

MILLIMAN REPORT

# The proposed amendment to the Scheme of Transfer between Phoenix Life Assurance Limited and The Royal London Mutual Insurance Society Limited

The supplementary report of the Independent Actuary

24 October 2022

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# 1. Introduction

## BACKGROUND TO ROYAL LONDON AND THE PLAL FUND

### The Royal London Mutual Insurance Society Limited

- 1.1 The Royal London Mutual Insurance Society Limited ("**RLMIS**") is a mutual insurance company that is the parent entity of the Royal London Group ("**RLG**").
- 1.2 As at 30 June 2022, RLMIS had £150 billion of assets under management, 8.8 million policies in force and £98 billion of Technical Provisions.
- 1.3 RLMIS currently consists of the Royal London Open Fund (the "**RL Open Fund**") and three ring-fenced funds referred to collectively as the "**RLMIS Closed Funds**". The RLMIS Closed Funds contain the assets and liabilities relating to business acquired through various acquisitions by RLMIS. The most relevant sub-funds for this Report are:
- The RL Open Fund; and
  - The PLAL With-Profits Fund (the "**PLAL Fund**").
- 1.4 All financial information in this Report is, unless otherwise stated, as at 30 June 2022, which is the date of the latest available published figures. From 30 June 2022 to the date of finalising this report, market conditions have been volatile, with rapid increases in UK interest rates (as measured by sterling swap yields), falls in UK equity markets and a deterioration in the outlook for price inflation in the UK. Therefore, I have also included commentary on the estimated position at 30 September 2022 based on RLMIS's internal modelling, and on the potential effect of subsequent developments in financial markets.

### The RL Open Fund

- 1.5 The RL Open Fund is the largest fund within RLMIS, and all new policies issued by RLMIS, with the exception of increments or options on existing policies allocated to some other funds, are written in the RL Open Fund.
- 1.6 The inherited estate of the RL Open Fund (the "**RL Open Fund Estate**") provides capital to support the business activities of RLMIS, including writing new business in the RL Open Fund. In return, the RL Open Fund Estate receives profits (or incurs losses) from these business activities.
- 1.7 The RL Open Fund's financial strength is managed to a target range measured by the fund's solvency coverage. As at 30 June 2022 (and as at 30 September 2022 based on RLMIS's internal modelling), the RL Open Fund was above its target range.

### The PLAL Fund

- 1.8 Phoenix Life Assurance Limited<sup>1</sup> ("**PLAL**") was formed in 1991 as Abbey National Life plc. In September 2006 it was acquired by Resolution Life plc ("**Resolution**") and renamed PLAL. PLAL was acquired by RLMIS in August 2008 and in December 2008, the long-term business of PLAL was transferred to RLMIS by way of a scheme of transfer ("**PLAL Scheme**").
- 1.9 Under the PLAL Scheme, the with-profits business of PLAL was transferred into the newly established PLAL Fund and the non-with-profits business of PLAL was transferred into the RL Open Fund.
- 1.10 The PLAL Fund comprises only Unitised With-Profits ("**UWP**") business, with a mixture of life and pension business. Some products are hybrid, allowing the policies ("**hybrid policies**") to hold a UWP investment in the PLAL Fund as well as unit-linked investments held in the RL Open Fund. These are referred to as the "**UWP element**" and "**unit-linked element**", respectively, of the policies throughout this Report.

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<sup>1</sup> Phoenix Life Assurance Limited is now also the name of a legal entity in the Phoenix Group, which is unrelated to RLMIS and this Amendment and Consequent Actions

- 1.11 The PLAL Fund is managed to a target solvency coverage in the same way as the RL Open Fund. As at 30 June 2022 (and as at 30 September 2022 based on RLMIS's internal modelling), the PLAL Fund was above its target range.
- 1.12 Where the financial strength of the PLAL Fund allows it, distributions are made from the estate of the PLAL Fund (the "**PLAL Estate**") to the UWP element of policies in the PLAL Fund using a combination of enhancements to asset share<sup>2</sup> and uplifts to claim values. The level of these enhancements and uplifts is chosen to manage the solvency position of the PLAL Fund to a target level over a short period of years, in line with RLMIS's capital management framework.
- 1.13 Under the terms of the PLAL Scheme, RLMIS may elect to cease to maintain the PLAL Fund once the value of the assets in the PLAL Fund falls below £50 million (indexed annually in line with the Retail Prices Index ("**RPI**")). In this Report, I refer to this provision of the PLAL Scheme as the "**PLAL Sunset Clause**" and the £50 million threshold (indexed with RPI) as the "**PLAL Sunset Clause Threshold**".
- 1.14 As a result of indexation, since 31 December 2021 the PLAL Sunset Clause Threshold has been £74 million (with total assets of the PLAL Fund being £401 million on 30 June 2022). Under best estimate projections, the PLAL Sunset Clause Threshold is expected to be reached in 2032.
- 1.15 The PLAL Scheme provides that, when RLMIS elects to cease maintaining the PLAL Fund (after reaching the PLAL Sunset Clause Threshold or otherwise):
- The provisions in the PLAL Scheme for the maintenance of the PLAL Fund as a separate sub-fund of RLMIS will cease to apply;
  - All of the policies, assets and liabilities of the PLAL Fund will be transferred to the RL Open Fund; and
  - Any other modifications and/or additions shall be made to the PLAL Scheme as may be necessary to give effect to the closure of the PLAL Fund.

