

Report by Simon Sheaf FIA FSAI, Independent Expert, on the Proposed Transfer of a Portfolio of Policies from QBE UK Limited to East West Insurance Company Limited

9 August 2019



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1 Introduction

- 1.1 Insurance business transfers are subject to Part VII of Financial Services and Markets Act 2000, as amended ("FSMA"). These transfers are required to be approved by the High Court of England and Wales ("the Court") (or the Court of Sessions in Scotland) under Section 111 of FSMA. Such transfers are often referred to as Part VII transfers.
- 1.2 Section 109 of FSMA requires that a scheme report must accompany an application to the Court to approve an insurance business transfer scheme. This scheme report should be produced by a suitably qualified independent person ("Independent Expert") who has been approved by the Prudential Regulation Authority ("PRA"), in consultation with the Financial Conduct Authority ("FCA"). The scheme report should address the question of whether any policyholders impacted by the proposed insurance business transfer are adversely affected to a material extent.
- 1.3 QBE UK Limited ("QBEUK") and East West Insurance Company Limited ("EWICL") have jointly nominated Simon Sheaf ("I", "me") of Grant Thornton UK LLP ("Grant Thornton", "we", "us") to act as the Independent Expert for the proposed insurance business transfer ("the Scheme") of part of the insurance business of QBEUK to EWICL. The Scheme is intended to be effected on 4 December 2019 ("the Effective Date").
- 1.4 This nomination has been approved by the PRA in consultation with the FCA.
- 1.5 QBEUK is a UK regulated non-life insurance company which is authorised by the PRA and regulated by the PRA and the FCA. QBEUK underwrites a range of insurance products in both the UK and internationally. Until 31 December 2018, QBEUK was known as QBE Insurance (Europe) Limited. Further details on this are provided in Section 5. For the purposes of this report, I will refer to QBEUK, whether referring to it in its current form or its previous form.
- 1.6 In conjunction with this name change, QBEUK transferred a portfolio of business to a newly created entity, QBE Europe SA/NV, as part of its preparations for Brexit (the "QBE Brexit Transfer"). This transfer was effective 1 January 2019. For the purposes of this report, all financial information as at 31 December 2018 has been prepared on an indicative basis following the QBE Brexit Transfer.
- 1.7 EWICL is a UK regulated non-life insurance company, authorised by the PRA and regulated by the PRA and the FCA.
- 1.8 QBEUK has agreed to transfer the liabilities in two portfolios to EWICL under the provisions of FSMA.
- 1.9 The first of these portfolios consists of all UK and Republic of Ireland employers' liability and public liability business which had incepted on or prior to 31 December 2007, and subject to some specific policies remaining in QBEUK ("the Autumn Portfolio"). Approximately 1.6m policies were written within the Autumn Portfolio and there are approximately 720,000 policyholders. This includes risks located in the Netherlands and Italy.
- 1.10 The substantial majority of the claims in the Autumn Portfolio relate to mesothelioma, other asbestos related diseases and other diseases. The policies remaining in QBEUK also include claims relating to mesothelioma, other asbestos related diseases and other diseases. The Autumn Portfolio and those specific policies remaining in QBEUK are discussed further in paragraphs 5.10 to 5.13.
- 1.11 The second of these portfolios ("the Chestnut Portfolio") consists of the following (subject to specific liabilities remaining in QBEUK as set out in paragraph 5.15):
 - UK employers' liability policies issued by QBE Insurance (Europe) Limited ("QIEL"), a predecessor company of QBEUK, for Tata Steel Europe Limited ("TSEL") from 1 January 1990 and expiring on or before 31 March 2016
 - Global public and products liability, UK motor and UK personal accident issued by QIEL for TSEL expiring on or before 31 March 2016

TSEL is the sole policyholder within the Chestnut Portfolio.

- 1.12 In this report, I refer to the combination of the Autumn Portfolio and the Chestnut Portfolio as the “Transferring Portfolio”. The Transferring Portfolio currently benefits from excess of loss reinsurance contracts, which is discussed further in paragraphs 5.18 to 5.19.
- 1.13 The combination of the Transferring Portfolio and the excess of loss reinsurance contracts benefiting it is referred to as the “Transferring Business” within the QBEUK witness statement.
- 1.14 As part of the agreement to transfer the Autumn Portfolio to EWICL, QBEUK entered into a reinsurance agreement (the “Autumn LPTA”) with Tokio Millennium Re AG, Bermuda Branch (“TMR”). This agreement provides 100% quota share reinsurance to QBEUK in respect of the Autumn Portfolio up to an aggregate limit of an amount equal to 155% of the reserves as defined in the agreement. TMR subsequently entered into a reinsurance agreement with the parent company to EWICL, ILS Property & Casualty Re Limited (“ILS”). This agreement provides 100% quota share reinsurance to TMR in respect of the Autumn Portfolio (the “Retrocession Agreement”).
- 1.15 As part of the agreement to transfer the Chestnut Portfolio to EWICL, QBEUK entered into a reinsurance agreement with ILS. This agreement provides 100% quota share reinsurance to QBEUK in respect of all claims in the Chestnut Portfolio apart from any amounts above £1m (the “Chestnut LPTA”).
- 1.16 For the purposes of this report, I refer the combination of the Autumn LPTA, the Retrocession Agreement and the Chestnut LPTA as “the LPTAs”. The LPTAs were put in place for the purpose of reinsuring the policies under the Scheme. Should the Scheme become effective, the LPTAs will be terminated and ILS and TMR will no longer provide reinsurance in respect of the Transferring Portfolio.
- 1.17 The liabilities relating to the policies described in paragraphs 1.8 to 1.11 (the Transferring Portfolio), will be transferred to EWICL and are the subject of the Scheme.
- 1.18 For the purposes of this report, I will refer to the policyholders that will remain in QBEUK as “the Remaining Portfolio”. In addition, I will refer to those policyholders that are currently in EWICL as “the Existing EWICL Portfolio”.
- 1.19 The terms of my engagement are set out in a letter dated 10 January 2019. An extract of this letter setting out the scope of my work is included in Appendix F.
- 1.20 QBEUK and EWICL have borne the costs of producing this report equally.
- 1.21 Appendices B and C to this report contain definitions of technical terms and explanations of abbreviations used in this report respectively.

Layout of this report

- 1.22 My report is structured as follows:
- This section sets out an introduction to the Scheme and to this report.
 - Section 2 is an executive summary, which summarises the Scheme and the various analyses conducted and describes my conclusion
 - Section 3 sets out the scope of this report
 - Section 4 provides a summary of the methodology I have employed in order to assess the Scheme
 - Section 5 describes the background to the entities involved
 - Section 6 describes the regulatory background
 - Section 7 describes the work that I have carried out to assess the claims reserves of QBEUK, EWICL and the Transferring Portfolio

- Section 8 describes the work that I have carried out to assess the capital requirements of QBEUK and EWICL
- Section 9 provides my assessment of the policyholder security considerations, including under insolvency
- Section 10 provides my assessment of other financial considerations
- Section 11 provides my assessment of other non-financial considerations
- Section 12 discusses the proposed policyholder communications strategy
- Section 13 sets out the reliances and limitations that apply to my analysis and this report
- Section 14 sets out my conclusions on the Scheme.

Professional Experience

- 1.23 I am a Fellow of the Institute and Faculty of Actuaries ("IFoA") and a Fellow of the Society of Actuaries in Ireland. I currently hold a Chief Actuary (Non-life with Lloyd's) Practising Certificate and a Lloyd's Syndicates Practising Certificate issued by the IFoA. In addition, I have previously held an Irish Signing Actuary Practising Certificate and have previously been recognised as a Responsible Actuary by the financial regulator in Liechtenstein.
- 1.24 I joined Grant Thornton's Financial Services Group as General Insurance Practice Leader in 2006. I am a Partner in Grant Thornton and my current job title is Head of General Insurance Actuarial and Risk and I lead the provision of actuarial and risk consulting services to the general insurance sector. Prior to joining Grant Thornton, I held senior roles at Tillinghast – Towers Perrin (now part of Willis Towers Watson) and Travelers Insurance Company Limited.
- 1.25 I have experience in all areas of general insurance actuarial work (including reserving, capital, pricing and transactions), and have previously acted as Independent Expert for eight other sanctioned insurance business transfer schemes.
- 1.26 Full details of my experience can be found in Appendix E.

Independence

- 1.27 I have no financial interest in, nor have I previously advised, QBEUK or any company in the group of companies to which QBEUK belongs.
- 1.28 I have previously acted as the Independent Actuary for the transfer of a portfolio of insurance liabilities from Zurich Insurance plc to EWICL. I do not believe this previous assignment impairs my independence to act as the Independent Expert in relation to the Scheme. This previous assignment was disclosed to the PRA and the FCA, prior to my approval as the Independent Expert in relation to the Scheme.

Use of this report

- 1.29 The purpose of this report is to inform the Court of the likely effect of the Scheme upon policyholders. This report is not necessarily suitable for any other purpose.
- 1.30 This report is provided for the use of the Court, the QBEUK Board, the EWICL Board, QBEUK's policyholders, EWICL's policyholders, the PRA, the FCA and any other relevant regulator for the sole purpose of considering the impact of the Scheme on the affected policyholders.

- 1.31 In addition, draft and final versions of my reports may be distributed to QBEUK's and EWICL's legal advisers, and companies within the groups to which QBEUK and EWICL belong as necessary in connection with the transaction. Should any of our reports be distributed to any of the entities listed in the previous sentence, no reliance should be placed on our reports by these entities, and we do not assume any liability to these entities or any other third parties that choose to rely on our reports. In addition, QBEUK shall be responsible for any confidentiality breach that arises from the distribution of my reports to QBEUK's legal advisers, to companies within the group to which QBEUK belongs, or to any other entities to which it releases our reports. EWICL shall be responsible for any confidentiality breach that arises from the distribution of my reports to EWICL's legal advisers, to companies within the group to which EWICL belongs, or to any other entities to which it releases our reports.
- 1.32 Copies of the final version of this report may be made available for inspection by policyholders and copies may be provided to any person requesting the same in accordance with legal requirements. The final version of this report may also be made available on websites hosted by or on behalf of each of QBEUK and EWICL in connection with the Scheme.
- 1.33 However, notwithstanding the above, Grant Thornton does not accept any liability to any party other than QBEUK, EWICL and the Court who chooses to act on the basis of this report.
- 1.34 I have prepared a summary of this report to be included in the information sent to policyholders ("the Summary Report").
- 1.35 Shortly before the date of the Court hearing at which an order sanctioning the Scheme will be sought, I will prepare an update to this report covering any relevant matters which have arisen since the date of this report ("the Supplementary Report").
- 1.36 I consent to the final versions of my Summary Report and Supplementary Report being made available on the website to be hosted by or on behalf of each of QBEUK and EWICL in connection with the Scheme.
- 1.37 However, as stated above, Grant Thornton does not accept any liability to any party other than QBEUK, EWICL and the Court who chooses to act on the basis of any of my reports.
- 1.38 Judgements about the conclusions drawn in this report should only be made after considering the report in its entirety as any part or parts read in isolation may be misleading.
- 1.39 The underlying figures in this report are calculated to many decimal places. In the presentation of the figures in the various tables, there may be reconciliation differences due to the effect of rounding.

Professional Guidance

- 1.40 As an Independent Expert reporting to the Court, I am required to act in accordance with Part 35 of the Civil Procedure Rules, Practice Direction 35 and the Guidance for the Instruction of Experts in Civil Claims. Accordingly, this report is prepared for the assistance of the Court and I confirm that I understand my duty to the Court and have complied with that duty.
- 1.41 This report has been prepared under the terms of the Statement of Policy produced by the PRA in April 2015, namely "The Prudential Regulation Authority's approach to insurance business transfers" and the guidance set out in Chapter 18 of the Supervision Manual ("SUP18") contained in the FCA Handbook of Rules and Guidance to cover scheme reports on the transfer of insurance business. In addition, this report has been prepared in accordance with the FCA's guidance paper, entitled "The FCA's approach to the review of Part VII insurance business transfers".
- 1.42 In my opinion, this report has been produced in line with the requirements of the Technical Actuarial Standards ("TASs") issued by the Financial Reporting Council ("FRC"). In particular, this report has been prepared in accordance with TAS 100: Principles of Technical Actuarial Work and TAS 200: Insurance.

- 1.43 This report has also been produced in line with the requirements of APS X3: The Actuary as an Expert in Legal Proceedings produced by the IFoA.
- 1.44 In addition, this report has been internally peer reviewed in line with the requirements of APS X2: Review of Actuarial Work, issued by the IFoA.
- 1.45 I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions that I have expressed and conclusions that I have drawn represent my true and complete professional opinions on the matters to which they refer.

2 Executive Summary

Overview of the Scheme

- 2.1 This report considers the impact of the proposed transfer of the Autumn Portfolio and Chestnut Portfolio from QBEUK to EWICL. The transferring policyholders are corporate clients.
- 2.2 As part of the agreement to transfer the Autumn Portfolio and the Chestnut Portfolio to EWICL, ILS and QBEUK have entered into the LPTAs. Under the Autumn LPTA, TMR provides 100% quota share reinsurance to QBEUK in respect of the Autumn Portfolio, up to an aggregate limit of an amount equal to 155% of the reserves as defined in the agreement. TMR subsequently entered into the Retrocession Agreement with ILS to provide 100% quota share reinsurance to TMR in respect of the Autumn Portfolio.
- 2.3 Under the Chestnut LPTA, ILS provides 100% quota share reinsurance to QBEUK in respect of the Chestnut Portfolio, excluding portions of claims above £1m.
- 2.4 The policyholders remaining in QBEUK are a mixture of individual and corporate clients. QBEUK offers a wide variety of products to its policyholders.
- 2.5 The existing policyholders of EWICL are also a mixture of individual and corporate clients. The liabilities are all in run-off and stem either from portfolios written by EWICL or from a previous transfer into EWICL. The outstanding claims on the portfolio written by EWICL relate solely to London Market reinsurance while the previous transfer was of UK Building Guarantee liabilities.
- 2.6 I understand from EWICL that it has the necessary permissions to write the class of business being transferred into it.

Background to the companies

- 2.7 QBEUK is an insurance company that was established in 1983 under the name Legibus 373 Limited. It has since undergone several name changes. The most recent change, from QBE Insurance (Europe) Limited to QBEUK, became effective from 1 January 2019. It writes a variety of classes of business including accident and health, commercial property, credit and bond, energy, engineering, liability, marine, motor, terrorism and political risk, and inwards reinsurance.
- 2.8 EWICL is a non-life insurance company, which was originally established in 1964 under the name National & General Insurance Company (UK) Limited. EWICL historically underwrote employers' liability policies up until 1997, through a number of distribution channels. However, all outstanding claims relate to reinsurance written in the London Market.
- 2.9 On 31 March 2018, a run-off portfolio of UK Building Guarantee liabilities was transferred into EWICL by means of a Section 13 Transfer, as defined in Appendix B. The portfolio was underwritten by Zurich Insurance Plc between 1993 and 2009 when a decision was taken to cease writing new policies. However, policies in respect of existing contracts continued to inception until the final quarter of 2012.

My approach

- 2.10 My approach to assessing the likely effects of the Scheme on policyholders is to:
- Understand the nature and structure of the Scheme
 - Identify the groups of policyholders that would be affected
 - Assess the financial positions of the companies involved
 - Consider the implications of the Scheme on the level of security provided to the affected policyholders
 - Consider the potential impact of the Scheme on levels of customer service
 - Consider other financial factors that might affect policyholders
 - Consider other non-financial factors that might affect policyholders
 - Consider the implications of the Scheme on reinsurers.
- 2.11 In order to consider the effect of the proposed Scheme on each of the entities and groups of policyholders concerned, I have been provided with comparative information for each legal entity, including:
- Balance sheet information based on figures as at 31 December 2018 for each of QBEUK and EWICL
 - Actuarial reserve calculations for the Autumn Portfolio undertaken by QBEUK as at 31 May 2018
 - Actuarial reserve calculations for the Chestnut Portfolio undertaken by QBEUK as at 30 September 2018
 - Actuarial reserve report and calculations for the Transferring Portfolio undertaken on behalf of ILS and EWICL as at 30 September 2018
 - Actuarial reserve report for QBEUK as at 30 September 2018
 - Actuarial reserve report for EWICL as at 31 December 2018
 - Estimates of the regulatory capital required for QBEUK as at 31 December 2018
 - Estimates of the regulatory capital required for EWICL as at 31 December 2018 and the Effective Date
 - 2018 Own Risk and Solvency Assessments for QBEUK and EWICL
 - Internal management information for QBEUK and EWICL.
- 2.12 The information that I have been provided with were the most recent available at the time of my review. For some of the items, more up to date versions will be available by the time of the first Court hearing. I will issue a Supplementary Report based on the most up to date information available to me prior to the final Court hearing.
- 2.13 In forming my opinion, I have conducted a number of interviews with key personnel responsible for core functions in QBEUK and EWICL.
- 2.14 In forming my opinion, I have also placed reliance on, amongst other information, estimates of the reserves provided by QBEUK and on behalf of ILS and EWICL. In Section 7, I describe what information I relied on in relation to the reserves of the Transferring Portfolio, QBEUK and EWICL and the analyses I have undertaken to assure myself that it is reasonable to rely on that information.

- 2.15 In order to form an opinion based on this information, I have considered:
- The appropriateness of the methods used by QBEUK and on behalf of ILS and EWICL to calculate the reserves for the Transferring Portfolio as well as their wider businesses
 - My assessment of the appropriate level of reserves for the Transferring Portfolio.
- 2.16 In addition, in forming my opinion, I have also placed reliance on, amongst other information, estimates of the capital required provided by QBEUK and on behalf of EWICL. In Section 8, I describe what information I relied on in relation to the capital requirements of QBEUK and EWICL and the analyses I have undertaken to assure myself that it is reasonable to rely on that information.
- 2.17 In order to form an opinion based on this information, I have considered:
- The appropriateness of the methods used by QBEUK and on behalf of EWICL to calculate the estimates of capital requirements
 - The relative capital strength of the two companies
 - The absolute capital strength of each of the two companies
 - My own testing of the robustness of the capital strength of each of QBEUK and EWICL
 - The stress and scenario testing undertaken by QBEUK and on behalf of EWICL in relation to their respective capital bases.

Findings

- 2.18 The findings of my report are summarised in this section. The detailed explanation behind these conclusions follows in the body of this report.
- 2.19 I have identified three distinct groups of policyholders. These are:
- The transferring policyholders
 - The policyholders remaining in QBEUK
 - The existing policyholders of EWICL.
- 2.20 With respect to the transferring policyholders I do not expect any material adverse impact on policyholder security, including under insolvency, as a result of the Scheme. These policyholders would be moving to a company that I believe has a sufficient level of capital in order to meet policyholder obligations. Note that this conclusion is predicated on the fact that ILS Property & Casualty Master Fund Ltd, ILS and Armour will provide support to EWICL, should additional funds be required, as discussed in paragraphs 8.100 to 8.103. However, even if EWICL was not able to receive additional funds from ILS Property & Casualty Master Fund Ltd, ILS or Armour, my view is that the likelihood of EWICL being unable to pay claims as they fall due is remote.
- 2.21 With respect to the policyholders remaining in QBEUK, I do not expect any material adverse impact on policyholder security, including under insolvency, as a result of the Scheme as the Transferring Portfolio is immaterial in the context of QBEUK's overall business.
- 2.22 With respect to the existing policyholders of EWICL, I do not expect any material adverse impact on policyholder security, including under insolvency, as a result of the Scheme as I believe that EWICL has a sufficient level of capital in order to meet policyholder obligations following the Scheme.
- 2.23 I do not anticipate any material adverse changes to the level of service provided to any of the groups of policyholders following the Scheme.

- 2.24 I do not expect any material adverse impact to any group of policyholders following the Scheme as a result of the other financial and non-financial factors considered. The other financial factors that I have considered are:
- Investment strategy implications
 - Implications of the Scheme on ongoing expense levels
 - Pension arrangements
 - Tax implications
 - Liquidity
 - New business strategy
 - Other transfers.
- 2.25 The other non-financial factors that I have considered are:
- Regulatory regime
 - Complaints
 - Brexit
 - Management and governance framework.
- 2.26 I expect no material adverse impact on the reinsurers of the Transferring Portfolio as a result of the Scheme.
- 2.27 I expect no material adverse impact on the reinsurers of QBEUK or EWICL as a result of the Scheme.

Conclusion

- 2.28 I conclude that the risk of any group of policyholders or reinsurers being materially adversely affected by the Scheme is sufficiently remote that there is no reason why the Scheme should not proceed.

3 Scope

- 3.1 I am required as Independent Expert to consider the likely effects of the Scheme on policyholders, including whether the Scheme will result in material detriment to any policyholders affected by the Scheme, relative to their current situation. The purpose of this report is to set out my considerations. For the purposes of this report, policyholders include existing and future claimants.
- 3.2 Material detriment in the context of this report means any material adverse effect on:
 - The security of policyholders' contractual rights
 - The levels of service provided to policyholders.
- 3.3 For the purposes of this report, a material adverse effect is defined as a negative change that is considered to have a material impact on policyholders. A material impact is one that could cause a policyholder to take a different view on the future performance of their policy. When considering policyholder security these would include changes to the assets and liabilities of the company such that there was a shift in the probability of a policyholders' claim being paid substantially larger than that which would be observed through the day-to-day fluctuation of the value of assets in the company's investment portfolio, or from the day-to-day reporting of claims. In terms of non-financial impacts, an assessment of materiality is more subjective, but as an example a change in claims handling process that added a few hours to the customer response time is probably not material, but if it added a few days then it could be, depending on the type of claim.
- 3.4 My report considers the effect on the following groups of policyholders:
 - The policyholders within the Transferring Portfolio
 - The policyholders remaining within QBEUK following the Scheme
 - The existing policyholders of EWICL
- 3.5 Shortly before the date of the Court hearing at which an order sanctioning the Scheme will be sought, I will prepare a Supplementary Report covering any relevant matters which might have arisen since the date of this report.
- 3.6 I have not considered the impact of the Scheme on any policyholders that subsequently effect policies with either QBEUK or EWICL.
- 3.7 I have considered the impact of the Scheme on any reinsurers that will continue to provide protection to the Transferring Portfolio. A material adverse impact on a reinsurer is one that could cause the reinsurer to take a different view on the future performance of the reinsurance policy they have written. A hypothetical example could be that the Scheme gives rise to a non-trivial additional exposure for the reinsurer.
- 3.8 I am not aware of any alternative scheme or proposal. In addition, I understand from QBEUK that, with respect to the Autumn Portfolio, there are specific policies remaining in QBEUK. These policies are not being transferred as QBEUK has ongoing relationships with the corresponding policyholders. Consequently, I have not considered it necessary to discuss alternative proposals within this report.

Future changes of ownership

- 3.9 I have not considered any future changes of ownership in either QBEUK or EWICL. I am not aware of any proposals to change ownership at the time of writing this report.

Exchange rates

- 3.10 The figures used throughout this report are shown in Sterling. All of the information provided to me by QBEUK has been presented in Sterling. Some of the information provided to me by EWICL has been provided to me in US Dollars and converted to Sterling using the following exchange rate as at 31 December 2018, which was provided by EWICL:

- £1 = \$1.2760

Reliance on data

- 3.11 I have not audited, nor have I independently verified the data and information supplied to me. However, I have reviewed it for reasonableness and for internal consistency.
- 3.12 A summary of the data provided to me can be found in Appendix A.
- 3.13 I have checked that all of the information I have been provided with has been supplied by persons appropriately qualified to provide such information and I am satisfied that it is reasonable for me to rely on this information.
- 3.14 I have been provided with all the information that I have requested.

Peer review process

- 3.15 In accordance with the Institute of Actuaries Guidance APS X2 on the Review of Actuarial Work and the internal control process of Grant Thornton, the work documented in this report has been peer reviewed by a suitably qualified person (an Actuary within my firm who has considerable experience in capital modelling and reserving in the general insurance market). The peer review process has included a review of the methodology and key assumptions used and discussion of the key elements of the analysis.

4 Methodology

- 4.1 In this section, I describe my approach to assessing the Scheme.
- 4.2 My conclusions have been drawn by undertaking the following activities:
- Review of documentation received from QBEUK and EWICL
 - Discussions with key personnel at both QBEUK and EWICL
 - Undertaking my own analysis, where necessary.
- 4.3 In particular:
- My view on the insurance liabilities of the Transferring Portfolio is based upon my review of the calculations and documentation provided to me by QBEUK and EWICL, and discussions with the relevant individuals at QBEUK and EWICL. In addition, I have undertaken my own high-level analysis to determine my view of the insurance liabilities in respect of the Transferring Portfolio.
 - My view on the insurance liabilities of QBEUK is based upon my review of documentation provided to me by QBEUK, and discussions with the relevant individuals at QBEUK.
 - My view on the insurance liabilities of EWICL is based upon my review of documentation provided to me by EWICL, and discussions with the relevant individuals at EWICL.
 - My view on the capital requirements and assessments of QBEUK is based upon my review of the calculations and documentation provided to me by QBEUK, and discussions with the relevant individuals at QBEUK.
 - My view on the capital requirements and assessments of EWICL is based upon my review of the calculations and documentation provided to me by EWICL, and discussions with the relevant individuals at EWICL. In addition, I have undertaken my own high-level analysis to assess the capital requirements of EWICL following the Scheme using my view of the insurance liabilities in respect of the Transferring Portfolio.
- 4.4 My approach to assessing the Scheme has been to perform the following specific activities:
- Understand the nature and structure of the Scheme and identify the groups of policyholders that will be affected
 - Assess the financial positions of QBEUK and EWICL
 - Consider the implications of the Scheme for the level of security, including under insolvency, being offered to each group of policyholders
 - Consider the potential impact on levels of customer service
 - Consider other factors that might affect policyholders
 - Consider the implications of the Scheme for reinsures.
- I provide additional details for each of the activities listed above in the remainder of this section.
- Understand the nature and structure of the Scheme and identify the groups of policyholders that would be affected**
- 4.5 I have discussed the nature and the structure of the Scheme with QBEUK and EWICL and reviewed the documentation I have received.

Assess the financial positions of QBEUK and EWICL

- 4.6 The level of security provided to policyholders of an insurance company depends on the available capital of the company and, in particular, the probability that this level of capital is sufficient to make claim payments as they fall due.
- 4.7 Insurers are subject to capital requirements imposed by regulators, the PRA in the case of QBEUK and EWICL. These capital requirements are discussed in more details in paragraphs 6.9 to 6.12. The level of available capital compared to regulatory capital requirements is a measure of the security provided to the policyholders.
- 4.8 Insurers are also required to undertake an assessment of their own risks and solvency needs. Another measure of the security provided to policyholders is the level of available capital compared to the insurer's view of required capital.
- 4.9 I have considered the balance sheets of QBEUK and EWICL, on a regulatory basis, as part of my assessment of their relative financial strengths, including the net assets and level of capital.
- 4.10 I have compared the balance sheets of QBEUK and EWICL prior to the Scheme with those following the Scheme based on data as at 31 December 2018, being the most recent date at which financial information was available. This is discussed in Section 8.
- 4.11 As discussed in paragraph 1.6, the QBEUK Brexit Transfer became effective on 1 January 2019. As a result, all of QBEUK's financial information as at 31 December 2018 has been prepared and reported prior to the QBEUK Brexit Transfer. For simplicity purposes for this report, I have requested QBEUK to prepare indicative financial and capital information as at 31 December 2018 on the basis that the QBEUK Brexit Transfer had become effective at that date.
- 4.12 I have discussed with QBEUK its approach to producing this indicative information and I am satisfied that it has taken appropriate steps to ensure that this information provides a reasonable view of the financial position of QBEUK as at 31 December 2018 had the QBEUK Brexit Transfer taken place.

Assess the claims reserve of QBEUK and EWICL

- 4.13 An important part of the security provided to policyholders is the strength of the claims reserves – the amount of money the insurer puts aside to pay out on future claims in respect of policies already sold. The claims reserves generally form the largest part of the liabilities for an insurer.
- 4.14 I have therefore considered the claims reserves included on the balance sheet for each of QBEUK and EWICL. This is discussed in Section 7.

Assess the capital modelling undertaken and the capital positions of QBEUK and EWICL

- 4.15 To further review the financial strength of QBEUK and EWICL, I have reviewed the modelling undertaken to assess the required regulatory capital.
- 4.16 In addition, I have undertaken my own testing to understand the robustness of the capital bases of QBEUK and EWICL to various stresses.
- 4.17 These reviews are discussed further in Section 8.

Consider the implications of the Scheme for the level of security, including under insolvency, being offered to each group of policyholders

4.18 I have considered each group of policyholders both before and after the Scheme and the relative level of security available to them, including under insolvency. This is discussed further in Section 9.

Consider the potential impact on levels of customer service

4.19 I have considered how the level of customer service, specifically claims handling and policy servicing, experienced by each group of policyholders could change following the Scheme. This is discussed in paragraphs 11.3 to 11.12.

Consider other financial factors that might affect policyholders

4.20 Through my discussions with QBEUK and EWICL and reviews of documentation, I have also considered various other financial factors that might affect policyholders, including the following:

- Investment strategy
- Implications of the Scheme on ongoing expense levels
- Liquidity position
- Tax implications.

4.21 These issues are discussed in Section 10 of this report.

Consider other non-financial factors that might affect policyholders

4.22 Through my discussions with QBEUK and EWICL and reviews of documentation, I have also considered various other non-financial factors that might affect policyholders, including the following:

- ‘Brexit’
- Governance and management frameworks
- Should the Scheme not become effective
- Policyholder notifications
- Reinsurer notifications.

4.23 These issues are discussed in Section 11 of this report.

Consider the implications of the Scheme for reinsurers

4.24 I have considered the implications of the Scheme on any reinsurers transferring. This is discussed in paragraphs 10.15 and 10.16.

5 Background

Purpose of the Scheme

- 5.1 The purpose of the Scheme is to transfer the legal obligations relating to the Transferring Portfolio from QBEUK to EWICL. The purpose of the LPTAs and the resulting Scheme from QBEUK's perspective is to dispose of a non-core legacy portfolio. I understand from EWICL that it intends to fulfil its contractual obligations in an orderly run-off and, in the process, hopes to make a saving on the current reserves.

