholders as a result of this.

12 MY OTHER CONSIDERATIONS ARISING FROM THE SCHEME

The future operation of the Scheme

12.1 If the Scheme is approved by the Court (and subject to any subsequent amendment of the Scheme, as considered below), PAC and PIA are committed to implementing the Scheme as set out in the Scheme document (and reflected in this report). In giving effect to those obligations, the Directors of PAC and PIA must act in accordance with their fiduciary responsibilities under UK and Irish company law.

12.2 At any time after the Court's sanction of the Scheme, PIA and (where applicable) PAC must apply to the Court for sanction of any amendments to it, except where the amendment is considered to be minor or technical, in which case PIA must notify the CBI, PRA and FCA.

12.3 The published financial position of PIA and PAC will be calculated by the firms' actuaries and accountants and will be subject to external audit.

12.4 In my opinion there are reasonable safeguards in place to ensure that, if approved by the Court, the Scheme will be operated as presented to the Court.

The exit of the UK from the EU – "Brexit"

12.5 As stated in Section 1, the exit of the UK from the EU could lead to considerable disruption in the market for financial services across Europe and in particular for UK and non-UK companies relying on passporting rights to write business via the EU's freedom of establishment or freedom of service rules into the rest of the EEA or the UK respectively.

12.6 At the time of writing this report, there remains considerable uncertainty as to when, and even if, the UK will leave the EU and around exactly what form that exit might ultimately take and I have, in this report, made no assumptions about the possible consequences of the UK leaving the EU, but have focussed on the implications of the implementation of the Scheme for the policyholders of PIA and PAC.

12.7 That said, if the Scheme were to be implemented, I am satisfied that in most non-extreme scenarios in which the UK does exit from the EU, the transferring business would be in a better position than the scenario where the UK exits the EU and the Scheme had not been implemented.

What would happen if the Scheme were not to be implemented?

12.8 If the Scheme does not proceed for any reason, then the transferring PAC policies will not become policies of PIA and will remain within PAC.

12.9 Under this scenario the reinsurance arrangement between PAC and Swiss Re would remain in place.

12.10 PAC's ability to manage, administer and service the transferring business in Poland, France, Malta, Germany and Ireland may be threatened and would be subject to the outcome of Brexit negotiations. Further actions might be required from PAC to ensure a continuation of the ability to service these policies.

The implications of the Scheme for Solvency II approvals

12.11 Given the size of the transferring business relative to the PAC technical provisions (less than 0.05%), implementation of the Scheme is not expected to have a material effect on the Solvency II approvals from the PRA for the TMTP, the matching adjustment or the PGIM.

The tax implications of the Scheme

12.12 PAC has retained Pricewaterhouse Coopers LLP ("PwC") and Deloitte Doradztwo Podatkowe ("Deloitte") to provide reports to identify significant tax issues arising from the proposed Scheme. I refer to PwC and Deloitte as the "external tax experts".

12.13 I have seen the final version of the report produced by PwC (dated 19 January 2018) and the final opinion produced by Deloitte (dated 18 January 2018) and, in forming my view on the proposed Scheme, I have relied on these as expert opinions on the tax implications of the proposed Scheme.

12.14 The reports and opinions of the external tax experts support the conclusion that the implementation of the proposed Scheme will not affect the tax position of the policyholders of the transferring PAC business.

12.15 Given the relative size of the transferring business, the implementation of the proposed Scheme is not expected to have a material effect on the tax position of PAC or PIA or on the tax position of the non-transferring PAC and PIA policyholders.

The effect of the proposed Scheme on previous schemes

12.16 PAC has commissioned a review by Slaughter and May of the previous schemes to which PAC has been party. I understand from PAC that, on the basis of this review, with the exception of the ELAS Scheme from 2007, it is satisfied that the implementation of the Scheme is not expected to have a material effect on any of the previous schemes to which PAC has been party.

12.17 The ELAS Scheme will be amended and submitted to the Court at the time of the Sanctions Hearing for this Scheme. I shall cover the implications of this in my Supplementary Report that will be presented to the Court for the Sanctions Hearing.

12.18 I consider that it is reasonable and appropriate for me in the circumstances to rely on this confirmation.

The PAC PPFM

12.19 Implementation of the proposed Scheme will not result in any material changes to the PAC PPFM other than those to reflect the PAC company structure and to describe (where appropriate) the effects of the implementation of the Scheme, including the amendments to the ELAS Scheme described above.

12.20 I will review a draft of the updated PPFM before the Sanctions Hearing and provide the results of my review in my Supplementary Report.

The PAC Pension Mis-selling Costs Assurance

12.21 As described in Section 5, Prudential plc has given an assurance that the deduction of personal pension mis-selling costs from the PAC inherited estate would not have an adverse effect on the level of the bonus paid to policyholders or on their reasonable expectations and, in the event of this proving not to be the case, an appropriate contribution to the appropriate with-profits fund would be made from the PAC shareholder backed business for as long as the situation continued.

12.22 The size of the business transferring from PAC in relation to the inherited estate is small (less than 1%) and, as a result of the reinsurance arrangements being set up between PIA and PAC, it is expected that policyholders who were originally covered by the PAC Pension Mis-selling Costs Assurance will continue to benefit from it following the transfer. The nature of the PAC Pension Mis-selling Assurance would be unchanged by the transfer.

12.23 Therefore, I am satisfied that, if the Scheme were to be implemented, the effect on the protection offered by the PAC Pension Mis-selling Costs Assurance would not be material and there would be no material adverse effect on the security of benefits or reasonable benefit expectations of the PAC policyholders.

The capital support in respect of the PAC Poland Branch business

12.24 The growth of the PAC Poland Branch business (since its inception in 2012) has been funded by the PAC shareholder backed business in respect of the non-profit business and the PAC with-profits business in respect of the with-profits policies.

12.25 In order to protect the PAC with-profits funds, the PAC shareholder backed business has, in effect, underwritten this funding, and this would be unaffected by the transfer of the relevant business to PIA.

12.26 The PAC WPA has stated that he believes this to be appropriate.

12.27 I am satisfied that there would be no effect on the security of benefits or on the policyholders' benefit expectations as a result of the continuation of the support provided to the PAC Poland Branch.

The outsourcing arrangement with Capita Ireland

12.28 On 31 January 2018, Capita plc, the parent company of Capita Ireland, released a 'profit warning' statement and announced a £700 million rights issue. As set out in Section 5 of this report, PAC (which owns PIMS) and PIA (through its service agreement with PIMS) rely on Capita Ireland for outsourced policy servicing and administration by way of the outsourcing arrangement between PIMS and Capita Ireland.

12.29 I have discussed this with senior management and I have seen a paper produced by the PIA Chief Risk Officer that sets out his analysis of the risk posed by these events. Apart from being confident that PIA senior management are monitoring the situation, it is too early to be able to tell what the outcome may be from these events but I will keep their possible effects on PIA under review and, if relevant, will provide an update in my Supplementary Report.

The restructuring of Prudential plc and the sale of part of the UK annuity portfolio

12.30 In August 2017, Prudential plc announced that it was combining two businesses within the Prudential group, Prudential UK & Europe and its asset manager, M&G, to form a combined business called M&G Prudential.

12.31 In March 2018, Prudential plc announced that:

- M&G Prudential would demerge from the Prudential group, resulting in two separately listed companies; and
- The legal ownership of Prudential plc's Hong Kong insurance subsidiaries would be transferred from PAC to Prudential Corporation Asia Limited (PCA), another subsidiary of Prudential plc, by the end of 2019.

