SCOTTISH FRIENDLY ASSURANCE SOCIETY LTD

Transfer of certain long term insurance business from Canada Life Limited to Scottish Friendly Assurance Society Limited

Final Report of the Chief Actuary of Scottish Friendly Assurance Society

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Date: 7 June 2019

Contents

1 Purpose of the Report and overall conclusions

1.1. Scottish Friendly Assurance Society Limited ("Scottish Friendly") has agreed to acquire a legacy portfolio of long-term insurance business from Canada Life Limited ("Canada Life"). I refer to the policies and related assets and liabilities transferring as a result of this agreement as the "Transferring Business".

1.2. The proposed transfer of the Transferring Business to Scottish Friendly will be achieved by a Scheme of Transfer ("the Scheme") under Part VII of the Financial Services and Markets Act 2000 ("FSMA"). If approved, the Scheme is expected to take effect at 00.01 on 1 November 2019.

1.3. The purpose of this report is to consider the impact of the proposed Scheme on the benefit expectations of the existing policyholders of Scottish Friendly, the future security of these benefits and how the policies will be managed in future.

1.4. The report is written for the Board of Scottish Friendly in my capacity as Chief Actuary for Scottish Friendly. As well as the Board, I expect this report to be considered by the Independent Expert, the High Court, the Prudential Regulation Authority ("PRA"), the Financial Conduct Authority ("FCA") and any overseas Regulators and Courts in forming their own judgements about the Scheme. Copies of my report have been provided to Mr Stephen Makin, in his capacity as the With-Profits Actuary of Scottish Friendly, and to Canada Life.

1.5. This report will also be published on the Scottish Friendly website (https://www.scottishfriendly.co.uk/canada-life).

1.6. This report and the underlying preparation work that has been carried out is, in my opinion, compliant with the relevant Technical Actuarial Standards issued by the Financial Reporting Council ("FRC") for members of the Institute and Faculty of Actuaries ("IFoA") in all material respects. The relevant standards include:

- Technical Actuarial Standard 100: Principles for Technical Actuarial Work
- Technical Actuarial Standard 200: Insurance

1.7. I have also considered the relevant professional standards issued by the IFoA and believe that my work complies with these standards.

1.8. In forming my opinions on the Scheme, I have considered the views of Mr Stephen Makin, the With-Profits Actuary of Scottish Friendly, on the implications of the Scheme for the with-profits policyholders of Scottish Friendly. Mr Makin has provided his opinions in a separate report to the Board of Scottish Friendly and I have reviewed an advanced draft version of that report.

1.9. I have been provided with a copy of near-final reports from Mr Chris Lewis and Mr Hitesh Shah, the Chief Actuary and With-Profits Actuary of Canada Life respectively, and have considered those reports in forming my opinions on the impact of the

Scheme. While I have not relied on the opinions presented in those reports, I have relied on the factual accuracy of the material presented therein.

1.10. Similarly, I have been provided with a copy of the near-final report of Mr Simon Grout FIA, who has been appointed as the Independent Expert in respect of the Scheme.

1.11. In preparing my report, I have relied on the accuracy of certain information provided by Canada Life in relation to the Transferring Business. This includes the information presented in the reports by the Chief Actuary and With-Profits Actuary and also the information provided by Canada Life as part of the transaction process. Elements of this information have been subject to review and scrutiny as part of the transaction process and, where relevant, I have requested clarification on specific matters to improve my understanding of the information presented.

Overall conclusions

1.12. For the reasons set out in the remainder of this report, it is my opinion that none of Scottish Friendly's existing policyholders will be materially adversely affected by the implementation of the Scheme.

1.13. I will continue to review the expected impact of the Scheme on the existing Scottish Friendly policyholders and expect to produce a supplementary report confirming (or otherwise) my conclusions in advance of the Sanctions Hearing for the Scheme.

Format of this report

1.14. This report covers the following information:

- Section 2 provides background information on Scottish Friendly and Canada Life;
- Section 3 provides an overview of the Scheme;
- Section 4 assesses the financial impact of the Scheme on Scottish Friendly;
- Section 5 considers the effect the Scheme will have on the existing Scottish Friendly policyholders; and
- Section 6 summarises my conclusions on the impact of the Scheme.

2 Background

Status

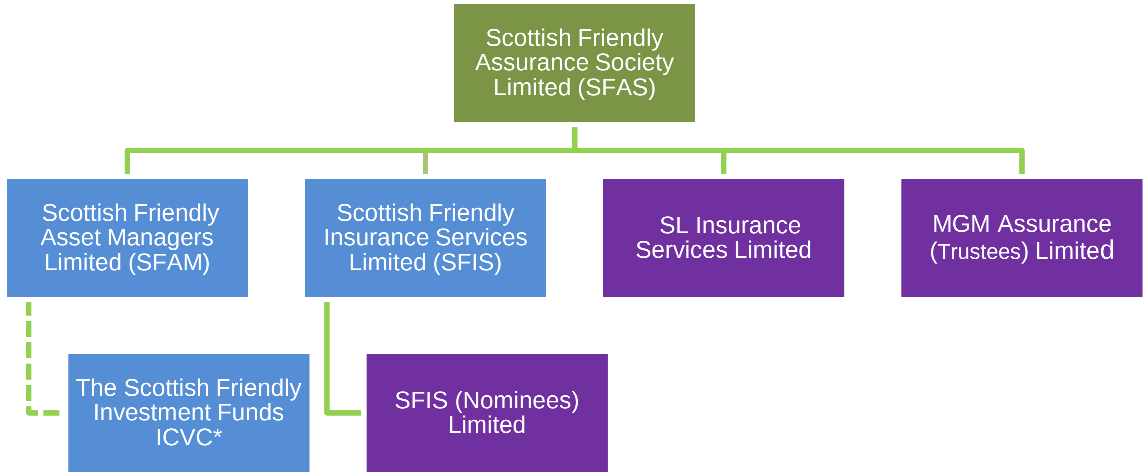
2.1. I am a Fellow of the Institute and Faculty of Actuaries and am writing this report in my capacity as Chief Actuary of Scottish Friendly. I am an employee of Scottish Friendly and have been since 30 July 2018. I was approved to act as Chief Actuary of Scottish Friendly with effect from 19 November 2018.

2.2. I confirm that I am not a policyholder in Canada Life and do not hold shares or have any other financial interest in Canada Life or any of the companies in the same group. As a member of the staff pension scheme, I am a policyholder of Scottish Friendly. I am satisfied that there are no conflicts of interest that would either prevent me from forming conclusions in relation to the Scheme or influence those conclusions.

History of Scottish Friendly

2.3. Scottish Friendly is a friendly society incorporated under the Friendly Societies Act 1992 and regulated by the PRA and the FCA. As a mutual, Scottish Friendly has no shareholders - it is run for the benefit of its members, whether they are with-profits policyholders or non-profit policyholders. Scottish Friendly has a Board of Directors, which is the ultimate governing body, and distribution of surplus and bonuses is determined by the Board upon the advice of the With-Profits Actuary.

2.4. Scottish Friendly traces its origins back to 1862 as the City of Glasgow Friendly Society, a friendly society. In the early 1990s, the City of Glasgow Friendly Society acquired Scottish Friendly and rebranded itself as the Scottish Friendly Assurance Society. The diagram below shows a summary of the expected organisational structure of Scottish Friendly immediately prior to the Scheme. The structure of Scottish Friendly will not be affected by the Scheme.