#### THE PROPOSED AMENDMENT TO THE PLAL SCHEME

- 1.16 It is proposed to amend the provisions of the PLAL Sunset Clause by increasing the PLAL Sunset Clause Threshold from its stated value of £50 million (indexed annually in line with RPI) to a fixed value of £500 million (of assets in the PLAL Fund). This would cause the PLAL Sunset Clause Threshold to be reached immediately.
- 1.17 Various other changes would be made to add clarity to the actions to be taken when the PLAL Sunset Clause is triggered, such as how the PLAL Estate should be distributed.
- 1.18 This is referred to in this Report as the "**Amendment**".
- 1.19 Under the terms of the PLAL Scheme, the Amendment can only be made with the consent of the High Court of England and Wales (the "**High Court**"), following consideration by an independent actuary who should provide a certificate to the High Court stating that in their opinion the Amendment does not adversely affect the reasonable expectations of the holders of the policies covered by the PLAL Scheme.
- 1.20 The Directions Hearing for the Amendment took place on 27 June 2022. At the Directions Hearing, the High Court approved the issue of the Notification Pack advising policyholders of the PLAL Fund of the proposal to make the Amendment. The Sanction Hearing for the Amendment will take place on 8 November 2022.
- 1.21 The Amendment would take effect from the "**Amendment Date**" (expected to be 5 December 2022).
- 1.22 As part of my role as Independent Actuary I have an obligation to assist the High Court in its deliberations. I have included the certificate of compliance required by Part 35 of the Civil Procedure Rules in Appendix C of this Report.

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<sup>2</sup> Asset share is a measure of the underlying value of a with-profits policy based on premiums paid, investment returns earned and expenses incurred in managing the policy.

## THE ACTIONS TAKEN AS A CONSEQUENCE OF THE AMENDMENT

- 1.23 If the Amendment is approved by the High Court, then the triggering of the PLAL Sunset Clause will result in the following actions being taken on the **"Implementation Date"** (expected to be 31 December 2022):
- The provisions in the PLAL Scheme for the maintenance of the PLAL Fund as a separate sub-fund of RLMIS will cease to apply;
  - An immediate uplift (the **"Uplift"**) will be applied to the asset share of policies in the PLAL Fund (and so to only the UWP element in the PLAL Fund for the hybrid policies) to distribute the PLAL Estate. The Uplift will take the form of a uniform percentage of the asset share on the Implementation Date (the **"Uplift percentage"**); and
  - All of the policies, assets and liabilities of the PLAL Fund will be transferred to the RL Open Fund.
- 1.24 In addition to the above actions taken on the Implementation Date, for policies where the policyholder is still paying regular contractual premiums, the same Uplift percentage will also be applied to the amounts allocated to asset share in respect of future contractual premiums, as and when those premiums are paid and credited to asset shares after the Implementation Date. For the avoidance of doubt this will not change the amounts of the premiums payable by policyholders.
- 1.25 These are referred to as the **"Consequent Actions"** in this Report.
- 1.26 The asset shares and future contractual premiums to which the Uplift will apply are subject to eligibility criteria.

## THE MOTIVATIONS FOR THE PROPOSED AMENDMENT AND THE CONSEQUENT ACTIONS

- 1.27 In the absence of the Amendment, the PLAL Scheme does not explicitly provide for all of the Consequent Actions or allow these to be carried out until the triggering of the PLAL Sunset Clause.
- 1.28 Carrying out the Amendment would provide clarity in the PLAL Scheme as to how the Consequent Actions should be implemented and would result in the RLMIS Board having the ability to trigger the PLAL Sunset Clause at any time after the Amendment Date. This would enable the Consequent Actions listed above in paragraphs 1.23 and 1.24 to be carried out.
- 1.29 The main motivations for the Consequent Actions are that they would simplify the management of RLMIS's business, and also lead to a fairer and more certain distribution of the PLAL Estate among PLAL Fund policies.

## MY ROLE AS THE INDEPENDENT ACTUARY

- 1.30 I have been appointed by RLMIS to fulfil the role of Independent Actuary and report on the effects on, and fairness to, the policyholders of RLMIS of:
- The proposed Amendment to the PLAL Scheme; and
  - The Consequent Actions taken by RLMIS,
- and to determine whether the proposals would be fair and reasonable to policyholders.
- 1.31 I am a Fellow of the Institute and Faculty of Actuaries. I am a partner of Milliman LLP (**"Milliman"**), part of Milliman Inc., a global consulting firm. I have over 40 years' experience in the UK life insurance industry and I have previously fulfilled the role of Independent Expert or Independent Actuary for more than 20 transfers of long-term insurance business under Part VII of the Financial Services and Markets Act 2000.
- 1.32 In relation to my independence from RLMIS:
- I am not a member of RLMIS;
  - I do not have any policies with RLG nor with any of its constituent companies; and
  - I am not a member of a pension scheme administered by RLG or by any of its constituent companies.

## MY MAIN REPORT AND REVIEW OF THE PROPOSED AMENDMENT AND CONSEQUENT ACTIONS

- 1.33 I prepared a report dated 10 June 2022 ("**my Main Report**") setting out my review of the proposed Amendment and Consequent Actions, and their likely effect on, and fairness to, the policyholders of RLMIS. My Main Report is available on the RLMIS website, and a paper copy may be requested from RLMIS.
- 1.34 In my Main Report I assessed the effects on the RLMIS policyholders of the proposed Amendment and Consequent Actions by considering a set of tests that should be passed in order for me to be satisfied that the implementation of the Amendment and Consequent Actions would be fair and reasonable to the policyholders of RLMIS. These tests are called the Fairness Tests and are as follows:
- The Security of Policyholder Benefits Test;
  - The Policyholder Outcomes Test;
  - The Adverse Scenario Test;
  - The Policyholder Communications Test; and
  - The Fair Conduct Test.
- 1.35 The Fairness Tests are set out in detail in Section 4 of my Main Report, and the work I carried out in the consideration of these Fairness Tests (and various other considerations) is described in Sections 5 to 15 of my Main Report.

