Report on the proposed business transfer from The Solicitors Indemnity Mutual Insurance Association Limited to R&Q Gamma Company Limited

Report of the Independent Expert under Part VII – Section 109 of the Financial Services and Markets Act 2000

24 May 2018

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1. Introduction

1.1 Section 109 of the Financial Services and Markets Act 2000 (‘FSMA’) requires that a scheme report must accompany an application to the High Court of England and Wales (the ‘Court’) to approve an insurance business transfer scheme. This scheme report should be produced by a suitably qualified independent person (the ‘Independent Expert’) who has been nominated or approved by the Prudential Regulation Authority (‘PRA’). The scheme report should address the question of whether any policyholders impacted by the insurance business transfer are adversely affected to a material extent.

1.2 The Solicitors Indemnity Mutual Insurance Association Limited (‘SIMIA’) and R&Q Gamma Company Limited (‘R&Q Gamma’) have jointly nominated Alex Lee (‘I’, ‘me’) of Ernst & Young LLP (‘EY’, ‘we’, ‘us’) to act as the Independent Expert for the proposed insurance business transfer scheme (the ‘Transfer’) of the insurance business of SIMIA to R&Q Gamma. The Transfer is intended to be effected on or before 30 September 2018 (the ‘Transfer Date’).

1.3 This nomination has been approved by the PRA in consultation with the Financial Conduct Authority (‘FCA’).

1.4 SIMIA is a mutual insurance company whose sole business is the provision of professional indemnity insurance to firms of solicitors based in England and Wales. It was established in 1986 by a group of law firms to reduce the cost and to secure the availability of professional indemnity insurance for solicitors. SIMIA is owned solely by its members.

1.5 In September 2016, SIMIA entered into a 100% reinsurance contract with R&Q Insurance Malta Limited (‘RQIM’) covering their entire business effective from 1 April 2016. This arrangement cedes all the retained net liabilities within SIMIA to RQIM. This reinsurance contract will terminate on the Transfer Date.

1.6 The SIMIA board previously delegated the day-to-day management of SIMIA to SIMIA Management Company, a subsidiary of the Thomas Miller group. On the inception of the 100% reinsurance agreement with RQIM, SIMIA’s claims management was outsourced to R&Q Market Services Limited (‘RQMS’). During December 2017, the claims handling agreement was novated from RQMS to R&Q Central Services Limited (‘RQCS’) as part of an internal reorganisation.

1.7 R&Q Gamma was acquired by Randall & Quilter Investment Holdings Ltd (‘R&Q’ or the ‘Group’) in December 2016 from The Royal London Mutual Insurance Society Limited (‘RLM’). R&Q Gamma both underwrote business directly and assumed business underwritten in the past by entities acquired by RLM. Direct business was written using the RLM sales force, brokers and through R&Q Gamma’s London operations. More details on the assumed business can be found in section 5.12 of this report.

1.8 R&Q Gamma’s administration has also been managed by RQMS until December 2017 and thereafter by RQCS.

1.9 The terms of my engagement are set out in a letter dated 31 August 2017. An extract of this letter setting out the scope of my work is included in Appendix B.

1.10 R&Q Gamma will be bearing the costs of producing this report.

Layout of this report

1.11 My report is structured as follows:

- The first five sections describe my conclusion, the detail of the Transfer, the scope of my report, background to the entities involved, and a summary of the methodology I have used to reach my conclusion.
- Section 6 describes the work that I have carried out to assess the claims reserves of SIMIA and R&Q Gamma.

- Section 7 describes the work that I have carried out to assess the capital modelling of SIMIA and R&Q Gamma.
- Section 8 includes balance sheets of SIMIA and R&Q Gamma and my assessment of the policyholder security considerations.
- This report contains a number of technical terms and these are defined in the Glossary in Appendix A.
- A checklist against the guidance on scheme reports as set out in the PRA's 'Statement of Policy, the PRA's approach to insurance business transfers – April 2015' ('PRA's Statement of Policy') and Chapter 18 of the Supervision Manual of the FCA Handbook ('SUP18 of the FCA Handbook') can be found in Appendix E.

Professional experience

1.12 I am a Fellow of the Institute and Faculty of Actuaries and am certified to act as a Signing Actuary for Lloyd's of London regulatory opinions.

1.13 I am an Associate Partner in the European Actuarial Services practice of Ernst & Young LLP, and have more than 20 years' experience in general insurance. Prior to joining Ernst & Young LLP in 1999 I worked in the Commercial Insurance department of Eagle Star / Zurich Financial Services.

1.14 I have skills in all areas of general insurance actuarial work (including reserving, capital, pricing, transactions, etc.), and have previously acted as Independent Expert for four other insurance business transfer schemes.

1.15 Full details of my experience can be found in Appendix A.

Independence

1.16 I can confirm that I have no direct or indirect connections with SIMIA or R&Q Gamma that I believe would affect my ability to act as the Independent Expert for the Transfer. In particular, I have never worked on any project involving SIMIA or R&Q Gamma.

1.17 The firm of Ernst & Young LLP has not carried out any projects for either SIMIA or R&Q Gamma.

1.18 I have no shareholding, investment or any other financial connection with any of the parties to the Transfer.

Use of this report

1.19 The purpose of this report is, as stated in SUP18 of the FCA Handbook and the PRA's Statement of Policy to inform the Court of the likely effect of the Transfer upon policyholders. This report is not necessarily suitable for any other purpose.

1.20 A copy of this report will be made available to the PRA, the FCA, the Court, and any other person entitled to receive a copy under the FSMA Regulations 2001. A copy will also be made available to any person on request.

1.21 I assume no responsibility whatsoever in respect of, arising out of, or in connection with the contents of this report to parties other than those mentioned above. If other parties choose to rely in any way on the contents of this report then they do so entirely at their own risk.

1.22 This report has been prepared solely for the purposes of the FSMA requirements for insurance business transfer schemes and solely in respect of the Transfer. It should not be relied upon for any other purpose by any party.

1.23 Where figures are shown within the report on a combined entity basis these are for illustrative purposes only. There are no statutory requirements to calculate figures on a combined entity basis unless otherwise stated.

1.24 Draft versions of this report and any other interim working papers must not be relied on by any person for any purpose.

1.25 Judgements about the conclusions drawn in this report should be made only after considering the report in its entirety as any part or parts read in isolation may be misleading.

1.26 The responsibilities of Ernst & Young LLP (including its partners and staff) shall also be limited as stated above.

Professional guidance

1.27 This report complies with the applicable rules on expert evidence and with the guidance for scheme reports set out by the PRA in the PRA's Statement of Policy and by the FCA in SUP 18 of the FCA Handbook, as noted above in section 1.19.

1.28 This report complies with Technical Actuarial Standards TAS100: Principles for Technical Actuarial Work and TAS 200: Insurance as issued by the Financial Reporting Council ('FRC'), which is responsible for setting UK actuarial standards.

1.29 The review performed on this work complies with Actuarial Profession Standard X2: Review of Actuarial Work issued by the Institute and Faculty of Actuaries.

1.30 The work is performed by someone who complies with Actuarial Profession Standard X3: The Actuary as an Expert in Legal Proceedings issued by the Institute and Faculty of Actuaries.

1.31 I believe that this compliance has been achieved with no major deviations from the guidelines. I have not discussed the timing of future cash flows as I do not believe this is of relevance to my report, or of value to the readers of my report given the purpose of this exercise.

2. Executive Summary

Purpose of this report

2.1 My report considers the effect of the Transfer upon policyholders of SIMIA and R&Q Gamma. It contains a description of the Transfer and the methodology used during the course of my work to assess the security provided to policyholders before and after the Transfer for the transferring policyholders (i.e., the policyholders of SIMIA) and the receiving policyholders (i.e., the existing policyholders of R&Q Gamma). I have also considered the impact of the Transfer on reinsurers whose reinsurance contracts are being transferred pursuant to the terms of the Transfer. I also provide my conclusion on the Transfer together with reasons why I have reached this conclusion.

Background to the entities involved

SIMIA

2.2 SIMIA is a mutual insurance company whose sole business is the provision of professional indemnity insurance excess of £1m to firms of solicitors based in England and Wales. It was established in 1986 by a group of law firms aiming to reduce the cost of and secure professional indemnity insurance for solicitors. Firms that have been insured by SIMIA may be subject to calls for further funds from SIMIA, may be able to share in any surplus that is available on a winding up of SIMIA and may also receive distributions of profit from SIMIA.

2.3 The board is made up of non-executive directors who are current or ex-partners of firms of solicitors insured with SIMIA.

2.4 SIMIA underwrote business from 1986 to 2011 underwriting years.

2.5 SIMIA's target was to underwrite a maximum limit of circa. £4.5m excess of a £1m underlying layer. All of its business was written in the UK with a small amount of the business covering risks arising out of branches of the law firms which were providing advice in other locations (including Europe and North America). The £4.5m target was achieved by writing varying percentages depending on the policy limits.

2.6 SIMIA purchased outwards reinsurance to reduce its exposure to a net £1m except for North American business where the exposure is limited to £1.5m. Further details on SIMIA's outwards reinsurance arrangements are covered in sections 5.18 to 5.26. In addition, SIMIA has some exposure in relation to the Assigned Risks Pool ("ARP") which is not covered by its outwards reinsurance arrangements. The ARP is the system under which solicitors who are unable to obtain insurance cover on the open market are given temporary cover to enable them to remain in practice. Overall, the amount of SIMIA's exposure from the ARP is considered to be immaterial.

2.7 In September 2016, SIMIA entered into a 100% reinsurance contract with R&Q Insurance Malta Limited ('RQIM') covering their entire business effective from 1 April 2016. This arrangement cedes all the retained net liabilities within SIMIA to RQIM. An amendment to the Loss Portfolio Transfer ('LPT') arrangement has been made by RQIM and SIMIA to allow for the LPT arrangement to terminate following the transfer of SIMIA's liabilities to R&Q Gamma. This arrangement will terminate on the Transfer Date.

2.8 The SIMIA board has delegated the day-to-day management of SIMIA's business affairs and operations to SIMIA Management Company ('Thomas Miller'), a subsidiary of the Thomas Miller group. On the inception of the 100% reinsurance agreement with RQIM, SIMIA's claims management was outsourced to RQMS, a subsidiary of R&Q. During December 2017, the claims handling agreement was novated from RQMS to RQCS as part of an internal reorganisation.

2.9 SIMIA is currently investing the majority of its assets in a Sterling Liquidity Fund, with a small proportion held as cash and bank deposits.

R&Q Gamma

2.10 R&Q Gamma Company Limited ('R&Q Gamma') was acquired by Randall & Quilter Investment Holding Ltd ('R&Q' or the 'Group') in December 2016 from Royal London Mutual Insurance Society Limited ('RLM'). Under the ownership of RLM, R&Q Gamma was called The Royal London General Insurance Company Limited. R&Q Gamma underwrote business directly and also assumed business underwritten in the past by entities acquired by RLM.

2.11 Direct business can be split into the following categories:

- Business written through the RLM sales force and brokers. This business consisted of household and commercial insurance policies written between 1985 and 1999, covering 38,000 unique policyholder names.
- Business written through the London operations of R&Q Gamma. This covered direct and facultative open market risks.

2.12 The business assumed by R&Q Gamma under Schedule 2C of the Insurance Companies Act 1982, which was approved on 27 December 2000, is summarised below:

- United Friendly Insurance Plc – household, accident and health business prior to and including 1st March 2000.
- United Friendly General Insurance Limited – motor, employers' liability and public liability business prior to and including 30th June 1996.
- Refuge Assurance Plc – household, motor, employers' liability and public liability business prior to and including 31st December 1996.
- The Lion Insurance Company Limited – motor business prior to and including 30th September 1995.

2.13 United Friendly Insurance Plc, United Friendly General Insurance Limited and Refuge Assurance Plc were acquired by RLM as a result of its acquisition of United Assurance Group. The Lion Insurance Company Limited was a wholly owned subsidiary of R&Q Gamma.

2.14 R&Q Gamma is exposed to occupational disease reserves. These are predominantly low severity hearing loss claims with a small proportion of asbestos related claims. There is also one potential larger public liability claim which is uncertain and is expected to be resolved through a court case in Q3 2018.

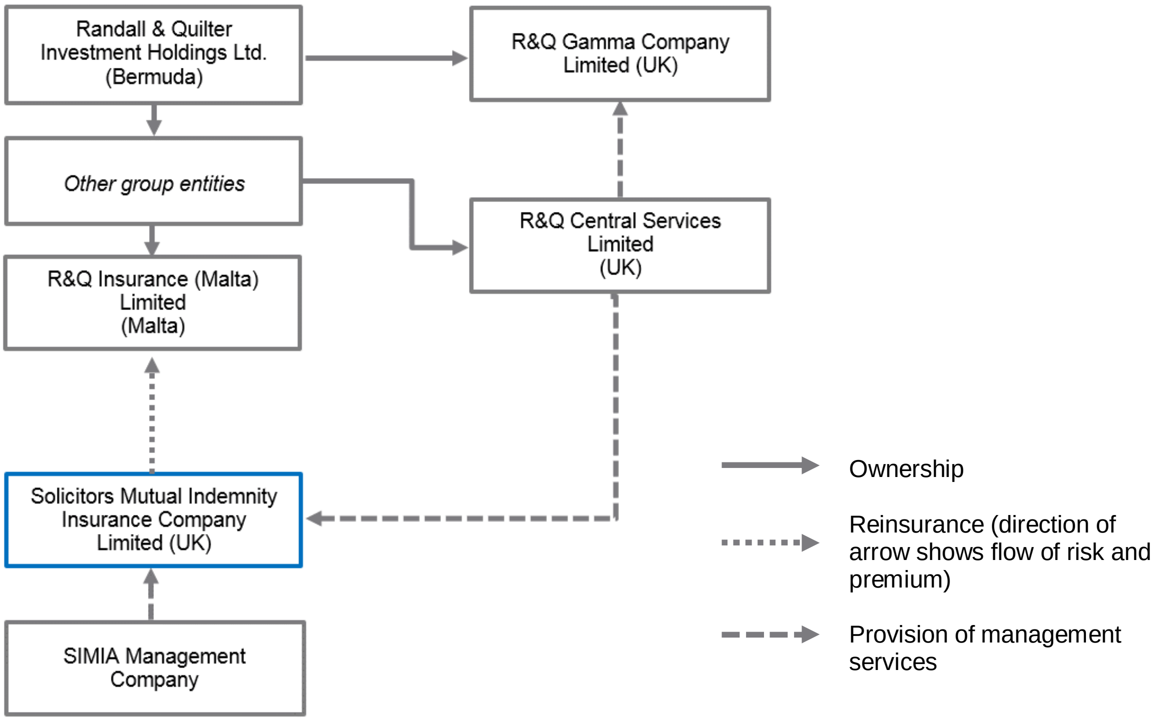
2.15 R&Q Gamma's administration is managed by R&Q Central Services Limited ('RQCS'), a subsidiary of R&Q.