Green - denotes insurance company subject to full SIMR rules.
Blue – denotes IFPRU firm, not in scope for SIMR/SMR rules.
Purple – denotes unregulated entity not in scope for SIMR.
* The Scottish Friendly Investment Funds ICVC is an Open Ended Investment Company, managed by SFAM.

2.5. Scottish Friendly has a three-part strategy to diversify and grow the business:

- organic growth through the development of the Scottish Friendly product range and distribution channels;
- business process outsourcing for partners, leveraging the efficiency of the Scottish Friendly processes and systems; and
- seeking mergers and acquisitions ("M&A") within the life insurance sector.

2.6. The proposed transfer is in line with the M&A strategic objective and is the latest in a series of successful M&A transactions undertaken by Scottish Friendly. A summary of the recent M&A activity is set out below:

- On 31 December 2005, Rational Shelley Friendly Society ("Rational Shelley") transferred its business to Scottish Friendly.
- On 31 May 2006, Preston Operative Assurance ("Preston Operative") transferred its business to Scottish Friendly.
- On 1 July 2007, Pioneer Friendly Society ("Pioneer") transferred its business to Scottish Friendly.
- On 30 September 2007, Scottish Legal Life Assurance Society Limited ("Scottish Legal") transferred its business to Scottish Friendly.
- On 31 December 2007, London Aberdeen & Northern Mutual Assurance Society ("LANMAS") transferred its business to Scottish Friendly.
- On 30 November 2012, Royal Standard Friendly Society ("Royal Standard") transferred its business to Scottish Friendly.
- On 31 May 2015, business was transferred from Marine & General Mutual Life Assurance Society ("M&GM") to Scottish Friendly by means of a Part VII Scheme.
- On 9 November 2018, a block of business was transferred from Mobius Life Limited ("MLL") to Scottish Friendly by means of a Part VII Scheme.

2.7. Scottish Friendly Asset Managers Limited ("SFAM"), Scottish Friendly Insurance Services Limited ("SFIS"), SL Insurance Services Limited ("SLIS") and SFIS (Nominees) Limited are wholly owned subsidiaries of Scottish Friendly. SFAM provides an "OEIC" (Open Ended Investment Company) investment vehicle, Child Trust Fund, ISA and Junior ISA products. SFIS provides back office support services for financial services organisations. SLIS was a subsidiary of Scottish Legal Life which sold third-party policies direct to policyholders.

2.8. MGM Assurance (Trustees) Limited is the trustee entity for oversight of closed pension schemes which transferred from M&GM.

Scottish Friendly sub-funds

2.9. Scottish Friendly maintains one long-term business fund, the "SF Main Fund". Within this structure, separate notional sub-funds are maintained in respect of business transferred from Scottish Legal, LANMAS, Rational Shelley and M&GM, each of which has its own investment strategy, bonus rates and Principles and Practices of Financial Management ("PPFM"). These sub-funds are ring-fenced for the benefits of the relevant policyholders. For conciseness, where this report refers to business in the SF Main Fund, it is referring to the business in the long-term business fund, other than that in the separate notional sub-funds.

2.10. All Scottish Friendly policyholders are members of Scottish Friendly, whether their policies have been written in the SF Main Fund or have transferred into any of the sub-funds. This includes the holders of with-profits policies, those with non-profit policies and those written by means of partnership agreements with third party distributors.

2.11. Scottish Friendly operates a delegate system to ensure that it engages with, and is accountable to, its members. Scottish Friendly has 30 delegate positions, each representing one of five geographical electoral districts (Scotland, Northern Ireland, North of England, South of England & Wales and Republic of Ireland). In addition to any vacancies that arise from time to time, one third of delegates have to retire in rotation each year and may offer themselves for re-election. The system allows members to have their views represented at the Annual General Meeting through their representative delegate (typically the delegate closest to them geographically).

2.12. At a high-level overview of the business in each of the sub-funds is provided below:

- SF Main Fund: with-profits business, both conventional and unitised, together with significant volumes of unit-linked business, such as certain ISAs, non-profit whole of life policies and term assurance business (most of which is reinsured).

- Scottish Legal: with-profits business, both conventional and unitised, together with unit-linked life and pension business, significant volumes of non-profit whole of life policies and small volumes of term assurance business.

- LANMAS: unitised with-profits business, together with unit-linked life and pension business and a small number of term assurance policies.

- Rational Shelley: conventional with-profits business and whole of life policies.

- M&GM: with profits business, both conventional and unitised, immediate annuities and flexible income annuities and business originally sold by M&GM International ("MGMI").

2.13. Further detail on the operation of the sub-funds is provided in the following paragraphs.

SF Main Fund

2.14. The SF Main Fund contains policies written by Scottish Friendly, along with business obtained through the acquisition of Royal Standard, Preston Operative and Pioneer. On 31 May 2015, a block of unit-linked and term assurance business was transferred from M&GM into the SF Main Fund as part of the acquisition of business from M&GM. In addition, the SF Main Fund holds a block of unit-linked pension business that transferred from Mobius Life Limited on 9 November 2018.

2.15. The SF Main Fund also holds policies sold via partnership arrangements and underwritten by Scottish Friendly. These include partnerships with Beagle Street, Neilson Financial Services, Golden Charter and Guardian Financial Services. Scottish Friendly makes extensive use of reinsurance arrangements to manage the risks associated with the partnerships.

2.16. Profits will emerge in the SF Main Fund from:

- non-profit business written by Scottish Friendly or transferred into the SF Main Fund (notably from M&GM and MLL);
- any profits arising in the subsidiaries of Scottish Friendly; and
- charges for administering the business held within the LANMAS, Rational Shelley and M&GM notional sub-funds. The SF Main Fund makes a charge against each of the notional sub-funds in line with the relevant court schemes that effected the transfers of these policies and the difference between those charges and the actual costs incurred in administering the business within the notional sub-funds emerges as a profit for the SF Main Fund.

2.17. In the first instance these profits are attributed to the working capital of the SF Main Fund. However the Board agreed in 2015 that a mechanism should be established for distributing these profits to with-profits policyholders. Each year an assessment is made of the profits emerging from the sources listed above, and a share of these profits is distributed by means of enhancing the investment returns applied to asset shares. Such distributions are discretionary in nature and Scottish Friendly has the right to vary or stop the distributions in future.

Other sub-funds

2.18. The Scottish Legal, LANMAS, Rational Shelley and M&GM notional sub-funds are all closed to new business, and contain policies written by Scottish Legal, LANMAS, Rational Shelley and M&GM prior to their transfer to Scottish Friendly. The charges made against policies within these sub-funds are governed by the relevant scheme of transfer.

2.19. In the event that one of these sub-funds required support to meet its expected liabilities to policyholders, then the SF Main Fund would be expected to provide that support. These capital support arrangements will be unaffected by this transfer. I note that the existing sub-funds can also provide support to the SF Main Fund in the event that solvency is threatened.

