

MOORE STEPHENS

Scheme report for the transfer of policies pursuant to The Financial Services and Markets Act 2000

From : Atlantic Mutual International Limited

**To : Bothnia International Insurance Company
Limited**

AND

**From : Atlantic Mutual Insurance Company (UK
Branch) of Atlantic Mutual Insurance
Company (in liquidation)**

**To : Bothnia International Insurance Company
Limited**

Report of the Independent Expert

**D James
Fellow of the Institute and Faculty of Actuaries**

Date of report: 16 October 2017

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1. OVERVIEW

Introduction

- 1.1 I, Dewi James have been appointed to act as the Independent Expert (“IE”) for the proposed insurance business transfer scheme which transfers rights and liabilities under policies underwritten or assumed by Atlantic Mutual International Limited (“AMIL”) and Atlantic Mutual Insurance Company - UK Branch (“AMIC-UK”), to Bothnia International Insurance Company Limited (“Bothnia”).
- 1.2 I refer to AMIL and AMIC-UK as “the Transferors”, to Bothnia as “the Transferee” and collectively “the Parties”. AMIL and AMIC-UK are a subsidiary and branch, respectively, of Atlantic Mutual Insurance Company in liquidation (“AMIC-ILQ”). I have referred to AMIC-ILQ, its branches and its subsidiaries collectively as the “Atlantic Group”. Bothnia is a wholly owned subsidiary of Compre Holdings Limited (“CHL”) whose ultimate parent is Cambridge TopCo Limited based in Malta. I have referred to CHL and its subsidiaries as the “Compre Group”. I refer to these proposed insurance business transfers as “the Transfers” or “the Transfer”, the business being transferred as the “Transferring Business” and the policyholders associated with the Transferring Business as the “Transferring Policyholders”.
- 1.3 The Transferors are both protected under a whole account quota share reinsurance provided by Bothnia, the details of which are set out in paragraph 6.6; the Transferors and the Transferee have a close business connection and I have considered the proposed Transfers in a single scheme report.
- 1.4 This is a scheme report as defined in Part VII section 109 of the Financial Services and Markets Act 2000 (“FSMA”) in respect of the Transfers. FSMA requires an application to Court for an order sanctioning an insurance business transfer scheme which must be accompanied by a report on the terms of the transfer. The primary purpose of the report is to assist the Court in assessing the impact of the proposed Transfers on affected parties. The report is also available to all parties affected by the proposed transfer to assist them in understanding the impact of the proposed transfer on their rights and must consider the consequences of the Transfers for all affected parties. The report must be prepared by an independent person having the skills necessary to make the report, who has been approved by the Prudential Regulation Authority (“PRA”) in consultation with the Financial Conduct Authority (“FCA”).
- 1.5 I am a Fellow of the Institute and Faculty of Actuaries with experience in the analysis of technical provisions, premium rating and capital requirement evaluation of non-life insurance businesses. I am satisfied that I am able to act in an independent capacity and the PRA has, in consultation with the FCA, approved my appointment as IE in this case.
- 1.6 The Transferee, Bothnia, is domiciled in Finland and is subject to regulation under the Finnish Financial Supervisory Authority (“FIN-FSA”). In order to ensure that I

have fully addressed aspects of legislation and practice under Finnish regulations with which I am not familiar, I have procured the professional services of a local insurance expert, Mr Matti Ruohonen who has confirmed to me that he has no conflict of interest in giving me technical support where necessary; I am satisfied that his experience and expertise meets my requirements. Mr Ruohonen's CV is included as Appendix 2 to the report.

- 1.7 A consequence of the Transfers is that the Transferring Business will move from entities which are regulated by the PRA and FCA in the UK, to Bothnia, which is regulated by FIN-FSA. I have set out my considerations on this, and other non-financial features in section 8.
- 1.8 In forming my opinion I have considered the following key aspects:
- Bothnia's balance sheet and the level of surplus funds in relation to its insurance liabilities and the required level of regulatory surplus capital (paragraphs 7.28 to 7.43)
 - The reserving standards and procedures relating to the estimation of insurance liabilities in Bothnia (paragraphs 7.12 to 7.26)
 - The whole account reinsurance provided by Bothnia in favour of AMIL and AMIC-UK (paragraphs 6.6 to 6.8)
 - The financial and administrative situation of AMIC-ILQ (paragraphs 5.48 to 5.53)
 - Various non-financial factors relating to the administration of the Transferring Business and other reporting requirements (section 8)
- 1.9 Financial information provided by AMIL and AMIC-UK was in GBP, information from AMIC-ILQ was in USD and information provided by Bothnia was in EUR. The values were converted to GBP using the prevailing exchange rates¹. I have included a schedule of key information used in Appendix 3.
- 1.10 Bothnia is financially neutral with respect to the Transfers in view of the existing whole account reinsurance in favour of the Transferors. I am also satisfied that Bothnia, as a solvent forward-looking business, is likely to provide a better long-term financial and administrative platform for the Transferring Policyholders than either of the Transferors.
- 1.11 This report has been prepared based on financial information at or around 31 December 2016, with updated information being used where appropriate. Bothnia's role within the Compre Group is to provide a platform to consolidate other insurance portfolios in run-off, whether these are existing subsidiaries of the Compre Group or external portfolios. Over the course of the preparation of this report Bothnia has engaged in a series of transactions, the most material of these transactions are:

¹ Key Exchange Rates used, USD:GBP @ 31/12/2016 \$1.23 = £1, EUR:GBP @ 31/12/2016 €1.17 = £1.