Background to QBEUK

- 5.2 QBEUK was established in 1983 under the name Legibus 373 Limited. It has since undergone several name changes. The most recent change, from QBE Insurance (Europe) Limited to QBEUK became effective from 1 January 2019, at the same time as the QBEUK Brexit Transfer.
- 5.3 QBEUK is a non-life insurance and reinsurance company domiciled in the UK which has been authorised by the PRA and is regulated by the FCA and the PRA.
- 5.4 QBEUK is a wholly-owned subsidiary of QBE Holdings (EO) Limited ("QBE Holdings EO"), which in turn is a wholly-owned subsidiary of QBE European Operations plc ("QBE EO"). Under Solvency II, QBE EO is an insurance holding company and subject to group supervision by the PRA. QBE EO is wholly owned by QBE Insurance Group Limited ("QBE Limited"), the ultimate parent company for the QBE Group. QBE Limited is domiciled in Australia and listed on the Australian Securities Exchange. It is one of the twenty largest non-life insurance and reinsurance companies in the world and is subject to prudential supervision by the Australian Prudential Regulation Authority.
- 5.5 QBEUK transferred a portfolio of business to a newly created entity in Belgium, QBE Europe SA/NV, as part of its preparations for Brexit. This transfer was initiated by QBE EO in response to the uncertainty created by Brexit in relation to the continuation of writing and servicing policies for policyholders based in the European Economic Area ("EEA") following the UK's departure from the European Union. The aim of the transfer was to create two entities. The first of these was QBEUK which would continue to underwrite business domiciled in the UK and outside of the EEA ("Non-EEA"). The second of these was QBE Europe SA/NV which would underwrite all the business domiciled in the EEA. This transfer was effective 1 January 2019.
- 5.6 QBEUK currently underwrites a range of products including:
- Accident and health
 - Commercial property
 - Credit and bond
 - Energy
 - Engineering
 - Liability
 - Marine
 - Motor
 - Terrorism and political risk
 - Inwards reinsurance.

- 5.7 QBEUK writes business in the EEA and Non-EEA through its branch located in Dubai. QBEUK (under its previous name) previously had branches in Romania and Switzerland. The branch in Switzerland is in run-off. I have been informed by QBEUK that the branch in Romania has run-off, has been deregistered with the Romanian regulator and is expected to be dissolved during the second half of 2019.
- 5.8 The table below shows a breakdown of QBEUK's business, based on gross written premiums between 1 January 2019 and 30 June 2019.

Table 5.1: Breakdown of QBEUK's business by class of business

Class of business	Percentage of business
Accident and health	0.3%
Commercial property	13.1%
Credit and bond	4.8%
Energy	3.0%
Engineering	1.7%
Liability	27.5%
Marine	1.1%
Motor	37.0%
Terrorism and Political Risk	0.1%
Reinsurance acceptances	11.5%

The Transferring Portfolio

- 5.9 QBEUK has decided to sell two portfolios, the Autumn and Chestnut portfolios, and has agreed to transfer the liabilities in these two portfolios to EWICL under the provisions of FSMA.

Autumn Portfolio

- 5.10 The Autumn Portfolio consists of UK and Republic of Ireland employers' liability and public liability business, including all associated policies attaching to binders, which had incepted on or prior to 31 December 2007, aside from certain policies which are set out in the Autumn LPTA and will be retained by QBEUK. Those policies retained by QBEUK did not form part of what was reinsured as a result of the Autumn LPTA and were never intended to form part of the Scheme, and are defined as the "Retained Autumn Policies" in the Scheme. These policies were retained as QBEUK has ongoing relationships with the corresponding policyholders. I understand from QBEUK that the Retained Autumn Policies contain around 100 policyholders.
- 5.11 The policies included in the Autumn Portfolio have been in run-off since 31 December 2007 and as a result, the substantial majority of the claims remaining in the Autumn Portfolio relate to mesothelioma, other asbestos related diseases and other disease.
- 5.12 The Autumn Portfolio also includes exposures relating to Electricity Industry Run-Off Services ("EIROS") which, until 2005, was known as the Associated Insurers (British Electric) Management Committee. EIROS was a market wide scheme established to meet the insurance needs of the then newly nationalised electricity industry in the UK including the main electricity generators. EIROS provided employers' liability and public liability insurance from 1949 until it effectively closed to new business in 1977.

5.13 Approximately 1.6m policies were written within the Autumn Portfolio and there are approximately 720,000 policyholders. All of the policies have now expired although claims can continue to be reported. There were 3,036 outstanding claims with a total value of £19.1m as at 31 December 2018.

Chestnut Portfolio

- 5.14 The Chestnut Portfolio consists of the following (subject to certain liabilities remaining with QBEUK):
- UK employers' liability policies issued by QIEL for TSEL from 1 January 1990 and expiring on or before 31 March 2016
 - Global public and products liability, UK motor and UK personal accident issued by QIEL for TSEL expiring on or before 31 March 2016
- 5.15 Liabilities not included in the Chestnut Portfolio (defined as the "Retained Chestnut Liabilities" in the Scheme) are:
- Any claim under the original policies issued by QIEL for TSEL relating to liabilities assumed by British Steel Limited ("British Steel"), or any predecessor entity or business of British Steel, pursuant to certain agreements affecting the transfer of the relevant undertaking from TSEL to British Steel
 - Any claims under the original policies issued by QIEL for TSEL relating to liabilities of Specialty Steel UK Limited ("Specialty Steel"), or any predecessor entity or business of Specialty Steel
 - Noise induced hearing loss/ deafness liabilities whereby the deafness is either caused or alleged to be caused over a period of time longer than one day. This means that The Chestnut Portfolio includes any claim for deafness or any similar hearing impairment that is caused or alleged to be caused by either a single exposure to sound pressure or other acute acoustic trauma occurring over a period of time of one day or less
- 5.16 Since there are certain policies issued by QIEL for TSEL that cover British Steel and/or Specialty Steel, these policies will need to be split in order to extract the Transferring Portfolio (the "Split Policies").
- 5.17 48 policies were written within the Chestnut Portfolio. There were 184 outstanding claims with a total value of £7.9m as at 31 December 2018. All of the policies have expired although claims can continue to be reported.

Reinsurance

- 5.18 In addition to the LPTAs, the Transferring Portfolio currently benefits from excess of loss reinsurance contracts that cover both the Transferring Portfolio and parts of the Remaining Portfolio. There are a number of contracts in place over the period that the policies were written with levels of coverage varying between the contracts. QBEUK does not expect any claims to generate recoveries against this reinsurance. I understand from QBEUK and EWICL that this reinsurance will continue to cover the transferring policyholders following the Scheme. I further understand from QBEUK and EWICL that this reinsurance will be shared between the Transferring Portfolio and the parts of the Remaining Portfolio that it currently covers.
- 5.19 The excess of loss reinsurance is the only reinsurance protection that will remain in place in respect of the Transferring Portfolio should the Scheme become effective.

Background to EWICL

- 5.20 EWICL is a UK non-life insurance company which has been authorised by the PRA and is regulated by the FCA and the PRA. It was originally set up as National & General Insurance Company (United Kingdom) Limited in 1964. Its name changed to EWICL in 1984.
- 5.21 EWICL is a 98.9% subsidiary of a cell of ILS. The remaining 1.1% share capital is held amongst a number of minority shareholders domiciled in Malaysia, Singapore, Hong Kong and the USA.
- 5.22 EWICL is primarily comprised of two portfolios: legacy business underwritten prior to and including 1997 ("the Legacy Portfolio"); and a UK building guarantee portfolio transferred in 2018 ("the UKBG Portfolio"). The Legacy Portfolio is described in paragraphs 5.23 to 5.26. The UKBG Portfolio is described in paragraphs 5.27 to 5.30.

The Legacy Portfolio

- 5.23 EWICL commenced underwriting general insurance business in 1964 and underwrote business through different distribution channels, namely:
- direct retail motor and household business written out of local UK branches in Gloucester, Leicester and Redhill until it formally ceased underwriting in 1997
 - participation in the English & American Underwriting Agency ("EAUA") which has since been closed through a Scheme of Arrangement
 - participation in London Market reinsurance ("LMX") business writing alongside Charter Re up until the 1992 underwriting year
 - direct commercial general insurance written through UK insurance brokers including employers' liability covering shops; offices; and light commercial and industrial risks from 1985 to 1993.
- 5.24 There are currently no open motor or household claims.
- 5.25 The remaining risks and liabilities were significantly reduced following the completion of a Scheme of Arrangement in September 2013 which closed all of the London Market business associated with EAUA.
- 5.26 EWICL's London Market business is showing little development and no new claims have been reported in recent years. There remain 57 outstanding claims resulting from 12 cedants, mostly marine and aviation reinsurance in nature. The last claim movement on any of these claims was in May 2015.

The UKBG Portfolio

- 5.27 On 31 March 2018, a run-off portfolio of UK Building Guarantee liabilities was transferred from Zurich Insurance Plc ("ZIP") to EWICL by means of a Section 13 Transfer. The portfolio was underwritten by ZIP between 1993 and 2009, with policies in respect of existing contracts continuing to inception until the final quarter of 2012.
- 5.28 This portfolio consists of predominantly ten and twelve year structural warranty policies. For some policies with registration years of 2005 and prior, there is an option to extend the ten year policies to cover a 15 year period. The policies were issued to home-buyers who bought houses/flats from builders registered with ZIP, and its predecessor companies in title.

- 5.29 The policies cover losses arising from the defective construction of the properties with three distinctive cover periods:
- Loss of Deposits ("LOD"): In the period from the issue of the initial building certificate to the issue of the final building certificate, cover is provided for the buyer's lost deposit as a result of the developer's bankruptcy, liquidation or fraud. This cover is generally up to a maximum of 10% of the purchase price, although there are a minority of contracts which provide cover up to a maximum of 20% of the purchase price.
 - Developers Guarantee Period ("DGP"): For the first two years after the latter of the issue of the final building certificate or exchange of contracts, the builder is liable to pay for remedial work to the property should there be any problems. Insurance cover is provided during this period should the builder fail to honour its obligations. Housing Associations do not have a DGP period and move straight into the following period.
 - Structural Indemnity Period ("SIP"): In most cases, this period is the eight years following the DGP. Cover is provided to pay for remedial work to the property due to a latent defect, subject to an excess. Extended policies have an additional five years of SIP cover. Housing Associations go straight into the SIP period and have 12 years of SIP cover.
- 5.30 I understand from EWICL that approximately 387,000 policies were written within this portfolio. As at 31 December 2018, there were 204 outstanding claims, totalling £13.5m. In addition, as at the end of December 2018, there were 37,916 policies open in respect of SIP. As at the end of December 2018, there were no open policies in respect of either LOD or DGP. Claims can only be reported under these policies whilst the coverage is in place. As a result, EWICL will know about all claims by 8 December 2026, when the final policy period finishes. No claims can be reported in the future in respect of LOD or DGP, only in respect of SIP.

ILS

- 5.31 ILS is a segregated accounts insurance company based in Bermuda. Under this structure it operates a number of cells, where the assets of a cell can only be used to meet the liabilities of that cell. ILS is ultimately owned by an investment fund ILS Property & Casualty Master Fund Ltd. based in the Cayman Islands.
- 5.32 As discussed in paragraph 5.21, EWICL is a 98.9% owned subsidiary of a cell of ILS.
- 5.33 As part of the transaction, two Loss Portfolio Transfer Agreements ("LPTAs") have been put in place between QBEUK and another cell of ILS, Cell G. Further details of the LPTAs are provided in paragraphs 5.41 to 5.59.
- 5.34 As part of the Scheme, funds from Cell G, currently contained in the segregated accounts discussed in paragraphs 5.46 to 5.48 and 5.55 to 5.56, will be transferred to EWICL as the liabilities relating to the Transferring Portfolio will be transferred to EWICL. The amount transferred will be in line with the figures in Table 8.5.

ILS Investment Management Limited

- 5.35 ILS Investment Management Limited ("ILSIM") provides administration to the fund which owns ILS. ILSIM has controlling rights over ILS. ILSIM is a wholly owned subsidiary of Armour Group Limited ("Armour").
- 5.36 Subject to regulatory approval, Armour will become part of the Aquiline Capital Partners ("Aquiline") group. Armour will be 80.6% owned by Aquiline and 19.4% owned by Trebuchet Group Holdings Limited (formerly Armour Group Holdings Limited).

Armour Risk Management Limited

- 5.37 Armour Risk Management Limited ("ARML"), a wholly owned subsidiary of Armour Risk Services (Bermuda) Limited which in turn is a wholly owned subsidiary of Armour, provides the following functions to ILS:
- Insurance services including claims
 - Risk and compliance
 - Finance
 - Actuarial
 - Operations including information technology.
- 5.38 Under the terms of the outsourcing agreement ("the Services Agreement"), ARML has provided claims handling and administration services for the Transferring Portfolio since 30 June 2016 and will continue to do so following the Scheme becoming effective.
- 5.39 Should the Scheme become effective, ARML will continue to provide services for the Transferring Portfolio through the support it provides to ILS described in paragraph 5.37.

Reinsurance

- 5.40 EWICL does not utilise outwards reinsurance to mitigate risk in relation to its existing business. However, following the Scheme the Transferring Portfolio would continue to benefit from the excess of loss reinsurance that it currently benefits from as described in paragraph 5.18. Following the Scheme, the Existing EWICL Portfolio will not benefit from any reinsurance.

Overview of LPTAs

Overview of the Autumn LPTA and the Retrocession Agreement

- 5.41 On 30 June 2016, QBEUK entered into the Autumn LPTA with TMR and ILS. This agreement provides:
- TMR will provide 100% quota share reinsurance to QBEUK in respect of the Autumn Portfolio up to an aggregate limit of an amount equal to 155% of the reserves (the "Autumn LPTA Aggregate Limit"), as defined in the agreement.
 - Cell G of ILS will provide 100% quota share reinsurance in respect of the Autumn Portfolio in excess of the Aggregate Limit, as defined in the agreement.
- 5.42 TMR subsequently entered into a reinsurance agreement with ILS, whereby Cell G of ILS has agreed to provide 100% reinsurance of the Autumn Portfolio to TMR ("the Retrocession Agreement").
- 5.43 As a result of the agreements described in paragraph 5.41 and 5.42, ILS provides 100% reinsurance of the Autumn Portfolio.
- 5.44 Should the Scheme become effective, the Autumn LPTA will be terminated and ILS and TMR will no longer provide reinsurance in respect of the Autumn Portfolio.

Administration under the Autumn LPTA

5.45 Under the terms of the LPTA and Services Agreement, ARML is responsible for managing the claims and the administration of the Autumn Portfolio. There are provisions within the Autumn LPTA should the Services Agreement between QBEUK and ARML terminate. Under these provisions, QBEUK will itself carry out or appoint a replacement provider to perform the administration, management and claims handling in respect of the Autumn Portfolio on terms no less favourable to TMR and ILS than those that currently exist.

Segregated accounts

- 5.46 An account has been created from which claim payments relating to the Autumn Portfolio will be made. This account (the "Autumn Claims Float Account") is operated by ARML and maintained at a minimum level by TMR and ILS.
- 5.47 As part of the Autumn LPTA, QBEUK placed the majority of the premium into a segregated account established by ILS ("the Designated Bank Account"), in the name of Cell G. The Designated Bank Account serves as collateral for the Retrocession Agreement.
- 5.48 As part of the Retrocession Agreement, ILS placed the initial deposit and premium for the agreement into an account (the "Trust Account"). ILS is responsible for maintaining, at all times, sufficient assets in the Trust Account in order to meet a minimum required level of collateral, as defined in the agreement.

Termination rights

- 5.49 QBEUK has the option to terminate the LPTA in the following circumstances:
- An insolvency occurs in relation to TMR or ILS
 - Either TMR or ILS suspends or ceases (or threatens to suspend or cease) to carry out all or a substantial part of its business, or ceases to be authorised by applicable law or regulation to carry out its obligations under the LPTA
 - The performance by either TMR or ILS of the whole or any part of the LPTA is prohibited or rendered impossible
 - Either TMR or ILS materially fails to comply with any terms and conditions of the LPTA where the failure is not capable of remedy or not rectified to the satisfaction of QBEUK within 30 days of receiving notice
 - Termination of the LPTA is required by either regulation or a relevant regulatory authority.
- 5.50 Should the Scheme not become effective, neither TMR nor ILS are entitled to terminate the LPTA.
- 5.51 The Retrocession Agreement shall remain in effect as long as TMR has any obligations or liabilities arising under the Autumn LPTA.

Overview of the Chestnut LPTA

- 5.52 On 29 August 2017, QBEUK entered into the Chestnut LPTA with ILS. This agreement provides 100% quota share reinsurance to QBEUK in respect of the Chestnut Portfolio up to an aggregate limit of £29m. Furthermore, the maximum amount recoverable at any time from ILS in respect of any one loss or cause is limited to £1m.
- 5.53 Should the Scheme become effective, the Chestnut LPTA will be terminated and ILS will no longer provide reinsurance in respect of the Chestnut Portfolio.

Administration under the Chestnut LPTA

5.54 Under the terms of the Chestnut LPTA and Services Agreement, ARML is responsible for managing the claims and the administration of the Chestnut Portfolio. There are provisions within the LPTA should the agreement between QBEUK and ARML terminate. Under these provisions, QBEUK will itself carry out or appoint a replacement provider to perform the administration, management and claims handling in respect of the Chestnut Portfolio on terms no less favourable to ILS than those that currently exist.

Segregated accounts

5.55 Accounts have been created from which claim payments relating to the Chestnut Portfolio will be made. These accounts (the "Chestnut Claims Float Accounts") are operated by ARML and maintained at a minimum level by ILS.

5.56 As part of the Chestnut LPTA, QBEUK paid the premium into accounts established by ILS (the "Collateral Accounts"). These accounts refer to accounts holding cash and securities. The Collateral Accounts serve as collateral for the Chestnut LPTA. ILS and QBEUK agree an investment manager to operate the Collateral Accounts in accordance with investment guidelines agreed by both QBEUK and ILS.

Termination rights

5.57 QBEUK has the option to terminate the LPTA in the following circumstances:

- ILS becomes insolvent
- ILS suspends or ceases (or threatens to suspend or cease) to carry out all or a substantial part of its business, or ceases to be authorised by applicable law or regulation to carry out its obligations under the LPTA
- The performance by ILS of the whole or any part of the LPTA is prohibited or rendered impossible
- ILS materially fails to comply with any terms and conditions of the LPTA where the failure is not capable of remedy or not rectified to the satisfaction of QBEUK within 30 days of receiving notice
- Termination of the LPTA is required by regulation or a relevant regulatory authority
- An amount is transferred out of the Collateral Accounts otherwise than is permitted as per the LPTA and the amount has not been repaid to the Collateral Accounts.

5.58 Should the Scheme not become effective ILS is not entitled to terminate the LPTA.

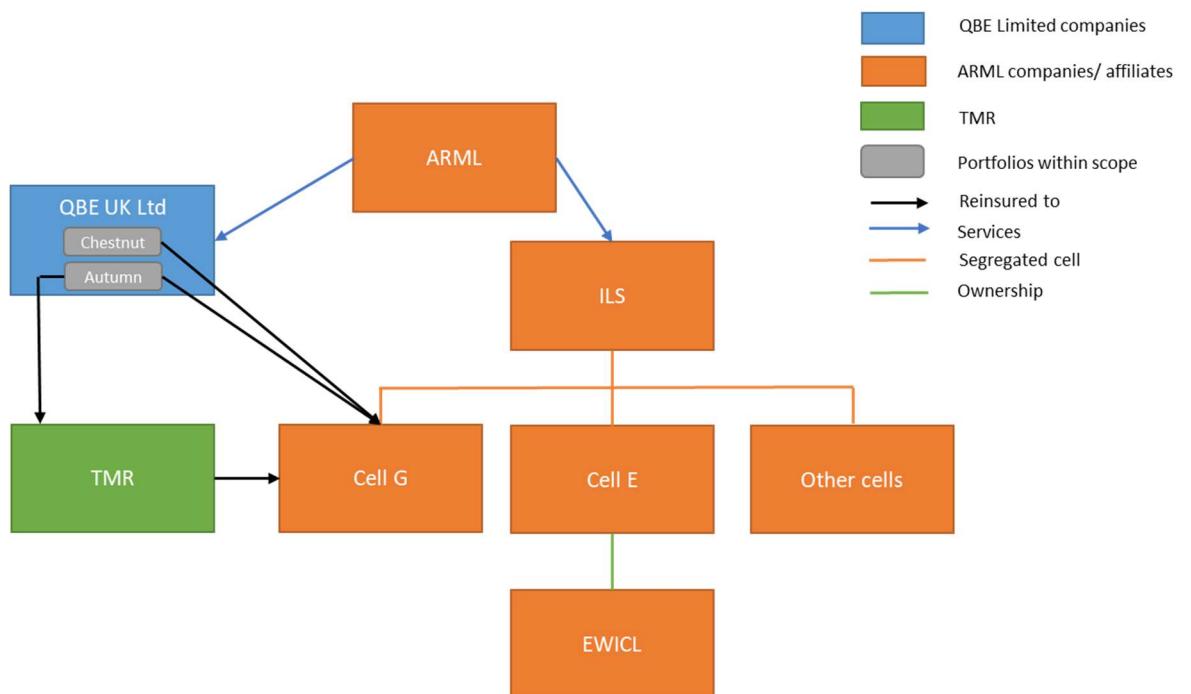
5.59 Should the Scheme become effective but not all policies are transferred, ILS is not entitled to terminate the LPTA.

Overview of structure

Overview of structure prior to the Scheme

- 5.60 The diagram below illustrates the structure of the businesses prior to the Scheme.

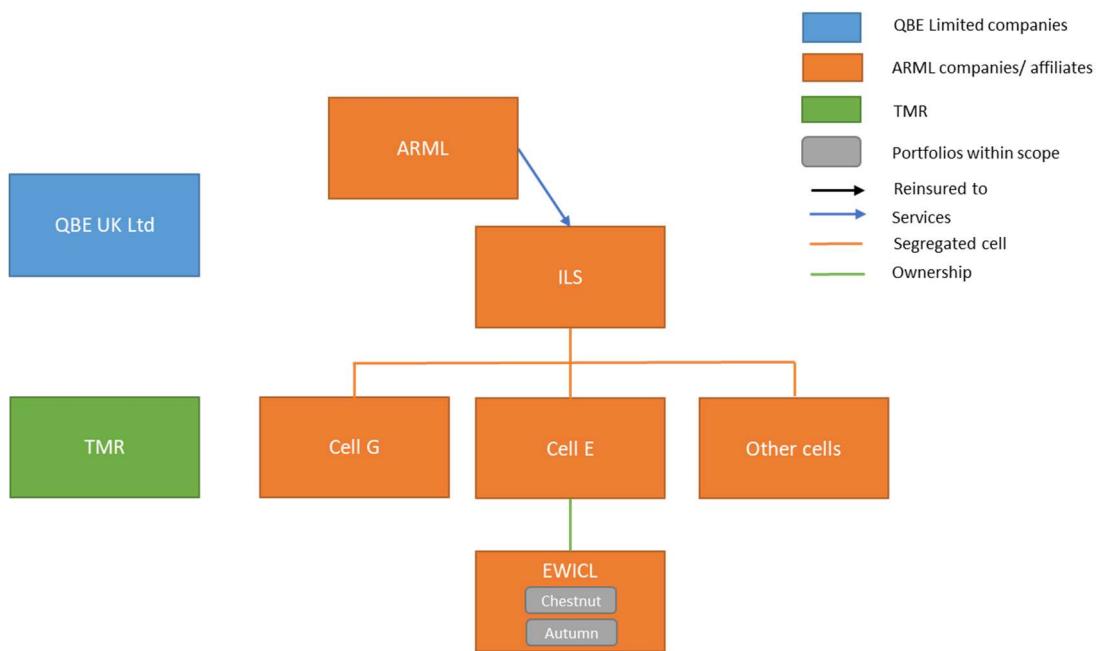
Figure 1: Simplified structure of businesses prior to the Scheme (showing main entities only)



Overview of structure following the Scheme

- 5.61 The diagram below illustrates the proposed structure of the businesses following the Scheme.

Figure 2: Simplified structure of businesses following the Scheme (showing main entities only)



Summary of the Scheme

- 5.62 The policies that are expected to transfer as a result of the Scheme are those in the Transferring Portfolio, namely the combination of the Autumn Portfolio and the Chestnut Portfolio. Following the Scheme, EWICL will become responsible for the liabilities in respect of those policies.
- 5.63 As part of the LPTAs, QBEUK transferred cash and securities to the segregated accounts discussed in paragraphs 5.46 to 5.48 and 5.55 to 5.56. The amount of those assets that will be transferred to EWICL under the Scheme will be in line with the figures in Table 8.5.
- 5.64 As discussed in paragraph 5.18, an excess of loss reinsurance programme that provides coverage in the respect of the Transferring Portfolio at present will continue to provide protection following the Scheme.
- 5.65 As is standard with most Schemes, there is a provision for certain liabilities and assets that may not be, or may not be capable of being, transferred on the Effective Date. These are defined as "Residual Assets" and "Residual Liabilities" within the Scheme document. I understand from QBEUK and EWICL that no Residual Assets and Residual Liabilities have been identified at this stage. The Scheme also provides a provision for QBEUK and EWICL to seek to transfer these policies at a later date (the "Subsequent Transfer Date").
- 5.66 The Retained Autumn Policies and the Retained Chestnut Liabilities will remain with QBEUK and will not transfer as part of the Scheme, either at the Effective Date or at a Subsequent Effective Date.

6 Regulatory background

- 6.1 In this section, I provide some background on the regulatory requirements in the UK. As discussed in paragraph 14.9, the opinions contained in this report are based on my own analysis and not based on regulators' views of the companies involved.
- 6.2 This section is structured as follows:
 - Paragraphs 6.3 to 6.6 discuss the impact of the EU referendum in the UK
 - Paragraphs 6.7 to 6.16 discuss the prudential regime that applies to all European insurers
 - Paragraphs 6.17 to 6.33 discuss the regulatory environment for insurers authorised in the UK.

Impact of EU referendum ('Brexit')

- 6.3 On 23 June 2016, the UK voted to leave the EU. On 29 March 2017, the UK officially notified the European Commission of its intention to withdraw from the EU. At this stage, it is unclear what will happen as a result of this vote. What is clear is that both QBEUK and EWICL are currently subject to the same regulatory regime, Solvency II. Solvency II is likely to continue to be the regulatory regime in the UK at least until the UK leaves the EU. At the time of writing this report, this is expected to be by 31 October 2019, although it may be sooner.
- 6.4 The developments in the regulatory regime in the UK will ultimately be determined by the PRA, the FCA and UK lawmakers. However, what will happen and when it may happen are not yet known.
- 6.5 This issue is discussed further in paragraphs 11.19 and 11.31.
- 6.6 I have written the sections below, on the prudential regime and regulatory environment within the UK, as they stand prior to any developments as a result of Brexit.

Solvency II

- 6.7 In 2016, insurance regulation in Europe underwent a major overhaul. Since 1 January 2016, all EU insurers have been required to meet a common set of requirements developed by the European Commission ("Solvency II").
- 6.8 Solvency II is a principles-based regime set around three pillars:
 - Pillar 1 – quantitative requirements
 - Pillar 2 – qualitative requirements
 - Pillar 3 – reporting and disclosure requirements.
- 6.9 Under Solvency II, there are two sets of capital requirements to allow for different levels of supervisory intervention.
- 6.10 The usually higher of these two is the Solvency Capital Requirement ("SCR"). This is the amount of capital required in excess of liabilities in order to ensure continued solvency over a one year time frame in 99.5% of cases.

- 6.11 The SCR can be calculated using one of four approaches; the Standard Formula, the Standard Formula with undertaking specific parameters, an Internal Model, or a Partial Internal Model:
- the Standard Formula approach uses a prescribed set of formulae and parameters in order to work out the SCR
 - within the Standard Formula framework, entities are able to use undertaking specific parameters ("USPs") in order to refine certain parameters, subject to regulatory approval
 - the Internal Model approach involves the entity using its own capital model to calculate the SCR. The model requires regulatory approval
 - the Partial Internal Model approach is a combination of the first, second and third approaches. An approved Internal Model is used to calculate parts of the SCR and the Standard Formula is used to calculate the remaining parts of the SCR.
- 6.12 The Minimum Capital Requirement ("MCR") defines the point of severe supervisory intervention.
- 6.13 I have been provided with details of the approaches taken to calculating the SCR and MCR by both QBEUK and EWICL.
- 6.14 Further to calculating the SCR, insurers are required to calculate the level of capital ("Own Funds") available to meet the SCR. This requires the calculation of a balance sheet according to Solvency II requirements. The Own Funds are then assessed and allocated into tiers depending on their eligibility to meet the SCR.
- 6.15 It is important to note that even if an insurer does not have sufficient Own Funds to meet its SCR, then this does not necessarily mean that it would not be able to settle all of its claims in full.
- 6.16 An additional requirement for Solvency II is that each year, every insurer must undertake an Own Risk and Solvency Assessment ("ORSA"). This sets out its current and future risk profile and the expected level of capital it will require over the next three to five years.

UK

Overview of regulation

- 6.17 UK insurers are regulated by both the PRA and FCA. The PRA and FCA are statutory bodies set up under the Financial Services Act 2012. Prior to 1 April 2013, all regulation of financial services institutions was undertaken by the Financial Services Authority ("FSA"). All regulatory responsibility was transferred from the FSA to the PRA and/or FCA on 1 April 2013.
- 6.18 The PRA is part of the Bank of England and is responsible for prudential regulation of:
- banks
 - building societies
 - credit unions
 - insurance companies
 - major investment firms.

6.19 Its three statutory objectives, as applicable to insurance companies, are:

- to promote the safety and soundness of the firms which it regulates
- to contribute to the securing of an appropriate degree of protection for insurance policyholders
- to facilitate effective competition.

The third objective above is secondary to the first two.

6.20 The FCA is a separate organisation and its strategic objective is to ensure that the relevant markets function well.

6.21 To support this, it has three operational objectives:

- to secure an appropriate degree of protection for consumers
- to protect and enhance the integrity of the UK financial system
- to promote effective competition in the interests of consumers.

Current capital requirements

6.22 Since 1 January 2016, most insurance companies in the UK are required to maintain capital in line with the Solvency II requirements as discussed in paragraphs 6.9 to 6.12.

Capital extraction

6.23 Insurers that are not in run-off are able to extract capital from the business without the PRA's prior approval. However the PRA expects insurers to maintain an adequate level of capital above the SCR.