12.32 Also in March 2018 it was announced that PAC had entered into a transaction to transfer a portion of the shareholder-backed non-profit annuity business to Rothesay. Under the terms of the agreement, approximately £12 billion of liabilities (as at 31 December 2017) would be reinsured to Rothesay, through a collateralised reinsurance arrangement, with the intention that this is followed by a Part VII insurance business transfer of the business by the end of 2019.

12.33 In respect of the implementation of the proposed Scheme that is the subject of this report:

- None of the transferring business under the proposed Scheme is included in the Rothesay reinsurance arrangement or will be included in the subsequent Part VII transfer of the business to Rothesay.
- The proposed Scheme will have no effect on the reinsurance arrangement with Rothesay.
- The Rothesay reinsurance arrangement does not change the effect of the proposed Scheme on either PAC or PIA.
- The Rothesay reinsurance arrangement has no effect on PIA so the post Scheme position for the transferring business is unaffected by the Rothesay reinsurance arrangement.
- The financial strength of PAC both before and after the Scheme is projected to be in excess of the PAC risk appetite statement with or without the impact of the Rothesay reinsurance arrangement and the PAC risk appetite statement is unchanged by the Rothesay reinsurance arrangement.

12.34 Given these points and the small size of the transferring business relative to PAC (less than 0.05% by liabilities), I am satisfied that neither the restructuring of Prudential plc nor the reinsurance arrangement with Rothesay will have any effect on the analysis in this report or on the conclusions reached.

13 MY CONCLUSIONS

13.1 I confirm that I have considered the issues affecting the policyholders of PAC and PIA separately, as set out in Sections 8, 9, 10, 11 and 12, and that I do not consider further subdivisions (other than those in this report) to be necessary.

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

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

13.3 I am satisfied that the Scheme is equitable to all classes and generations of PIA and PAC policyholders.

Oliver Gillespie

Partner of Milliman LLP

Fellow of the Institute and Faculty of Actuaries

29 June 2018

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

Solvency II financial information as at 31 December 2017

£ million	Total PAC PH Funds[1]	PAC SHF	NPSF	PIA[2]	Total PAC SH Funds	Total PAC SH Funds – Restated[3]
Assets	**132,826**	**3,779**	**55,218**	**6,752**	**77,291**	**78,556**
Technical provisions	**116,358**	**-**	**46,000**	**6,445**	**58,656**	**60,192**
Other Liabilities	**6,890**	**1,274**	**3,543**	**104**	**4,636**	**4,554**
Own Funds (post TMTP)	**9,578**	**2,506**	**5,675**	**203**	**13,999**	**13,810**
SCR	**4,775**	**2,151**	**5,651**	**130**	**7,884**	**7,143**
Excess Assets after SCR	**4,803**	**354**	**24**	**74**	**6,115**	**6,666**
Solvency coverage ratio	**201%**	**116%**	**100%**	**157%**	**178%**	**193%**

Notes:

1. The figures for the PAC policyholder funds represent an economic view of the Solvency II balance sheet for the with-profits business, including the liability and associated capital requirements related to the present value of the future shareholder transfers. The surplus assets after SCR are distributed among the three ring-fenced funds as follows:

   - £200 million inherited estate in SAIF. In addition SAIF receives capital support from the WPSF (including any support to meet solvency capital requirements) in return for charges levied on asset shares;
   - No surplus funds in the DCPSF. It is provided with capital support from the WPSF to meet guarantees and smoothing and to cover the risk margin and solvency capital requirements in exchange for charges levied on asset shares;
   - Remaining surplus funds held in the WPSF.

2. The assets and liabilities for PIA exclude the assets and liabilities of PIMS.

3. The restated PAC shareholder-backed business position allowing for the reinsurance arrangement with Rothesay.

Pre-Scheme Balance Sheets

£ million	Poland NP	Poland WP	France NP	France WP	ELAS	Malta	PIA[1]	Total PAC PH Funds[2]	Total PAC SH Funds
Assets[3]	8	5	5	39	24	3	6,752	132,826	77,291
Technical provisions	(15)	2	5	39	24	3	6,445	116,358	58,656
Other Liabilities	26	-	-	-	-	-	104	6,890	4,636
Own Funds (post TMTP)	(3)	2	-	-	-	-	203	9,578	13,999
SCR	13	6	-	-	-	-	130	4,775	7,884
Excess Assets after SCR	(15)	(4)	-	-	-	-	74	4,803	6,115
Solvency coverage ratio	N/A	N/A	N/A	N/A	N/A	N/A	157%	201%	178%

Notes:

1. The assets and liabilities for PIA exclude the assets and liabilities of PIMS.
2. The figures for the PAC policyholder funds represent an economic view of the Solvency II balance sheet for the with-profits business, including the liability and associated capital requirements related to the present value of the future shareholder transfers.
3. Where the assets are presented for the transferring blocks of business under the Scheme, the assets associated with the with profits blocks of business are part of the ‘PAC PH Funds’ assets and the assets associated with the non-profit blocks of business are part of the ‘PAC SH Funds’ assets.

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

Post-Scheme Balance Sheets

£ million	Poland NP	Poland WP	France NP	France WP	ELAS	Malta	PIA[1]	PIA (update)[2]	Total PAC PH Funds[3]	Total PAC SH Funds
Assets[4]	-	3	5	39	24	3	6,828	6,828	132,826	77,360
Technical provisions	(12)	3	5	39	24	3	6,498	6,506	116,358	58,725
Other Liabilities	-	-	-	-	-	-	109	109	6,890	4,636
Own Funds (post TMTP)	12	-	-	-	-	-	222	214	9,578	13,999
SCR	14	-	-	-	-	-	143	146	4,775	7,884
Excess Assets after SCR	(2)	-	-	-	-	-	79	68	4,803	6,115
Solvency coverage ratio	N/A	N/A	N/A	N/A	N/A	N/A	155%	147%	201%	178%

Notes:

1. The assets and liabilities for PIA exclude the assets and liabilities of PIMS.
2. This reflects updates in the methodology and the assumptions to accommodate the transferred business. This includes:
   - Set up of expense overrun reserve for Non-Profit business (£7 million increase in BEL, £1 million increase in SCR).
   - Change in methodology for SCR calculation of the Poland NP Business (£1 million reduction in SCR and £1 million increase in the risk margin).
   - An allowance for currency translation risk which relates to the risk of exchange rate fluctuations impacting the consolidated PIA position and an allowance for the ongoing regulatory challenge to old endowment. It is not expected that the regulatory challenge is high risk, and therefore no pre-transfer allowance is currently held for this. These result in a combined £3 million increase in SCR.
   - An allowance for future cost increases in the normal course of business: a £2 million increase in the BEL.
3. The figures for the PAC policyholder funds represent an economic view of the Solvency II balance sheet for the with-profits business, including the liability and associated capital requirements related to the present value of the future shareholder transfers.
4. Where the assets are presented for the transferring blocks of business under the Scheme, all the assets are part of PIA. PIA has no ring-fenced funds.

APPENDIX C: THE PRODUCT TYPES WRITTEN BY PIA AND PAC

With-profits business

1 With-profits business refers to insurance business where policyholders are entitled to share in the profits of the insurer. It typically refers to both of the following:

- Conventional with-profits ("CWP") business; and
- Unitised with-profits ("UWP") business.