## THE PURPOSE OF MY SUPPLEMENTARY REPORT

- 1.36 This report is supplemental to my Main Report and is referred to as "**my Supplementary Report**" or "**this Supplementary Report**". The purpose of my Supplementary Report is to consider the following:
- An update on the effect of the implementation of the Amendment and Consequent Actions based upon more up-to-date financial information and on any other material developments since the date of my Main Report.
  - Whether the Amendment and Consequent Actions would remain fair and reasonable under a range of circumstances and scenarios ahead of the expected Implementation Date.
  - The communication materials in respect of the Amendment and Consequent Actions due to be issued to policyholders after the implementation of the Amendment and Consequent Actions (the "**Confirmation Mailing**").
  - Any policyholder objections in relation to the Amendment and Consequent Actions.
  - Any significant events or market changes that have occurred between the finalisation of my Main Report and the finalisation of this Supplementary Report.
- 1.37 This Supplementary Report will be presented to the High Court at the Sanction Hearing, and before then will be made available to policyholders and others via the RLMIS website.
- 1.38 As is the case with my Main Report, this Supplementary Report does not provide financial or other advice to individual policyholders.

## TERMINOLOGY USED IN THIS REPORT

- 1.39 Throughout this Report I have used certain terms that are in common usage within the UK insurance industry, particularly terms that relate to with-profits products and to the accounting, regulatory and solvency regime that applies to UK insurers.
- 1.40 Unless otherwise stated, these terms, and the abbreviations used herein, have the same definition and explanation as given in Appendix E of my Main Report.

1.41 A summary of the UK life insurance market and regulatory environment is set out in Appendix A to my Main Report.



## 2. Significant developments since the finalisation of my Main Report

### SUMMARY OF DEVELOPMENTS

2.1 Since my Main Report dated 10 June 2022 was finalised, there have been a number of developments, which I describe below:

- I have been provided with an update on the effect of the implementation of the Amendment and Consequent Actions based upon financial information as at 30 June 2022, and a further estimate based on the position at 30 September 2022. As noted in paragraph 1.4, there have been significant changes in financial conditions since 30 June 2022, including a substantial increase in long term interest rates and in price inflation in the UK, with the outlook remaining highly uncertain.
- The interim Uplift percentage that will be applied on the Implementation Date (expected to be 31 December 2022) has been estimated as at 30 September 2022 to be 5.6%, although this percentage has not been finalised as at the date of this Supplementary Report.
- I have been provided with information on the expected final Uplift percentage under a range of circumstances and scenarios as at 30 June 2022.
- RLMIS has received one expression of dissatisfaction from a PLAL Fund policyholder following the Notification Mailing.
- The Confirmation Mailing has been drafted by RLMIS.
- The Liver Schemes have proceeded to the policyholder votes following the Convening Hearings in June 2022 and, if approved, would become effective on the same day as the Consequent Actions (i.e. 31 December 2022).
- The FCA has published its Policy Statement and Finalised Guidance for the new Consumer Duty.

2.2 I cover these in turn below.

### THE EFFECT OF THE AMENDMENT AND CONSEQUENT ACTIONS ON THE SECURITY OF THE GUARANTEED BENEFITS OF THE RLMIS POLICYHOLDERS

#### Introduction

2.3 Section 5 of my Main Report summarised the outcome of the Security of Policyholder Benefits Test based on the financial conditions and actuarial assumptions as at 31 March 2022. My Main Report was finalised on 10 June 2022 and I now have access to financial information as at 30 June 2022 (the date of the latest available published figures).

2.4 In this section of my Supplementary Report, I cover the outcome of the Security of Policyholder Benefits Test based on the financial conditions and actuarial assumptions as at 30 June 2022. In light of recent market volatility, I have also considered the estimated financial information as at 30 September 2022, and the potential effect of subsequent changes in financial conditions up to the date of this Supplementary Report.

2.5 I have considered the impact of the change in the outlook for price inflation in the UK in paragraphs 2.17 to 2.19.

#### Policyholders of the PLAL Fund and the RL Open Fund

2.6 If the Amendment and Consequent Actions are implemented, the PLAL Fund policies will be consolidated into the RL Open Fund and these policies, together with the existing policies in the RL Open Fund, will derive security for their guaranteed benefits from:

- The assets in the RL Open Fund held to cover (in respect of the current RL Open Fund policies and the policies currently in the PLAL Fund that would be transferred under the PLAL Fund Consolidation):
  - The Technical Provisions and Internal SCR calculated in accordance with the UK Solvency II regulatory regime; and
  - The buffer held in excess of its Internal SCR in line with the RLMIS Capital Framework; and
- The capital support arrangements set out in the RL Long Term Fund Principles and Practices of Financial Management, under which, in extreme circumstances, the estates of the remaining RLMIS Closed Funds would be available to provide capital support to the RL Open Fund should this be required.

2.7 Table 2.1 below shows the pre-Amendment and Consequent Actions financial position of the RL Open Fund and the PLAL Fund, as well as the *pro forma* post-Amendment and Consequent Actions financial position of the RL Open Fund. The figures are shown on a UK Solvency II basis as at 30 June 2022.

2.8 The financial information in Table 2.1 assumes that the Liver Schemes have not been implemented, and that the UK Liver Fund remains in the group of RLMIS Closed Funds. I have considered the impact of the Liver Schemes further in paragraphs 2.42 to 2.52.

