LCP INSIGHT CLARITY ADVICE

Scheme Report of the Independent Actuary on the proposed transfer of insurance business from

R&Q Theta Designated Activity Company to Accredited Insurance (Europe) Limited

in accordance with Section 13 of the Assurance Companies act 1909

In accordance with Section 13 of the Assurance Companies act 1909

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LCP

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1. Executive summary

1.1. The Proposed Transfer

The firms involved

R&Q Theta is an Irish domiciled insurance company. Prior to its acquisition by R&Q Group, it was known as Electric Insurance Ireland DAC ("EIIDAC"). EIIDAC was an Irish domiciled captive insurance company, wholly owned by Electric Insurance Company ("EIC"), a company incorporated in the United States. In May 2021, the R&Q Group received regulatory approval from the Central Bank of Ireland ("CBI") to complete the acquisition of EIIDAC.

Following the acquisition in 2021, EIIDAC's name was changed to R&Q Theta Designated Activity Company ("R&Q Theta"). R&Q Theta is a subsidiary of Randall & Quilter Investment Holdings Limited (RQIH), the parent company of the R&Q Group.

Accredited Insurance (Europe) Limited ("AIEL") is R&Q Group's primary European insurance operation. AIEL is headquartered in Malta and its portfolio is made up of both legacy portfolios, which write no new business, as well as active programmes written via managing coverholders.

AIEL's strategy is to secure run-off business through acquisition, transfer or merger from third parties and selected European portfolios already within the R&Q Group. These portfolios are run off by AIEL, or alternatively sold on. Since 2016, AIEL also started underwriting live business through selected coverholders who would not otherwise have access to EEA business. This is done with the support of well rated reinsurers.

Through the Proposed Transfer, AIEL aims to manage the run-off of the R&Q Theta liabilities.

The Transferring Business

R&Q Theta's portfolio consists of General Liability, Employer's Liability and Motor insurance cover. As part of the acquisition of EIIDAC in May 2021, the existing reinsurance arrangement with EIC was commuted and replaced by a new reinsurance programme with R&Q Re (Cayman) Limited ("R&Q Cayman"), also part of the R&Q Group.

Proposed Transfer (the Scheme): It is proposed that, pursuant to Section 13 of the Assurance Companies Act 1909, all the liabilities of R&Q Theta (the Transferring Business) will transfer to AIEL. All rights and obligations of R&Q Theta relating to the Transferring Business will also be transferred to AIEL.

It is planned that all policyholders of R&Q Theta will transfer to AIEL, and that R&Q Theta will be liquidated in due course.

Effective Date

The Effective Date (the date when the Proposed Transfer is expected to occur) will be shortly after the Sanctions Hearing which is scheduled for 3 October 2022.

Reinsurance

In preparation for the Proposed Transfer, R&Q Theta purchased an aggregate excess of loss reinsurance treaty in May 2021, which replaced all existing reinsurance contracts. The reinsurance contract is with R&Q Re (Cayman) Limited ("R&Q Cayman") Limited. The aggregate attachment point is €3m and the maximum aggregate limit is €55m. The reinsurance has been placed on a funds withheld basis.

I understand that, coinciding with the transfer, the reinsurance treaty will be novated from R&Q Theta to AIEL so that it will remain in place to protect the Transferring Business following the Proposed Transfer.

Claims handling

Claims handling for R&Q Theta's business is outsourced to Crawfords, a large publicly listed provider of outsourced claims management services. Following the Proposed Transfer, claims handling for the transferring business will continue to be performed by Crawfords on behalf of AIEL.

1.2. My role as Independent Actuary

R&Q Theta and AIEL have jointly appointed me to act as the Independent Actuary ("IA") for the Proposed Transfer. The CBI has been notified of my appointment.

As IA my overall role is to assess whether:

- The security provided to policyholders of R&Q Theta and AIEL will be materially adversely affected by the implementation of the Proposed Transfer.
- The Proposed Transfer will have any adverse impact on service standards experienced by policyholders.

This report is my Scheme Report for the Proposed Transfer. I will also prepare a Supplementary Report ahead of the Sanctions Hearing for the Proposed Transfer. The purpose of the Supplementary Report is to confirm and/or update my conclusions in this report, based on any new material or issues that arise.

1.3. Summary of my conclusions

I have set out below my summary conclusions, considering the effect of the Proposed Transfer on the following two parties:

- "Transferring Policyholders", ie R&Q Theta policyholders whose liabilities will transfer to AIEL as a result of the Proposed Transfer.
- "Existing AIEL Policyholders", ie policyholders of AIEL immediately prior to the Proposed Transfer, who will remain with AIEL after the Proposed Transfer.

In drawing my conclusions, I have considered the impact of the Proposed Transfer on all underlying Claimants and Beneficiaries (these terms are defined in section 4).

Transferring R&Q Theta Policyholders

R&Q Theta have identified 772 Transferring Policyholders of whom 634 remain active. The Transferring Business represents 100% of R&Q Theta's business based on technical provisions as at the Effective Date.

I have concluded that

- **the security provided to Transferring Policyholders will not be materially adversely affected by the Proposed Transfer.**
- **no material impact on service standards is expected for Transferring Policyholders following the Proposed Transfer.**

Summary rationale:

- The Transferring Policyholders will remain within the R&Q Group and AIEL is subject to the same group-wide policies as R&Q Theta.
- I am satisfied that the approaches used to calculate the Solvency II and GAAP technical provisions for the Transferring Business from R&Q Theta are appropriate, and AIEL has confirmed that these will be materially unchanged post-transfer.
- The SCR coverage ratio for Transferring Policyholders is expected to decrease slightly from 177% (R&Q Theta pre-transfer) to 173% (AIEL post-transfer) as a result of the Proposed Transfer. I do not consider the security provided to Transferring Policyholders to be materially adversely affected by this decrease, as AIEL will still be well capitalised.
- Further, AIEL's SCR coverage ratio is projected to be at levels similar to R&Q Theta's pre-transfer coverage ratio by December 2024.
- The reinsurance treaty with R&Q Cayman, which protects the transferring business, will remain in place following the Proposed Transfer and will continue to be in a funds-withheld basis.
- I am satisfied that AIEL is expected to remain well capitalised under a range of adverse scenarios in relation to both the Transferring Business and its other business. In more extreme adverse scenarios, where AIEL's SCR coverage ratio would fall below 100%, I am satisfied that the likelihood of such scenarios is sufficiently remote such that Transferring Policyholders are not materially adversely affected as a result of the Proposed Transfer.

- R&Q Theta's net reserves are less than 2% of AIEL's total net reserves on an IFRS basis. The Transferring policyholders will benefit from being part of a bigger, diversified portfolio as their risk runs off over time.
- AIEL is an EEA entity so the Transferring Policyholders business will continue to be regulated in the EEA following the Proposed Transfer. I do not expect the rights of policyholders in respect of access to compensation schemes, eg the Irish Insurance Compensation Fund, to change as a result of the Proposed Transfer.
- The claims handling of the Transferring Business is currently being managed by Crawfords. AIEL has confirmed that this will continue to be the case following the Proposed Transfer, which provides continuity of service to policyholders.

Existing AIEL Policyholders

At the Effective Date of the Proposed Transfer, Existing AIEL Policyholders are projected to represent 92.6% of AIEL's projected post-transfer gross technical provisions, and 97.8% of AIEL's projected post-transfer net technical provisions.

I have concluded that

- **the security provided to Existing AIEL Policyholders will not be materially adversely affected by the Proposed Transfer.**
- **no material impact on service standards is expected for Existing AIEL Policyholders following the Proposed Transfer.**

Summary rationale:

- I am satisfied that the approaches used to calculate the Solvency II and GAAP technical provisions for AIEL are appropriate, and AIEL has confirmed that these will be materially unchanged post-transfer.
- The SCR coverage ratio for AIEL Policyholders is expected to decrease from 185% to 173% as a result of the Proposed Transfer. The reduction in coverage ratio is caused by differing approaches in the valuation of technical provisions and treatment of certain assets pre and post-transfer. This is discussed in more detail in section 6. I do not consider the security provided to Existing AIEL Policyholders to be materially adversely affected by this decrease, as AIEL will still be well capitalised.
- Further, AIEL is projected to remain well capitalised throughout the projected period to December 2024.
- I am satisfied that AIEL is expected to remain well capitalised under a range of adverse scenarios in relation to both the Transferring Business and its other business. In more extreme adverse scenarios, where AIEL's SCR coverage ratio would fall below 100%, I am satisfied that the likelihood of such scenarios is sufficiently remote such that Existing AIEL Policyholders are not materially adversely affected as a result of the Proposed Transfer.
- AIEL is not planning any material changes to how its existing business is carried out. In particular, there are no plans to change how Existing AIEL Policyholders are serviced following the Proposed Transfer.

1.4. Next steps

The remainder of this report sets out my conclusions and other supporting information in more detail.

I will be reviewing these conclusions and preparing a Supplementary Report ahead of the Sanctions Hearing for the Proposed Transfer. The purpose of the Supplementary Report is to confirm and/or update my conclusions based on any new material or issues that arise.

Specific issues that I have highlighted in this report which require further review include:

- Updated reserves and capital positions.
- Any policyholder objections received.
- Any changes to the detail of the scheme.

2. Introduction

2.1. Background

Any transfer of business carried out by one Irish authorised insurance company to another Irish or EEA authorised insurance company is governed by Section 13 of the Assurance Companies Act 1909, Section 36 of the Insurance Act 1989 and Regulation 41 of the European Union (Insurance and Reinsurance) Regulations 2015.

Under Section 13 of the 1909 Act, any scheme that provides for a transfer, in whole or in part, of the business of an Irish authorised insurance company to another Irish or EEA authorised insurance company requires prior sanction of the High Court. The Court will consider the scheme on the basis of a petition brought by the Boards of Directors of both the transferor and transferee companies and, while not mandatory for a non-life transfer such as the Proposed Transfer, in practice, the petition is accompanied by a report on the terms of the scheme by an Independent Actuary.

The purpose of the Independent Actuary's report is to provide an independent opinion for the Court on the likely effects of the scheme on the policyholders of the two companies concerned. The security of policyholders' contractual benefits and the effects of the scheme on the fair treatment and reasonable expectations of policyholders are the main considerations of the report.

This report is the Scheme Report for the Proposed Transfer. I will also prepare a Supplementary Report ahead of the Sanctions Hearing for the Proposed Transfer. The purpose of a Supplementary Report is to confirm and/or update my conclusions in this report, based on any new material or issues that arise.

2.2. Independent Actuary appointment

My appointment

R&Q Theta and AIEL have jointly appointed me to act as the IA for the Proposed Transfer. The CBI has been notified of my appointment. AIEL will bear the costs associated with the production of my report. I understand that no costs or expenses of the Proposed Transfer will be borne by policyholders.

My experience

I am a Fellow of the Society of Actuaries in Ireland (FSAI). I am the Head of Actuarial function for two Irish regulated insurers and perform a similar role for two Maltese regulated insurers.

I am the Lead Partner in LCP's Irish Insurance Consulting practice. I have experience in a wide range of areas of general insurance actuarial work including reserving, capital, pricing, Solvency II and transactions.

I have been appointed as the IA on two previous Section 13 transfers and have been peer reviewer on an insurance Part VII transfer.

I have over 30 years' industry experience, over 25 of which are in general insurance. Appendix 3 contains my CV with further details of my experience.

Independence statement

I confirm that I, Declan Lavelle, and all members of the LCP team assisting me in my IA role are independent from the parties of the transfer and that I am able to act as your IA.

I confirm that neither I, nor any of the team, have any direct or indirect interests in the R&Q Theta or AIEL ("the firms"), either personally or via LCP.

In particular:

- Neither I, nor any member of the team, is a shareholder in the firms or subsidiaries nor a member of any pension scheme under the management of any of these entities.
- Neither I, nor any member of the team, hold any insurance policies issued by the firms or any subsidiaries.

Other than as outlined below, LCP has not previously performed any work for the firms or for other entities in the R&Q Group:

- Another LCP partner has acted as Independent Actuary (IA) on a Part VII transfer, which is the UK equivalent of a Section 13 transfer involving an entity in the R&Q Group.
- I have previously been IA on non-life insurance Section 13 transfer from Western Captive Insurance Company DAC to AIEL in 2019. I do not believe this impairs my independence. While this previous role gives prior insight into the capital positions of AIEL, I consider that a sufficient period of time has passed such that my Report to the Court will be appropriately informed but in no way prejudiced or anchored to previous work.

I do not consider that these engagements affect my ability to act as IA on the Proposed Transfer.

2.3. Scope of this Scheme Report

Appendix 2 contains an extract from my terms of reference, which defines the scope of my work in relation to the Proposed Transfer. The actual work performed is in line with this agreed scope.

This Scheme Report considers the effect of the Proposed Transfer upon the policyholders of R&Q Theta and AIEL. It contains a description of the Proposed Transfer, the methodology I have used to analyse the Proposed Transfer, the opinions I have formed, and reasons why I have formed those opinions.

The use of "I", "me" and "my" in this report generally refers to work carried out by me or by the team operating under my direct supervision. However, when it is used in reference to an opinion, it is mine and mine alone.

For presentational purposes, in this report, the AIEL GBP amounts have been converted to EUR at an exchange rate of £1 = EUR1.19 as at 31 December 2021.

2.4. Use of this Scheme Report

This Scheme Report has been produced by Declan Lavelle FSAI of LCP under the terms of our written agreements with R&Q Theta and AIEL. It is subject to any stated limitations (eg regarding accuracy or completeness).

This Scheme Report has been prepared for the purpose of accompanying the application to the Court in respect of the proposed insurance business transfer scheme described in this report, in accordance with Section 13 of the Assurance Companies Act 1909. The Scheme Report is not suitable for any other purpose.

A copy of the Scheme Report will be sent to the CBI and will accompany the Scheme application to the Court.

This report is appropriate only for the purpose described above and should not be used for anything else. No liability is accepted or assumed for any use of the Scheme Report for any other purpose other than that set out above.

2.5. Reliances

I have based my work on the data and other information made available to me by R&Q Theta and AIEL. Appendix 4 contains a list of key data and other information that I have considered. I have also held discussions with the relevant staff of R&Q Theta, AIEL and their advisors.

Actual data

I have used actual data as at 31 December 2021, where available, for my analysis. Prior to the Sanctions Hearing for the Proposed Transfer, I will prepare a Supplementary Report to confirm and/or update my conclusions in this report, based on any new material or issues that arise.

Projected data as at the Effective Date

The Effective Date of the Proposed Transfer is expected to be shortly after the Sanctions Hearing which is scheduled for 3 October 2022.

- R&Q Theta's projected SCR and coverage ratios immediately before and after the Proposed Transfer are based on an effective date of 30 September 2022. The projections as at 30 September are expected to approximately reflect the impact of the Proposed Transfer as at the actual Effective Date.

- AIEL's projected SCR and coverage ratios are based on its year-end date of 31 December 2022. The impact of the transfer of the liabilities is not expected to be materially different between the Effective Date and 31 December 2022 and the value of the liabilities is not expected to change materially in this period given their long-tailed nature.