Summary of the Business

2.20. The following tables summarise the in-force business as at 31 December 2018, including the best-estimate of the cost of the policy liabilities:

Scottish Friendly Main Fund	**Policy count**	**Gross reserves (£m)**	**Net of reinsurance reserves (£m)**
CWP	99,346	231	231
UWP	49,547	85	85
Unit-linked life	54,585	303	303
Unit-linked pensions	25,921	488	186
Whole of life	270,302	22	22
Term assurance	256,376	189	-13
Other	15,980	26	19
Total	**772,057**	**1,344**	**833**

M&GM	**Policy count**	**Gross reserves (£m)**	**Net of reinsurance reserves (£m)**
CWP	11,423	464	66
UWP	4,682	84	84
MGMI	366	13	13
Unit-linked life	-	-	-
Unit-linked pensions	-	-	-
Whole of life	1,674	3	3
Term assurance	-	-	-
Other	12,658	314	25
Total	**30,804**	**879**	**191**

Scottish Legal	Policy count	Gross reserves (£m)	Net of reinsurance reserves (£m)
CWP	106,640	48	48
UWP	296	2	2
Unit-linked life	702	5	5
Unit-linked pensions	161	1	1
Whole of life	346,128	8	8
Term assurance	464	0	0
Other	3,563	2	2
Total	**457,954**	**68**	**68**

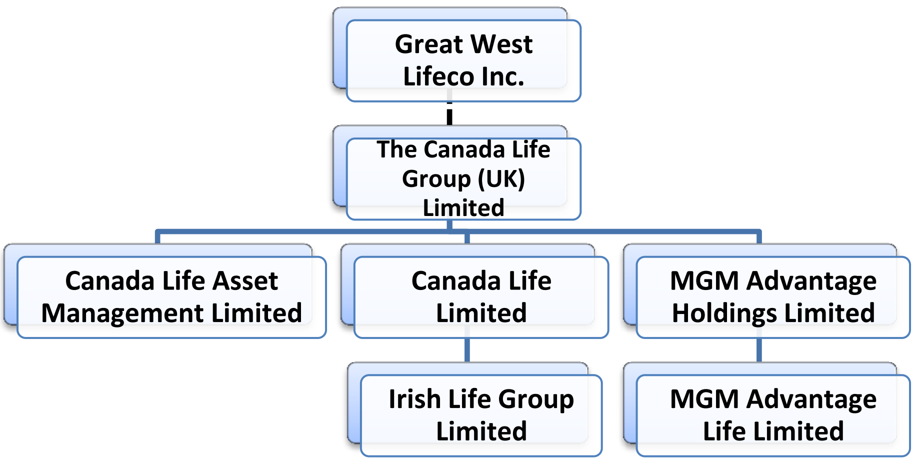
LANMAS	Policy count	Gross reserves (£m)	Net of reinsurance reserves (£m)
CWP	-	-	-
UWP	848	12	12
Unit-linked life	580	6	6
Unit-linked pensions	70	0	0
Whole of life	-	-	-
Term assurance	98	0	0
Other	7	0	0
Total	**1,604**	**18**	**18**

Rational Shelley	Policy count	Gross reserves (£m)	Net of reinsurance reserves (£m)
CWP	1,030	3	3
UWP	-	-	-
Unit-linked life	-	-	-
Unit-linked pensions	-	-	-
Whole of life	1,744	1	1
Term assurance	19	0	0
Other	567	1	1
Total	**3,360**	**5**	**5**

Canada Life

2.21. Canada Life is part of a group that was founded in Canada in 1847 and is the oldest Canadian life assurance company. In the UK, Canada Life has provided financial solutions for UK customers since 1903 including pensions, life assurance and investment products. Canada Life is a wholly owned by The Canada Life Assurance Company, a subsidiary of Great West Lifeco Inc.

2.22. The diagram below shows a simplified the structure chart of the group of companies of which Canada Life forms a part:



2.23. The Transferring Business is held in Canada Life Limited and is managed as part of the Individual Onshore business. The Individual Onshore business includes the provision of annuities, income drawdown products, unit-linked products and business held in a with-profits fund. The Transferring Business forms the ‘Legacy’ element of the Individual Onshore business and consists of a mix of unit-linked life and pensions, protection business and with-profits business. The other elements of the Individual Onshore business are remaining within Canada Life.

3 Outline of the Scheme

Overview of the Scheme

3.1. Under the Scheme, a legacy portfolio of long-term insurance business of Canada Life will transfer to Scottish Friendly at the Transfer Date, which is expected to be 00.01 on 1 November 2019.

3.2. The Transferring Business is formed of around 134,000 policies with c.£2.3bn of best estimate liabilities (on a Solvency II Pillar 1 basis) as at 31 December 2018, and is made up of:

- c.£2.1bn of non-profit business currently managed in a non-profit fund in Canada Life, comprising a wide range of unit-linked life (c.£0.4bn), unit-linked pensions (c.£1.5bn), and non-linked life, pensions and protection business (c£0.2bn); and

- c.£0.2bn with-profits and non-profit business in the Manulife ring-fenced with-profits sub-fund, mainly comprising with-profits whole-of-life business.

3.3. It is intended that the assets and liabilities of the Manulife ring-fenced fund will form a fifth ring-fenced notional sub-fund in Scottish Friendly, i.e. in addition to the M&GM, Scottish Legal Life, LANMAS and Rational Shelley ring-fenced sub-funds. All other assets and liabilities will transfer to the SF Main Fund.

3.4. Following the transfer, the Transferring Business will be administered by Scottish Friendly, with the investment management and administration carried out by Canada Life Asset Management Limited ("CLAM") and CLFIS (U.K.) Limited ("CLFIS"), as is currently the case.

3.5. Under the terms of the Scheme, Canada Life will transfer assets to Scottish Friendly equal to the value of the Solvency II technical provisions (including the risk margin) plus an amount based on the value of the standalone solvency capital ratio determined by the Standard Formula. This additional amount is expected to be £50m[1]. Following the transfer, Scottish Friendly will have responsibility for liabilities relating to the Transferring Business[2].

3.6. Following an exercise undertaken by Canada Life independent of the Scheme, by the time of the transfer, all of Canada Life's unit-linked funds are expected to invest only in shares and units of collective investment vehicles. The majority of these funds' investments will be "standard" collective investment vehicles (OEICs and unit trusts), albeit with most property exposure achieved by means of holding units in an Authorised Contractual Scheme ("ACS"). A small number of property assets are held directly by the fund.

3.7. Scottish Friendly will establish unit-linked funds which correspond one-for-one to the linked funds invested in by the transferring policies at the date of the transfer. The

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[1] Dependent on the SCR of the standalone Solvency II SCR being in the region of £40m - £60m.
[2] With the exception of liabilities relating to mis-selling or administrative errors, where Canada Life will indemnify Scottish Friendly (subject to certain time caps and monetary limits).

approach to ensuring continuity of the underlying investments of these funds is expected to operate as follows:

- To the extent that Canada Life's funds consist of "standard" collective investment vehicles (OEICs and unit trusts), the appropriate number of shares/units will be transferred directly to Scottish Friendly.

- The investment exposure for the property funds will be achieved by means of reinsurance to Canada Life, with Canada Life continuing to hold the ACS units and any directly held property assets.

- CLAM will retain the investment management mandate for the assets in the linked funds. While Scottish Friendly will have overall responsibility for administering the funds, CLFIS will continue to perform investment administration and pricing for the new linked funds established in Scottish Friendly.

3.8. Scottish Friendly will manage the assets backing the non-linked liabilities transferring to the SF Main Fund as well as the assets of the Manulife sub-fund.

3.9. It is proposed that the transfer of any business which may have been written by Canada Life in Guernsey or Jersey or to policyholders resident in Guernsey will be effected by means of separate schemes in Guernsey and Jersey. These schemes will provide for the transfer of policies on the same terms as the Scheme and are expected to have the same transfer date as the Scheme.