**TABLE 2.1 PRE- AND POST-AMENDMENT AND CONSEQUENT ACTIONS FINANCIAL POSITION (UK SOLVENCY II) AS AT 30 JUNE 2022**

	Pre-Amendment and Consequent Actions		Post-Amendment and Consequent Actions
£million	PLAL Fund	RL Open Fund	RL Open Fund
Assets (A)	401	84,725	85,126
Liabilities (B)	381	80,550	80,951
<i>Of which asset shares</i>	367	10,720	11,107
<b>Available capital before adjustments (C = A - B)</b>	<b>20</b>	<b>4,176</b>	<b>4,175</b>
Risk margin (D)	0	1,039	1,039
TMTP (E)	0	926	928
Sub-debt (F)	-	1,297	1,297
<b>Internal Own Funds (G = C - D + E + F)</b>	<b>21</b>	<b>5,361</b>	<b>5,361</b>
Internal SCR (H)	6	2,361	2,362
<b>Excess capital (G - H)</b>	<b>15</b>	<b>3,000</b>	<b>2,999</b>
<b>Internal SCR Cover (G / H)</b>	<b>342%</b>	<b>227%</b>	<b>227%</b>

2.9 The Internal SCR Cover of the PLAL Fund and the RL Open Fund have both increased since the 31 March 2022 figures shown in my Main Report. However, the impact of the implementation of the Amendment and Consequent

Actions is broadly unchanged; that is, if the Amendment and Consequent Actions had been implemented on 30 June 2022 then:

- There would have been no material change to the RL Open Fund's Internal SCR Cover, which would have remained at 227% when rounded. Therefore, the RL Open Fund would have remained above the acceptable range of the RLMIS Capital Framework.
- The PLAL Fund business would be transferred from a fund with 342% Internal SCR Cover (which is above the target range under the RLMIS Capital Framework), to a fund with an Internal SCR Cover of 227%.

The relatively high current Internal SCR Cover for the PLAL Fund arises principally because the SCR of the PLAL Fund is small in absolute terms, rather than because the PLAL Fund's available capital is very high. The Internal SCR Cover of 227% (the projected position for the RL Open Fund post-Amendment and Consequent Actions) remains a high level of coverage of the SCR. Noting that the SCR itself is the capital estimated to ensure solvency over a one-year time horizon with a likelihood of at least 99.5%, an Internal SCR Cover of 227% provides significant additional security to policyholders above the SCR. Therefore, it is my view that PLAL Fund policyholders would not experience a material reduction in the security of their benefits as a result of the difference between the Internal SCR Cover levels before and after the Amendment and Consequent Actions.

2.10 Considering the market volatility since this time, based on RLMIS's internal modelling, as at 30 September 2022:

- The Internal SCR Cover of the PLAL Fund remained above the target range under the RLMIS Capital Framework;
- The Internal SCR Cover of the RL Open Fund has decreased marginally to around 225%, while still comfortably exceeding the requirements of the RLMIS Capital Framework; and
- The expected impact of the Amendment and Consequent Actions on the financial position of the RL Open Fund is unchanged, with no material change to the RL Open Fund's Internal SCR Cover if the Amendment and Consequent Actions had been implemented on 30 September 2022.

2.11 Overall, I am satisfied that the implementation of the Amendment and Consequent Actions would not have a material adverse effect on the financial strength of the fund in which the policies are held (which for the PLAL Fund policies would change to be the RL Open Fund following the Amendment and Consequent Actions).

2.12 There have been no other changes to the financial position of either the PLAL Fund or the RL Open Fund since the finalisation of my Main Report that would affect my conclusions on the security of guaranteed benefits for the policyholders in these funds. In particular, there have been no material changes to the risk profiles of either fund or to the RLMIS Capital Framework.

#### **Policyholders of the Other RLMIS Closed Funds**

2.13 Implementation of the proposed Amendment and Consequent Actions would only affect holders of policies in the Other RLMIS Closed Funds if it had a material impact on the financial strength of the RL Open Fund, and thereby on the security provided by the RL Open Fund to the Other RLMIS Closed Funds.

2.14 As noted in paragraph 2.9, based on figures as at 30 June 2022, the implementation of the Amendment and Consequent Actions would have resulted in no material change to the RL Open Fund's Internal SCR Cover and so the RL Open Fund would have remained above the acceptable range of the RLMIS Capital Framework.

2.15 I am not aware of any other developments since the finalisation of my Main Report that would affect my conclusions for the policyholders of the Other RLMIS Closed Funds.

#### **Conclusion**

2.16 Having considered the more up-to-date financial information, I am satisfied that my conclusions in respect of the Security of Policyholders' Benefits Test set out in my Main Report remain valid, i.e. I remain satisfied that the

implementation of the Amendment and Consequent Actions would have no material effect on the security of guaranteed benefits of any of the policies of RLMIS.

## THE OUTLOOK FOR INFLATION

- 2.17 All of the business of the PLAL Fund is subject to Annual Management Charges (“**AMCs**”), which are transferred to the RL Open Fund. The RL Open Fund then covers the incurred management costs associated to the PLAL Fund, including the costs of administration and investment management, and so the RL Open Fund bears the expense risk for the PLAL Fund policies. The expected claim payments for PLAL Fund policies, including the potential Uplift under the Amendment and Consequent Actions are therefore not directly affected by levels of inflation (although they may be indirectly affected by associated impacts on interest rates and investment returns more generally).
- 2.18 Higher inflation could also bring forward the date at which the PLAL Sunset Clause Threshold is expected to be reached. However, the inflation adjustment is only applied annually, and there would be no change to this date as a result of changes in market expectations of inflation that occurred between 31 December 2021 and 30 June 2022.
- 2.19 The level of inflation will affect the expenses that the RL Open Fund has to cover in respect of the PLAL Fund policies, whereas the AMCs received for PLAL Fund policies are fixed in percentage terms. However, this will be the case whether or not the Amendment and Consequent Actions are implemented. I am satisfied that the elevated uncertainty over future inflation rates will not cause the Amendment and Consequent Actions to have an adverse effect on the financial position of the RL Open Fund.