2.16 R&Q Gamma's assets consist predominantly of an intercompany loan to RQIH. The loan is denominated in GBP and reflects a 12 month renewable contract with the loan amount callable on demand. RQIH is rated bbb by AM Best (which is a rating given to entities thought to have a good ability to meet their financial obligations).

2.17 Full details on the background of SIMIA and R&Q Gamma can be found in section 5 of the report.

2.18 The diagram below illustrates the key relationships between stakeholders and entities at present.

Figure 1: Current structure of R&Q Gamma and SIMIA (showing the main entities only)



The Transfer

2.19 SIMIA wishes to transfer

- its entire insurance liabilities
- all of the reinsurance assets apart from the 100% reinsurance arrangement with RQIM (as this will terminate at the time of the Transfer), including any rights associated with the above
- the right to receive funds in the segregated account on termination of the reinsurance arrangement with RQIM
- all rights, liabilities, obligations and powers in relation to the ARP
- all rights and title in the records that relate to the transferred policies

to R&Q Gamma by means of a Part VII transfer.

2.20 The transferred business includes all policies written by or on behalf of or which is otherwise a policy of SIMIA prior to the Transfer Date. SIMIA does not expect any policies to be excluded from the Transfer, but as set out in paragraphs 2.44 and 2.75, the Transfer makes provision for the theoretical possibility that a subset of policies may be excluded due to regulatory or legal reasons.

2.21 All reinsurance contracts, apart from the 100% reinsurance arrangement with RQIM, relating to SIMIA business prior to the Transfer Date will also be transferred to R&Q Gamma.

2.22 SIMIA's reinsurance agreement with RQIM will terminate on the date of the Transfer and the balance of funds in the segregated account will be due to SIMIA on termination.

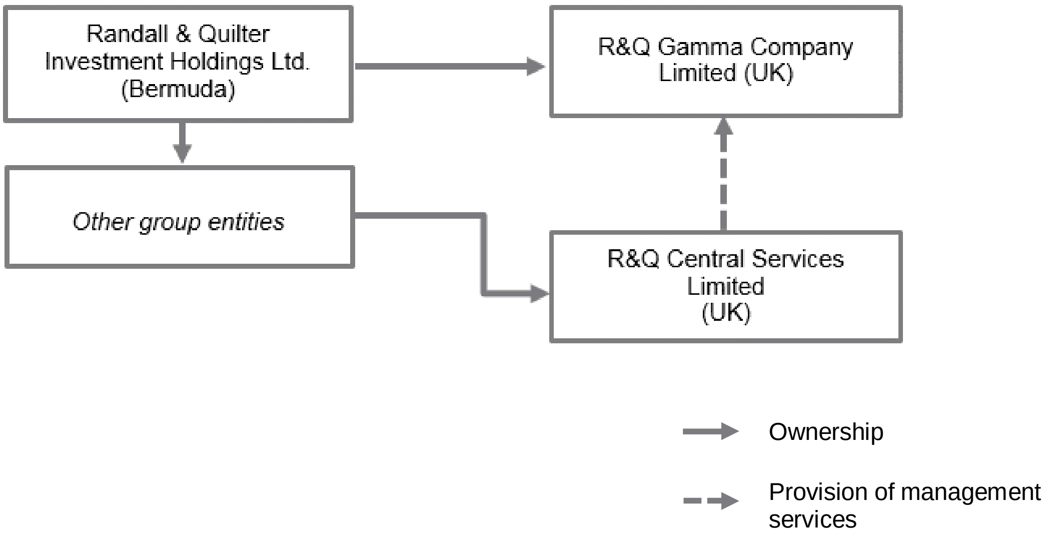
2.23 Following the Transfer, all policyholders of SIMIA would become policyholders of R&Q Gamma.

2.24 Subject to all liabilities being transferred, SIMIA plans to cancel their Part 4A permission to carry out regulated activities, distribute any remaining assets to eligible solicitors firms and dissolve without winding up pursuant to the Order of the Court that sanctions the Scheme. This will be effective from the date on which a director of SIMIA certifies that the final distribution of the remaining assets of the Transferor has taken place (after the Part 4A permission has been cancelled by the PRA).

2.25 The rights and powers of SIMIA under its articles of association and rules will not transfer to R&Q Gamma, and will remain with SIMIA until SIMIA is dissolved. This means that until SIMIA is dissolved, firms that have been insured by SIMIA will remain obliged to contribute capital in the event of a call being made by SIMIA and will remain able to receive a distribution in relation to the SIMIA's profits. I would not expect that SIMIA would be required to make a call on firms for capital following the Transfer given all of its insurance liabilities will have been transferred to R&Q Gamma and hence SIMIA would not be exposed to any further claims deteriorations.

2.26 The diagram below illustrates the key relationships between stakeholders and entities as they are expected to be after the Transfer.

Figure 2: Expected structure of R&Q Gamma post-Transfer (showing the main entities only)



Purpose of the Transfer

2.27 The purpose of the Transfer is to ensure that the entire insurance business of SIMIA is transferred to R&Q Gamma.

2.28 The Transfer is closely linked to the 100% reinsurance agreement ceding all of SIMIA’s retained net liabilities to RQIM. This reinsurance agreement offers protection against adverse claims experience and the possibility of an unexpected deterioration in SIMIA’s claims exposure. Some substantial deteriorations have been seen in SIMIA’s historical claims experience and despite a comprehensive reinsurance programme, there sometimes remains a cost of reinstating the reinsured layers in response to large claims exhausting particular layers.

2.29 As described above, pursuant to the terms of its reinsurance arrangement with RQIM, SIMIA is already ceding 100% of its professional indemnity liabilities to RQIM. Further, RQCS already manages the handling of SIMIA’s claims under a Claims Handling and Administration Services Agreement effective from December 2017.

2.30 The Transfer is also proposed to give financial certainty to the firms that have been insured by SIMIA upon whom cash calls can be made if required. This is due to the following reasons:

- SIMIA has been granted exemption by the PRA from meeting Solvency II regulatory capital requirements until January 2019. This has been granted on the basis that all of SIMIA's insurance liabilities will be extinguished or transferred by January 2019. SIMIA is currently required to meet the base capital resources requirement which is lower than the regulatory capital requirements under Solvency II. So if the Transfer were not to take place, SIMIA would be required to hold more capital which could result in calls on the firms that have been insured by SIMIA. Details of the capital requirements can be found in section 7 of the report.

- The Transfer would also allow a reduction in operational costs as it is expected that SIMIA would be dissolved following the transfer of all of its liabilities and the distribution of its remaining assets to the firms that have been insured by SIMIA. The costs associated with running the company were the Transfer not to take place could require a further supplementary call to be made on the firms that have been insured by SIMIA.

2.31 I do not expect the Transfer to be contentious for the following reasons:

- R&Q Gamma is well capitalised, holding well in excess of the regulatory capital required to meet its liabilities, whereas SIMIA has currently been granted permission by the PRA to hold lower capital than would be required under Solvency II until January 2019 on the basis that all of its insurance liabilities would be extinguished or transferred by January 2019. If the Transfer were not to take place, SIMIA would be required to hold more capital to meet regulatory capital requirements. The Transfer will ensure that the policyholders are directly protected by the Solvency II capital requirements applicable to R&Q Gamma.

- SIMIA is currently ceding 100% of its insurance liabilities to RQIM, and hence is exposed to the counterparty default risk where RQIM fails to meet its reinsurance obligations, although the reinsurance premium has been kept in a segregated account and can only be withdrawn to pay out for claims covered under the reinsurance arrangement, and hence any counterparty default risk is small. This reinsurance arrangement will terminate on the Transfer Date and as a result SIMIA will no longer have exposure to this risk.

- In addition, the security of SIMIA and R&Q Gamma policyholders is improved by the Transfer as R&Q Gamma has a stronger solvency ratio following the Transfer compared to that prior to the Transfer as well as a stronger solvency ratio relative to RQIM and SIMIA. It must also comply with Solvency II regulatory requirements unlike SIMIA's current regulatory arrangements. Therefore, neither policyholders nor claimants would be at a disadvantage as a result of the Transfer. Details on the change of R&Q Gamma's solvency ratios before and after the Transfer can be found in section 8 of this report.

- The outsourcing of handling SIMIA claims to RQMS began in September 2016 and this claims handling agreement was novated to RQCS in December 2017. RQCS will continue to manage claims after the Transfer. RQCS has experience of handling run-off insurance business. The claims handling agreement specifies the level and performance of service expected to be provided and this will be maintained after the Transfer. As a result, there should not be any changes in the claims handling or customer service as a result of the Transfer.

- Operational efficiencies may be gained by transferring SIMIA's policyholders into R&Q Gamma and subsequently dissolving SIMIA. These efficiencies could be gained through reduced compliance, regulatory, audit and administrative costs.

Which liabilities are moved from SIMIA to R&Q Gamma as part of the Transfer?

2.32 The Transfer will involve moving all of the insurance liabilities of SIMIA to R&Q Gamma. This includes all liabilities arising from transferred policies and transferred reinsurance contracts.

2.33 After the Transfer, R&Q Gamma would be responsible for paying all of the insurance claims of policyholders, including those of SIMIA.

2.34 The 'chain of security' for policyholders of each of SIMIA and R&Q Gamma is described below. This shows the order in which assets can be used to make a claim payment to a policyholder. I believe that the changes to the chain of security that result from the Transfer are not material for the reasons given in paragraphs below.

Chain of security - current SIMIA policyholders before the Transfer

2.35 From the point of view of SIMIA's policyholders the current chain of security is as follows:

1. SIMIA has comprehensive reinsurance cover from a range of London Market and Lloyd's reinsurers and these recoveries would be collected first where applicable to an individual claim.

2. LPT reinsurance between SIMIA and RQIM who reinsures 100% of SIMIA's insurance liabilities, net of external reinsurance. This would also cover any bad debt or non-performance from external reinsurers.

3. Other assets, such as cash, of SIMIA. Details of the assets are shown in the table in section 8.5.

4. Under the provisions of SIMIA's Articles of Association and rules, the Board of SIMIA can, if necessary, levy calls on the firms that have been insured by SIMIA in order to raise the required funds.

5. In the event of insolvency of SIMIA, any assets of SIMIA would be available to claimants. There may also be claimants (depending on the nature of their policy and claim) who may be protected by the Financial Services Compensation Scheme in the UK in such an insolvency.

Chain of security - current R&Q Gamma policyholders before the Transfer

2.36 From the point of view of R&Q Gamma's policyholders the current chain of security is as follows:

1. External reinsurance available to R&Q Gamma where applicable to an individual claim. For more details on R&Q Gamma's reinsurance arrangements, please see paragraphs 5.18 to 5.26.

2. Assets of R&Q Gamma. Details of the assets are shown in the table in section 8.5.

3. In the event of insolvency of R&Q Gamma, any assets of R&Q Gamma would be available to claimants. There may also be claimants (depending on the nature of their policy and claim) who may be protected by the Financial Services Compensation Scheme in the UK in such an insolvency.

Chain of security - Policyholders after the Transfer

2.37 After the Transfer, all policyholders will be insured by R&Q Gamma and the chain of security for all policyholders should be identical to the policyholders of R&Q Gamma before the Transfer as follows:

1. External reinsurance available to R&Q Gamma.

2. Assets of R&Q Gamma (post Transfer).

3. In the event of insolvency of R&Q Gamma, any assets of R&Q Gamma would be available to claimants. There may also be claimants (depending on the nature of their policy and claim) who may be protected by the Financial Services Compensation Scheme in the UK in such an insolvency.

2.38 Following the Transfer, the policyholders of SIMIA will no longer benefit from the 100% reinsurance agreement between SIMIA and RQIM or the possibility of SIMIA raising further capital via supplementary calls as steps in the chain of security. However, this does not have a negative impact on the security of either SIMIA or R&Q Gamma policyholders as the solvency position of R&Q Gamma following the Transfer offers a more than adequate level of policyholder protection as described in more detail in paragraph 8.14.

Reinsurance arrangements being transferred

2.39 As part of the Transfer, all contracts of reinsurance whereby external reinsurers provide reinsurance to SIMIA, apart from the reinsurance arrangement with RQIM which will terminate on the date of the Transfer, will be transferred so that following the Transfer such reinsurance shall be for the benefit of R&Q Gamma.

2.40 Any default on these third party recoveries will be borne by R&Q Gamma.

Which assets are moved from SIMIA to R&Q Gamma as part of the Transfer?

2.41 All insurance liabilities and reinsurance assets of SIMIA and any rights related to these will be transferred to R&Q Gamma as part of the Transfer. This includes:

- The benefit of reinsurance contracts with external reinsurers, apart from the reinsurance arrangement with RQIM, as mentioned above.

- All contracts and the benefit of any services provided to SIMIA. The claims management services agreement with RQCS will terminate on the Transfer Date and RQCS will continue to manage claims services as part of its existing agreement with R&Q Gamma.

- All rights against any third party in relation to the transferred business or arising as a result of SIMIA having carried on the aforementioned business.

2.42 In addition, the full amount of the LPT premium for the 100% reinsurance arrangement between SIMIA and RQIM which is currently contained in a segregated account, less any claims made and a £250k interim RI fee payable to RQIM, will be released to SIMIA on the Transfer Date and will then transfer to R&Q Gamma under the Transfer Scheme. All the assets in the segregated account are held in cash. More details can be found in section 8 of the report.

2.43 The rights and powers of SIMIA under its articles of association and rules will not transfer to R&Q Gamma, and will remain with SIMIA until SIMIA is dissolved. This means that until SIMIA is dissolved, firms that have been insured by SIMIA will remain obliged to contribute capital in the event of a call being made by SIMIA and will remain able to receive a distribution in relation to the SIMIA's profits.

Policies, liabilities and assets not transferring

2.44 The investments that SIMIA currently has which are outside of the segregated account will remain within SIMIA and will not be transferred.

2.45 The Transfer scheme makes provision for the possibility that a SIMIA policy does not transfer because (a) a policy was concluded in another EEA state and the local regulator objects to its transfer (SIMIA does not believe any policy was concluded in another EEA state) (b) SIMIA and R&Q Gamma agree before the final hearing date that it should not transfer or (c) the Court, for some reason, determines that the policy should not transfer. R&Q Gamma and SIMIA do not expect that there will be any such policies.