3.10. The Scheme provides for policies which are unable to be transferred on the effective date of the Scheme due to some legal impediment ("Residual Policies") to be reinsured to Scottish Friendly, until such time as it is possible to complete the transfer (or Canada Life and Scottish Friendly agree to terminate the reinsurance). As the economic and financial effect of this arrangement is equivalent to a transfer, I have assumed, for the purposes of this report and the impacts shown, that there are no Residual Policies.

Rationale for the Scheme

3.11. Scottish Friendly operates a three-part growth strategy, a core component of which is mergers and acquisitions. Under this strategy, Scottish Friendly seeks to acquire books of business from other insurers, with the intention of enhancing member value by achieving efficiencies in the management of the business. The transfer of the block of business from Canada Life is consistent with this growth strategy and represents a significant acquisition for Scottish Friendly.

3.12. In addition to supporting the growth of Scottish Friendly, the transfer will provide the opportunity for expansion into different target markets, and will provide the opportunity for future cost savings through operational efficiencies. The transfer is expected to generate a profit for the SF Main Fund which, in due course, I would expect to form part of the surplus distributed from that fund.

3.13. In contrast, Canada Life is disposing of the block of legacy business to focus on its core growth areas. The Transferring Business is no longer core to its expected strategic priorities and the costs of maintaining the IT systems were increasing.

Assets and Liabilities being transferred

3.14. The table below provides a summary of the Solvency II Best Estimate Liabilities ("BEL") of the Transferring Business as at 31 December 2018:

	No. Policies	Unit Value (£m)	Non-linked BEL (£m)	Gross BEL (£m)	Re - insurance (£m)	Net BEL (£m)
Unit-Linked Life	24,064	412.1	29.3	441.4	2.5	438.9
Unit-Linked Pensions	77,932	1,449.4	83.1	1,532.4	-	1,532.4
Non-Linked Life	10,730	-	116.1	116.1	5.1	111.0
Non-Linked Pension	322	-	18.8	18.8	-	18.8
Non-Linked Protection	8,320	-	23.4	23.4	4.2	19.2
Manulife WP Fund	12,322	-	158.6	158.6	-	158.6
Total	**133,690**	**1,861.5**	**429.3**	**2,290.8**	**11.8**	**2,279.0**

3.15. The figures presented in the table are based on figures provided by Canada Life for year ending 31 December 2018, before any adjustment to allow for Scottish Friendly's assessment of the level of expenses that will be incurred in administering the business. These expenses are expected to be lower than those allowed for in the figures produced by Canada Life and this difference is reflected in the financial impact of the Scheme, shown in Section 4. The figures above exclude £2.4m of reserves related to the Transferring Business that were held by Canada Life at 31 December 2018, but which Canada Life has confirmed are not expected to be held at the transfer date.

3.16. The following sections provide an overview of the product types transferring. All figures are as at 31 December 2018, unless otherwise stated.

Unit-linked pension policies

3.17. The unit-linked pension liabilities account for the largest proportion of the proposed transfer. The liabilities comprise of mainly individual linked pension products but also include c.3,000 workplace pension policies.

Unit-linked life policies

3.18. The unit-linked life policies comprise of Whole of Life, Endowment and Investment Bonds.

Non-linked life policies

3.19. The non-linked life policies predominantly comprise of whole of life and term assurance products. They also include c.2,000 ex-with-profits policies held in the With-Profits Fund of Canada Life Limited that converted to non-profit with effect from 1 August 2017, comprising endowment and whole of life.

Non-linked pension

3.20. The non-linked pension policies are principally defined benefit annuities. They also include some policies which were converted to non-profit, including pensions and deferred annuities.

Non-linked protection

3.21. The non-linked protection policies include Income Protection and Critical Illness products.

Manulife with-profits policies

3.22. The Manulife Fund is a ring-fenced fund that primarily comprises Whole of Life policies and c.2,200 non-profit policies.

Assets

3.23. The assets transferring comprise the assets held in the Manulife fund (£0.2bn)[3], the assets backing the total unit-linked liability (£1.9bn) plus assets equal to the value of non-unit technical provisions (£0.3bn) plus £50m. The value of the technical provisions excludes any reduction to this amount in respect of the Transitional Measure on Technical Provisions available under Solvency II. The nature of the assets (other than the unit-linked assets) that can be transferred in respect of this amount has been agreed between Scottish Friendly and Canada Life.

3.24. The assets of the Manulife Fund will be transferred to a newly-formed fifth ring-fenced sub-fund within Scottish Friendly. All of the other assets will transfer to the SF Main Fund.

3.25. Where relevant, the assets transferring will include the reinsurance assets relating to the existing reinsurance agreements on the Transferring Business and the reinsurance on the property unit-linked funds.

3.26. Under the terms of the property unit-linked reinsurance agreement and related security agreements, Scottish Friendly will gain security rights over the ACS units held in respect of the liabilities reinsured. To the extent that there are likely to be any direct

[3] Other than a small amount of cash retained by Canada Life to meet the costs of claims already made, but not yet processed, as agreed between Canada Life and Scottish Friendly.

property holdings within the property funds (in addition to the ACS units) at the Scheme Effective Date, Scottish Friendly and Canada Life expect to enter into a similar agreement to provide security over those assets.

Capital support

3.27. The nature of the capital support arrangements between the SF Main Fund and the existing sub-funds will be unaffected by this transfer.

3.28. Following the transfer, capital support will be extended to the Manulife sub-fund. This sub-fund has the capacity to absorb significant losses in excess of the estimated Solvency Capital Requirement (as explained in Section 4 of this report) for this business, with a future discretionary benefit reserve as at 31 December 2018 of £39m and an estimated SCR of £14m (before any allowance for the ability of the fund to cut bonuses in the event of a stress). Given this significant buffer of assets over the guaranteed liabilities, it would take a very adverse scenario to require support to be provided to the Manulife sub-fund from the SF Main Fund. Under the terms of the Scheme, the Manulife sub-fund will not be able to provide support to the SF Main Fund. It is possible, although not certain, that in the extremely unlikely event of the insolvency of Scottish Friendly the assets in the Manulife sub-fund would be available to help meet the cost of benefits payable on policies outside the Manulife sub-fund.

Costs related to the Scheme

3.29. Scottish Friendly and Canada Life will each meet their own transaction costs, such as legal and consultancy fees and costs incurred in carrying out the migration. Shared costs, such as the Independent Expert and Legal Counsel, will be shared equally between Scottish Friendly and Canada Life.

Membership rights

3.30. The transfer will result in around 134,000 policies transferring to Scottish Friendly which comprises of around 100,000 unique policyholders. While still relatively small compared to Scottish Friendly's current policy base of well over one million policies, there will be some dilution of the rights of existing members as a result of the transfer.

3.31. As a result of the transfer, the number of delegates is expected to remain the same. As members, Transferring Policyholders will obtain voting rights, including in relation to the ability to nominate and vote for delegates.

Governance Advisory Arrangement ("GAA")

3.32. At the Effective Date, the pension policies transferred as part of the Scheme will be overseen by Scottish Friendly's GAA.

3.33. The primary role of the GAA is to ensure compliance with the FCA rules for independence governance committees (as amended from time to time), and to act in accordance with all applicable legislation, regulations rules and guidance, whether made by the FCA or otherwise.