## THE EXPECTED FINAL UPLIFT PERCENTAGE UNDER A RANGE OF CIRCUMSTANCES AND SCENARIOS

- 2.20 The Adverse Scenario Test is intended to ensure that the conclusions of my Main Report and this Supplementary Report would remain valid in the event of foreseeable but unexpected changes in investment, and other, conditions before the Implementation Date.
- 2.21 I noted in my Main Report that, as the interim Uplift percentage was due to be calculated as at 30 September 2022 and I would be submitting a further report (this Supplementary Report) to the High Court for the Sanction Hearing for the Amendment on 8 November 2022, I would comment on the Adverse Scenario Test in my Supplementary Report only, taking account of more up-to-date financial information.
- 2.22 As set out in Section 12 of my Main Report on the Adverse Scenario Test, for practical reasons, the actual Uplift percentage that would be applied to PLAL Fund policies would be calculated and applied in two stages:
- An interim Uplift percentage calculated at 30 September 2022, based on the projected value of the PLAL Estate on 31 December 2022. This interim Uplift percentage is 5.6% and will be applied to asset shares on the Implementation Date; and
  - A final Uplift percentage will be calculated shortly after the Implementation Date based on the actual value of the PLAL Estate on 31 December 2022. This will be applied as follows:
    - If the difference between the interim and final Uplift percentages is not material in the opinion of the RLMIS WPA, the adjustment for the final Uplift percentage (whether an increase or a decrease) will be made at the next planned bonus declaration date, which for the PLAL Fund will be 31 December 2023; or
    - If the difference is material, the RLMIS Board (on the advice of the RLMIS WPA and RLMIS WPC) may consider amending bonuses earlier in 2023, e.g. from 1 July 2023.
- 2.23 For the Adverse Scenario Test, I therefore need to consider whether foreseeable but unexpected changes in conditions could lead to a materially different final Uplift percentage being calculated compared with the interim Uplift percentage. For practical reasons this analysis is based on financial information at 30 June 2022, which

produced an expected final Uplift percentage of 5.8%, but my considerations set out below apply equally to the shorter period between the calculation of the interim Uplift percentage (at 30 September 2022) and the final Uplift percentage (at 31 December 2022).

2.24 RLMIS has carried out some analysis of the possible changes in conditions that could occur in the period between 30 June 2022 and the Implementation Date, considering:

- Potential changes to the levels of equity markets, interest rates or inflation; and
- Differences in actual policy run-off patterns (policy surrenders, transfers, maturities, retirements, and deaths) compared with those expected and used in the calculation of the Uplift percentage at 30 June 2022 (projected to 31 December 2022).

2.25 Analysis of these scenarios assumed to occur between 30 June 2022 and the Implementation Date shows that the final Uplift percentage would be:

- 0.9 percentage points higher following a 20% fall in the value of equities (so a final Uplift percentage in this scenario of 6.7%); and
- 1.0 percentage points lower following a 20% increase in the value of equities (so a final Uplift percentage in this scenario of 4.8%).

2.26 While an increase in the value of equities would lead to a lower final Uplift percentage, this arises because the asset shares of the PLAL Fund policies would increase whereas the PLAL Fund Estate, which has no investment in equities, would not benefit from the same growth. I do not consider this to be detrimental to PLAL Fund policyholders as, although the percentage uplift reduces in this scenario, the absolute size of the potential uplift to their PLAL Fund policies does not.

2.27 The final Uplift percentage is significantly less sensitive to changes in interest rates, inflation and policy run-off patterns and so I am less concerned that there could be a material adverse impact in these scenarios.

2.28 I note that there has been a very significant increase in interest rates since 30 June 2022, which has led to a small decrease in the expected Uplift percentage from 5.8% based on financial information at 30 June 2022 to 5.6% based on financial information at 30 September 2022, with 5.6% being the interim Uplift percentage that will apply on the Implementation Date. This reduction in the Uplift percentage arises from a larger fall in the value of the PLAL Fund Estate (which is invested in fixed interest assets) than the fall in the asset shares, and also leads to a reduction in the absolute size of the potential uplift. However, this small change in the Uplift percentage in response to reasonably extreme changes in interest rates leads me to conclude that the Uplift percentage is stable enough not to give rise to a material further reduction in the value of the uplift over the three month period between the calculation of the interim and final Uplift percentages.

2.29 Those exiting before the next bonus declaration would receive the interim Uplift percentage, which has been locked in three months ahead of the Implementation Date at 5.6%. These policyholders would therefore:

- Be protected against any adverse changes in conditions over this three month period, which would otherwise have led to a lower Uplift percentage; but
- Not benefit from any favourable changes in conditions over this three month period, which would otherwise have led to a higher Uplift percentage.

2.30 As set out in Section 7 of my Main Report, for claims arising in 2023, the uplift that would have applied in the absence of the Amendment and Consequent Actions is 4.2% (through a combination of an enhancement to all asset shares of 0.8% in 2023 and an uplift on claim of 3.4%). Therefore, the expected interim Uplift percentage of 5.6% provides a higher uplift for these policyholders claiming in 2023 than in the absence of the Amendment and Consequent Actions, even if this is ultimately lower than the final Uplift percentage, and there is the added benefit of the downside protection for these policyholders. I therefore do not consider that the proposed approach of an

interim Uplift percentage for those claiming in the short term (chosen for practical reasons) would have a material adverse effect on PLAL Fund policyholders.

2.31 Finally, considering the policyholders of the RL Open Fund, the RL Open Fund Estate would:

- If the interim Uplift percentage is higher than the final Uplift percentage, meet the additional cost of applying the interim Uplift percentage to policies exiting before the next bonus declaration date; or
- If the interim Uplift percentage is lower than the final Uplift percentage, benefit from the reduced cost of applying the interim Uplift percentage to policies exiting before the next bonus declaration date.

2.32 However, the PLAL Fund Estate, which is the approximate total value of uplifts to be applied, is small relative to the size of the RL Open Fund Estate (£20 million compared to £4.2 billion as at 30 June 2022, or less than 0.5%), and so the cost of any variation in the uplift percentage being applied would not be material in the context of the size of the RL Open Fund Estate. Furthermore, the impact could be limited by RLMIS by amending bonuses on former PLAL Fund policies earlier in 2023, as set out in paragraph 2.22.

