

Explanatory Note

Special Resolution, Special General Meeting 26th September 2018

1. Background

- 1.1. Scottish Friendly flourishes through a three-part growth strategy of organic growth, mergers and acquisitions and business process outsourcing.
- 1.2. ‘Mergers and Acquisitions’ includes ‘transfers of engagement’ and the aim is to gain additional economies of scale plus a diversified income stream. These aims are reflected in the opportunity now presented for Scottish Friendly: scale will be achieved through the increased policyholder numbers and uplift in assets under management and a diversified income stream will be provided from the new line of pensions business which we propose to acquire (see details in Section 2 below) and which we would hope to grow in the future.
- 1.3. Since 2006 we have transferred in Rational Shelley Friendly Society Limited, Preston Operative Friendly Society, a small book of business from Pioneer Friendly Society Limited, London Aberdeen & Northern Mutual Assurance Society (LANMAS), Royal Standard Friendly Society Limited, Scottish Legal Life Assurance Society Limited and most recently, Marine & General Mutual Life Assurance Society (M&GM). The transfer of the M&GM book of business in June 2015 was the biggest transfer undertaken by Scottish Friendly to date, more than doubling Scottish Friendly’s assets under management. Collectively, however, these seven transactions have added over £1bn funds under management and generate significant administration income per annum to Scottish Friendly policyholders.
- 1.4. The proposed transfer from Mobius Life Limited (Mobius Life) is another opportunity in line with Scottish Friendly’s overall strategy.

2. Mobius Life

- 2.1. Mobius Life is a unit-linked life insurance company, established in 1997. The focus of Mobius Life is UK pension schemes. The part of the business that Scottish Friendly proposes to acquire is a book of contract-based group pension schemes, which Mobius Life has concluded is not core to its business.
- 2.2. Mobius Life’s transferring business has approximately 13,000 policyholders and £350m of admissible assets at 31 March 2017.
- 2.3. The impact of the transfer on the capital position of Scottish Friendly is shown in the table below. It is expected that the capital position will deteriorate albeit to a level judged to be appropriate for the investment being made. The capital cover will reduce from 199% to 191% with the excess capital resources reducing from £80.9m to £78.0m.

SF Pillar 1 result 31 December 2016	Pre transfer	Post transfer
Total Assets	£2,552.4m	£2,892.6m
Total Liabilities	£2,369.8m	£2,708.9m
Excess of Assets over Liabilities	£182.6m	£183.7m
Own Funds ¹	£162.7m	£163.8m
Capital resources requirement (SCR)	£81.8m	£85.8m
Excess capital resources	£80.9m	£78.0m
Capital cover	199%	191%

- 2.4. The Solvency Capital Requirement (SCR) is estimated to increase by £4.0m. This is primarily driven by additional market risk.

3. Corporate Governance

- 3.1. In February 2017, an information memorandum issued on behalf of Mobius Life was made available to a number of life offices across the UK. The responses were considered by the financial advisers retained on behalf of Mobius Life and Scottish Friendly was selected as the partner for exclusive discussions in July 2017.
- 3.2. Scottish Friendly conducted due diligence of the relevant Mobius Life business during 2017; throughout, Scottish Friendly was supported by EY; legal advice was provided by CMS Cameron McKenna Nabarro Olswang LLP.
- 3.3. The legislation that applies to Friendly Societies, such as Scottish Friendly, requires that the transfer of insurance business is approved by the Delegates on behalf of members. As Mobius Life is an insurance company, Delegates' approval is sought by way of the special resolution, as per the Notice. Mobius Life is not a mutual society and therefore does not have any members. Mobius Life does not need any express policyholder approval for the transfer.

4. Process

- 4.1. The proposed transfer is to be carried out under section 111(1) of the Financial Services and Markets Act 2000. Scottish Friendly and Mobius Life have followed a strict legal and regulatory process that includes obtaining an assessment of the transfer from an Independent Expert. The duty of the Independent Expert is to review the impact of the changes resulting from the transfer against the interests of all affected policyholders (including the Scottish Friendly policyholders) and to write a report on his findings to the Court. That report is also provided to the Regulators. A summary of the Independent Expert's report is attached, having been duly approved as providing the key points of the proposal.
- 4.2. We have also consulted with our regulators, the Prudential Regulation Authority ('PRA') and the Financial Conduct Authority ('FCA') (together the 'Regulators').

¹ This represents the total capital resources once ring-fencing of sub-funds has been allowed for.

- 4.3. The Chief Actuary and the With-Profits Actuary of Scottish Friendly, together with the Chief Actuary of Mobius Life have each written their own reports on the effects of the transfer on the companies and policyholders.
- 4.4. The terms of the transfer are detailed in documentation ('the Scheme'). Copies of the full Scheme document are available on request from the Secretary, Martin Pringle and on the Scottish Friendly website www.scottishfriendly.co.uk.
- 4.5. The transfer requires an order given by the High Court of Justice of England and Wales (the 'Court') sanctioning the Scheme. The proposed effective date of this transfer is 9 November 2018.
- 4.6. In addition to the approvals which are being sought as described in paragraph 4.1 above, legislation requires both Scottish Friendly and Mobius Life to notify its respective policyholders of the proposed transfer and invite them to make representations (if any) to the Court. Scottish Friendly has been granted a waiver from the Court from the requirement to notify its policyholders on the basis that the approval process from the delegates, coupled with the extensive advertisement of the transfer which Scottish Friendly and Mobius Life are undertaking, are sufficient.

5. Key Features of the Terms of the Transfer

- 5.1. Scottish Friendly will purchase certain of the unit linked group pension business of Mobius Life for £3.1m payable on transfer; those policies will transfer into the Scottish Friendly main fund.
- 5.2. All holders of Mobius Life policies will become members of Scottish Friendly, with the same rights in future as Scottish Friendly members.
- 5.3. The member administration of the Mobius Life policies to be transferred is currently undertaken by Aegon. It is intended that the agreement between Mobius Life and Aegon will be novated to Scottish Friendly on transfer and accordingly Aegon will continue to administer the policies post-transfer.
- 5.4. The investment administration of the Mobius Life policies to be transferred is currently undertaken by Mobius Life themselves. It is intended that Mobius Life will continue the investment management and investment administration of the assets and this has been included in the price proposed. A reinsurance arrangement will be put in place with Mobius Life with effect from the effective date to reinsure the liability of Scottish Friendly under the Mobius Life policies to be transferred. This will be accompanied by a floating charge intended to provide protection to Scottish Friendly in case of an insolvency event of Mobius Life.

6. Concluding Remarks

- 6.1. The Scottish Friendly Board has considered the strategic, prudential, operational and conduct risks of this transaction in detail, with risk registers assessing the risks of both the transaction and the implementation.

6.2. As noted above, the transaction is in line with the agreed strategy; the Board is satisfied that it does not compromise any other strategic initiatives.

Please feel free to contact me or Martin Pringle as Company Secretary, if you wish to raise any questions in advance of the meeting. Otherwise there shall of course be an open discussion and an opportunity for questions in the course of the meeting.

The Board very much hopes that the resolution will meet with your approval in what it judges to be a valuable opportunity for Scottish Friendly, in the best interests of members.

Jim Galbraith
Chief Executive

[Date]

Attachments

1. Mobius Life Policyholders Circular
2. Summary Report of Independent Expert