2.46 In the unlikely event that any policy does not transfer on the Effective Date, the Transfer scheme ensures that related reinsurance remains in place in relation to that policy until such time as the policy can subsequently transfer to R&Q Gamma.

Methodologies adopted in my review

2.47 The scope of my review is to consider the effect of the Transfer on policyholders of SIMIA and R&Q Gamma, and the reinsurers of SIMIA whose contracts are being transferred. I have checked that the Transfer would not adversely affect any group of policyholders to a material extent.

2.48 An important part of the scope is to assess whether the security provided to any group of policyholders or reinsurers is adversely affected to a material extent by the Transfer. A policyholder's security would be adversely affected to a material extent if, following the Transfer, that policyholder's insurer would be materially less likely to be able to pay any future claim that is due to the policyholder. Similarly a reinsurer would be adversely affected if their exposure to claims was increased. The groups of policyholders that I have considered in this report include the following:

- Transferring policyholders of SIMIA
- Non-transferring policyholders of SIMIA (if any)
- Existing policyholders of R&Q Gamma

I have also considered in this report reinsurers of SIMIA whose contracts are being transferred.

2.49 For the purpose of this report, I have considered the transferring policyholders of SIMIA to be one class without considering separately the effect of the Transfer on policyholders with and without claims. This is due to the fact that the effect of the Transfer on policyholders' security and level of service will be the same regardless of their claims situation.

2.50 I have used a number of different approaches to determine the quantitative effect on the security provided to policyholders. I have performed a review of the modelling work carried out both by R&Q Gamma and SIMIA.

2.51 The claims reserve of an insurance company is an estimate of the amount of money that the company will need to pay out to its policyholders as claim payments in the future. It is an unknown amount of money (because future claim amounts are unknown and uncertain) but it can be estimated by the company by using various statistical techniques. An important question when considering the security provided to policyholders of a company is whether the estimation of the claims reserves has been carried out in an appropriate way. This is because there is a risk that the company has underestimated the amount of money that it will need to pay future claim amounts to policyholders, and therefore a risk that it will not be able to pay those claim amounts. Therefore, I have considered the adequacy of the most significant parts of the claims reserves.

2.52 A second important aspect of the modelling work I have reviewed relates to the uncertainty over the size of the future claim amounts. The amount of capital in an insurance company is the difference between the value of the assets of the company (e.g., investments, cash and amounts due from debtors), and the value of the liabilities of the company (e.g., future claim payments and amounts due to creditors). It is one measure of the financial strength of the company. Insurance regulators require that an insurance company has at least a certain minimum amount of capital (i.e., so that it has a level of buffer to help make future claim payments). The capital requirement is needed because the ultimate amount of the future claim payments is uncertain; the insurance company and the regulator wish to be confident that the company is able to meet all future claim payments, even in an unlikely adverse scenario. However, this does not mean that a company will be able to meet all claim payments in all circumstances; only that there is a high probability of being able to do so. As part of my work I have checked that the probability of SIMIA and R&Q Gamma being able to meet their respective future claim payments is not adversely affected by the Transfer, and also that R&Q Gamma and SIMIA's ability to meet the regulatory capital requirements is not adversely affected by the Transfer.

2.53 For the review of both the capital and the claims reserves I have used my wider market knowledge derived from similar projects to benchmark the appropriateness of the methods and assumptions used (by benchmarking I mean that I have reviewed the methods and parameters used by SIMIA and R&Q Gamma and compared them against the methods and parameters used across the insurance market by similar companies). A summary of my methodology is provided in section 6 for the analysis of the claims reserves and section 7 for the analysis of the capital model.

2.54 To assess whether the security provided by any reinsurer is adversely affected by the Transfer I have considered whether the liabilities of any reinsurers will change following the Transfer.

Accounting basis used for my assessment of the Transfer

2.55 Both SIMIA and R&Q Gamma value their assets and liabilities according to UK GAAP (UK Generally Accepted Accounting Principles).

2.56 I consider that UK GAAP is an appropriate basis for considering the Transfer from the perspective of SIMIA and R&Q Gamma.

2.57 I also consider the impact of the Transfer on a Solvency II basis to assess the capital positions of the two entities and how these are affected by the Transfer.

What happens if the Scheme does not proceed

2.58 I have not considered in any detail what would happen if the Scheme were not to proceed (e.g. the scheme is not sanctioned or either party decides not to proceed). My understanding is that if this were to happen the existing structure and arrangements would continue with the LPT not being terminated although I note that SIMIA would have the option to terminate the LPT in this scenario. Were the LPT not to be terminated then the policyholders would then be continue in their current structure and so would not be adversely affected.I consider it very unlikely that SIMIA would exercise its option to terminate the LPT in this scenario because this would require it to obtain further funding, from the law firms who are its members, in order to meet regulatory capital requirements under Solvency II.

Overall conclusion

2.59 I confirm that I understand my duty to the Court.

2.60 I have considered the Transfer and its likely effects on the transferring policyholders of SIMIA and the existing policyholders of R&Q Gamma. I have also considered the effect on any remaining policyholders of SIMIA should they not transfer to R&Q Gamma pursuant to the Transfer.

2.61 I conclude that there would be no material change to the security provided to policyholders and that no group of policyholders or reinsurers affected by the Transfer of the contracts would be adversely affected to a material extent by the Transfer, and that therefore there is no reason that the Transfer should not go ahead.

Key reasons

2.62 The purpose of the Transfer is to ensure that the entire insurance business of SIMIA is transferred to R&Q Gamma.

2.63 Further, as discussed in paragraph 2.31 the outsourcing of handling SIMIA claims to RQMS began in September 2016 and this claims handling agreement was novated to RQCS in December 2017. RQCS will continue to manage claims after the Transfer and it has experience of handling run-off insurance business. The claims handling agreement specifies the level and performance of service expected to be provided and this will be maintained after the Transfer. As a result, there should not be any changes in the claims handling or customer service as a result of the Transfer.

2.64 The Transfer is proposed to simplify matters by transferring the insurance business of SIMIA to R&Q Gamma and ultimately liquidating SIMIA. This will eliminate the compliance and administrative costs of operating and maintaining SIMIA as a separate legal entity, which under Solvency II is required to hold any overheads within the technical provisions as well as the Solvency Capital Requirement.

2.65 There would be no material changes to the reinsurance arrangements with the exception of the reinsurance agreement with RQIM which will terminate on the date of the Transfer.

2.66 The changes to the chain of security are not material (as discussed in 2.34).

2.67 SIMIA is currently only required to meet the base capital resources requirement and it holds capital at a lower level than the Solvency II regulatory capital requirements. This has been approved by the PRA on the condition that all of SIMIA's insurance liabilities will be extinguished or transferred by January 2019. The Transfer would ensure that the policyholders are better protected by the higher capital requirements on R&Q Gamma who must comply with the Solvency II regulation.

2.68 R&Q Gamma has sufficient capital to meet its Solvency II Solvency Capital Requirement ('SCR'). R&Q Gamma currently meets its capital requirement by a large margin; it has calculated a solvency ratio, of available capital divided by the SCR, of 434% as at 30 June 2017. I consider this to be a strong level of capital to account for both R&Q Gamma's and SIMIA's liabilities and have reviewed the appropriateness of the available capital and tested the appropriateness of the SCR by calculating a number of capital measures as described in more detail in section 7 of this report. This suggests that the security provided to policyholders by R&Q Gamma is good.

2.69 I have carried out a review of the claims reserves. The amount of this claims reserve is reasonable in my opinion, although as the SIMIA reserves relate to professional indemnity claims, they are subject to considerable uncertainty. This is based on the review I have carried out of the claims reserving work done on behalf of SIMIA.

2.70 I have outlined below the impact of the Transfer on the different groups of policyholders I refer to in paragraph 2.48 and the reinsurers of SIMIA whose contracts are being transferred:

- **Transferring policyholders of SIMIA:** Following the Transfer, policyholders of SIMIA will benefit from better protection as a result of a stronger solvency ratio of R&Q Gamma. The level and performance of claims handling services will be unchanged, as described in paragraph 2.63**,** as SIMIA's claims handling agreement (which was originally with RQMS but was novated to RQCS in December 2017) will continue on the same terms after the Transfer.

- **Non-transferring policyholders of SIMIA (if any):** In the remote possibility a policy does not transfer from SIMIA to R&Q Gamma for some reason, the policyholder will not be adversely affected by the Transfer as the existing reinsurance protection provided by RQIM will be replaced by an indemnity from R&Q Gamma which shall remain until the relevant policy is transferred to R&Q Gamma.

- **Existing policyholders of R&Q Gamma:** Following the Transfer, policyholders of R&Q Gamma will benefit from better protection as a result of a stronger solvency ratio of R&Q Gamma. The level and performance of claims handling services do not change as a result of the Transfer and are therefore not impacted. In addition, there will be no material changes to the chain of security as described in paragraph 2.37**.**

- **Reinsurers of SIMIA whose contracts are being transferred:** I have considered whether the liabilities of any reinsurers will change following the Transfer. I do not believe that the liabilities of SIMIA's reinsurers will change as they will continue to be required to pay out claims in respect of the same events as before the Transfer. As a result I do not believe that the reinsurers are adversely affected by the Transfer.

2.71 For the above reasons I conclude that the Transfer would not have a material adverse impact on the policyholders of R&Q Gamma and SIMIA or the reinsurers of SIMIA whose contracts are being transferred.

Legal Opinions

2.72 I have not needed to take any third party legal opinion on any aspect of the Transfer.

Insured risks outside of EU

2.73 I have discussed with the management of SIMIA and R&Q Gamma the possible impact on policyholders outside of the European Union ('EU') or European Economic Area ('EEA'). If the Transfer were not seen to be effective in those non-EU jurisdictions I do not believe there would be a negative impact on policyholders for SIMIA or R&Q Gamma. All policyholders of SIMIA are based in the UK. Although some policyholder entities have branches in overseas jurisdictions, any overseas exposure is expected to be small. All the contracts were governed by English law and as a result the Transfer will be effective to transfer these contracts. As SIMIA has no assets overseas which could be attached in satisfaction of a claims, in the unlikely event that a policyholder or claimant obtained a judgment against SIMIA in another jurisdiction in respect of a claim under a policy, that judgment would have to be enforced in the UK, where the effectiveness of the Transfer would be recognised. The terms of the Transfer provide that any proceedings in respect of the business transferred to R&Q Gamma (which would include proceedings to enforce a judgment) which are commenced against SIMIA after the Transfer Date will be deemed to have been commenced against R&Q Gamma. Any order resulting from such proceedings would therefore be made against R&Q Gamma.

2.74 In any event, I consider it unlikely that beneficiaries outside of the EU or EEA would seek to challenge before their local courts the power of the Court to authorise the Transfer from SIMIA to R&Q Gamma as they are not materially disadvantaged by the Transfer and it would imply that they would prefer for their policies to stay within an insurance company with very limited assets (and no assets at all, once dissolved following completion of the Transfer)**.**

Retained policies

2.75 It is expected that all policies will be transferred on the Transfer Date. Should any policies not transfer on the Transfer Date, R&Q Gamma shall indemnify SIMIA against any liabilities arising out of any retained business on a continuing basis. SIMIA shall then reimburse R&Q Gamma in respect of any payment made by R&Q Gamma out of, and to the extent of, any recovery subsequently made in respect of such liabilities under a retained reinsurance.

Brexit

2.76 'Brexit' has introduced or exacerbated a number of risks for insurers operating in the UK, particularly for those that trade across EU borders. Some potential areas of concern are market volatility with a particular emphasis on exchange rate volatility, a higher risk of negative interest rates in the future and the impact of a changing regulatory environment. There is also the potential that post Brexit that UK insurers lose the ability that currently exists to insure risks in the EU (outside of the UK) without obtaining authorisation from the local regulators.

2.77 Despite these risks to the insurance market as a whole, I do not believe that changes in the insurance market or the UK regulatory environment resulting from the outcome of the EU referendum will have an adverse effect on policyholders or affect my conclusions relating to the Transfer as set out in this report. Reasons for these are detailed in section 8 (paragraphs 8.38 to 8.41) of the report.

3. Scope

3.1 The scope of my work is detailed in the extract from my terms of reference provided in Appendix B. There are no areas where the actual work performed differs from this agreed scope.

3.2 My review of the balance sheets of R&Q Gamma is as at 30 June 2017 and that of SIMIA is as at 31 May 2017, being the most recent date at which financial accounts were available.

3.3 My report considers the effect of the Transfer upon the policyholders of SIMIA and R&Q Gamma, and reinsurers of SIMIA whose contracts are being transferred. It contains a description of the Transfer, the methodology I have used to analyse the Transfer, the opinions I have formed, and reasons why I have formed these opinions.

3.4 The use of 'I' and 'my' in this report generally refers to the work done by myself and the team operating under my direct supervision during the course of this review. However when it is used in reference to an opinion, it is mine and mine alone.

Alternative arrangements

3.5 I am not aware of any alternative arrangements to the Transfer proposed by any party, so I have not considered it necessary to discuss alternative proposals within this report.

Use of data and reports

3.6 My view on the insurance liabilities of the companies involved is based upon my review of the actuarial reports and other supporting working files produced by SIMIA, R&Q Gamma, RQIM and their external advisors, and discussions with R&Q actuaries, including a review of some of their documentation.

Reliance on data

3.7 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 and also note that much of my analysis has been based on financial and internal management accounts which have been verified by SIMIA and R&Q Gamma themselves or their external auditors. I have also received specific statements of data accuracy from the management of R&Q Gamma and SIMIA.

3.8 A summary of the data provided to me can be found in Appendix D. All the data I have requested I have been provided.

3.9 I have also placed reliance upon the data insofar as when assessing claims I have not considered potential future claims arising from causes not substantially recognised in the historical data except to the extent that such claims (and their impact) are included incidentally in the data. I consider this approach to be reasonable and in line with accepted actuarial practice.

Future changes of ownership

3.10 I have not considered any future changes of ownership of any of the companies involved in the Transfer. I am not aware of any proposals to change ownership at the time of writing this report.

Peer review process

3.11 In accordance with the internal control processes of Ernst & Young LLP, the work documented in this report has been peer reviewed by a suitably qualified person (an Actuary within my own firm who has considerable experience working in capital modelling and reserving in the London Market). The peer review process has included a review of the methodology used and discussion of the key elements of the analysis.

4. Methodology

4.1 In this section I describe my approach to assessing the Transfer.

4.2 The scope of my review is to consider the effect of the Transfer on R&Q Gamma's policyholders and the policyholders of SIMIA, as well as the reinsurers of SIMIA whose contracts are being transferred.