6.24 In relation to proposed capital extractions from firms in run-off, the PRA expects firms to request its views at an early stage and ensure that any concerns it may have are properly addressed before the proposal is implemented.

FCA conduct principles

6.25 The FCA has set out its Principles for Businesses, the general statements of the fundamental obligations of firms under its regulatory system. These principles include the following that relate to the fair treatment of customers:

- Principle 6: A firm must pay due regard to the interests of its customers and treat them fairly
- Principle 7: A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading
- Principle 8: A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client
- Principle 9: A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely on its judgement.

Security under wind up

6.26 The winding up of an insurance undertaking is governed by the Insurers (Reorganisation and Winding Up) Regulations 2004 in the UK. Under these regulations, insurance claims take precedence over other claims on the insurance undertaking with the exception of certain preferential claims (e.g. claims by employees, rights in rem etc). Therefore, direct policyholders rank equally and above inwards reinsurance policyholders and all other unsecured/non preferential creditors in the event that an insurer is wound up.

Financial Services Compensation Scheme

- 6.27 The Financial Services Compensation Scheme ("FSCS") is the compensation fund of last resort for customers of authorised financial services firms.
- 6.28 Most private policyholders, small businesses and charities are eligible for protection from the FSCS, in the event that an insurer is unable to meet its liabilities.
- 6.29 The FSCS will pay 100% of any claim incurred for compulsory insurance (eg motor third party liability insurance) and 90% of the claim incurred for non-compulsory insurance without any limit on the amount payable. The FSCS is funded by levies on firms authorised by the PRA. No protection is available for Goods in Transit, Marine, Aviation and Credit Insurance and contracts of reinsurance are also not protected.
- 6.30 The impact of the Scheme on the level of compensation available to the transferring policyholders is discussed in paragraph 9.14.

Financial Ombudsman Service

- 6.31 The Financial Ombudsman Service ("FOS") was set up as an independent public body. Its job is to resolve individual disputes between consumers and financial services businesses. In order to access FOS, it is necessary for the insurance policy to have been administered from within the UK.
- 6.32 Eligible claimants are defined to be:
- Consumers, which for these purposes means natural persons acting for purposes outside their trade, business or profession;
 - Micro-enterprises, which means any enterprise (being a person, irrespective of legal form, engaged in an economic activity) which employs fewer than 10 persons and has a turnover or annual balance sheet that does not exceed €2 million.
 - Charities which have an annual income of less than £1 million
 - Trustees of a trust which has a net asset value of less than £1 million.
- 6.33 FOS is discussed further in paragraphs 11.15 to 11.17.

7 Claims reserves

- 7.1 In this section, I discuss the claims reserve strength of the Transferring Portfolio, Remaining Portfolio and the Existing EWICL Portfolio. In doing so, I have considered:
- The best estimate reserves for the Transferring Portfolio by claim type as calculated by QBEUK
 - The adjustments applied by QBEUK to determine the Solvency II technical provisions for the Transferring Portfolio from the best estimate reserves
 - The best estimate reserves for the Transferring Portfolio by claim type as calculated by EWICL
 - The adjustments applied by EWICL to determine the Solvency II technical provisions for the Transferring Portfolio from the best estimate reserves
 - The best estimate reserves for the Remaining Portfolio
 - The adjustments applied by QBEUK to the best estimate reserves in order to determine the Solvency II technical provisions for the Remaining Portfolio
 - The best estimate reserves for the Existing EWICL Portfolio
 - The adjustments applied by EWICL to the best estimate reserves in order to determine the Solvency II technical provisions for the Existing EWICL Portfolio
 - The governance process relating to the reserves of QBEUK and EWICL.
- 7.2 This section is set out as follows:
- Paragraphs 7.3 to 7.11 outline a summary of the reserves for each of QBEUK and EWICL, both before and after the Scheme
 - Paragraphs 7.12 to 7.26 discuss the process by which each of QBEUK and EWICL undertake in setting reserves, including my opinion on the robustness of these processes
 - Paragraphs 7.27 to 7.137 discuss the Transferring Portfolio, including my opinion on the strength of the reserves and the Solvency II Technical Provisions
 - Paragraphs 7.138 to 7.148 discuss the Remaining Portfolio, including my opinion on the strength of the reserves and the Solvency II Technical Provisions
 - Paragraphs 7.149 to 7.171 discuss the Existing EWICL Portfolio, including my opinion on the strength of the reserves and the Solvency II Technical Provisions.

Summary of reserves

- 7.3 The tables below show the booked claims reserves for QBEUK and EWICL, both gross and net of reinsurance, prior to and post the Scheme as at 31 December 2018. As EWICL does not utilise outwards reinsurance, the net of reinsurance reserves are equal to the gross of reinsurance reserves. The position post Scheme is hypothetical had the Scheme become effective on 31 December 2018. In addition, the QBEUK net of reinsurance reserves shown in the table below take account of the Autumn LPTA and Chestnut LPTA as these were in place as at 31 December 2018.

Table 7.1: Booked claims reserves of QBEUK before and after the Scheme

£m	Before Scheme	After Scheme	Difference
Gross of reinsurance	2,861.2	2,773.1	88.1
Net of reinsurance	2,091.0	2,091.0	0

Table 7.2: Booked claims reserves of EWICL before and after the Scheme

£m	Before Scheme	After Scheme	Difference
Gross of reinsurance	27.9	102.4	74.4
Net of reinsurance	27.9	102.4	74.4

- 7.4 As can be seen from the tables above, QBEUK's gross claims reserves reduce by more than EWICL's reserve increase following the Scheme. This is because the underlying assumptions used by ARML, on behalf of EWICL, to calculate the reserves for the Transferring Portfolio differ to those used by QBEUK. This is discussed in further detail below.

Summary of conclusions

- 7.5 Based on my experience and my knowledge of the market, the process for setting the GAAP reserves and Solvency II technical provisions at QBEUK appears robust. My reasons for reaching this conclusion are given in paragraphs 7.13 to 7.19.
- 7.6 I understand from QBEUK that it is currently going through a process to improve and simplify its reserving tools. However, I further understand from QBEUK that these changes are not expected to change the reserves.
- 7.7 Based on my experience and my knowledge of the market, the process for setting the GAAP reserves and Solvency II technical provisions at EWICL appears robust. My reasons for reaching this conclusion are given in paragraphs 7.20 to 7.26. In addition, I understand from ARML that this process will remain the same following the Scheme and the same process will apply to the Transferring Portfolio.
- 7.8 In respect of the Transferring Portfolio, the conclusion of my review of the estimates provided by QBEUK and ARML is that both lie within a reasonable range of possible outcomes. My reasons for reaching this conclusion are given in paragraphs 7.27 to 7.102. However, given the large differences set out in the tables above, I have deemed it necessary to analyse the material differences in order provide my best estimate of the reserves for the Transferring Portfolio as at 31 December 2018. This is discussed in paragraphs 7.103 to 7.125
- 7.9 In respect of the Remaining Portfolio, I have no reason to believe that the reserves or Solvency II Technical Provisions for QBEUK lie outside a range of reasonable estimates. My reasons for reaching this conclusion are discussed in paragraphs 7.138 to 7.148.

- 7.10 In respect of the Existing EWICL Portfolio, I have no reason to believe that the reserves or Solvency II Technical Provisions for EWICL lie outside a range of reasonable estimates. My reasons for reaching this conclusion are discussed in paragraphs 7.149 to 7.171.
- 7.11 There is a limitation upon the accuracy of any estimate of claims reserves in that there is an inherent uncertainty in any estimate of future liabilities. This is due to the fact that the claims will be subject to the outcome of events yet to occur, such as judicial decisions, legislative actions, claim consciousness amongst potential claimants, claims management, claim settlement practices, changes in inflation and economic decisions. As a result, it should be recognised that future claim emergence will likely deviate, perhaps materially, from any estimate of claims reserves.

Process for setting reserves

- 7.12 In this section, I discuss the process for setting reserves within each of QBEUK and EWICL, both before and after the transfer.

QBEUK's process

- 7.13 In general, QBEUK undertakes reserving on a half-yearly basis. However, in respect of the Transferring Portfolio, QBEUK has historically undertaken reserving on an annual basis.
- 7.14 The reserving team holds discussions with both the claims team and underwriting team at the start of each reserving process to keep abreast of any changes that may affect the reserving process. It also maintains an open dialogue with the claims and underwriting teams throughout the reserving process.
- 7.15 I understand from QBEUK that is currently going through a process to improve and simplify its reserving tools. However, I further understand from QBEUK that these changes are not expected to change the reserves.
- 7.16 The claims reserves estimated by QBEUK, both for the Transferring Portfolio and the Remaining Portfolio, are subject to several layers of internal review which take place for every reserving exercise. These are:
- Review by actuarial managers
 - Review by underwriters and sign off at divisional meetings
 - Peer review and sign-off by Head of Reserving
 - Review by Reserve Working Group and recommendations made by it in support of holding adequate reserves
 - Approval of reserving outputs by Finance Management Group and recommendations made to Audit Committee
 - Overall approval of reserving outputs by Audit Committee.
- 7.17 In addition, the external auditor of QBEUK undertakes a review of the claims reserves annually.
- 7.18 QBEUK has informed me that the governance process that currently applies to QBEUK will continue to apply to the Remaining Portfolio following the Scheme.

- 7.19 Based on my experience and my knowledge of the market, my view is that the process for setting the GAAP reserves and Solvency II technical provisions at QBEUK appears to be appropriate and robust for the following reasons:
- The process followed is in line with processes that are regularly used elsewhere
 - There are sufficiently experienced individuals conducting the analysis as I have concluded in paragraphs 7.35 and 7.139.
 - There are several layers of review performed, giving the opportunity for a number of people to challenge the analysis and results

EWICL's process

- 7.20 Prior to the Scheme, ARML undertakes reserving for the Existing EWICL Portfolio on an annual basis. In addition, ARML undertakes reserving for the Transferring Portfolio on behalf of Cell G of ILS on an annual basis.
- 7.21 I understand from EWICL that, following the Scheme, ARML will continue to undertake reserving for both the Existing EWICL Portfolio and for the Transferring Portfolio on behalf of EWICL. I understand from EWICL that this will continue to occur on an annual basis.
- 7.22 The reserving team at ARML holds discussions with the relevant claims teams at the start of each reserving process to keep abreast of any changes that may affect the reserving process. It also maintains an open dialogue with the claims teams throughout the reserving process.
- 7.23 The claims reserves for EWICL are subject to several layers of internal review which take place for every review. These are:
- Peer review by another actuary
 - Sign-off of reserves by the Chief Actuary
 - Approval of reserves by EWICL's Board.
- 7.24 In addition, the external auditor of EWICL undertakes a review of the claims reserves at least annually.
- 7.25 EWICL has informed me that the governance process that currently applies to EWICL will apply to the Transferring Portfolio and continue to apply to the Existing EWICL Portfolio following the Scheme.
- 7.26 Based on my experience and my knowledge of the market, my opinion is that the process for setting the GAAP reserves and Solvency II technical provisions at EWICL appears to be appropriate and robust for the following reasons:
- The process followed is in line with processes that are regularly used elsewhere
 - There are sufficiently experienced individuals conducting the analysis as I have concluded in paragraphs 7.69 and 7.150
 - There are several layers of review performed, giving the opportunity for a number of people to challenge the analysis and results

Transferring Portfolio

- 7.27 I have been provided with two actuarial reserve reviews undertaken on the Transferring Portfolio for the purposes of reporting as at 31 December 2018.
- 7.28 The first was undertaken by QBEUK and is based on data as at 31 May 2018 for the Autumn Portfolio and 30 September 2018 for the Chestnut Portfolio. In addition, I have been provided with a report

produced in respect of QBE EO's reserves, including the Transferring Portfolio, as at 30 September 2018.

- 7.29 The second review was undertaken by ARML on behalf of both EWICL and ILS Cell G and is based on data as at 30 September 2018. In addition, I have been provided with a report documenting the results of this review.
- 7.30 The table below shows the actuarial best estimate reserves of the Transferring Portfolio used for reporting as at 31 December 2018, as estimated by each of QBEUK and ARML. The figures below have been rolled forward by QBEUK and ARML to 31 December 2018 by deducting the paid claims from the reserves estimated during the reserve reviews at 31 May 2018 and 30 September 2018.

Table 7.3: Actuarial best estimate reserves as at 31 December 2018

Portfolio	QBEUK estimate (£m)	ARML estimate (£m)	Difference
Autumn	78.6	64.6	14.0
Chestnut	9.5	8.5	1.0
Total	88.1	73.1	15.0

- 7.31 As can be seen from the table above, there is a substantial difference between the estimates provided to me.
- 7.32 In this section, I will discuss:
- QBEUK's approach to reserving for the Transferring Portfolio, in paragraphs 7.34 to 7.67.
 - ARML's approach to reserving for the Transferring Portfolio, in paragraphs 7.68 to 7.102.
 - The reasons for the differences between the estimates determined by QBEUK and the estimates determined by ARML, in paragraphs 7.103 to 7.125.
 - My consideration of the appropriate reserves for the Transferring Portfolio and the conclusions I have drawn, in paragraphs 7.126 to 7.137.
- 7.33 The reserve reviews that I have considered in this section were the most recent available at the time of my analysis. For my Supplementary Report, I will consider claims movements since these reviews and any more recently available actuarial reserve reviews.

QBEUK's estimate of the reserves for the Transferring Portfolio

- 7.34 I have been provided with actuarial reserve reviews as at 31 May 2018 for the Autumn Portfolio and as at 30 September 2018 for the Chestnut Portfolio which were undertaken by the Actuarial team at QBEUK. In addition, I have been provided with an actuarial report for QBE EO as at 30 September 2018, which describes the analyses undertaken in respect of both the Autumn and Chestnut Portfolios.
- 7.35 I have seen the CVs of the individuals that undertook this analysis. Based on these and my interactions with those individuals, I am satisfied that the actuaries at QBEUK who undertook this review have the necessary experience and expertise to undertake a review of this nature and for me to rely on this review.
- 7.36 Below I have summarised the methodologies and major assumptions used by QBEUK to estimate the claims reserves for the Transferring Portfolio. I provide my opinion on the reasonableness of the claims reserves for the Transferring Portfolio as estimate by QBEUK in paragraph 7.63.

7.37 The claims data used in the review was as at 31 May 2018 and 30 September 2018 for the Autumn and Chestnut Portfolios respectively. A high level review was subsequently undertaken using data as at 31 December 2018 to check the reasonableness of the estimates produced using the earlier data and to make allowance for claims paid between the reserving date and 31 December 2018.

Reinsurance

7.38 The Transferring Portfolio does currently benefit from an excess of loss programme that covers multiple areas of QBEUK's business. I understand from QBEUK that there are no claims attaching to the Transferring Portfolio that have breached the excess and that QBEUK is not allowing for any recoveries in respect of the Transferring Portfolio against this contract.

Methodology and assumptions for actuarial best estimate reserves – Autumn Portfolio

7.39 The claims reserves for the Autumn Portfolio have been estimated using the following splits of data:

Table 7.4: QBEUK classes of business for the Autumn Portfolio

Long Tailed Disease ("LTD") classes	Non-LTD and Other classes
<ul style="list-style-type: none">• Mesothelioma• Asbestos related disease (excluding mesothelioma)• Cancers (excluding asbestos related cancers)• Deafness/ Noise Induced Hearing Loss ("NIHL")• Hand and Arm Vibration Syndrome ("HAVS")• Respiratory diseases	<ul style="list-style-type: none">• Non-LTD• EIROS, where this class relates to claims on a specific bordereau

LTD classes

7.40 A frequency- severity approach has been taken to project the claims for each LTD class of business to their ultimate position, on a reporting year basis. Furthermore, nil and non-nil claims have been considered separately and are used to estimate both pure IBNR relating to future claims as well as IBNER on existing claims.

7.41 A nil claim is defined as a claim with zero damages incurred but which may incur third party costs such as third party adjuster (TPA) costs or costs relating to QBEUK. Damage costs are used to determine if a claim is nil for claims reported from 2011 onwards. Due to data constraints in older years, the reporting years 2010 and prior use a £1,000 threshold to define nil claims. I understand from QBEUK that discussions have taken place internally with claims handlers to determine that this threshold is consistent with historical average TPA costs.

7.42 The key assumptions used for the projection of claims to their ultimate positions as at 31 December 2018 are:

- Number of claims reported in 2018 and 2019
- Reported claims run-off
- Proportion of claims to be settled as non-nil
- Average Cost Per Claims (ACPC) for non-nil claims
- ACPC for nil claims
- Claims inflation for nil and non-nil claims.

Number of claims reported in 2018 and 2019

- 7.43 For each LTD class, the number of claims expected to be reported in the current and following year is a key assumption and is selected with reference to:
- The number of claims reported in prior years
 - The reporting pattern in recent years
 - The number of claims reported to date in the current year
- 7.44 Internal or external factors which may influence the number of claims.

Reported claims run-off

- 7.45 For each LTD class, QBEUK considers the run-off rate and duration of claims.
- 7.46 For mesothelioma claims, this is based on the 2009 model produced by the Asbestos Working Party ("AWP"), a working party of the IFoA, with the underlying assumptions updated based on the latest statistics available.
- 7.47 For the remaining LTD classes, the run-off pattern is based on historical run-off rates observed by QBEUK.

Proportion of claims to be settled as non-nil

- 7.48 For each LTD class, the proportion of claims to be settled as non-nil is selected after consideration of:
- The non-nil rates to date for settled claims
 - Internal or external factors which may lead the selected non-nil rate to deviate from historical experience.
- 7.49 In particular, for the Deafness class, QBEUK has applied different nil rates to each reported year to reflect the impact of changing market conditions.

ACPC for non-nil claims

- 7.50 For asbestos related disease (excluding mesothelioma), mesothelioma and deafness claims, an estimate of the current reported year ACPC at a market level is selected by QBEUK. I understand from QBEUK that this is based on industry data from the AWP or the Deafness Working Party ("DWP", another working party of the IFoA). QBEUK subsequently selects its share for each of these disease types based on historical experience for settled claims and discussions with claims handlers.
- 7.51 For the remaining diseases, the market level ACPC is not readily available from external sources and therefore QBEUK selects its share of the ACPC based on an inflation adjusted historical settled ACPC.
- 7.52 Where appropriate, QBEUK takes into consideration any internal and external factors which may lead the selected ACPC to deviate from historical experience.

ACPC for nil claims

- 7.53 For nil claims, the current reported year ACPC is based on the experience on settled claims in the most recent years. The number of years selected varies by claim type.

Claims inflation for nil and non-nil claims

- 7.54 For non-nil claims, excluding mesothelioma, the ACPC is inflated by applying a future claims inflation rate assumption of 3.5% per annum to the current average cost. This rate is based on QBEUK's expectation of a long-term average earnings inflation rate.

- 7.55 For mesothelioma non-nil claims, the inflation rate assumption is based on the AWP 2009 average costs model which considers court, Retail Price Index and wage related inflation.
- 7.56 For nil claims, the ACPC is inflated by applying a future claims inflation rate assumption of 3.5% per annum to the current average cost. This rate is based on the assumption that the claims handling and other non-damage related costs will increase in line with QBEUK's expectation of a long-term average earnings inflation rate.

Non-LTD and EIROS classes

- 7.57 QBEUK has estimated the IBNR for the EIROS class by using IBNR-to-outstanding ratios. These ratios are based on an analysis of QBEUK's employers' liability LTD book of business.
- 7.58 For the non-LTD classes, QBEUK has assumed that the case reserves will be sufficient based on standard development patterns and therefore assumes nil IBNR.

Methodology and assumptions for actuarial best estimate reserves – Chestnut Portfolio

- 7.59 The claims reserves for the Chestnut Portfolio have been estimated using the following splits of data:
- Employers' liability
 - Public liability
 - Motor.
- 7.60 For disease related employers' liability claims, QBEUK has estimated the IBNR by using IBNR-to-outstanding ratios. These ratios are based on an analysis of QBEUK's employers' liability LTD book of business.
- 7.61 For all other classes with the Chestnut Portfolio, QBEUK uses standard actuarial development factor methods to estimate the reserves.

UK GAAP booked reserves – Autumn and Chestnut Portfolios

- 7.62 QBE EO's reserve working group is responsible for determining whether or not any margin is required in addition to the actuarial best estimate when setting the reserves to be booked in the UK GAAP accounts. I understand from QBEUK that there was no margin set in respect of the Transferring Portfolio as at 31 December 2018.
- 7.63 Based on my experience, the process for calculating the actuarial best estimate and the booked reserves appears appropriate and robust as I have concluded in paragraph 7.19. I have no reason to believe that the booked reserves for the Transferring Portfolio, as estimated by QBEUK, lie outside a range of reasonable estimates. In reaching this conclusion I have considered the following:
- The approaches adopted are in line with those I have seen used elsewhere for business of this type
 - The analysis that QBEUK has conducted in relation to its own experience is appropriate
 - QBEUK's selected share for mesothelioma claims is higher than I would consider a best estimate based on the historical experience of the Transferring Portfolio. However, although the selected share is above what I would consider a best estimate, it can be justified as a reasonable outcome.
 - The remaining assumptions are broadly in line with QBEUK's historical experience and/or other external statistics
 - The reasonableness of the outputs compared to the historical experience and AWP report
 - My experience and expertise relating to claims reserving.

Solvency II technical provisions– Autumn and Chestnut Portfolios

- 7.64 The Solvency II technical provisions are the sum of the best estimate provisions, calculated on a cash flow basis under Solvency II, and a risk margin.
- 7.65 I have been informed by QBEUK that it calculates its Solvency II technical provisions at a total portfolio level and does not estimate those solely in respect of the Transferring Portfolio as the Transferring Portfolio is a small proportion (approximately 4%) of its total portfolio.
- 7.66 The adjustments made to QBEUK's overall actuarial best estimate reserves to derive its Solvency II technical provisions are discussed in paragraphs 7.142 to 7.148.
- 7.67 QBEUK has not estimated a risk margin solely in respect of the Transferring Portfolio as it does not expect its SCR and therefore its Risk Margin to change materially as a result of the Scheme. I understand from QBEUK that this is based on the fact that the Transferring Portfolio is already 100% reinsured and, whilst there will be a reduction in the default risk for QBEUK, it is unlikely that this will be material.

ARML's estimate of the reserves for the Transferring Portfolio

- 7.68 I have been provided with actuarial reserve reviews, and the corresponding reserve reports, for each of the Autumn and Chestnut Portfolios as at 30 September 2018 that were undertaken by a senior actuary at ARML on behalf of EWICL and ILS Cell G.
- 7.69 I have seen the CVs of the individuals that undertook and reviewed this analysis. Based on these and my interactions with those individuals, I am satisfied that the actuaries at ARML have the necessary experience and expertise to undertake a review of this nature and for me to rely on this review.
- 7.70 In preparing the review, I understand from ARML that it relied on information provided by QBEUK at the point of migration of data, and that the data provided was not audited by the report author although it was reviewed for reasonableness and consistency at a high level.
- 7.71 Below I have summarised the methodologies and major assumptions used by ARML to estimate the claims reserves for the Transferring Portfolio on a GAAP basis. I provide my opinion on the reasonableness of the claims reserves for the Transferring Portfolio as estimated by ARML in paragraph 7.98.
- 7.72 The report covers only the Transferring Portfolio business on the following basis:
- On all exposure earned as at 30 September 2018
 - Net of salvage and subrogation recoveries
 - Gross and net of reinsurance recoveries
 - Excludes bad debt provisions and estimates for claims equalisation provisions
 - Includes allocated claims handling expenses
 - Excludes unallocated claims handling expenses.
- 7.73 I understand from ARML that Cell G has a per claim cap of £1m with respect to the Chestnut Portfolio. Amounts in respect of individual claims in excess of £1m are borne by QBEUK under the terms of the Chestnut LPTA.
- 7.74 I further understand from ARML that the reserve analysis for the Chestnut Portfolio allows for this £1m cap and has removed the amounts in excess of it. Three claims have previously breached this limit and out of these, there is one open claim. ARML has told me that it does not believe that any further claims have the potential to breach the limit.

7.75 I understand from ARML that, following the Scheme, QBEUK will retain exposure in respect of individual claims in excess of £1m. I further understand from ARML that these claims will continue to be reserved for in the same way as they are currently.

Reinsurance

7.76 ARML's estimate of the reserves takes account of the excess of loss reinsurance programme which provides protection to the Transferring Portfolio, as discussed in paragraph 7.38. However, as there are no recoveries expected on the excess of loss reinsurance programme and there is no other outward reinsurance in relation to Cell G, the net of reinsurance reserves are equal to the gross of reinsurance reserves for the Transferring Portfolio.

Methodology and assumptions for actuarial best estimate reserves – Autumn Portfolio

7.77 The claims reserves have been estimated using the following splits of data for the Autumn Portfolio:

Table 7.5: ARML classes of business for the Autumn Portfolio

LTD classes	Non-LTD and Other classes
<ul style="list-style-type: none">• Mesothelioma• Asbestos related disease (excluding mesothelioma)• Cancers• Deafness/ Noise Induced Hearing Loss ("NIHL")• HAVS• Respiratory diseases	<ul style="list-style-type: none">• Public liability• Employers' liability non-LTD• EIROS

7.78 The business is further split into the following and the same methodology as described in the paragraphs below is applied to each cohort:

- Claims relating entirely to exposures from 2007 and prior, and are therefore wholly the responsibility of ILS
- Claims that have exposure which straddles 1 January 2008 (i.e. the exposure starts prior to 1 January 2008 and finishes after 1 January 2008). The liability for these claims is split between QBEUK and EWICL
- Omitted claims which relate to policies that were thought to be excluded from the LPTA at the time of ARML's reserve review as at 30 September 2017, but which were subsequently agreed to be included in the Autumn Portfolio.

LTD classes

7.79 A frequency-severity approach has been taken to project the claims for each LTD class of business to their ultimate position, on a reporting year basis. Furthermore, nil and non-nil claims have been considered separately and are used to estimate both pure IBNR relating to future claims as well as IBNER on existing claims.

7.80 A nil claim is defined as a claim with zero damages incurred but which may incur third party costs. I understand from ARML that, at the time of its review, it did not have data which provided a split between expenses and indemnity. It has selected a lower threshold to define nil claims than QBEUK, at £500. I understand that AMRL can now review claims split between expenses and indemnity and will review the appropriateness of the nil claims threshold for future reviews.

7.81 The key assumptions used for the projection of claims to their ultimate positions as at 31 December 2018 are:

- Number of claims reported in 2018 and 2019
- Estimated number of future claims/ decay rate
- Nil settlement rate
- ACPC for non-nil claims
- ACPC for nil claims
- Claims inflation for nil and non-nil claims.

Number of claims reported in 2018 and 2019

7.82 For each LTD, the number of claims expected to be reported in the current and following years is a key assumption and is selected after consideration of historical experience and the judgement of the actuaries at ARML.

Estimated number of future claims/ decay rate

7.83 For each LTD, ARML estimated the number of claims in the future for reporting years 2018 to 2050.

7.84 For mesothelioma claims, this is based on the AWP 2009 model with the following key assumptions:

- The analysis used by ARML is based on a specific scenario within the AWP 2009 report, scenario 23, which is the AWP's central estimate. This has been used by ARML to calculate the number of claimants and the average cost per mesothelioma claim by notification year
- ARML has considered insurance claims only rather than all mesothelioma deaths
- As the policies within the Autumn Portfolio only have exposure up to year end 2007, ARML has removed exposure from the AWP 2009 model from 2008 onwards.

7.85 For the remaining LTDs, this is based on assumptions for the decay rate on notifications, where a specific assumption has been selected for each of these LTDs. I have been informed by ARML that this assumption is based on the industry experience and judgement of the actuaries at ARML.

Nil settlement rates

7.86 The nil settlement rate is the percentage of claims reported that settle without an indemnity payment.

7.87 I have been informed by ARML that the nil settlement rate assumption has been based on historical nil rates, supplemented by judgement to allow for trends appearing in the data over time.

ACPC for nil and non-nil claims

7.88 I have been informed by ARML that the selected ACPCs have been based on historical average claim costs, supplemented by judgement to allow for trends emerging in the data over time.

Claims inflation for nil and non-nil claims

7.89 For nil and non-nil claims, ARML has used a future claims inflation rate assumption of 2.5%. I understand from ARML that this assumption has been selected after consideration of inflation rates over the last 20 years and is consistent with that experienced in the historical claims data.

Non-LTD classes

- 7.90 The IBNR relating to public liability, employers' liability non-LTD and EIROS have been estimated by using IBNR-to-outstanding ratios.
- 7.91 I have been informed by ARML that claims relating to these classes constitute less than 5% of the total liability of the Autumn Portfolio. For public liability and employers' liability non-LTD, ARML has selected an assumption of 25% for the IBNR-to-outstanding ratio. For EIROS, ARML has used an IBNR-to-outstanding ratio derived from the disease classes.

Methodology and assumptions for actuarial best estimate reserves – Chestnut Portfolio

- 7.92 The claims reserves have been estimated using the following splits of data for the Chestnut Portfolio:

Table 7.6: ARML classes of business for the Chestnut Portfolio

LTD classes	Non-LTD classes
<ul style="list-style-type: none">• Mesothelioma• Asbestos related disease (excluding mesothelioma)• Cancers• HAVS• Respiratory diseases• Other diseases – a combination of upper limb disorder, dermatitis psychiatric conditions and other diseases	<ul style="list-style-type: none">• Employers' liability non-LTD• Motor• Other liability

LTD classes

- 7.93 As per the Autumn Portfolio, ARML has taken a frequency-severity approach to project the claims for each LTD class of business to their ultimate position on a reporting year basis. Furthermore, nil and non-nil claims have been considered separately and are used to estimate both pure IBNR relating to future claims as well as IBNER on existing claims.
- 7.94 ARML uses the same methodology and key assumptions as described in paragraphs 7.79 to 7.89 to calculate the ultimate claims and reserves for the LTD classes within the Chestnut Portfolio.

Non-LTD classes

- 7.95 For employers' liability non-LTD and Other liability, claims have been projected to their ultimate position using standard actuarial development factor methods.
- 7.96 For the Motor class, ARML has assumed that the case reserves will be sufficient and therefore assumes nil IBNR.