- On 12 February 2016 Bothnia assumed the liabilities of the members of the Ridgwell, Fox and Partners Pool (“RFP”) which was managed by Ridgwell, Fox and Partners (Underwriting Management) Limited (“RFPUM”). I discuss the background to this portfolio in paragraphs 5.26 to 5.33. This business is currently the subject of a series of insurance business transfers including a Part VII transfer scheme to Bothnia. The Sanctions Hearing for this transfer is scheduled for 17th November 2017 and I have conferred with the RFP IE in order to ensure that no matters have been brought to the attention of either myself or the IE acting on RFP which affect my consideration with respect to the Transfers.
 - In December 2016 Bothnia merged with another Compre Group company, Stockholm Reinsurance Company (“Stockholm Re”). I describe the background to this transaction in paragraph 5.34.
 - In 2016 Bothnia acquired interests in the underwriting pools managed by RW Gibbon Limited (Underwriting Agencies) and RW Gibbon & Son Ltd (“Gibbon”). These interests consist of the participations within the pools of Swiss Reinsurance Company Ltd. (“Swiss Re”) and AG Belge d’Assurances (“AG”). Further, on 5 July 2017 Bothnia acquired the obligations of AXA Insurance Limited (“AXA”) as a participant in Gibbon. This is discussed in paragraph 5.36.
 - In May 2017 Bothnia entered into a whole account reinsurance designed to provide downside reserve risk protection and to optimise its regulatory capital requirement. The reinsurance is placed with a AA rated EU reinsurer and the reinsurance protection applies retrospectively from 1st January 2017. I refer to this reinsurance in my report as the “Bothnia ADC”² and have explained the structure and effect of the reinsurance in paragraph 5.42.
- 1.12 I have formed my opinion based on Bothnia’s position reflecting all of the above transactions.
- 1.13 On 29 March 2017, in a letter to the President of the European Council, the UK government triggered Article 50 of the Lisbon Treaty and formally started the process by which the UK will leave the EU (“Brexit”). I have considered some of the possible ramifications in paragraph 8.13 and, whilst Brexit introduces wider uncertainties, I do not consider these wider issues to adversely impact the Transferring Policyholders.
- 1.14 I will prepare a supplementary report shortly prior to the Sanction Hearing in order to update the Court on any other material changes in the intervening period which may have influenced my opinion.

² Adverse Development Cover

Declaration by the Independent Expert

- 1.15 In producing this report on the Transfers, I owe a duty to the Court to help the Court on matters within my expertise. This duty overrides any obligation to any person from whom I have received instructions or by whom I am paid. 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.
- 1.16 I confirm that I have read and complied with Part 35 of the Civil Procedure Rules, the accompanying practice direction and the document titled "Guidance for the instruction of experts in civil claims 2014".

Summary of the key aspects of the proposed Transfers and of the conclusions reached

- 1.17 A summary of the key aspects of the Transfers is set out under the following headings:
- Background to the Transferors
 - Background to the Transferee
 - Commercial motivation for the Transfers
 - Transferring Policyholders
 - Transferring Reinsurances
 - Transferring Assets
 - Policyholder safety nets
 - Change of Regulatory Authority
- 1.18 A Summary of Conclusions is also included under the following headings:
- Effect on current policyholders of Bothnia
 - Excluded policyholders
 - Financial effect on Transferring Policyholders and policyholders of AMIC-ILQ
 - Non-financial effect on Transferring Policyholders
 - Effect on transferring reinsurers of the Transferors

Summary of the key aspects of the Transfers

<p>1</p>	<p><u>Background to the Transferors</u></p> <p><u>AMIC-UK</u> is the UK branch of AMIC-ILQ. It underwrote a small portfolio of Marine, Property and Liability business from 1968 until 2001 when it entered run-off (see paragraph 5.2).</p> <p><u>AMIL</u> is a UK based subsidiary of AMIC-ILQ which was established in 2000. It underwrote Property and Liability business for approximately 18 months before closing for new business in July 2003 (see paragraph 5.7).</p> <p>There are no notified outstanding claims to either AMIC-UK or AMIL.</p> <p><u>AMIC-ILQ</u> is the parent company of AMIC-UK and AMIL. The formal liquidation of AMIC-ILQ commenced on 27 April 2011 (see paragraph 5.48).</p> <p>AMIC-ILQ is under the management of the New York Liquidation Bureau (“NYLB”), it is financially impaired and the liabilities of AMIL represent approximately 0.1% of AMIC-ILQ’s claims provisions, AMIC-UK has no claims provisions.</p>
<p>2</p>	<p><u>Background to the Transferee</u></p> <p>Bothnia is a Finnish insurer which was registered to operate in 1993. It is part of the Compre Group (see structure chart in Appendix 4), and its role is to provide a platform to consolidate insurance portfolios in run-off, either from existing Compre Group subsidiaries or from third parties. Its business objective is to manage run-off portfolios at a profit by applying the specialist knowledge and skills of the Compre Group.</p> <p>Bothnia’s balance sheet already reflects the liabilities of the Transferors under a 100% whole account quota share reinsurance which it issued in favour of the Transferors with effect from July 2013.</p> <p>Bothnia is a continuing entity and is fully compliant with the regulatory and capital requirements of Solvency II (see paragraph 4.20). I have set out in paragraph 4.21 the current status of AMIL and AMIC-UK with respect to the requirements of Solvency II.</p>
<p>3</p>	<p><u>Commercial motivation for the Transfers</u></p> <p>The NYLB, AMIC-UK, AMIL and Bothnia are all commercially motivated to effect the Transfers.</p> <ul style="list-style-type: none"> • The Transfers relieve the Transferors of the burden of Solvency II and provide on-going security to the remaining policyholders. • The Transfers will enable the NYLB to take further steps towards completing the liquidation of AMIC-ILQ. • Bothnia is a specialist in the management of portfolios in run-off and considers the Transfers to represent a profitable commercial opportunity. <p>I have expanded on the commercial rationale of the Parties in paragraph 6.2.</p>