2.33 Taking the above into account, I am satisfied that my conclusions in relation to the Security of Policyholder Benefits Test and the Policyholder Outcomes Test would not be affected by foreseeable changes in investment conditions and/or unexpected changes in the volume of business in the PLAL Fund between 30 September 2022 and the Implementation Date (expected to be 31 December 2022).

#### **THE NOTIFICATION MAILING AND CORRESPONDENCE RECEIVED FROM POLICYHOLDERS**

2.34 At the Directions Hearing, the High Court approved the issue of the Notification Pack advising policyholders of the PLAL Fund of the proposal to make the Amendment.

2.35 Beginning in April 2022, RLMIS worked with specialist tracing partners to reduce the number of uncontactable policyholders, with the aim of maximising the number of policyholders of the PLAL Fund that could be notified of the proposed Amendment and Consequent Actions. This tracing activity initially focused on those policyholders for which RLMIS did not hold a valid address, but was later extended to include policyholders for whom a valid address was held, but which was flagged as potentially being out of date. Around 2,800 addresses were updated through this exercise, which represents approximately 31% of those included in the tracing exercise.

2.36 Dispatch of the Notification Mailing commenced on 22 August 2022 and ended on 16 September 2022. In respect of the c. 30,000 policyholders of the PLAL Fund, 24,746 mailings were issued during this period. Since 16 September it has been possible to send mailings to around 100 more policyholders. The remaining policyholders have not been mailed as it has not been possible to validate their addresses.

2.37 As at the date of finalising this Supplementary Report, RLMIS has received one expression of dissatisfaction from a policyholder of the PLAL Fund in respect of the proposals. This policyholder holds two with-profits policies in the PLAL Fund, with one policy maturing prior to the Implementation Date and one maturing after the Implementation Date, such that only the latter policy will receive the Uplift following the Amendment and Consequent Actions. Although I understand the policyholder's frustration in this circumstance, there must be a cut-off date for the application of the Uplift and, in my view, it would not be reasonable to treat this policyholder any differently from those with only a policy/policies maturing prior to the Implementation Date (who have not been informed of the planned Uplift and will not receive it).

2.38 As at the date of finalising this Supplementary Report, no objections from policyholders have been received by RLMIS or by me directly. I will review any policyholder objections (or any further expressions of dissatisfaction) that arise before, or on, the date of the Sanction Hearing and provide my views on these to the High Court at the Sanction Hearing, as required.

## THE CONFIRMATION MAILING

- 2.39 If the High Court sanctions the Amendment at the Sanction Hearing, a Confirmation Mailing will be sent to PLAL Fund policyholders following the Implementation Date of the Consequent Actions (expected to be 31 December 2022) to inform them of the uplift applied to their policy's asset share and that their policy now resides in the RL Open Fund.
- 2.40 At the time of finalising my Main Report, I had not yet seen a working version of this Confirmation Mailing. I have since seen and reviewed a draft version of the letter. I am satisfied that it clearly sets out the impact of the Amendment and Consequent Actions, and in particular it clearly states that the policies have remained as with-profits policies, so their value can still change over time.
- 2.41 Therefore I remain satisfied that the requirements of the Policyholder Communications Test have been met.

## THE LIVER SCHEMES

- 2.42 As described in Section 15 of my Main Report, during 2022 RLMIS intends to seek the approval of the High Court for the UK Liver Scheme and Royal London insurance DAC intends to seek the approval of the Irish High Court for the co-dependent Ireland Liver Scheme. Under the Liver Schemes, the UK Liver Fund would be consolidated into the RL Open Fund and its estate would be distributed to its policies that are eligible for distributions from the estate (which includes certain policies in the Ireland Liver Fund reinsured into the UK Liver Fund).
- 2.43 If approved, the Liver Schemes would become effective on the same day as the Consequent Actions (i.e. 31 December 2022).
- 2.44 Since the finalisation of my Main Report:
- The Convening Hearings for the Liver Schemes took place in June 2022. At these hearings, the relevant High Court (in the UK and Ireland) granted an order to convene the scheme meetings; and
  - The scheme meeting for the Ireland Liver Scheme took place on 20 October 2022, at which the policyholders eligible for this scheme voted on the scheme, and the thresholds for the policyholder vote were met.
- 2.45 The scheme meeting for the UK Liver Scheme is due to take place on 15 November 2022 and so the outcome of the policyholder vote for that Scheme is not yet known. However, if the thresholds for this policyholder vote are also met, the Liver Schemes can proceed to sanction.
- 2.46 I therefore need to consider the effects of the implementation of the proposed Amendment and Consequent Actions on the RLMIS policies in the scenario where the Liver Schemes have been implemented.
- 2.47 There have been no developments since the finalisation of my Main Report that would affect my conclusions in respect of the Liver Schemes set out in Section 15 of my Main Report, and so below I consider only the more up-to-date financial information made available to me by RLMIS.
- 2.48 As described in paragraph 2.9, if the Amendment and Consequent Actions had been implemented on 30 June 2022, there would have been no material change to the Internal SCR Cover of the RL Open Fund, so it would have remained at 227%. Based on estimated figures, there is also expected to be no material change to the Internal SCR Cover of the RL Open Fund if the Amendment and Consequent Actions had been implemented on 30 September 2022.
- 2.49 This is relevant because it is the financial position of the RL Open Fund after the implementation of the Amendment and Consequent Actions that will largely determine the financial strength available to support the guaranteed benefits of the PLAL Fund policies that are to be consolidated into the RL Open Fund under the Amendment and Consequent Actions, as well as the existing policies of the RL Open Fund.
- 2.50 In the event that the Liver Schemes were implemented at the same time as the Amendment and Consequent Actions, the overall impact on the financial position of the RL Open Fund (as at 30 June 2022) would have been a



decrease in the Internal SCR Cover of the RL Open Fund from 227% to 219%. However, the financial position of the RL Open Fund would have remained above the acceptable range under the RLMIS Capital Framework, i.e. still exceeding the target of the RLMIS Capital Framework so able to withstand a 1-in-20 year event without breaching its Internal SCR. The impact of the Liver Schemes on the RL Open Fund's Internal SCR Cover is expected to be broadly unchanged based on figures as at 30 September 2022, and so the RL Open Fund would have still exceeded the target if the Liver Schemes had been implemented on that date.