3.34. The GAA was set up following the transfer of the ex-Mobius Life pension policies on 9 November 2018. The GAA has oversight of all of Scottish Friendly's pension business which encompasses both ex-Mobius Life policies and existing Scottish Friendly pension business. The remit of the GAA will extend to include an oversight role in respect of the group pension business of the transferring business from Canada Life.

4 Financial position before and after the transfer

Background

4.1. UK insurance companies are required, by law, to maintain a minimum level of capital resources to reduce the risk that they are unable to meet their future obligations to policyholders. These capital resources and the capital requirement are determined under the "Solvency II" regime, the current regulatory requirement for European Union and EEA life insurers.

4.2. The Solvency II regime specifies an approach to assessing the capital position, which I refer to as the "Pillar 1" basis and is the basis of the results shown in this report. Insurers are also required to perform their own assessment of their solvency requirements, to support effective management of risks with the insurer. I refer to this as the "Pillar 2" basis.

Pillar 1

4.3. The Pillar 1 results are prepared in line with the specified requirements of Solvency II. Insurers are required to disclose their results to the regulator on a quarterly basis and to publish them annually on their website.

4.4. Solvency II requires an assessment of an insurer's "Own funds": the capital resources, calculated in line with the principles of market consistency, available to meet losses that could arise in the future. For Scottish Friendly, the Own Funds are equal to the excess of the value of assets held over the Technical Provisions and any non-insurance liabilities. The Technical Provisions are the sum of the Best Estimate Liabilities (a best-estimate of the cost of providing the benefits to policyholders) and a Risk Margin (an additional prudence margin, intended to reflect the amount that would be required to transfer the liabilities to a third party insurer).

4.5. The capital requirement under Solvency II (the Solvency Capital Requirement ("SCR")) is assessed by considering the loss that might be incurred in a very severe scenario, expected to occur only once in every 200 years.

4.6. The SCR must be determined using either an Internal Model, which is subject to approval by the PRA, or the Standard Formula prescribed in the relevant regulations. Scottish Friendly uses the Standard Formula to assess the amount of capital it holds, and expects to continue to use this approach in the future.

4.7. Scottish Friendly does not utilise any of the measures included in the regulations which would serve to reduce the liabilities under Solvency II, such as the Matching Adjustment, Volatility Adjustment or the Transitional Measures on Technical Provisions.

Pillar 2 (ORSA)

4.8. Solvency II also requires insurers to undertake their own assessment of the amount of capital they need to hold, based on the risks to which the firm is exposed, to ensure they remain able to meet its liabilities to policyholders. This assessment is referred to as the Own Risk & Solvency Assessment ("ORSA"), also referred to as Pillar 2, and is submitted to the regulators privately (unlike Pillar 1 which is disclosed as part of the public disclosures).

4.9. Scottish Friendly's ORSA basis is similar in nature to the Pillar 1 calculation, but includes an allowance for certain risks that are not included in the Pillar 1 Standard Formula and allows for the measurement of certain risks in a way that is more in line with Scottish Friendly's assessment of those risks.

Risk Appetite Framework

4.10. Scottish Friendly has a Risk Appetite Framework that is used to support the management of risk in the business (both prudential or financial risks and conduct or operational risks). The Risk Appetite Framework prescribes triggers and thresholds based on Scottish Friendly's appetite for each risk.

4.11. An important part of the Risk Appetite Framework is the consideration of the solvency position of Scottish Friendly, as measured using the Pillar 2 basis. Under this requirement, a minimum capital threshold is determined as the solvency level that is sufficient to retain at least 100% capital coverage on a Pillar 2 position following an adverse scenario of a severity that is expected to occur over the next year with a probability of no more than one-in-ten. The framework also specifies a trigger point based on a 30% buffer above that minimum. The minimum has been calibrated as a solvency level (defined as the ratio of the own funds to the SCR) of 150%, resulting in a trigger of 180%.

4.12. Falling below the 180% trigger indicates that the solvency level is lower than would be expected in the normal course of events and Scottish Friendly will consider whether actions may be required to increase the solvency level.

4.13. If the solvency level falls below 150%, then Scottish Friendly would expect to take actions to improve this solvency position. Such actions could include de-risking the asset holdings, reducing the volume of new business sold or reducing the levels of bonus payable.

4.14. Similar trigger and minimum levels have been specified for the Pillar 1 position, again based on a "one-in-ten" minimum, with a calibration of a minimum of 130% and a trigger of 150%. The lower target reflects that the Pillar 1 ratio is relatively less volatile than the Pillar 2 position, as a result of the ring-fencing requirements for the sub-funds.

4.15. Triggers and minimum tolerance levels have also been set for each of the sub-funds, in order to support their ongoing management and to avoid actions being taken in those sub-funds that unreasonably increase the likelihood of support being required. The entity level financial position is the primary determinant of security for policyholders and is the focus of my analysis in this report.

Expected impact of the Scheme: Pillar 1

4.16. The table below shows the reported financial position of Scottish Friendly and its solvency ratio as at 31 December 2018, with an indication of the pre and post transfer position of Scottish Friendly, as if the transfer had taken place at that date.

4.17. The estimated post-transfer position shown below is based on the expected value of the assets, liabilities and capital requirements of the Transferring Business as at 31 December 2018. The estimated position is reliant on the accuracy of the data provided by Canada Life, both as part of the initial transaction process and subsequent to that. Work was undertaken as part of the diligence process to verify the reasonableness of the results and further modelling work has been undertaken to assess the accuracy of the liability results. I will continue to monitor the expected impact of the Scheme on the financial position of Scottish Friendly and expect to present any revisions to these estimates in my supplementary report on the Scheme, prior to the Scheme being approved (or otherwise).

Pillar 1 position As at 31 December 2018	Pre transfer	Post transfer (£m)
Assets (£m)	2,633.2[4]	5,005.2
Liabilities (£m)	2,447.1	4,761.2
Excess of assets over liabilities (£m)	186.1	243.9
Impact of ring-fencing	(75.3)	(75.3)
Own funds (£m)	110.8	168.6
SCR (£m)	58.8	98.2
Solvency ratio	188%	172%

4.18. Based on the position as at 31 December 2018 the impact of the transfer is to reduce the capital cover from 188% to 172%.

4.19. The results show that Scottish Friendly is expected to be able to meet its Pillar 1 capital requirements immediately after the Scheme.

4.20. The main drivers of the movements are:

- Assets: increase of £2.37bn, representing the transferring assets, including the £50m margin over the liabilities. The movement in assets also reflects the expected costs of the Scheme;

[4] The pension scheme surplus is shown as a negative liability in this table. It is shown as an asset in the annual report and accounts.

- Liabilities: increase of £2.31bn, representing the transferring liabilities, assessed using the expected expense base that will apply in Scottish Friendly;

- SCR: increase of £39.4m, reflecting the capital requirements for the Transferring Business, net of additional diversification with the existing risks in Scottish Friendly.

4.21. The following table shows the expected pre- and post-transfer positions for the SF Main Fund in isolation.

Pillar 1 position: SF Main Fund As at 31 December 2018	Pre transfer	Post transfer (£m)
Assets (£m)	1,493.4	3,697.8
Liabilities (£m)	1,414.3	3,560.9
Own Funds (£m)	79.1	136.9
SCR (£m)	28.4	67.9
Solvency ratio	278%	202%

4.22. The figures show that, although the solvency ratio of the SF Main Fund reduces as a result of the transfer, the SF Main Fund continues to have a significant excess over its Pillar 1 SCR. Indeed, both the level of Own Funds and the excess of Own Funds over the SCR are expected to increase in absolute terms.