I am comfortable that R&Q Theta's 30 September 2022 projected figures and AIEL's 31 December 2022 projected figures materially reflect the expected capital positions immediately before and after the Proposed Transfer as at the Effective Date.

I have received all of the information that I have requested for the purposes of the production of my report. In this respect:

- Each of R&Q Theta and AIEL has provided a data accuracy statement confirming that the data and information provided to me regarding the Proposed Transfer is accurate and complete.
- R&Q Theta and AIEL have read this IA Scheme Report and each has agreed that it is correct in terms of all factual elements of the Proposed Transfer.
- I have conducted basic checks on the data provided to me for internal consistency and reasonableness.
- My checks of the data have not revealed any cause for me to doubt that it is materially appropriate for me to rely on the integrity of the information provided for the purpose of this report.

The conclusions in my report take no account of any information that I have not received, or of any inaccuracies in the information provided to me.

I have not needed to take any third-party legal advice on any aspects of the Proposed Transfer. R&Q Theta and AIEL have confirmed that they have received no other specific legal advice relevant to my role as IA for the Proposed Transfer.

Figures in this report may be subject to small rounding differences and so totals within the tables may not equal the sum of the rounded components.

2.6. Professional standards

I have considered the Code of Professional Conduct as issued by the Society of Actuaries in Ireland ("SAI") while producing this report. This report has been prepared in accordance with the following Actuarial Standards issued by the SAI and the Financial Reporting Council (FRC) in the UK:

- SAI: Actuarial Standard of Practice PA-2 (ASP-PA-2) General Actuarial Practice;
- SAI: Actuarial Standard of Practice LA-6 (ASP-LA-6) Transfer of Long-Term Business of an Authorised Insurance Company (although, strictly speaking, this guidance is required to be followed only in the case of a scheme which relates to "long-term business", ie life assurance);
- FRC: Technical Actuarial Standard 100: Principles for Technical Actuarial Work (TAS 100); and
- FRC: Technical Actuarial Standard 200: Insurance (TAS 200).

This report has been subject to independent peer review prior to its publication, in line with ASP PA-2. This peer review has been undertaken by another Partner at LCP. The peer reviewer was not involved in the production of the report. They have appropriate experience and expertise to act as peer reviewer of this report.

2.7. Materiality

I have considered matters are material if they could, individually or collectively, influence the decisions to be taken by users of this report. An assessment of such materiality is a matter of reasonable judgement that requires consideration of both the users of the report and the context for which it is prepared.

I have applied this concept in planning, performing and reporting the work described in this Scheme Report. In particular, I have applied this concept of materiality when using my professional judgement to determine the risks of material misstatement or omission and to determine the nature and extent of my work.

In complying with the reporting requirements of ASP-PA2 and TAS 100, I have made judgements on the level of information to include in this Scheme Report. For example, to make the report easier to read, I have not included all the details that would normally be included in a formal actuarial report, such as details of the methodologies and assumptions underlying the reserve and capital assessments.

2.8. Definition of "materially adverse"

In order to determine whether the Proposed Transfer will have a "materially adverse" impact on any group of policyholders, it has been necessary for me to exercise my judgement in the light of the information that I have reviewed.

The Proposed Transfer will affect different policyholders in different ways and, for any one group of policyholders, there may be some effects of the Proposed Transfer that are positive, and others that are adverse. When assessing whether the Proposed Transfer will have a "materially adverse" impact, I have considered the aggregate impact of these different effects on each group of policyholders.

Throughout the report, I have provided the rationale for my judgements and conclusions. These explain why, in each case, I have concluded whether policyholders are materially adversely affected or otherwise.

3. Outline of Proposed Transfer

3.1. The firms involved

R&Q Theta Designated Activity Company ("R&Q Theta")

R&Q Theta was known as EIIDAC prior to 27 May 2021. R&Q Theta is a subsidiary of Randall & Quilter Investment Holdings Limited (RQIH), the parent company of the R&Q Group.

Electric Insurance Ireland DAC ("EIIDAC") was an Irish domiciled captive insurance company, wholly owned by Electric Insurance Company ("EIC"), a company incorporated in the United States. In May 2021, the R&Q Group received regulatory approval from the Central Bank of Ireland ("CBI") to complete the acquisition of EIIDAC. EIIDAC stopped writing business since January 2021.

Accredited Insurance (Europe) Limited ("AIEL")

Accredited Insurance (Europe) Limited ("AIEL") is R&Q Group's primary European operation. AIEL is headquartered in Malta.

AIEL's strategy is to secure run-off business through acquisition, transfer or merger from third parties and selected European portfolios already within the R&Q Group. These portfolios are run off by AIEL, or alternatively sold on, if and where appropriate. Since 2016, AIEL also started underwriting live business through selected coverholders who would not otherwise have access to the EEA business.

AIEL has exposure to several lines of business, with around 54% of its total gross claims IFRS reserves in Motor, followed by 16% in Property and 15% in General Liability as at 31 December 2021.

The lines of business written through managing coverholders include motor, surety, liability, property, miscellaneous financial loss and after-the-event (ATE) business. The risks are domiciled in the United Kingdom, Republic of Ireland, Italy, Greece, Spain, Poland, Luxembourg and the Netherlands.

AIEL reinsures its book extensively through the use of quota share, excess of loss and stop loss reinsurance with reinsurers that are at least A- rated.

3.2. Description of the Proposed Transfer

The Transferring Business

R&Q Theta's portfolio consists of General Liability, Employer's Liability and Motor insurance cover. As part of the acquisition of R&Q Theta (formerly known as EIIDAC), the existing reinsurance arrangement with EIC was commuted and replaced by a new reinsurance programme with R&Q Cayman, part of the R&Q Group.

From 2006 to 2020, EIIDAC insured risks associated with the American multinational conglomerate, General Electric Company ("GE") and its subsidiaries and affiliates in the European Economic Area ("EEA"), the UK and Gibraltar (the "GE Group"). These risks were insured through primary layer contracts (which attach from the ground-up) and an excess layer contract. The primary layer contracts cover Employer's Liability and General Liability claims. The excess layer also covers Employer's Liability and General Liability claims, but additionally covers motor liability claims, the primary layer of which was insured externally with ACE. EIIDAC ceased underwriting risks in January 2021.

It is proposed that all the liabilities from R&Q Theta (the Transferring Business) will transfer to AIEL (the Proposed Transfer, the Scheme). All rights and obligations of R&Q Theta relating to the Transferring Business will also be transferred to AIEL.

Based on its policyholder records, R&Q Theta has identified 772 policyholders of whom 634 remain active. All active policyholders are corporate entities associated with the American multinational conglomerate, General Electric Company ("GE") and its subsidiaries and affiliates in the European Economic Area ("EEA") and the UK (the "GE Group"). R&Q Theta does not have any individual policyholders. There are no remaining active policyholders in Gibraltar.

All policyholders of R&Q Theta will transfer to AIEL and R&Q Theta will be liquidated shortly after the Proposed Transfer has completed.

Effective Date

The Effective Date (the date when the Proposed Transfer is expected to occur) will be shortly after the Sanctions Hearing which is scheduled for 3 October 2022.

Residual policies

If there are any R&Q Theta policies for which a relevant national regulator has expressly not consented to the Proposed Transfer or for which the Court determines shall not be transferred on the Effective Date of the Scheme, these Residual Policies will remain liabilities of R&Q Theta pending their transfer. I understand that, as at and from the Effective date

- all liabilities in relation to any Residual Policies will be 100% reinsured by AIEL;
- AIEL will assume responsibility for all aspects of administration of any Residual Policies.

At a later date, these Residual Policies will transfer to AIEL when the necessary regulatory consents have been received. I note that although the Scheme provides for Residual Policies for the reasons outlined above, no such Residual Policies are anticipated.

Reinsurance

In preparation for the Proposed Transfer, R&Q Theta purchased an aggregate excess of loss reinsurance treaty in May 2021. The reinsurance contract is with R&Q Re (Cayman) Limited ("R&Q Cayman") Limited. The aggregate attachment point is €3m and the maximum aggregate limit is €55m. The reinsurance has been placed on a funds withheld basis.

I understand that, coinciding with the transfer, the reinsurance treaty will be novated from R&Q Theta to AIEL so that it will remain in place following the Proposed Transfer, and will continue to be on a funds withheld basis.

Claims handling

Claims handling for R&Q Theta's business is outsourced to Crawfords, a large publicly listed provider of outsourced claims management services. Following the Proposed Transfer, claims handling for the transferring business will continue to be performed by Crawfords on behalf of AIEL.

3.3. Purpose of the Proposed Transfer

R&Q Theta (formerly known as EIIDAC) was acquired by the R&Q Group in May 2021. R&Q Theta had already been closed to new business and renewals prior to the acquisition. As part of the business plan regarding the acquisition, R&Q Group had envisaged that all remaining liabilities would transfer across from R&Q Theta to AIEL, subject to a Section 13 transfer, if approved by the Irish High Court.

AIEL is a specialist provider of run-off solutions for legacy books of business. It has significant experience in managing run-off liabilities. Through the Proposed Transfer, AIEL aims to manage the run-off of the R&Q Theta liabilities.

3.4. Alternative options considered

As outlined above, the intent on acquiring R&Q Theta (formerly EIIDAC) was always to transfer the business to AIEL and is in line with the Group's business strategy. In the absence of the Proposed Transfer, R&Q Theta would remain as a stand-alone entity, which is not capital efficient for the Group.

This report considers the effects on the relevant policyholders, if the Proposed Transfer being presented to the Court is implemented. The responsibility to consider alternative schemes rests with the directors and managers of the companies involved. I understand that no alternative schemes of transfer were considered in this case.

3.5. Key dependencies

The key dependencies of the Proposed Transfer are as follows:

- Irish High Court approval is required for the Proposed Transfer – the Directions Hearing is scheduled for 30 May 2022 and the Sanctions Hearing is currently scheduled for 3 October 2022. The High Court will take into account whether the CBI has any objections to the Proposed Transfer.
- Any objections raised by policyholders after the Directions Hearing – I will comment on these (if any exist) in my Supplementary Report.

In the event of the Proposed Transfer not going ahead, policies would remain with R&Q Theta and the existing reinsurance treaty with R&Q Cayman would stay in place.

4. My approach as IA

Overall role

As IA, my overall role is to assess whether:

- The security provided to policyholders of R&Q Theta or AIEL will be materially adversely affected by the implementation of the Proposed Transfer.
- The Proposed Transfer will have any adverse impact on service standards experienced by policyholders.

The two key affected parties

To make these assessments, I have considered the effect of the Proposed Transfer on the following two parties:

- "Transferring Policyholders", ie R&Q Theta policyholders whose liabilities will transfer to AIEL as a result of the Proposed Transfer.
- "Existing AIEL Policyholders", ie policyholders of AIEL immediately prior to the Proposed Transfer, who will remain with AIEL after the Proposed Transfer.

In addition to the policyholders described above, in drawing my conclusions, I have considered the impact of the Proposed Transfer on potential Beneficiaries and Claimants, for example the employees of those companies who hold Employers' Liability insurance policies with R&Q Theta.

Five-step approach to analysing the Proposed Transfer

My approach to assessing the Proposed Transfer has been to perform the following five steps analysing evidence provided by R&Q Theta and AIEL to support the Proposed Transfer:

Step 1: Assessing the provisions of R&Q Theta and AIEL

The first important form of security that an insurer provides to policyholders is the level of provisions. Provisions are based on an estimate of the amount of money the insurer will need to pay policyholders' claims and to cover the other costs associated with running the insurer.

Therefore, I have assessed the appropriateness of the provisions included on R&Q Theta's balance sheet and the approach to be used for the calculation of provisions for both R&Q Theta and AIEL pre- and post-transfer. Details of this step are set out in section 5.

Step 2: Assessing the capital positions of R&Q Theta and AIEL

In addition to the level of provisions, insurers hold capital designed to withstand more extreme levels of claims. The level of capital held is the second important form of security provided to policyholders.

For both R&Q Theta and AIEL, the level of capital required is set under the European Solvency II standard. A key regulatory solvency metric is the Solvency Capital Requirement. This is an estimate of the capital required to cover the losses that an insurer could experience over the next 12 months with a probability of 99.5% (ie a 1 in 200 probability adverse outcome).

I have assessed the appropriateness of the projected capital requirements of R&Q Theta and AIEL. Details of this step are set out in section 6.

Step 3: Assessing overall policyholder security

Under this step, I have considered the level of provisions and capital (from steps 1 and 2) in the context of the assets held by each of R&Q Theta and AIEL and other forms of security such as compensation schemes.

For this analysis, I have considered the current balance sheets of R&Q Theta and AIEL as well as the post transfer pro-forma balance sheets for each of R&Q Theta and AIEL. Details of this step are set out in section 7.

Step 4: Assessing policyholder communications

I have assessed the appropriateness of R&Q Theta's communication strategy to inform policyholders and other stakeholders of the Proposed Transfer. The key focus of my assessment was whether the policyholders and other stakeholders are to be provided with sufficient and clear enough information so that they can understand how the Proposed Transfer may affect them. Details of this step are set out in section 8.

Step 5: Assessing potential impact on customer service and other considerations that might affect policyholders

I have considered how the level of customer service provided to policyholders could change following the Proposed Transfer. I have also considered a range of other factors that might affect policyholders, such as ongoing expense levels and tax implications. Details of this step are set out section 9.

5. Reserving considerations

5.1. Introduction to insurance reserving

For an insurance firm, the primary purpose of reserving is to assess the provisions that need to be set in order to pay policyholders' claims and to cover the other costs associated with running an insurer.

Depending on how they are set, the provisions may be on a "best estimate" basis (with no deliberate optimism or pessimism) or include a "margin for uncertainty" (additional provisions to cover higher than expected claims). This is sometimes referred to as a "management margin". Where the provisions include a margin for prudence, this is typically designed to cover claims that are moderately higher than expected rather than more extreme levels of claims. A best estimate basis is intended to indicate a single "point-estimate" of the provisions, but practically there often exists a range of estimates that could be justified as a best estimate.

In addition to any margin for uncertainty, the insurer would nearly always hold additional capital designed to withstand more adverse levels of claims. My considerations related to capital for the Proposed Transfer are set out in section 6.

Introduction to reserving bases

Insurers use a range of different reserving bases (ie different measures of the provisions), for different purposes.

For example, financial accounting standards require the provisions to be calculated in particular ways, and an insurer may also use a different basis for internal management accounts. Solvency II requires provisions to be calculated in yet another way.

For the Proposed Transfer, I have considered the provisions under two reserving bases, which are each relevant for different purposes, namely:

- International Financial Reporting Standards (IFRS) - these are the accounting standards used to set the booked provisions underlying the published financial accounts of R&Q Theta and AIEL respectively. IFRS provisions are relevant for policyholders as they are used as a reference point when setting provisions to cover future claims and other costs.
- Regulatory technical provisions (or "Solvency II technical provisions") – these are calculated in line with the European Solvency II regulations that came into effect in the EU from 1 January 2016. These provisions are relevant for policyholders as they are the basis for calculating the capital required and assessing solvency for both R&Q Theta and AIEL.