- 2.51 I am therefore satisfied that the implementation of the Liver Schemes alongside the Amendment and Consequent Actions would not have any effect on my conclusions under the Security of Policyholder Benefits Test in respect of the policies in the PLAL Fund (and for the avoidance of doubt, the RL Open Fund and the Other RLMIS Closed Funds).
- 2.52 Taking into account the above, I remain satisfied that the implementation of the Liver Schemes would not affect my conclusions in respect of the Fairness Tests.

### **THE FCA'S CONSUMER DUTY**

- 2.53 The FCA published its Policy Statement and Finalised Guidance for the new Consumer Duty in July 2022, which will set higher and clearer standards of consumer protection across financial services in the UK and require firms to put their customers' needs first. The duty includes, amongst other things, a new Consumer Principle that requires firms to deliver good outcomes for retail customers. These rules will come into force on 31 July 2023 for new and existing products or services that are open to new business, and on 31 July 2024 for closed products or services.
- 2.54 While the exact impact of the new duty on RLMIS and its policyholders is currently unknown, I note that the impact will be the same whether or not the Amendment and Consequent Actions are implemented. In particular, the same standards under the Consumer Duty will apply regardless of whether the PLAL Fund policies reside in a separate with-profits fund (i.e. the PLAL Fund) or in the RL Open Fund.



### 3. My conclusions

3.1 In this Supplementary Report I have reviewed the conclusions in my Main Report (finalised on 10 June 2022) in light of events since that date and I am satisfied that my conclusions as set out in Section 16 of my Main Report remain valid, i.e. that:

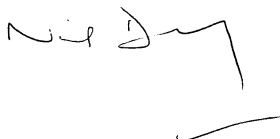
- I am satisfied that if the proposed Amendment and Consequent Actions are implemented there will not be a material adverse effect on:
  - The security of guaranteed benefits of the policies of RLMIS;
  - The reasonable benefit expectations of policyholders of RLMIS; and
  - The standards of administration, servicing, management and governance applying to the policies of RLMIS.
- The information that has been or is to be provided to policyholders in respect of the Amendment and Consequent Actions is clear, concise, and of an appropriate level of detail, and will have been provided to policyholders with sufficient time for them to assess the proposals and make an informed decision regarding whether to make representations to RLMIS and the High Court, or object to the proposals.
- In respect of the following areas the conduct of RLMIS in respect of the proposed Amendment and Consequent Actions is fair and reasonable to all policyholders:
  - The treatment of uncontactable policyholders; and
  - The legal mechanism used to consolidate the PLAL Fund into the RL Open Fund, and in particular RLMIS's decision not to effect the PLAL Fund Consolidation using a scheme of arrangement.

3.2 Furthermore, having considered more up-to-date financial information, I am satisfied that the Amendment and Consequent Actions would remain fair and reasonable under a range of circumstances and scenarios ahead of the expected Implementation Date.

3.3 I am therefore satisfied that the requirements of the Fairness Tests set out in Section 4 of my Main Report have been met.

3.4 I am satisfied that these conclusions would hold whether or not the Liver Schemes proceed.

3.5 The certificate wording specified in the PLAL Scheme, which is reproduced in full in Appendix C, requires an Independent Actuary to confirm that, in their opinion, the proposed amendments to the PLAL Scheme will not adversely affect the reasonable expectations of the holders of PLAL Fund policies. In accordance with the language conventionally used in reports such as this, for the reasons explained in paragraphs 4.28 and 4.29 of my Main Report, my conclusion above is that they will not have a material adverse effect on such reasonable expectations. However, having considered any potential immaterial adverse effects identified in my Main Report or this Supplementary Report, I expect to be able to provide the certificate in the prescribed form.



Nick Dumbreck

24 October 2022

Partner of Milliman LLP

## 4. Reliances and limitations of this Report

### MATTERS CONSIDERED

- 4.1 As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the Amendment and Consequent Actions proposals and in preparing this Report that nonetheless should be drawn to the attention of policyholders in their consideration of the terms of the Amendment and Consequent Actions proposals.

### INFORMATION AND DATA PROVIDED

- 4.2 In preparing my Supplementary Report, I have had access to certain documentary evidence provided by RLMIS and I have had access to, and discussions with the senior management of RLMIS. My conclusions depend upon the substantial accuracy of this information and I have relied on this information without independent verification. I have considered, and am satisfied with, the reasonableness of this information based upon my own experience across the UK life assurance industry.
- 4.3 In addition to the principal documents listed in Appendix B to my Main Report and Appendix A to my Supplementary Report, I have also relied upon the accuracy of financial information which has been provided to me by RLMIS. There has been no information that I have requested that has not been provided.
- 4.4 RLMIS has been advised by its own legal advisers, Pinsent Masons LLP ("**Pinsent Masons**"), and, in respect of certain matters, I have reviewed the legal advice provided by Pinsent Masons to RLMIS and have relied on that advice in reaching my conclusions on the basis set out in Section 4 of my Main Report. I have described in Section 4 of my Main Report why I believe it is reasonable to rely on advice given to RLMIS by Pinsent Masons. For the avoidance of doubt, Pinsent Masons has no liability to me in respect of that advice.