Booked reserves – Autumn and Chestnut Portfolios

- 7.97 The booked reserves for Cell G in respect of the Autumn and Chestnut Portfolios are £80k higher than the actuarial best estimate. I understand from ARML that the reason for this is that the booked reserves do not allow for the £1m claims cap. I understand from EWICL that, following the Scheme, EWICL will book reserves in line with the actuarial best estimate, although this will be subject to review by EWICL's Board, which may choose to book reserves above the actuarial best estimate for any risks it feels are not sufficiently captured by the actuarial analysis.

- 7.98 The process for calculating the actuarial best estimate and the booked reserves appears appropriate and robust as concluded in paragraph 7.26. I have no reason to believe that the booked reserves for the Transferring Portfolio, as estimated by ARML, lie outside a range of reasonable estimates. In reaching this assessment I have considered the following:
- ARML utilises a market standard approach to estimating reserves of this type by applying a frequency-severity approach on a notification year basis
 - Whilst it is more common practice to use the AWP market study as a starting point when estimating the ACPC for mesothelioma claims, ARML has decided to base its ACPC on the historical claims experience of the Autumn Portfolio. I have reviewed the approach taken and consider it to be an appropriate alternative to the more commonly used approach. Furthermore, it is an approach that I have seen used elsewhere. Although ARML's selected ACPC is below what I would consider a central best estimate, I consider it to be within the range of possible estimates.
 - In addition, the selected claims inflation rate for mesothelioma claims of 2.5% is lower than that suggested by the AWP. While I consider this selection to be below my best estimate, I do believe it to be within the range of possible estimates.
 - Offsetting the possible understatements of the ACPC selection and the inflation rate discussed in the previous two bullet points, at least to some extent, the selected nil settlement rate for mesothelioma claims is lower than what I would consider a best estimate based on the historical experience of the Transferring Portfolio (ie. a prudent assumption that leads to fewer nil claims). Again, although the selected nil settlement rate is below what I would consider a best estimate, I consider it to be within the range of possible estimates.
 - The analysis that ARML has conducted in relation to the experience of the Transferring Portfolio is appropriate
 - The remaining assumptions are broadly in line with the Transferring Portfolio's historical experience and/or other external statistics
 - The reasonableness of the outputs compared to the historical experience
 - My experience and expertise relating to claims reserving.

Solvency II technical provisions adjustments – Autumn and Chestnut Portfolios

- 7.99 ARML has made a number of adjustments to its actuarial best estimate reserves to derive its Solvency II technical provisions for the Transferring Portfolio. These adjustments are as follows:
- Allowance for ENIDs
 - Allowance for expenses associated with the run-off of claims
 - Discounting the payments to allow for the time value of money, using the yield curves published by EIOPA at the relevant date
 - Allowance for a risk margin, calculated assuming the SCR decreases in line with best estimate technical provisions.
- 7.100 I have been informed by ARML that the actuarial best estimate reserves do not include any additional margin and therefore an adjustment for this is not required.
- 7.101 I note that there is uncertainty about the appropriate level of adjustments to make in order to estimate the technical provisions under Solvency II. ARML could have made other equally valid adjustments which would lead to different results.

- 7.102 The process for calculating Solvency II technical provisions appears appropriate and robust as concluded in paragraph 7.26. I have no reason to believe that the Solvency II technical provisions for the Transferring Portfolio lie outside a range of reasonable estimates. In reaching this assessment, I have considered the following:
- ARML is making the adjustments I would expect in order to determine its Solvency II Technical Provisions
 - The adjustments that ARML has made are in line with the adjustments I have seen elsewhere in the market for similar liabilities
 - My experience and expertise relating to Solvency II Technical Provision calculations.

Differences between QBEUK and ARML's reserves for Transferring Portfolio

- 7.103 In this section, I describe the differences between the estimates of the claims reserves and the Solvency II Technical Provisions for the Transferring Portfolio produced by QBEUK and ARML.
- 7.104 Although there are similarities in the overall methods used to derive the actuarial reserves and the Solvency II Technical Provisions, including the split of classes, QBEUK and ARML have differing views on some of the key assumptions and on what they believe to be the best estimate of the liabilities of the Transferring Portfolio. As set out in the previous sections, there are certain assumptions made by each of QBEUK and ARML that I would not consider as my best estimates. As a result, following my description of the differences in the key assumptions in this section, I set out my own estimate of the claims reserves of the Transferring Portfolio in paragraphs 7.129 to 7.137.

Differences in the claims reserves

- 7.105 One of the drivers of the differences in QBEUK's and ARML's estimates of the reserves for the Transferring Portfolio is that the analyses were conducted at different dates. QBEUK's analysis was conducted at 31 May 2018 for the Autumn portfolio and as at 30 September 2018 for the Chestnut portfolio, while ARML's analysis was conducted as at 30 September 2018. During the time between the valuation dates for the Autumn Portfolio reviews, claims would have been paid and would no longer be considered in the reserves. I understand from ARML, that in that period £1.0m of claims were paid on the Autumn portfolio.
- 7.106 After allowing for these timing differences by reducing all of the reserve estimates for the claims paid between the valuation dates and 31 December 2018, QBEUK's estimate of reserves is £15.0m higher than that of ARML.
- 7.107 The key driver of this difference, contributing £11.1m, is the different assumptions selected by QBEUK and ARML with respect to Mesothelioma in the Autumn Portfolio. I have provided more detail of the differences in Mesothelioma assumptions in paragraphs 7.110 to 7.111 below.
- 7.108 Another large driver of the difference arises from the assumption regarding the average cost of Deafness claims within the Autumn Portfolio. I have been informed by ARML that its claims team has been actively settling these claims for amounts lower than the case reserves and its IBNR gives some weight to this recent improvement whereas QBEUK has not allowed for this improvement. This has contributed £3.0m to the overall difference in the reserve estimates.
- 7.109 The differences resulting from Mesothelioma and Deafness claims are partially offset by differences in the other classes in the opposite direction.

Difference in Mesothelioma assumptions

- 7.110 The main contributor to the difference, at £11.1m, relates to the estimated reserves for Mesothelioma within the Autumn Portfolio. Both QBEUK and ARML use a frequency-severity approach to estimate the reserves for Mesothelioma. Therefore, the differences in the selected assumptions are the driver of the overall difference for this claim type.
- 7.111 ARML has undertaken an investigation into the differences in the selected assumptions for the Mesothelioma class within the Autumn Portfolio. The paper setting out this investigation has been reviewed by QBEUK. I have reviewed the outcome of this investigation and highlighted key differences in the following areas:
- ACPC for non-nil claims
 - Inflation
 - Nil settlement rate.

Difference in calculation of ACPC for non-nil claims

- 7.112 ARML has calculated an ACPC for non-nil claims of £40k. QBEUK has calculated an ACPC for non-nil claims of £76k
- 7.113 ARML has based its ACPC assumption on historical average claim costs, supplemented by judgement to allow for trends emerging in the settlement amounts. In particular, ARML has given some weight to the reducing trend that it has observed in the ACPC in the historical data.
- 7.114 In addition, I understand from ARML that it estimates its ACPC using historical data in respect of the Transferring Portfolio only and does not utilise any other data on mesothelioma claims.
- 7.115 For non-nil claims, ARML has selected an ACPC of £40k. I have been informed by ARML that this is based on the ACPC of the full data history of the Transferring Portfolio, allowing for a trend it has observed in the ACPC in recent years. For non-nil claims closed over the entire history of the Portfolio the ACPC is £64k. This reduces to £41k when considering only non-nil closed claims that were reported between 2008 and 2017. When considering claims reported between 2013 and 2017, the ACPC for non-nil closed claims is £37k. When considering claims reported between 2015 and 2017, the ACPC for non-nil closed claims is £23k.
- 7.116 By contrast, QBEUK uses the ACPC estimates from the AWP and scales these to its share of the liabilities. It also does not give any weight to the reducing trend that ARML has observed in the ACPC from historical data.

Difference in claims inflation

- 7.117 ARML has assumed a future claims inflation rate of 2.5% which is based on typical RPI over the last 20 years. I have been informed by ARML that this is also consistent with historical data.
- 7.118 In addition, ARML has informed me that the historical claims data suggests the ACPC is decreasing and therefore it has not inflated historical claims to present values.
- 7.119 By contrast, QBEUK has assumed a future claims inflation rate from the AWP, which ranges between 3% and 4.5% per annum. In addition, when selecting its ACPC for future claims settlements, QBEUK has inflated historical claims to present values using the AWP's observed historical claims inflation statistics.

Difference in nil settlement rate

- 7.120 Although both ARML and QBEUK have selected nil settlement rates based on historical data, their differing definitions of the nil claim threshold has resulted in different selections. As ARML and QBEUK have selected different nil claim thresholds, the nil settlement rates are not directly comparable. However, there is a difference between them which is worth noting and this is discussed below.
- 7.121 At the time of the review, ARML was unable to split claims between indemnity and expenses. It selected a nil claims threshold of £500.
- 7.122 I have been informed by ARML that the average nil settlement rate for the ten reported years to 2012 (which are almost all fully closed years) is 46%. The nil settlement rates of closed claims observed in 2013, 2014 and 2015 are 40%, 20% and 27% respectively. These years are mostly closed. The nil settlement rates of closed claims observed in 2016 and 2017 are 28% and 44% respectively. These two years have a substantially higher proportion of open claims remaining than the earlier years. In order to allow for this trend, ARML has selected a nil settlement rate of 30%. The selection of this rate leads to a higher reserve than if ARML had selected a higher nil settlement rate, all other things being equal.
- 7.123 By contrast, QBEUK's data can be split between expenses and indemnity amounts from 2011 onwards. QBEUK has selected a nil claims threshold of £1,000 based on discussions with claims handlers about historical TPA fees.
- 7.124 QBEUK has selected a nil settlement rate of 52.5%.
- 7.125 A higher nil settlement reduces the estimated number of non-nil claims and increase the estimated reserves. However, selecting a different nil claim threshold also serves to affect the selection of the ACPC for non-nil claims. If a lower nil claims threshold is selected, then more lower value claims will be considered as non-nil claims and therefore reduce the ACPC of the historical non-nil claims.

My analysis of the reserves of the Transferring Portfolio

- 7.126 I have performed an analysis to determine what I believe to be an appropriate estimate of the reserves for the Transferring Portfolio as at 31 December 2018. The analysis involved:
- A review of the reserves provided by QBEUK's actuaries
 - A review of the reserves provided by ARML's actuary
 - A review of the report produced by ARML and QBEUK to identify differences in their estimates of the reserves as at 31 December 2018
 - A review of the methods used to estimate the reserves compared with industry best practice
 - Discussions with individuals at QBEUK and ARML to understand the approaches used by each to estimate the reserves
 - my own projections of various components of the reserves to estimate what I believe to an appropriate reserve as at 31 December 2018
- 7.127 I have concluded in paragraphs 7.63 and 7.98 that the approaches used by both QBEUK and ARML to estimate the reserves for the Transferring Portfolio are reasonable.
- 7.128 In addition, I have concluded in paragraphs 7.63 and 7.98 that the estimates provided by QBEUK and ARML both lie within a reasonable range of possible outcomes, although I note that some assumptions made by both QBEUK and ARML differ from my own assessment of central best estimates.
- 7.129 In light of this and given the large differences described in the section above, I have deemed it necessary to analyse the material differences in order provide my estimate of the reserves for the Transferring Portfolio as at 31 December 2018.

- 7.130 It should be noted that, in developing my estimate, I focussed on the mesothelioma claims arising on the Autumn Portfolio since, as discussed above, this is the area where the main difference between QBEUK and ARML's estimates arose. I did not consider the other elements of the reserves since, in aggregate, the estimates of QBEUK and ARML were broadly in line for those and, as discussed above, I believe the approaches adopted to be reasonable.
- 7.131 I have not considered it necessary to estimate the adjustments required to convert the claims reserves to Solvency II Technical Provision, since as discussed in paragraph 7.102, I believe ARML has used assumptions that are appropriate to EWICL's business in converting the claims reserves to Solvency II Technical Provisions.
- 7.132 The table below shows my estimate of the reserves for the Transferring Portfolio as at 31 December 2018, alongside the estimates provided by QBEUK and ARML.

Table 7.7: Actuarial best estimates of reserves for Transferring Portfolio as at 31 December 2018

£m	QBEUK's estimate	ARML's estimate	My estimate
Reserves	88.1	73.1	80.5

- 7.133 For the reason discussed in paragraph 7.129, the difference between my estimate and the estimate provided by ARML all relates to mesothelioma claims arising on the Autumn Portfolio.

Mesothelioma claims

- 7.134 As described in the section above, QBEUK and ARML use a different definition for determining what threshold to use for a nil claim. I have decided to use ARML's definition and therefore any changes in assumptions I have set out below should be compared to ARML's assumptions rather than those used by QBEUK.

Claims inflation

- 7.135 The historical data from the AWP suggests that claims inflation for these types of claims has been at about 3% per annum for the past ten years. As a result, I have selected a claims inflation assumption of 3%. I have used this assumption to project the ACPC over future report years.

Nil settlement rate

- 7.136 Whilst there is some evidence of lower nil settlement rates in the two most recent reporting years, a longer term average would suggest that a 40% nil settlement rate would be more appropriate. As a result, in my estimate I have selected this as my assumption.

ACPC for non-nil claims

- 7.137 In order to select the ACPC for the 2018 year, I have inflated the historical claims into present terms using the historical inflation rates observed in market data as produced by the AWP. I have then selected the average cost from the 2008 to 2017 reported years, including both closed and open claims. This has resulted in an average cost per claim of £53,500.

Remaining Portfolio

- 7.138 I have been provided with a report on the claims reserves of QBEUK covering its entire portfolio as at 30 September 2018. I am comfortable that this report is sufficient to form an opinion given the scale of QBEUK's wider portfolio in comparison to the Transferring Portfolio, which only makes around 4% of QBEUK's total portfolio, gross of reinsurance.
- 7.139 I have seen the CVs of the individuals that undertook this analysis. Based on these and my interactions with those individuals, I am satisfied that the actuaries at QBEUK have the necessary experience and expertise to undertake a review of this nature and for me to rely on this review.
- 7.140 The table below shows the booked reserves as at 31 December 2018, both gross and net of reinsurance.

Table 7.8: Booked reserves for the Remaining Portfolio as at 31 December 2018

£m	Gross of reinsurance	Net of reinsurance
Outstanding claims reserve (actuarial best estimate)	2,234.0	1,551.9
Unearned premium reserve	539.1	539.1
Booked reserves	2,773.1	2,091.0

- 7.141 In determining the reserves, I understand from QBEUK that there are discussions between the actuarial team and other functions within the business such as claims and underwriting. The reserves are discussed in detail through the reserve committee meetings and other deep dives into various aspects.
- 7.142 The Solvency II technical provisions are the sum of the best estimate provisions, calculated on a cash flow basis under Solvency II, and a risk margin.
- 7.143 I have been provided with the Actuarial Function Report for 31 December 2017, which sets out the adjustments that QBEUK has made to its actuarial best estimate reserves to derive its Solvency II technical provisions. These adjustments are as follows:
- Removal of any margins for prudence
 - Allowance for ENIDs
 - Allowance for business that is yet to be inceptioned but that QBEUK is legally obligated to underwrite at the valuation date
 - Allowance for expenses associated with the run-off of claims
 - Discounting the payments to allow for the time value of money, using the risk-free yield curves published by EIOPA at the relevant date
 - Allowance for a risk margin.
- 7.144 The table below shows the Solvency II Technical Provisions as at 31 December 2018, both gross and net of reinsurance:

Table 7.9: Solvency II Technical Provisions for the Remaining Portfolio as at 31 December 2018

£m	Best estimate	Risk Margin	Solvency II Technical Provisions
Gross	2,497.3	280.6	2,777.8
Net	1,822.5	280.6	2,103.0

- 7.145 As discussed in 7.65, QBEUK does not estimate the Solvency II technical provisions solely in respect of the Transferring Portfolio and therefore the Solvency II technical provisions in respect of the Transferring Portfolio are equal to outstanding claims reserves. As a result of this, the gross best estimate and gross Solvency II technical provisions in the table above for the Remaining Portfolio have been calculated by excluding the outstanding claims reserves for the Transferring Portfolio from the figures for QBEUK as a whole.
- 7.146 We note that there is uncertainty regarding the appropriate level of adjustments to make in order to estimate the technical provisions under Solvency II. QBEUK could have made other equally valid adjustments which would lead to different results.
- 7.147 I have performed an analysis to satisfy myself that QBEUK's estimate of the insurance liabilities are consistent with my expectations for insurance business of the nature that it writes. This analysis involved:
- A review of the reserve report as at 30 September 2018 produced by QBEUK's actuaries
 - A review of the Actuarial Function Report as at 31 December 2017 which sets out the approach taken to deriving Solvency II Technical Provisions
 - A review of the methods used to estimate the reserves and Solvency II Technical Provisions compared with industry best practice
 - Discussions with individuals at QBEUK to understand the approaches used to estimate the reserves and Solvency II Technical Provisions. These discussions have also involved considering whether any material changes have occurred to the processes since the date of the information received.
- 7.148 I have concluded that the process appears appropriate and robust in paragraph 7.18. I have no reason to believe that the reserves or Solvency II Technical Provisions for QBEUK lie outside a range of reasonable estimates. In reaching this assessment, I have considered the following:
- QBEUK has utilised market standard approaches in determining its estimates
 - The analyses that QBEUK has conducted in relation to its own experience that is appropriate
 - The outputs appear reasonable given my experience and expertise relating to claims reserving and Solvency II Technical Provisions.

Existing EWICL Portfolio

- 7.149 I have been provided with a report on the claims reserves and Solvency II Technical Provisions of EWICL as at 31 December 2018. These were calculated by a senior actuary at ARML and the report covers its entire portfolio. The report sets out the results of the reserve review, methodologies used and key assumptions made in respect of the Existing EWICL Portfolio.
- 7.150 I have seen the CVs of the individuals that undertook and reviewed this analysis. Based on this and my interactions with those individuals, I am satisfied that the actuaries at ARML have the necessary experience and expertise to undertake a review of this nature and for me to rely on this review.

- 7.151 The table below shows the undiscounted actuarial best estimate reserves and the booked reserves as at 31 December 2018 on a gross of reinsurance basis. Since EWICL does not utilise outwards reinsurance, the net of reinsurance reserves are identical those shown below.

Table 7.10: Booked reserves for the Existing EWICL Portfolio as at 31 December 2018

£m	The Legacy Portfolio	The UKBG Portfolio	Total
Actuarial best estimate	0.1	26.8	26.9
Expense provision	0.0	1.0	1.0
Booked reserves	0.1	27.8	27.9

The Legacy Portfolio

- 7.152 As can be seen from the table above, EWICL currently has very few remaining liabilities and little in the way of reserves in respect of the Legacy Portfolio.
- 7.153 I understand from ARML that the estimates of outstanding claims have been set by ARML's claims handlers and that the IBNR has been judgementally selected by ARML's actuaries.
- 7.154 I understand that ARML considers all motor and household claims to be closed. In my view, given the age of the portfolio and that there are no outstanding motor or household claims, this is a reasonable assumption.
- 7.155 There have been no new commercial liability claims reported in last six years. As a result, I believe ARML's assumption that there will be no new claims reported within the Legacy Portfolio to be reasonable.
- 7.156 EWICL's London Market business is showing little development and no new claims have been reported in recent years. There remain 57 outstanding claims resulting from 11 cedants, mostly marine and aviation in nature. I understand from ARML that the last claim movement on any of these claims was in May 2015.
- 7.157 On the basis of the limited claims activity, I have no reason to believe that the reserves for the Legacy Portfolio lie outside a range of reasonable estimates.

The UKBG Portfolio

- 7.158 The table below shows the actuarial best estimate reserves for the UKBG Portfolio split by coverage period and between small and large claims.

Table 7.11: Actuarial best estimate reserves for the UKBG Portfolio as at 31 December 2018 (£m)

Coverage period	Small claims	Large claims	Total
LOD	0.0	0.0	0.0
DGP	0.9	4.8	5.6
SIP	8.0	13.1	21.2
Total	8.9	17.9	26.8

- 7.159 As can be seen from the table above, the majority of EWICL's reserves relate to the SIP coverage period.

- 7.160 ARML estimates EWICL's reserves by projecting claims to their ultimate position using standard actuarial techniques and by also discussing certain claims with claims handlers. ARML's reserving approach splits the data between small and large losses.
- 7.161 LOD outstanding claims are not material (£24k) and no further development is expected. There have been no new small claims since 2015 and the last new large claim was notified in 2016.
- 7.162 The DGP period has now expired on all policies. It is possible for DGP claims to arise, however, they will arise under the SIP exposure. There has only been one new small DGP claim reported since the beginning of 2017. For small claims, ARML is holding an IBNR of £0.2m, based on actuarial techniques and a pure IBNR of £0.1m which has been judgementally selected. I understand from ARML that there are eight large losses classified with outstanding reserves. ARML is holding no IBNR or pure IBNR for large DGP losses.
- 7.163 There are 34 large losses classified as SIP with outstanding reserves and ARML has informed me that it expects claims to continue to arise for this coverage period. ARML has told me that it has reviewed each of the large claims individually in conjunction with its claims team to select its IBNR. It has selected an IBNR of £5.5m.
- 7.164 For IBNR on small claims and pure IBNR of small and large claims, ARML has used standard actuarial techniques to project the claims. It has selected an IBNR of £2.2m for small claims and pure IBNR of £1.8m and £1.1m for small claims and large claims respectively.
- 7.165 I have performed an analysis to satisfy myself that the insurance liabilities are consistent with my expectations for insurance business of this nature. This analysis involved:
- A review of the reserve report as at 31 December 2018 produced by ARML's actuary
 - A review of the methods used to estimate the reserves compared with industry best practice
 - Discussions with individuals at ARML to understand the approaches used to estimate the reserves.
- 7.166 The process appears robust as concluded in paragraph 7.26. I have no reason to believe that the reserves for the UKBG Portfolio lie outside a range of reasonable estimates. In reaching this assessment, I have considered the following:
- ARML has utilised a standard approach for these types of liabilities in determining its estimates
 - ARML has conducted analysis in relation to its own experience that is appropriate
 - The outputs appear reasonable given my experience and expertise relating to claims reserving.

Solvency II technical provision adjustments – Legacy and UKBG Portfolios

- 7.167 The Solvency II technical provisions are the sum of the best estimate provisions, calculated on a cash flow basis under Solvency II, and a risk margin.
- 7.168 ARML has made a number of adjustments to the actuarial best estimate reserves to derive the Solvency II technical provisions for Existing EWICL Portfolio. These adjustments are as follows:
- Removal of any margins for prudence
 - Allowance for ENIDs
 - Allowance for expenses associated with the run-off of claims
 - Discounting the payments to allow for the time value of money, using the risk-free yield curves published by EIOPA at the relevant date
 - Allowance for a risk margin.

- 7.169 The table below shows the Solvency II Technical Provisions as at 31 December 2018, both gross and net of reinsurance:

Table 7.12: Solvency II Technical Provisions for the Existing EWICL Portfolio as at 31 December 2018

£m	Best estimate	Risk Margin	Solvency II Technical Provisions
Gross	27.5	2.8	30.3
Net	27.5	2.8	30.3

- 7.170 We note that there is uncertainty about the appropriate level of adjustments to make in order to estimate the technical provisions under Solvency II. ARML could have made other equally valid adjustments which would lead to different results.
- 7.171 The process for calculating Solvency II technical provisions appears appropriate and robust as concluded in paragraph 7.26. I have no reason to believe that the Solvency II technical provisions for the Existing EWICL Portfolio lie outside a range of reasonable estimates. In reaching this assessment, I have considered the following:
- ARML is making the adjustments I would expect in order to determine its Solvency II Technical Provisions
 - The outputs appear reasonable given my experience and expertise relating to Solvency II Technical Provisions.

8 Capital Requirements

- 8.1 In considering the solvency position, I have considered the following:
- the position of QBEUK in respect of its regulatory capital requirements both before and after the Scheme
 - my own stress testing of QBEUK's capital position to assess the likelihood of it not being able to meet its liabilities over the course of the run-off of the liabilities
 - the latest ORSA report produced by QBEUK
 - the position of EWICL in respect of its regulatory capital requirements both before and after the Scheme
 - my own stress testing of EWICL's capital position to assess the likelihood of it not being able to meet its liabilities over the course of the run-off of the liabilities following the Scheme
 - the latest ORSA report produced by EWICL.
- 8.2 It should be noted that one of the key limitations of the SCR is that it only represents the amount of capital that a firm is required to hold over the next year. When considering policyholder security, it is also important to consider whether a firm will have enough assets to meet its liabilities over the course of the run-off of the business, or at least whether the risk of that not being the case is remote.
- 8.3 As a result, whilst in this section I do consider the SCR for each firm and the coverage of its Own Funds above the SCR, I also conduct my own stress testing to assess the likelihood of each firm not being able to meet its liabilities over the course of the run-off of the liabilities following the Scheme.
- 8.4 In addition to this, I also consider the latest ORSA produced by each firm which sets out the firm's view of the resilience of its capital base to being able to meet policyholder needs.
- 8.5 It is the combination of the three of these items that I consider when assessing policyholder security, although the most weighting is applied to my own stress testing since it considers the position following the Scheme and also considers the position over the course of the run-off of the liabilities.

QBEUK

Capital strategy

- 8.6 I understand from QBEUK that it has a long term aim to maintain a buffer above its SCR at a target level and this is set out in its Capital Appetite Framework, which is reviewed annually. In addition, the Capital Appetite Framework sets out what actions to take if the coverage of its SCR drops below its long term target and what actions to take if the coverage of the SCR drops below 100%.
- 8.7 As per its Capital Appetite Framework there are a number of options available to QBEUK to improve its coverage of the SCR, including requesting additional capital from its parent.

Solvency II balance sheet

- 8.8 The simplified indicative Solvency II balance sheets for QBEUK as at 31 December 2018, both before the Scheme and after the Scheme, on the basis the Scheme had become effective, at 31 December 2018, are shown in the table below. For the avoidance of doubt, the balance sheets below have been prepared on an indicative basis following the QBEUK Brexit Transfer.

Table 8.1: Indicative QBEUK Solvency II balance sheets as at 31 December 2018 (£m)

	Before the Scheme	After the Scheme
Assets:		
Cash	187.9	187.9
Investments	2,757.9	2,757.9
Ceded Technical Provisions	762.9	674.8
Other assets	409.7	409.7
Total Assets:	4,118.4	4,030.3
Liabilities:		
Gross Technical Provisions (excl risk margin)	2,585.4	2,497.3
Risk margin	280.6	280.6
Other liabilities	288.0	288.0
Total Liabilities:	3,153.9	3,065.8
Excess of assets over liabilities	964.5	964.5
Adjustments	0.0	0.0
Eligible Own Funds	964.5	964.5

- 8.9 As discussed in paragraph 7.65, QBEUK does not estimate the Solvency II technical provisions solely in respect of the Transferring Portfolio and therefore, the difference between the Gross Technical Provisions figures between the two columns in the table above is equal to the outstanding claims reserves for the Transferring Portfolio. In addition, as discussed in paragraph 7.67, QBEUK has not estimated a risk margin solely for the Transferring Portfolio which is why the figures in the two columns in the table above are identical.
- 8.10 As can be seen from the above table, both the Gross Technical Provisions and the Ceded Technical Provisions reduce by £88.1m following the Scheme. This amount is the best estimate Solvency II Technical Provisions as estimated by QBEUK in respect of the Transferring Portfolio as at 31 December 2018, which is equal to the outstanding claims reserves as discussed in paragraph 8.9.

- 8.11 Since the QBE Brexit Transfer became effective on 1 January 2019, the first Solvency II balance sheet that has been submitted to the PRA is as at 31 March 2019. This is shown in the table below:

Table 8.2: QBEUK Solvency II balance sheet as at 31 March 2019 (£m)

	Before the Scheme
Assets:	
Cash	124.8
Investments	2,864.9
Ceded Technical Provisions	710.7
Other assets	321.7
Total Assets:	4,021.5
Liabilities:	
Gross Technical Provisions (excl risk margin)	2,378.9
Risk margin	274.7
Other liabilities	329.9
Total Liabilities:	2,983.1
Excess of assets over liabilities	1,038.4
Adjustments	0.0
Eligible Own Funds	1,038.4

- 8.12 It can be seen that Eligible Own Funds have increased between the indicative QBEUK Solvency II balance sheet at 31 December 2018 and the actual QBEUK Solvency II balance sheet at 31 March 2019. This is a result of profit generated by QBEUK between the development of the indicative balance sheet at 31 December 2018 and 31 March 2019. I have been informed by QBEUK that it calculates its SCR once a year and the latest SCR available for QBEUK is as at 31 December 2018. As the SCR at 31 March 2019 is not available, I have calculated the coverage ratios for QBEUK, as shown in table 8.4 below as at 31 December 2018.
- 8.13 I have considered the approach used to calculate the Solvency II balance sheets for QBEUK, including the Technical Provisions, and consider the approach and results to be reasonable. I understand from QBEUK that the approach used will not change following the Scheme.
- 8.14 I have also reviewed the calculation of the risk margin. The approach adopted is in line with that generally used in the market whereby the SCR is run-off in line with the liabilities. Consequently, I consider this to be appropriate.
- 8.15 QBEUK has confirmed that all its Eligible Own Funds as at 31 December 2018 are Tier 1, the highest tier of Own Funds, except for the deferred tax asset (which amounts to approximately £29.6m following the Scheme). The deferred tax asset is considered Tier 3 under Solvency II. I consider this allocation of Own Funds to the tiers to be reasonable.

Accounting balance sheet

- 8.16 The simplified accounting (UK Generally Accepted Accounting Principles, "UK GAAP") balance sheets for QBEUK as at 31 December 2018, both before the Scheme and after the Scheme, on the basis the Scheme had become effective, at 31 December 2018, are shown in the table below. For the avoidance of doubt, the balance sheets below have been prepared on an indicative basis following the QBEUK Brexit Transfer.

Table 8.3: UK GAAP balance sheets as at 31 December 2018 (£m)

	Before the Scheme	After the Scheme
Assets		
Cash	141.1	141.1
Investments	3,406.8	3,406.8
Reinsurers' share	770.2	682.1
Other assets	73.9	73.9
Total Assets	4,392.0	4,303.9
Liabilities		
Outstanding claims reserves	2,322.1	2,234.0
Unearned premium reserve	539.1	539.1
Other liabilities	420.0	420.0
Total Liabilities	3,281.2	3,193.1
Capital and reserves	1,110.8	1,110.8

- 8.17 As can be seen in the above table, the only movements as a result of the Scheme are reductions of £88.1m in the Reinsurer's share and Outstanding claims reserves. This amount is the reserves as booked by the QBEUK in respect of the Transferring Portfolio as at 31 December 2018.