Expected impact of the Scheme: Pillar 2

4.23. The results on a Pillar 2 basis are not publicly available. The absolute solvency ratio on a Pillar 2 basis is higher than the equivalent Pillar 1 result pre-Scheme and that is expected to remain the case post-Scheme. The impact of the Scheme on the financial position is consistent with that shown for Pillar 1, with the solvency position reducing as a result of the transfer, and the drivers of the results are the same.

4.24. Based on the position as at 31 December 2018, the solvency ratio on a Pillar 2 basis is expected to be significantly above both the entity trigger level and the minimum level specified in the Risk Appetite Framework.

Risk profile of the business

4.25. The proposed Scheme contains a significant proportion of unit-linked business, c.£2.0bn out of a total £2.1bn of liabilities which will transfer to the SF Main Fund under the Scheme. The SF Main Fund already contains unit-linked business which accounts for around half of the Main Fund liabilities. After the transfer, it is expected that the unit-linked business will account for around 80% of the liabilities within the SF Main Fund.

4.26. The proposed Scheme also contains significant volumes of pensions and protection business which will transfer to the SF Main Fund. While the SF Main Fund is already exposed to some of the risks relating to these types of business, the mix of risks will change as a result of the Scheme.

4.27. The following table shows the estimated proportion of market, counterparty, life, health and operational risks at 31 December 2018 for Scottish Friendly only, the proposed transferring business, and both combined. These are measured by Pillar 1 SCR, expressed as a percentage of the undiversified capital requirements.

Risk Category	Scottish Friendly only	Transferring Business	Scottish Friendly incl. Proposed Scheme
Market	41%	31%	37%
Counterparty	10%	0%	7%
Life	42%	56%	46%
Health	0%	8%	3%
Operational	7%	5%	7%

4.28. The following table shows the proportions of risk for SF Main Fund only, the proposed transferring business, and both combined at 31 December 2018. These are also measured by Pillar 1 SCR, expressed as a percentage of the undiversified capital requirements.

Risk Category	SF Main Fund only	Transferring Business	SF Main Fund incl. Proposed Scheme
Market	22%	31%	26%
Counterparty	9%	0%	5%
Life	61%	56%	58%
Health	0%	8%	5%
Operational	8%	5%	7%

4.29. Market and life insurance risk are expected to remain the dominant risks within Scottish Friendly following the transfer. The main contributor to the market risk from the proposed transfer is equity risk from the unit-linked business and credit spread risk on the unit-linked pensions. The main contributor to life insurance risk is in respect of policyholder lapse behaviour differing from expectations.

4.30. The largest proportionate change relates to health risk arising from c.8,100 income protection policies on guaranteed premiums. Scottish Friendly is not currently exposed to material levels of risk associated with income protection products. This exposure will require careful claims management post transfer to ensure that all claims are valid and customers are supported appropriately. Ensuring the processes are in place to manage this exposure is a key focus of the preparation work being undertaken by Scottish Friendly. I am content with the plans that have been outlined to me, and I will comment on progress made in my supplementary report.

4.31. Life risk is expected to increase proportionately, primarily due to the exposure to the risk of different to expected lapse rates on the Transferring Business. This results in life risk being the Scottish Friendly's Main Fund dominant risk type.

4.32. Operational risk increases, in line with the prescribed formula in the Standard Formula calculation. I have considered the change in operational risk in more detail in paragraphs 5.13 to 5.16.

4.33. There is not expected to be any material impact on the counterparty risk exposure of Scottish Friendly, as the collateral arrangements in place for the property unit-linked funds provide protection to Scottish Friendly in the event that Canada Life defaults.

Risk of capital support required for Manulife Fund

4.34. The capital support arrangements in place between the SF Main Fund and the other four sub-funds will be extended to the newly formed Manulife sub-fund post Scheme Effective Date.

4.35. This sub-fund has significant headroom to reduce final bonuses on the policies in the fund, without reducing payouts below the guaranteed level. This "terminal bonus cushion" was c.£39m at 31 December 2018 and is expected to be able to comfortably absorb a loss equal in size to the estimated SCR (c.£14m at 31 December 2018, before allowance the impact of reducing bonuses). As a result, it is unlikely that any support will be required by the new sub-fund and I am satisfied that extending capital support to the Manulife sub-fund would not materially adversely affect the financial position of Scottish Friendly.

Use of Standard Formula

4.36. Scottish Friendly uses the Standard Formula to assess the amount of capital it is required to hold on a Pillar 1 basis. Canada Life also currently use the Standard Formula for assessing the block of business to be transferred as part of the Scheme.

4.37. It is expected that Scottish Friendly will continue to use the Standard Formula post Scheme Effective Date and will continue to formally assess the ongoing appropriateness of doing so, as required under the Solvency II regulations.

5 Effect on policyholders

5.1. In this section I consider the impact of the Scheme on the existing policyholders of Scottish Friendly. My report does not consider the impact on policyholders transferring under the Scheme or policyholders remaining with Canada Life. These impacts are considered by the Chief Actuary and With-Profits Actuary of Canada Life.

Security of benefits

5.2. In assessing the security of benefits for the Scottish Friendly policyholders, I have primarily focussed on the impact of the Scheme on the ability of Scottish Friendly to meet its regulatory capital requirements and the requirements of its Risk Appetite Framework.

5.3. The transfer is expected to result in a reduction in Scottish Friendly's solvency coverage ratio, on both a Pillar 1 and Pillar 2 basis. Despite this reduction, and based on the 31 December 2018 position, Scottish Friendly expects to hold a significant level of excess capital over the regulatory capital requirement on a Pillar 1 basis (and the trigger on a Pillar 1 basis under the proposed update to the Risk Appetite Framework). It also expects to hold an excess over the minimum and trigger levels under the Risk Appetite Framework on a Pillar 2 basis.

5.4. The most recent ORSA report included projections of the capital position, including an allowance for the expected impact of the business transferring. These projections showed a broadly consistent impact of the transfer to the impact as at 31 December 2018 (as shown above), albeit with the pre- and post-Scheme position showing a higher capital coverage ratio to reflect the position when the projections were undertaken and the increase in solvency position that is expected over time as the business runs off. These projections also show the solvency position improving following the transfer, as the business runs off and the associated capital requirements are released.

5.5. Given the result as at 31 December 2018 and expected improvement in solvency over time, I am satisfied that the reduction does not materially adversely affect the security of the benefits.

5.6. While consideration of the impact on solvency ratios provides an indication of relative security before and after the Scheme, I believe it is also important to note the following:

- The existing policyholders will continue to be held in an insurer that is subject to the Solvency II regime, which provides a strong underlying level of protection for policyholders. Indeed, a solvency level of 100% under Solvency II (significantly lower than is expected to be the case) is still expected to be sufficient to meet policyholder liabilities in all but the most extreme scenarios. Further to this, failing to meet the regulatory capital requirements does not, in itself, mean that Scottish Friendly would be unable to meet its obligations to policyholders, but would require Scottish Friendly to take steps to restore its solvency position.