5.2. My considerations relating to reserving

As IA, my overall assessments related to reserving are:

- whether an appropriate level of provisions is maintained for all relevant policyholders, that is: Transferring Policyholders and Existing AIEL Policyholders; and
- whether any aspects of the reserving may lead to policyholders being materially adversely affected by the Proposed Transfer.

To make these assessments, I have considered the following areas:

- Appropriateness of booked and regulatory provisions for R&Q Theta and AIEL (sections 5.3 to 5.6);
- Key uncertainties when setting the provisions and other risks (sections 5.7 to 5.8);
- Current R&Q Theta and AIEL reserving process and governance (section 5.9); and
- Future reserving approach and governance (section 5.10).

Within these areas, I have also considered any expected differences in the reserving approach between R&Q Theta and AIEL to understand how this may affect policyholders.

Further details on each of these considerations are set out below, and I have stated my overall conclusion related to reserving in section 5.11.

Approach to my review

I have considered the appropriateness of the following:

- IFRS booked provisions for R&Q Theta and AIEL as at 31 December 2021; and
- Solvency II technical provisions for R&Q Theta and AIEL as at 31 December 2021

I have reviewed a number of documents provided by R&Q Theta and AIEL relating to the setting of provisions, including the reserving process and governance. I have also had meetings with R&Q Theta and AIEL to discuss the information provided and any questions I have had on the reserving approach.

I have reviewed the approach used to set the IFRS claims reserves and the conversion to Solvency II technical provisions. I have also reviewed the movement of estimates from year to year since December 2020. While I have not sought to re-perform the calculations, my review has allowed me to assess the appropriateness of the actuarial estimates and volatility of the underlying business.

A list of the key data and documentation is provided in Appendix 4.

5.3. Summary of booked provisions for R&Q Theta and AIEL

The following table shows the level of booked provisions (as per the latest available figures at the time of writing) for the transferring business for R&Q Theta and the Existing Business for AIEL. The figures below are net of deferred acquisition costs and include provisions for unexpired risks, unallocated loss adjustment expenses, reinsurance bad debt and margins for uncertainty.

Summary of IFRS booked provisions at 31 December 2021

€m	Gross of reinsurance	Net of reinsurance
R&Q Theta	32.6	1.9
AIEL	574.3	96.4

Source R&Q Theta: Draft Actuarial Report on Technical Provisions as at 31 December 2021
Source AIEL: Schedule of December 2021 IFRS figures

R&Q Theta's net liabilities are less than 2% of AIEL's net liabilities as at 31 December 2021.

R&Q's Theta's Actuarial Function is outsourced to an external consultancy, and R&Q Theta's reserves are analysed quarterly by the external Head of Actuarial Function. The booked reserves include a margin for uncertainty which is set by the company. In determining the provisions, discussions are held with internal senior management, claims and reinsurance teams. External auditors review the reserves on an annual basis and feedback is incorporated into the reserving and reporting thereafter.

AIEL's reserves are analysed quarterly by the R&Q Group Chief Actuary supported by the internal actuarial team. In determining the provisions, discussions are held with internal senior management, claims and reinsurance teams. AIEL also engages an external actuarial consultancy to review the reserves on an annual basis.

The table below shows the breakdown of the gross reserves for each entity.

Breakdown of gross IFRS booked provisions at 31 December 2021

€m	R&Q Theta	AIEL
Outstanding claim reserves	16.2	238.7
Incurred but not reported	14.2	77.9
Unearned Premium Reserve	0.0	257.7
Unallocated loss adjustment expenses	1.3	0
Margin for uncertainty	0.9	0
Total provisions	**32.6**	**574.3**

R&Q Theta's provisions are made up of earned claims reserves. The unearned premium reserves are zero as the business in run-off and all the premium written prior to 1 January 2021 is fully earned.

AIEL's provisions are made up of earned claims reserves and unearned premium reserves (to cover future incidents). AIEL's practice is not to hold an explicit provision for Unallocated Loss adjustment expenses as it considers that investment income will be sufficient to cover these costs.

5.4. Booked provisions for R&Q Theta

The table below shows the level of provisions estimated by the Head of Actuarial Function for R&Q Theta, and the margin for uncertainty set by the company, as at 31 December 2021 (the latest available figures at the time of writing of this report), broken down by the reserving classes.

R&Q Theta – Summary of IFRS booked provisions at 31 December 2021

€m	Gross of reinsurance	Net of reinsurance
General Liability	25.6	n/a
Employers' Liability incl Noise Induced Hearing Loss	4.5	
Motor	0.3	
Unallocated Loss adjustment expenses	1.3	
Margin for uncertainty	0.9	
Total Transferring Business	**32.6**	**1.9**

Source R&Q Theta: Draft Actuarial Report on Technical Provisions as at 31 December 2021

R&Q Theta ceased writing business in January 2021. The provisions are made up of earned claims reserves only; there is no unearned premium reserve as all business is earned.

I describe below the reserving approach used by R&Q Theta's Actuarial Function in estimating the claims reserves shown in the table above.

Claims are reserved using standard actuarial techniques, such as the Development Factor Model, Bornhuetter-Ferguson method and the Gunnar-Benktander method. Claims are grouped together on an accident year basis, other than for Noise Induced Hearing Loss for which claims are analysed on a reporting-year basis.

In my opinion, the Actuarial Function's reserving approach is reasonable and in line with market practice.

5.5. Booked provisions for AIEL

AIEL secures legacy businesses through acquisition, transfer or merger from third parties and selected European portfolios already within the R&Q Group.

Since 2016, AIEL also started underwriting live business, ie the program portfolio, through selected coverholders who would not otherwise have access to the EEA business. This is done with the support of reinsurers with at least an A- credit rating. Where a reinsurer does not have this rating, or is downgraded, they are required to provide collateral to AIEL that is at least equivalent to the projected level of reserves.

The following table shows the level of provisions estimated by the Actuarial Function as at 31 December 2021 (the latest available figures at the time of writing this report) for AIEL. The figures below are net of deferred acquisition costs and include provisions for unexpired risks, unallocated loss adjustment expenses, reinsurance bad debt and margins for uncertainty.

AIEL – Summary of IFRS booked claims reserves at 31 December 2021

€m	Gross of reinsurance	Net of reinsurance
Legacy	85.0	63.1
Program	489.3	33.3
Total AIEL	**574.3**	**96.4**

Source: AIEL Schedule of IFRS figures as at 31 December 2021

AIEL has exposure to several lines of business, with around 54% of its total gross claims IFRS reserves in Motor, followed by 16% in Property and 15% in General Liability as at 31 December 2021.

AIEL commissioned an external consultancy to perform an independent reserve review using data as at 30 September 2021, followed by an update as at 31 December 2021. The external actuaries produced independent projections for a selection of the portfolios and reviewed AIEL's internal reserve estimates on the remainder of the portfolios. The external opinion provides an independent challenge to AIEL's booked claims provisions.

As at 31 December 2021, AIEL's aggregate booked IFRS net reserves were approximately 5% higher than the values indicated by the external opinion.

I describe below the reserving approach used by AIEL's Actuarial Function in estimating the claims reserves shown in the table above.

AIEL - reserving for Legacy portfolio

The underlying legacy books within AIEL contain a variety of exposures including Property, UK Employer's Liability, including asbestos claims and US Asbestos, Pollution & Health. A range of actuarial techniques are used to estimate the provisions.

For UK Asbestos exposure, models from the actuarial Asbestos Working Party ("AWP") are used and parameterised to be in line with the data in the portfolio. This is assessed and combined with expert judgement. For US and Australian asbestos exposures, a combination of detailed ground-up analysis, survival ratios and IBNR to outstanding reported claims ratios is used. Specific methods are determined by the portfolio in question and the data available.

Where sufficient data is available, other segments of the Legacy portfolio are reserved using Development Factor Model methods where appropriate. This involves the projection of paid and incurred triangle development data.

AIEL - reserving for Program portfolio

Reserves are calculated using a mixture of standard actuarial projection methods. Where classes or years of account are undeveloped, the predominant method involves the use of the Initial Expected Loss Ratio (IELR). These IELRs are based on historical experience and benchmark loss ratios.

Where classes are more developed or have higher levels of historical data the Development Factor Model and Bornhuetter-Ferguson methods are used.

AIEL – net reserves

Legacy: To estimate the net of reinsurance reserves, the main approach is to apply net to gross ratios, based on past experience and actuarial judgement.

Program: To estimate the net of reinsurance reserves, the actuarial team apply a mixture of net to gross ratios, and explicit netting down of the gross reserves by direct application of the reinsurance programme in place.

In my opinion, AIEL's reserving approach is reasonable and in line with market practice.

5.6. Approach for setting Solvency II technical provisions

I have reviewed the approach taken by R&Q Theta and AIEL to convert the booked IFRS provisions into Solvency II technical provisions (TPs). I have not sought to re-perform the calculation of the TPs or to perform detailed checking of the calculations performed by R&Q Theta and AIEL. Instead, I have focused on the appropriateness of the approach and the reasonableness of the results.

I have focused my review on the areas which, in my experience, are of greatest relevance to an independent reviewer. These included Events Not in the Data (ENIDs) and the Risk Margin.

ENIDs

R&Q Theta and AIEL make an allowance for ENIDs within the TPs as the data used to calculate the best estimate does not typically include experience from rare events.

R&Q Theta's ENID load as at 31 December 2021 is around 5% of the total gross best estimate claims provisions.

AIEL's ENID load as at 30 September 2021 is around 1% of the Legacy gross best estimate provisions and around 5% of the Program gross best estimate provisions. The loading will continue to be at similar levels following the Proposed Transfer.

In my experience, I consider these loadings to be broadly in line with those typically held by other insurers writing similar lines of business, and the method used to calculate the ENID provisions is commonly used.

Risk margin

The risk margin within the TPs under Solvency II represents the amount in addition to the best estimate that a third-party insurer would require to take over the insurance obligations.

There are a number of ways to calculate the risk-margin. Both R&Q Theta and AIEL calculate the Risk Margin using a simplified cost of capital approach in line with regulatory guidance. These approaches involve projecting capital requirements over the remining lifetime of the liabilities, and normally involve a level of simplification. In my view, the approaches taken by R&Q Theta and AIEL are appropriate and in line with common market practice.

Conclusion on Solvency II technical provisions

In my opinion, the approaches used by R&Q Theta and AIEL to calculate the Solvency II TPs are appropriate.

5.7. Key uncertainties when setting provisions

The ultimate costs of settling general insurance claims are subject to uncertainty in terms of both the frequency (ie how many valid claims there will be) and severity (ie the cost of settling each claim) including exposure to inflation in claim amounts over time. Therefore, there are uncertainties when setting the corresponding provisions.

Key uncertainties – Transferring Business

Key reserving uncertainties, specific to the Transferring Business are as follows:

- R&Q Theta's reserves relate entirely to liability business. Such business has the potential for late notifications and material developments and so the tail on these reserves can be long and subject to a large degree of uncertainty. Given the specific risks covered by R&Q Theta there is also exposure to latent claims, notably for industrial diseases such as Noise Induced Hearing Loss which is reserved for as its own class, and Vibration White Finger, the reserves for which are included with Employer's Liability reserves.
- I understand that there are a small number of claims notified with asbestos exposure, all of which have closed with nil or small claims handling fees. While there is some potential for these cases to re-open or for new claims to emerge, R&Q Theta considers that the likelihood of the emergence of additional material losses in this regard, which are not captured by the existing reserving models, is sufficiently low that no specific allowance for this has been made in the calculation of the reserves."
- R&Q Theta covers risks denominated in multiple currencies, but all amounts are valued in EUR. This exposes R&Q Theta to currency risk as its EUR liabilities will increase should foreign currencies weaken against the Euro.
- The standard actuarial methodology used to calculate the reserves assumes that historical inflation will remain consistent across the projection horizon. This may not be appropriate; for example, inflation has increased in recent months which may have a prolonged impact on claims settlements. No explicit allowance has been made for this in the calculation of the technical provisions given the uncertainty around future inflation changes and also the differences across jurisdictions which are difficult to incorporate into the reserving process for a book of this size. However, the selected trending approach applied for the assumption setting for the General Liability reserving class can be considered to implicitly make some allowance for the recent increase in inflation.
- There is increased uncertainty in liability projections at present due to ongoing disruption caused by the COVID-19 pandemic, including uncertainty around the adjustments required to allow for lockdowns and resulting claims notification delays. Allowing for an additional one month's delay to the development of claims would increase the gross reserves by €575k (2%).

In my view, the protection provided by the excess of loss reinsurance programme means that the impact of any of the scenarios above would not be significant on a net basis.

Given R&Q Theta's high level of reinsurance, the net technical provisions are dominated by the expense provisions. These expenses are exposed to inflationary pressures, particularly in the current economic environment. Therefore, to support my work in producing this report I requested some inflation sensitivities to illustrate this uncertainty. These sensitivities show that additional expense inflation of 2% and 3% respectively per annum over the future lifetime of the liabilities would add €136k (8%) and €328k (19%) respectively to the net technical provisions.

Key uncertainties – Existing AIEL business

Key reserving uncertainties, specific to the existing business in AIEL, are as follows:

- AIEL holds significant reserves relating to industrial diseases, such as mesothelioma and Noise Induced Hearing Loss. These claims have an inherently long tail, which increase the uncertainty of the reserves. They are also modelled on low volumes of past data and are subject to legal risk in the form of court interpretations and legislative change which could materially alter reserves. However, these portfolios are considered mature with circa 15% of net reserves relating to these risks.
- The reinsurance recovery for the Legacy portfolios within AIEL has been estimated using net to gross ratios based on past experience and actuarial judgement. The specific reinsurance programmes and wordings have not been reviewed in detail and there is a risk that recoveries in practice are not as has been assumed.
- The Program portfolio is relatively new to AIEL, and there are a number of material uncertainties associated with its reserves:
    - the business is fairly immature and benchmarks have been used heavily in setting reserves;

- some of the business is volatile and long tailed;
- large motor claims in particular can be settled by periodical payment order which have a high degree of uncertainty about their present value;
- approximately 90% of the gross ultimate is reinsured, leaving significant exposure to reinsurance default or dispute; and
- uncertainties relating to COVID-19; specifically reduced exposure to motor claims during lockdowns, and the outcome of the Supreme Court case on business interruption wordings for a which a specific IBNR is being held.

The uncertainties described above in the R&Q Theta and AIEL portfolios are typical of the risks written within a general insurance portfolio. Reinsurance is used to mitigate the impact of these key uncertainties and also a risk margin is held within the Solvency II technical provisions.

5.8. Other risks

Impact of COVID-19 on the Proposed Transfer

The most recent policy years for AIEL are impacted by the COVID-19 pandemic. The uncertainty around the impact of COVID-19 is expected to continue until the Effective Date of the Proposed Transfer and beyond.

Key impacts on AIEL's business include:

- reduced exposure to motor claims during lockdowns
- exposure to claims through business interruption cover provided by one of the coverholders, for which a specific IBNR is being held
- a slowdown in premium income due to termination of some programs and some programs going live later than expected due to delays in regulatory approvals.
- losses on the investment portfolio following the economic uncertainty arising from the pandemic.