2 CWP business typically refers to policies where policyholders' premiums are fixed and they have a maturity benefit that is guaranteed at the outset in monetary terms. This benefit can subsequently be increased by bonuses that are awarded at the discretion of the insurer, depending upon the surplus emerging in the insurance fund in which the policies are invested. Once they have been awarded, bonuses are typically guaranteed and insurers are not able to take them away. A final bonus may also be awarded at maturity.

3 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 include a final bonus amount.

4 It is typical for insurers to target policyholder pay-outs to be relatively close to the policy's "asset share", which is a measure of the true value of the policy based on actual investment returns and expenses incurred by the fund. Therefore, where final bonuses are paid, it is typical for these to be calibrated in order to target something close to asset share, subject often to a degree of smoothing of investment returns, as well as being subject to honouring any guaranteed benefits to which the policyholder is entitled.

5 Most with-profits business in the UK is written either in a "90:10" fund or in a "100:0" fund. In a 90:10 fund, policyholders are entitled to at least 90% of the surplus arising from the with-profits business, with shareholders of the insurer entitled to the remainder. The shareholders are typically only permitted to withdraw money from a 90:10 fund upon declaration of a bonus to with-profits policyholders, upon which they would receive 1/9th of the value of the declared bonus.

6 In a 100:0 fund, policyholders are typically entitled to 100% of the investment surplus emerging in the fund. It is sometimes the case that in 100:0 funds the shareholder is entitled to receive 100% of the non-investment surplus, principally any excess of charges made to policyholders over actual expenses incurred.

Non-profit business

7 Non-profit business refers to insurance business where policyholders do not share in the profits of the insurer and all surplus is attributable to the insurer's shareholders. Non-profit business typically refers to the following classes of insurance business:

- Conventional non-profit business;
- Unit-linked business; and
- Index-linked business.

8 Conventional non-profit business refers to insurance business where the benefits received by policyholders are fixed in terms of monetary amount, for example a life insurance policy that pays a fixed death benefit or a pension annuity that pays a fixed annuity amount each year whilst the policyholder is alive. Insurance companies make a profit from conventional non-profit business by setting premium amounts that, in conjunction with the investment returns earned on invested policyholder premiums, are more than sufficient to cover the benefits payable and any associated expenses.

9 Unit-linked business is principally a type of investment product where policyholders' premiums are used to buy units in investment funds. The value of the policyholder's units then moves in line with the performance of the investments in the fund. At maturity, policyholders receive the value of their units.

10 Charges are deducted from the policyholders' premiums or from their units, and insurance companies' profits are determined by the extent to which the income they receive from these charges exceed the expenses they incur in incepting and maintaining the business.

11 Index-linked business is an insurance product where the policyholder's benefits are determined by reference to an index, such as an inflation index, rather than being a fixed monetary amount. An annuity whose payments are linked to changes in the Retail Price Index ("RPI") is an example of an index-linked contract.

APPENDIX D: THE SOLVENCY II REGULATORY REGIME

Introduction

1 A new 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 and it aims to introduce solvency requirements that better reflect the risks that insurers and reinsurers actually face and to introduce consistency across the EEA.

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

3 Solvency II is based on three pillars:

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

The Pillar 1 requirements

4 Assets are, broadly speaking, reported at market value under Pillar 1.

5 The determination of a market consistent value of liabilities under Solvency II requires the insurer to calculate the best estimate liabilities ("BEL"). The expected future obligations of the insurer are projected over the lifetime of the contracts using the most up-to-date financial information and the best estimate actuarial assumptions, and the BEL represents the present value of these projected cash-flows.

6 Under Solvency II, a company's Pillar 1 liabilities are called the "technical provisions" which consist of the sum of the BEL and the "risk margin". The risk margin is an adjustment designed to bring the technical provisions up to the amount that another insurance or reinsurance undertaking would be expected to require in order to take over and meet the insurance obligations in an arm's length transaction.

7 The Solvency Capital Requirement ("SCR") under Solvency II is the capital requirement under Pillar 1, and is intended to be the amount required to ensure that the firm's assets continue to exceed its technical provisions over a one year time frame with a probability of 99.5%.

8 The Minimum Capital Requirement ("MCR"), which is lower than the SCR, defines the point of intensive regulatory intervention. The MCR calculation is simpler, more formulaic and less risk-sensitive than the SCR calculation.

9 In calculating the SCR, it is expected that most firms will use the "Standard Formula", as prescribed by the European Insurance and Occupational Pensions Authority ("EIOPA"). However, Solvency II also permits firms to use their own internal models (or a combination of a "partial internal model" and the Standard Formula) to derive the SCR. These internal models and partial internal models are subject to approval by the relevant regulator: in the UK this is the PRA and In Ireland this is the CBI.

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

10 EIOPA has published the implementing technical standards ("ITS") and guidelines for the new regime and these have been endorsed by the European Commission, are legally binding and apply to all national regulators under the scope of Solvency II.

11 Many of the technical requirements of Solvency II are contained in Commission Delegated regulation (EU) 2015/35, known as the Delegated Acts, adopted by the European Commission in October 2014.

Own funds and capital

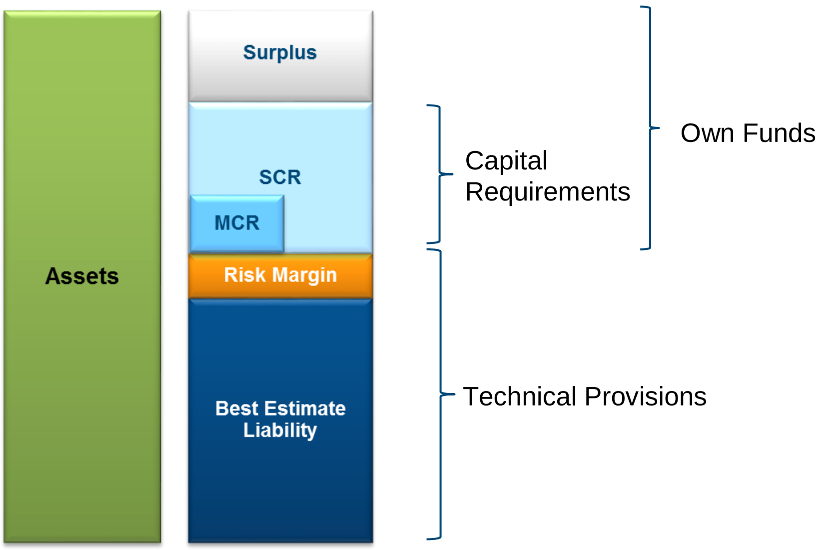
12 Under the Solvency II regime, the excess of assets over liabilities, plus any subordinated liabilities, is known as Own Funds. Own Funds can be thought of as the capital available in the company to cover capital requirements.

13 Under Solvency II, companies are required to classify their Own Funds into three tiers, which broadly represent the quality of the Own Funds in relation to their ability to absorb losses. The Own Funds of the highest quality are classified as Tier 1. In order to be classified as Tier 1, Own Funds must exhibit both of the following:

- Permanent availability, i.e. the item is available, or can be called up on demand, to fully absorb losses on a going concern basis, as well as in the case of winding up.
- Subordination, i.e. in the case of winding up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations towards policyholders and beneficiaries of insurance and reinsurance contracts, have been met.

14 Own Funds that are classified as Tier 2 or Tier 3 are of a lower quality, with less ability to fully absorb losses.

15 The following diagram shows the structure of the balance sheet for a UK life insurance company under a Solvency II market consistent valuation.