Regulatory capital requirements

SCR and MCR

- 8.18 QBEUK uses an Internal Model approach to calculate its SCR and MCR. Its Internal Model has been approved for use by the PRA.
- 8.19 The following key risks, arising in the next 12 months, are modelled within QBEUK's Internal Model:
- **Earned reserve risk** – the risk of the best estimate claims reserves deteriorating i.e. the reserves are insufficient to cover the unpaid claims that have already occurred
 - **Unearned reserve risk** – the additional risk that the expected claims related to the unearned exposure in the closing balance sheet at year end are higher than expected at the beginning of the year.
 - **Underwriting risk** – the risk that premiums received for the business written in the following 12 months will not be sufficient to cover future claims and related costs arising from that business.

- **Natural catastrophe risk** – the risk of claims arising due to natural catastrophes affecting multiple insurance policies e.g. floods, windstorms, earthquakes etc.
 - **Man-made catastrophe risk** - the risk of claims arising due to man-made catastrophes such as fire or aggregation of liability claims
 - **Market risk** – the risk of adverse changes in net asset value as a result of movements in market risk variables such as interest rates, exchange rates, equity values etc. It also includes the exposure to investment credit risk (the risk of default or adverse movements in credit ratings of the assets)
 - **Reinsurance credit risk** - the risk that losses arise due to credit defaults and deteriorations in the credit quality of outstanding third party reinsurance
 - **Premiums credit risk** – the risk that Own Funds will be impacted due to unexpected failure to collect from counterparties (other than reinsurers) in the next year
 - **Operational risk** - the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events
 - **Intra group risk** – the risk of loss in value due to actions taken by another group entity.
- 8.20 I have reviewed the Capital Model Design and Operation document provided by QBEUK, which sets out its Internal Model approach, the governance around the Internal Model, the methodology and key assumptions for the key risk areas, and details of the use test.
- 8.21 I have considered the approach used to perform the Internal Model calculations for QBEUK and consider the approach to be reasonable and proportionate to the scale and complexity of its operations. I understand from QBEUK that the approach used to perform the Internal Model calculations will not change following the Scheme and consider this to be reasonable given the immaterial size of the Transferring Portfolio in the context of QBEUK.
- 8.22 I note that, whilst I have considered the methodology for each element described above, I have not reviewed the calculations or the assumptions used in detail.
- 8.23 In addition, I have reviewed the 2018 independent validation report for the Internal Model, which was produced by a firm of external actuaries. The firm of external actuaries is independent of the operation of the Internal Model. The independent validation report, a requirement for having an approved Internal Model, sets out in detail the validation that has been carried out on the Internal Model in order to ensure the results are appropriate.
- 8.24 As is to be expected, there are a number of limitations that have been highlighted in the independent validation report. However, there is nothing in the independent validation report that makes me believe that the SCR or MCR, as derived by the Internal Model, is materially misstated.
- 8.25 I understand that from QBEUK that it is currently making an application to get approval from the PRA to change some of the methodologies in its Internal Model. In my experience, it is commonplace for insurers to apply for such approvals as they seek to improve the quality of their Internal Model. I have been informed by QBEUK that these changes are not expected to materially impact QBEUK's SCR. I will provide further comment on this in my Supplementary Report.
- 8.26 I have seen the CVs of the individuals that are responsible for the internal model. Based on these and my interactions with those individuals, I am satisfied that the capital team at QBEUK has the necessary experience and expertise to develop an internal model and for me to rely on their work. In addition, I have seen the CV of the person responsible for the external validation. Based on that review, I am satisfied that he has the necessary experience and expertise to validate an internal model and for me to rely on his work.

As at 31 December 2018

- 8.27 The table below shows the coverage ratio of QBEUK, on the following bases at 31 December 2018:
- 1 Indicative coverage ratio following the QBE Brexit Transfer
 - 2 Hypothetical, on the basis that the Scheme had become effective at 31 December 2018

Table 8.4: Coverage ratios for QBEUK as at 31 December 2018 (£m)

	1	2
SCR	692.1	689.9
Eligible Own Funds to meet the SCR	964.5	964.5
SCR coverage ratio	139%	140%

Projected to the Effective Date

- 8.28 I have been informed by QBEUK that it does not expect its coverage ratio to change materially between 31 December 2018 and the Effective Date, and therefore it has not provided me with figures projected to the Effective Date. I am comfortable that relying on information as at 31 December 2018 is sufficient to form an opinion given that QBEUK has confirmed that it is not expecting to materially change its processes, methodologies or assumptions between 31 December 2018 and the Effective Date.

Stress tests

- 8.29 As discussed in paragraph 8.2, one of the key limitations of the SCR is that it only represents the amount of capital that a firm is required to hold over the next year.
- 8.30 As a result, in order to test the sufficiency of QBEUK's Own Funds over the run-off of the liabilities and to support my conclusions, I have undertaken a number of high-level stress tests as set out in the paragraphs below.
- 8.31 I have assessed the resilience of QBEUK's capital position against a number of scenarios. I have selected the scenarios below based on my review of QBEUK's business structure and risk profile. The scenarios that I have considered represent, in my opinion, the risks that could most significantly impact QBEUK's financial and capital strength. The scenarios I have considered in my stress tests are as follows:
- Deterioration of QBEUK's net best estimate technical provisions
 - Deterioration in QBEUK's combined ratio for the upcoming underwriting year
 - Financial losses from significant catastrophe events
 - Reduction in the reinsurance asset as a result of default by reinsurers
 - Deterioration in the value of QBEUK's investment portfolio
 - Deterioration of QBEUK's net best estimate technical provisions combined with a reduction in the reinsurance asset.

Net best estimate technical provisions

- 8.32 QBEUK's net technical provisions (excluding the Solvency II risk margin) as at 31 December 2018 (on a hypothetical basis following the Scheme) are £1,822m. In order to reduce its SCR coverage ratio to 100% or below, QBEUK would need to experience a deterioration in the region of 15% of its net best estimate technical provisions. QBEUK has estimated there to be a likelihood of less than 6% that the reserves of QBEUK could deteriorate by this amount which I consider to be unlikely. In reaching this conclusion, I have considered the following:
- I have reviewed the approach to this estimation and it is line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation.
 - I have reviewed the outputs of the estimation against other firms that have provided similar estimations.
 - QBEUK has a well-diversified portfolio of liabilities and so a 15% deterioration would need to correspond into a much more severe deterioration in a small number of classes, either simultaneously or gradually over time.
- 8.33 In order for QBEUK's assets to fall beneath its liabilities, QBEUK would need to experience a deterioration in the region of approximately 53% of its net best estimate technical provisions (excluding the Solvency II risk margin). QBEUK has estimated there to be a likelihood of less than 0.5% that the reserves of QBEUK could deteriorate by this amount. Based on my experience, I consider this likelihood to be remote.

Combined ratio

- 8.34 For the upcoming underwriting year, QBEUK has assumed a combined ratio of 97%. In order to reduce the coverage ratio to 100% or below, QBEUK would need to experience an increase in its combined ratio from 97% to 132% and QBEUK has estimated that this has a likelihood of less than 0.5%, which I consider to be remote. In reaching this conclusion, I have reviewed the approach to this estimation and it is line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation.
- 8.35 Since a scenario that would reduce assets to be less than liabilities would need to be more extreme than the scenario discussed in paragraph 8.34, I consider the likelihood of assets falling beneath liabilities as a result of an increase in the combined ratio for the upcoming underwriting year to be remote.

Catastrophe

- 8.36 In QBEUK's ORSA report, it has considered its exposure to a number of Lloyd's of London's "Realistic Disaster Scenarios". The most severe of these is a pandemic which QBEUK has estimated would cause a loss of £249m. Even in this scenario, QBEUK is expected to maintain a coverage ratio above 100% of its SCR. Therefore, it would need a scenario more extreme than this to reduce its coverage beneath the SCR. I consider the likelihood of a loss of £249m to be remote based on the fact that the scenario is designed to be deliberately extreme.
- 8.37 Since a scenario that would reduce assets to be less than liabilities would need to be more extreme than the scenario discussed in paragraph 8.36, I consider the likelihood of assets falling beneath liabilities as a result of a catastrophe to be remote.

Reinsurance recoveries

- 8.38 The reinsurance recoveries at 31 December 2018 (on a hypothetical basis following the Scheme) amount to £675m. In order to reduce the coverage ratio to 100% or below, QBEUK would need to experience a reduction in the value of its reinsurance recoveries in the region of 40% as a result of default by the reinsurers. QBEUK has estimated there to be a likelihood of less than 0.5% that the reinsurance recoveries of QBEUK could deteriorate by this amount which I consider remote. In reaching this conclusion, I have considered the following:
- I have reviewed the approach to this estimation and it is line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation.
 - QBEUK has a well-diversified portfolio of reinsurers with high credit ratings.

- 8.39 Since a scenario that would reduce assets to be less than liabilities would need to be more extreme than the scenario discussed in paragraph 8.38, I consider the likelihood of assets falling beneath liabilities as a result of reinsurance default to be remote.

Investments

- 8.40 The investments held by QBEUK at 31 December 2018 (on a hypothetical basis following the Scheme) amount to £2,758m. In addition, it has projected cash of £188m. In order to reduce the coverage ratio to 100% or below, QBEUK would need to experience a reduction in the value of its investments (excluding cash) in the region of 10% and QBEUK has estimated that this has a likelihood of less than 0.5%, which I consider remote. In reaching this conclusion, I have considered the following:
- I have reviewed the approach to this estimation and it is line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation.
 - QBEUK's investment strategy is relatively cautious as the majority of its funds are invested in high quality liquid fixed income assets.

- 8.41 Since a scenario that would reduce assets to be less than liabilities would need to be more extreme than the scenario discussed in paragraph 8.40, I consider the likelihood of assets falling beneath liabilities as a result of reductions in investment value to be remote.

Combination of net best estimate technical provisions and reinsurance recoveries

- 8.42 In order for QBEUK's assets to fall beneath the liabilities following the Scheme as a result of a deterioration in a combination of its net best estimate technical provisions and its reinsurance asset, it would require a deterioration of £965m across a combination of the two. There are an infinite number of combinations that could achieve this so, in my test, I have considered the following three options as a sample of those available:
- a £500m (27%) deterioration in the net best estimate technical provisions and a £465m (69%) reduction of its reinsurance asset
 - a £700m (39%) deterioration in the net best estimate technical provisions and a £265m (39%) reduction of its reinsurance asset
 - a £900m (49%) deterioration in the net best estimate technical provisions and a £65m (10%) reduction of its reinsurance asset
- 8.43 For each of these scenarios, QBEUK has estimated there to be a likelihood of less than 0.5% that such a scenario could occur.

8.44 I consider the likelihood of such a combination to be remote. In reaching this conclusion, I have considered the following:

- I have reviewed the approach to this estimation and it is in line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation.
- Both components of each of the scenarios would need to occur simultaneously or close to each other so that QBEUK was unable to recover.

Summary of my testing

- 8.45 As shown in table 8.4, QBEUK will maintain a buffer in relation to the SCR following the Scheme. The buffer is designed to ensure that it does not regularly breach its respective capital requirements. The testing above demonstrates the types of events that would need to happen in order for Own Funds to fall beneath the SCR. In addition, those events would need to be more severe for the assets to fall beneath liabilities over the course of the run-off of the liabilities.
- 8.46 Further, the testing that I have undertaken which I have described in paragraphs 8.29 to 8.44 demonstrates to me that, should the Scheme become effective, the likelihood of the assets of QBEUK falling beneath its liabilities over the course of the run-off of the liabilities is remote.

ORSA

- 8.47 I have been provided with a copy of the report outlining QBE EO's most recent ORSA. The ORSA covers all the operating subsidiaries of QBE EO, including QBEUK, which at the time was known as QIEL. The document is dated 8 March 2018 and has been approved by QBE EO's Board and QIEL's Board. This represents a forward-looking assessment of the risk profile and capital requirements.

Stress tests within the ORSA report

- 8.48 The ORSA projects that the coverage of QBEUK's SCR will be maintained above its target set out in the Capital Appetite Framework for the period considered in the ORSA. I have reviewed the process by which QBEUK has projected the coverage of its SCR and believe it to be reasonable. It follows that I consider the projected coverage of the SCR to be reasonable.
- 8.49 QBEUK has conducted various stress and scenario tests within its ORSA to test the robustness of its capital base. The stress and scenario testing cover a wide range of risks that QBEUK is exposed to. The stress and scenario testing that QBEUK has undertaken demonstrates that only in extreme scenarios does it fail to have sufficient capital to meet its SCR. Furthermore, there were no stresses considered that reduce the level of assets below the level of liabilities. I consider the range of stresses and scenarios that QBEUK has considered to be reasonable.

Access to capital

- 8.50 QBEUK has informed me that it has the ability to request additional capital from its parent in the event that its target capital has been breached and the other options available to it have been exhausted.
- 8.51 At 31 December 2018, QBE EO had assets of approximately £4,004m and liabilities of approximately £1,284m so had substantial capital that it could use to support QBEUK should it so wish.

EWICL

Capital strategy

- 8.52 I understand from EWICL that it has a long-term aim to maintain a buffer above its SCR at a target level and this is set out in its Risk Appetite Statement, which is reviewed annually. I note that the increase that EWICL applies to its SCR in order to achieve the buffer is significantly higher than the corresponding increase applied by QBEUK in percentage terms. In addition, the Risk Appetite Statement sets out the actions EWICL will consider should the coverage of its SCR drop below 100%.
- 8.53 As per its Risk Appetite Statement there are a number of options available to EWICL to improve its coverage of the SCR, including requesting additional capital from its existing shareholders or third-party investors.

Solvency II balance sheet

- 8.54 The simplified Solvency II balance sheets for EWICL before the Scheme and after the Scheme, on the basis the Scheme had become effective, at 31 December 2018 are shown in the table below.

Table 8.5: EWICL Solvency II balance sheets as at 31 December 2018 (£m)

Reserve	Before the Scheme	After the Scheme
Assets:		
Cash	0.6	0.6
Investments	62.9	177.6
Ceded Technical Provisions	0.0	0.0
Other assets	0.1	0.3
Total Assets:	63.6	178.6
Liabilities:		
Gross Technical Provisions (excl risk margin)	27.5	98.2
Risk margin	2.8	14.2
Other liabilities	0.2	0.3
Total Liabilities:	30.5	112.7
Excess of assets over liabilities	33.2	65.8
Adjustments	0.0	0.0
Eligible Own Funds	33.2	65.8

- 8.55 As a result of the Scheme, the Technical Provisions (excluding risk margin) will increase by the amount in the Transferring Portfolio. In addition to this, as the SCR will increase which can be seen in tables 8.7 and 8.8 below, the risk margin will also increase.
- 8.56 I have reviewed the calculation of the risk margin. The approach adopted is in line with that generally used in the market whereby the SCR is run-off in line with the liabilities. Consequently, I consider the approach used to calculate the risk margin to be appropriate. It follows from this that I consider the quantum of risk margin before and after the Scheme as shown in Table 8.5 to be appropriate.

- 8.57 In addition, ILS will transfer assets from Cell G to EWICL in order to ensure that it meets its capital target.
- 8.58 I have considered the approach used to calculate the Solvency II balance sheets for EWICL, including the Technical Provisions, and consider the approach and results to be reasonable. I understand from EWICL that the approach used will not change following the Scheme.
- 8.59 EWICL has confirmed that all its Eligible Own Funds at 31 December 2018 are Tier 1, the highest tier of Own Funds. I have reviewed this allocation of all Own Funds to Tier 1 and consider it to be reasonable. In addition, following the Scheme, I understand from EWICL that all EWICL's Own Funds will be classified as Tier 1.

Accounting balance sheet

- 8.60 The simplified accounting (UK GAAP) balance sheets for EWICL before the Scheme and after the Scheme, on the basis the Scheme had become effective, at 31 December 2018 are shown in the table below.

Table 8.6: EWICL UK GAAP balance sheets as at 31 December 2018 (£m)

Reserve	Before the Scheme	After the Scheme
Assets		
Cash	0.6	0.6
Investments	62.9	177.6
Reinsurers' share	0.0	0.0
Other assets	0.1	0.3
Total Assets	63.6	178.6
Liabilities		
Outstanding claims reserves	27.9	102.4
Unearned premium reserve	0.0	0.0
Other liabilities	0.2	0.3
Total Liabilities	28.1	102.7
Capital and reserves	35.5	75.9

- 8.61 The movements between the accounting balance sheets above as a result of the Scheme are similar to those in the Solvency II balance sheets.

Regulatory capital requirements

SCR and MCR

- 8.62 EWICL uses a Standard Formula approach to calculate its SCR and MCR.
- 8.63 The following key risks are modelled within EWICL's calculation of the Standard Formula:
- **Reserve risk** – the risk of the best estimate claims reserves deteriorating i.e. the reserves are insufficient to cover the unpaid claims that have already occurred

- **Market risk** – the risk of adverse changes in EWICL's net asset value as a result of movements in market risk variables such as interest rates, exchange rates, equity values etc. It also includes the exposure to investment credit risk (the risk of default or adverse movements in credit ratings of the assets)
 - **Counterparty default risk** – the risk of losses due to default or downgrade of reinsurers or due to non-payment of receivables from third parties
 - **Operational risk** - the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.
- 8.64 EWICL has assessed that the Standard Formula is appropriate for calculating its regulatory capital requirements prior to the Scheme. Its assessment concluded the following:
- The non-life risk for UKBG is overstated based on a calculation it performed to understand the capital it believed it required to service those policyholders over their lifetime – this is primarily because the UKBG class is in the Miscellaneous Financial Loss class, which has the most penal capital charges
 - The investments are not complex and the Standard Formula provided a reasonable measure of market risk
 - The counterparty default risk was in line with its exposure characteristics
 - The operational risk was a simplistic measure but EWICL had no evidence to support the use of an alternative method
- 8.65 EWICL has not yet undertaken an assessment of whether the Standard Formula is appropriate for calculating the regulatory requirements following the Scheme as Transferring Portfolio does not yet reside in EWICL.
- 8.66 The risks of any entity are unlikely to perfectly match the design of the Standard Formula as it has been designed to be used by a wide range of insurance companies. However, as discussed in paragraph 8.52, EWICL maintains a buffer in excess of its SCR to allow for the limitations in using the Standard Formula. In addition to this, the Standard Formula is widely used and is also used by larger more complex firms than EWICL. Further to this, in my view and based on my experience, the costs of building an Internal Model and the time involved would be disproportionate to the size and complexity of EWICL.
- 8.67 In order to address the limitations in the Standard Formula, I have undertaken various stress tests to test the robustness of the capital base of EWICL over the course of the run-off of the liabilities. These are discussed in paragraphs 8.80 to 8.92.
- 8.68 I have considered the approach used to perform the Standard Formula calculations for EWICL prior to the Scheme and consider the approach to be reasonable and proportionate to the scale and complexity of its operations. I understand from EWICL that its approach to undertaking the Standard Formula calculations for EWICL will not change after the Scheme, and I consider this to be reasonable.
- 8.69 I note that whilst I have considered the methodology for each element described above, I have not reviewed the calculations in detail. I have considered the final results of the calculation, and I have not identified any reason to believe the calculated SCR materially understates the capital required by EWICL prior to the Scheme.

As at 31 December 2018

- 8.70 The table below shows the coverage ratio of EWICL, on the following bases at 31 December 2018:
- 1 Actual coverage ratio
 - 2 Hypothetical, on the basis that the Scheme had become effective at 31 December 2018

Table 8.7: Coverage ratios for EWICL as at 31 December 2018 (£m)

	1	2
SCR	17.6	38.2
Eligible Own Funds to meet the SCR	33.2	65.8
SCR coverage ratio	188%	173%

- 8.71 As can be seen in the table above, EWICL's coverage ratio is expected to reduce slightly as a result of the Scheme.
- 8.72 It can also be seen from the table above that EWICL has substantial Own Funds in excess of the SCR both before and after the Scheme.

Projected to the Effective Date

- 8.73 The table below shows the coverage ratio of EWICL, on the following bases projected to the Effective Date:
- 3 On the basis the Scheme has not become effective on that date
 - 4 On the basis the Scheme becomes effective on that date

Table 8.8: Coverage ratios for EWICL as at the Effective Date (£m)

	3	4
SCR	13.0	32.0
Eligible Own Funds to meet the SCR	34.4	55.2
SCR coverage ratio	264%	173%

- 8.74 The movements in the coverage ratio at the Effective Date as a result of the Scheme shown in the table above are similar to the movements as at 31 December 2018 shown in Table 8.7. The table above also shows that EWICL has substantial Own Funds in excess of the SCR both before and after the Scheme.

Coverage ratio using my estimate of the reserves

- 8.75 As discussed in paragraphs 7.126 to 7.136, I undertook an exercise to determine my own estimate of the reserves for the Transferring Portfolio. As shown in table 7.6, my estimate is £7.4m higher than AMRL's estimate.
- 8.76 EWICL has undertaken a high-level calculation to assess its coverage of its SCR following the Scheme, as at the Effective Date using my estimate of the reserves. In particular, for the purposes of this exercise, EWICL has increased its reserves in respect of the Transferring Portfolio as at 31 December 2018 by £7.4m. EWICL has then projected the SCR and Own Funds as at the Effective Date.

8.77 The following table shows the results of EWICL's calculations using my estimate of the reserves:

Table 8.9: Coverage ratio for EWICL as at the Effective Date using my estimate of reserves (£m)

After the Scheme	
SCR	33.9
Eligible Own Funds to meet the SCR	48.4
SCR coverage ratio	143%

8.78 The table above shows that, based on using my estimate of the reserves, EWICL continues to have Own Funds in excess of the SCR. In addition, EWICL would continue to have enough capital to meet its capital target.

8.79 As a run-off insurer, any future capital extractions are subject to the approval of the PRA.

Stress tests

8.80 As discussed in paragraph 8.2, one of the key limitations of the SCR is that it only represents the amount of capital that a firm is required to hold over the next year.

8.81 As a result, in order to test the sufficiency of EWICL's Own Funds and to support my conclusions, I have undertaken a number of high-level stress tests as set out in the paragraphs below. In testing the sufficiency of Own Funds, I have used the estimate of Own Funds and the SCR derived using my estimate of the reserves (as shown in table 8.9) as a starting point. To that end, the stresses below have already allowed for a reduction in Own Funds when compared to EWICL's expectation of the Own Funds.

8.82 When considering the stresses below, it should be noted that the percentages given represent the percentage deterioration that would be required based on the data at the Effective Date. In the normal course of business, assuming EWICL pays off claims in line with its expectations, its Own Funds would be expected to grow as a result of investment income being higher than the expenses required to run the business assuming that capital is not extracted. As a result, if the deteriorations were to happen at some future point after the Effective Date, the percentage deteriorations required to breach the various thresholds would be expected to be higher assuming EWICL has made profits in between the Effective Date and that point in time.

8.83 I have assessed the resilience of EWICL's capital position against a number of scenarios. I have selected the scenarios below based on my review of EWICL's business structure and risk profile. The scenarios that I have considered represent, in my opinion, the risks that could most significantly impact EWICL's financial and capital strength. The scenarios I have considered in my stress tests are as follows:

- Deterioration of EWICL's net best estimate technical provisions from the UKBG Portfolio
- Deterioration of EWICL's net best estimate technical provisions from the Transferring Portfolio
- Deterioration in the value of EWICL's investment portfolio
- A combination of a deterioration in EWICL's net best estimate and a deterioration in the value of EWICL's investment portfolio.

UKBG Portfolio

- 8.84 EWICL's net technical provisions (excluding the Solvency II risk margin) projected to the Effective Date (on a hypothetical basis following the Scheme) in respect of the UKBG Portfolio are £19.4m. In order to reduce its SCR coverage ratio to 100% or below, EWICL would need to experience a deterioration in the region of 75% of its net best estimate technical provisions. EWICL has estimated there to be a likelihood of less than 0.5% that the reserves of the UKBG Portfolio could deteriorate by this amount, which I consider remote. In reaching this conclusion, I have considered the following:
- I have reviewed the approach to this estimation and it is in line with other approaches seen in the market. This satisfies me that I am able to place reliance on this estimation
 - ARML, on behalf of EWICL, has undertaken detailed reviews of the claims reserves on the UKBG Portfolio in order to understand the risks that are inherent. I have set out my conclusions in respect of the reserve strength of the UKBG Portfolio in paragraph 7.166, where I have concluded that the reserves lie within a reasonable range of estimates.
- 8.85 Since a scenario that would reduce assets to be less than liabilities would need to be more extreme than the scenario discussed in paragraph 8.84, I consider the likelihood of assets falling beneath liabilities (and, therefore of EWICL being unable to pay claims as they fall due) as a result of a deterioration in the best estimate technical provisions for the UKBG Portfolio to be remote.

Transferring Portfolio

- 8.86 EWICL's net technical provisions (excluding the Solvency II risk margin) projected to the Effective Date (on a hypothetical basis following the Scheme) in respect of the Transferring Portfolio are £65.2m, using my estimate of the reserves. In order to reduce its SCR coverage ratio to 100% or below, EWICL would need to experience a deterioration in the region of 22% of its net best estimate technical provisions. In my opinion, given the uncertainty around the claims liabilities in the Transferring Portfolio, a deterioration by this amount is within the range of reasonably foreseeable outcomes, although it would lead to technical provisions higher than those estimated by QBEUK in respect of the Transferring Portfolio.
- 8.87 However, even in this scenario, EWICL would still have substantial Own Funds in excess of its MCR (£48.4m Own Funds compared to its MCR of £9.8m). In order to reduce its MCR coverage ratio to 100% or below, EWICL would need to experience a deterioration in the region of 59% (or £38.7m). Additionally, in order to reduce assets such that they are below the liabilities, EWICL would need to experience a deterioration in the region of 74% (or £48.4m). Based on my experience, I consider the likelihood of deteriorations of 59% or 74% to be remote. In reaching this conclusion, I have considered the following:
- The type of scenario that would see a 74% deterioration in the net best estimate technical provisions would be if the average cost per claim on mesothelioma claims were to increase to approximately £117k from my estimate of £53.5k
 - ARML has undertaken a detailed review of the claims reserves on the Transferring Portfolio in order to understand the risks that are inherent. I have reviewed this estimation and provided my conclusions in paragraph 7.98 where I have concluded that ARML's estimate lies within a reasonable range of reserves.
 - In addition, I have undertaken my own high-level estimation of the reserves to assess what I believe is a best estimate. This is the reserve figure that has been used to calculate the Own Funds that I have stressed in this test.
- 8.88 Given the above, it is my view that the likelihood that EWICL will have insufficient capital to pay claims to its policyholders as they fall due as a result of a deterioration in the best estimate technical provisions for the Transferring Portfolio to be remote.

Investments

- 8.89 The projected investments held by EWICL at the Effective Date (on a hypothetical basis following the Scheme) amount to £56.1m. In addition, it has cash of £91.4m. In order to reduce assets beneath liabilities, EWICL would need to experience a reduction in the value of its investments (excluding cash) in the region of 86%.
- 8.90 I consider the likelihood of such a deterioration to be remote. In reaching this conclusion I have considered the following:
- EWICL has informed me that following the Scheme it expects its investment portfolio to be solely in government and corporate debt instruments, which is also the case now.
 - EWICL has informed me that 98% of its current debt instruments have credit ratings between AAA and BBB- and that 91% have credit ratings of A or above. I expect EWICL to hold a similar proportion of assets in highly rated debt instruments after the Scheme since I have been informed by EWICL that the investment strategy will not change.
 - Whilst highly rated debt instruments can and do lose value over the short term, they are generally quite stable in the medium and long term.

Combination of net best estimate technical provisions and investments

- 8.91 In order for EWICL's assets to fall beneath the liabilities following the Scheme as a result of a deterioration in a combination of its net best estimate technical provisions and the value of its investments, it would require a deterioration of £48m across a combination of the two. There are an infinite number of combinations that could achieve this so, in my test, I have considered the following three options as a sample of those available:
- A £29m (34%) deterioration in the net best estimate technical provisions and a £19m (35%) deterioration in its investment portfolio.
 - A £39m (46%) deterioration in the net best estimate technical provisions and a £9m (17%) deterioration in its investment portfolio.
 - A £19m (23%) deterioration in the net best estimate technical provisions and a £29m (52%) deterioration in its investment portfolio.
- 8.92 I consider the likelihood of any of these combinations occurring (and, therefore, of EWICL being unable to pay claims as they fall due) to be remote. In reaching this conclusion, I have considered the following:
- Both components of the stress would need to occur simultaneously or close to each other so that EWICL was unable to recover
 - ARML, on behalf of EWICL has undertaken detailed reviews of the claims reserves on the Transferring Portfolio and the Existing EWICL Portfolio in order to understand the risks that are inherent
 - The type of scenario that would see a 34% deterioration (for instance in the first option above) in the net best estimate technical provisions would be if the average cost per claim on mesothelioma claims were to increase to approximately £92k from my estimate of £53.5k, which is a significant increase in itself. This is before combining this stress with a deterioration in the investment portfolio
 - For the second option above, whilst the investment stress is more likely, the deterioration in the net best estimate technical provisions is more unlikely.
 - For the third option above, whilst the deterioration in the net best estimate technical provisions is less likely, it would still require, for instance, the average cost per claim on mesothelioma claims were to increase to approximately £80k from my estimate of £53.5k. This is before combining the stress with a more severe investment deterioration.

Summary of my testing

- 8.93 As shown in tables 8.7 and 8.8, EWICL will maintain a buffer in relation to the SCR following the Scheme. The buffer is designed to ensure that it does not regularly breach its regulatory capital requirements.
- 8.94 Based on using my estimate of the reserves, that buffer would be reduced as shown in table 8.9. The testing above demonstrates the types of events that would need to happen in order for Own Funds to fall beneath the SCR, using my estimates. I have additionally shown the more severe types of events that would need to happen for assets to fall beneath the liabilities over the course of the run-off of the liabilities (and therefore threaten claim payments).
- 8.95 Further, the testing that I have undertaken which I have described in paragraphs 8.80 to 8.92 demonstrates to me that, should the Scheme become effective, the likelihood of the assets of EWICL falling beneath its liabilities over the course of the run-off of the liabilities, and of EWICL therefore being unable to pay claims as they fall due, is remote.