The COVID-19 pandemic has not had a significant impact on the Transferring business ie R&Q Theta's claims, in terms of direct losses. Any impact of COVID-19 is confined to policies written in 2020. R&Q Theta has confirmed that, for the Transferring Business, there have been only two notified claims to date where the claim is known to be related to COVID-19. These claims relate to the ventilators used on COVID-19 patients and do not appear to indicate an additional exposure specific to COVID-19. Given that there have been so few claims reported to date, this is not expected to be a material source of future claims.

Potential impacts on the business include a general disruption to claims notification, development and settlement processes. An example of how this may impact the reserves includes court closures leading to backlogs and reduced availability of medical services. This may delay the development of injury claims. In order to allow for the impact of this disruption, R&Q Theta has allowed a delay factor of 3 months in the development patterns used to estimate the reserves.

Even if some of the potential impacts above were to materialise, the impact on the reserves for the Transferring Business would be unlikely to be material relative to the reserving scenarios presented in section 6.10.

Although the impact of the pandemic is uncertain, in my view the impact on the Transferring Business is limited relative to the overall uncertainty in these liabilities.

In my opinion, the COVID-19 pandemic does not materially change my overall conclusions as set out in section 1.3.

I will provide an update on the potential impacts of COVID-19 in my Supplementary Report.

Climate change

In my view, the potential impact of climate change on the business written by R&Q Theta and AIEL is less significant than other risks considered in this report and therefore does not materially affect my conclusions.

It is possible that the reserves could be impacted by climate change given the uncertainty and far-reaching impacts it may continue to have. Examples of areas that could be impacted include latent liability claims and changes in social behaviour, which in turn could drive an increase in claims frequency or severity.

However:

- For R&Q Theta, as the business is in run-off, there is no exposure to an increase in the frequency or severity of natural catastrophes, the most obvious impact of climate change.
- The line of business most exposed to climate change for AIEL is Property, which accounts for approximately 15% of AIEL's gross claims reserves. However, because property catastrophic events are reported quickly, the climate related uncertainty AIEL's in current reserves is low. Therefore, the main impact of climate change will be in the future.
- The future impact of climate change is expected to be gradual and the risks and uncertainties in AIEL's business can be managed over time.

5.9. Current reserving process and governance

R&Q Theta – reserving process and governance

R&Q's reserves are calculated by the external actuarial function with input and challenge from the R&Q group reserving function. Technical Provisions are calculated in accordance with R&Q's Reserving Policy and approved by R&Q's board.

The Actuarial Function applies its own internal control and quality control procedures, including a peer review in accordance with the relevant actuarial standards.

In accordance with the CBI's domestic actuarial regime, the actuarial function provides an annual Actuarial Opinion on Technical Provisions, supported by an Actuarial Report on Technical Provisions addressed to the board.

AIEL – reserving process and governance

The AIEL reserves are calculated by R&Q Group's actuarial team.

Following the Proposed Transfer, I understand that the R&Q Group will continue to provide the reserving for the existing business as well as for the Transferring Business.

AIEL's reserves are subject to several layers of internal review which take place on a quarterly basis. This includes peer review of reserving methodology and assumptions within the reserving team, review by the R&Q Group Chief Actuary and sign-off by the AIEL Board.

AIEL appoints an external consultancy to carry out an independent review of the AIEL reserves at Q3, with a roll forward to Q4. I understand that AIEL intends to continue performing external actuarial reviews on a regular basis to provide challenge to the internal reserving process.

5.10. Future reserving approach and governance

AIEL has confirmed that it plans to continue to use the current approach to reserving for the existing business following the Proposed Transfer. While reserving for the Transferring Business will, in future, be performed by R&Q Group's actuarial team, the methods and approach to calculating and reporting provisions will be consistent with the approach adopted currently by R&Q Theta's external outsourced Actuarial Function.

I understand that AIEL intends to continue to commission external independent actuarial reviews on a regular basis to provide challenge to the internal reserving process.

5.11. Overall conclusion: reserving considerations

I set out below my overall conclusions related to reserving. These reserving considerations should not be considered in isolation. For example, the overall level of protection for policyholders also depends on the level of capital held, and a range of other considerations. My overall conclusions on the Proposed Transfer are set out in section 10.

Transferring Policyholders

I have concluded that the Transferring Policyholders will not be materially adversely affected by the reserving aspects of the Proposed Transfer. My key reasons are as follows:

- R&Q Theta's calculation of provisions for the Transferring Business has been performed using appropriate techniques.
- The reinsurance treaty with R&Q Cayman will remain in place following the Proposed Transfer.
- AIEL has confirmed that claims handling for R&Q Theta's business will continue to be performed by Crawfords following the Proposed Transfer.
- AIEL has confirmed that the transferring policies will continue to be reserved in the same way post-transfer as pre-transfer.
- AIEL has confirmed that the reserving process and governance following the Proposed Transfer will be materially unchanged post-transfer.

Existing AIEL Policyholders

I have concluded that the Existing AIEL Policyholders will not be materially adversely affected by the reserving aspects of the Proposed Transfer. My key reasons are as follows:

- The calculation of provisions for AIEL has been performed using techniques and approaches appropriate for the portfolios within AIEL.
- The transferring provisions are relatively small compared to the existing AIEL provisions and so the Proposed Transfer will have a limited impact.
- AIEL has confirmed that the reserving process and governance following the Proposed Transfer will be materially unchanged post-transfer.

6. Capital considerations

6.1. Introduction to insurance capital setting

A key reason why insurers hold capital is to withstand adverse or extreme levels of claims and other losses. The capital is held in excess of the provisions for policyholders' claims and for the other costs associated with running an insurer.

A key metric under solvency regulations is the Solvency Capital Requirement (SCR). This is an estimate of the capital required to cover the loss that an insurer could experience over the next 12 months with a probability of 99.5% (ie, a 1 in 200 probability adverse outcome). Under Solvency II, firms are required to hold capital equal to at least 100% of the SCR.

An insurer's SCR coverage ratio is calculated as the available capital, in excess of provisions, divided by the SCR. This is a measure of capital strength, with a higher ratio indicating there is more capital available per €1 of capital required. The SCR coverage ratio does not capture all aspects of policyholder protection, but a higher coverage ratio indicates more protection, all else being equal. Under Solvency II, the level of available capital is referred to as "own funds".

I consider the SCR coverage ratio an appropriate measure to consider as part of my assessment of policyholder security before and after the transfer for the following reasons:

- The SCR coverage ratio is an objective measure of the financial strength of an insurer that can be compared on a consistent basis at two points in time;
- Both companies use the Solvency II standard formula to calculate their SCRs, so that it is possible to compare their financial strengths on a consistent basis; and
- The SCR is a risk-based metric that is disclosed to both regulators and the public.

My assessment of the capital considerations regarding policyholder security is also supported by a review of the impact of a range of adverse scenarios on each of R&Q Theta and AIEL (section 6.10). The adverse scenarios applied to claim reserves consider risks on an ultimate basis, ie beyond the one-year horizon captured by the SCR.

Definition of "well capitalised" and "very well capitalised"

For the purposes of this report, I describe a company as having "sufficient capital" if the SCR coverage ratio is between 100% and 150%. I describe a company as "well capitalised" if the SCR coverage ratio is between 150% and 200% and "very well capitalised" if the SCR coverage ratio is in excess of 200%.

6.2. My considerations related to capital

As IA, my overall assessments related to capital are:

- whether the projected capital requirements have been calculated appropriately for both R&Q Theta and AIEL;
- whether there are expected to be any material adverse changes in the strength of capital protection for any group of policyholders (I have assessed this by comparing the projected SCR coverage ratios pre- and post-the Proposed Transfer); and
- whether any other aspects of the capital considerations may lead to policyholders being materially adversely affected by the Proposed Transfer.

To make these assessments, I have considered the following areas:

- R&Q Theta and AIEL's approach to calculating capital requirements (section 6.4);
- The capital policy for each of R&Q Theta and AIEL (section 6.6);
- SCR appropriateness for R&Q Theta and AIEL (section 6.7);
- Projected SCR coverage ratios as at the Effective Date (section 6.8);
- The planned capital structures for R&Q Theta and AIEL (section 6.9); and
- The SCR under stressed scenarios (section 6.10).

6.3. Approach to my review

I have reviewed a number of documents provided by R&Q Theta and AIEL relating to the calculation of capital requirements and projected coverage ratios. A list of the key data and documentation reviewed is provided in Appendix 4.

6.4. Calculating capital requirements

For both R&Q Theta and AIEL, the level of regulatory capital required is set under the European Solvency II directive.

Under Solvency II, there are three ways in which the SCR can be calculated:

- Standard formula: under this approach, the SCR is set using a prescribed calculation and parameters, as specified in the Solvency II regulations. Within the standard formula framework, insurers can use undertaking-specific parameters (USPs) to tailor specific aspects of the parameterisation of the calculation to better reflect their risk profile.
- Internal model: under this approach, the SCR is set using the insurer's own internal capital model. The internal model is developed and parameterised by the insurer to reflect their specific business.
- Partial internal model: under this approach, the SCR is set using a combination of the standard formula and the insurer's own internal capital model. Some aspects of the SCR are calculated using the internal model, and the remainder is calculated using the standard formula.

The choice of approach is made by the insurer. However, an insurer needs to obtain regulatory approval in order to use USPs, an internal model or a partial internal model to calculate its SCR. An insurer does not need approval to calculate its SCR using the standard formula without USPs but does need to complete its own annual assessment of the appropriateness of the standard formula for this purpose.

Both R&Q Theta and AIEL use the standard formula without USPs to calculate their SCRs.

Minimum Capital Requirement

In addition to the SCR, another key measure of capital under Solvency II is the Minimum Capital Requirement (MCR).

The MCR is a simpler calculation than the SCR, using a formula based on volumes of premiums and Solvency II technical provisions.

For non-life insurers, the MCR is between 25% and 45% of the SCR, subject to a minimum of €3.7m or €2.5m depending on the business written. This minimum typically only bites for the smallest insurers.

Firms need to hold capital equal to at least the greater of the SCR and the MCR. The purpose of the MCR is to ensure that firms are holding at least a minimum level of capital. Breaching the MCR will result in more intensive regulatory intervention than would be the case for a breach of the SCR.

The MCR coverage ratio is calculated as the available capital in excess of provisions divided by the MCR.

Both R&Q Theta and AIEL are projected to be very well capitalised on this measure with MCR coverage ratios of:

- 224% for R&Q Theta, and 741% for AIEL immediately Pre-Transfer
- 691% immediately Post-Transfer for the AIEL. The projected drop in coverage Post-Transfer is explained by (i) AIEL using an alternative higher estimate for the transferring technical provisions and (ii) AIEL treating ring-fenced assets transferred from R&Q Theta as ineligible own funds in AIEL. The restrictions on these transferred assets are expected to be lifted during 2023.
- 689% and 706% for AIEL entity at December 2023 and December 2024 respectively.

For both R&Q Theta and AIEL, both Pre-Transfer and Post-Transfer, the SCR is higher than the MCR. Therefore, I have not considered the MCR further as part of my assessment of capital considerations, and my primary focus is on the SCR.

6.5. Components of capital requirements

The key components of the SCR for both R&Q Theta and AIEL are:

- Market risk: the risk of changes in an insurer's financial position due to changes in the market value of assets, liabilities and financial instruments. For example, this includes the risk of falls in the value of investment assets that are being held to make future claims payments.

  For R&Q Theta, there is an adjustment for Funds at Lloyd's ("FAL") within the market risk component, which is calculated separately. The FAL adjustment in respect of R&Q Theta's investment in a corporate Lloyd's member and the corresponding ring-fencing of that investment. To allow for this investment within the SCR, the FAL investment is treated as an unrated Type 2 equity investment. This approach was agreed by the Actuarial Function with R&Q Theta's management, the capital team and R&Q Theta's auditors. AIEL has similar ring-fenced funds and the treatment of these within the SCR is consistent with R&Q Theta's treatment.

- Underwriting risk: the risk that the value of insurance claims proves to be higher than expected. This includes the risk of an increase in claims and uncertainties related to existing liabilities included on the balance sheet (reserving risk).

  For AIEL, underwriting risk also includes the risk of experience being worse than planned for business that will be earned or written over the following year (premium risk). For R&Q Theta, there is no premium risk for the transferring liabilities as no new business is being written or earned over the following year.

- Counterparty default risk: the risk of defaults or downgrades by counterparties that either owe the insurer money or hold money on its behalf. For example, this includes the risk of the failure of a reinsurer.

- Operational risk: the risk of losses caused by failures in an insurer's operational processes, people and systems, or from events that are external to the insurer. For example, this would include the risk of fraud or IT failure.

The sum of these components gives the "undiversified" SCR. The SCR (ie diversified SCR) is typically lower than the undiversified SCR, as it allows for the statistical diversification between the components.

R&Q Theta and AIEL have provided actual SCR calculations as at 31 December 2021, and projected SCR calculations at the time of the proposed transfer. I have summarised the key risks as a percentage of the total SCR, both pre-transfer and post-transfer, below. There are no projections for R&Q Theta post-transfer as all the liabilities are planned to transfer across to AIEL on the Effective Date.

The figures shown for R&Q Theta are projections as at 30 September 2022. The figures shown for AIEL are projections as at 31 December 2022. In both cases, given the stability of the solvency projections, these serve suitable proxy for values as at the proposed transfer date which is expected to be in October 2022.

R&Q Theta: Projected breakdown of SCR risk components pre-Transfer

Risk components €m	As at 31 December 2021		Pre-transfer	
Market risk	4.2	*86%*	4.2	*90%*
Counterparty default risk	0.1	*2%*	0.1	*2%*
Underwriting risk	0.5	*11%*	0.2	*5%*
Diversification	(0.3)	*(7%)*	(0.2)	*(5%)*
Operational risk	0.4	*8%*	0.3	*7%*
SCR	**4.9**	***100%***	**4.7**	***100%***

Source: R&Q Theta

For R&Q Theta, the most material component of the projected SCR is market risk, which represents around 90% of the projected SCR. Underwriting risk, at 5%, is low compared to a typical insurer. This is because R&Q Theta has a very high level of reinsurance protection, so that the net risk retained is small. R&Q Theta's counterparty default risk is low because the risk of reinsurer default is mitigated because the reinsurance has been placed on a funds withheld basis.

AIEL: Projected breakdown of SCR risk components pre- and post- Proposed Transfer

Risk components €m	As at 31 December 2021		Pre-transfer		Post-transfer	
Market risk	18.0	*34%*	23.3	*34%*	26.3	*37%*
Counterparty default risk	11.3	*21%*	14.4	*21%*	14.0	*20%*
Underwriting risk	27.6	*51%*	34.0	*50%*	34.7	*49%*
Diversification	(14.3)	*(27%)*	(19.5)	*(29%)*	(20.4)	*(29%)*
Operational risk	11.2	*21%*	15.7	*23%*	16.4	*23%*
SCR	**53.8**	***100%***	**67.8**	***100%***	**70.9**	***100%***

Source: AIEL

For AIEL, the most material component of the SCR is underwriting risk, which represents 50% and 49% of the SCR pre- and post-transfer respectively. Market risk is also a material contributor to the SCR, representing 34% of the SCR pre-transfer and 37% of the SCR post-transfer.