Regulatory approvals under Solvency II

16 Any UK firms intending to use an internal model, transitional measures, a matching adjustment or a volatility adjustment (as described in the paragraphs below) must apply to the PRA for approval. Irish firms must apply to the CBI for approval

17 At the end of 2016, 16 life insurers in the UK had applied and been approved for the volatility adjustment and 18 life insurers had been approved for the matching adjustment. This compares to seven life insurers approved for the volatility adjustment and none for the matching adjustment in Ireland.

18 Under the Solvency II regulations, the PRA has the right to remove approvals for the use of any of these measures, if the firm is found to be in breach of the restrictions and conditions on which the original approval was based.

19 Firms must apply to the PRA if they wish to make changes to the terms of their existing approvals. For example, firms would seek approval from the PRA to make a major change to their internal model and would not be expected to submit more than one major change application per year. A major change can comprise a single change or an accumulation of minor changes that, in aggregate, comprise a major change.

20 Additionally, firms are permitted to seek approval to undertake a recalculation of their Transitional Measure on Technical Provisions (the "TMTP" as described below) every six months if their risk profile has changed materially since the previous recalculation.

21 For Irish firms the same process applies, with the CBI fulfilling the role of the PRA.

The matching adjustment

22 In calculating the BEL, the Solvency II regulations permit firms to apply to their regulator to make use of the "matching adjustment". The matching adjustment is an increase to the discount rate used in the calculation of the BEL that allows firms to take credit for the additional investment return in excess of the risk free rate (swap rates under Solvency II) that they expect to earn from a "hold to maturity" investment strategy for their less liquid assets, which are used to back their most stable and predictable liabilities, typically non-profit in-payment annuity liabilities.

23 Firms using the matching adjustment are subject to various restrictions around the types of asset that are permitted to back the relevant liabilities, the circumstances in which the assets may be traded, and the extent to which mismatching of asset and liability cash flows is permitted.

The volatility adjustment

24 Where insurers have liabilities that are not eligible for use of the matching adjustment, the Solvency II regulations permit firms to apply to their regulator to make use of the "volatility adjustment". The volatility adjustment is an increase to the discount rate used in the calculation of the BEL (other than for liabilities that are subject to the matching adjustment) which aims to prevent forced sales of assets in the event of extreme bond spread movements.

25 The volatility adjustment is based on the spreads on a representative portfolio of assets for each relevant currency and the risk-free discount curves which include the volatility adjustment are published by EIOPA.

The transitional measures

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

- The Transitional Measure on Technical Provisions ("TMTP") allows firms to phase in the increase in technical provisions under Solvency II Pillar 1 (in relation to business written prior to 1 January 2016) over a sixteen year period. In the UK, the increase is measured relative to the firm's Solvency I Pillar II liabilities.

- The Transitional Measure on the Risk-Free Interest Rate allows firms to phase in any reduction in the discount rate used to calculate their liabilities under Solvency II relative to the previous regime over a sixteen year period.

27 For a given firm, the TMTP is calculated as at the implementation date of Solvency II, i.e. 1 January 2016. The TMTP is calculated as the difference, to the extent that this difference is a positive number, between the firm's technical provisions under Solvency II and the firm's insurance liabilities under the previous Solvency I Pillar II regime.

28 A further test is then carried out to determine whether deducting the calculated TMTP from the firm's Solvency II technical provisions at 31 December 2015 would result in a Financial Resources Requirement ("FRR") under Solvency II that is lower than the firm's FRR under the previous Pillar I and Pillar II regimes at the same valuation date.

29 The FRR for a given solvency regime is calculated as the total liabilities plus the firm's capital requirement under that regime. If the Solvency II FRR after deduction of the TMTP is lower than the FRR under the Solvency I regime (Pillar I and Pillar II) then the calculated TMTP must be reduced to a level that ensures that this is no longer the case. The purpose of the FRR test is to ensure that firms are not able to hold lower amounts of financial resources under Solvency II than under the Solvency I regime as a result of the use of the TMTP.

30 The final calculated TMTP is deducted from the firm's technical provisions in its Solvency II balance sheet at 1 January 2016. For valuation dates after 1 January 2016, the TMTP that was calculated at 1 January 2016 is reduced linearly to zero over a sixteen year period.

31 The PRA has stated publicly[3] that it regards the financial benefit conferred by the TMTP as Tier 1 capital.

32 The Solvency II Directive provides for firms' TMTPs to be subject to recalculation every two years, with more frequent recalculations permitted if the firm's risk profile has materially changed, as described above.

Ring-fenced funds

33 Solvency II includes the concept of a ring-fenced fund. This refers to any arrangement where an identified set of assets and liabilities are managed as though they were a separate undertaking, meaning that there are restrictions on the extent to which surplus in the ring-fenced fund may be transferred to shareholders or used to cover losses outside the ring-fenced fund.

34 In the UK, many firms have set up ring-fenced funds in order to reflect the arrangements applicable to their with-profits funds (as defined under the previous regulatory regime) and the with-profits and non-profit business within the with-profits fund.

The long-term fund and shareholders' fund in the UK

35 Prior to the implementation of Solvency II, proprietary firms in the UK writing long-term insurance business were required to identify the assets attributable to their long-term insurance business and keep those assets separate from shareholder funds in what was referred to as a long-term insurance fund (the "LTF"). The other assets of a proprietary company were typically allocated to the shareholders' fund (the "SHF"). Under the PRA rules, the assets in the LTF were only available to be used to support the firm's long-term insurance business and firms were required to maintain assets in the LTF sufficient in value to cover the fund's mathematical reserves.

36 Following the implementation of Solvency II, the requirement to maintain a separate LTF has been removed and therefore a firm's "fund structure" now consists of the ring-fenced funds and the business outside of the ring-fenced funds. This business outside the ring-fenced funds is often called the "non-profit fund" (if it is all long-term business) or the "shareholder backed fund" (this could include short-term or general insurance business) but whatever the name it includes the assets and liabilities of what were, under the previous regime, called the non-profit fund (in the LTF) and the shareholders' fund (outside of the LTF).

37 Although not required to do so for regulatory purposes, some firms, including PAC, continue to maintain a notional fund for accounting purposes in respect of long-term business outside of the ring-fenced funds. Such a notional fund is sometimes referred to as the non-profit fund.

[3] http://www.bankofengland.co.uk/publications/Pages/speeches/2015/829.aspx

APPENDIX E: THE REGULATION AND GOVERNANCE OF INSURANCE COMPANIES IN THE UK AND IRELAND

The regulators in the UK

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

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

3 The PRA has statutory objectives to promote the safety and soundness of the insurers that it regulates, and to contribute to ensuring that policyholders are appropriately protected. More generally, these statutory objectives can be advanced by seeking to ensure that regulated UK insurers have resilience against failure (although this is not a 'zero failure' regime) and that disruption to the stability of the UK financial system from regulated UK insurers is minimised.

4 The FCA regulates the conduct of all UK financial services firms in relation to consumer protection, market integrity and the promotion of competition in the interests of consumers. The FCA does not have conduct of business responsibility for the policies serviced under the EU's passporting regime as responsibility for the conduct of business of such policies lies with the host state supervisors.

The regulator in Ireland

5 In Ireland, responsibility for the regulation of insurance companies rests with the CBI.

6 The CBI also carries out the prudential regulation and supervision of banks, building societies, credit unions, insurance intermediaries and investment firms.