### USE OF THIS REPORT

- 4.5 My Supplementary Report should be read in conjunction with my Main Report and must be considered in its entirety as individual sections, if considered in isolation, may be misleading. The reliances and limitations listed in Section 13 of my Main Report also apply equally to my Supplementary Report. Draft versions of my Supplementary Report should not be relied upon for any purpose. No summary of my Supplementary Report may be made without my express consent.
- 4.6 My Supplementary Report has been prepared on the basis of terms of reference agreed with RLMIS, for use by the High Court, RLMIS and the other bodies listed below in the context of the Amendment and Consequent Actions and must not be relied upon for any other purpose. No liability will be accepted by Milliman, or me, for any application of my Supplementary Report to a purpose for which it was not intended, nor for the results of any misunderstanding by any user of any aspect of my Supplementary Report. In particular, no liability will be accepted by Milliman or me under the terms of the Contracts (Rights of Third Parties) Act 1999.
- 4.7 My Supplementary Report, as well as my Main Report and the summary of my Main Report, do not provide financial or other advice to individual policyholders. In particular, in my Supplementary Report, I have considered the impact of the Amendment and Consequent Actions on different groups of policyholders at what I believe is a level of granularity that is sufficient for me to make an assessment of the overall fairness of the terms of the Amendment and Consequent Actions. However, I have not considered the terms of proposals made at the level of individual policyholders. Affected policyholders may wish to consider seeking guidance or advice before making a decision on the course of action that is most suitable for their individual circumstances and my Supplementary Report is not a substitute for such advice or guidance.
- 4.8 My Supplementary Report contains certain terminology related to insurance products, the UK Solvency II regime and other areas. Where this terminology has been defined and explained in my Main Report, I have not in all cases

reproduced the relevant definition and explanation in my Supplementary Report. Readers of my Supplementary Report should refer to the definitions and explanations of such terminology that are in my Main Report.

#### **THE PARTIES FOR WHOM MY SUPPLEMENTARY REPORT HAS BEEN PREPARED**

4.9 My Supplementary Report has been prepared particularly for the use of:

- The High Court;
- The Directors and senior management of RLMIS;
- The RLMIS With-Profits Committee; and
- The PRA and the FCA as the regulators of RLMIS.

4.10 I am available to assist any of the parties listed above in interpreting this Report.

4.11 My Supplementary Report is also to be made available to the policyholders of RLMIS.

#### **PROFESSIONAL STANDARDS**

4.12 My Supplementary Report has been prepared subject to the terms of Technical Actuarial Standards (the “**TASs**”) applicable to insurance related work. In my opinion my Supplementary Report complies with TAS 100 (Principles for Technical Actuarial Work) and TAS 200 (Insurance) issued by the Financial Reporting Council.

4.13 To the extent that these TASs apply to the work done by RLMIS and its agents in order to produce the information upon which I have relied in preparing my Supplementary Report, I have relied without independent verification upon individuals within RLMIS and its agents to have complied with those standards in producing that information, except where non-compliance is explicitly stated. Subject to this reliance, in my opinion my Supplementary Report complies with TAS 100 and TAS 200.

4.14 Actuarial Profession Standard X2, as issued by the Institute and Faculty of Actuaries (“**IFoA**”), requires members of the IFoA to consider whether their work requires an independent peer review.

4.15 In my view my Supplementary Report does require independent peer review, and this has been carried out by a senior actuary in Milliman who has not been part of the team working on this assignment.

## Appendix A: Data relied upon

A.1 In addition to discussions (both orally and electronically) with RLMIS staff and the documents listed in Appendix B of my Main Report, I have relied upon the following principal documents in formulating my conclusions in this Supplementary Report:

- Balance Sheet Data as at 30 June 2022 , as well as estimated figures at 30 September 2022
- Chief Actuary's supplementary report on the proposed PLAL Amendment and Consequent Actions
- Confirmation Mailing
- RLMIS Tactical Model, including provisional calculation of the interim Uplift percentage
- With-Profit Actuary's supplementary report on the proposed PLAL Amendment and Consequent Actions

## Appendix B: Certificate of Compliance

I understand that my duty in preparing my report is to help the High 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 the requirements applicable to experts set out in Part 35 of the Civil Procedure Rules, the Practice Direction and the Guidance for the Instruction of Experts in Civil Claims 2014 produced by the Civil Justice Council, and have complied with and will continue to comply with them. As required by Part 35 of the Civil Procedure Rules, I hereby confirm that I have understood my duty to the High Court and have complied with and will continue to comply with this duty.

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.

I understand that proceedings for contempt of court may be brought against anyone who makes, or causes to be made, a false statement in a document verified by a statement of truth without an honest belief in its truth.



Nick Dumbreck

24 October 2022

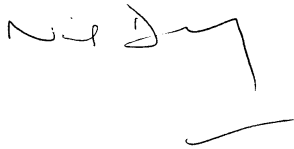
Fellow of the Institute and Faculty of Actuaries

## Appendix C: Independent Actuary's Certificate

Certificate under Clause 21.3 of the Scheme of Transfer between The Royal London Mutual Insurance Society Limited and Phoenix Life Assurance Limited (the "**PLAL Scheme**") as sanctioned by the English High Court, under which the long-term business of Phoenix Life Assurance Limited was transferred to The Royal London Mutual Insurance Society Limited pursuant to Part VII of the Financial Services and Markets Act 2000 on 29 December 2008.

I certify that, in my opinion, the proposed amendments to the PLAL Scheme will not adversely affect the reasonable expectations of the holders of policies transferred from Phoenix Life Assurance Limited to The Royal London Mutual Insurance Society.

In coming to this opinion I have taken account of the proposals as a whole and their impact on holders of policies transferred from Phoenix Life Assurance Limited as a whole.



Nick Dumbreck

24 October 2022

Fellow of the Institute and Faculty of Actuaries

Independent actuary appointed by The Royal London Mutual Insurance Society