4.3 My approach to assessing the Transfer has been to perform the following activities.

Understand the nature and structure of the Transfer and identify the groups of policyholders that would be affected

4.4 I have discussed the nature and structure of the Transfer, as well as the groups of policyholders that would be affected by the transfer with SIMIA and R&Q Gamma, and reviewed their documentation.

Assess the financial positions of R&Q Gamma and SIMIA

4.5 The level of security provided to policyholders of an insurance company depends on the available capital of the company, and in particular on the probability that this level of capital is sufficient to make claim payments as they fall due.

4.6 Insurers are also subject to capital requirements imposed by regulators; the PRA in the case of R&Q Gamma and SIMIA. If the actual level of capital of the insurer comes close to or falls below the level of required capital then the regulator may intervene or impose restrictions on the day-to-day running of the company. The level of actual available capital compared to regulatory required capital is another measure of the security provided to policyholders. See paragraph 4.11 below for further information on my review of the modelling undertaken by R&Q Gamma with respect to regulatory capital (SIMIA is not currently required to calculate Solvency II capital requirements and instead is required to meet the base capital resources requirement, as discussed in section 7.26).

4.7 I have considered the balance sheets of R&Q Gamma and SIMIA as part of my assessment of their relative financial positions, including the net assets of the companies and the level of capital.

4.8 I have compared the balance sheets of R&Q Gamma (as at 30 June 2017) and SIMIA (as at 31 May 2017), being the most recent date at which financial accounts were available. This is discussed in section 8.

Assess the claims reserves of R&Q Gamma and SIMIA

4.9 An important part of the security provided to policyholders is the strength of the claims reserves (i.e., the estimate of the amount of money the insurer will have to pay out in the future in respect of policies already sold). The claims reserves generally form the largest part of the liabilities of an insurer.

4.10 I have therefore considered the appropriateness of the claims reserves included on the balance sheet for each of R&Q Gamma and SIMIA. This is discussed in section 6.

Assess the capital modelling undertaken and the capital positions of R&Q Gamma and SIMIA

4.11 To further review the financial position of R&Q Gamma and SIMIA, I have reviewed the modelling undertaken to assess regulatory required capital.

4.12 The European Commission has developed regulatory requirements for insurance and reinsurance undertakings within the EU known as 'Solvency II'.

4.13 The key metric to trigger regulatory intervention under Solvency II is the SCR, which should be determined as the economic capital to be held by insurance and reinsurance undertakings in order to ensure that those undertakings will still be in a position, with a probability of at least 99.5 %, to meet their obligations to policyholders and beneficiaries over the following 12 months. It is intended to represent a normal target level of capital for the insurer, and capital falling below this level would trigger a response from the insurer's regulator. A Minimum Capital Requirement ('MCR') is also calculated.

4.14 Companies which are exempted from complying with Solvency II are required to meet the Capital Resources requirement, which is equal to the higher of the base capital resources requirement (an absolute minimum specified by regulation) and the general insurance capital requirement (calculated by reference to the company's premiums and claims).

4.15 I have considered the capital position of SIMIA and the approach taken by R&Q Gamma in calculating its SCR. This is discussed in section 7.

Consider the potential impact of the Transfer on levels of customer service

4.16 I have considered how the level of customer service provided to policyholders could change following the Transfer. This is discussed in section 8.

Consider the implications of the Transfer for the level of security being offered to each group of policyholders

4.17 I have considered each group of policyholders both before and after the Transfer and the relative level of security available to them. This is discussed in section 2 relating to the chain of security, sections 6 and 7 relating to claims reserves and capital, and section 8 relating to financial statements and solvency.

Consider other factors that might affect policyholders (such as ongoing expense levels)

4.18 I have considered other factors that might affect policyholders, such as ongoing expense levels, tax implications, investment management implications and pension arrangement through discussions with R&Q Gamma and their external advisors. These are described in section 8.

5. Background

History of SIMIA and R&Q Gamma

SIMIA

5.1 SIMIA is a mutual insurance company whose sole business is the provision of professional indemnity insurance excess of £1m to firms of solicitors based in England and Wales. It was established in 1986 by a group of law firms aiming to reduce the cost and secure the availability of professional indemnity insurance for solicitors. Firms that have been insured by SIMIA may be subject to calls for further funds from SIMIA, may be able to share in any surplus that is available on a winding up of SIMIA and may also receive distributions of profit from SIMIA.

5.2 The board is made up of non-executive directors who are current or ex-partners in firms of solicitors insured with SIMIA.

5.3 SIMIA underwrote business from 1986 to 2011. The policies were issued on a claims made basis (i.e. policies covered actual or potential claims against solicitors that were notified by solicitors to SIMIA within the policy period). Professional negligence claims against solicitors are subject to limitation periods which mean that those claims must be brought within certain time limits. The applicable limitation period in most professional negligence cases is 6 years from the date of the negligence. However, this may be extended where the negligence only becomes apparent at a later stage. In those cases the relevant limitation period is three years from the date of knowledge of the facts which give rise to the claim. There is a ‘long stop’ date of 15 years within which claims must be brought.

5.4 The policy years 1986 to 2001 are now closed as they are over 15 years ago which means no new claims can be made against the insured solicitors’ firms can be made for those underwriting years.

5.5 SIMIA’s target was to underwrite a maximum limit of circa. £4.5m excess of a £1m underlying layer. Most of its business was written in the UK with a very small amount covering branches of the law firms which were providing advice in other locations (including Europe and North America). The £4.5m target was achieved by writing varying percentages depending on the policy limits.

5.6 SIMIA purchased outwards reinsurance to reduce its exposure to a net £1m except for North American business where the exposure is limited to £1.5m. Further details on SIMIA’s outwards reinsurance arrangements are covered in sections 5.18 to 5.26.

5.7 In September 2016, SIMIA entered into a 100% reinsurance contract with RQIM covering their entire business effective from 1 April 2016. This arrangement cedes all the retained net liabilities within SIMIA to RQIM. This arrangement was originally put in place in the anticipation that the SIMIA’s liabilities would be transferred to RQIM. Now the intention is to transfer the liabilities to R&Q Gamma. The reinsurance contract will be terminated on the Transfer Date.

5.8 The board previously delegated the day-to-day management of SIMIA to specialist managers, SIMIA Management Company, a subsidiary of the Thomas Miller group. This group also manages several mutual insurance companies, including the UK P&I Club. On the inception of the 100% reinsurance agreement with RQIM, SIMIA’s claims management was outsourced to RQMS. During December 2017, the claims handling agreement was novated from RQMS to RQCS as part of an internal reorganisation.

5.9 SIMIA is currently investing the majority of its assets in a Sterling Liquidity Fund, with a small proportion held as cash and bank deposits.

R&Q Gamma Company Limited

5.10 R&Q Gamma was acquired by R&Q in December 2016 from RLM. Under the ownership of RLM, R&Q Gamma was called The Royal London General Insurance Company Limited. R&Q

Gamma underwrote business directly and also assumed business underwritten in the past by entities acquired by RLM.

5.11 Direct business can be split into the following categories:

- Business written through the RLM sales force and brokers. This business consisted of household and commercial insurance policies written between 1985 and 1999, covering 38,000 unique policy holder names.
- Business written through R&Q Gamma's London operations. This covered direct and facultative open market risks.

5.12 The business assumed by R&Q Gamma under Schedule 2C of the Insurance Companies Act 1982, which was approved on 27 December 2000, is summarised below:

- United Friendly Insurance Plc – household, accident and health business prior to and including 1st March 2000.
- United Friendly General Insurance Limited – motor, employers' liability and public liability business prior to and including 30th June 1996.
- Refuge Assurance Plc – household, motor, employers' liability and public liability business prior to and including 31st December 1996.
- The Lion Insurance Company Limited – motor business prior to and including 30th September 1995.

5.13 United Friendly Insurance Plc, United Friendly General Insurance Limited and Refuge Assurance Plc were all acquired by RLM as a result of its acquisition of United Assurance Group. The Lion Insurance Company Limited was a wholly owned subsidiary of R&Q Gamma.

5.14 Prior to the establishment of R&Q Gamma as a general insurer, RLM had reinsured its general insurance business to Norwich Union Fire Insurance Society Limited ('Norwich Union') under a general business reinsurance and administration agreement. RLM transferred the whole of its general insurance business to R&Q Gamma on 31 December 1983. R&Q Gamma then reinsured all general insurance business with Norwich Union under a quota share reinsurance, ceding 60% of risks underwritten in 1984 and 50% of risks underwritten in 1985, following which the reinsurance arrangement ceased.

5.15 R&Q Gamma is exposed to occupational disease reserves. These are predominantly low severity hearing loss claims with a small proportion of asbestos related claims. There is also one potential larger public liability claim which is uncertain and is expected to be resolved through a court case in Q3 2018.

5.16 R&Q Gamma's assets consist predominantly of an intercompany loan to RQIH. The loan is denominated in GBP and reflects a 12 month renewable contract with the loan amount callable on demand. RQIH is rated bbb by AM Best (which is given to entities thought to have a good ability to meet their financial obligations).

5.17 R&Q Gamma's administration is managed by RQMS until December 2017 and thereafter by RQCS.

Reinsurance arrangements

Before the Transfer

SIMIA

5.18 SIMIA has placed reinsurance with a number of reinsurers operating within the Lloyd's and London Market through the broker, Miller Insurance Services. This consists of excess of loss reinsurance for each of the 2002 to 2010 years of account. The maximum line placed with any one reinsurer on any one layer has not exceeded 27% (with the exception of Munich Re as discussed in paragraph 5.24).

5.19 SIMIA purchased outwards reinsurance to reduce its exposure to a net £1m except for North American business where the exposure is limited to £1.5m. However, the first £1m layer of the outwards reinsurance programme has an aggregate excess of £1m so that SIMIA cannot recover the first £1m of losses that otherwise this layer would respond to. In addition, SIMIA has some exposure in relation to the Assigned Risks Pool (“ARP”) which is not covered by its outwards reinsurance arrangement. The ARP is the system under which solicitors who are unable to obtain insurance cover on the open market are given temporary cover to enable them to remain in practice. Overall, the amount of SIMIA’s exposure from the ARP is considered to be immaterial.

5.20 In addition to the £4.5m professional indemnity cover provided by SIMIA under each underlying contract with its policyholders, SIMIA provided cover for defence costs in an unlimited amount. Each year SIMIA had outwards reinsurance in respect of £1.0m per underlying policy in respect of these defence costs (which was referred to as "Fees break-out cover"). I understand from SIMIA that this cover has only been used very infrequently.

5.21 For all years apart from 2008 and 2010, the aggregate excess of £1m has been breached so recoveries have been made from SIMIA’s reinsurers. In all cases apart from one, reinsurance claims have not exceeded the second layer of reinsurance cover.

5.22 For the 2008 and 2010 years, there are currently no reinsurance claims paid and any adverse development of claims for these years will initially have to be borne by SIMIA. The first layer of reinsurance cover for these two years is £1m excess of £1m and both years have an aggregate excess of £1m. This means that before being able to recover amounts on this layer SIMIA would need to retain the first £1m of claims that fell into this layer.

5.23 For the UK business, each open year has multiple reinstatements available in order to reinstate the reinsurance cover that has been exhausted in return for the additional payment of premium. There are four reinstatements available at 100% for the 2002 to 2007 years and four reinstatements at 75% for the 2008 to 2010 years. The 2006 year, which has the worst claims experience of any year, still has reinstatements to cover a further two total losses. For the US business, where the reinsurance was provided as a single layer of £3m excess of £1.5m there is one reinstatement available for each year from 2002 to 2007 and then two reinstatements for 2008 to 2010.

5.24 During the period 1 October 2005 to 30 September 2009, SIMIA acted as a fronting company for Munich Re UK General Branch. Excess of loss reinsurance was placed with limits of £5m excess of £4.5m. All of this business was ceded to Munich Re in exchange for a fee as part of the fronting arrangement so SIMIA’s net liability for these claims would effectively be nil. R&Q was advised that these policies have never been impacted by any claims.

5.25 The reinsurer security on the excess of loss programme is 100% Lloyd’s and AM Best ‘A’ or higher rated London market companies, with the exception of a 4% line on the 2002 year of the programme underwritten by Global General which underwent a solvent scheme in 2011, the effect of which was to extinguish Global General’s liability in respect of the reinsurance.

5.26 In September 2016, SIMIA entered into a 100% reinsurance contract with RQIM covering their entire business effective from 1 April 2016. This arrangement cedes all the retained net liabilities within SIMIA to RQIM. This reinsurance contract will terminate on the Transfer Date.

R&Q Gamma

5.27 R&Q Gamma’s reinsurance programme is summarised below. All the covers incepted on 1 January 1989 and had a 12-month duration.

- £50,000 excess of £100,000 covering public liability, health liability and householders’ liability.
- £350,000 excess of £150,000 covering motor liability and physical damage, public liability, employers’ liability and householders’ liability.

- £500,000 excess of £500,000 covering motor liability and physical damage, public liability, employers' liability and householders' liability.

For example, if R&Q Gamma incurs a £1m loss on a public liability claim, it would retain the first £100,000 of loss and receive a recovery of £900,000 from its reinsurers. If it incurs a £1m loss on an employers' liability claim, then it would retain the first £150,000 of loss and receive a recovery of £850,000 from its reinsurers.

After the Transfer

5.28 It is intended that all SIMIA's reinsurance arrangements, apart from the reinsurance agreement with RQIM, will be transferred as part of the Transfer such that R&Q Gamma will be substituted as the reinsurer party on the same terms which applied prior to the Transfer Date. Any reinsurance recoveries received by SIMIA in relation to third party reinsurance will be transferred to R&Q Gamma.

5.29 Any default on these third party recoveries will be borne by R&Q Gamma.

Priority of policyholders

5.30 In the event of insolvency, the insolvency procedure for both SIMIA and R&Q Gamma would be governed by English law. As such, direct policyholders of SIMIA and R&Q Gamma would be at the same rank before and after the transfer and have the same right to the assets representing the technical provisions of the insurance company. Any reinsurance policyholders would rank after the direct policyholders, both before and after the Transfer. Within SIMIA and R&Q Gamma all policyholders are direct policyholders. There is therefore no change in priority for those policyholders.

6. Claims reserves

6.1 The following table shows a breakdown of the gross and net claims reserves of SIMIA as at 31 May 2017 and R&Q Gamma as at 30 June 2017.

Table 1: Total gross and net reserves of SIMIA (as at 31 May 2017) and R&Q Gamma (as at 30 June 2017) (£'000s)

	SIMIA	R&Q Gamma
Gross Reserves	9,152	1,191
Net Reserves	0	487

6.2 SIMIA underwrote business from 1986 to 2011. The policies were issued on a claims made basis (i.e. policies covered actual or potential claims against solicitors that were notified by solicitors to SIMIA within the policy period). Professional negligence claims against solicitors are subject to limitation periods which mean that those claims must be brought within certain time limits. The applicable limitation period in most professional negligence cases is 6 years from the date of the negligence. However, this may be extended where the negligence only becomes apparent at a later stage. In those cases the relevant limitation period is three years from the date of knowledge of the facts which give rise to the claim. There is a 'long stop' date of 15 years within which claims must be brought.