ORSA

- 8.96 I have been provided with a copy of the report outlining EWICL's most recent ORSA. The document is dated 11 July 2018 and has been approved by EWICL's Board. This represents EWICL's forward looking assessment of its risk profile. It should be noted that EWICL's ORSA covers only the business prior to the Scheme. This is because at the time it was written, it was not confirmed that EWICL would be accepting the Transferring Portfolio.

Stress tests within the ORSA report

- 8.97 EWICL has conducted various stress and scenario tests within its ORSA to test the robustness of its capital base. The stress and scenario testing covers a number of risks that EWICL is exposed to. I consider the range of stresses and scenarios that EWICL has considered to be reasonable. I have reviewed the approach undertaken in relation to these stresses and consider the approach and key assumptions to be reasonable.
- 8.98 None of the stress tests undertaken reduced EWICL's coverage of its SCR to below 100%.
- 8.99 EWICL also analysed what it might take for Own Funds to reduce below both the SCR and the MCR. Whilst those scenarios are possible, I consider them to be unlikely. For instance, EWICL has estimated that it would require a 38% increase in the Technical Provisions for the Own Funds to be beneath the SCR, or a 94% increase in Technical Provisions for the Own Funds to be beneath the MCR.

Access to capital

- 8.100 EWICL has informed me that it would only request additional capital from ILS in the event that its target capital has been breached and the other options available to it have been exhausted.
- 8.101 However, in that situation EWICL is able to request additional capital from ILS. At 31 December 2018, ILS had assets of approximately \$660m and liabilities of approximately \$290m so had substantial capital that it could use to support EWICL should it so wish.
- 8.102 In addition, in the event that ILS has insufficient capital to support EWICL, it has the ability to request additional capital from its parent, ILS Property & Casualty Master Fund Ltd, ILS has provided me with a letter from its investment manager evidencing that ILS Property & Casualty Master Fund Ltd has access to a substantial amount of committed capital from its investors. I understand from the documentation provided to me that this committed capital substantially exceeds the capital requirement set out in Table 9.2. I further understand from ILS and its external asset managers that these capital commitments are legally binding and irrevocable.

- 8.103 I note that there is no legal obligation for either ILS or ILS Property & Casualty Master Fund Ltd to support EWICL should additional funds be required. However, my view is that there is a substantial incentive for them to do so. This is because Armour's business model is reliant on its ability to service and pay claims on the run-off portfolios that it manages. As a result, if an entity such as EWICL suffered significant financial difficulties, Armour would lose credibility in the market and be restricted in its ability to purchase further portfolios.

9 Policyholder security

- 9.1 In this section, I describe the effect of the Scheme on each group of policyholders with regards to security, including under insolvency, and explain how I have reached my conclusions.

Impact of the Scheme on the solvency positions of the affected companies

- 9.2 The capital requirements and the approach to capital modelling of QBEUK and EWICL are discussed in Section 8.
- 9.3 The tables below show the coverage of the SCR before and after the Scheme for each of QBEUK and EWICL. The information in the tables below is a repeat of the information in Section 8 which is shown here for convenience.
- 9.4 The coverage of the SCR before and after the Scheme for QBEUK is as at 31 December 2018. As mentioned in paragraph 8.28, QBEUK has not provided me with figures projected to the Effective Date as it does not expect the coverage ratio to change materially between 31 December 2018 and the Effective Date.

Table 9.1: QBEUK coverage ratios at 31 December 2018 (£m)

	Before the Scheme	After the Scheme
SCR	692.5	690.4
Eligible Own Funds to meet the SCR	964.5	964.5
SCR coverage ratio	139%	140%

- 9.5 QBEUK's coverage of its SCR is materially unchanged by the Scheme becoming effective. There are two reasons for this:
- The Transferring Portfolio is immaterial in the context of QBEUK
 - The economic risk in relation to the Transferring Portfolio has already transferred out of QBEUK as a result of the LPTAs. The Scheme simply provides QBEUK with the legal transfer of these liabilities.

Table 9.2: EWICL coverage ratios at the Effective Date (£m)

Before the Scheme	After the Scheme –	After the Scheme –	After the Scheme –
	using ARML	– using my reserve estimate	using QBEUK reserve estimate
SCR	13.0	32.0	33.9
Eligible Own Funds to meet the SCR	34.4	55.2	48.4
SCR coverage ratio	264%	173%	143%
			116%

- 9.6 As can be seen in the table above, EWICL's Own Funds and the coverage of its SCR is dependent on the net best estimate technical provisions selected.
- 9.7 As discussed in paragraph 8.52, EWICL aims to maintain a buffer above its SCR. As discussed in paragraphs 8.71 and 8.72, that buffer is slightly reduced as a result of the Scheme. However, EWICL still maintains substantial Own Funds in comparison to its SCR based on EWICL's reserve estimate. Using my estimate of the reserves, this buffer is reduced, however it remains in line with EWICL's target capital ratio. The testing I have undertaken in paragraphs 8.80 to 8.92 shows that the likelihood of the EWICL's assets falling below its liabilities over the course of the run-off of the liabilities is remote.
- 9.8 Furthermore, if EWICL has insufficient capital it has the ability to request additional capital from ILS and, for the reason discussed in paragraph 8.103, I believe that ILS and its parent have a substantial incentive to provide that support.
- 9.9 Based on the above, I am of the opinion that EWICL is sufficiently capitalised to meet policyholder obligations over the course of the run-off of the Transferring Portfolio and the Existing EWICL Portfolio. In addition, I am of the opinion that QBEUK is sufficiently capitalised to meet policyholder obligations over the course of the run-off of the Remaining Portfolio. Note that these conclusions are predicated on the fact that ILS Property & Casualty Master Fund Ltd, ILS and Armour will provide support to EWICL, should additional funds be required. However, even if EWICL was not able to receive additional funds from ILS Property & Casualty Master Fund Ltd, ILS or Armour, my view is that the likelihood of EWICL being unable to pay claims as they fall due is remote.

Impact of the Scheme on the security of the transferring policyholders

- 9.10 The transferring policyholders would lose the following protections as a result of the Scheme:
- The security of QBEUK
 - In respect of the Autumn Portfolio, the security of TMR as the reinsurer plus Cell G of ILS as a retrocessionaire as the Autumn LPTA would no longer be in place following the Scheme.
 - In respect of the Chestnut Portfolio, the security of Cell G of ILS as reinsurer as the Chestnut LPTA would no longer be in place following the Scheme.
- 9.11 However, they would gain the security associated with EWICL. EWICL has a lower Own Funds in absolute terms compared to QBEUK but the coverage of the SCR for EWICL is expected to be higher in percentage terms following the Scheme than QBEUK, and in a similar region to QBEUK using my estimate of the reserves.

- 9.12 On the face of it, transferring from a large insurer to a smaller insurer and losing the reinsurance protections provided by the LPTAs appears to have an adverse impact on the security of the transferring policyholders. However, my opinion is that it is not a material adverse impact for the following reasons:
- The stress testing I have conducted demonstrates that only in remote scenarios does EWICL not expect to be able to meet its liabilities
 - As described in paragraph 9.9, I am of the opinion that EWICL will be sufficiently capitalised in order to meet policyholder obligations over the course of the run-off of the Transferring Portfolio and the Existing EWICL Portfolio
 - As set out in paragraphs 8.100 to 8.103, EWICL has the ability to request capital from ILS should it get into financial difficulties and require it
 - As explained in paragraph 8.103, there is a substantial incentive for ILS Property & Casualty Master Fund Ltd, ILS and Armour to support EWICL should additional funds be required
 - EWICL will continue to be regulated by the PRA and any capital extractions would need to be approved by the PRA
 - The reinsurance protections arising from the LPTAs were put in place for the purpose of conducting the Scheme. Without the Scheme, those LPTAs would not have been in place.
- 9.13 Both QBEUK and EWICL are incorporated in the UK and so are both subject to the same wind-up regulations. The transferring policyholders are direct policyholders of QBEUK pre-Scheme and will become direct policyholders of EWICL post-Scheme. As a result, the transferring policyholders would benefit from the same legal protections in the event of wind-up of EWICL post-Scheme compared to the event of wind-up of QBEUK pre-Scheme.
- 9.14 The transferring policyholders' rights in respect of the FSCS in the event of the insolvency of EWICL post-Scheme will be identical to their rights in the event of the insolvency of QBEUK pre-Scheme. As a result, these rights will not change as a result of the Scheme.
- 9.15 It follows from the preceding paragraphs that, even though the monetary value of the funds that the transferring policyholders will have access to will reduce, my opinion is that I do not expect there to be a material adverse impact on the transferring policyholders in relation to security, including under insolvency, as a result of the Scheme.

Impact of the Scheme on the security of the policyholders remaining in QBEUK

- 9.16 As discussed in paragraph 9.5, QBEUK's coverage of its SCR is materially unchanged by the Scheme becoming effective.
- 9.17 In addition, the Scheme will have no material impact on the protections afforded to the policyholders remaining in QBEUK in the event of insolvency of QBEUK, including access to the FSCS.
- 9.18 As a result, the policyholders remaining in QBEUK will not be materially affected by the Scheme in terms of security, including under insolvency.

Impact of the Scheme on the security of the existing policyholders in EWICL

- 9.19 As discussed in paragraph 9.6, EWICL's coverage of its SCR reduces as a result of the Scheme. Furthermore, due to the nature of the liabilities, the addition of the Transferring Portfolio increases the volatility in EWICL.
- 9.20 Despite this, my opinion is that this does not create a material adverse impact for the following reasons:
- The absolute value of Own Funds has increased. In addition to this, the absolute value of the buffer in excess of the SCR has increased.
 - The stress testing I have conducted demonstrates that only in remote scenarios does EWICL not expect to be able to meet its liabilities
 - As described in paragraph 9.9, I am of the opinion that EWICL will be sufficiently capitalised in order to meet policyholder obligations over the course of the run-off of the Transferring Portfolio and the Existing EWICL Portfolio
 - As set out in paragraphs 8.100 to 8.103, EWICL has access to considerable capital should it get into financial difficulties and require it
 - As explained in paragraph 8.103, there is a substantial incentive for ILS and Armour to support EWICL should additional funds be required
 - EWICL will continue to be regulated by the PRA and any capital extractions would need to be approved by the PRA
 - In the absence of the Scheme, I understand that ILS would seek to extract capital from EWICL, subject to PRA approval, thereby reducing the coverage ratio of the SCR on the current basis.
- 9.21 The Scheme will have no material impact on the protections afforded to the policyholders remaining in EWICL in the event of insolvency of EWICL, including access to the FSCS.
- 9.22 As a result, my opinion is that I do not expect there to be a material adverse impact on the existing policyholders of EWICL in relation to security, including under insolvency, as a result of the Scheme.

10 Other financial considerations

10.1 In this section, I discuss the following items in turn:

- Investment strategy implications
- Implications of the Scheme on ongoing expense levels
- Pension arrangements
- Tax implications
- Liquidity position
- Impact on transferring reinsurers
- Impact of new business strategy
- Impact of other transfers.

Investment strategy implications

- 10.2 QBEUK's is subject to QBE EO's investment strategy, which is to meet annual return targets, taking into account QBE EO's risk tolerances. QBE EO has policies and limits to manage investment risk and keep its asset allocation in line within its risk tolerance. It sets limits on what type of investments should be invested in and how much should be invested with each counterparty. Its investment committee meets quarterly to review and monitor asset allocation and asset/liability exposure. QBEUK's investments are predominantly securities, investment funds, loans, cash and derivatives.
- 10.3 EWICL's investment objective is to match its insurance liabilities whilst adhering to its investment guidelines. It has policies and limits to manage investment risk. It sets limits on what type of investments should be invested in and how much should be invested with each counterparty. The responsibility for investment risk is delegated to the Chief Financial Officer who reports to the Board on a quarterly basis. EWICL's assets are denominated in Sterling and predominantly comprise a mixture of cash and securities.
- 10.4 I understand from EWICL that its investment strategy will remain the same following the Scheme.
- 10.5 I do not expect that EWICL's investment strategy will have a material adverse impact on the transferring policyholders as, based on my review of the investment strategies, EWICL's investments do not appear to be any more risky than those of QBEUK.
- 10.6 There will be no change to the investment strategy that the policyholders remaining in QBEUK are exposed to as a result of the Scheme.
- 10.7 There will be no change to the investment strategy that the existing policyholders of EWICL are exposed to as a result of the Scheme.

Implications of the Scheme on ongoing expense levels

- 10.8 The ongoing expense levels of EWICL will increase as a result of the Scheme, as ARML will provide more services to EWICL. These expenses have been allowed for in the projections provided to me in relation to capital and, as discussed in paragraph 9.9, I expect EWICL to have sufficient capital to meet policyholder obligations. Therefore, I do not believe that any changes in the expenses of EWICL will have a material adverse impact on either the transferring policyholders or the existing policyholders of EWICL.
- 10.9 I do not anticipate that there will be material changes in expense levels as a result of the Scheme that will create an adverse impact to the policyholders remaining within QBEUK because of the Transferring Portfolio's immaterial size in the context of QBEUK.

Pension arrangements

- 10.10 Neither QBEUK nor EWICL are sponsors of a defined benefit pension scheme and, as a result, there are no pension arrangements that are relevant to the Scheme.

Tax implications

- 10.11 QBEUK and EWICL have informed me that they do not believe there are likely to be any material tax implications as a result of the Scheme.
- 10.12 I have taken advice from the tax experts at Grant Thornton who specialise in the insurance sector. They have reviewed the information provided to me and do not believe there to be any material tax implications that affect the Scheme.

Liquidity position

- 10.13 I have reviewed the asset allocation and investment strategies of both QBEUK and EWICL. Both have sufficiently liquid assets to meet liabilities as they fall due, both before and after the Scheme.
- 10.14 As a result, I do not anticipate that the Scheme will create any material adverse impact with respect to liquidity for the transferring policyholders, the policyholders remaining within QBEUK or the existing policyholders of EWICL.

Impact on transferring reinsurers

- 10.15 As discussed in paragraph 7.38, the Transferring Portfolio does benefit from an excess of loss programme that covers multiple areas of QBEUK's business. I understand from QBEUK that no recoveries in respect of the Transferring Portfolio have been made to date from that reinsurance. This reinsurance, which is set out in multiple contracts, is expected to partially transfer as part of the Scheme, to the extent it will be shared between EWICL and QBEUK and will cover exactly the same risks as prior to the Scheme. Consequently, I do not expect that these reinsurers will be materially disadvantaged by the Scheme.
- 10.16 There are no other reinsurers of QBEUK whose contracts are expected to transfer as a result of the Scheme.

Impact of new business strategy

- 10.17 QBEUK's new business strategy will not change as a result of the Scheme. It follows that I have not identified any material adverse impact to the policyholders remaining in QBEUK as a result of the Scheme in relation to the new business strategy that they are exposed to.
- 10.18 EWICL does not write new business and will not do so following the Scheme. EWICL's business model is to acquire books of non-life insurance that are in run-off and this model will not change following the Scheme. Any further acquisitions are subject to approval from the PRA.
- 10.19 It follows that I have not identified any material adverse impact to the existing EWICL policyholders as a result of the Scheme in relation to the new business strategy that they are exposed to.
- 10.20 QBEUK and EWICL have different new business strategies. I do not envisage that this will have a material adverse impact on the transferring policyholders for the following reasons:
- Both QBEUK and EWICL are authorised by the PRA and regulated by the PRA and the FCA
 - Both QBEUK and EWICL are authorised to operate in the way that they do
 - Both QBEUK and EWICL hold capital to support the risks that they are exposed to. In addition, as concluded in Section 9, I am of the opinion that both companies have sufficient capital to meet policyholder obligations
 - As I have concluded in Section 11, both QBEUK and EWICL have appropriate management frameworks in place to support their respective businesses.
- 10.21 It follows that I have not identified any material adverse impact to the transferring policyholders as a result of the Scheme in relation to the new business strategy that they are exposed to.

Impact of other transfers

- 10.22 I am not aware of any other transfers into or out of EWICL that will affect any of the transferring policyholders or the existing policyholders of EWICL.
- 10.23 I understand from QBEUK that it is in the early stages of planning a transfer of policies to another entity within the QBE Group. I further understand from QBEUK that the transfer is driven by Brexit as the transferring portfolio relates to business that is currently carried out on a freedom of service basis. QBEUK is planning for this transfer to become effective in the second half of 2020. Given the current stage of this transfer, there is limited information available at the time of writing this report. Based on the materiality of the Scheme to QBEUK, I do not expect this additional transfer will give me reason to change the conclusions in this report. However, I will consider this further in my Supplementary Report.

11 Other non-financial considerations

11.1 In this section, I discuss the following items in turn:

- Changes in regulatory regime
- Claims handling
- Policy servicing
- Complaints
- ‘Brexit’
- Governance and management framework
- Should the Scheme not become effective.

Impact of changes in regulatory jurisdiction

11.2 Both QBEUK and EWICL are authorised by the PRA and regulated by the PRA and the FCA. Consequently, there will be no changes in regulatory jurisdiction as a result of the Scheme.

Claims handling

11.3 Prior to the LPTAs, claims handling was undertaken by QBEUK. As part of the LPTAs, the additional agreements that support the LPTAs and the subsequent operational migration to ARML, some of QBEUK’s claims team, including a claims manager, transferred to ARML to continue to manage the claims. As a result of this, there has been some continuity in the people handling claims in respect of the Transferring Portfolio.

11.4 Therefore, as a result of the LPTAs, ARML is responsible for the claims handling of the Transferring Portfolio at present. In addition, I understand from ARML that it will be responsible for the claims handling of the Transferring Portfolio following the Scheme. Further, I understand from ARML that there is no intention for there to be any changes in the terms of the outsourcing of claims handling from EWICL compared to the current situation where claims handling is outsourced from QBEUK.

11.5 Based on consideration of the above, I do not anticipate any material adverse changes to the claims handling provided to the transferring policyholders following the Scheme.

11.6 There will be no change in claims handling for the policyholders remaining within QBEUK.

11.7 Claims arising from the existing policyholders of EWICL are handled by ARML. This is done by a separate team to those that handle claims for the Transferring Portfolio. This will continue to be the case following the Scheme. As a result, I do not envisage a material adverse impact in respect of claims handling for these policyholders.

Policy servicing

- 11.8 QBEUK currently deals with all policy servicing queries. I understand from ARML that it will provide policy servicing following the Scheme.
- 11.9 As all of the Transferring Portfolio is in run-off, there are very few policy servicing queries that are not claims related.
- 11.10 QBEUK has provided me with documentation regarding how it deals with policy servicing queries at present. In addition, ARML has provided me with documentation regarding how it expects to deal with policy servicing queries following the Scheme. Both of these documents set out processes that I consider to be reasonable as they are in line with what I have seen elsewhere in the market in relation to policy servicing queries for run-off portfolios.
- 11.11 As a result, I do not anticipate any material adverse impact to the transferring policyholders in respect of policy servicing as a result of the Scheme.
- 11.12 There will be no change in policy servicing for the policyholders remaining within QBEUK or the existing policyholders of EWICL as a result of the Scheme.

Complaints

- 11.13 Prior to the Scheme, ARML passes complaints in respect of the Transferring Portfolio to QBEUK. QBEUK has provided me with its complaints handling policy. It adopts all applicable FCA requirements in relation to complaints handling. I understand from QBEUK that it is committed to treating all complainants fairly and will uphold a positive complaints culture, ensuring all regulatory standards for complaints handling are adopted.
- 11.14 Following the Scheme, ARML will be responsible for complaints handling, acting on behalf of EWICL. ARML has provided me with its complaints handling policy. It adopts all applicable FCA requirements in relation to complaints handling. I understand from ARML that it is committed to treating all complainants fairly and will uphold a positive complaints culture, ensuring all regulatory standards for complaints handling are adopted. I further understand from ARML that its complaints handling policy will not change as a result of the Scheme. In addition to this, EWICL, through its Audit and Risk Committee reviews decisions, actions and activity in relation to complaints handling. I consider this oversight to be appropriate based on my understanding of the process and my experience of processes in place elsewhere in the market.
- 11.15 There will be no change in eligibility for FOS for any policyholders as a result of the Scheme. Consequently, any transferring policyholders who are currently eligible to refer complaints to FOS will continue to be eligible to refer complaints to FOS following the Scheme.
- 11.16 There will be no change in either complaints handling or FOS eligibility for the policyholders remaining within QBEUK as a result of the Scheme.
- 11.17 Similarly, there will be no change in either complaints handling or FOS eligibility for the existing EWICL policyholders as a result of the Scheme.
- 11.18 As a result, my opinion is that the Scheme does not create any material adverse impact for any group of policyholders in respect of complaints.

‘Brexit’

- 11.19 I have been informed by QBEUK and EWICL that there are 374 policies (which are in respect of 133 policyholders) within the Autumn Portfolio that were underwritten in the Republic of Ireland and that the most recent claim from one of these policies was reported in 2016. Given this, I am of the opinion that it is reasonable to assume that the likelihood of significant numbers of claims being reported from policies underwritten in the EEA outside of the UK is remote.
- 11.20 I understand from QBEUK and EWICL that, with respect to the Autumn Portfolio, there are only two open claims where risks are located in the EEA outside of the UK - one where the risk is located in Italy and one where the risk is located in the Netherlands. QBEUK and EWICL have both estimated that there is no requirement for IBNER to be held in respect to these claims nor pure IBNR for future claims arising from the EEA outside of the UK. In addition to this, the last such claim notified was in early 2017.
- 11.21 In addition, there have been claims closed in other EEA states outside the UK. However, all of these claims relate to public liability policies where the claims closed a number of years ago. It is unlikely that there will be additional claims on these policies as, in my experience, claims on public liability policies tend to be reported quickly. I have been informed by EWICL that the historical experience of the Transferring Portfolio also supports the view that claims on public liability policies are reported quickly.
- 11.22 Given the above, my opinion is that it is reasonable to assume that the likelihood of significant numbers of claims being reported from policies covering risks in the EEA outside of the UK is remote.
- 11.23 I also understand from QBEUK and EWICL that, with respect to the Chestnut Portfolio, there are open claims where risks are located in the EEA outside of the UK. I further understand from QBEUK and EWICL that all of these claims are in respect of a subsidiary in the Netherlands and that all of the insured risks within the Chestnut Portfolio are located in either the UK or the Netherlands. I understand from EWICL that there are 14 open claims and that the most recent one was reported in 2016. Given this, and the fact that the majority of the insured's business is in the UK, my opinion is that it is reasonable to assume that the likelihood of significant numbers of further claims being reported from policies covering risks in the EEA outside of the UK is remote.
- 11.24 In addition to this, I have been provided with details of EWICL's contingent Brexit planning. Its preferred option, providing it is allowed following the Brexit negotiations, would be to continue to rely on passporting rights in order to settle any EEA claims outside of the UK.
- 11.25 Should those passporting rights (or some equivalent of those) be removed, EWICL will seek to rely on the relevant legal frameworks across the EEA. In that event, EWICL will seek to liaise with the relevant EEA regulators to ensure it can continue to service policyholders in the EEA. It is expected that, if passporting rights are removed, there will be arrangements made for a transition period by EEA regulators. With respect to the Republic of Ireland, EWICL has informed me that it is aware that legislation in the Republic of Ireland provides a transition period of three years from a hard Brexit date within which Republic of Ireland risks would need to be run-off or serviced from a third country branch of EWICL. Further, EWICL has told me that it understands that Italian legislation provides for a transition period of two years. For the Netherlands, EWICL has informed me that it is aware that there is no transition period currently proposed although it believes it likely that there will be one in the event of a hard Brexit.
- 11.26 In the event an EEA regulator does provide a legal framework or mechanism for EWICL to continue to service policyholders in the EEA, EWICL has informed me that it will seek to apply for a branch in that EEA state. I have been further informed by EWICL that it proposes not to commence the process to establish third country branches in relevant EEA States unless and until it becomes necessary to do so (for example, in the event of a hard Brexit). EWICL does not believe that it is effective from a time and cost perspective to commence engagement with local regulators or counsel when the form that Brexit will take is far from certain. In addition, based on earlier legal advice and discussions with EEA

regulators, EWICL understands that it is not possible to commence the process of establishing a third country branch of a UK insurer whilst the UK is part of the EU/EEA.

- 11.27 In the meantime, EWICL has told me that it will seek legal advice on the timing requirements for establishing Third Country branches in relevant EEA States and, in particular, whether the transitional period (if any) to be implemented in each such EEA State following a hard Brexit is sufficient for a Third Country branch to be established without adversely affecting policyholders. Where it is not, the transfer of affected policies under the Scheme may need to be delayed.
- 11.28 I understand from QBEUK and EWICL that, should a claim be reported within the Autumn Portfolio in relation to a non-UK EEA state other than the Republic of Ireland, Italy and the Netherlands between now and the Effective Date and should EWICL not be able to legally service the policy as a result of the outcome of Brexit, QBEUK's and EWICL's current intention is not to transfer the policy to EWICL under the Scheme as at the Effective Date. I understand from QBEUK that, if passporting rights are removed, QBEUK expects there to be transitional periods put in place by the various EEA regulators (as discussed in paragraph 11.25) and that it will consider alternatives to servicing such claims during these transitional periods.
- 11.29 In the event that such policies are discovered after the Effective Date, I understand from QBEUK and EWICL that they will be considered to have transferred to EWICL under the Scheme. I understand that EWICL will take such steps as would be necessary at the time to be able to ensure that each such claim is serviced. In particular, following the Directions Hearing, EWICL will request certificates of consent from the PRA in respect of the regulators in the Republic of Ireland and the Netherlands.
- 11.30 Having reviewed the details of EWICL's contingent Brexit planning, it is my opinion that EWICL has appropriately considered the options available to it given the uncertainty that still remains around Brexit. In addition, it is my opinion that the options considered are appropriate given the low materiality of the non-UK EEA business.
- 11.31 As a result, although the negotiations regarding Brexit are ongoing at the time of writing this report and the situation following Brexit remains unclear, I do not believe there are any material issues arising from Brexit that affect the Scheme.

Governance and management framework

- 11.32 Prior to the Scheme, the day to day management of the Transferring Portfolio is operated by ARML and ILSIM as a result of the LPTAs and the Services Agreement, although QBEUK remains responsible for the Transferring Portfolio as the insurer. I understand from QBEUK and ARML that ARML provides management information to QBEUK on a regular basis on claim notifications and movements.
- 11.33 EWICL retains direct management and decision-making over its primary activities, specifically areas related to strategy, capital, claims strategy, risk, expense control and business planning. Many other activities are outsourced to specialist service providers where a broader experience base and depth of resources can be more easily assured. The vast majority of these outsourced services are to ARML. As a result, the day to day management of the Transferring Portfolio will largely continue to be operated by ARML.
- 11.34 Furthermore, I understand from ARML that there is no intention to change any of the other outsource providers as a result of the Scheme.
- 11.35 The Board of EWICL comprises three executive Board members and four non-executive Board members. Two of the non-executive members of EWICL's Board are members of ILS's Board. The other two non-executive members are independent of EWICL and ILS. The three executive Board members retain responsibility for the various areas set out within its operations model. Following the Scheme, oversight for the Transferring Portfolio will be provided solely by EWICL.

- 11.36 There is one formal committee that reports to the Board, namely the Audit and Risk Committee. It is chaired by an independent non-executive member of the Board.
- 11.37 There are three series of management meetings that are operated by the executive management, namely:
- Service provider management
 - Risk and capital management
 - Expense management
- 11.38 In addition, I understand from ARML that in its capacity as a servicing company it has its own governance structure focussed on the roles and responsibilities regarding how it will continue to provide high quality services including financial, IT and claims solutions to both its internal and external run off clients.
- 11.39 I have reviewed EWICL's management and governance framework and, in my opinion, based on my experience of such frameworks in the market, it is proportionate to the size and complexity of EWICL's business and will continue to be so following the Scheme.
- 11.40 QBEUK shares its governance framework with the other operating subsidiaries of QBE EO. The Board comprises of a mixture of executive and independent non-executive directors, including an independent non-executive director who serves as the Chairman of the Board.
- 11.41 There are a number of formal committees that report to the Board, namely the:
- Audit Committee
 - Risk and Capital Committee ("RCC")
 - Investment Committee
 - Remuneration and Nomination Committee
- 11.42 There is also a UK Executive Management Board ("EMB"). The EMB, together with the Management Committee ("QEMC"), has constituted four formal Management Groups, namely the:
- Finance Management (incl. Reserving) Group
 - Underwriting Management (incl. Reinsurance) Group
 - Operations Management Group
 - Disclosure Management Group
- 11.43 Each Management Group has Terms of Reference (approved by the EMB) which set out its role and levels of authority. Each Management Group reports as appropriate to the EMB (the Chair of the Management Group being a member of the EMB) in relation to the matters it has considered and /or escalated to the EMB.
- 11.44 The RCC has three formal sub-groups, namely the:
- Compliance Management Group
 - Risk & Capital Group
 - Conduct Risk Group
- 11.45 I have reviewed the management and governance framework of QBEUK and, in my opinion, based on my experience of such frameworks in the market, it is proportionate to the size and complexity of QBEUK's business.

- 11.46 I have not identified any material adverse impact to any of the groups of policyholders in relation to the management and governance framework as a result of the Scheme.