As can be seen from the table, the risk profile, ie the relative mix of risks, is not materially affected by the proposed transfer. This is because the transferring business is small relative to the existing AIEL business.

6.6. Capital policy for each of R&Q Theta and AIEL

I have reviewed the companies' Risk Appetite Statements to assess their capital policy in terms of minimum acceptable solvency coverage. Both R&Q Theta and AIEL target a minimum buffer above the regulatory SCR as part of their Risk Appetite Statements. These buffers are set by the companies' respective boards to reflect the nature, scope and complexity of their risk profiles.

AIEL's policy is to maintain total capital above 125% of the SCR. R&Q Theta's policy is to maintain a solvency margin of at least 110% of the SCR. I note that AIEL's minimum buffer over SCR is higher than R&Q Theta's and, all else being equal, this indicates higher level of capital security for policyholders.

However, in both cases, I would consider this to be sufficient capital as described in section 6.1. In addition, as at 31 December 2021 both companies were well above their risk appetites for SCR coverage. Based on the projections in section 6.8, AIEL is expected to remain well above its risk appetite after the Proposed Transfer and throughout the projection period.

6.7. SCR appropriateness for R&Q Theta and AIEL

For R&Q Theta and AIEL, I have considered SCR appropriateness by considering two aspects:

- reviewing each company's assessment of the appropriateness of using the standard formula for the purposes of setting the SCR; and
- reviewing each company's documentation of its standard formula SCR calculations and process to satisfy myself that the calculations are being performed in line with the Solvency II Delegated Regulations.

R&Q Theta - appropriateness of the standard formula

R&Q Theta's risk management function has assessed the appropriateness of the standard formula for the purpose of calculating the SCR in its 2021 Own Risk and Solvency Assessment ("ORSA"). The review concluded that the standard formula is appropriate given the risk profile of R&Q Theta. The assessment noted that while there are some risks that are not captured within the standard formula, adequate risk mitigation is in place for these risks. This is a typical approach for addressing risks which are more qualitative in nature, and in my view the standard formula captures R&Q Theta's material quantifiable risks.

R&Q Theta's external Actuarial Function has commented on the company's assessment in its 2021 ORSA Opinion and Actuarial Function Report, and noted that the company had addressed previous recommendations for improvement in the assessment. The Actuarial Function considered the Standard Formula to be appropriate as a basis for capital calculations and scenario analysis.

I have reviewed the standard formula assessment provided by R&Q Theta. I note that:

- Market risk is, by far, the most dominant component of R&Q Theta's SCR. R&Q Theta has no non-standard investments other than its Funds at Lloyd's investment. The FAL investment is treated prudently in R&Q Theta's application of the standard formula as an unrated Type 2 equity investment. In my opinion R&Q Theta's calculation of market risk is appropriate.
- As discussed in section 5.7, given R&Q Theta's high level of reinsurance, the net technical provisions are dominated by the expense provisions, and therefore expense inflation risk needs to be considered as part of underwriting risk.
    - The standard formula reserve risk factors are not necessarily appropriate in this case as they are calibrated to reflect claims volatility rather than expense inflation.
    - However, R&Q Theta's claims volatility is significantly reduced owing to the high levels of reinsurance, and in my opinion, the calculated value for reserve risk is a reasonable proxy for expense inflation risk.
    - Moreover, because of the dominance of market risk, even if there were an understatement of underwriting risk it would not cause a material mis-statement of the overall SCR.

I am satisfied that, allowing for the nature, scale and complexity of the company, and the fact that the company is in run-off, it supports the conclusion that the standard formula is appropriate for R&Q Theta.

R&Q Theta - review of SCR calculation process

I have reviewed R&Q Theta's documentation of its approach to determining the SCR using the standard formula. R&Q Theta's Actuarial Function utilises a proprietary Solvency II Standard Formula model that is widely used in the Irish Market. I have also held discussions with R&Q Theta's Actuarial Function to understand the drivers of the movement in SCR over recent quarters.

Based on my review and discussions I am satisfied that the standard formula SCR for R&Q Theta has been calculated materially correctly.

AIEL - appropriateness of the standard formula

AIEL has reviewed the appropriateness of the standard formula for the purpose of calculating the SCR in its SCR report as at 2021 year-end. The review concluded that the standard formula is appropriate given the risk profile of AIEL, ie where there are limitations, they are not material. There are some risks that AIEL has identified which are not captured within the standard formula. These are Strategic risks and Reputational risks, which AIEL considers to be best managed through internal controls and governance. In my experience, this is a common approach to managing these types of risks.

AIEL has also assessed that the standard formula continues to be appropriate for the liabilities transferring from R&Q Theta following the Proposed Transfer.

I have reviewed the standard formula assessment provided by AIEL and I am satisfied that it supports the conclusion that the standard formula is appropriate for AIEL.

The key limitation to the standard formula identified by AIEL is on non-life underwriting risk. For reserve risk, the standard formula calibrates an average European insurer's reserve deterioration across Solvency II lines of business. However, AIEL's legacy portfolios contain reserves relating to asbestos, UK industrial disease and liability, which tend to have higher degrees of reserve uncertainty. However, these portfolios are considered mature with circa 15% of net reserves relating to these risks. Therefore, the Standard Formula calibration is not considered inappropriate for Reserve Risk capital.

AIEL - review of SCR calculation process

AIEL produces a formal annual report documenting the approach to determining the SCR under the Standard Formula basis. A separate SCR report is produced quarterly highlighting key movements in the SCR and SCR coverage ratio.

AIEL's Actuarial Function utilises a widely used proprietary Solvency II Standard Formula model to calculate its SCR. AIEL follows a robust process for the calculation, review and validation of the SCR which involves the initial calculations being carried out by the Capital Actuary, the Head of Capital reviewing the inputs, results and report produced by the Capital Actuary, followed by a formal review of the report by the executive directors.

My review of the SCR report and conversations with AIEL regarding the process followed in calculating its SCR, provide me with the evidence required to support my conclusion that the standard formula SCR for AIEL has been calculated materially correctly.

6.8. Projected SCR coverage ratios for R&Q Theta and AIEL

Projected SCR coverage ratios immediately before and after the Proposed Transfer

The table below sets out the projected SCR and coverage ratios, as prepared by R&Q Theta and AIEL, immediately before and after the Proposed Transfer.

Projections before and after the Proposed Transfer €m	Own Funds	SCR	Own Funds less SCR	SCR coverage ratio	Movement in coverage ratio
Day 0 – before Transfer					
R&Q Theta	8.3	4.7	3.6	177%	
AIEL	125.7	67.8	57.9	185%	
Day 1 – after-Transfer					
R&Q Theta	n/a	n/a	n/a	n/a	n/a
AIEL	122.6	70.9	51.6	173%	(13%)

Source: R&Q Theta and AIEL

In summary:

- Transferring Policyholders: The SCR coverage ratio for liabilities transferring from R&Q Theta to AIEL is projected to decrease marginally from 177% to 173%. However, AIEL is still projected to be well capitalised (as defined in section 6.1) immediately after the Proposed Transfer.
- Existing AIEL Policyholders: the SCR coverage ratio for Existing AIEL policyholders is projected to decrease from 185% to 173% after the Proposed Transfer. AIEL is well capitalised prior to the Proposed Transfer, with own funds in excess of the SCR of €57.9m. After the Proposed Transfer, the SCR coverage ratio is projected to fall, and the excess own funds over the SCR will decrease from €57.9m to €51.6m.
- The drop in AIEL's projected SCR coverage ratio from Day 0 to Day 1 is largely driven by:
  - A €3.0m increase in market risk due to an increase in spread risk and currency risk due to R&Q Theta's transferring assets; and
  - A €3.2m decrease in eligible own funds following the Proposed Transfer. This explained by (i) AIEL using an alternative higher estimate for the transferring technical provisions and (ii) AIEL treating ring-fenced assets transferred from R&Q Theta as ineligible own funds in AIEL. The restrictions on these transferred assets are expected to be lifted during 2023.

Based on this analysis, both R&Q Theta and AIEL are projected to remain well capitalised both immediately pre- and post- Transfer. Therefore, I do not expect the changes in SCR coverage ratios immediately pre- and post- the Proposed Transfer to lead to any material adverse changes in the strength of capital protection for either group of policyholders.

Projected SCR coverage ratios for a number of years after the Proposed Transfer

AIEL has provided projections for the SCR coverage ratio for a number of years after the Proposed Transfer.

Immediately following the Proposed Transfer, AIEL's SCR coverage ratio is expected to be 173%. The SCR coverage ratio is then projected to reduce marginally to 172% at year-end 2023 and then increase by year-end 2024, reflecting the ongoing run-off of the liabilities. AIEL is expected to be well capitalised (as defined in section 6.1) immediately after the Proposed Transfer and to continue to be well capitalised throughout the remainder of the projection period.

In practice, AIEL's average coverage ratios may be higher or lower than these projections depending on the claims and other experience of AIEL. AIEL will routinely monitor the capital, and projected capital, position in line with its capital management policy (considered in section 6.6 above) – this could also lead to the coverage ratios being higher or lower than projected.

6.9. The planned capital structures for R&Q Theta and AIEL

Own funds items are classified in three tiers, depending on their nature and value. The tiers are subject to quantitative limits. Therefore, not all of the "available" own funds are necessarily "eligible", ie some own fund items may not be counted towards fulfilling the SCR and the MCR.

R&Q Theta

Based on data as at 31 December 2021, R&Q Theta's own funds consist mainly of Tier 1 capital. Therefore, all own funds are eligible, in full, to meet the SCR and all tier 1 capital is eligible to meet the MCR.

AIEL

Based on data as at 31 December 2021, 73% of AIEL's own funds were classified as unrestricted tier 1, ie the highest quality, 21% were classified as tier 2 and 3% of were classified as tier 3. The remainder ie 3% of the total own funds were inadmissible. The proportions of tier 1, tier 2 and tier 3 capital are expected to remain broadly consistent under the capital projections as at 31 December 2022 both immediately before and after the Proposed Transfer.

AIEL's tier 2 capital is fully eligible to cover the SCR and approx. 67% of AIEL's tier 3 capital is eligible to cover the SCR. AIEL's SCR at 31 December 2021 is €53.8m and its tier 1 capital is €84.5m ie AIEL's SCR is fully covered by own funds classified as tier 1.

No material change is planned to AIEL's capital structure post transfer.

The projected capital coverage ratios provided by AIEL, and my overall assessments regarding policyholder security incorporate the impacts of these tiered limits.

6.10. SCR scenario analysis

I have considered the impact of a range of adverse scenarios based on projections prepared by AIEL and R&Q Theta based on their ORSAs. The purpose of such scenario analysis is to assess whether the companies can withstand plausible adverse experience and whether, under these circumstances, they can still provide appropriate security to all policyholders. The scenarios include a "reverse stress test" – reverse stress tests are scenarios that, by design, consider potential events that could lead to insolvency of an insurer.

It is also possible that there could be favourable scenarios, eg a shorter tail of future claims than expected. However, I have not considered such scenarios in detail as these have not been necessary in order to form my opinion regarding the Proposed Transfer.

The following discussion summarises the adverse scenarios that I have considered. These scenarios are intended to represent a range of possible deteriorations that may occur over the ultimate time horizon, including both moderate and extreme scenarios, but don't represent the full range of all possible outcomes. All of the scenarios were reviewed for reasonableness by me, but the calculations have been performed by R&Q Theta and AIEL.

Note that the scenarios for R&Q Theta are from the 2021 ORSAs, so the base SCR coverage ratios are different to the most recent projections, but the scenarios provide a clear indication of the relative impact on the coverage ratios. R&Q Theta have confirmed that the impacts would be similar if they were to be updated to align with the most recent projections.

R&Q Theta – impact of adverse scenarios on SCR coverage ratios

R&Q Theta's ORSA assesses the impact of four adverse scenarios as at 31 December 2021. The projections provided for subsequent year-ends assume that the Proposed Transfer has completed, and that the company has no remaining policyholders. As such, these projections are irrelevant for the purposes of this report.

Projected as at December 2021	SCR coverage ratio	Impact on SCR coverage ratio
Base (from 2021 ORSA)	**153%**	
1. Economic downturn causing a downgrade in credit rating of the largest corporate investment bond holding	152%	(1%)
2. Economic downturn causing a downgrade in credit rating of the Bank of Ireland	139%	(14%)
3. Reserve deteriorations	99%	(54%)
4. Reverse stress test: Failure of R&Q Cayman	72%	(81%)

I consider the scenarios above to be reasonable for the following reasons:

- The scenarios focus on the key risks that drive R&Q Theta's capital position as a company that has entered run-off.
- The focus on investment risks reflects the dominance of market risk in R&Q Theta's SCR.
- Reserve deterioration could occur as an adverse movement on an individual large claim, or as a general deterioration across multiple claims.
- The reverse stress test ie the scenario which causes insolvency focusses on the credit risk associated with the R&Q Theta's reinsurance and is expected to be remote.

These scenarios demonstrate that R&Q Theta remains well capitalised or sufficiently capitalised in the event of the assumed market risks.

In the event of scenarios 3 and 4, where the SCR coverage ratio would breach the 100% threshold in December 2021, the MCR coverage ratio still stays well above 100%. In this situation, the R&Q Theta Board would be required to immediately put a recovery plan in place, which would be likely to involve a combination of withdrawing funds from the FAL investment and accelerating the settlement of any open claims.

AIEL – impact of adverse scenarios on SCR coverage ratios

AIEL's ORSA considers both stresses and scenarios. Stresses are single events that impact one key driver of the business, whereas scenarios are combinations of events that impact the business at the same time or across a time period. By their nature scenarios are more adverse than single event stresses.

In addition to premium volumes, reinsurer default, loan default and investment stresses, AIEL models the five scenarios described below over their planning horizon. I consider these scenarios to provide an appropriate view of plausible, but relatively extreme, outcomes the following reasons:

- The scenarios focus on the key risks that drive AIEL's capital position.
- The reserve and economic stresses are quite severe: the reserve deterioration is calibrated by AIEL as a 1-in-25 year event, and the adverse claims experience is calibrated as a 1-in-15 year event. In addition, these are overlaid by a partial reinsurer default.
- The reverse stress test, ie the scenario which causes insolvency, focusses on the key risks for AIEL and is expected to be remote, with the stresses combined in this scenario representing outcomes comparable to AIEL's SCR, and as such nearly as extreme as a 1-in-200 year event".

These scenarios demonstrate that, except in the reverse stress, AIEL remains sufficiently capitalised pre and post-transfer in the event of a deterioration in AIEL's reserves, investment market shocks and reinsurer default. The reverse stress is by design intended to illustrate the type of scenario that would breach capital requirements.