6.3 SIMIA entered into a 100% reinsurance contract with RQIM in September 2016 covering its entire business effective from 1 April 2016, and hence has a net reserve of zero.

6.4 The table below shows the outstanding liabilities booked by SIMIA as at 31 May 2017 and by R&Q Gamma as at 30 June 2017 within their respective management accounts.

Table 2: Gross Outstanding liabilities for SIMIA (as at 31 May 2017) and R&Q Gamma (as at 30 June 2017) (£000s)

	Case Reserves	IBNR	Total Reserves
SIMIA	5,297	3,855	9,152
R&Q Gamma	189	1,002	1,191
Total	**5,486**	**4,857**	**10,343**

6.5 As shown in the table above, SIMIA's gross outstanding liabilities are £9.2m which would represent 88% of the total gross claims reserves for R&Q Gamma once the Transfer takes place.

6.6 In addition, case reserves ('OS claims') make up 58% of SIMIA's total reserves with the rest being made up of IBNR claims.

6.7 I will issue a supplementary report prior to the final Court hearing after reviewing the most recent information on claims reserves, including commentary on any significant movements in the claims reserves or changes arising from claims settlements.

Reserving analysis carried out on behalf of SIMIA

6.8 SIMIA's sole business is the provision of professional indemnity insurance excess of £1m to firms of solicitors based in England and Wales.

6.9 Due to the claims made nature of the contracts it is expected that there is minimal exposure to new claims being reported ('Pure IBNR'). Furthermore these claims typically will settle as a lump sum rather than a series of partial payments, this further reduces the uncertainty once the court award has been made.

6.10 Since the commencement of the reinsurance contract between RQIM and SIMIA, RQIM has treated SIMIA as one of its owned entities for reserving and capital modelling purposes. The table below shows the outstanding liabilities of SIMIA estimated by RQIM as at 30 June 2017.

Table 3: Total gross and net reserves of SIMIA estimated by RQIM (as at 30 June 2017) (£000s)

	SIMIA
Gross Reserves	7,553
Reserves net of third party reinsurance	5,116
Reserves net of reinsurance with RQIM	0

6.11 The difference in gross reserves between SIMIA's management account as shown in table 1 and that estimated by RQIM as shown in table 3 is largely driven by the reduction in a single claim from May to June 2017.

6.12 In addition to the internal actuarial review by RQIM, an external Actuarial Advisor ('AA') is periodically commissioned by RQIM to review its outstanding liabilities including SIMIA's professional indemnity claims. The most recent detailed review by the AA was carried out as at 30 September 2016 and provides estimates of outstanding liabilities split between those relating to SIMIA and other entities owned by RQIM. Notified claims are analysed on a case by case basis, the outstanding case estimates are updated regularly to reflect claims development and changes in the claims environment.

6.13 The estimate of IBNR produced covers both Pure IBNR to cover claims not yet reported and Incurred But Not Enough Reported ('IBNER') to cover claims which have already been notified to SIMIA.

6.14 IBNER is their estimate of the difference between current case reserves for already reported claims and the ultimate cost of settling those claims. This is calculated using a simplified approach of assuming 25% of the outstanding claims reserve.

6.15 RQIM has estimated the Pure IBNR for SIMIA by assessing the potential new claims by year of account. RQIM has currently allowed for 3 new claims for SIMIA and then applied expert judgement to come up with the cost of each new claim.

6.16 Where the term IBNR is used in what follows, it is generally assumed to represent the sum of IBNER and Pure IBNR.

My review of technical provisions for SIMIA

6.17 To review the methodology, I have held meetings with the R&Q actuaries to understand the claims reserving approach adopted by RQIM to calculate the reserves for SIMIA.

6.18 The approach adopted, some features of which are described above in paragraphs 6.12 to 6.15, appears to be reasonable and is in line with accepted actuarial practice for estimating these types of liabilities when a book is in run off.

6.19 To review the results and assumptions, I have compared the results and a selection of key assumptions against benchmark portfolios from my wider market experience. I have also reviewed the assumptions against SIMIA's own experience to date and the claims movement over the historical years.

6.20 I note that SIMIA has small exposures remaining in very specific insurance classes. Due to the unique exposure, there are differences between SIMIA's experience to the 'average' insurer. These differences are amplified with the size of the remaining book. I have considered these differences in making my comparison of the professional indemnity reserves to my market benchmarks. I consider the benchmarks I have used to be reasonable in the context of SIMIA's liabilities.

6.21 I note the following in relation to the measures I have considered for professional indemnity:

- **IBNR : Outstanding**: I have considered the IBNR amount as a percentage of the current case reserves. SIMIA's ratio is approximately 73%. This is higher than the benchmarks for other UK Solicitors PI which have ratios between 20%-35% for similar underwriting years. However, as SIMIA is in run-off and relatively small it may be subject to more volatility. Therefore it is not unreasonable for SIMIA to have a higher than average ratio of IBNR to outstanding claims.

- **IBNR claim numbers**: I have considered the future estimated number of claims as yet unreported. RQIM has allowed for three new claims in SIMIA's Pure IBNR. Given that SIMIA's 2001 and prior underwriting years are now considered closed and will not be exposed to new claims, and the contracts were written on a claims made basis, the likelihood of any new claims emerging is small. Therefore, I consider this approach to be reasonable.

- **Average cost per claim:** I have considered the average cost per claim assumed by RQIM for SIMIA's liabilities. The Pure IBNR assumptions have been estimated using expert judgment. RQIM has estimated three new claims with an average cost of £1m. This is on the lower end of SIMIA's own experience with historic average cost per claim of £1.7m. However, I believe that the frequency assumption is relatively conservative and hence the overall Pure IBNR assumption is reasonable.

6.22 The reinsurance programmes have been applied to each of the open and the three new claims to calculate the reinsurance recoveries from the third party reinsurers. All the reserves net of third party reinsurance have been ceded under the reinsurance arrangement with RQIM, resulting in a net reserve of zero for SIMIA. I have reviewed the approach and consider it to be reasonable.

6.23 Based on my discussions with R&Q's actuaries, I consider the approach adopted to be in line with accepted actuarial practice, the assumptions set appear to lie within a reasonable range and I have not identified any reason to believe that the reserve estimates for SIMIA lie outside a reasonable range. I believe that RQIM's booked professional indemnity claims reserves for SIMIA lie within a range of reasonable estimates.

Reserving analysis carried out by R&Q Gamma

6.24 R&Q Gamma is exposed to occupational disease reserves. These are predominantly low severity hearing loss claims with a small proportion of asbestos related claims. There is also one potential larger claim which is uncertain and is expected to be resolved through a court case in Q3 2018.

6.25 As at June 2017 there remains 23 open claims, of which the majority are hearing loss claims. There has been 10 new claims notified during the last six months. Claims severity remains low and stable.

6.26 A frequency severity decay model has been adopted to gain comfort with the block IBNR held for hearing loss claims. The model estimates the likelihood of new claims emerging in future years and sets an average cost to each of these claims, taking into account the effect of future claims inflation and allowing for the reduction in claims frequency over time. I believe that the overall approach and estimates are reasonable.

6.27 R&Q Gamma has assessed the impact of the recent changes to the Ogden discount rate used for determining awards for larger bodily injury claims in the UK. Due to the low severity of their claims, the impact is expected to be immaterial. As such, no allowance has been made in the reserves to allow for recent changes and remaining uncertainty over the Ogden discount rate used to determine awards for larger bodily injury claims.

6.28 There is no provision for unallocated claims handling expenses within the GAAP reserves. R&Q Gamma has assessed these requirements and anticipate them to be minimal due to the marginal expenses allocated to these classes being small. It is expected that the future investment income from these classes will more than offset any such requirement.

My review of technical provisions for R&Q Gamma

6.29 To review the methodology, I have held meetings with R&Q Gamma's actuaries to understand the claims reserving approach for the employers' liability and public liability held by R&Q Gamma.

6.30 The approach adopted appears to be reasonable and is in line with accepted actuarial practice for estimating these types of liabilities when a book is in run off.

6.31 I have also reviewed the movement in the claims amount and the number of claims over the past few years. Given the small volume of the book, the claims experience can be volatile. However, I have not identified any reason to believe that the reserve estimates for R&Q Gamma lie outside a reasonable range. I believe that R&Q Gamma's booked claims reserves are reasonable.

7. Capital Requirements

7.1 In considering the solvency position I have considered the following:

- ► The position of R&Q Gamma in respect of UK regulatory capital requirements before and after the Transfer.
- ► The position of SIMIA in respect of UK regulatory capital requirements before and after the Transfer.

Regulatory capital requirements

7.2 As mentioned in section 4, the European Commission has developed regulatory requirements for insurance and reinsurance undertakings within the EU known as ‘Solvency II’ which was implemented on 1 January 2016.

7.3 Under Solvency II, the key metrics to judge capital requirements are the Solvency Capital Requirement (‘SCR’) and the Minimum Capital Requirement (‘MCR’). These measures account for the various risk types that affect an insurer’s capital adequacy including underwriting, market, credit and operational risk.

7.4 The SCR should be determined as the economic capital to be held by insurance and reinsurance undertakings in order to ensure that those undertakings will still be in a position, with a probability of at least 99.5%, to meet their obligations to policyholders and beneficiaries over the following 12 months. It is intended to represent a normal target level of capital for the insurer, and capital falling below this level would trigger a response from the insurer’s regulator.

7.5 The MCR is calculated as a linear function of specified variables with a floor of 25% of the SCR and a cap of 45% of the SCR. In addition, there is an absolute floor of the MCR which is currently €3.7m which equates to £3.3m.

7.6 Insurers can choose one of three methods on which to base their SCR and MCR calculations; a Standard Formula approach, an Internal Model approach or a Partial Internal Model approach:

- ► The Standard Formula approach entails a prescribed basis for calculation and a prescribed set of parameters to use in working out the capital requirement. Within the Standard Formula framework, entities can employ undertaking specific parameters (‘USPs’) to improve the appropriateness of the parameterization for their specific business.
- ► The Internal Model approach involves the (re)insurer using their own capital model to calculate their regulatory capital requirement. Both the approach to calculating available capital (via the Solvency II balance sheet) and the approach to calculating the capital required are different to the Standard Formula approach.
- ► The Partial Internal Model approach is a mixture of the Standard Formula approach and the Internal Model approach. An Internal Model is used to calculate parts of the regulatory capital, and the Standard Formula to calculate the remainder.

7.7 The choice of which of these three approaches to use is made by the (re)insurer themselves, however the form and structure of Internal Models and Partial Internal Models are subject to approval by the relevant regulator (generally the regulator in the home country of the (re)insurer). In cases where the regulator does not approve an Internal Model or Partial Internal Model, the Standard Formula will be applied by default.

7.8 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 an economic balance sheet according to Solvency II requirements. This Solvency II balance sheet differs from the GAAP balance sheet as the valuation rules for several balance sheet items under Solvency II differ from those under GAAP. For example, the technical provisions must be on a discounted Best Estimate basis on the Solvency II balance sheet, whereas under GAAP they could be undiscounted and may include a margin for prudence.

7.9 Any Own Funds on the Solvency II balance sheet are then assessed and allocated to tiers according to their eligibility for meeting the SCR. Further 'ancillary' assets, such as potential calls on the firms that have been insured by SIMIA, may also be used as Own Funds to meet the SCR if they meet the eligibility criteria for a particular tier.

7.10 It is important to note that even if an insurer does not have sufficient eligible Own Funds to meet the required capital level (whether this be on a (Partial) Internal Model basis or a Standard Formula basis), then this does not necessarily mean that it would not be able to settle all its claims in full. The balance sheet strength of the insurer would be sufficient to pay its liabilities, but the regulatory capital amount considered to include an appropriate buffer against uncertainty would be higher.

R&Q Gamma

Approach to assessing capital requirements

7.11 R&Q Gamma carries out Solvency II capital modelling to assess its regulatory capital requirements both on R&Q Gamma alone and on the basis of R&Q Gamma and SIMIA combined. For the combined basis, the capital modelling includes all of SIMIA's transferred assets and liabilities without distinction from other assets and liabilities of R&Q Gamma.

7.12 A Standard Formula approach is used to calculate an SCR as at June 2017. This approach considers the main risks to which R&Q Gamma is exposed in very adverse circumstances. These risks are modelled in the following four key categories:

- **Market Risk:** This describes the risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. This includes the uncertainties relating to investments performance (the investment return achieved and the value of the assets held by R&Q Gamma could go up or down, and the amount by which they go up or down is uncertain). This risk type is further subdivided into interest rate risk, equity risk, property risk, currency risk and concentration risk.

- **Underwriting Risk:** This includes risks relating to the upcoming year of insurance business to be written, the risks relating to unexpired policies at the balance sheet date, and also the uncertainties relating to the claims reserves at the balance sheet date (i.e., the uncertainty that the cost of settling these liabilities could be higher or lower than the booked reserve amount). In other words, R&Q Gamma will need to pay some insurance claims to their policyholders over the coming years, but the amount of those payments and the timing of those payments is uncertain. There is a risk that the amount to be paid is more than expected. R&Q Gamma only considers the reserve risk submodule of underwriting risk since their business is in run off and hence there is no unexpired exposure left.

- **Counterparty Default Risk:** This covers the risk of any defaults of counterparties. This includes any institution or individual that is a debtor to R&Q Gamma, and in particular, the reinsurers of R&Q Gamma.

- **Operational Risk:** This includes uncertainties relating to failures in operational procedures. For example, the (remote) risk that all IT systems fail or that there is a large scale fraud from within the organisation.

7.13 I have considered the approach used to perform the Solvency II Standard Formula calculation for R&Q Gamma, and consider the approach to be reasonable and proportionate to the scale and complexity of its operations.

7.14 I note that whilst I have considered the approach for each element of the Standard Formula calculation, I have not reviewed in detail all the assumptions used as I do not consider these will change my conclusions as they will make an immaterial impact. 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 R&Q Gamma.

Before the Transfer

7.15 R&Q Gamma's capital modelling has led to a calculated SCR figure of £0.5m as at June 2017. Since this is below the absolute floor of MCR, the absolute floor of MCR of £3.3m has been adopted as the regulatory SCR.