7 The CBI aims to ensure that regulated firms are financially sound and safely managed. Regulation of financial institutions and markets is undertaken through risk-based supervision, which is underpinned by credible enforcement deterrents. This mandate is delivered through a range of tools which include:

- Supervising banks within the Single Supervisory Mechanism ("SSM") framework;
- Monitoring of regulatory returns filed with the Bank;
- Approval of persons under the relevant fitness and probity standards; and
- Taking enforcement actions when necessary.

8 The CBI aims to take a proportionate approach to its actions as an intrusive and assertive regulator and does not seek to ensure a 'zero-failure' system of regulation and supervision but to safeguard that any firms that fail do so in a way that avoids significant disruption to financial services or consumers.

9 The CBI and the PRA are aligned in their approach to prudential supervision in terms of the adherence to the Solvency II regime, adherence to the appropriate risk appetite statements, and the standards of governance required.

10 The CBI also regulates the conduct of all financial services firms in relation to consumer protection and conduct of business. As with the FCA in the UK, the CBI does not have conduct of business responsibility for the policies serviced under the EU's passporting regime as responsibility for the conduct of business of such policies lies with the host state supervisors.

The governance of long-term insurers in the UK and Ireland

Governance in the UK

11 The Board of Directors of a proprietary long-term insurer is the firm's governing body, and is ultimately responsible for setting the strategic direction of the firm, overseeing the activities of the firm's day-to-day management and approving the firm's financial statements.

12 Under Solvency II, all insurers are required to establish the following key functions:

- Actuarial function: This function is required, inter alia, to coordinate the calculation of technical provisions, and to ensure the appropriateness of the methodologies, underlying models and assumptions used in the calculation of technical provisions.
- Compliance function: This function is required, inter alia, to advise the insurer on compliance with the Solvency II regulations.
- Internal audit function: This function is required, inter alia, to evaluate the adequacy and effectiveness of the insurer's internal control system and other elements of its system of governance. The internal audit function is required to be objective and independent from the company's operational functions.
- Risk management function: This function is required, inter alia, to facilitate the implementation of the insurer's risk management system.

13 These functions are not defined by the Solvency II regulations as being performed by an individual; however, in the UK, the PRA has introduced a governance regime for UK insurers called the Senior Insurance Managers Regime ("SIMR") which became effective on 7 March 2016, and which defines a set of senior insurance management functions ("SIMF"), including:

- SIMF 1 - Chief Executive Officer;
- SIMF 2 - Chief Financial Officer;
- SIMF 4 - Chief Risk Officer;
- SIMF 5 - Head of Internal Audit; and
- SIMF 20 - Chief Actuary.

14 Under SIMR, the persons having responsibility for the actuarial function, internal audit function and risk management under Solvency II are the Chief Actuary, Head of Internal Audit and Chief Risk Officer respectively, and the individuals responsible for these functions will be subject to PRA approval.

15 In addition to the roles listed above, those firms with with-profits business must appoint an actuary (or actuaries) to perform the "with-profits actuary function" (the "WPA"). This individual's responsibilities include advising the firm's management on the key aspects of the discretion to be exercised affecting those classes of the with-profits business of the firm in respect of which he has been appointed. The WPA role is SIMF 21 under SIMR.

16 Firms with with-profits business must appoint a With-Profits Committee ("WPC") (or a "with-profits advisory arrangement" if appropriate given the size, nature and complexity of the fund in question) in respect of the with-profits business. The WPC's role is to advise and provide recommendations to the firm's governing body on the management of the with-profits business, and to act as a means by which the interests of with-profits policyholders are appropriately considered within a firm's governance structures.

Governance in Ireland

17 As in the UK, the Board of Directors of a proprietary long-term insurer is the firm's governing body, and is ultimately responsible for setting the strategic direction of the firm, overseeing the activities of the firm's day-to-day management and approving the firm's financial statements.

18 In Ireland, the CBI has implemented a Fitness and Probity Regime ("F&P Regime") for Irish insurers which defines a set of Pre-Approval Controlled Functions ("PCFs"), including:

- PCF-1 – Executive Director;
- PCF-2 – Non-Executive Director;
- PCF-8 - Chief Executive Officer;
- PCF-11 - Head of Finance;
- PCF-13 - Head of Internal Audit;
- PCF-14 - Chief Risk Officer;
- PCF-18 - Head of Underwriting; and
- PCF-48 - Head of Actuarial Function.

19 Under the F&P Regime, the persons having responsibility for the actuarial function, internal audit function and risk management under Solvency II are the Head of Actuarial Function, Head of Internal Audit and Chief Risk Officer respectively, and the individuals responsible for these functions will be subject to CBI pre-approval.

20 Unlike in the UK, those firms with with-profits business are not required to appoint an actuary (or actuaries) to perform a 'with-profits actuary function". Instead, in situations where "any rights of life assurance policyholders entitle them to participate in profits related to a particular fund or part of a fund" the Head of Actuarial Function is given an explicit requirement to make "a recommendation on any allocation of profits related to those policyholder rights".

21 There is no requirement in Ireland for firms with with-profits business to appoint a WPC or a WPA.

APPENDIX F: COMPLIANCE WITH THE PRA POLICY STATEMENT

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

PRA Policy Statement Reference	Requirement	Scheme Report paragraph reference
2.30 (1)	Who appointed the independent expert and who is bearing the costs of that appointment	1.10, 1.16
2.30 (2)	Confirmation that the independent expert has been approved or nominated by the appropriate regulator.	1.14
2.30 (3)	A statement of the independent expert's professional qualifications and (where appropriate) descriptions of the experience that fits him for the role	1.13
2.30 (4)	Whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest	1.15
2.30 (5)	The scope of the report	1.7 to 1.9
2.30 (6)	The purpose of the scheme	Section 7
2.30 (7)	A summary of the terms of the scheme in so far as they are relevant to the report	Section 7
2.30 (8)	What documents, reports and other material information the independent expert has considered in preparing his report and whether any information that he requested has not been provided	Appendix J
2.30 (9)	The extent to which the independent expert has relied on: (a) information provided by others; and (b) the judgment of others	Section 1
2.30 (10)	The people on whom the independent expert has relied and why, in his opinion, such reliance is reasonable	Sections 1 and 4
2.30 (11)	His opinion of the likely effects of the scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee	Section 8 Section 9 Section 10
2.30 (12)	His opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme	Section 8
2.30 (13)	What matters (if any) that the independent expert has not taken into account or evaluated in the report that	1.31

	might, in his opinion, be relevant to policyholders' consideration of the scheme	
2.30 (14)	For each opinion that the independent expert expresses in the report, an outline of his reasons.	Sections 7-12
2.32 (1)	The summary of the terms of the scheme should include a description of any reinsurance agreements that it is proposed should pass to the transferee under the scheme	Section 7
2.32 (2)	The summary of the terms of the scheme should include a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred	7.22
2.33 (1)	The independent expert's opinion of the likely effects of the scheme on policyholders should include a comparison of the likely effects if it is or is not implemented	Section 12
2.33 (2)	The independent expert's opinion of the likely effects of the scheme on policyholders should state whether he considered alternative arrangements and, if so, what	4.9
2.33 (3)	The independent expert's opinion of the likely effects of the scheme on policyholders should, where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences he considers may be material to the policyholders	Section 8, 9, 10
2.33 (4)	The independent expert's opinion of the likely effects of the scheme on policyholders should include his views on: (a) the effect of the scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer; (b) the likely effects of the scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect: (i) the security of policyholders' contractual rights; (ii) levels of service provided to policyholders; or (iii) for long-term insurance business, the reasonable expectations of policyholders; and (c) the cost and tax effects of the scheme, in so far as they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations	Section 8, 9, 10, 11, 12
2.35 (1)	For any mutual company involved in the scheme, the report should describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders	Not applicable
2.35 (2)	For any mutual company involved in the scheme, the report should state whether, and to what extent,	Not applicable