4	<p><u>Transferring Policyholders</u></p> <p>Under the Transfers all future insured losses arising from the Transferring Business will belong to Bothnia. The Transferring Policyholders will become policyholders of Bothnia and their rights will be exercisable against Bothnia in substitution for the Transferors.</p> <p>The Transfers anticipate that all policyholder liabilities will be transferred, leaving no policyholder liabilities in the Transferor entities. However, there may be circumstances that arise which preclude certain policyholder liabilities from being transferred when the final Court sanction is made. I consider such circumstances to be highly unlikely, however, if some policyholder liabilities are not transferred, then the objective of the Transferors to wind up AMIC-UK and AMIL will not have been met as intended. In paragraph 6.12 I explain the consequences of either of the Transfers being unsuccessful. If a situation should arise where there is a residual policyholder liability, then it is likely that the whole account quota share would remain in place for a length of time because the quota share agreement does not allow for a cancellation unless all policyholder liabilities are transferred. The only exceptions to this are where both parties agree otherwise or Bothnia suffers an insolvency event. Should a situation arise where certain policyholder liabilities are not transferred, then an alternative means of finality would be pursued, but I am not able to anticipate the actions that the Parties may take beyond those outlined at paragraph 6.12.</p>
5	<p><u>Transferring Reinsurances</u></p> <p>The Transferors have the benefit of reinsurance protections procured while they were active underwriters. Of the reinsurance only those contracts in respect of low-layer property reinsurance of AMIL where AMIC-ILQ was not a named party are subject to the Transfers. Any contracts of reinsurance where AMIC-ILQ was the reinsurer, in whole or in part, or where the reinsurance was shared with AMIC-ILQ are not being transferred (see paragraph 6.3 for further detail).</p> <p>Upon completion of the Transfers the 100% whole account quota share reinsurance of the Transferors by Bothnia will terminate (see paragraph 6.9).</p>
6	<p><u>Transferring Assets</u></p> <p>Under the terms of the 100% whole account quota share reinsurance the reinsurance premium due to Bothnia is held as collateral by AMIL. Upon completion of the Transfers, the funds withheld will be released as cash to Bothnia and no further premium is payable in respect of the Transfers (see paragraph 6.6).</p>
7	<p><u>Policyholder Safety Nets</u></p> <p>Direct policyholders of AMIC-UK and AMIL benefit under the UK Financial Ombudsman Service (“FOS”) and the Financial Services Compensation Scheme (“FSCS”). Following the Transfers there is no change to the protection provided under the FSCS (see paragraph 8.5) and no discernible change to the support provided under FOS (see paragraph 8.6).</p>
8	<p><u>Change of Regulatory Authority</u></p> <p>Following the Transfers the regulatory authority in respect of the Transferring Business will change from the PRA and FCA to the FIN-FSA. A comparative analysis of the objectives of the respective regulatory bodies is set out in paragraph 8.1.</p>

Summary of Conclusions

1	<p><u>Effect on current policyholders of Bothnia</u></p> <p>Bothnia is a well-reserved and Well Capitalised insurance company (see paragraphs 7.31 and 7.36). It currently provides whole account reinsurance to both AMIL and AMIC-UK, and therefore already reflects the insurance liabilities of the Transferors in its risk profile and capital requirements.</p> <p>For all practical purposes therefore, Bothnia’s financial and risk profile already reflects the effect of the Transfers. The associated claims liabilities are expected to be minimal and upon completion of the Transfers, there is no material effect to the current policyholders of Bothnia.</p>
2	<p><u>Excluded policyholders</u></p> <p>Subject to the Court’s approval of the Transfers there will be no remaining policyholders in AMIL or AMIC-UK post-Transfers.</p>
3	<p><u>Financial effect on Transferring Policyholders and policyholders of AMIC-ILQ</u></p> <p>The Transfers are likely to have a beneficial effect on the Transferring Policyholders of both AMIL and AMIC-UK. This is because:</p> <ul style="list-style-type: none"> • The Transferee is a Solvency II compliant, forward-looking business with a long-term business plan which offers improved administrative facilities. This contrasts with the circumstances of the Transferors whose parent, AMIC-ILQ is insolvent and wishes to wind-up their operations as quickly as possible. • AMIC-UK is a branch operation of an insolvent company, AMIC-ILQ. The Transfers will secure the payment of its policyholder liabilities in full and in a timely manner whereas the liquidation proceedings of the parent company may take several years to conclude and are highly unlikely to result in 100% payment of claims given the financial position of the parent (see paragraph 5.53). • AMIL is a solvent subsidiary of an insolvent parent, AMIC-ILQ. The Transfers will confer a degree of certainty with respect to the future payment and handling of any contingent claims that may arise. Also, the Transfers will confer security to the AMIL policyholders as there will be no further risk arising as a result of the liquidation proceedings of AMIC-ILQ. • The Transfers are likely to have a beneficial impact on the estate of AMIC-ILQ since the Transfers facilitate the closure of AMIL and AMIC-UK which will lead to reduced costs and administration. This will enable the NYLB to progress with its closure strategy of AMIC-ILQ. As part of the Transfers AMIC-ILQ will lose the potential benefit of recoveries under the Bothnia whole account reinsurance of AMIC-UK; however, given the scale of any potential AMIC-UK recoveries compared to the balance sheet deficit