Projected as at December 2021	Day 0: Pre-Transfer		Day 1: Post-Transfer	
SCR coverage ratio	SCR coverage ratio	Impact on SCR coverage ratio	SCR coverage ratio	Impact on SCR coverage ratio
Base	**185%**		**173%**	
1. Reserve deficiency with adverse claims experience and reinsurance default	131%	(55%)	121%	(52%)
2. Decline in bond valuations and a control failure resulting in a regulatory fine	137%	(48%)	120%	(53%)
3. Reserve deterioration with liquidity constraints and a cyber event	137%	(48%)	126%	(46%)
4. Reserve deficiency with default of largest reinsurer and a cyber-attack.	139%	(47%)	128%	(45%)
5. Reverse stress test: reserve deterioration, reinsurance default, decline in bond portfolio and cyber attack.	93%	(92%)	77%	(95%)

AIEL's capital projections also include capital coverage beyond 2021 out to the end of the planning period at 31 December 2024 for each of these scenarios.

- Other than in the reverse stress test, SCR coverage remains above 100% in all scenarios out to the end of the planning period.
- The projected SCR coverage ratios at 31 December 2024 remain above the Risk Appetite target buffer of 125% except in Scenario 1, where it falls to 117%. AIEL estimates that the stresses combined in this scenario represent an outcome more extreme than a 1-in-100 year event.
- In the event that the Risk Appetite target buffer of 125% was breached, AIEL has identified a number of management actions it would consider taking. These include, but are not limited to, calling in of inter-company loan, securing additional capital support from the wider group and considering external sources of capital or strategic reinsurance protections.

Impact of adverse scenarios on transferring business post transfer

To illustrate the impact of the Transferring business on AIEL's SCR post Transfer, scenario 3 above for R&Q Theta shows the impact of reserve deteriorations. This results in an increase in R&Q Theta's SCR of €1.8m and a reduction in own funds of €0.9m. AIEL's SCR and own funds on Day 1 ie post transfer are €70.9m and €122.6m respectively. Hence the impact of reserve deteriorations on the Transferring business is likely to have an immaterial impact on AIEL post Transfer.

Impact of adverse scenarios relating to R&Q Cayman post transfer

R&Q Cayman is regulated as a Class B insurer by the Cayman Islands Monetary Authority (CIMA). I have been provided with R&Q Cayman balance sheets and income statement as at 31 December 2021. These show that R&Q Cayman comfortably exceeds the Prescribed Capital Requirement (PCR) set by CIMA, with net assets of US$11.9m compared to a PCR of US$3.3m.

However, the PCR requirement in the Cayman Islands is not as stringent as the Solvency II SCR, and R&Q Cayman is an unrated reinsurer. R&Q Theta's reinsurance with R&Q Cayman has been arranged on a funds-withheld basis to manage counterparty default risk in respect of this reinsurance. Following the Proposed Transfer, when this reinsurance is novated to AIEL, it will continue to be on a funds withheld basis, again reducing the impact of default by R&Q Cayman.

R&Q Theta's reverse stress assesses the impact of a failure of R&Q Cayman. I have used the R&Q stress results to understand what the corresponding impact would be on AIEL post-Transfer. There would be two impacts on AIEL if R&Q Cayman were to fail:

- AIEL would retain the full value of the funds-withheld. As these exceed the corresponding reinsurance recoverables, this would increase AIEL's own funds by €2.9m, as at the date of the Proposed Transfer.
- AIEL's SCR would increase because it would no longer have the benefit of the reinsurance. This would amount to €11.7m, assuming the same increase in SCR as modelled by R&Q Theta. Note that this is likely to be a conservative estimate, because AIEL would also benefit from some diversification of risk which is not available to R&Q Theta.

On this conservative basis, AIEL's SCR coverage ratio would change as follows in the event of R&Q Cayman failing:

€m	AIEL Day 1	R&Q Cayman Failure Scenario
SCR	70.9	82.6
Own Funds	122.6	125.4
SCR Coverage Ratio	173%	152%

AIEL's SCR coverage would reduce in this scenario, but AIEL would still continue to be well capitalised after the failure.

6.11. Overall conclusion: Capital considerations

I have set out below my overall conclusions related to capital. These capital considerations should not be considered in isolation. For example, the overall level of protection for policyholders also depends on a range of other considerations. My overall conclusions on the Proposed Transfer are set out in section 10.

Based on the work and rationale described above I have concluded that:

- The projected capital requirements have been calculated materially appropriately for both R&Q Theta and AIEL.
- Following the Proposed Transfer, I do not expect there to be any materially adverse changes in the strength of capital protection for either group of policyholders.

7. Policyholder security

7.1. My considerations relating to policyholder security

As IA, my overall assessments related to policyholder security are:

- whether the likelihood of valid policyholder claims being paid is maintained following the Proposed Transfer for Transferring R&Q Theta Policyholders and Existing AIEL Policyholders.
- whether any change in policyholder security results in policyholders being materially adversely affected by the Proposed Transfer.

To make these assessments, I have considered the following areas:

- The Solvency II balance sheets of R&Q Theta and AIEL (section 7.2)
- The solvency positions of R&Q Theta and AIEL (section 7.3)
- Reinsurance arrangements (section 7.4)
- Access to Insurance Compensation Schemes (section 7.5)
- Access to Insurance Ombudsman Services (section 7.6)
- Insurance regulation (section 7.7)

Further details on each of these considerations are set out below, and my overall conclusion related to policyholder security is set out in section 7.8.

7.2. Impact on the balance sheets of R&Q Theta and AIEL

I have based my analysis on projected balance sheets immediately pre- and post- the Proposed Transfer, on the anticipated Effective Date.

Solvency II balance sheets of R&Q Theta and AIEL

€m	Pre-Transfer		Post-Transfer		Movement due to Proposed Transfer	
	R&Q Theta	AIEL	R&Q Theta	AIEL	R&Q Theta	AIEL
Participations	-	20.4	-	20.4	-	-
Intra-Group loans	-	39.6	-	39.6	-	-
Reinsurance recoverables	23.6	256.8	-	285.3	-	+28.5
Bonds	44.7	206.3	-	239.2	-	+32.9
Other investment assets	4.3	72.1	-	72.4	-	+0.2
Total assets	**72.6**	**595.3**	-	**656.9**	-	**+61.6**
Technical provisions	24.4	395.1	-	426.6	-	+31.6
Other Liabilities	39.9	71.0	-	102.4	-	+31.4
Subordinated debt	-	25.2	-	25.2	-	-
Total liabilities	**64.3**	**491.3**	-	**554.2**	-	**+62.9**
Tier 1 basic own funds	8.3	97.0	-	93.8	-	-3.2
Tier 2 ancillary own funds	-	25.2	-	25.2	-	-
Tier 3 own funds	-	3.6	-	3.6	-	-

€m	Pre-Transfer		Post-Transfer		Movement due to Proposed Transfer	
	R&Q Theta	AIEL	R&Q Theta	AIEL	R&Q Theta	AIEL
Inadmissible own funds		3.4		5.3		+1.9
Total own funds	**8.3**	**129.2**	n/a	**127.9**	n/a	**-1.3**
Total eligible own funds	**8.3**	**125.7**	n/a	**122.6**	n/a	**-3.2**

Source: R&Q Theta, AIEL

The table above shows simplified Solvency II balance sheets for R&Q Theta and AIEL pre- and post- the Proposed Transfer.

All of R&Q Theta's total Solvency II liabilities are expected transfer to AIEL hence there is no Solvency II balance sheet for R&Q Theta following the Proposed Transfer.

Key movements – AIEL

The key movements in the balance sheet for AIEL are as follows:

Net Assets Transferred

- €33.1m increase in investments driven by the bonds expected to be transferred from R&Q Theta to AIEL;
- €31.4m increase in other liabilities as a result of the funds withheld being transferred from R&Q Theta to AIEL.
- Therefore, the net assets transferred from R&Q Theta to AIEL are €1.8m = €33.1 - €31.4m.

Net Technical Provisions Transferred

- €31.6m increase in technical provisions as a result of the R&Q Theta liabilities being transferred into AIEL. This increase is higher than the R&Q Theta's technical provisions Pre-Transfer of €24.4m, because, AIEL have used a higher estimate of technical provisions for R&Q Theta's transferring liabilities than R&Q Theta.
- €28.5m increase in reinsurance recoverables, which is AIEL's best estimate of the amount recoverable under the contract with R&Q Cayman. This is again higher than R&Q Theta's estimate.
- Therefore, AIEL's technical provisions net of reinsurance increase by €3.1m = €31.6 - €28.5m.

Overall AIEL's total own funds are projected to decrease by €1.3m (= €1.8m – €3.1m) following the Proposed Transfer. The net assets transferred by R&Q Theta into AIEL are sufficient to cover the liabilities as valued by R&Q Theta. However, given the higher valuation of R&Q Theta's technical provisions by AIEL, the total capital is expected to decrease slightly.

AIEL's eligible own funds are also projected to decrease following the Proposed Transfer. This is driven by:

- the higher valuation of R&Q Theta's net technical provisions by AIEL; and
- the treatment of the FAL contribution transferred from R&Q Theta to AIEL as an inadmissible asset. AIEL plans to release this investment during 2023, thereby allowing these funds to be reclassified as admissible.

7.3. Impact on the solvency positions of R&Q Theta and AIEL

The projected solvency positions of R&Q Theta and AIEL pre- and post-transfer are summarised in the following table.

Projected solvency positions of R&Q Theta and AIEL immediately before and after the Proposed Transfer

	R&Q Theta	AIEL
Pre-transfer		
Total own funds eligible to meet SCR	8.3	125.7
SCR	4.7	67.8
SCR coverage ratio	**177%**	**185%**
Post-transfer		
Total own funds eligible to meet SCR	n/a	122.6
SCR	n/a	70.9
SCR coverage ratio	n/a	**173%**

R&Q Theta and AIEL are both well capitalised immediately before and after the Proposed Transfer (as described in section 6.8).

7.4. Reinsurance arrangements

As part of the acquisition of EIIDAC in May 2021, and in preparation for the Proposed Transfer, the existing reinsurance arrangements of R&Q Theta were commuted and replaced by a new reinsurance programme with R&Q Cayman.

The new programme is aggregate excess of loss reinsurance. The aggregate attachment point is €3m and the maximum aggregate limit is €55m. The reinsurance has been placed on a funds withheld basis.

I understand that, coinciding with the transfer, the reinsurance treaty will be novated from R&Q Theta to AIEL so that it will remain in place to protect the Transferring Business following the Proposed Transfer.

AIEL has no existing reinsurance placed with R&Q Cayman so the proposed transfer does not increase the concentration risk in AIEL's overall reinsurance programme. Post-novation, the reinsurance with R&Q Cayman will continue to be on a funds withheld basis, which will protect AIEL's policyholders from the counterparty default risk associated with the reinsurance programme.

I am therefore satisfied that neither the Transferring Policyholders nor the Existing AIEL Policyholders will be materially adversely affected by the reinsurance aspects of the transfer.

7.5. Access to Insurance Compensation Schemes

All of the transferring policyholders are located in the EEA or the UK.

EEA Policyholders

In some EEA states, a national insurance compensation scheme may provide compensation to insurance policyholders or claimants in the event of the insolvency of an insurance company. The Irish Insurance Compensation Fund is one such scheme. However, this is not relevant to the non-Irish Transferring Policyholders as it is designed to facilitate compensation only in relation to risks situated in Ireland. Similarly, no relevant scheme, which would cover the type of business being transferred in the Proposed Transfer, exists in Malta.

Therefore, any compensation schemes on which the Transferring Policyholders might rely would be in the countries in which the risks are situated, rather than in the country in which the Insurer is situated (ie Ireland or Malta).

R&Q Theta and AIEL have confirmed that they are not aware of any loss of access to such compensation schemes for Transferring EEA Policyholders as a result of the Proposed Transfer.

UK Policyholders

Separate from the Proposed Transfer, AIEL has established a branch in the UK that is authorised by the PRA to carry on insurance business in the UK in accordance with the UK Temporary Permissions Regimes.

The Financial Services Compensation Scheme (FSCS) in the UK provides consumer protection for policyholders in the UK. This statutory "fund of last resort" compensates customers in the event of the insolvency of a financial services firm.

I understand that, for insurance policies issued by an EEA insurer on or prior to 31 December 2020 (as is the case for all of R&Q Theta's policies) if the policy was FSCS-protected prior to that date it will generally remain FSCS protected after this date as long as the insurer remains a 'relevant person' in the UK. I further understand that AIEL remains a relevant person by virtue of its UK branch.

I have therefore concluded the Transferring Policyholders will not be disadvantaged in terms of access to national insurance compensation schemes.

7.6. Access to the Insurance Ombudsman Services

EEA Policyholders

FIN-NET is a network of national ombudsman services organisations responsible for settling consumers' complaints in the area of financial services out of court. The network covers the countries of the EEA. However, these ombudsman services are applicable only to policyholders who fall within the definition of "consumer" which varies from EEA Member State to Member State. For example, in Ireland, consumers are defined as personal customers and limited companies, charities, clubs, trusts and partnerships with turnover of less than €3m.

All of R&Q Theta's Transferring EEA Policyholders are corporate entities, which do not meet the definition of a consumer under the Financial Services and Pensions Ombudsman Act 2017, as such entities are part of a corporate group that has turnover in excess of €3m. On the basis that the policyholders are corporate entities that are not as a matter of Irish law "consumers", such that the Financial Services and Pensions Ombudsman would not have jurisdiction over the complaint, my understanding is that such ombudsman services are not relevant to my considerations.

UK Policyholders

The Financial Ombudsman Service (FOS) provides private individuals, micro enterprises and small businesses with a free, independent service for resolving disputes with financial companies. For the purposes of the FOS, a micro enterprise is defined as having an annual turnover or balance sheet of less than €2m and fewer than 10 employees, and small businesses are defined to be businesses with less than £6.5m turnover and either fewer than 50 employees or a balance sheet total of less than £5m. It is not necessary for the private individual, micro enterprise or small business 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.

Again, because all of R&Q Theta's Transferring UK Policyholders are corporate entities which do not fall with the scope of the FOS, the services provided by the FOS are not relevant to my considerations.

I have therefore concluded the none of the Transferring Policyholders will be disadvantaged by loss of access to an insurance ombudsman service.

7.7. Insurance regulation

Prudential regulation

Prudential regulation requires financial firms to control risks and hold adequate capital to ensure regulated firms are being run in a safe and sound way. Both Ireland and Malta are currently regulated under Solvency II. Solvency II covers the prudential regulation of insurers, including risk management and capital requirements.

Based on the above considerations, I do not expect Transferring Policyholders to be materially adversely affected by the changes in prudential insurance regulation governing their policies from Ireland to Malta.

Conduct regulation

EEA Policyholders

Conduct regulation of financial firms typically includes consumer protection, market conduct rules and ethical codes of conduct. Within the EEA, conduct is generally regulated by the insurance regulator in the country in which a risk is located and/or the location from which the business is carried out.

The location of risks currently insured by R&Q Theta will not change as a result of the Proposed Transfer. Therefore, the key relevant comparison is between the conduct regulations in Ireland and Malta. If these were materially different, this could potentially affect Transferring Policyholders where the business is currently carried out in Ireland and post-transfer will be carried out in Malta.