	members will receive compensation under the scheme for any diminution of proprietary rights	
2.35 (3)	For any mutual company involved in the scheme, the report should comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without.	Not applicable
2.36 (1)	For a scheme involving long-term insurance business, the report should describe the effect of the scheme on the nature and value of any rights of policyholders to participate in profits	Sections 8, 9, 10
2.36 (2)	For a scheme involving long-term insurance business, the report should, if any such rights will be diluted by the scheme, how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders;	Not applicable
2.36 (3)	For a scheme involving long-term insurance business, the report should describe the likely effect of the scheme on the approach used to determine: (a) the amounts of any non-guaranteed benefits such as bonuses and surrender values; and (b) the levels of any discretionary charges	Sections 8, 9 ,10
2.36 (4)	For a scheme involving long-term insurance business, the report should describe what safeguards are provided by the scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm	Section 12
2.36 (5)	For a scheme involving long-term insurance business, the report should include the independent expert's overall assessment of the likely effects of the scheme on the reasonable expectations of long-term insurance business policyholders	Sections 8, 9 ,10
2.36 (6)	For a scheme involving long-term insurance business, the report should state whether the independent expert is satisfied that for each firm the scheme is equitable to all classes and generations of its policyholders	13.3
2.36 (7)	For a scheme involving long-term insurance business, the report should state whether, in the independent expert's opinion, for each relevant firm the scheme has sufficient safeguards (such as principles of financial management or certification by a with-profits actuary or actuarial function holder) to ensure that the scheme operates as presented.	Section 12

APPENDIX G: COMPLIANCE WITH THE FCA PROPOSED GUIDANCE

The table below indicates how I have complied with the proposed guidance of the FCA to the review of Part VII insurance business transfers (“GC17/5”, dated 15/05/2017) that pertain to the form of the Scheme Report.

FCA GC17/5 reference	Requirement	IE Report paragraph reference
6.2	Report is constructed in such a way that it is easily readable and understandable by all its users, paying attention to the following:	
	• Technical terms and acronyms should be defined on first use.	Appendix I
	• There should be an executive summary that explains, at least in outline, the proposed transfer and the IE’s conclusions.	Section 2
	• The business to be transferred should be described early in the report.	Section 2
	• The detail given should be proportionate to the issues being discussed and the materiality of the Transfer when viewed as a whole. While all material issues must be discussed, IEs should try to avoid presenting reports that are disproportionately long.	Sections 8, 9, 10
	• IEs should prepare their reports in a way that makes it possible for non-technically qualified readers to understand.	
6.3	Report must consider and compare: • Reasonable benefit expectations (including impact of charges). • Type and level of service (including claims handling). • Management, administration and governance arrangements.	Sections 8, 9, 10
The level of reliance on the Applicants assessments and assertions		
6.6	Question the adequacy of assessments carried out by Applicants before relying on them to reach own conclusions (including requesting additional work and evidence from Applicants in order to support their assertions).	4.23 to 4.37
6.7	Explain the nature of any challenges made to the Applicants and the outcome of these within the IE report, rather than just stating the final position.	Documented separately
6.8	Where conclusions are supported solely or largely by statements such as ‘I have discussed with the firm’s management and they tell me that…’ followed by ‘I have no reason to doubt what they have told me…’, then:	
	• Where a feature of the proposed transfer forms a significant part of the IE’s own assessment of the Scheme’s impact, the IE should review relevant underlying material, rather than relying on the Applicants’ analysis of the material and subsequent assertions.	Appendix J
	• If there are concerns about matters that fall outside the IE’s sphere of expertise, such as legal issues, the Applicants must provide the IE with any advice that they have received. If the issue is significant or remains uncertain, the IE must ensure that the Applicants had obtained appropriate advice from a suitably qualified independent subject matter expert.	1.27
6.9	IE has challenged calculations carried out by the Applicants if there is cause for doubt on review of the Scheme and supporting documents. As a minimum, the IE should:	
	• review the methodology used and any assumptions made to satisfy themselves that the information is likely to be accurate and to challenge it where appropriate	1.25
	• challenge the factual accuracy of matters that, on the face of the documents or considering the IE’s knowledge and experience, appear inconsistent, confusing or incomplete	Not applicable
6.10	Documents provided by the Applicants have been challenged where they contain an insufficient level of detail or analysis. For example:	

	• Applicants' assertions that service levels will be maintained to at least the pre-transfer standard: IE should include not only details of the Applicant's plans and any gap analyses that have been produced but also include their view of their adequacy.	Section 8
	• Change in governance arrangements in the Transferee that may lead to poorer customer outcomes: the IE must review and compare the governance arrangements in the Transferor which produce good customer outcomes (e.g. any committees with conduct responsibilities) within the Transferee's governance arrangements.	Section 8
	• Consideration of the strain on resources that may occur post-transfer and that could impact on the service standards of the Transferee's existing customers and/or control over conduct of business risk. The IE report should include a review of relevant management information indicators and related contingency planning.	8.97
Sufficient comparative regulatory framework analysis		
6.11	Where the regulatory framework is different for the Transferor and Transferee, the IE has carried out sufficient analysis of the differences including, where appropriate, taking independent advice.	Section 3, 8, 11 Appendix D
6.12	For cross-border transfers ensure there is a sufficiently detailed analysis of regulatory protections post-transfer. This can include:	
	• The extent to which existing regulatory requirements and protections continue, including whether there is continued access to the Financial Ombudsman Service and the Financial Services Compensation Scheme.	Section 3
	• The comparative regulatory requirements and conduct protections across any relevant jurisdictions, including but not limited to complaints or compensation bodies compared to the UK.	Section 3, Appendix D
	• Analysis of the likely impacts. For example, the number of Policyholders affected, the size of possible claims and any potential mitigations.	Sections 8-12
	• Whether a Solvency II equivalence assessment is necessary.	Section 3
6.13	The IE report must contain a statement describing the two regimes as well as a considered comparison, highlighting points of significant difference that could adversely impact Policyholders. The level of detail to be included must be sufficient for the Court to be in a position to be satisfied.	Section 3
6.14	If the IE's analysis is inconclusive or there are potential conduct risks due to differences in the regulatory framework, we expect to see sufficient explanation of how Policyholders may be affected and the Applicant's proposals to mitigate these risks.	Section 11
6.15	When stating that the IE is satisfied by referencing the Scheme, the IE must adequately explain how the features have led to their satisfaction. The IE must include both the evidence and their reasoning.	Sections 8-12
Balanced judgements and sufficient reasoning		
6.16	The IE must state in their report whether they are certain there will be no material adverse impact to Policyholders or whether this is their best judgement, but lacks certainty. In these instances, the IE must consider the following:	
	• Where the IE takes the view that there is probably no material adverse impact, the IE must challenge the Applicants about further work the Applicants could undertake to enable the IE to be satisfied to a greater degree.	Documented separately
	• The IE should challenge the Applicants in order to gain the necessary level of confidence that their report's conclusions are robust. Applicants and IEs should be aware that they will need to consider how any proposed changes/mitigations will impact all Policyholder groups.	Section 8, 9, 10