	<p>of AMIC-ILQ I consider the benefits resulting from the facilitation of the closure of AMIC-ILQ to outweigh this potential loss.</p> <p>The transferring liabilities in the statutory accounts are small in relation to those of Bothnia, representing approximately 0.4% of the claims provisions net of reinsurance (see paragraph 7.27).</p> <p>As a result of the proposed Transfers there is no material adverse effect to the Transferring Policyholders of AMIL and AMIC-UK and there is no material adverse effect to the policyholders and creditors of AMIC-ILQ.</p>
4	<p><u>Non-financial effect on Transferring Policyholders</u></p> <p>The Transfers will have a positive effect on the affected policyholders with respect to non-financial matters, in particular:</p> <ul style="list-style-type: none"> - The administration of claims and policyholder rights will be the responsibility of Bothnia, which has an appropriate claims management infrastructure and greater resources than that of AMIL and AMIC-UK. - Bothnia has a forward-looking business plan with the objective of assimilating and running-off additional portfolios at a profit as opportunities present themselves, whereas the Transferors are either the subject of liquidation proceedings (AMIC-UK) or a subsidiary of an entity in liquidation (AMIL) - Bothnia is subject to the regulatory jurisdiction of FIN-FSA and is compliant with Solvency II which requires rigorous governance processes and controls over business operations and the maintenance of prescribed levels of regulatory capital. Should the Transfers not take place then the requirement for full regulatory compliance will fall upon the Transferors, whose resources are limited due to AMIC-ILQ's liquidation; the Transfers will therefore ensure that the Transferring Policyholders will benefit under Bothnia's Solvency II compliance regime.
5	<p><u>Effect on transferring reinsurers of the Transferors</u></p> <p>Reinsurers of AMIC-UK and AMIL who are subject to the Transfers are not materially affected since the nature of the claims to which they are exposed is not changed as a consequence of the Transfers.</p> <p>In addition, the administration of the remaining reinsurance programmes is likely to be improved as a result of the more extensive resources which Bothnia and the Compre Group have.</p>

2. SCOPE OF WORK

- 2.1 I, Dewi James have been appointed by CHL to act as IE. CHL is meeting the costs of the IE. Bothnia is a wholly-owned subsidiary of the Compré Group and in Appendix 4 I show a structure chart of entities making up the Compré Group.
- 2.2 I am a Fellow of the Institute and Faculty of Actuaries with experience in the analysis of technical provisions, premium rating and capital requirement evaluation of non-life insurance businesses. I am actively involved in providing consulting advice to a number of insurance entities, some of whom have similar liabilities to those of the Transferors and the Transferee. I have worked as an actuary in the non-life insurance market for over 25 years. My CV is included as Appendix 1.
- 2.3 I am satisfied that I am able to act in an independent capacity as neither I nor my firm has a financial or other connection with any of the Parties.
- 2.4 I have reviewed Mr Ruohonen's credentials and discussed my requirements as IE with him and I am satisfied that he has the necessary technical local knowledge – a copy of Mr Ruohonen's CV is included in Appendix 2. I have explained the requirement for independence and he has confirmed to me that he is not conflicted in his capacity to provide me with supporting, independent advice on Finnish regulation and practice.
- 2.5 I confirm that the PRA, in consultation with the FCA, has approved my appointment as IE in this case.
- 2.6 This report considers the effects of the Transfers on the following:
- Bothnia's existing policyholders
 - Transferring Policyholders of AMIL and AMIC-UK
 - Policyholder liabilities remaining in AMIC-ILQ
 - Reinsurers of AMIL and AMIC-UK
- Upon completion of the Transfers, it is not anticipated that there will be any residual policyholder liabilities in either of AMIL or AMIC-UK.
- 2.7 This report and the work undertaken in its production is not intended to be an audit, or form part of any due diligence and should not be relied upon as such. It has been produced solely for the purpose of enabling me to express my opinion on the impact of the Transfers upon the affected parties.
- 2.8 I am required to comply with relevant professional standards and guidance which are issued by the Financial Reporting Council ("FRC") and adopted by the Institute and Faculty of Actuaries. With effect from 1 July 2017 the framework for Technical Actuarial Standards ("TAS") was modified into a two-tier system. The TASs that are relevant to this report are:
- TAS 100: Principles for Technical Actuarial Work
 - TAS 200: Insurance

My report conforms with the requirements of TAS 100 and TAS 200.