- In the very unlikely event that Scottish Friendly did become insolvent, then policyholders may be eligible to claim from the Financial Services Compensation Scheme, which covers up to 100% of claims. The Scheme does not affect the eligibility of existing policyholders to claim under this Scheme.

5.7. The Transferring Business is expected to generate profits for the SF Main Fund as the risk margin and SCR are released as the business runs off. Over time this release of capital into the fund will increase the security of existing policyholders' benefits and/or enhance benefit expectations of with-profits policyholders in the SF Main Fund.

5.8. Consequently, I do not believe there is a material adverse impact on the security of benefits for existing Scottish Friendly policyholders as a result of the transfer.

Capital support arrangements

5.9. Scottish Friendly operates a capital support arrangement such that any of the sub-funds can, either on a temporary or permanent basis, be provided with capital from the SF Main Fund. In extreme circumstances, where there is a threat to solvency, it is possible for the sub-funds to also provide capital to the SF Main Fund.

5.10. As a result of the transfer of the Transferring Business, it is expected that an additional ring-fenced sub-fund will be created for the c.£0.2bn ex-Manulife with-profits ring-fenced fund. The £2.1bn of other, mainly unit-linked, business will transfer directly to the SF Main Fund.

5.11. The existing capital support arrangements are not expected to be affected by the transfer of the Transferring Business and will continue to operate in their current form. The solvency coverage ratio of the SF Main Fund will reduce but is expected to remain comfortably in excess of the SCR for the fund (and the minimum risk appetite for that fund). Further, the absolute level of both the Own Funds and the excess over the SCR for the fund are expected to increase. Taking this into consideration, I do not consider that the reduced solvency position will materially adversely affect the benefit security or benefit expectations of existing Scottish Friendly policyholders across the sub-funds or the ability of the SF Main Fund to provide support to the sub-funds if required.

5.12. The capital support arrangements will need to be extended to the Manulife sub-fund. As a result, there is a theoretical chance that, should the SF Main Fund or an existing sub-fund require capital to support its solvency, such capital will be unavailable as it is supporting the Manulife sub-fund. However, as this sub-fund has a significant terminal bonus cushion the likelihood of providing support is very low, and I do not expect that extending capital support to the Manulife sub-fund would materially adversely affect either benefit security or benefit expectations of policyholder in the SF Main Fund or, indirectly, the existing sub-funds.

Operational risk

5.13. As part of the transfer, the majority of policies are to be migrated onto the Scottish Friendly administration system. The number of policies administered is expected to increase by around 10% from c.1.3m to c.1.4m. The transfer also introduces new product types and variants and new contractual arrangements (e.g. with suppliers and reinsurers). Under the terms of the commercial transfer agreement, but separate to the Scheme, a small number of Hong Kong-based policies will be administered by SFIS but are not transferring to Scottish Friendly.

5.14. To manage and mitigate the operational risks relating to the transfer itself, a robust and detailed migration, test and implementation plan has been developed. This plan is subject to oversight from the risk function, with regular updates provided to the executive and Risk Committee of the Board.

5.15. Furthermore, the transfer agreement includes provisions to enter into a transitional services agreement (under which Canada Life would continue to provide administration for a period). This limits the risk of the transfer causing any operational disruption to the existing policyholders of Scottish Friendly.

5.16. Given this, I am satisfied that the change in the level of operational risk as a result of the transfer should have no material adverse effect on the existing policyholders.

Investment policy

5.17. Scottish Friendly's current practice is to consider investment policy separately for the SF Main Fund and each of the sub-funds. The investment policy of each fund is set out in the relevant PPFM.

5.18. The transfer of the Transferring Business to the SF Main Fund is not expected to alter the investment profile of the fund: unit-linked liabilities will be matched with unit-linked assets and non-unit liabilities, which are relatively small in the context of the fund, will be matched with fixed interest securities.

5.19. Scottish Friendly's investment managers, the asset selection processes, and the investment strategy will not change as a consequence of the transfer.

5.20. Canada Life currently operates a Principles and Practices of Financial Management (Unit-Linked Funds). It is anticipated that a corresponding document will be produced for Scottish Friendly, formalising the current approach to managing unit-linked business. I view this as a positive change for the existing Scottish Friendly policyholders with unit-linked policies.

Benefit expectations – with-profits business

5.21. The terms and conditions for existing Scottish Friendly with-profit policies are unaffected by the transfer.

5.22. There will be no material changes to investment strategy, expense allocation, policy charges, or the methodology for setting or allocating bonuses for existing Scottish Friendly with-profits policyholders as a result of the transfer.

5.23. Although the transfer results in the SF Main Fund being exposed to an increased absolute level of risk, assets to cover the capital requirements associated with these risks are also being transferred and it is expected that existing with-profits policyholders may ultimately benefit from profits for the SF Main Fund generated by the Transferring Business (other than those profits retained in the Manulife sub-fund) and the release if the risk margin and SCR over time.

5.24. Therefore, I do not expect that the benefit expectations of with-profits policyholders will be materially adversely affected by the transfer. Indeed, I would expect benefit expectations to be improved to the extent that the anticipated expense synergies can be achieved.

5.25. The With-Profits Actuary has prepared a report for the Board of Scottish Friendly on the impact of the Scheme on the with-profits policyholders of Scottish Friendly. The report considers the existing with-profits policyholders, their benefits and expectation of future benefits, the impact of membership rights and practical considerations in relation to managing the with-profits policies.

5.26. The key conclusions of the report are:

- the Scheme does not have a materially adverse effect on the security of benefits, benefit expectations, or the fair treatment of Scottish Friendly's existing with-profits policyholders,
- the Scheme does not result in a significant dilution of membership rights, and that
- there is no reason, in those terms, why the transfer should not proceed.

Benefit expectations – non-profit business

5.27. The terms and conditions for existing Scottish Friendly non-profit policies (including charges, premiums and promised benefits) will be unaffected by the transfer.

5.28. In addition, the range of unit-linked funds available to existing policyholders will not change and there will be no changes to unit pricing or investment administration processes as a result of the transfer. A legal agreement is being entered into between SF and CLFIS for CLFIS to provide investment administration for the unit-linked business.

5.29. The Scheme will not change the level of charges on unit-linked funds held by existing policyholders. To the extent that there is discretion in the level of charges and these are reviewed in future, I would expect the Scheme to, all else being equal, act to reduce the level of charges, as there will be more business in Scottish Friendly over which to spread fixed costs.

5.30. Therefore, I am satisfied that the benefit expectations of non-profit policyholders will not be materially adversely affected by the Scheme.

With-Profits Governance

5.31. As part of its ongoing role as a conduct regulator for insurers, between 2017 and 2019 the FCA has been undertaking a thematic review of how with-profits business is managed within the UK. This included information gathering and on-site interviews at a number of firms.

5.32. In light of that exercise, Scottish Friendly is undertaking a number of actions relating to how it manages its with-profits business, including a review of the with-profits governance arrangement.

5.33. The governance review work completed in early 2019 and, as a result, Scottish Friendly has established a With-Profits Committee, which will play a key role in the management of with-profits business by Scottish Friendly. I view such a change to represent a strengthening of the governance in this area. Neither this nor any of the other work being undertaken is expected to have a material bearing on the financial position of Scottish Friendly.

5.34. Overall, based on the progress to date and the nature of the actions being undertaken, I see no reason why this work will have any adverse effect on the existing policyholders. Any such impact would have occurred regardless of the Scheme and, as a result, I am satisfied that it has no bearing on my conclusions in relation to the Scheme.