6.17	The IE must check that the documents they are relying, and forming judgements, on are the most up-to-date available when finalising their report.	1.25
6.18	If market conditions have changed significantly since the IE's analysis was carried out and they formed their judgement, the Applicants must discuss any changes with the IE and for the IE to update their report as necessary. If the Scheme document has been finalised, the IE should comment in more detail in their Supplementary Report or by issuing supplementary letters to the Court to confirm whether their judgement is unchanged.	Section 1
Sufficient regard to relevant considerations affecting Policyholders		
6.19	Consider all relevant issues for each individual group of Policyholders in both firms, as well as how an issue may impact each group. The IE is expected, when giving their opinion, to consider the:	
	• Current and proposed future position of each Policyholder group	Section 8-10
	• Potential effects of the transfer on each of the different Policyholder groups	Section 8-10
	• Potential material adverse impacts that may affect each group of Policyholders, how these impacts are inter-related and how they will be mitigated	Section 8-10
6.20	Consider whether the groups of affected Policyholders have been identified appropriately. For example, this could include instances where certain Policyholder groups' services are provided by an outsourced function which is changing, but other Policyholder groups do not.	13.13
6.21	Review and give opinion on administrative changes affecting Policyholders, including:	
	• Consideration of the impact of an outsourcing agreement entered into by the parties before the Part VII process began, where the administration duty 'moved' from the Transferor to the Transferee in preparation for the transfer. Provide a comparison of the pre and post-outsourced administration arrangements so the IE can clearly review and compare any changes to Policyholder positions and service expectations.	Sections 8-10
	• For the case where the IE concludes that because the transfer will not create any change to the administrative arrangements, there will be no material impact on Policyholders: consider what might happen if the Transfer does not proceed and the possibility that the outsourcing agreement could be cancelled, returning the administrative arrangements to the original state. In such circumstances, consider the impact on Policyholders and claimants of the outsourcing agreement as part of the Part VII process.	Sections 8-12
6.22	Review and provide opinion on all relevant issues for all Policyholder groups where reinsurance was entered into in anticipation of a transfer:	
	• Some firms pre-empt regulatory scrutiny by buying reinsurance against risks before they begin the transfer process. In these instances, consider if it is appropriate to compare the proposed Scheme with the position the Transferor would be in if they did not benefit from the reinsurance contract.	Not applicable
	• If the transfer is not sanctioned and the reinsurance either terminates automatically or can be terminated by the Transferee, consider the Scheme as if the reinsurance was not in place.	Not applicable
6.23	If the IE identifies particular sub-groups of Policyholders whose benefits, without other compensating factors, are likely to be adversely affected, the IE should take into account the Transferor's obligations under Principle 6 (Customers' interests) of the FCA's Principles for Businesses.	Not applicable
6.24	Ensure there is consideration and analysis of alternatives when a loss is expected for a particular subgroup of Policyholders, even if the IE does not consider this loss to be material.	Section 8

6.25	Provide the analysis outlined in 6.24 even if the IE is able to conclude that the Policyholder group as a whole is not likely to suffer material adverse impact, even if a minority may. For example where: • Some Policyholders within a group/sub-group will suffer higher charges post-transfer because the Transferee has a different charging structure. • Some Policyholders within a group/sub-group had free access to helplines that will no longer be available or have a significantly altered service after the transfer.	Not applicable Not applicable
6.26	Ensure that no conclusions are reached based on the balance of probabilities and without adequately considering the possible impact on all affected Policyholder groups.	Not applicable
6.28	Present the consideration, evidence and reasoning to support the IE's opinion that a change due to the Part VII Transfer will not materially adversely impact a group of Policyholders.	Sections 8-12
Commercially sensitive or confidential information		
6.29	When considering commercially sensitive information, consider Policyholders interests as the information will not be publically available.	Risk Appetite Statements and costs of Scheme
6.30	In these situations, document the analysis and the information relied upon. Consider sending a separate document with further details, solely for the Court's use and not for public disclosure	Appendix J
The level of reliance on the work of other experts		
6.31	For large scale and complex insurance business transfers, if relying on the analytical work of other qualified professionals, it is still expected the IE to have carried out their own review of this analysis to ensure they have confidence in, and can place informed reliance on, the opinions they draw from another professional's work.	4.24
6.32	Obtain a copy of any legal advice given to the Applicants. This should be in writing or transcribed, and approved by the advisor. It should also be in a sufficiently final form for the IE to be able to review and rely on it. The IE should reflect this review, and the opinions drawn from the advice, within their report.	Section 4, Appendix J
6.33	If referring to factors outside of expertise and relying on advice received by the Applicants, the IE should consider whether or not to obtain their own independent advice on the relevant issue.	4.34 to 4.37
6.34	Consider if the IE needs to obtain separate legal advice, this will depend on the significance and materiality of the issue.	1.26
6.35	Consider whether it is reasonable for the IE to rely on advice and whether their independence is compromised by doing so. Whether or not the legal advisor has acknowledged that it owes a duty of care to the IE will be relevant to this consideration. Depending on how complex the legal issue is, IEs who rely on the Applicants' legal advice and merely state that they have no reason to doubt the advice and/or that it is consistent with their understanding of the position or experience of similar business transfers may be challenged.	4.34 to 4.37
6.36	When deciding whether to obtain independent legal advice, the IE should consider, amongst other things, the following: • The significance of the issue and the degree of potential adverse impacts to Policyholders if the position turns out to be different from that considered likely in the legal advice. • How much the IE relies on the legal advice to reach their conclusions and, if they did not rely on the legal advice, would the report contain too little information to justify the view that there is no material adverse impact? • The difficulty, novelty or peculiarity of the issue to the Applicants' own circumstances.	Section 4

	• Applicants' proposals to explain to Policyholders in communication documents the issues involved, any uncertainty, and any residual risks. • Whether, depending on the issue's significance or uncertainty, the Applicants have obtained an adequate level of advice. Where relevant, whether the Applicants have engaged external advisors with the appropriate expertise and qualifications for the specific subject or jurisdiction. • Whether any advice already received is heavily caveated, qualified or there is a significant degree of uncertainty.	4.36 Not applicable
6.37	The IE may need to explain why they consider that they do not need to get independent advice to be adequately satisfied on a point. The IE's assessment should consider whether there are credible alternative arguments that could be made, whether identified in the Applicant's advice or otherwise. Consider where risks are identified with no suggestion about how they can be mitigated, or what the impact on Policyholders may be if the risks do occur. These considerations would allow the IE to consider the worst case scenario of these impacts.	4.36
6.38	Consider the Applicant's contingency plans if the risks identified in the legal advice occur and whether this may create negative consequences for Policyholders.	Not applicable
6.40	Consider obtaining a legal opinion on whether a transfer involving overseas Policyholders will be recognised in non-EEA jurisdictions. Should the work of overseas legal advisors be relied upon, the IE should not use such advice as the sole basis of their conclusion that there are no materially adverse effects, the IE is expected to consider the position if the advice turns out to be incorrect.	Not applicable
6.41	If the IE is uncertain and cannot form a conclusion on an issue, they may wish to obtain further independent legal advice to ensure they can reach a more considered conclusion. Additionally: • Get a legal opinion that states that it is likely that an overseas jurisdiction will recognise the transfer, but that there is a degree of uncertainty. The IE should consider, and be satisfied with, what the impact on Policyholders may be if the transfer is not recognised overseas. • Where the Transferor is to have their authorisations cancelled and wind up, then the IE should consider and explain what may happen if the transfer is not recognised in the overseas jurisdiction. • Consider obtaining advice that even if the Scheme is not formally recognised in another jurisdiction, the Courts of that jurisdiction would still act to prevent the Transferee from denying that it is liable. • In cases with unresolved risk or uncertainty, the IE should properly consider, and see legal advice which explains, what the impact on Policyholders would be and any ways to mitigate this impact. Mitigates could include Transferee indemnities in the Scheme which are directly enforceable by Policyholders in either the UK or the relevant jurisdiction.	Not applicable Not applicable Not applicable Not applicable
6.42	Where the Transferor remains in existence and the Scheme anticipates that the Policyholders will still be able to claim against the Transferor; an IE may want to seek an independent legal opinion on how likely it is that the Transferee will indemnify the Transferor in these circumstances.	Not applicable
6.43	Ensure the likelihood for consumers to be adversely affected is low. The IE should take a view on that and seek the appropriate reassurances.	Sections 8-12
6.45	At the start of the document, the IE should provide a description of where they propose to rely on information provided by the Applicants. Overly general reliance will indicate a lack of critical assessment or challenge.	1.24 to 1.31
6.47	If the report does not reach a clear conclusion, either generally or on a specific issue, the IE report should state clearly:	