- 2.9 The Institute and Faculty of Actuaries issues Actuarial Professional Standards (“APS”) to which all members must comply. This report has been prepared in accordance with those standards, in particular APS X2: Review of Actuarial Work which sets out the responsibilities in relation to peer review, and APS X3: The Actuary as an Expert in Legal Proceedings which sets out principles to apply when acting as an expert in relation to legal proceedings. Peer review of this report has been carried out by a senior actuary working at Moore Stephens LLP who was suitably independent of the work being carried out.
- 2.10 This report complies with the applicable rules on expert evidence and with the expectations for scheme reports as set out by the PRA, in its April 2015 Statement of Policy (“PS7/15”), and the FCA, in Chapter 18 of the Supervision Manual (“SUP 18”).
- 2.11 I have complied with such standards, subject to the principles of proportionality and I have relied upon the work and information provided to me by the professional staff of the Parties and their advisors to be consistent and accurate. I explained the role of the IE to the senior personnel upon commencement of my work and ensured that the people upon whom I have relied have clearly understood my responsibilities to the Court. I am therefore satisfied that it is reasonable to have relied upon the senior personnel to provide the information which I sought. I have obtained formal confirmation from the senior function holders of the Parties that to the best of their knowledge and belief:
- All factual information concerning the Parties contained in this Report is correct and not misleading; and
 - All matters of judgement which have been expressed by the Parties and their representatives are honestly held and based upon reasonable assumptions
- 2.12 Moore Stephens LLP’s and my responsibilities and liabilities are limited to AMIL, AMIC-UK, AMIC-ILQ, Bothnia, affected parties and the Court and exist only in the context of the use of my report for the purpose set out above. Neither Moore Stephens LLP, nor I, will accept any liability or responsibility in relation to the use of this report for any other purpose. For the avoidance of doubt, the advice that has been provided to me by Mr Ruohonen is under my instruction and solely for the purposes of supplementing the information available to me in producing this report.
- 2.13 The PRA has consulted with the FCA and approved the form of this report.

3. RELIANCE PLACED ON THE DATA PROVIDED AND ON THE JUDGMENT OF OTHERS

- 3.1 I set out in Appendix 3 a schedule of the main items of information I have used in forming my opinion.
- 3.2 I have relied upon the data itemised in Appendix 3 to be accurate. I have applied limited cross checks to certain items in the financial statements provided to me and found the data provided to be consistent with these checks. I have relied in particular upon the audited accounts of Bothnia as at 31 December 2016, the unaudited accounts of AMIL as at 31 December 2016, and the unaudited management accounts of AMIC-UK and AMIC-ILQ as at 31 December 2016. I note that with respect to the audited Bothnia accounts there were no qualifications to the opinions expressed by the auditors. I have compared the various financial statements of AMIL, AMIC-UK and AMIC-ILQ with those of the previous year and, with respect to AMIL and AMIC-UK, discussed with their respective senior function holders the financial movements experienced over the course of 2016 and I was advised that the movements have been minimal. This is consistent with the run-off status of the portfolios. I have also compared the AMIC-ILQ December 2016 position with that of the previous 2 years and based on these various cross checks and confirmations, I am satisfied that to any material degree, the lack of formal audited financial statements does not affect my opinion.
- 3.3 In paragraph 4.10 I have explained the background to Solvency II, which defines the basis for regulatory capital requirements with effect from 1 January 2016. I have relied upon the Compre Group to provide me with financial information presented on the new regulatory accounting basis and the resulting regulatory capital requirement. I have satisfied myself through a series of cross-checks that the information provided accurately reflects the regulatory requirements.
- 3.4 As noted in paragraph 1.6 I have relied upon the expertise of Mr Matti Ruohonen, who is an experienced Finnish insurance professional and actuary, to provide me with the additional knowledge of Finnish insurance law and practice where I required this in order to assist me in forming my opinion. I have also obtained input from Bothnia's legal advisors on a limited number of aspects of local law and practice which Mr Ruohonen also reviewed to ensure a consistency of view on any information provided. I further asked the Parties' UK and Finnish legal advisors to prepare synopses of the legal and regulatory framework in the UK and in Finland (Appendix 7), to enable me to form a comparative view on the impact of the Transfers on the affected parties as a result of the change of domicile of the insurer; I have explained this further in paragraph 8.1. I made clear to all the professional advisors at the outset that my responsibilities are primarily to the High Court of England and Wales and the significance of this role was understood by the various advisors. I am satisfied that the advice that I have received, both in a written form

and verbally, is not subject to any bias and is of a high standard and that it is appropriate for me to have relied on the advice received.

3.5 The senior members of staff upon whom I have relied are highly experienced insurance professionals across a range of disciplines. I explained the role of the IE to the senior personnel upon commencement of my work and ensured that the people upon whom I have relied have clearly understood my responsibilities to the Court. I am therefore satisfied that it is reasonable to have relied upon the senior personnel to provide the information which I sought.

3.6 The senior personnel or function holders of the Parties upon whom I have relied, and who I refer to within my report as “senior function holders” consist of the following individuals:

Compre Group:

- Rhydian Williams – Managing Director – Operations
- Jonathan Lloyd – Formerly Technical Due Diligence manager, now consultant to Compre Group
- Will Bridger – Managing Director – Acquisitions
- Mark Lawson – Group Actuarial Director
- Paul Matson – Chief Financial Officer
- Kari Maki – Managing Director – Bothnia

NYLB:

- Ronald Labenski – Chief Financial Officer
- Ted Coopersmith – Comptroller
- David Axinn – Special Deputy Superintendent of Insurance

Willkie Farr & Gallagher (UK) LLP (“Willkie Farr”)³:

- Nicholas Bugler – UK Partner
- Stephen Murphy – Associate

3.7 I have discussed with the senior function holders of AMIC-UK, AMIL and Compre Group with relevant responsibility, the control processes relating to data quality, reconciliation to financial ledgers, peer review, external review and benchmark testing. I am satisfied that these processes are comprehensive and of a high standard but I have not independently performed a data or process audit.