7.16 In order to test the appropriateness of R&Q Gamma's SCR, I have calculated the ratio of SCR : reserves and I have compared the results against the same ratios from a number of market benchmarks. I have carried out these comparisons against a wide group of market benchmarks, and also against a subset of these market benchmarks which have a high proportion of employer's liability exposures, which constitutes the majority of R&Q Gamma's remaining exposure.

7.17 I note the following in relation to the measures I have considered:

- **SCR: net reserves for employer's liability market benchmarks**: I have compared the ratio of R&Q Gamma's SCR to net reserves against a number of market benchmarks with employer's liability exposure. R&Q Gamma has a ratio of 105% which is higher than the market benchmarks which range from 56% to 90%. However due to the small and run-off nature of R&Q Gamma's liabilities, I do not believe this to be unreasonable.

- **SCR: net reserves for wider market benchmarks**: I have also investigated how R&Q Gamma's SCR to net reserve ratio compares against a wider group of insurers (i.e. not restricted to those with a high proportion of employer's liability business). The range for this group of market benchmarks is 31% to 667% with 75% of my market benchmarks lying between 51% and 77%. R&Q Gamma's ratio is on the upper end of these benchmarks, however due to the run-off nature of the liabilities I do not believe the ratio to be out of line with the market benchmarks.

7.18 For these measures, R&Q Gamma's results fall within our range of market benchmarks and given the run-off nature of its liabilities this suggests that the SCR is set at an appropriate level and is consistent with those seen in the wider market.

7.19 I have also reviewed the MCR amount set by R&Q Gamma and consider this to be in line with the Solvency II regulatory requirement. As the calculated SCR is below the absolute floor of the MCR, the regulatory SCR of £3.3m has been adopted as the capital requirement for R&Q Gamma (equal to the absolute floor of the MCR).

7.20 The Solvency II balance sheet of R&Q Gamma as at 30 June 2017, is shown in the table below:

Table 4: Solvency II balance sheet for R&Q Gamma (£000s)

	R&Q Gamma
Cash	573
Reinsurers share of technical provisions	661
Intra-Group Loans	14,376
Insurance activities and other debtors	91
Total Assets	**15,700**
Gross Technical Provisions	1,194
Risk Margin	49
Creditors	325
Total Liabilities	**1,568**
Basic Own Funds	**14,132**
Regulatory SCR	**3,255**
Solvency Ratio	**434%**

7.21 I have considered the approach used to calculate the Solvency II balance sheet for R&Q Gamma, including the technical provisions, and consider the approach and results to be reasonable.

7.22 R&Q Gamma considers that the £14,132m Basic Own Funds shown in the balance sheet above meet the eligibility criteria to be used as capital to meet the regulatory SCR. The Basic Own Funds consists predominantly of an intercompany loan to RQIH. The loan is denominated in GBP and reflects a 12 month renewable contract with the loan amount callable on demand. RQIH is rated BBB by AM Best. I consider this assessment of total available eligible Own Funds to be reasonable.

7.23 Dividing the total available eligible Own Funds by the regulatory SCR (i.e. the absolute floor of the MCR) gives a solvency ratio of 434% which I consider to be a very strong level of capital for R&Q Gamma's liabilities.

After the Transfer

7.24 Following the Transfer, I do not expect there to be any material changes in R&Q Gamma's regulatory SCR. In particular, the calculated SCR is still expected to be lower than the MCR and as such, the regulatory SCR will be set to be equal to the absolute floor of the MCR and hence will remain the same.

7.25 R&Q Gamma has carried out financial modelling to project the Own Funds position and the solvency ratio on the basis of R&Q Gamma and SIMIA's combined assets and liabilities as at 30 June 2017, and it has been shown that the Own Funds position and hence the solvency ratio have been improved after the transfer of SIMIA's business. Details of this analysis can be found in section 8 of this report.

SIMIA

Approach to assessing capital requirements

7.26 As mentioned in section 2 of this report, SIMIA has been granted exemption by the PRA from meeting Solvency II regulatory capital requirements until January 2019, meaning the relevant requirements of the Solvency II Directive does not currently apply. SIMIA is therefore not required to meet Solvency II minimum capital requirements. Instead, SIMIA is required to meet the base capital resources requirement of £2.25m, which is below SIMIA's available capital resources of £2.6m as at October 2017. This shows that SIMIA meets their current capital requirements.

7.27 SIMIA carries out no modelling of its own capital requirements. However, RQIM has carried out an assessment of SIMIA's capital requirement as at June 2017 whereby SIMIA is treated as though it is one of RQIM's own entities (i.e. without the reinsurance arrangement with RQIM). The MCR and SCR calculated under Solvency II as at June 2017 are £3.3m and £2.4m respectively. The Own Funds available to SIMIA is £2.6m as at October 2017 which implies a solvency ratio of 79%.

7.28 Were SIMIA to carry out its own assessment of capital requirements taking into account of the reinsurance agreement with RQIM, its most significant risk would be the counterparty default risk in respect of RQIM. RQIM's strong solvency margin (c. 200%) and the fact that the reinsurance premium is held in a segregated account mean that the likelihood of default by RQIM is small. As a result, SIMIA's counterparty default risk is likely to be small and the capital requirement would again be set at the MCR of £3.3m.

Before the Transfer

7.29 Should SIMIA be subject to Solvency II it would have a minimum regulatory capital requirements of £3.3m which it would not currently be able to meet.

7.30 However, the current policyholders of SIMIA do benefit from the security of the reinsurance arrangement with RQIM. Any counterparty default risk to which policyholders are exposed due to this arrangements is considered to be small given RQIM's solvency margin and the funds withheld basis for the reinsurance premium (which means that the premium is held in a segregated bank account in SIMIA's name).

After the Transfer

7.31 Following the Transfer, subject to all insurance liabilities, reinsurance assets and assets relating to the LPT within the segregated account being transferred, SIMIA will be deauthorised as an insurer and policyholders will benefit from the security of the capital held by R&Q Gamma and would be in an entity which would meet its Solvency II capital requirements.

7.32 Following the Transfer the main asset supporting liabilities to SIMIA's policyholders will be the intercompany loan to RQIH which is callable by R&Q Gamma on demand. Prior to the Transfer the main asset held by SIMIA to support its liabilities to its policyholders is the 100% LPT with RQIM, a subsidiary of RQIH. Given that: (i) RQIH and RQIM are related counterparties in the same Group and hence are subject to similar types of risk; (ii) that the available capital within R&Q Gamma from the intercompany loan is much larger than the reserve estimates post the Transfer; and (iii) that the intercompany loan is callable on demand, I do not believe that exposure to the intercompany loan will lead to any material disadvantage to SIMIA's policyholders.

8. Policyholder security and other considerations

8.1 In this section I will describe the effect of the Transfer on the different groups of policyholders and explain how I have reached my conclusions regarding the fairness of the Transfer.

Impact of the Transfer on the balance sheets of the affected companies

8.2 The table below shows simplified balance sheets before and after the Transfer. The amounts shown for the positions before the Transfer are consistent with the financial statements of R&Q Gamma as at 30 June 2017 and SIMIA as at 31 May 2017, except where it is noted otherwise.

8.3 The amounts shown for the positions after the Transfer are hypothetical, based on a Transfer on 30 June 2017. The actual Transfer Date is intended to be in the year ending 31 December 2018, but may be later.

8.4 The actual balance sheets before and after the Transfer will be different to that represented below due to the actual experience of the companies involved between 30 June 2017 and the Transfer Date. However, I believe that this gives the best available picture of the companies involved at this time and how they will be affected.

8.5 I will issue a supplementary report prior to the final Court hearing after reviewing the most up-to-date information.

Table 5: Impact of the Transfer on the GAAP balance sheets of R&Q Gamma and SIMIA (£000s)

	Before Transfer		After Transfer	
	R&Q Gamma	SIMIA	R&Q Gamma (incl. SIMIA)	SIMIA
	[A]	[B]	[C]	[D]
Investments and cash	573	7,396	8,914	2,616**
Recoveries from 3rd party reinsurers	704	2,437*	3,141	0
Recoveries from LPT		5,116*		
Debtors arising out of insurance and reinsurance operations	91	971	91	0
Group Loans	14,375		14,375	
Other Assets	0	469	0	469
Total Assets	**15,743**	**16,386**	**26,521**	**3,085**
Technical Provisions	1,191	7,553*	8,744	0
Creditor – LPT deferred premium		4,780		
Creditors arising out of insurance and reinsurance operations	0	971	971	0
Other creditors including taxation and accruals and deferred income	147	62	147	62
Other Liabilities	178	0	178	0
Total Liabilities	**1,516**	**13,366**	**10,040**	**62**
Free Reserves	**14,227**	**3,023**	**16,481**	**3,023**

Notes:
Column [A] shows the GAAP balance sheet from the management account of R&Q Gamma as at 30 June 2017.
Column [B] shows the GAAP balance sheet from the management account of SIMIA as at 31 May 2017, which is the latest account available and is used to approximate the position as at 30 June 2017, except for the technical provision figures marked with * as explained below.
*The figures for the technical provisions have been updated to those estimated by RQIM as at 30 June 2017 to reflect the reduction of reserves between May and June, as discussed in section 6.11.
** The reduction in investments and cash for SIMIA before and after the Transfer relates to the £4,780k within the segregated fund being paid over (which matches the Creditor-LPT deferred premium item before the Transfer)
Column [C] and [D] show the balance sheets of R&Q Gamma and SIMIA as at 30 June 2017 after the Transfer on the basis that the Transfer was effected on that date.

Any differences between total amounts shown above and the individual items making them up are due to rounding and are not material.

8.6 The key movements are listed below.

a) After the transfer, the amount of cash and investment on R&Q Gamma's balance sheet will increase from £0.6m to £8.9m as the LPT premium of £8.6m in the segregated account less £250k interim RI fee payable to RQIM will be transferred to R&Q Gamma upon the termination of the reinsurance arrangement between SIMIA and RQIM on the Transfer Date.

b) If, on the Transfer Date, the total of net claims paid plus the net claims reserves in relation to the LPT as at the Transfer Date is equal to or less than £7.0m, R&Q Gamma shall pay £0.5m back to SIMIA. The LPT premium of £8.6m noted in paragraph 8.6 a) above is gross of this £0.5m. In the event that the £0.5m is paid back to SIMIA, the solvency position of R&Q Gamma would be slightly worse following the Transfer. However, I do not consider this would make any material impact on the policyholders of either SIMIA or R&Q Gamma.

c) On the Transfer Date, SIMIA will pay the deferred premium due under the LPT between R&Q Gamma and SIMIA (shown in the SIMIA management accounts as £4.8m) to the segregated account and hence its investment and cash position will be reduced to £2.6m after the transfer.

d) It is not expected there will be any SIMIA policies excluded from the Transfer but for any such policies the position will be as described in 2.75.

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

8.7 The capital requirements and the approach to capital modelling have already been discussed in section 7.

8.8 The projected positions before and after the Transfer as at 30 June 2017 are summarised in the following table and comments.

Table 6: Impact of the Transfer on the solvency positions of R&Q Gamma and SIMIA (£000s)

	Before Transfer		After Transfer	
	R&Q Gamma	SIMIA	R&Q Gamma (incl. SIMIA)	SIMIA
Solvency II Regulatory SCR	3,255	n/a	3,255	n/a
Total available eligible Own Funds	14,132	n/a	16.557	n/a
Solvency Ratio	**434%**	**n/a**	**509%**	**n/a**

Note: SIMIA's solvency ratio is not shown before the Transfer since SIMIA is not required to meet Solvency II minimum capital requirements. It does currently meet its regulatory capital resource requirement of £2.25m with available capital resources of £2.6m.

8.9 As discussed in paragraph 7.26, SIMIA is not required to meet Solvency II minimum capital requirements as it has been granted exemption by the PRA from meeting Solvency II regulatory capital requirements until January 2019. However, if SIMIA were to be required to meet Solvency II requirements it would not currently have sufficient capital to meet the current minimum regulatory capital requirements of £3.3m.

8.10 Current policyholders of SIMIA do not benefit from a high level of security based on the amount of capital held by SIMIA, although they benefit instead from the security of the reinsurance arrangements with RQIM. Any counterparty default risk to which policyholders are exposed due to these arrangements is considered to be small given RQIM's solvency margin.

8.11 R&Q Gamma carries out Solvency II capital modelling to assess its regulatory capital requirements on the basis of R&Q Gamma and SIMIA combined. This capital modelling includes all of SIMIA's transferred assets and liabilities without distinction from other assets and liabilities of R&Q Gamma.

8.12 A Standard Formula approach is used to calculate an SCR of £0.5m and an MCR of 3.3m for R&Q Gamma. This approach considers the main risks to which R&Q Gamma is exposed in very adverse circumstances. This covers market risk, underwriting risk, counterparty default risk and operational risk. More details on the risk types can be found in paragraph 7.12.

8.13 Total available eligible Own Funds capital is calculated to be £14.1m so R&Q Gamma has a strong solvency margin at 434% before the Transfer.

8.14 This margin would be increased by the Transfer leading to a solvency ratio of 509% for R&Q Gamma having taken account of the transferred business from SIMIA. The transfer of SIMIA's business does not lead to an increase in the solvency capital requirement above the minimum capital requirement of £3.3m, hence there is no change in R&Q Gamma's regulatory capital requirement. However its total available Own Funds are expected to increase from £14.1m to £16.6m with the transfer of LPT premium as discussed in section 2.42, which would drive the solvency ratio improvement.

Other considerations

8.15 I have considered the additional issues set out below.

Implications on proprietary rights of policyholders of R&Q Gamma and SIMIA

8.16 Following the Transfer, all current policyholders of SIMIA will become policyholders of R&Q Gamma.

8.17 The rights and powers of SIMIA under its articles of association and rules will not transfer to R&Q Gamma, and will remain with SIMIA until SIMIA is dissolved. This means that until SIMIA is dissolved, firms that have been insured by SIMIA will remain obliged to contribute capital in the event of a call being made by SIMIA and will remain able to receive a distribution in relation to the SIMIA's profits. I would not expect that SIMIA would be required to make a call on firms for capital following the Transfer given all of its insurance liabilities will have been transferred to R&Q Gamma and hence SIMIA would not be exposed to any further claims deteriorations.

8.18 As discussed in paragraph 5.30, in the event of insolvency, the insolvency procedure for both SIMIA and R&Q Gamma would be governed by English law and the policyholders have the same right to the assets of the insurance company. Therefore, I do not anticipate that material changes in the order of priority of existing policyholders of R&Q Gamma and transferring policyholders of SIMIA in an insolvency as a consequence of the Transfer.