	• That the IE has considered and is satisfied about the likely level of impact on a particular point. Where uncertainty remains, the IE report needs to include details of, and reasons for, this uncertainty as well as any further steps the IE has taken to get clarification, such as seeking further advice from a subject matter expert. • How the IE satisfied themselves about the identified uncertainty and formed an opinion on any potential impact.	4.18 to 4.22 4.18 to 4.22
Demonstrating challenge		
6.48	To ensure the IE report is complete and considered there should be challenge from all involved parties. Including evidence that Applicants have made appropriate challenges, particularly when believed that the IE has not fully addressed issues. Applicants have an interest in ensuring that the Court, regulators and Policyholders are able to rely on the IE report, taking into account to the IE's disclaimers. Applicants should make the challenges without compromising the IE's independence.	1.18
6.49	To ensure effective two-way challenge it is expected the IE engages with FCA or PRA approved persons of sufficient seniority at the Applicant firm, such as senior actuaries, including possibly the Chief Actuary, the Chief Financial Officer, Senior Underwriters and so on.	Appendix J
6.50	IEs who are members of the Institute & Faculty of Actuaries should pay proper regard to the Technical Actuarial Standards (TAS) published by the Financial Reporting Council,10 particularly those for compiling actuarial reports.	1.32
6.51	IEs should be aware of TAS (TAS 100: Principles for Technical Actuarial Work and TAS 200: Insurance) specifically apply to technical actuarial work to support Part VII Transfers.	1.32
6.52	Ensure compliance with paragraph 5 of TAS 100 which states that actuarial communications should be 'clear, comprehensive and comprehensible so that users are able to make informed decisions understanding the matters relevant to the actuarial information' and to paragraph 5.2 of TAS 100 which states that 'the style, structure and content of communications shall be suited to the skills, understanding and levels of relevant technical knowledge of users'.	1.32
6.53	Actuarially qualified IEs and peer reviewers should also bear in mind the Actuaries' Code and Actuarial Profession Standards documents APS X2: Review of Actuarial Work and APS L1: Duties and Responsibilities of Life Assurance Actuaries.	1.33
Review of the communications strategy		
7.3	IEs should include consideration of the proposed communications strategy and any supporting requests for dispensations from the Transfer Regulations in their report. There should be evidence that the IE has challenged proposed communications that are not clear and fair and do not adequately explain the transfer and the potential impacts on Policyholders and how these have been addressed.	11.17

APPENDIX H: CERTIFICATE OF COMPLIANCE

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

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

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

APPENDIX I: GLOSSARY OF TERMS

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

A

APS	Actuarial Profession Standards
Asset share	A measure of a policy's value in the absence of guarantees, defined as the total premiums paid by policyholders, accumulated by actual investment returns, less attributable expenses, benefits paid and other relevant deductions.

B

BEL	The best estimate liability under Solvency II

C

CBI	Central Bank of Ireland

E

EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
ELAS	The Equitable Life Assurance Society

F

FCA	Financial Conduct Authority
FOS	Financial Ombudsman Service
FSCS	Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
FTSE	Financial Times Stock Exchange

H

HMRC	HM Revenue & Customs

I

ITS	Implementing Technical Standards

M

MA	Matching Adjustment
MAP	Matching Adjustment Portfolio
MCR	Minimum Capital Requirement

O

ORSA	Own Risk and Solvency Assessment

P

PAC	The Prudential Assurance Company Limited
PDL	Prudential Distribution Limited
PFO	Polish Financial Ombudsman

PIA	Prudential International Assurance plc
PGIM	Prudential Group Internal Model
PRA	The Prudential Regulation Authority
S	
SCR	Solvency Capital Requirement
SHF	Shareholders’ Fund
SIMF	Senior Insurance Management Functions
SIMR	The PRA’s Senior Insurance Managers Regime
T	
TAS	Technical Actuarial Standards
TEU	Treaty on European Union
TCF	Treating Customers Fairly
TMTP	Transitional Measure on Technical Provisions
W	
WPA	With-Profits Actuary
WPC	With-Profits Committee
WPF	With-Profits Fund

APPENDIX J: DATA RELIED UPON

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

Document	Date of document
PIA Project Brexit Business Case	30/08/2017
Mailing Population Approach	15/06/2018
The SFCR of PIA	May 2018
The SFCR of PAC	May 2018
The PAC Shareholder Risk Appetite Framework (2015)	17/04/2015
SRA Calibration under Solvency II	11/11/2015
The PIA Risk Appetite Statement (May 2017)	30/05/2017
The 2017 ORSA of PIA	18/12/2017
The 2017 ORSA of PAC	24/04/2017
Scheme Document	08/05/2018
Financial Impact Tables of the Scheme from Prudential	25/05/2018
PAC Annual Actuarial Function Report	19/01/2017
PIA Annual Actuarial Function Report	23/11/2016
Note on Operation of the Polish Underpin and the impact of the Scheme on it	September 2017
Principal of Transfer paper presented to the PAC WPC	22/09/2017
Note on Operation of Polish With-profits Expenses	September 2017
Q&A Policyholder Circular	03/10/2017
Draft Policyholder Letters to Policyholders for Scheme	15/06/2018
The report of the PAC Chief Actuary on the proposed transfer	17/05/2018
The report of the PAC With-Profits Actuary on the proposed transfer	09/05/2018
The report of the PIA Head of Actuarial Function on the proposed transfer	17/05/2018
PIA PAC Reinsurance Agreements for transferring business	21/05/2018
Cost allocation proposal for Scheme	15/01/2018
PwC Policyholder taxation analysis for Malta, France, Germany and Ireland	19/01/2018
Deloitte Polish tax consequences memo	18/01/2018
Slaughter and May FSCS Position note	22/01/2018
PIA 100K simulations spreadsheet for year-end 2016	15/02/2018
AL Goodbody note on ring-fencing	07/02/2018
CBI letter with Conditions & Certificate of Authorisation	08/01/2016
Moody’s annual default study table of cumulative global default rates 1920-2017	15/02/2018
PIA Risk Function Update Note on Capita	08/02/2018