³ Willkie Farr & Gallagher (UK) LLP is an international law firm which is appointed by the NYLB to advise on English law matters in relation to AMIL and AMIC-UK

4. POLICYHOLDERS CONSIDERED AND KEY EVALUATION CRITERIA

4.1 In this section of the report I have:

- Identified the categories of policyholders that I have considered when forming my opinion
- Explained the criteria that I have considered in forming my opinion
- Summarised the basis of regulatory capital requirements under Solvency II, to which most EU insurers are subject
- Summarised the extent to which the Parties are meeting the new regulatory requirements

Categories of policyholders considered

4.2 In forming my opinion I consider the financial and non-financial implications of the Transfers upon the following categories of policyholder:

- The existing policyholders of Bothnia
- The transferring policyholders of AMIL
- The transferring policyholders of AMIC-UK
- The policyholders of AMIC-ILQ excluding those of AMIC-UK

Following the Transfers it is not anticipated that there will be any remaining policyholder liabilities in either of the Transfers.

4.3 The financial implications are assessed in relation to the security afforded each of the above policyholder categories both pre- and post- Transfers.

4.4 I have also considered the impact of the Transfers on reinsurers of the Transfers whose reinsurance contracts are included in the scope of the Transfers.

The criteria used in my consideration

4.5 I have considered both financial and non-financial aspects of the proposed Transfers. To evaluate the financial impact of the Transfers the criterion that I have focussed on is whether the security of the above categories of policyholder with respect to their ability to recover claims under their policies of insurance is materially adversely affected.

4.6 In forming my opinion on the comparative financial security afforded the affected policyholders pre- and post- Transfers, the measure of financial strength that I have used relates to the level of surplus assets in the respective balance sheets and, for Bothnia, the level of surplus in relation to the regulatory requirement under Solvency

II. The level of surplus assets is the value of assets remaining after meeting all policyholder and other creditor liabilities as measured using the appropriate accounting standard. In considering the level of surplus assets I have reviewed, at a high level, the approach used in estimating the provisions for future claim payments in order to satisfy myself that a reasonable approach is being taken.

- 4.7 In forming my opinion I have considered only the impact of these Transfers on Bothnia's current position. I have not anticipated the potential impact of further future business activities of Bothnia. However in paragraph 7.43 I have considered Bothnia's Own Risk and Solvency Assessment⁴ ("ORSA") Report and the financial objectives stated in relation to future portfolio acquisitions as set out in its ORSA which was first completed for year-end December 2014 and subsequently as at December 2015 and most recently mid-year 2016, submitted to the FIN-FSA in 2017.
- 4.8 I have considered wider aspects of a non-financial nature in section 8, which include, amongst other things:
- Continuity of claims handling post-Transfers
 - The Regulatory framework and the effect of changes as a result of the Transfers
 - Policyholder protection safety nets and claimant protection schemes
- 4.9 I set out in Appendix 3 a schedule of the main items of information that I have used in forming my opinion. As commented in section 3, I have relied on the information provided to me to be accurate and I consider the people, whose opinions I have relied on, to be highly experienced professionals. Given the financial situation of AMIC-ILQ, AMIC-UK and AMIL, I am satisfied that the lack of audited financial statements, as at 31 December 2016, does not affect my opinion.

Regulatory capital - overview

- 4.10 With effect from 1 January 2016 insurance entities falling under EU insurance supervision are subject to a risk-based regulatory capital requirement set out under the Solvency II Directive ("Solvency II"). Solvency II has been adopted in the UK, as applicable to AMIL and AMIC-UK and in Finland as applicable to Bothnia. Therefore, there is broad equivalence with respect to the overarching regulatory capital requirement system applicable to the Parties.
- 4.11 Solvency II is a principles-based regime and is based on three pillars:

⁴ The Own Risk and Solvency Assessment is a set of processes under Solvency II constituting a tool for decision-making and strategic analysis. It aims to assess, in a continuous and prospective way, the overall solvency needs related to the specific risk profile of the insurance company

- Under Pillar I, quantitative requirements define a market consistent framework for valuing the company's assets and liabilities, and determining the Solvency Capital Requirement ("SCR");
 - Under Pillar II, insurers must meet minimum standards for their corporate governance, and also for their risk and capital management. Insurers must regularly complete an ORSA;
 - Under Pillar III, there are explicit requirements governing disclosures to supervisors and policyholders.
- 4.12 A key feature under Solvency II is that both the assets and liabilities are valued on a market consistent basis; this feature is most material in its impact on the valuation of the balance sheet liabilities, or Technical Provisions. Under Solvency II the calculation of Technical Provisions, in respect of claims incurred and losses arising from unexpired exposures, may change substantially when compared to the statutory accounting basis. Since Bothnia deals exclusively in managing portfolios in run-off, it has no Technical Provisions in respect of unexpired risks.
- 4.13 Under Solvency II, Technical Provisions are established on a "best estimate" basis and are discounted to allow for the time-value of money over the projected cash-flow of the provisions. A best estimate basis means that the Technical Provisions should be established without any built-in margins for conservatism.
- 4.14 The Technical Provisions required under Solvency II as relating to general insurance business are:
- The premium provision – the expected present value ("best estimate") of all future cash-flows (claim payments, expenses and future premiums due) relating to future exposures arising from policies that the insurer is obligated to at the valuation date. This is nil for Bothnia, AMIL and AMIC-UK;
 - The claims provision – the expected present value ("best estimate") of all future cash-flows (claim payments, all future expenses of management and future premiums due) relating to claim events prior to the valuation date; and
 - The risk margin – the risk margin is intended to represent a premium that another (re)insurer taking on the liabilities at the valuation date would require over and above the discounted "best estimate". Under Solvency II, the risk margin is calculated using a cost-of-capital approach (presently employing a 6% cost of capital parameter as set out in the Commission Delegated Regulation (EU) 2015/35).
- 4.15 Under Solvency II, the SCR is determined by reference to a Standard Formula ("SF") calculation prescribed pursuant to the Solvency II Directive. Where the SF is not considered to adequately represent the risk profile of the entity, variations are available which are subject to additional validation, related control and governance