Should the Scheme not become effective

- 11.47 I have considered the likely effects on the transferring policyholders, the existing policyholders of EWICL and the policyholders remaining within QBEUK should the Scheme not become effective.
- 11.48 If the Scheme were not to become effective, TMR and ILS would continue to provide 100% reinsurance in respect of the Transferring Portfolio under the existing LPTAs and would run-off the existing liabilities until the earliest of expiry of those liabilities, the Scheme becoming effective at a subsequent date, the LPTAs being commuted, or the LPTAs being terminated for one of the reasons described in paragraphs 5.49 and 5.57.
- 11.49 As discussed in paragraphs 9.10 to 9.15, I do not believe that the transferring policyholders will be materially disadvantaged as a result of the Scheme in terms of security. Therefore, it is my opinion that the transferring policyholders will not be materially better off should the Scheme not become effective.
- 11.50 There is no change in the regulatory jurisdiction for the Transferring Portfolio whether the Scheme becomes effective or not. As a result, I do not believe the transferring policyholders will be materially better off in respect of regulatory jurisdiction should the Scheme not become effective.
- 11.51 Should the Scheme not become effective, the Services Agreement will remain in place alongside the LPTAs and ARML will continue to provide claims handling and administration services in respect of the Transferring Portfolio. I have concluded in paragraph 11.5 that I do not anticipate any material adverse changes to the claims handling provided to the transferring policyholders following the Scheme. Therefore, it is my opinion that the transferring policyholders will not be materially better off in respect of claims handling should the Scheme not become effective.
- 11.52 Should the Scheme not become effective, QBEUK will also continue to deal with policy servicing queries. I have concluded in paragraph 11.11 that I do not anticipate any material adverse impact to the transferring policyholders in respect of policy servicing as a result of the Scheme. Therefore, it is my opinion that the transferring policyholders will not be materially better off in respect of policy servicing should the Scheme not become effective.
- 11.53 In addition, should the Scheme not become effective, QBEUK will continue to handle complaints in respect of the Transferring Portfolio. I have concluded in paragraph 11.18 that the Scheme does not create any material adverse impact for the transferring policyholders in respect of complaints. Therefore, it is my opinion that the transferring policyholders will not be materially better off in respect of complaints handling should the Scheme not become effective.
- 11.54 Any issues that present themselves as a result of Brexit will be the same whether the policyholders have transferred or not. This is because, should the Scheme not become effective, the transferring policyholders would still be part of a UK insurer. As a result, I do not believe the transferring policyholders will be materially better off in respect of Brexit should the Scheme not become effective.
- 11.55 Should the Scheme not become effective, ARML and ILSIM would continue to undertake the day to day management in respect of the Transferring Portfolio and as a result there would be no change from the current position in respect of the governance and management framework.
- 11.56 Should the Scheme not become effective, I understand from EWICL that it would continue to operate as it has, continuing to pay claims on its existing portfolio and seeking new opportunities to purchase portfolios.
- 11.57 As discussed in paragraphs 9.19 to 9.22, I do not believe that the existing policyholders of EWICL will be materially disadvantaged as a result of the Scheme. Therefore, it is my opinion that the existing policyholders of EWICL will not be materially better off should the Scheme not become effective.

- 11.58 If the Scheme were not to become effective, there would be no impact on the policyholders remaining in QBEUK compared to the current position given the magnitude of the Transferring Portfolio in the context of QBEUK as a whole.

12 Communications

Policyholder notifications

- 12.1 The regulations surrounding 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 Scheme. The affected companies may apply for waivers considering, amongst other things, the likely benefits of contacting the policyholders compared with the practicality and costs of doing so.
- 12.2 QBEUK and EWICL are seeking waivers from this requirement to write to all policyholders and have selected specific groups of policyholders that they intend to notify. Paragraphs 12.3 to 12.11 set out a summary of the policyholders and third parties that QBEUK and EWICL intend to notify directly.

Summary of notifications

Transferring Portfolio

- 12.3 QBEUK intends to directly notify the following policyholders within the Transferring Portfolio:
- In respect of the Autumn Portfolio, any policyholder who:
 - Has an open claim
 - Has notified at least one industrial disease claim since 1 January 2014
 - Holds a policy covering risks located in the Republic of Ireland according to QBEUK's records
 - In respect of the Chestnut Portfolio, the sole named policyholder, TSEL.
- 12.4 QBEUK does not intend to directly notify any other policyholders in the Transferring Portfolio.
- 12.5 I understand from QBEUK that in respect of the Autumn Portfolio, it intends to notify 3,230 of the approximately 720,000 policyholders, which represents 0.4% of the Autumn Portfolio. The reasons why QBEUK does not intend to notify the other approximately 717,000 policyholders are discussed in paragraph 12.18.

Remaining Portfolio

- 12.6 QBEUK does not intend to directly notify any of the policyholders within the Remaining Portfolio, with the exception of those policyholders with Split Policies. This is discussed further in paragraphs 12.20 to 12.21.

Existing EWICL Portfolio

- 12.7 EWICL intends to directly notify the following policyholders within the Existing EWICL Portfolio:
- In respect of the Legacy Portfolio:
 - Policyholders with open claims relating to policies within the LMX portfolio
 - Any policyholder with an employers' liability policy within EWICL's direct commercial general insurance portfolio and for whom EWICL holds a current valid address
 - In respect of the UKBG Portfolio:
 - Any policyholder who has an unexpired policy as at 1 August 2019 for whom EWICL holds a current valid address
 - Any additional policyholder who, as at 1 August 2019, has an open claim
- 12.8 EWICL does not intend to directly notify any other policyholders in the Existing EWICL Portfolio.

Third party notifications

- 12.9 I understand from QBEUK that it also intends to directly notify each broker that has either placed one of the policies defined in paragraph 12.3 or has handled a claim relating to one of the policies defined in paragraph 12.3. I further understand from QBEUK that it will request that these brokers forward details about the Scheme to any policyholder within the Transferring Portfolio for whom they act. The notices forwarded to policyholders would be in addition to QBEUK or EWICL notifying directly.
- 12.10 In addition, I understand from QBEUK that it intends to directly notify any solicitors who handle open claims relating to policies within the Transferring Portfolio. I further understand from QBEUK that it will request these solicitors to forward details about the Scheme to any person the solicitor deems may be of interest and for whom they act. Any notices forwarded to policyholders with open claims against QBEUK would be in addition to QBEUK notifying directly.
- 12.11 I understand from EWICL that it also intends to directly notify any brokers representing policyholders within the LMX Portfolio with an open claim.

Rationale for seeking waivers

Transferring Portfolio

- 12.12 I understand from QBEUK that it is seeking a waiver from the requirement to notify all policyholders within the Transferring Portfolio. In particular, QBEUK is seeking a waiver from the requirement to notify the policyholders within the Autumn Portfolio outside of those discussed in paragraph 12.3, namely:
- Those with policies other than employers' liability (i.e. public liability) without open claims, except those policies covering risks located in the Republic of Ireland
 - Those with employers' liability policies where no industrial disease claims have ever been reported, except those policies covering risks located in the Republic of Ireland
 - Those with employers' liability policies with industrial disease claims notified prior to 1 January 2014 and where those claims have closed, except those policies covering risks located in the Republic of Ireland

Public liability policies without open claims

- 12.13 QBEUK believes that there would be little or no benefit to policyholders with such policies being notified directly about the Scheme for the following reasons:
- It expects that 98% of claims arising under these policies to be notified within ten years of the claim event and, as at the Effective Date, these policies will have been in run-off since 2007 and all claim events will have occurred at least 11 years ago
 - For the small proportion of policyholders who may report a claim in the future:
 - There is no change expected to the administration of claims as ARML will continue to administer these claims following the Scheme albeit on behalf of EWICL in place of QBEUK
 - There will be no change to the legal or regulatory regimes governing these policies
 - The policyholders within the Transferring Portfolio will continue to benefit from access to the FOS and FSCS following the Scheme.
- 12.14 QBEUK has estimated the cost of notifying policyholders with public liability policies, in addition to those with open claims, to be approximately between £6,000 and £7,000. Accordingly, I understand that QBEUK believes that the expense would be disproportionate given the limited benefit of notifying them about the Scheme.

12.15 QBEUK has provided me with its analysis in relation to this waiver. I have reviewed this and challenged it where necessary and my opinion is that it is proportionate and reasonable for QBEUK to seek this waiver given the reasons stated above.

Employers' liability policies QBEUK intends not to notify

12.16 I understand from QBEUK that it has chosen the cut-off date of 1 January 2014 following an analysis undertaken by AMRL of the historical data for policyholders within the Autumn Portfolio. I have been informed by ARML that, based on this analysis, it has estimated the following:

- Approximately 90% of claimants who have made an industrial disease claim over the last 19 years, have made a previous industrial disease claim
- Approximately 97.5% of policyholders who have made multiple industrial disease claims made a subsequent claim within five years of their previous industrial disease claim.

Consequently, QBEUK believes that notifying policyholders who have made at least one industrial disease claim since 1 January 2014 will cover a substantial proportion of the transferring policyholders who are likely to have a future claim.

12.17 I understand from ARML that it also tested a range of cut-off dates. For example, ARML considered a cut-off date of 1 January 2009 and estimated that approximately 99% of policyholders who have made multiple industrial disease claims made a subsequent claim within 10 years of their previous industrial disease claim. I further understand from ARML that the extra cost of having a cut-off date five years earlier would result in a disproportionately large increase to the number of additional policyholders who would be contacted, the majority of who would not be expected to make any future claims.

12.18 There are approximately 720,000 policyholders within the Autumn Portfolio and QBEUK intends to notify approximately 3,000 of these policyholders (i.e. the number of policyholders with open claims or at least one industrial disease claim notified since 1 January 2014). QBEUK has provided me with the following reasons as to why it believes that notifying the remaining approximately 717,000 policyholders would be of limited benefit to them:

- Of the approximately 717,000 policyholders, QBEUK only holds address for approximately 27,000 policyholders, which is a small proportion of the whole. I understand that QBEUK believes that undertaking a tracing exercise to determine contact details for the remainder would have a considerable expense and human resource cost.
- Industrial disease claims made against employers' liability policies can be traced through Employers' Liability Tracing Office ("ELTO"). ELTO provides a mechanism for tracing the insurer that a third-party claimant should be making a claim against. Therefore, for those policyholders who would not be notified directly about the Scheme, QBEUK is of the opinion that there is an established avenue through which any claims can be brought in the future.
- There is already a process in place for referring claims relating to the Transferring Portfolio from QBEUK to ARML. I understand from QBEUK that this process will continue following the Scheme so that in the event that claims are notified to QBEUK following the Scheme, they will also be passed on to EWICL.
- I understand from QBEUK and EWICL that they propose to advertise the Scheme in a number of publications that are in addition to the required publications. These publications are discussed further in paragraphs 12.44 to 12.45.
- Even if QBEUK held addresses for all approximately 717,000 policyholders, it has estimated the incremental printing and posting cost to be approximately £824,000. Accordingly, I understand that QBEUK believes that the expense would be disproportionate given the reasons stated above.

12.19 QBEUK and ARML have provided me with all the analyses undertaken in relation to this waiver, including the analysis relating to the cut-off date. I have reviewed this and challenged it where necessary and my opinion is that it is proportionate and reasonable for QBEUK to seek this waiver given the reasons stated above.

Remaining Portfolio

- 12.20 I understand from QBEUK that it is seeking a waiver from the requirement to notify all policyholders within the Remaining Portfolio, except those policyholders with Split Policies
- 12.21 QBEUK has provided me with the following reasons as to why it believes that notifying all policyholders within the Remaining Portfolio would be of no benefit to them:
- The liabilities in respect of the Transferring Portfolio are a small proportion (approximately 4%) of QBEUK's total liabilities as at 31 December 2018
 - The liabilities in respect of the Transferring Portfolio are already 100% reinsured by TMR and ILS and therefore the policyholders within the Remaining Portfolio are not exposed to the liabilities of the policyholders within the Transferring Portfolio. Consequently, although transferring these liabilities to EWICL by way of the Scheme, eliminates the gross exposure of the policyholders within the Remaining Portfolio to these liabilities, it does not change their net exposure.
 - The policyholders within the Remaining Portfolio are not transferring to another insurer as a result of the Scheme but will remain policyholders of the same legal entity. Accordingly, any notification would in effect be simply to notify them that their policies are remaining with the same insurer and that nothing is changing with respect to their circumstances or security of benefits
- 12.22 Further to this, QBEUK has estimated that the additional cost for mailing all of the policyholders within the Remaining Portfolio would be approximately £690,000 (based on printing and posting estimates obtained by QBEUK). I understand from QBEUK that it believes that notifying these policyholders of the Scheme would be disproportionate given the estimated costs involved in doing so.
- 12.23 QBEUK has provided me with its analysis in relation to this waiver. I have reviewed this and challenged it where necessary and my opinion is that it is proportionate and reasonable for QBEUK to seek this waiver given the reasons stated above.

Existing EWICL Portfolio

- 12.24 I understand from QBEUK that it is seeking waivers from the requirement to notify all policyholders within the Existing EWICL Portfolio as described in the paragraphs below.

The Legacy Portfolio

- 12.25 The Legacy Portfolio consists of the following portfolios:
- direct retail motor and household
 - EAUA
 - LMX
 - direct commercial general insurance
- 12.26 For the direct retail motor and household and EAUA portfolios, no policy records exist. EWICL is therefore seeking a waiver from the requirement to notify policyholders with policies within these portfolios.
- 12.27 Furthermore, in respect of the EAUA portfolio, I understand that EWICL believes there is a lack of utility in notifying policyholders since all the liabilities relating to the EAUA portfolio were closed in September 2013 by means of a scheme of arrangement. There are no outstanding claims in relation to the EAUA

portfolio and no claims can be made in the future. Accordingly, EWICL believes that notifying the policyholders of such policies about the Scheme would serve no purpose.

- 12.28 For the LMX portfolio, I understand from EWICL that it only holds records and contact details for the 12 policyholders with open claims. EWICL intends to write to these 12 policyholders and is seeking a waiver from the requirement to notify the remaining policyholders within the LMX portfolio on the grounds that it would not be possible to notify them as no contact details exist.
- 12.29 For the direct commercial general insurance portfolio, I understand from EWICL that as part of the Section 13 Transfer from ZIP to EWICL, it identified contact details for 43 out of 54 policyholders. However, for 9 of these policyholders with known contact details, the notice of this prior transfer was returned. EWICL does not propose to undertake another exercise to identify the contact details of these 9 policyholders as it does not believe it will yield a materially different result from its attempt to identify the contact details during the Section 13 Transfer process. EWICL therefore proposes to write to the 34 policyholders for whom it has last known addresses and is seeking a waiver from the requirement to notify any other policyholder with a policy in this portfolio on the grounds that it would not be possible to notify such policyholders.
- 12.30 It is my opinion that it is proportionate and reasonable for EWICL to seek these waivers in relation to the Legacy Portfolio given the reasons stated above.

The UKBG Portfolio

- 12.31 Paragraph 12.7 sets out the policyholders in the Existing EWICL Portfolio that EWICL intends to notify.
- 12.32 EWICL does not intend to contact those policyholders where the policy has expired and there is not an open claim. As the policies are on a claims made basis, these policyholders can no longer make claims.
- 12.33 I understand from EWICL that as at 1 August 2019, there were 302,778 UKBG policies, where 276,532 had expired and 26,346 policies were unexpired. It remains possible to make a claim under the unexpired policies. For the unexpired policies, 6,783 were issued to housing associations and the remaining 19,563 policies were issued to individual homeowners.
- 12.34 In relation to the unexpired housing association policies, where the housing association is the developer and/or the property owner, there were 2,041 registered providers of social housing in the UK as at 2 November 2016. This analysis was undertaken by ZIP for the purposes of the Section 13 Transfer from ZIP to EWICL. EWICL proposes to write to each of these housing associations at their registered address to notify them about the Scheme.
- 12.35 In relation to policies issued to individual homeowners and under which claims were still possible, ZIP undertook a cleansing exercise to identify addresses for policyholders for the purposes of the Section 13 Transfer from ZIP to EWICL; however, ZIP was not able to identify all contact details. As at 1 August 2019, I understand from EWICL that it had an address in respect of the 19,563 individual homeowners with unexpired policies. This contained 21,831 addresses. Of these, 2,268 related to communication packs that had been returned from the initial ZIP mailing as a result of the addresses being incorrect. Revised addresses for these policyholders were subsequently identified by ZIP. I understand from EWICL that it will make reasonable efforts to identify which of the 2,268 subsequently identified addresses should be used in place of the initial contact list addresses prior to sending the communications.
- 12.36 I understand from EWICL that it does not intend to carry out a secondary cleansing exercise on top of that performed by ZIP for the purposes of the Section 13 Transfer because it does not believe there is anything further that can be done to trace any additional addresses.
- 12.37 EWICL is therefore seeking a waiver from the requirement to notify the policyholders with unexpired policies for which it is not able to identify a valid address following reasonable efforts to do so.

12.38 It is my opinion that it is proportionate and reasonable for EWICL to seek these waivers in relation to the UKBG Portfolio given the reasons stated above.

Advertisements

- 12.39 Further to the above, regulations surrounding Part VII transfers require that a notice stating that an application has been made in connection with the Scheme must be published:
- a) in the London, Edinburgh and Belfast Gazettes
 - b) in two national newspapers in the UK
 - c) where an EEA State other than the UK is the state in which the risk is situated for any direct (as opposed to reinsurance) policy that is being transferred, once in each of two national newspapers in that EEA State
 - d) where, for any inwards reinsurance policy that is being transferred, an EEA State other than the UK is the State in which the establishment of the policyholder to which the policy relates is situated at the date when the contract was entered into, once in one business newspaper which is published or circulated in that EEA State
- 12.40 The policies within the Autumn Portfolio cover risks located in the UK and other countries within the EEA. However, for countries in the EEA other than the UK, there are only two open claims - one where the risk is located in Italy (a reinsurance policy) and one where the risk is located in the Netherlands (a direct policy). The policies within the Chestnut Portfolio cover risks located in the UK and other countries within the EEA. However, for countries in the EEA other than the UK, there are 14 open claims all of which are in respect of a subsidiary in the Netherlands.
- 12.41 QBEUK and EWICL are seeking a waiver from the requirement to publish the notice in the Netherlands as set out in requirement c) of paragraph 12.39. I understand from QBEUK and EWICL that, with respect to the Chestnut Portfolio, risks in relation to the subsidiary in the Netherlands are insured under policies written for TSEL only and, as TSEL will be notified directly about the Scheme, no additional benefit will be served by advertising in these jurisdictions. I also understand that, with respect to the Autumn Portfolio, QBEUK and EWICL intend to contact all policyholders with open claims, including the claim where the risk is located in the Netherlands. I have been informed by QBEUK and EWICL that the most recently reported direct claim in the Autumn Portfolio where the risk is located in the EEA outside of the UK was notified in 2012. Given this, my opinion is that it is reasonable to assume that the likelihood of significant numbers of claims being reported from policies covering risks in the EEA outside of the UK is remote and therefore no additional benefit will be served publicising in these jurisdictions.
- 12.42 QBEUK and EWICL are seeking a waiver from requirement d) as stated in paragraph 12.39 to publish notice in a business newspaper in Italy. This is on the basis that the inwards reinsurance policyholder has an open claim and will be directly notified of the Scheme. Given this, my opinion is that it is reasonable to assume that no additional benefit will be served publicising in this jurisdiction.
- 12.43 Given the above, QBEUK and EWICL intend on publishing a notice stating that the Part VII application has been made in:
- the London, Edinburgh and Belfast Gazettes
 - The Times and The Daily Mail
 - in Republic of Ireland, in Iris Oifigiúil and The Irish Times.

- 12.44 QBEUK also intends on publishing a notice of the Scheme in the following UK professional and specialist trade publications:
- the Insurance Times
 - Machinery
 - New Civil Engineer
 - Construction Plant News.
- 12.45 In addition, QBEUK intends on approaching the following market bodies and associations with a request to publicise notice of the Scheme:
- Association of British Insurers
 - Association of Insurance and Reinsurance Run-Off Companies
 - Insurance and Reinsurance Legacy Association
 - Employers' Liability Tracing Office
 - Association of Insurance and Risk Managers in Industry and Commerce
 - British Insurance Brokers Association
 - London and International Insurance Brokers Association.
- 12.46 It is my opinion is that the above advertisement strategy is proportionate and reasonable with regards to the Scheme.

Documentation

- 12.47 I have reviewed the drafts of the proposed communications material and in my opinion:
- The material is straightforward, provides sufficient information for the policyholders to understand the Scheme, and details any required actions where relevant
 - It explains to the policyholders their right to object and the ways in which they can exercise this right
 - The access to the available documentation and relevant information is clear.
- 12.48 In addition to the communications discussed above, all of the material related to the Scheme will be published on websites hosted by QBEUK and Armour. I have seen a draft of the text to be contained on these websites.
- 12.49 Having reviewed the proposed documentation, it is my opinion that it is clear, proportionate and reasonable.

Reinsurer notifications

- 12.50 It is a requirement to send notifications to every reinsurer whose contracts of reinsurance are to be transferred, in part or in whole. In addition, it is a requirement to notify person(s) in cases where such a contract has been placed with or through a person authorised to act on behalf of the reinsurer.
- 12.51 The Transferring Portfolio currently benefits from excess of loss reinsurance contracts that cover both the Transferring Portfolio and parts of the Remaining Portfolio. It is proposed that the Transferring Portfolio will continue to benefit from this reinsurance following the Scheme. QBEUK intends to directly notify the reinsurers (and/or the intermediaries authorised to act on their behalf) who reinsure the Transferring Portfolio about the Scheme.

12.52 I understand from QBEUK that there are no other reinsurance protections covering the Transferring Portfolio.

12.53 I believe the proposed approach to reinsurer notification to be proportionate and reasonable.

Opinion

12.54 In reviewing the policyholder and reinsurer notification strategy, I have:

- Held discussions with QBEUK and EWICL
- Reviewed the analysis undertaken in respect of waivers requested
- Reviewed information provided to the PRA and FCA setting out the approach to policyholder notifications
- Reviewed the witness statements setting out the policyholder notification strategy
- Reviewed the proposed communications materials
- Reviewed the draft text for the websites.

12.55 Given the size and implications of the Scheme, I believe that the proposed approach to policyholder and reinsurer notifications is proportionate and reasonable.

12.56 In my Supplementary Report, I will discuss how the policyholder and reinsurer notification strategy has been implemented. In addition, I will discuss any objections that have been received following notification of the Scheme

13 Reliances and limitations

Events following the modelling date

- 13.1 The conclusions in this report are based on analyses that have been undertaken on data as at different points in time. I have been informed by QBEUK and EWICL that there have been no material changes between the modelling dates and the date of this report. However, future events could occur between the date of this report and the Effective Date that could change my conclusions. I will provide a Supplementary Report prior to the sanction of the Scheme to update the Court on whether there have been any material changes since the issue of this report.

Reliance on other parties

- 13.2 In developing the conclusions in this report, I have relied on the data and accompanying explanations provided to me by and on behalf of QBEUK and EWICL. I have not specifically reviewed the data for accuracy and completeness, but I have reviewed it for reasonableness.
- 13.3 I have carried out investigations, as detailed in this report, to gain comfort on the appropriateness of the methodology and conclusions for the most significant liabilities and capital requirements.
- 13.4 For the Transferring Portfolio, I have performed a high-level re-estimation of the gross claims reserves and I have assessed, at a high-level, the impact of using my estimation of the gross claims reserves to calculate the regulatory capital requirements. I have also relied on the calculations and documentation provided to me by, and on behalf of, QBEUK and EWICL. I believe this is reasonable given the testing that I have done. The reviews that I have carried out give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.
- 13.5 For QBEUK, my review has not amounted to a full re-estimation of the liabilities for every class of business or a detailed calculation of the capital requirements. Instead, I have relied upon reserving work and estimation of capital requirements performed by QBEUK. I believe this is reasonable given the experience and professional qualifications of the authors of the reserving and capital documents provided to me by QBEUK, the testing that I have done and the immateriality of the Transferring Portfolio in the context of QBEUK as a whole. The reviews that I have carried out give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.
- 13.6 For EWICL prior to the Scheme, my review has not amounted to a full re-estimation of the liabilities for every class of business or a detailed calculation of the capital requirements. Instead, I have relied upon reserving work and estimation of capital requirements performed by ARML. I believe this is reasonable given the experience and professional qualifications of the authors of the reserving and capital documents provided to me by ARML and the testing that I have done. The reviews that I have carried out give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.
- 13.7 I have also relied on discussions that I have had with the managements of QBEUK, EWICL and ARML. Where appropriate, I have sought documentation from them to evidence the assertions made to me in those discussions.

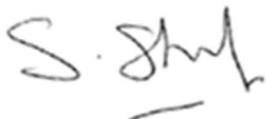
Other

- 13.8 In my judgement, the results and conclusions contained in this report are reasonable given the information made available to me.
- 13.9 However, there is a limitation upon the accuracy of any estimate of claims reserves or capital requirements in that there is an inherent uncertainty in any estimate of future liabilities. This is due to the fact that the claims will be subject to the outcome of events yet to occur, such as judicial decisions, legislative actions, claim consciousness amongst potential claimants, claims management, claim settlement practices, changes in inflation, and economic decisions. As a result, it should be recognised that future claim emergence will likely deviate, perhaps materially, from any estimate of claims reserves. In addition, it should be recognised that the actual capital required will likely deviate, perhaps materially from any estimate of the capital requirements.
- 13.10 The underlying figures in this report are calculated to many decimal places. In the presentation of the figures in the various tables, there may be reconciliation differences due to the effect of rounding.

14 Conclusions

- 14.1 I have considered the Scheme and its likely effects on the transferring policyholders, the policyholders remaining in QBEUK, and the existing EWICL policyholders.
- 14.2 In reaching the conclusions set out below, I have applied the following principles as set out in relevant professional guidance. I have sought to:
- Exercise my judgement in a reasoned and justifiable manner;
 - Describe the impact on all classes of beneficiaries (for the purposes of this report, being the transferring policyholders, the policyholders remaining in QBEUK and the existing policyholders of EWICL) and reinsurers;
 - Indicate how the Scheme might lead to any changes in the material risks to the benefits of the different classes of beneficiaries;
 - Assess the impact on all the classes of beneficiaries;
 - Indicate the proposed rationale for the Scheme to proceed;
 - Include (in summary) the most material information on which my opinion is based
 - Describe the rationale for my opinion.
- 14.3 I have concluded that there will be no material adverse impact to the service provided to the transferring policyholders and no material adverse impact on the security provided to them. Note that the latter conclusion is predicated on the fact that ILS Property & Casualty Master Fund Ltd, ILS and Armour will provide support to EWICL, should additional funds be required, as discussed in paragraphs 8.100 to 8.103. However, even if EWICL was not able to receive additional funds from ILS Property & Casualty Master Fund Ltd, ILS or Armour, my view is that the likelihood of EWICL being unable to pay claims as they fall due is remote.
- 14.4 Therefore, I do not expect that the transferring policyholders would be materially adversely affected by the Scheme.
- 14.5 I have also concluded that there will be no material adverse impact to the service provided to the policyholders remaining in QBEUK and no material adverse impact on the security provided to them. Therefore, I do not expect that the policyholders remaining in QBEUK would be materially adversely affected by the Scheme.
- 14.6 In addition, I have concluded that there will be no material adverse impact to the service provided to the existing policyholders of EWICL and no material adverse impact on the security provided to them. Therefore, I do not expect that the existing policyholders of EWICL would be materially adversely affected by the Scheme.
- 14.7 In addition, I identify no reinsurers that will be materially adversely affected by the Scheme.
- 14.8 Given the above, I conclude that the risk of any group of policyholders or reinsurers being materially adversely affected by the Scheme is sufficiently remote that there is no reason why the Scheme should not proceed.

- 14.9 I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions that I have expressed and conclusions that I have drawn represent my true and complete professional opinions on the matters to which they refer.
- 14.10 As required by Part 35 of the Civil Procedure Rules, I hereby confirm that I understand my duty to the Court, I have complied with that duty and I will continue to comply with that duty.
- 14.11 I do however consider it necessary that I review the most recent information, up to the date of the Sanctions hearing, when this becomes available later in the year, before confirming my conclusions and opinions.

A handwritten signature in black ink, appearing to read "S. Sheaf".

Simon Sheaf FIA, FSAI
Partner and Head of General Insurance Actuarial & Risk
Grant Thornton UK LLP

A Information received

Information provided by or on behalf of EWICL

- Signed report and accounts as at 30 June 2018
- Management account as at 31 December 2018
- ILS P&C Re balance sheet as at 31 December 2018
- Solvency and Financial Condition Report at 30 June 2017
- Solvency and Financial Condition Report at 30 June 2018
- Quarterly Quantitative Reporting Templates at 31 March 2018, 30 June 2018 and 30 September 2018
- Annual Quantitative Reporting Templates at 30 June 2018
- Actuarial Function Report as at 30 June 2018
- Actuarial reserving report for the Existing EWICL Portfolio as at 30 June 2018
- Actuarial reserving report for the Existing EWICL Portfolio as at 31 December 2018
- Reserving analysis for the Transferring Portfolio as at 30 September 2018
- Actuarial reserving report for the Autumn Portfolio as at 30 September 2018
- Actuarial reserving report for the Chestnut Portfolio as at 30 September 2018
- Document setting out differences between ARML estimate and QBEUK estimate in respect of the Transferring Portfolio
- Roll forward of reserves for the Transferring Portfolio to 31 December 2018
- Financial model setting out projected balance sheets (GAAP and Solvency II), SCR, MCR and capital coverage at a variety of dates, including 31 December 2018 and the Effective Date, both before and after the Scheme
- Document setting out the results of the financial model
- ORSA report dated 11 July 2018
- EWICL's Risk Appetite Statement
- EWICL's Risk Management Framework
- EWICL's investment guidelines
- Claims handling guidelines in respect of mesothelioma claims
- ARML's claims reserving guide for long tail disease claims
- Employers' liability and public liability claims handling process documentation
- Claims handling guidelines in respect of the UKBG Portfolio
- First Notification of Loss process documentation
- Large Loss Documentation Form
- ARML's complaints handling procedures
- Matrix of accountabilities for EWICL
- Armour Group organisational chart
- Armour UK organisational chart

- ILS's organisational chart
- Documentation setting out EWICL's governance model
- EWICL's organisational chart and governance structure
- Chestnut Framework Agreement
- Chestnut Loss Portfolio Transfer Agreement
- Retrocession Agreement between TMR and ILS
- Autumn Loss Portfolio Transfer Agreement
- CVs of key individuals involved in the reserving and capital processes at ARML

Information provided by or on behalf of QBEUK

- QBEUK balance sheet as at 31 December 2018, before and after the Scheme
- QBE EO Solvency and Financial Condition Report at 31 December 2017
- QBEUK's analysis of the reserves of the Autumn Portfolio as at 31 May 2018
- QBEUK's analysis of the reserves of the Chestnut Portfolio as at 30 September 2018
- Roll forward of reserves for the Transferring Portfolio to 31 December 2018
- QBE EO Actuarial Analysis of Provisions Report as at 30 September 2017 and 30 September 2018
- Reserve Working Group meeting exhibits
- QBE Reserving Overview as at 2 July 2018
- QBE Responsibilities of Actuarial Function
- QBE Actuarial Function Report as at 31 December 2017
- Actuarial Summary of QBE EO Reserves as at 31 December 2017
- QIEL 2018 Quarterly Quantitative Reporting Templates
- QIEL 2017 Annual Quantitative Reporting Templates
- QBEUK Solvency II balance sheet at 31 December 2018, before and after the Scheme
- QBEUK's SCR as at 31 December 2018, before and after the Scheme
- Documentation setting out the design and operation of QBEUK's Internal Model
- QBEUK's Capital Appetite Framework
- QBEUK's Internal Model validation reports, undertaken by a firm of external actuaries
- Internal Model validation risk area reports
- Schematic setting out QBE EO reinsurance programme
- QBE EO investment guidelines
- LTD Reserving Philosophy Guide
- Claims handling guidelines and processes
- Annual ORSA Report dated 8 March 2018
- QBE Group Risk Management Strategy

- Enterprise Risk Management Framework
- QBE Complaints procedure and guidelines
- Charts setting out the QBE EO group structure
- QBEUK Governance map
- QBE UK 2019 business plan extract
- CVs of key individuals involved in the reserving and capital processes at QBEUK

Information provided by legal advisers

- Draft insurance business transfer scheme document
- Draft letter to policyholders within the Autumn Portfolio
- Draft letter to TSEL, the sole policyholder within the Chestnut Portfolio
- Draft letter to policyholders within the Legacy Portfolio
- Draft letter to policyholders within the UKBG Portfolio
- Draft letter to brokers of policyholders within the Transferring Portfolio
- Draft letter to brokers of policyholders within the Existing EWICL Portfolio
- Draft letter to outwards reinsurers of the Autumn Portfolio
- Draft letter to the solicitors of claimants within the Transferring Portfolio
- Draft information pack for policyholders being notified
- Draft letter to recipients of information pack
- Draft communications strategy
- Draft witness statement for Gavin Bridges, European Claims Manager and Head of Legacy at QBEUK
- Draft witness statement for Steve Ryland at EWICL
- Draft text for the website

Other

I also relied on information arising from correspondence and discussions with QBEUK, EWICL, ARML and their legal advisers.