Membership rights

5.35. The transfer will result in around 134,000 policies transferring to Scottish Friendly. While still relatively small compared to Scottish Friendly's current policy base of well over one million policies, there will be some dilution of the rights of existing members as a result of the transfer.

5.36. The dilution of membership rights is not significant and therefore not expected to adversely impact existing members' rights. The transfer is consistent with Scottish Friendly's business strategy and is expected to provide a new source of profits which will benefit the existing with-profit policyholders and membership more generally.

Taxation

Existing policyholders

5.37. There is not expected to be any impact on the tax position of existing Scottish Friendly policyholders as a result of the transfer of the Transferring Business.

Tax clearances

5.38. The appropriate tax clearances will be sought from HMRC in respect of the transfer. These are expected to be in place prior to the Scheme taking effect.

Quality of Administration

5.39. There will be no change to the administration of existing Scottish Friendly policies as a result of the transfer.

5.40. The administration of the Transferring Business is currently undertaken by Canada Life. As part of the transfer, the Transferring Business will be migrated onto Scottish Friendly's administration platform. For a small number of policies, c. 1,000, Canada Life operates a spreadsheet or database system to administer and maintain these policies. It's expected that these systems will transfer to Scottish Friendly on the Scheme Effective Date.

5.41. There are risks associated with the data and IT developments needed to migrate the transferring policies to Scottish Friendly systems. However, as changes will be made as part of controlled change programme, this should not be expected to pose a threat to the administration of existing Scottish Friendly policies. Plans have been developed to support the successful migration and to ensure there is sufficient resource in place to support the ongoing administration of the enlarged business post-transfer.

Brexit

5.42. On 23 June 2016, the UK voted to leave the European Union ("Brexit") in a referendum. On 29 March 2017, the UK government triggered Article 50 formally giving notice of the UK's intention to withdraw from the EU. Following extensions to the original date of 29 March 2019, the formal withdrawal is scheduled to occur on or before 31 October 2019.

5.43. Scottish Friendly has a small portfolio of EEA policies (c.21,000 policies), of which >90% reside in the Republic of Ireland. Scottish Friendly do not currently sell into the EU and do not plan to do so in the future.

5.44. Further, as part of the transferring business, c.1,100 EEA policies will transfer. Canada Life has confirmed that these policyholders were UK resident at the point that they purchased their policy, but have subsequently moved abroad.

5.45. The UK government has been negotiating the terms on which the UK will withdraw from the EU. Although there is not yet a clear view on whether the deal negotiated will be accepted by the UK parliament, Scottish Friendly expect to be able to continue to fulfil existing contracts for policyholders residing in any EU country. Scottish Friendly is monitoring the situation as new developments arise and will take further steps once the withdrawal arrangements are more clear.

5.46. I note that, it is possible that, in the event that the UK leaves the EU with no deal in place, there is a risk that there are operational or legal barriers to servicing the policyholders resident in the EU. This would have been the case with or without the Scheme. As a result, I am satisfied that this risk does not impact my considerations on the impact of the Scheme on the existing policyholders.

Notification to Scottish Friendly policyholders

5.47. The regulations governing Part VII transfers require that, unless the Court orders otherwise, all policyholders in all affected companies should be written to in order to inform them of the proposed transfer.

5.48. Scottish Friendly operates a delegate system, whereby 30 members are selected to represent the interests of the policyholder book. The 30 delegates have the right to vote on certain matters on behalf of all other members, a transfer of insurance business by Part VII transfer is one of them.

5.49. Given that I do not expect the transfer to have a material adverse effect on existing policyholders, and as the With-Profits Actuary does not consider there to be a material dilution of existing membership rights, I would support an application being made for a waiver from mailing all Scottish Friendly policyholders provided also that the delegates are written to in a timely manner outlining the nature and expected effect of the transfer.

Treating customers fairly

5.50. In my opinion, the contents of the Scheme are consistent with the requirements to treat customers fairly with respect to the policyholders of Scottish Friendly. Although there is expected to be a deterioration in the capital solvency position of Scottish Friendly following the Scheme, the expected post-Scheme position is above the risk appetite limit. The proposed transfer is consistent with the strategy of Scottish Friendly and is expected to provide other positives to the policyholders in the long term such as a new profit stream.

6 Conclusions

6.1. In my opinion, as Chief Actuary of Scottish Friendly, and taking into account the analysis and opinions set out above, none of Scottish Friendly's existing policyholders will be materially adversely affected by the implementation of the Scheme. In particular, I believe that the Scheme should not have any material adverse impact on the security of benefits or benefit expectations of the Scottish Friendly policyholders.

6.2. This report and the conclusions within it apply equally to business carried on in, or from within, Jersey or Guernsey and to policies issued to residents of the Bailiwick of Guernsey as they do to business comprising policies held by residents in the UK or any other territory.

Alan Rankine FFA

Chief Actuary – Scottish Friendly Assurance Society Limited

7 June 2019

Appendix 1: Glossary of Terms

ACS	Authorised Contractual Scheme
CLAM	Canada Life Asset Management Limited
CLFIS	CLFIS (U.K.) Limited
CLL	Canada Life Limited
IE	Independent Expert
FCA	Financial Conduct Authority
FRC	Financial Reporting Council
FSMA	Financial Services and Markets Act 2000
GAA	Governance Advisory Arrangement
IFoA	Institute and Faculty of Actuaries
LANMAS	London, Aberdeen and Northern Mutual Assurance Society
M&A	Mergers and Acquisitions
M&GM	Marine & General Mutual Life assurance Society
MLL	Mobius Life Limited
OEIC	Open-Ended Investment Company
ORSA or Pillar 2	Own Risk & Solvency Assessment
Own Funds	The capital resources, calculated in line with the principles of market consistency, available to meet losses that could arise in the future.
Pillar 1	The approach to assessing the capital position prescribed under the Solvency II regulations
Pioneer	Pioneer Friendly Society
PPFM	Principles and Practices of Financial Management
Preston Operative	Preston Operative Assurance

PRA	Prudential Regulation Authority
Rational Shelly	Rational Shelly Friendly Society
Royal Standard	Royal Standard Friendly Society
SFAS or SF	Scottish Friendly Assurance Society Limited
SFAM	Scottish Friendly Asset Managers Limited
SFIS	Scottish Friendly Insurance Services Limited
SLIS	Scottish Legal Insurance Services Limited
Solvency II	The current regulatory requirement for European Union and EEA life insurers
SCR	Solvency Capital Requirement
WPA	With-Profits Actuary

Appendix 2: Information Relied Upon

The following key documents and data were used in the preparation of the Report. Reliance was also placed on the accuracy of the information disclosed by Canada Life as part of the transaction process.

Item	Received from	Date
Draft Scheme	CLL	24/05/19
Business Transfer Agreement and related agreements	N/A	19/06/19
Report of the Scottish Friendly With-Profits Actuary	Hymans Robertson	07/06/19
Report of the CLL Chief Actuary	CLL	07/06/19
Draft report of the CLL WPA Report	CLL	07/06/19
Manulife Principles and Practices of Financial Management	CLL	March 2018
Responses to queries on figures in CLL reports	CLL	Various
CLL product cashflows	CLL	30/06/17 and 31/12/17
CLL reserves and SCR, split by risk	CLL	30/06/17, 31/12/17 and 31/12/18