processes and are subject to regulatory approval. The regulators⁵, may apply capital add-ons to the SCR in circumstances where the SF is used and is not considered to adequately represent the risk profile of the business. In the circumstances where a company is in run-off and has submitted a plan to its regulator⁵ to de-authorise prior to 1st January 2019, the firm can apply the Transitional Measures available to Firms in Run-Off to avoid the burden of Solvency II rules on regulatory capital.

- 4.16 Bothnia, in common with the majority of firms operating portfolios in run-off, is adopting the SF basis for its SCR and has not had any add-ons applied. AMIL, as a subsidiary, has applied the Transitional Measures available to it in order to avoid the burdens of Solvency II compliance. AMIC-UK, as a third country branch, cannot apply the Transitional Measures available to firms in run-off with respect to relief of the regulatory capital requirement and it is not in compliance with the Solvency II capital requirements. This position is unlikely to change given the inability of AMIC-ILQ to supply additional capital in view of its insolvency (see paragraph 4.21).
- 4.17 The objective of the SCR is to ensure that balance sheet surplus capital is sufficient to sustain the solvency of the entity, over a one-year time frame, with 99.5% likelihood. Solvency II also stipulates a Minimum Capital Requirement (“MCR”). The MCR has been characterised as representing a security level in the region of 85% as opposed to the target operating level under the SCR of at least 99.5%. Under Solvency II, surplus capital over and above the level of technical provisions which is used to meet the SCR and MCR is referred to as “Own Funds”⁶. Should the level of Own Funds fall below the SCR then it is likely that regulatory intervention will be triggered. The degree of intervention would become more severe as the Own Funds approach the MCR, below which an authorisation to carry on business may be withdrawn by the regulator⁵. The MCR is subject to a fixed floor value, the Absolute Minimum Capital Requirement (“AMCR”), which is dependent upon the business classes underwritten.
- 4.18 Under certain circumstances Own Funds may not be available to absorb losses in equal proportion across an entire portfolio due to contractual obligations associated with specific segments of the portfolio. Arrangements of this nature are referred to as Ring Fenced Funds (“RFF”). Under Solvency II, all arrangements of this nature must be identified and the notional SCR for each segment of the portfolio which is subject to a RFF restriction must be calculated separately. The SCR for the entity as a whole is then the SCR for the “non-RFF” segment of the portfolio together with each of the separately calculated SCRs of the RFF segments. Additionally, restrictions apply within the SF calculation whereby any surplus assets over the SCR for the RFF segments of the portfolio must not be included within the Own Funds for the portfolio as a whole, as these assets remain restricted to only meet liabilities

⁵ In the UK the relevant regulator is the PRA

⁶ The principles of the Solvency II balance sheet are summarised in Appendix 8

in respect of the RFF segments they are associated with. In the case of Bothnia, RFF restrictions arise for the following reasons:

- The premium in respect of the whole account quota share issued by Bothnia in favour of the Transferors is retained on a “funds withheld” basis by AMIL. As such the RFF restriction is applied in respect of this segment.
- Similarly, for both RFP and Gibbon, contractual restrictions exist on the extent to which the reinsurance premiums under these transactions may be used by Bothnia to fund claims arising on other segments of its portfolio. These restrictions mean that the RFF principles are also applicable.

In paragraph 7.35 I have shown the level of Bothnia’s Own Funds in relation to the SCR and identified the extent to which the RFF restrictions apply.

- 4.19 The level of available Own Funds relative to the SCR gives a quantitative basis for assessing the degree of policyholder security afforded by the entity’s balance sheet. I have referred to the ratio of Own Funds to the SCR as the “Capital Ratio” and in my evaluation I have used the following terms:

Capital Ratio	Description
100% - 119%	Sufficiently Capitalised
120% - 149%	More than Sufficiently Capitalised
150% - 199%	Well Capitalised
Greater than 200%	Very Well Capitalised

The SF relies on the application of a series of risk loading factors to the different components of the entity’s financial make-up. The calibration of the factors was derived over a number of years from a series of quantitative studies and dry-run exercises amongst EU firms - it is therefore unlikely that the SF will be an ideal representation of the risk profile of every firm. In forming my view of the financial resilience of Bothnia’s balance sheet I have not relied solely upon the SCR as a measure of solvency and I applied stress tests to certain parts of Bothnia’s balance sheet in order to satisfy myself as to its financial resilience. The results of the tests are set out in paragraphs 7.33 and 7.39.