I have checked that all of the above information has been supplied by persons appropriately qualified to provide such information and I am satisfied that it is reasonable for me to rely on this information.

A number of the items received are of a commercially sensitive or confidential nature. All relevant information received has been used to inform the conclusions given in this report, whilst taking care to respect the confidentiality of the entities involved. It should be noted that there are no instances where I have omitted implications of this documentation from this report for the sake of respecting confidentiality. Therefore, in my opinion it is not necessary to produce a separate document exclusively for the Court providing further details of these data items although these items can be made available to the Court if required.

B Glossary of terms

Autumn LPTA Aggregate Limit	155% of the reserves of the Autumn Portfolio, as defined in the Autumn LPTA
Asbestos	A material previously commonly employed for its fire-retardant and insulation properties, Exposure to asbestos has subsequently been determined to cause cancer.
Asset	Generally, any item of property whether tangible or intangible, that has financial or monetary value.
Attritional claims	Claims which are not considered 'large' claims. Generally, these are claims with relatively low value.
Autumn Claims Float Account	The account created in respect of the Autumn LPTA from which claim payments relating to the Autumn Portfolio are made. This account is operated by ARML and maintained at a minimum level by TMR and ILS.
Autumn LPTA	The loss portfolio transfer agreement between QBEUK, TMR and ILS which covers the Autumn Portfolio
Autumn Portfolio	QBEUK's UK and Republic of Ireland employers' liability and public liability business which had inceptioned on or prior to 31 December 2007, except some specific policies remaining in QBEUK. The specific policies remaining in QBEUK are defined as the Retained Autumn Policies
Available capital	Total assets less total liabilities.
Available Own Funds	The portion of Own Funds that can be used to meet capital requirements after taking account of any restrictions.
Bad debt	A debt that cannot be recovered. Under Solvency II, technical provisions include an allowance for reinsurance bad debt.
Balance sheet	A statement of the assets, liabilities, and capital of a business or other organisation at a point in time.
Booked reserve	The claims reserve shown in the financial statements.
Capital requirements	The level of funds that an insurance or reinsurance undertaking is required to hold.
Catastrophe	An event that can cause severe damage or suffering. The event could be natural or man-made.
Chestnut Claims Float Accounts	The accounts created in respect of the Chestnut LPTA from which claim payments relating to the Chestnut Portfolio are made. These accounts are operated by ARML and maintained at a minimum level by ILS.
Chestnut LPTA	The loss portfolio transfer agreement between QBEUK and ILS which covers the Chestnut Portfolio
Chestnut Portfolio	<p>This portfolio consists of the majority of:</p> <ul style="list-style-type: none"> • UK employers' liability policies issued by QBE Insurance (Europe) Limited ("QIEL"), a predecessor company of QBEUK, for Tata Steel Europe Limited ("TSEL") expiring on or before 31 March 2016 • Global public and products liability, UK motor and UK personal accident policies expiring on or before 31 March 2016 <p>except for certain specific liabilities remaining in QBEUK. The liabilities remaining in QBEUK are defined as the Retained Chestnut Liabilities</p>

Claims reserve	Funds held for the payment of future claims.
Collateral Accounts	As part of the Chestnut LPTA, QBEUK paid the LPTA premium into these accounts established by ILS. These accounts refer to accounts holding cash and securities. They serve as collateral for the Chestnut LPTA. ILS and QBEUK agreed an investment manager to operate these accounts in accordance with investment guidelines agreed by both QBEUK and ILS.
Counterparty risk	The risk that the counterparty of a contract will not fulfil its contractual obligations.
Coverage ratio	The quantum of assets an insurer has to meet its regulatory capital requirements, expressed as a percentage of its regulatory capital requirements.
Credit rating	A measure of the financial security of a company provided by a third party agency.
Designated Bank Account	As part of the Autumn LPTA, QBEUK placed the majority of the LPTA premium into a segregated account established by ILS, in the name of Cell G. This account serves as collateral for the Autumn LPTA.
Direct policyholders	Policyholders of an insurance undertaking who are not themselves insurers or reinsurers.
Effective Date	The date at which the Scheme becomes legally binding. This is expected to be 4 December 2019.
Excess of Loss	This is a type of reinsurance contract whereby cover is provided by the reinsurer above a certain amount, up to a certain limit.
Existing EWICL Portfolio	The policyholders of EWICL prior to the Scheme.
Gross	Excluding the effect of reinsurance arrangements. For example, 'gross insurance liabilities' refers to insurance liabilities before taking into account any offsetting reinsurance assets.
Incurred but not enough reported ("IBNER")	An allowance for future developments on claims that have already been reported to the insurer.
Incurred but not reported ("IBNR")	An allowance for claims that have occurred prior to a particular date but have not yet been reported to the insurer plus future developments on claims that have already been reported to the insurer.
Incurred claims	The sum of the paid and outstanding claims
Independent Expert	The suitably qualified person that produces an independent report on the Scheme, in accordance with FSMA
Internal Model	A bespoke model developed by an insurance or reinsurance undertaking to calculate its Solvency Capital Requirement under Solvency II. All insurers are required to calculate their Solvency Capital Requirement using either an Internal Model or the Standard Formula.
Inwards reinsurance	Reinsurance coverage provided by a reinsurance undertaking to other insurance or reinsurance undertakings.
Large claims	Individual claims with a relatively high value which may be modelled at an individual level for reserving and capital modelling.

Legacy Portfolio	EWICL commenced underwriting general insurance business in 1964 and underwrote business through different distribution channels, namely: <ul style="list-style-type: none"> • direct retail motor and household business written out of local UK branches in Gloucester, Leicester and Redhill until it formally ceased underwriting in 1997 • participation in the English & American Underwriting Agency which has since been closed through a Scheme of Arrangement • participation in London Market reinsurance business writing alongside Charter Re up until the 1992 underwriting year • direct commercial general insurance including employers' liability written through UK insurance brokers covering shops; offices; and light commercial and industrial risks from 1985 to 1993. This business is referred to in this report as the "Legacy Portfolio".
Liability	A claim against the assets, or legal obligations of a person or organisation, arising out of past or current transactions or actions.
Liquidity	The degree to which an asset or security can be quickly bought or sold in the market without affecting the asset's price.
Long Tailed Disease	A disease where the symptoms take many years following the exposure period to present themselves
Man-made catastrophe risk	The risk of claims arising due to man-made catastrophes such as fire or aggregation of liability claims.
Market risk	Risk of adverse changes in net asset value as a result of movements in variables such as interest rates, exchange rates, equity values etc. It also includes the exposure to investment credit risk (the risk of default or adverse movements in credit ratings of the assets)
Mesothelioma	Cancer that affects the lining of the lungs, heart or abdomen often caused by inhalation of asbestos fibres.
Minimum Capital Requirement ("MCR")	The lower level of regulatory capital requirement under the Solvency II regime.
Natural catastrophe risk	The risk of claims arising due to natural catastrophes e.g. floods, windstorms, earthquakes etc.
Net	Including the effect of reinsurance arrangements. For example, 'net insurance liabilities' refers to insurance liabilities after deducting any offsetting reinsurance assets from the gross insurance liabilities.
Nil claims	A claim that results in no payment by the insurer.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events
Outstanding claims	The estimate of the claims made by the claims handling team of an insurer for claims that have been reported but not yet paid.
Own Funds	The excess of an insurer's assets over its liabilities on a Solvency II basis, as defined by the Solvency II rules.

Own Risk and Solvency Assessment ("ORSA")	The insurance or reinsurance undertaking's own assessment of the risks to which it is exposed and its solvency, as required under Solvency II.
Parent	An enterprise that controls another (called the subsidiary) through the ownership of greater than 50 percent of its voting stock.
Peer review	Process by which a piece of work is considered by at least one other individual, having appropriate experience and expertise, for the purpose of providing assurance as to the quality of the work in question.
Premium credit risk	The risk that Own Funds will be impacted due to unexpected failure to collect from counterparties (other than reinsurers) in the next year
Pure IBNR	An allowance for claims that have occurred prior to a particular date but have not yet been reported to the insurer. This excludes any future developments on claims that have already been reported to the insurer.
Quota share reinsurance	A type of reinsurance whereby risks are shared in pre-determined proportions between the insurer and reinsurer.
Reinsurance	An arrangement that an insurer has with another insurer or reinsurer whereby risks are shared (or passed on).
Reinsurance Credit Risk	The risk that losses arise due to credit defaults and deteriorations in the credit quality of outstanding third party reinsurance.
Remaining Portfolio	The policyholders that will remain in QBEUK following the Scheme.
Reserve strength	A measure of the likelihood that the claims reserve will be sufficient to meet future claims.
Residual Assets	Assets relating to the Transferring Portfolio that may not be, or may not be capable of being, transferred on the Effective Date.
Residual Liabilities	Liabilities relating to the Transferring Portfolio that may not be, or may not be capable of being, transferred on the Effective Date.
Retained Autumn Policies	Certain policies within QBEUK's UK and Republic of Ireland employers' liability and public liability business which had inceptioned on or prior to 31 December 2007, and which will be retained by QBEUK following the Scheme
Retained Chestnut Liabilities	<ul style="list-style-type: none"> • Any claim under the original policies issued by QIEL for TSEL relating to liabilities assumed by British Steel Limited ("British Steel"), or any predecessor entity or business of British Steel, pursuant to certain agreements affecting the transfer of the relevant undertaking from TSEL to British Steel • Any claims under the original policies issued by QIEL for TSEL relating to liabilities of Specialty Steel UK Limited ("Specialty Steel"), or any predecessor entity or business of Specialty Steel • Noise induced hearing loss/ deafness liabilities whereby the deafness is either caused or alleged to be caused over a period of time longer than one day. This means that The Chestnut Portfolio includes any claim for deafness or any similar hearing impairment that is caused or alleged to be caused by either a single exposure to sound pressure or other acute acoustic trauma occurring over a period of time of one day or less. <p>These liabilities will be retained by QBEUK following the Scheme</p>

Retrocession	The reinsurance of reinsurance
Retrocession Agreement	The agreement between TMR and ILS that covers the retrocession in respect of the Autumn Portfolio.
Reverse stress testing	An analysis to understand the events and circumstances that would render an insurer's business model unviable.
Risk Margin	Under Solvency II, insurers must hold a risk margin in excess of their best estimate of liabilities. This risk margin is designed to represent the amount of capital a third party would require to take on the obligations of a given insurance company. It effectively means that if an insurer were, as a result of a shock, to use up all its free surplus and capital, then it would still have sufficient assets to safely wind-up and transfer its obligations to a third party.
Run-off	A line of insurance business or an insurance undertaking that does not accept new business but continues to provide coverage for claims arising on its policies still in force and that makes payments for claims that have occurred on its policies.
the Scheme	Insurance Business Transfer Scheme of a portfolio of policies from QBEUK to EWICL
Section 13 Transfer	An insurance business transfer under Section 13 of the Assurance Companies Act 1909 in Ireland
Services Agreement	The agreement which sets out the outsourcing of certain services to ARML in respect of the Transferring Portfolio.
Solvency II	A regulatory regime for insurers which came into force on 1 January 2016 aimed at harmonising insurance regulation across all EU and EEA countries.
Solvency Capital Requirement ("SCR")	The higher level of regulatory capital requirements under the Solvency II regime.
Standard Formula	A standardised calculation for the Solvency Capital Requirement of an insurance or reinsurance undertaking, as prescribed under Solvency II. All insurers are required to calculate their Solvency Capital Requirement using either the Standard Formula or an Internal Model.
State of Risk	If the policyholder is an individual, the EEA State in which that policyholder has habitual residence at the date the contract is entered into. If the policyholder is not an individual, the EEA State in which the establishment of the policyholder to which the policy relates is situated at the date the contract is entered into.
Stress and scenario testing	An analysis to test the robustness of a financial quantity by varying a number of underlying assumptions (either one at a time or in various combinations) and observing the resulting change in the quantity of interest.
Subsequent Transfer Date	The date on which any Residual Assets and Residual Liabilities would be set to transfer to EWICL.
Subsidiary	An enterprise controlled by another (called the parent) through the ownership of greater than 50 percent of its voting stock.

Technical provisions	The insurance liabilities of an insurer, as determined for regulatory purposes. These are calculated as the provisions for the ultimate costs of settling all claims arising from events which have occurred up to the balance sheet date, including provision for claims incurred but not yet reported, less any amounts paid in respect of these claims; plus the provisions for claims arising on unexpired periods of exposure less any premium in respect of the business written that has not yet been received.
Transferring Business	The combination of the Transferring Portfolio and the excess of loss reinsurance contracts benefiting, as defined within the QBEUK witness statement.
Transferring Portfolio	The combination of the Autumn Portfolio and the Chestnut Portfolio
Trust Account	As part of the Retrocession Agreement, ILS placed the initial deposit and premium for the agreement into this account. ILS is responsible for maintaining, at all times, sufficient assets in this account in order to meet a minimum required level of collateral, as defined in the agreement.
UKBG Portfolio	The run-off portfolio of UK Building Guarantee liabilities transferred from Zurich Insurance Plc to EWICL by means of a Section 13 Transfer in March 2018
Underwriting risk	The risk that claims arising from premium earned over the following 12 months deviate adversely from those expected at the beginning of the year.
Unearned premium	The premium corresponding to the time period remaining on an insurance policy. Unearned premiums are in respect of the unexpired portion of the insurance and appear as a liability on the insurer's balance sheet.
Unearned reserve risk	The risk that the claims related to the unearned exposure in the closing balance sheet at year end are higher than expected at the beginning of the year.

C Abbreviations

ACPC	Average Cost Per Claim
APS	Actuarial Professional Standards
Aquiline	Aquiline Capital Partners
ARML	Armour Risk Management Limited
Armour	Armour Group Limited
AWP	Asbestos Working Party
British Steel	British Steel Limited
CICL	Crucible Insurance Company Limited
DGP	Developers Guarantee Period
DWP	Deafness Working Party
EAUA	English & American Underwriting Agency
EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
EIROS	Electricity Industry Run-Off Services
ELTO	Employers' Liability Tracing Office
EMB	QBEUK's Executive Management Board
ENIDs	Events Not In Data
EWICL	East West Insurance Company Limited
FCA	UK Financial Conduct Authority
FIA	Fellow of the Institute and Faculty of Actuaries
FOS	UK Financial Ombudsman Service
FRC	UK Financial Reporting Council
FSA	UK Financial Services Authority
FSAI	Fellow of the Society of Actuaries in Ireland
FSCS	UK Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
GAAP	Generally Accepted Accounting Principles
Grant Thornton	Grant Thornton UK LLP
HAVS	Hand and Arm Vibration Syndrome
IBNER	Incurred But Not Enough Reported
IBNR	Incurred But Not Reported

IFoA	Institute and Faculty of Actuaries
ILS	ILS Property & Casualty Re Limited
ILSIM	ILS Investment Management Limited
LMX	London Market Excess of Loss Reinsurance
LOD	Loss of Deposits
LPTA	Loss Portfolio Transfer Agreement
LTD	Long Tailed Disease
MCR	Solvency II Minimum Capital Requirement
NIHL	Noise Induced Hearing Loss
ORSA	Own Risk and Solvency Assessment
PRA	UK Prudential Regulation Authority
QBE EO	QBE European Operations plc
QBE Holdings EO	QBE Holdings (EO) Limited
QBE Limited	QBE Insurance Group Limited
QBEUK	QBE UK Limited
QIEL	QBE Insurance (Europe) Limited
RCC	QBEUK's Risk and Capital Committee
RPI	Retail Price Index
SCR	Solvency II Solvency Capital Requirement
SIP	Structural Indemnity Period
Specialty Steel	Specialty Steel UK Limited
SUP 18	Chapter 18 of the Supervision Manual from the FCA handbook
TAS	Technical Actuarial Standard
the Court	the High Court of England & Wales
the Scheme	Insurance Business Transfer Scheme of a portfolio of policies from QBEUK to EWICL
TMR	Tokio Millennium Re AG, Bermuda Branch
TPA	Third Party Adjuster
TSEL	Tata Steel Europe Limited
UKBG	United Kingdom Building Guarantee
USP	Undertaking Specific Parameter
ZIP	Zurich Insurance Plc

D Checklist against PRA's Statement of Policy and SUP18

The table below cross references the relevant sections of this report to the requirements for the Scheme Report, as set out in the Statement of Policy produced by the PRA in April 2015, namely "The Prudential Regulation Authority's approach to insurance business transfers".

It also cross references the relevant sections of this report to the guidance set out in Chapter 18 of the Supervision Manual ("SUP18") contained in the FCA Handbook of Rules and Guidance to cover scheme reports on the transfer of insurance business. These requirements are identical to those set out in the PRA's Statement of Policy. However, please note that the paragraph references in the table below are to the PRA Statement of Policy rather than to SUP18.

Reference to the PRA's approach to business transfers	Reference to relevant section within this report
<i>2.30 The Scheme report should comply with the applicable rules on expert evidence and contain the following information:</i>	
(1) who appointed the independent expert and who is bearing the costs of that appointment;	Paragraph 1.3 and 1.20
(2) confirmation that the independent expert has been approved or nominated by the PRA;	Paragraph 1.4
(3) a statement of the independent expert's professional qualifications and (where appropriate) descriptions of the experience that makes them appropriate for the role;	Paragraphs 1.23 to 1.26 and Appendix E
(4) whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence and details of any such interest;	Paragraphs 1.27 to 1.28
(5) the scope of the report;	Paragraphs 3.1 to 3.5
(6) the purpose of the Scheme;	Paragraph 5.1
(7) a summary of the terms of the Scheme in so far as they are relevant to the report;	Paragraphs 5.9 to 5.17
(8) what documents, report and other material information the independent expert has considered in preparing the report and whether any information that they requested has not been provided;	Appendix A
(9) the extent to which the independent expert has relied on:	
(a) information provided by others; and	Paragraphs 13.2 to 13.7
(b) the judgement of others;	Paragraphs 13.2 to 13.7

(10) the people the independent expert has relied on and why, in their opinion, such reliance is reasonable;	Paragraphs 13.2 to 13.7
(11) Their opinion of the likely effects of the Scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between:	
(a) transferring policyholders;	Paragraph 2.20
(b) policyholders of the transferor whose contracts will not be transferred; and	Paragraph 2.21
(c) policyholders of the transferee;	Paragraph 2.22
(12) Their opinion on the likely effect of the Scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the Scheme;	Paragraphs 2.26, 2.27 and 10.15 and 10.16
(13) what matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in their opinion, be relevant to policyholders' considerations of the Scheme; and	Paragraphs 3.6, 3.8 and 3.9
(14) for each opinion that the independent expert expresses in the report, an outline of their reasons.	Throughout the report
<i>2.32 The summary of the terms of the Scheme should include:</i>	
(1) a description of any reinsurance arrangements that it is proposed should pass to the transferee under the Scheme; and	Paragraph 5.18
(2) a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred.	N/A
<i>2.33 The independent expert's opinion of the likely effects of the Scheme on policyholders should:</i>	
(1) include a comparison of the likely effects if the Scheme is or is not implemented;	Likely effects if the Scheme is implemented – Addressed throughout the report Comparative assessment of likely effects should the Scheme not be implemented – Paragraphs 11.47 to 11.58
(2) state whether they considered alternative arrangements and, if so, what;	Paragraph 3.8

(3) where different groups of policyholders are likely to be affected differently by the Scheme, including comments on those differences they consider to be material to the policyholders; and	Sections 7 to 11
(4) include their views on:	
(a) the effect of the Scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;	Section 9
(b) the likely effects of the Scheme on matters such as investment management, new business strategy, administration, claims handling, expense levels and valuation bases in relation to how they may affect:	<p>Investment management - Paragraphs 10.2 to 10.7</p> <p>New business strategy: Paragraphs 10.17 to 10.21</p> <p>Administration (Policy servicing) - Paragraphs 11.8 to 11.12</p> <p>Claims handling - Paragraphs 11.3 to 11.7</p> <p>Expense levels - Paragraphs 10.8 to 10.9</p> <p>Valuation bases:</p> <p>Assets: Paragraphs 8.13 and 8.58</p> <p>Liabilities: Sections 7, 8 and 9, paragraphs 8.13 and 8.58</p>
(i) the security of policyholders' contractual rights;	Section 9
(ii) levels of service provided to the policyholders; or	Paragraphs 11.3 to 11.12
(iii) for the long-term insurance business, the reasonable expectations of policyholders; and	Not applicable to Scheme – the Scheme does not involve long term insurance business
(c) the cost and tax effects of the Scheme, in relation to how they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations.	<p>Cost implications of the Scheme: Paragraphs 10.8 to 10.9</p> <p>Tax implications: Paragraphs 10.11 to 10.12</p>
2.36 For a scheme involving long-term insurance business, the report should:	
(1) describe the effect of the Scheme on the nature and value of any rights of policyholders to participate in profits:	N/A
(2) if any such rights will be diluted by the Scheme, describe how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable	N/A

as between different classes and generations of policyholders;	
(3) describe the likely effect of the Scheme on the approach used to determine:	
(a) the amount of any non-guaranteed benefits such as bonuses and surrender values; and	N/A
(b) the levels of any discretionary charges;	N/A
(4) describe what safeguards are provided by the Scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm;	N/A
(5) include the independent expert's overall assessment of the likely effects of the Scheme on the reasonable expectations of long-term insurance business policyholders;	N/A
(6) state whether the independent expert is satisfied that for each firm, the Scheme is equitable to all classes and generations of its policyholders; and	N/A
(7) state whether, in the independent expert's opinion, for each relevant firm the Scheme has sufficient safeguards (such as principles of financial management or certification by a with-profits actuary or actuarial function holders) to ensure that the Scheme operates as presented.	N/A

E My experience

My professional experience is set out below:

- I have worked in or consulted to the general insurance industry for more than 25 years.
- I am a Partner in Grant Thornton and lead Grant Thornton's provision of actuarial and risk services to the general insurance sector.
- I have fulfilled the role of Independent Expert for several Part VII Transfers and Section 13 Transfers of insurance liabilities, with my other transaction experience including acting as Scheme Actuary for several schemes of arrangements; independent expert assignments; and due diligence for mergers and acquisitions.
- I am currently fulfilling the role of Independent Expert for a transfer of non-life insurance liabilities from an insurance group to a run-off insurance specialist under Part VII of FSMA in the UK
- In addition, the table below sets out the Part VII Transfers and Section 13 Transfers on which I have acted as the Independent Expert or Independent Actuary.

Transfer	Transfer type	Sanctioned
Aviva Insurance Limited to Aviva Insurance Ireland DAC	Part VII	January 2019
CNA Insurance Company Limited to CNA Insurance Company (Europe) S.A.	Part VII	December 2018
Zurich Insurance plc to Catalina Insurance Ireland DAC	Section 13	October 2018
Zurich Insurance plc to East West Insurance Company Limited	Section 13	March 2018
Congregational & General Insurance plc to International Insurance Company of Hannover SE	Part VII	November 2017
Colbourne Insurance Company Limited to NRG Victory Reinsurance Limited	Part VII	July 2017
Guardian Assurance Limited to R&Q Insurance (Malta) Limited	Part VII	September 2016
Harworth Insurance Company Limited to Royal & Sun Alliance plc	Part VII	August 2014

- I have substantial reserving experience for an extensive variety of classes of business, including personal and commercial lines, and for a very wide range of companies.
- My other experience in the general insurance sector includes: producing skilled persons reports under s166 of FSMA 2000; Solvency II including all three pillars; design and construction of capital models; provision of strategic advice; design and implementation of management information systems; rating of portfolios and individual risks; reviews of rating adequacy; development of pricing models; and review and design of reinsurance programmes.
- In 2010, I set up an actuarial team for Quinn Insurance Limited (Under Administration) ("Quinn"). Between 2010 and 2012, I acted as the de facto Chief Actuary and Chief Underwriting Officer for Quinn.
- Prior to joining Grant Thornton in 2006, I was the Chief Actuary for Travelers Insurance Company Limited in the UK and Ireland.
- Before that, I was a senior consultant in the general insurance division of Towers Perrin.

- I hold a Chief Actuary (Non-life with Lloyd's) Practising Certificate and a Lloyd's Syndicates Practising Certificate. I have previously also held an Irish Signing Actuary Practising Certificate and been recognised as a Responsible Actuary by the financial regulator in Liechtenstein.
- My professional experience includes terms on the Institute and Faculty of Actuaries' Council, Management Board, General Insurance Board, Education Board, General Insurance Reserving Oversight Committee, General Insurance Education and CPD Committee (including a term as chairman), and Education Committee.

F Extract from Engagement Letter

Terms of engagement between QBE UK Limited, East West Insurance Company Limited and Grant Thornton UK LLP

Fulfilling the role of Independent Expert on the proposed Part VII transfer from QBE UK Limited to East West Insurance Company Limited

We write to acknowledge your instructions to act in the above matter and set out below our understanding of the work that you wish us to perform and the terms on which we shall undertake it.

Our Instructions

You have asked us to provide an Independent Expert to report on the proposed insurance business transfer scheme to transfer business from QBE UK Limited ("QBEUK") to East West Insurance Company Limited ("EWICL") (the "Scheme"). The Independent Expert's report will be prepared in accordance with and for the purposes set out in Part VII of the Financial Services and Markets Act 2000 ("FSMA") and for no other purpose.

As part of this assignment, the Independent Expert will produce the following reports:

- the main Independent Expert report, prior to the Directions Hearing
- the summary report, prior to the Directions Hearing
- the supplementary report, prior to the Sanctions Hearing

The different groups of policyholders affected by the Scheme are expected to be:

- the transferring policyholders
- the policyholders who will remain with QBEUK following the transfer
- the policyholders who are with EWICL prior to and following the transfer.

The Independent Expert's analysis and formal reports will follow the relevant FSMA requirements and associated supplemental guidance. His reports will consider the Scheme as a whole and its effect on the policyholders of QBEUK and EWICL. In particular, it will include, but not be limited to, an opinion on:

- the terms of the Scheme generally and the effect which the Scheme will have on the (re)insurance policies of QBEUK and EWICL.
- the way in which QBEUK and EWICL will conduct their (re)insurance business but taking into account the particular circumstances of each of the different groups of policyholders
- the likely scope for deteriorations in each of QBEUK's and EWICL's claims reserves (i.e. the likelihood and extent to which each of the companies' reserves may prove inadequate).
- the impact of the Scheme on the security/financial strength afforded to the different groups of policyholders of QBEUK and EWICL involved in the Scheme.
- the corporate governance structures operating in QBEUK and EWICL and the impact on the different groups of policyholders in QBEUK and EWICL involved in the Scheme.
- the impact of the Scheme on the policyholders' access to the Financial Service Compensation Scheme and the Financial Ombudsman Service.
- the impact of the Scheme on the levels of service, including claims handling, provided to the different groups of policyholders of QBEUK and EWICL involved in the Scheme.

- the existing and proposed agreements between QBEUK and EWICL and their reinsurers.
- guarantees and/or agreements (if any) between QBEUK and EWICL.
- guarantees and/or agreements (if any) between each of QBEUK and EWICL and their respective parent company.
- transactions (outside the Scheme) that impact upon one or both of QBEUK and EWICL.
- the terms and conditions (if any) expected to be imposed by the Scheme to be presented to the Court.
- the adequacy of any safeguards in the Scheme intended to protect the interests of the affected policyholders
- the fairness of any mechanism implemented at the same time as the Scheme, but not included in the Scheme
- the communications made to policyholders.
- the matters required by applicable provisions of the PRA's Policy Statement PS7/15 and Chapter 18 of the supervision manual in the FCA's Handbook.
- any other matters drawn to my attention by the PRA or FCA or which are required by the PRA or FCA to be addressed within my reports.

The above list is not intended to be exclusive to any other aspects which may be identified during the completion of the project and which are considered by the Independent Expert to be relevant.

We have been informed by QBEUK and EWICL that they are currently updating their reserve reviews. We have further been informed that, following these exercises, we may receive different reserving positions from the two entities.

The Independent Expert will not be directly involved in the formulation of the proposed Scheme although he expects to give guidance during the evolution of the detailed proposals on those issues which concern the Independent Expert or which the Independent Expert considers unsatisfactory. The Independent Expert will meet with QBEUK and EWICL at an early stage to identify key issues and will support the companies in their liaison with and provision of information to the PRA and FCA, and share his reports (and drafts of them) with the legal advisers retained by QBEUK and EWICL and those employees and directors of QIEL and EWICL or their affiliates involved in the Scheme.

Any changes to the scope of the assignment should be by mutual agreement and confirmed in writing.