There is currently less harmonisation in conduct regulation across the EEA compared to prudential regulation. However, a number of existing EU Directives govern consumer regulation across the EEA, and so apply to both the Ireland and Malta. For example, since October 2018, the Insurance Distribution Directive (IDD) strengthens and consolidates the rules covering the distribution of insurance and reinsurance, and also the administration and performance of an insurance policy once it has been written.

As a result, there is access to similar mechanisms in terms of conduct regulation in Ireland and Malta for the Transferring EEA Policyholders based on EU Directives.

UK Policyholders

In the UK, the Financial Conduct Authority (FCA) is responsible for conduct regulation. The FCA seeks to ensure that consumers are treated fairly in their dealings with insurers. Its rules and guidance include conduct related requirements covering the way in which an insurance firm organises, manages and oversees and governs its business, including codes of conduct, fit and proper requirements and training and competence standards. In addition, conduct regulation covers the full product life cycle, from product design and development, sales and communications with customers, cancellations and claims handling, and complaints handling and compensation.

By virtue of its UK branch, AIEL's UK business will be regulated by the FCA on conduct matters post-transfer, and I would not expect the conduct regulation to change for policyholders due to the Proposed Transfer.

Based on this consideration, I do not expect Transferring UK Policyholders to be adversely affected by the Scheme due to conduct regulation.

Conclusion on regulation

As R&Q Theta and AIEL are subject to the same EU and UK based regulatory regimes, I have concluded that policyholders will not be adversely affected by the Proposed Transfer from a regulatory standpoint.

7.8. Overall conclusion: Policyholder security

Based on the work and rationale described above, I have concluded that it is unlikely that policyholders will be materially adversely affected by the Proposed Transfer.

8. Policyholder communications

8.1. My considerations relating to policyholder communications

I have assessed the appropriateness of R&Q Theta and AIEL's proposed communication strategy to inform policyholders of the Proposed Transfer. The key focus of my assessment was whether the policyholders are to be provided with sufficient and clear enough information so that they can understand how the Proposed Transfer may affect them.

8.2. Overview of communications strategy

R&Q Theta and AIEL have developed a communication strategy to notify affected parties of the Proposed Transfer and allow time for any affected parties to raise objections to the High Court. I have summarised the main points of the communications strategy below:

Publicity

- Notice of the Proposed Transfer will be published in Iris Oifigiúil and such other publications as the Court will direct, and in accordance with the laws of the other EEA Member States in which there are Transferring Policyholders.
- It is also intended to publish the notice of the Proposed Transfer in accordance with the laws of England and Wales, Northern Ireland, and Scotland.
- The Court documents, including this Report, will be displayed at the registered offices of R&Q, Theta DAC and AIEL in accordance with Section 13 (3) (c) of the 1909 Act. I note that all of R&Q Theta's policies were issued in the English language, and it is not proposed to provide translations of this Report.
- R&Q Theta DAC and AIEL will include notices on their website homepages linking directly to dedicated webpages relating to the Proposed Transfer, where a copy of the Scheme will be available to read or download.

Direct policyholder communications

- I understand that there is no legal requirement to write to transferring policyholders of a non-life insurance portfolio transfer and R&Q Theta does not propose to do this, except for its policyholders located in the UK with English law governed policies.
- I understand that, in advance of the Directions hearing, R&Q Theta plans to write those Policyholders with English law governed policies located in the UK outlining details of the proposed Scheme, and seeking their consent to the proposed Portfolio Transfer, and submission to the jurisdiction of the Irish courts in respect of the Transfer.
- It is not proposed to issue individual notifications to AIEL policyholders. I note that there is no requirement for AIEL's policyholders to be advised by individual notifications and also that the impact of the transfer on AIEL policyholders would not be sufficiently material to warrant the expense in doing so.

Given my overall findings regarding policyholder security and service standards, and subject to the agreement of the CBI, MFSA and the Court, I am satisfied with this communication approach.

8.3. Requested waivers

I understand that the communication plan outlined above meets the requirements of Section 13 of the 1909 Act and that no waivers are requested or required.

8.4. Clarity of communication

I have reviewed a draft of the proposed letters to be provided to R&Q Theta's policyholders located in the UK explaining the background to the Proposed Transfer and the transfer process. I have additionally reviewed the notices to be provided to be published.

I am satisfied the communication to policyholders regarding the Proposed Transfer is clear, fair and not misleading.

8.5. Overall conclusion: Policyholder communications

Based on my review of the communication strategy, I have concluded the planned communications strategy will ensure adequate coverage of affected parties.

I have also concluded that the planned communication is sufficiently clear for policyholders to understand the effects of the Proposed Transfer and that R&Q Theta and AIEL have sufficient resources to deal with any objections, enquiries or complaints received following the communication exercise.

Given my overall findings regarding policyholder security and service standards, and subject to the agreement of the CBI, MFSA and the Court, I am satisfied with this communication approach.

9. Customer service and other considerations

9.1. Customer service

I have reviewed the customer service arrangements of R&Q Theta and AIEL and concluded that there will be no material changes to policyholder administration and claims handling, ie the policyholder experience, in respect of:

- Transferring Policyholders; and
- Existing AIEL Policyholders.

Claims handling for R&Q Theta's business is outsourced to Crawfords, a large publicly listed provider of outsourced claims management services. Following the Proposed Transfer, claims handling for the transferring business will continue to be performed by Crawfords on behalf of AIEL. This arrangement provides Transferring policyholders with continuity of service in respect of claims handling.

Any complaints in respect of the services provided by Crawfords will be notified to AIEL instead of R&Q Theta. In both cases, the respective claims policies specify that a complaint should be acknowledged within 5 working days and that a full response must be provided to the complainant within 20 working days. There have been no complaints received to date in respect of Crawfords handling of the claims.

In addition, AIEL has confirmed that there will be no changes to policyholder administration and claims handling for their Existing Policyholders as a result of the Proposed Transfer.

9.2. Tax implications

In relation to the Proposed Transfer, the three types of tax that potentially impact the premium policyholders are charged are:

- Corporation tax: this is levied on profits and policyholders are not directly affected by R&Q Thetas or AIEL's obligation to pay corporate tax.
- Value added tax (VAT): policyholders do not pay VAT on insurance premiums.
- Insurance premium tax (IPT): the applicable IPT rate for each policyholder is determined by the location of the risk insured which will not change. Therefore, the amount of IPT charged will not be affected by the Proposed Transfer.

Therefore, there are no direct tax implications of the Proposed Transfer on Transferring R&Q Theta or existing AIEL policyholders.

9.3. Investment management implications

R&Q Theta and AIEL's investment strategies are recommended by Randall & Quilter Investment Holdings Limited's investment committee with oversight by the boards. The investment committee determines, implements and reviews investment strategies to deliver on the Group's objectives.

- As at 31 December 2021, the majority of R&Q Theta's invested assets were in corporate bonds and government bonds. A small proportion of assets were invested in equities.
- As at 31 December 2021, the majority of AIEL's invested assets were in government bonds and corporate bonds. A small proportion of assets were invested in cash, holdings in other undertakings and property.

The investment strategies of R&Q Theta and AIEL follow the wider strategy of R&Q Group, and both are managed in a similar manner. No changes to AIEL's investment strategies are planned as a result of the Proposed Transfer.

Therefore, I do not anticipate any materially adverse impact for any group of policyholders in terms of investment management as a consequence of the Proposed Transfer.

9.4. Implications for ongoing expense levels

All costs and expenses incurred relating to the Proposed Transfer will be borne by AIEL and will not be borne by policyholders. One-off costs associated with the Proposed Transfer are expected to be modest relative to the combined size of the transferring business and existing portfolio of AIEL.

Therefore, there are no impacts for any group of policyholders as a result of any changes to ongoing expense levels.

9.5. Impact on liquidity position

The liquidity position of a company represents its ability to meet all claim payments and other obligations as and when they fall due. R&Q Theta and AIEL monitor liquidity risk as part of their ORSA processes to ensure that sufficient funds are available to settle claims and expenses as they fall due.

R&Q Theta maintains a large proportion of its assets in liquid asset classes, including government bonds and corporate bonds. As such, R&Q Theta does not expect any material cashflow risk.

AIEL invests mainly in government bonds and corporate bonds which are normally readily convertible into cash. As AIEL writes new business, liquidity is also available from premium income.

Following the Proposed Transfer, AIEL's financial assets will increase by approx. €60m as a result of the assets received from R&Q Theta under the terms of the Proposed Transfer. These assets will continue to be held in highly liquid asset classes, so AIEL does not expect any material cashflow risk.

Therefore, I do not anticipate any materially adverse impacts on the liquidity position for any group of policyholders as a consequence of the Proposed Transfer.

9.6. Impact of other transfers

I am not aware of any significant future transfers into or out of either R&Q Theta or AIEL that will affect any of the Transferring policyholders or the Existing AIEL policyholders.

Any future transfers would need to go through a separate approval process to ensure that policyholders would not be materially adversely affected.

9.7. Set-off

I have considered whether the Proposed Transfer is likely to lead to any changes in the rights of set-off for creditors or debtors of R&Q Theta or AIEL. "Set-off" is a right that allows parties to cancel or offset mutual debts with each other by subtracting one from the other and paying only the balance.

R&Q Theta and AIEL have confirmed that there are no changes in set-off rights as a result of the Proposed Transfer. I have also not identified any material set-off rights as part of my review.

Therefore, considerations around set-off do not impact my conclusions.

9.8. Overall conclusion: Customer service and other considerations

Based on the work and rationale described above, I have concluded that no material impact on service standards (or any other considerations within this section of the report) is expected following the Proposed Transfer.

10. Conclusions and Statement of Truth

10.1. Conclusion

I have considered the Proposed Transfer and its likely effects on the Transferring Policyholders and the Existing AIEL Policyholders.

- In reaching the conclusions set out below, I have applied the principles as set out in relevant professional guidance, being the Actuarial Standards of Practice (ASPs): ASP-PA-2 General Actuarial Practice and ASP-LA-6 Transfer of Long-Term Business of an Authorised Insurance Company and Technical Actuarial Standards (TASs) TAS 100: Principles for Technical Actuarial Work and TAS 200: Insurance.

I have concluded that:

- The security provided to Transferring Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for Transferring Policyholders following the Proposed Transfer.
- The security provided to Existing AIEL Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for Existing AIEL Policyholders following the Proposed Transfer.

10.2. Issues to highlight

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

Specific issues that I have highlighted in this report which require further review include:

- Updated reserves and capital positions.
- Any policyholder objections received.
- Any changes to the detail of the scheme.

I will consider these points further as part of my Supplementary Report.

10.3. IA duty and declaration

My duty to the Court overrides any obligation to those from whom I have received instructions or paid for this Report. I confirm that I have complied with that duty.

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 represent my true and complete professional opinions on the matters to which they refer.

Declan Lavelle

Declan Lavelle
Partner

20 May 2022

Professional standards

Our work in preparing this document complies with the following actuarial professional standards.

Issued by the Society of Actuaries in Ireland: ASP PA-2 General Actuarial Practice and ASP LA-6 Transfer of Long-Term Business of an Authorised Insurance Company.

Issued by the Financial Reporting Council: Technical Actuarial Standard 100: Principles for Technical Actuarial Work, together with Technical Actuarial Standard 200: Insurance.

The use of our work

This work has been produced by Lane Clark & Peacock LLP under the terms of our written agreement with R&Q Theta Designated Activity Company and Accredited Insurance (Europe) Limited ("Our Clients").

This work is only appropriate for the purposes described and should not be used for anything else. It is subject to any stated limitations (e.g. regarding accuracy or completeness). Unless otherwise stated, it is confidential and is for your sole use. You may not provide this work, in whole or in part, to anyone else without first obtaining our permission in writing. We accept no liability to anyone who is not Our Client.

If the purpose of this work is to assist you in supplying information to someone else and you acknowledge our assistance in your communication to that person, please make it clear that we accept no liability towards them.

About Lane Clark & Peacock LLP

Appendix 1 – Glossary

Term	Definition
Actuarial Standard of Practice (ASP)	ASPs are professional actuarial standards issued by the Society of Actuaries in Ireland.
Asbestos Working Party (AWP)	An actuarial working party in the UK that has performed extensive work based on UK market data to estimate the total claims cost of UK asbestos-related claims
Best estimate	An estimate prepared with no margin for either prudence or optimism.
Bornhuetter-Ferguson method	A blend of development factor modelling and the Expected Loss Ratio Method (defined later in this glossary). The weighting given to each is dependent on how developed the claims are for a policy year.
Cede	When a company reinsures its liability with another. The insurance company that purchases reinsurance is the "ceding company" that "cedes" business to the reinsurer.
Cayman Islands Monetary Authority (CIMA)	The regulator of the financial services sector in the Cayman Islands.
Central Bank of Ireland (CBI)	The regulator of the insurance sector in Ireland.
Counterparty default risk	The risk of defaults or downgrades by counterparties that either owe an insurer money or hold money on its behalf. For example, this covers the risk of the failure of a reinsurer or a broker.
Development Factor Modelling	An actuarial method for estimating future claims development using assumptions based on past patterns of claims development. "Development" could mean the reporting of claims, payment of claims or the progression of case reserves.
Effective Date	The date when the Proposed Transfer is expected to occur, which will be shortly after the Sanctions Hearing which is scheduled for 3 October 2022.
European Economic Area (EEA)	The EEA Agreement established the EEA on 1 January 1994. The EEA unites the 27 EU member states with Iceland, Liechtenstein, and Norway into an internal market governed by the same basic rules. These rules aim to enable goods, services, capital, and persons to move freely about the EEA in an open and competitive environment, a concept referred to as the four freedoms.
Events not in data (ENIDs)	An estimate of possible future events or developments that are not reflected in the insurer's historical data. Insurers need to make allowance for ENIDs in their Solvency II technical provisions.
Existing AIEL Policyholders	Policyholders of AIEL at the time of the Proposed Transfer, who will remain with AIEL after the Proposed Transfer.
Expected Loss Ratio method	An actuarial method for estimating future claims development based on combining an exposure measure and an assumed rate per unit of exposure (the "initial expected loss ratio").
Financial Conduct Authority (FCA)	The UK regulatory agency that focuses on the regulation of conduct by retail and wholesale financial services firms. The FCA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
Financial Ombudsman Service (FOS)	Set up by the UK Parliament, the FOS is a free service that settles complaints between consumers and business that provide financial services. Parliament set up the FOS and has legal powers in the UK to address unresolved complaints between a business and a customer relating to financial services.