Customer service

8.19 The outsourcing of handling SIMIA claims to RQMS began in September 2016 and this claims handling agreement was novated to RQCS in December 2017. RQCS will continue to manage claims after the Transfer and it has experience of handling run-off insurance business. Firms like R&Q Gamma who outsource run-off management services are required to impose contractual obligations and other controls on service providers like RQCS to mitigate the risk that performance of the outsourced services would unfairly prejudice policyholders. As a result, there should not be any changes in the claims handling or customer service as a result of the Transfer.

8.20 I do not, therefore, anticipate any changes to the customer service provided to policyholders after the Transfer.

Pension arrangements

8.21 SIMIA and R&Q Gamma do not have any direct employees so are not liable for any pension arrangements.

8.22 Following the Transfer I do not anticipate that these arrangements will change and as a result

I do not anticipate that this will create any adverse impact to the R&Q Gamma or SIMIA policyholders as a consequence of the Transfer.

Tax implications of the Transfer

8.23 I have been provided with a summary of the tax implications of the Transfer by R&Q's tax advisers. Based on this and our understanding of the Transfer I do not believe that there are any tax implications which will materially affect the policyholders of either R&Q Gamma or SIMIA.

Investment Management implications of the Transfer

8.24 SIMIA is currently investing the majority of its assets in a Sterling Liquidity Fund, which is a liquid fund akin to a money market investment, with a small proportion held as cash and bank deposits. Following the completion of the Transfer, SIMIA plans to distribute its remaining assets to eligible solicitors firms. R&Q Gamma will be investing the majority of its assets (apart from the intercompany loan to RQIH which is callable on demand) in corporate bond funds which are deemed to have a duration of one year, and hence are also considered as liquid funds. As a result I do not anticipate that changes in investment management will create any adverse impact to the R&Q Gamma or SIMIA policyholders as a consequence of the Transfer.

Implications of the Transfer on ongoing expense levels

8.25 Other than the initial costs of the Transfer and the subsequent costs of liquidating SIMIA, the ongoing expenses of R&Q Gamma and SIMIA are not anticipated to increase after the Transfer, as all claims handling is already managed by RQCS. I therefore do not anticipate that this will create any adverse impact to the R&Q Gamma or SIMIA policyholders as a consequence of the Transfer.

Financial Services Compensation Scheme

8.26 Consumer protection is provided by the Financial Services Compensation Scheme ('FSCS') in the UK. This is a statutory 'fund of last resort' which compensates customers in the event of the insolvency of a financial services firm. Insurance protection exists for private policyholders and small businesses (with annual turnover of less than £1 million) in the situation where an insurer is unable to meet its liabilities. The FSCS will pay 100% of any claim incurred for compulsory insurance (e.g., motor third party liability insurance or professional indemnity insurance) and 90% of the claim incurred for non-compulsory insurance (e.g., home 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. Contracts of reinsurance are also not protected.

8.27 As SIMIA's policyholder base is mostly made up of partnerships who would be too large to qualify for FSCS protection it is estimated that FSCS protection would only be available to 20% or less of the policyholders and potential claimants of SIMIA. The Transfer does not affect the availability of this compensation under the FSCS so the same protection from the FSCS would continue to exist for these policyholders currently covered after the Transfer. The R&Q Gamma policyholders would also continue to be protected in the current way and the Transfer would not affect this protection, I have therefore concluded that these policyholders are not adversely affected by the Transfer in relation to the FSCS arrangements.

Financial Ombudsman Service

8.28 The Financial Ombudsman Service (FOS) provides private individuals and micro-enterprises with a free, independent service for resolving disputes with financial companies. Micro-enterprises are defined to be businesses with less than €2m annual turnover and fewer than ten employees.

8.29 It is not necessary for the private individual or micro enterprise to live or be based in the UK for a complaint regarding an insurance policy to be dealt with by the FOS. However, it is necessary for the insurance policy concerned to be, or have been, administered from within the UK and/or issued from within the UK.

8.30 Any transferring policyholders that qualify for the FOS will continue to be eligible following the Transfer and as a result I do not believe any policyholders will be affected by the Transfer in relation to the FOS.

Liquidity position

8.31 Following the Transfer, the liquidity position of R&Q Gamma's policyholders will be improved since the amount of cash and liquid funds on R&Q Gamma's balance sheet will increase after the transfer, as discussed in section 8.6. As a result of the Transfer I do not anticipate any material change to the liquidity position of SIMIA's policyholders as before the transfer, SIMIA's policyholders claims are already covered by the LPT premium in the segregated account via the reinsurance arrangement with RQIM. After the transfer, this LPT premium will be on R&Q Gamma's balance sheet which is still available to meet the claims of SIMIA's transferred policyholders.

8.32 As a result I do not anticipate any adverse impact to the R&Q Gamma or SIMIA policyholders as a consequence of the Transfer due to changes in the liquidity position.

Set off

8.33 I do not believe that there are any material set-off rights that can be exercised by cedants or reinsurers. I have not identified any set-off issues as part of my work.

Policyholder communication strategy

8.34 R&Q Gamma and SIMIA propose to undertake procedures to notify policyholders of the Transfer. I understand that the following actions will be undertaken:

- ► Notify all SIMIA policyholders who are currently actively pursuing a claim.
- ► Notify a selected subgroup of R&Q Gamma's policyholders. R&Q Gamma has around 42,000 policyholders, of which many relate to old policies where contact details are likely to be outdated. R&Q Gamma intends to notify policyholders with outstanding claims and claimants pursuing claims against such policyholders, in each using the address details held in its records. R&Q Gamma believes it has up to date contact details for all such policyholders and claimants.
- ► All reinsurers of SIMIA will be notified through its reinsurance broker.
- ► R&Q Gamma intends to request that the Court grants a waiver from the requirement to publish a notice in two national newspapers in each EEA state in which the risk of a policy is situated and one business newspaper in each EEA state which is the State of establishment of a reinsured policyholder. R&Q Gamma intends to publish a notice regarding the Transfer in the Daily Mail, The Sun and the Financial Times. The reasons for the waiver request are given below:
    - ► SIMIA considers that amount of time and effort spent in publishing notice of the Transfer in each relevant EEA state are disproportionate given that all the law firms insured are based in the UK and took out the policy in the UK.
    - ► Further, the insurance was procured on a centralised basis hence it is unlikely that any overseas branch offices of insured law firms were aware of the cover except at a high level.
    - ► R&Q Gamma estimates that the cost of advertising in two newspapers in every EEA state would be materially disproportionate compared with the cost of the intended targeted approach outlined above and I concur with that view.

8.35 I am not aware of anything in the proposed communication to policyholders that would lead to a material adverse effect on any group of policyholders or reinsurers, and therefore consider the proposed strategy to be reasonable.

Obtaining permission for the Transfer from the Solicitors Regulation

Authority

8.36 As part of insuring solicitors SIMIA has requested permission from the Solicitors Regulation Authority to transfer the SIMIA business R&Q Gamma. This permission has been granted in a letter dated 23 June 2017.

Variation of Permission

8.37 This report has been written on the basis that R&Q Gamma will have its variation of permission application accepted and will be able to accept the proposed Transfer from SIMIA. Currently, the application is pending approval but in the unlikely circumstance that the application is rejected, the Transfer will not proceed.

'Brexit'

8.38 In June 2016, the UK voted in a referendum to leave the EU, adding additional uncertainty to the operating environment for insurers. It will take some time for the full implications of this decision to become clear with Article 50 of the Treaty on European Union indicating that there will be a minimum two year delay during which time the UK is able to fully negotiate the terms of its exit following the decision of the UK government to notify the European Council of its decision to leave the EU. Nevertheless, 'Brexit' has introduced or exacerbated a number of risks for insurers operating in the UK, particularly for those that trade across EU borders. There is also the potential that post Brexit UK insurers lose the ability that currently exists to insure risks in the EU (outside of the UK) without being authorised by local regulators. Some potential areas of concern are market volatility with a particular emphasis on exchange rate volatility, a higher risk of negative interest rates in the future and the impact of a changing regulatory environment.

8.39 Despite these risks to the insurance market as a whole, I do not believe that changes in the insurance market or the UK regulatory environment resulting from the outcome of the EU referendum will affect my conclusions relating to the Transfer as set out in this report. This is for the following reasons:

- All SIMIA's policyholders are currently UK based (although they do cover branches of law firms in other jurisdictions including the EU) and R&Q Gamma, which will be the insurer of the transferring policyholders after the Transfer, will remain in the UK and remain subject to aspects of the UK regulatory regime.

- Once the nature of any changes to the insurance market or the UK regulatory environment is determined for the industry post-Brexit, R&Q Gamma will comply with the requirements at that time in respect of its policyholders.

8.40 The majority of SIMIA and R&Q Gamma's liabilities are denominated in GBP and there is very little exposure to movements in other currencies. As such, there would not be any material impact of the exchange rate volatility on their liabilities.

8.41 I will comment on further Brexit developments in my Supplementary Report nearer the date of the Transfer although I do not anticipate that any such developments would affect my conclusions on the Transfer.

Impact of other Part VII Transfers into R&Q Gamma

8.42 We understand that R&Q Gamma is currently planning to enter into another Part VII Transfer agreement with Anglo French Pool ("AFP"). This would cover AFP's US liability business written for a pool of French and UK insurance companies from 1957 to 1966. This business is currently subject to a 100% reinsurance agreement with RQIM which commenced in June 2017. R&Q Gamma anticipate that this transfer will be completed in early 2019.

8.43 I have not considered the impact of the AFP transfer on R&Q Gamma and SIMIA policyholders in this report given that the proposed completion date of the AFP transfer is after the Transfer Date. In addition, if the AFP transfer takes place after the SIMIA transfer, it will only be able to proceed with the sanction of the Court, who will be informed by a separate Independent Expert report in relation to that transfer. In the unlikely event that the AFP transfer were to be completed prior to the Transfer Date, the conclusions from this report may no longer be valid. It would be necessary to re-assess the impact of the Transfer on policyholders with both pre and post-Transfer scenarios inclusive of the AFP business.

9. Reliance and Limitations

Events following the modelling date

9.1 The conclusions in this report are based on various analyses that have been carried out on data as at different points in time (typically 30 June 2017). I have been informed by R&Q Gamma 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 of the Transfer that could change my conclusions. I will provide a letter prior to the sanction of the Transfer to update the Court on whether there have been any material changes since the issue of this report.

9.2 The balance sheets shown in this report are based on data as at 30 June 2017 for R&Q Gamma and as at either 31 May 2017 or 30 June 2017 for SIMIA. I would expect some changes to have taken place between then and the date of this report.

Reliance on other parties

9.3 In developing the conclusions in this report I have relied on the data and accompanying explanations supplied to me by and on behalf of SIMIA and R&Q Gamma. I have received specific statements of data accuracy from SIMIA and R&Q Gamma. I have not specifically reviewed the data for accuracy and completeness but I have reviewed it for reasonableness.

9.4 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. However this has not amounted to a full re-estimation of every class of business, so by definition I have relied upon the reserving work performed on behalf of SIMIA and R&Q Gamma for some components of the claims reserves. I believe that this is reasonable given the experience and professional qualification of the authors of the documents and the testing that I have carried out. The reviews that I have carried out on the reserves give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.

9.5 I have also relied upon discussions that I have had with the management of SIMIA and R&Q Gamma. Where appropriate, I have sought documentation from them to evidence the assertions made to me in these discussions.

Use of benchmarks

9.6 As well as analysing the trends of the historical claims development, I have also relied upon benchmarks from wider market experience. Whilst SIMIA and R&Q Gamma’s own development can be expected to vary from the benchmarks based on individual circumstances, I believe that the benchmarks are an appropriate check. However, benchmarks are revised periodically as new information and trends emerge, and it is likely that individual accounts will differ from the average. Therefore, it is possible that these benchmarks will not be predictive of the future claim reporting of SIMIA or R&Q Gamma.

9.7 I have also used other benchmarks based on my wider market experience to assess the appropriateness of some of the assumptions used within the reserve estimations and capital modelling performed for SIMIA and R&Q Gamma.

Other

9.8 The underlying numbers contained in this report are calculated to many decimal places and so totals and summaries are subject to rounding differences.

9.9 In my judgement, the results and conclusions contained in this report are reasonable given the information made available to me. However, the actual cost of settling future claims and those still outstanding as at the valuation date is uncertain as, amongst other things, it depends on events yet to occur such as future court judgments. It could be different from the estimates shown in this report, and possibly materially so. Such differences between the estimated and actual outcome could possibly have a material impact upon the balance sheet strength of the companies involved, and therefore upon the Transfer.

10. Conclusions and Statement of Truth

10.1 I have considered the Transfer and its likely effects on the policyholders of R&Q Gamma and SIMIA.

10.2 In reaching the conclusions set out below, I have applied the following principles. 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 policyholders of SIMIA and R&Q Gamma);
- Indicate how the Transfer might lead to any changes in the material risks to the benefits of different classes of beneficiaries;
- Indicate (in broad terms) the impact on the actuarial information of adopting alternative plausible assumptions;
- Assess the impact on all classes of beneficiaries;
- Indicate the proposed rationale for the Transfer to proceed;
- Include (in summary) the most material information on which my opinion is based; and,
- Describe the rationale for my opinion.

10.3 I have concluded that there will be no change to the service and very little change in the security provided to policyholders, therefore no policyholders would be adversely affected to a material extent by the Transfer.

10.4 In addition, reinsurers of SIMIA will not be adversely affected by the Transfer as all of SIMIA's reinsurance contracts other than with RQIM will be transferred to R&Q Gamma. As a result, exposure to claims faced by SIMIA's reinsurers will not increase following the Transfer and they will continue to be required to pay out claims in respect of the same events as before the Transfer.

10.5 Given the reasons discussed above, I conclude that the risk of any group of policyholders, reinsurers or other parties being adversely affected by the Transfer is sufficiently remote that there is no reason why the Transfer should not proceed. Details of the key reasons behind my conclusions can be found in sections 2.62 to 2.70.

10.6 I do not believe that there are any matters that are relevant to SIMIA's or R&Q Gamma's policyholders' consideration of the scheme which I have not taken into account.

10.7 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 I have expressed and conclusions I have drawn represent my true and complete professional opinions on the matters to which they refer.

10.8 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.

10.9 I do however consider it necessary that I review the most recent information, up to the date of the Transfer, when this becomes available later in the year, before confirming my opinion and conclusions.

24 May 2018

Alex Lee
Fellow of the Institute and Faculty of Actuaries
Associate Partner
Ernst & Young LLP

Appendix A Glossary

The following key terms have been used throughout this report and are gathered here for ease of reference.