Term	Definition
Financial Reporting Council (FRC)	The body responsible for setting actuarial standards in the UK. The FRC also regulates auditors and accountants and sets the UK's Corporate Governance and Stewardship Codes.
Financial Services Compensation Scheme (FSCS)	The FSCS is the compensation fund of last resort for customers of UK authorised financial services firms. This covers insurance for individuals and some insurance for small businesses.
Funds withheld	A reinsurance arrangement where assets that would normally be paid over to a reinsurer are withheld by the ceding company to reduce the potential credit risk, or to retain control over investments.
Funds at Lloyd's (FAL)	R&Q Theta and AIEL have both invested some of their Own Funds in an R&Q Group corporate Lloyd's member. Each member of Lloyd's is required to provide capital as security to support their total Lloyd's underwriting business. This is known as Funds at Lloyd's. The level of Funds at Lloyd's determines the amount of insurance business a member can underwrite.
IFRS accounting Standards	International Financial Reporting Standards (IFRS) - these are the accounting standards used to set the booked provisions underlying the published financial accounts of insurers.
Gunnar-Benktander method	An iteration of the Bornhuetter-Ferguson method, which involves a blend of development factor modelling and the Bornhuetter-Ferguson method.
High Court / Court	The High Court of Ireland
Incurred but not enough reported (IBNER)	See definition of IBNR.
Incurred but not reported (IBNR)	The provision for claims that may be reported in the future but relate to events that have already occurred. This also includes provision for possible future development of existing open claims, ie those that have been reported but not fully settled. The provision possible development of open claims is called IBNER (Incurred But Not Enough Reported). Depending on the type of insurance being considered and the claims handling approach, both the IBNR and IBNER can be either positive or negative.
Independent Actuary	A suitably qualified person appointed to produce an independent report, for the Court, on an insurance business transfer scheme, in accordance with Section 13 of the Assurance Companies Act 1909. The Independent Actuary's primary duty lies with the Court, and the opinion of the actuary is independent of those of the sponsoring companies involved in the Transfer and the CBI.
Malta Financial Services Authority (MFSA)	The regulator of the insurance sector in Malta.
Market risk	The risk of changes in an insurer's financial position due to changes in the market value of assets, liabilities and financial instruments. For example, this covers the risk of falls in the value of assets that are being held to make future claims payments.
MCR coverage ratio	The MCR coverage ratio is the ratio of own funds to Required Capital (MCR). This is a measure of the capital strength of the insurer – the higher the ratio, the stronger the insurer.
Minimum Capital Requirement (MCR)	A formulaic calculation of the capital requirement as part of the European Solvency II regulations for insurers. Breaching the MCR defines the point of intensive regulatory intervention. The calibration of the MCR is to be the capital required to give an 85% confidence level of sufficient capital to last one year. The MCR is a simpler calculation than the SCR and is typically a less onerous requirement.
Noise Induced Hearing Loss	Permanent hearing loss that is caused by being around loud noises over a long period of time.

Term	Definition
Novation	A Novation is a commercial agreement between a policyholder and two insurers which cancels a policy from inception with one insurer and replaces it with a new contract with the second insurer.
Occupational disease	A disease contracted primarily as a result of an exposure to risk factors arising from work activity. For example, exposure to asbestos is associated with a number of diseases, including mesothelioma, asbestosis, pleural thickening and various cancers.
Operational risk	The risk of losses caused by failures in an insurer's operational processes, people and systems, or from events that are external to the insurer. For example, this would cover the risk of fraud or IT failure.
Own funds	The capital in excess of provisions available to meet the SCR capital requirements under Solvency II.
Proposed Transfer	The proposed insurance business transfer from R&Q Theta to AIEL under Section 13 of the Assurance Companies Act 1909, Section 36 of the Insurance Act 1989 and Regulation 41 of the European Union (Insurance and Reinsurance) Regulations 2015
Prudential Regulation Authority (PRA)	The part of the Bank of England that carries out the prudential regulation of financial firms in the UK, including banks, investment banks, building societies and insurance companies. The PRA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
Quota share reinsurance	A reinsurance contract in which the insurer and reinsurer share both claims and premiums in the same proportion. The reinsurer usually pays a commission to the insurer to allow for their costs of selling and administering the policy.
Reinsurance	An arrangement with another insurer to share or pass on risks. For example, in the case of the Proposed Transfer, R&Q Theta is transferring underwriting (insurance) risk to R&Q Cayman using an aggregate excess of loss reinsurance arrangement.
Reinsurance bad debt	Reinsurance bad debt is a provision for amounts that are owed by reinsurers but which may not be paid, eg due to the insolvency of the reinsurer.
Required Capital	The amount of capital an insurer must hold in order to meet its regulatory capital requirements (ie the SCR).
Residual Policy	Any Transferring Policy in relation to which any competent regulator has not provided a necessary certificate as to consent (and such consent is not otherwise deemed to have been given) or which the Court for whatever reason determines shall not be transferred by virtue of the Scheme or the Order.
Scheme Document	A document submitted to the High Court setting out details of the Scheme or Proposed Transfer.
Scheme Report	This report prepared by me, as the Independent Actuary, for submission to the High Court.
SCR coverage ratio	The ratio of an insurer's available capital to its Required Capital (SCR). This is a measure of the capital strength of the insurer – the higher the ratio, the stronger the insurer (all else being equal).
Solvency Capital Requirement (SCR)	The amount of capital an insurer is required to hold under Solvency II regulations. This is an estimate of the capital required to cover the loss that an insurer could experience over the next 12 months with a probability of 99.5% (ie, a 1 in 200 event). If an insurer's capital (ie 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 Financial Condition Report (SFCR)	Solvency II requires each insurer to publish an SFCR annually that contains certain qualitative and quantitative information.

Term	Definition
Solvency II	The system for establishing (among other things) minimum capital requirements for EEA insurers under the Solvency II Directive 2009/138/EC.
Standard formula	A prescribed approach under Solvency II for the calculation of capital based on an insurer's financial information (eg premiums and claims provisions).
TAS	The FRC issued Technical Actuarial Standards which apply to all relevant actuarial work produced after 1 July 2017.
Technical provisions	Under Solvency II, the technical provisions cover the ultimate costs of settling all claims arising from events occurring up to the balance sheet date plus the provisions for future claims (and premiums) arising on unexpired periods of risk.
Tier 1/2/3 capital	Under Solvency II, capital is categorised into 3 tiers based on the permanence and loss absorbency of the form of capital. Tier 1 capital is the highest quality.
Transferee	The insurer to which the business is being transferred, Accredited Insurance (Europe) Limited (AIEL).
Transferor	The insurer from which the business is being transferred, R&Q Theta Designated Activity Company (R&Q Theta).
Transferring Policyholders	R&Q Theta policyholders whose policies will be transferred to AIEL as a result of the Proposed Transfer.
Unallocated Loss Adjustment Expenses (ULAE)	Unallocated Loss Adjustment Expenses are expenses relating to the handling of claims that are not allocated to specific claims, eg claim handlers' salaries and office space.
Underwriting risk	The risk that the value of insurance claims proves to be higher than expected.
Unearned Premium Reserve (UPR)	A provision for the unexpired portion of insurance policies. This appears as a liability on the insurer's balance sheet, since the premium would be paid back upon cancellation of the policy.
Vibration White Finger	A long-term condition that can result from prolonged use of vibrating tools, either for occupational or recreational use.

Appendix 2 – Extract from Terms of Reference

Summary of agreed scope of work

I, Declan Lavelle, will act as Independent Actuary ("IA") to support your planned Section 13 transfer from R&Q Theta Designated Activity Company ("R&Q Theta") to Accredited Insurance (Europe) Limited ("AIEL").

Your primary requirement is for the IA to act in line with Section 13 of the Assurance Companies Act 1909.

The key deliverables from the work will be:

- the main IA scheme report prior to the Directions Hearing;
- the supplementary report prior to the Sanctions Hearing; and
- presenting my findings as IA to the Court and responding to any queries and additional Court requests.

Appendix 3 – CV of Declan Lavelle

Declan is a Partner in LCP's Insurance Consulting practice and a Fellow of the Society of Actuaries in Ireland since 1999.

Career history

Declan joined LCP in 2004. He has 18 years' experience as a general insurance actuarial consultant, and a further 14 years' experience working in the insurance industry prior to joining LCP. His clients include insurance companies and public sector bodies, both in Ireland and overseas.

Prior to joining LCP, Declan was Head of Finance and Actuarial for Halifax Insurance Ireland Limited. He was responsible for financial reporting, business planning and managing the actuarial team.

Declan began his career as an actuary with Aviva Insurance, formerly Norwich Union Ireland, where he initially worked in life insurance before transferring to non-life insurance in the mid-1990s.

Section 13 and Part VII transfers

Declan has acted as the Independent Actuary on two previous Section 13 transfers and has been peer reviewer for a UK Part VII Transfer.

Head of Actuarial Function appointments

Declan is an Irish Head of Actuarial Function (HoAF) for two non-life insurance firms. As a HoAF, he advises clients on reserving and technical provisions as well as providing opinions on underwriting, reinsurance and the ORSA process.

He also provides similar services to two regulated insurers in Malta.

Other

Declan is a member of the Council of the Society of Actuaries in Ireland and serves as Vice-President of the Society for the 2021/22 year.

He previously served on Society's General Insurance and Solvency II committees and as the Society's representative on the Actuarial Association of Europe's Insurance Committee.

Appendix 4 – Summary of data provided

The following is a list of the key data items I have requested and received in assessing the Proposed Transfer. All data I have requested has been provided to me.

Data accuracy statement

- R&Q Theta and AIEL have each provided a data accuracy statement confirming that the data provided to me regarding the Proposed Transfer are accurate and complete.
- R&Q Theta and AIEL have read this IA Scheme Report and each has confirmed that it is correct in terms of all factual elements of the Proposed Transfer.

Documents relating to R&Q Theta

- Capital Management Policy (dated 10 January 2022)
- Risk Appetite (dated 17 December 2021)
- Investment policy (dated 7 September 2021)
- Reinsurance contract with R&Q Cayman incepting on 14 May 2021
- Independent auditor's report as at 31 December 2020 (dated 6 April 2021)
- 2020 YE SFCR
- Technical provisions summary as at 30 September 2021
- Actuarial report on technical provisions as at 30 June 2021 (dated August 2021)
- Actuarial report on technical provisions as at 31 December 2021 (dated April 2022)
- 2021 AFR (dated December 2021)
- Expense inflation sensitivity test as at 31 December 2021
- SCR report as at 2021 year-end (dated February 2022)
- SCR report as at 30 June 2021 (dated August 2021)
- SCR report as at 30 September 2021 (dated November 2021)
- 2021 ORSA
- 2021 ORSA Opinion (dated December 2021)
- Projections of future balance sheets and capital requirements at the point of the proposed transfer
- Summary of cash and investments as at 31 December 2021 (dated 14 January 2022)
- R&Q Cayman financial information (dated 31 March 2022)

Documents relating to AIEL

- Claims handling policy (dated 16 September 2019)
- Risk appetite (dated 22 June 2021)
- Reserving process documents for legacy and program business (dated 13 July 2021)
- External review reserve report at 30 September 2020 (dated 21 January 2021)
- Solvency II technical provisions report as at 30 September 2021 (dated October 2021)
- Internal review reserve report at 30 September 2021 (dated 17 November 2021)
- Reserve report at 31 December 2021 (dated 2 March 2022)
- 2021 AFR (dated 15 March 2022)
- 2020 YE SFCR
- SCR report as at 2021 year-end (dated 2 March 2022)

- 2021 ORSA (dated June 2021)
- Projections of future balance sheets and capital requirements at the point of the proposed transfer and over the next two year-ends

Documents relating to the Communications Plan

- Draft communications plan
- Newspaper notice for Iris Oifigiúil
- Policyholder details by country
- Draft letter to policyholder

Documents relating to Court

- Notice of motion
- Affidavit in support of motion for Directions
- Draft petition document
- Draft scheme document

Appendix 5 – Breakdown of R&Q Theta policyholders by country

The table below shows a breakdown by country of all R&Q Policyholders who have held a policy since 2007. All policyholders are GE Group Entities located in EEA countries and the UK.

- There were 772 policyholders originally, of which 140 have been dissolved or merged into other entities.
- 632 active policyholders remain, and of these 632 policyholders, 507 remain in the GE Group and 125 have been sold by the GE Group. There are no remaining active policyholders in Gibraltar.

Country	Entities	Active	Sold	Dissolved or Merged
Austria	9	9	0	0
Belgium	9	8	1	0
Bulgaria	1	1	0	0
Croatia	3	2	0	1
Cyprus	4	2	2	0
Czechia	6	6	0	0
Denmark	10	9	0	1
Estonia	2	2	0	0
Finland	13	11	2	0
France	59	53	5	1
Greece	3	3	0	0
Hungary	7	6	1	0
Ireland	257	52	101	104
Italy	23	22	0	1
Lithuania	3	3	0	0
Luxembourg	8	4	1	3
Malta	1	0	1	0
Netherlands	69	60	5	4
Norway	14	14	0	0
Poland	16	16	0	0
Portugal	6	6	0	0
Romania	6	6	0	0
Slovakia	2	2	0	0
Spain	24	23	0	1
Sweden	23	22	1	0
United Kingdom	192	165	5	22
Gibraltar	2	0	0	2
Total	**772**	**507**	**125**	**140**

Appendix 6 – Mapping to requirements

The table below shows the relevant section references in the Scheme Report where I have addressed each point in the guidance from ASP x.x: Actuarial Standard of Practice LA-6.

Guidance reference	Guidance	Scheme report reference
ASP 4.6(i)	The name of the party which has appointed the Independent Actuary and a statement of who is bearing the costs of that appointment	2.2 (page 7)
ASP 4.6(ii)	A statement of the Independent Actuary's professional qualification	2.2 (page 7) Appendix 3 (page 52)
ASP 4.6(iii)	Whether or not the Independent Actuary has a direct or indirect interest in any of the parties which might be thought to influence the Independent Actuary's independence, and details of any such interest	2.2 (page 7)
ASP 4.6(iv)	The scope of the report	2.3 (page 8) Appendix 2 (page 51)
ASP 4.6(v)	The purpose of the scheme	3.3 (page 12)
ASP 4.6(vi)	A summary of the terms of the scheme insofar as they are relevant to the contents of the Independent Actuary's report	3 (page 11)
ASP 4.6 (vii)	What documents and reports the Independent Actuary has considered in relation to each of the companies involved in the transfer and whether there was any additional information which was requested but not provided	Appendix 4 (page 53)
ASP 4.6 (viii)	The cost and tax consequences of the scheme, insofar as these will affect policyholders' funds	9.2 (page 43) 9.4 (page 43)
ASP 4.6 (ix)	The effect of the scheme on the security of policyholders' contractual benefits	1.3 (page 5) 10 (page 45)
ASP 4.6 (xii)	The likely effects of the scheme on matters such as investment management, fund choice, administration and fund management platforms, use of third-party administrators and custodians, new business strategy, administration, expense levels and assumptions used in the calculation of technical provisions, insofar as they may affect the ability of the companies to meet throughout the lifetime of existing policies the reasonable expectations of the holders of those policies	9 (page 43)
ASP 4.6 (xiv)	Which matters, if any, the Independent Actuary has not taken into account or evaluated in the report that might nevertheless be relevant to policyholders' consideration of the scheme.	1.4 (page 6) 10.2 (page 45)

The Proposed Transfer does not involve any mutual companies or long-term insurance business. As such, ASP 4.6(x), (xi), (xiii), and (xv) do not apply.

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