Term	Definition
AA	Any external actuarial advisor that has been employed by RQIM
Best Estimate	An estimate prepared with no margin for either prudence or optimism included
Chain of Security	The assets available to make a claim payment to a policyholder expressed in the order that they would be used to make that payment
Counterparty Default Risk	The risk of any defaults of counterparties (i.e. any institution or individual that is a debtor to the undertaking)
Court	The High Court of England and Wales
Direct policyholders	Policyholders that are not insurers or reinsurers
EEA	European Economic Area
EU	European Union
External reinsurance	Reinsurance cover provided by reinsurers (before the application of the loss portfolio transfer reinsurance between SIMIA and RQIM).
FCA	The Financial Conduct Authority, one of the regulators of the insurance industry in the UK (in conjunction with the PRA).
FRC	The Financial Reporting Council, the body responsible for setting actuarial standards in the UK
FSMA	Financial Services and Markets Act 2000
IBNR	Incurred but not reported. Refers to the amounts an insurer will have to pay for claims that are reported in the future but relate to events that have already occurred. Often used to refer to any amounts insurers must pay over and above existing case reserves and hence also includes IBNER (as defined below). Where it does not include IBNER, it is sometimes referred to as 'Pure IBNR'.
IBNER	Incurred but not enough reported. Refers to the amounts an insurer will have to pay over and above existing case reserves for claims that have already been reported, i.e., the estimated cost of any anticipated future development on known claims. This is often included within IBNR.
Independent Expert	The suitably qualified person appointed by the court to produce an independent report on the Transfer, in accordance with the FSMA

Term	Definition
Insurance Risk	Risks relating to insurance policies sold, i.e., the risk that the cost of claims for which the insurer is responsible proves to be higher than expected
Latent Claims	A latent claim is a claim that arises from a risk not anticipated by the underwriter and not priced for in the original policy. Typically the claims of this type will exhibit significant reporting delays.
Loss Portfolio Transfer (LPT)	An arrangement whereby the economic burden in respect of a specified book of business is passed in its entirety from one insurance entity to another.
Market risk	Risks relating to investment performance and changes in the value of investments
MCR	Minimum Capital Requirement, a formulaic calculation of the capital requirement as part of the existing European Solvency II regulations for insurers
Operational risk	Risks relating to failure of operational procedures
ORSA	Own Risk and Solvency Assessment, a reporting requirement where management conduct their own assessment of risks and associated economic capital needs in accordance with Solvency II
Own Funds	Available capital to meet the capital requirements under Solvency II
PI	Professional Indemnity insurance indemnifies the insured against legal liability to third parties arising from the insured's negligent services or advice.
Policy year	Year in which policy was written
PRA	The Prudential Regulatory Authority, one of the regulators of the insurance industry in the UK (in conjunction with the FCA).
Pure IBNR	See IBNR.
SCR	Solvency Capital Requirement. The amount of capital insurers are required to hold under Solvency II regulations. If an insurer's capital (i.e., the excess of its assets over its liabilities) falls below the SCR, it will trigger regulatory intervention, with the intention of remedying that position
Solvency II	An updated set of regulatory requirements for insurers that operate in the EU. These requirements apply to insurers from 1 January 2016
Solvency Ratio	A measure to indicate the strength of a company's capital position. This is usually calculated as total own funds divided by regulatory SCR.
Standard formula	A prescribed approach under Solvency II for the calculation of capital based on an insurer's financial information (e.g. premium, claims reserves, etc.)

Term	Definition
TAS 100	The Technical Actuarial Standard issued by the FRC which should be applied to all aspects of technical actuarial work.
TAS 200	The Technical Actuarial Standard issued by the FRC relating to matters where there is a high degree of risk to the public interest.
Transfer	The proposed insurance business transfer of the business of SIMIA to R&Q Gamma
Transfer Date	The date on which the Transfer becomes effective, currently expected to be 30 September 2018
UK	United Kingdom of Great Britain and Northern Ireland
UK GAAP	Generally Accepted Accounting Principles as defined in the UK
Underwriting Risk	The risks relating to the upcoming year of insurance business to be written, unexpired policies at the balance sheet date, and the uncertainties relating to the claims reserves at the balance sheet date
USP	Undertaking specific parameters- if the standard formula does not provide an appropriate representation of the undertaking’s underlying risks, they may replace a subset of parameters (standard parameters) by parameters specific to them.

The following are the abbreviations used to define the companies referred to in this report.

Abbreviation	Company name
R&Q	Randall & Quilter Investment Holdings Ltd
RQIM	R&Q Insurance (Malta) Limited
RQMS	R&Q Market Services Limited
RQCS	R&Q Central Services Limited
R&Q Gamma	R&Q Gamma Company Limited
SIMIA	Solicitors Indemnity Mutual Insurance Association
RLM	Royal London Mutual Insurance Society Limited
RLGI	The Royal London General Insurance Company Limited, former name of R&Q Gamma
Norwich Union	Norwich Union Fire Insurance Society Limited

Appendix B Extract from Terms of Engagement

Scope of services

This engagement will cover the appointment of Alex Lee as Independent Expert for the SIMIA to R&Q part VII transfer (the 'Transfer'). We note that the primary duty of the Independent Expert in an insurance business transfer in the UK is to the High Court of England and Wales ('the Court').

We will:

- Analyse work you have carried out on the companies and portfolios of policies involved in the Transfer, including (but not limited to) the adequacy of the claims reserves and capital modelling analysis (under solvency rules) for each of the groups of policyholders who are affected by the Transfer.

- Supplement this with such additional calculations and investigations as the Independent Expert believes are necessary to enable him to form a view on the implications of the Transfer on the policyholders involved and communicate this to the Court.

We will prepare the following reports (together the 'Reports'):

- A report (the 'Report') providing the Independent Expert's conclusions on the Transfer and explanation of those conclusions, to be presented in draft to the PRA and FCA (together the 'UK financial regulators') on a date agreed with the UK financial regulators and then updated as required following the feedback from both the UK financial regulators and then delivered to the Court in sufficient time prior to the initial directions hearing.

- A supplementary report (the 'Supplementary Report') to supplement the Report, to be presented to the Court at the final court hearing to consider the sanction of the Transfer. The Supplementary Report will discuss issues that have arisen between preparation of the Report and the final court hearing that the Independent Expert considers material to the Transfer, as well as any impact on his conclusions.

- A summary report (the 'Summary Report'). In accordance with the Financial Services and Markets Act 2000 and subordinate regulations, a summary of the Independent Expert's report will be provided to affected policyholders and any other person entitled to receive a copy to assist them with assessing the Transfer.

- Such further reports as may be required by the Court, the UK financial regulators or by you in connection with the Transfer, it being acknowledged that the preparation of such reports may incur additional costs which (if relevant) will be agreed in advance of the relevant work being undertaken.

Appendix C Alex Lee – Relevant experience

Background

- Over 20 years' general insurance experience
- Qualified as a Fellow of the Institute & Faculty of Actuaries in 1997
- Joined Ernst and Young in 1999 and prior to this worked in the Commercial Insurance department of Eagle Star / Zurich Financial Services

Skills

- Experienced in advising clients in the London & Bermuda markets
- Focused on reserving, capital modeling, pricing, mergers and acquisitions and process review
- Responsible for Research & Development and Knowledge Management

Professional Experience

- Alex has been involved in many mergers and acquisitions of both ongoing companies and those in run-off working for both buyer and seller. As part of this work Alex has performed reviews of London Market, US and European business with significant experience in US Latent Claims reserving estimates and producing cash flow and business planning models to assess the viability of transactions.
- He has significant reserving experience in the London Market and runs regular reserve reviews for some of the largest managing agencies in the Lloyd's of London market including performing the role of statutory signing actuary. In addition to this Alex has also performed many independent reserve reviews within the London market, Bermuda and UK retail markets. These reviews have included exposure to professional indemnity business through mutuals, companies and Lloyd's syndicates.
- He has performed the role of independent expert on four previous transactions and also has worked on several Part VII transfers both producing information for the independent expert and as peer reviewer.
- He assisted in the role of peer review actuary for two of the largest insolvencies in the London Market covering extensive US Latent claim exposures.
- He has assisted with the production of ICA submissions for both Lloyd's and UK insurance entitles. In addition, Alex has also assisted in capital modelling for management for their internal clients.
- He has been extensively involved in the audit of reserves for a wide range of EY audit clients both in the UK retail and London market area.
- He has also been involved in pricing and process reviews. In particular, Alex was involved in a review of pricing processes for a large pan-European insurer.
- He has also performed detailed reviews of reinsurance contracts and finite risk reinsurance arrangements for clients, in particular reviewing the accounting impact of these transactions on company's balance sheet and profit and loss statements.

- Alex has the role in the actuarial leadership team of running the Research and Development function and the Knowledge Management area.

Appendix D Summary of data provided

The following is a list of the data items I have requested and received in assessing the Transfer.

- Draft Insurance Business Transfer Scheme in the matter of SIMIA and R&Q Gamma
- SIMIA Scheme documents
  - SIMIA Claims Agreement - Execution Version
  - SIMIA LPTA - Execution Version
  - SIMIA Transfer Scheme - Agreed Form
  - SIMIA Transfer Agreement - Execution Version
  - Special Resolution - Agreed Form
- SIMIA claims bordereaux as at 30 June 2017
- R&Q full group structure as at 01 August 2017
- SIMIA Director's Report and Financial Statements as at 30 September 2016
- SRA consent letter to SIMIA for the transfer of insurance business as at 27 June 2017
- Regulatory correspondence between the PRA and R&Q regarding Brexit as at 27 July 2017
- R&Q Gamma Variation of Permission application
- R&Q Gamma Reinsurance arrangement files
- SIMIA Reinsurance arrangement files
- SIMIA appraisal doc
- R&Q Gamma appraisal doc
- Scheme of Operations for Gamma 2017
- Most recent regulatory returns
  - SFCR Gamma 2017 05 18
  - Latest audited accounts for SIMIA as at 30 September 2016 and for R&Q Gamma as at 31 December 2016
  - R&Q Gamma June 2017 management accounts
  - SIMIA management account narrative as at 31 May 2017
- Recent actuarial function reports and internal actuarial results
  - RQIM Actuarial Function Report 2016

  - R&Q Gamma Actuarial Function Report 2016
  - R&Q Gamma Reserve review as at Q4 2016
  - RQIM Reserve review as at Q4 2016 and as at Q2 2017
- External actuarial reports
  - PwC R&Q Malta Reserve Review as at 30 September 2016
  - PwC R&Q Malta Reserve Review as at 31 December 2016
- R&Q Gamma ORSA Policy
- R&Q Gamma Outsourcing Policy
- R&Q Gamma Risk Appetite
- R&Q Gamma Risk Register as at 3 August 2017
- R&Q Gamma ORSA 2016
- SIMIA list of members 2002 to 2010
- Analysis of and provisions for any bad and doubtful debt
  - R&Q Gamma bad debt positions on balances and RI share of technical provisions as at 30 June 2017
  - SIMIA bad debt positions as at 31 December 2016.
- R&Q Gamma's projected balance sheet from 2017 to 2019
- Supporting documents for reserving and capital
  - SIMIA reserve results as at 30 June 2017
  - R&Q Gamma open claims as at 30 June 2017
  - R&Q Gamma and SIMIA capital inputs for SF SCR
- R&Q Gamma and SIMIA Risk Margin analysis for SCR as at 30 June 2017
- Royal London 1983 and 1984 accounts

Appendix E Checklist against PRA’s Statement of Policy and SPU18 of the FCA Handbook

The table below shows the relevant section references in this report where I have addressed each point in the guidance from Chapter 18 of the Supervision Manual of the FCA Handbook and the PRA’s ‘Statement of Policy - The PRA’s approach to insurance business transfers – April 2015’ with regards to the scheme report.

Guidance Reference	Guidance	Scheme Report reference
PRA 2.30 (1) FCA 18.2.33 (1)	Who appointed the independent expert and who is bearing the costs of that appointment	1.2, 1.10
PRA 2.30 (2) FCA 18.2.33 (2)	Confirmation that the independent expert has been approved or nominated by the PRA (or appropriate regulator);	1.3
PRA 2.30 (3) FCA 18.2.33 (3)	A statement of the independent expert’s professional qualifications and (where appropriate) descriptions of the experience that makes them appropriate for the role;	1.12-1.15 Appendix A
PRA 2.30 (4) FCA 18.2.33 (4)	Whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest;	1.16-1.18
PRA 2.30 (5) FCA 18.2.33 (5)	The scope of the report;	Section 3, Appendix B
PRA 2.30 (6) FCA 18.2.33 (6)	The purpose of the scheme;	2.27-2.29
PRA 2.30 (7) FCA 18.2.33 (7)	A summary of the terms of the scheme in so far as they are relevant to the report;	2.19-2.26
PRA 2.30 (8) FCA 18.2.33 (8)	What documents, reports and other material information the independent expert has considered in preparing the report and whether any information that they requested has not been provided;	3.6, 3.8, Appendix D
PRA 2.30 (9) FCA 18.2.33 (9)	The extent to which the independent expert has relied on: (a) information provided by others; and (b) the judgement of others;	3.7, 9.3
PRA 2.30 (10) FCA 18.2.33 (10)	The people the independent expert has relied on and why, in their opinion, such reliance is reasonable;	9.4, 9.5
PRA 2.30 (11) FCA 18.2.33 (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	2.60, 2.61

	policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee;	
PRA 2.30 (12) FCA 18.2.33 (11 A)	Their opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme;	2.70, 10.4
PRA 2.30 (13) FCA 18.2.33 (12)	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' consideration of the scheme	10.6
PRA 2.30 (14) FCA 18.2.33 (13)	For each opinion that the independent expert expresses in the report, an outline of their reasons.	Section 10 and throughout the report
PRA 2.33 (1) FCA 18.2.36 (1)	Include a comparison of the likely effects if it is or is not implemented;	8.2-8.14
PRA 2.33 (2) FCA 18.2.36 (2)	State whether they considered alternative arrangements and, if so, what;	3.5
PRA 2.33 (3) FCA 18.2.36 (3)	Where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences they consider may be material to the policyholders; and	2.60, 2.61
PRA 2.33 (4) FCA 18.2.36 (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; (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: (i) the security of policyholders' contractual rights; (ii) levels of service provided to policyholders; or (iii) for long-term insurance business, the reasonable expectations of policyholders; and (c) the cost and tax effects of the scheme, in relation to how they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations.	(a) 8.8 (b) 8.15-8.33 (c) 8.23
PRA 2.35 (1) FCA 18.2.38 (1)	For any mutual company involved in the scheme: Describe the effect of the scheme on the proprietary rights of members of the company, including the	2.42, 8.16, 8.18

	significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders;	
PRA 2.35 (2) FCA 18.2.38 (2)	State whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights; and	N/A
PRA 2.35 (3) FCA 18.2.38 (3)	Comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without	N/A