Overview of the Parties' compliance with the Solvency II requirements

4.20 I have confirmed with senior function holders of the Compré Group that Bothnia has complied with all Solvency II requirements as of the date of this report and expects to meet all future requirements. I have also been provided with detailed explanations and examples of the way in which Bothnia calculates its regulatory capital requirement; and I am satisfied that systems are in place to meet any future requirements.

4.21 AMIC-UK and AMIL have taken minimal action towards compliance with Titles I, II and III of the Solvency II Directive. AMIC-UK and AMIL have informed the UK regulator (the PRA) of their status with respect to Solvency II compliance which is summarised below:

- AMIL has applied the Transitional Measures under Title VI of the Solvency II Directive on the basis that all undertakings in the Atlantic Group have ceased to conduct new business and that the Transfers and subsequent de-authorisation of the firm will conclude before 1 January 2019, the final deadline for Transitional Measures under Title VI.
- AMIC-UK, as a third country branch, cannot adopt the Transitional Measures available to EEA firms in run-off. It is subject to Titles I to VI of the Solvency II Directive and it is not currently in compliance with certain aspects of Solvency II. The PRA expects AMIC-UK to meet the requirements of Solvency II. Therefore, AMIC-UK is in breach of certain regulatory obligations through its non-compliance.

Since neither AMIL nor AMIC-UK has any notified policyholder liabilities I have viewed the position pragmatically, namely that if the Transfers are effected, then for both AMIL and AMIC-UK policyholders, any current Solvency II related regulatory breach is inconsequential, since the burden of compliance will fall to Bothnia. If the Transfers are not effected, then any Solvency II regulatory burden will remain with AMIC-UK and AMIL, potentially leading to extensive additional costs which are unlikely to be met due to the impaired financial condition of AMIC-ILQ. I have discussed this further in paragraph 6.15.

4.22 I have expanded on the Parties' Solvency II compliance in paragraph 8.2 specifically and considered in further detail the regulatory framework of Finland and the UK in section 8 generally.

5. BACKGROUND TO THE PARTIES AND THE TRANSFERRING BUSINESS

5.1 In this section I set out a brief background to the entities whose portfolios are affected by the Transfers, i.e.:

- **Atlantic Mutual Insurance Company - UK Branch** (“AMIC-UK”)
- **Atlantic Mutual International Limited** (“AMIL”)
- **Bothnia International Insurance Company Limited** (“Bothnia”)
- **Atlantic Mutual Insurance Company Limited - in liquidation** (“AMIC-ILQ”)

Within the background notes on Bothnia I have separately identified RFP, Stockholm Re, Gibbon and the Bothnia ADC in view of their significance to its financial position.

Atlantic Mutual Insurance Company - UK Branch (AMIC-UK)

5.2 AMIC-UK is the UK branch of AMIC-ILQ with a UK Companies House registered company number FC006292 and UK establishment number: BR012721.

5.3 AMIC-UK was established on 10 July 1968 and underwrote as a participant in the Willis Faber Underwriting Management agency (the “WFUM Pool”). As a member of the WFUM Pool, AMIC-UK underwrote Marine, Property and Liability business.

5.4 The WFUM Pool ceased underwriting in December 1991, and has been through an extensive exercise to achieve finality via a Scheme of Arrangement. The Scheme of Arrangement led to the resolution and termination of the involvement of each of the WFUM Pool members and a Completion Certificate of the Scheme of Arrangement was issued to AMIC-ILQ on 18 July 2013. The Scheme of Arrangement did not encompass UK compulsory lines of business and this means that AMIC-UK remains potentially liable for UK Employers’ Liability (“UK EL”) claims arising from direct contracts of insurance written through the WFUM Pool.

5.5 After exiting the WFUM Pool AMIC-UK underwrote a limited portfolio of business in the UK as part of AMIC-ILQ’s strategy of providing insurance cover to the European subsidiaries of its US corporate clients. The business was written in partnership with Lombard Continental Insurance Company Limited (“Lombard”), which underwrote certain risks proposed by AMIC-ILQ, which were reinsured in full by AMIC-UK under a 100% facultative reinsurance arrangement with Lombard. In addition to the Lombard business, AMIC-UK wrote a limited amount of business in its own right, consisting of 1 excess of loss and 1 proportional reinsurance contract. All of these policies were subject to English governing law and the jurisdiction of the English courts. The last risk on the policy register inceptioned in

November 2001 and any risks that policyholders wished to be renewed were underwritten by AMIL.

- 5.6 There are no notified claims to AMIC-UK and no reinsurance assets recorded on its financial statements, I did not therefore consider it necessary to examine its historical reinsurance arrangements and I have relied on the Compré Group to outline the arrangements to me. I have been informed by the Compré Group that there is no remaining reinsurance in relation to AMIC-UK's exposure to the WFUM Pool business since the WFUM Pool outwards reinsurance was realised under the Scheme of Arrangement. With respect to the other business written by AMIC-UK, I am advised by both the senior staff at the Compré Group and Willkie Farr that AMIC-UK did not have its own reinsurance programme and that reinsurance was arranged by AMIC-ILQ and was shared between AMIC-UK and its parent; I have not obtained details of the reinsurance arrangements of AMIC-UK since I did not consider this relevant to my opinion given that no recoveries are anticipated and none of AMIC-UK's historical reinsurance contracts is subject to the Transfers.

Atlantic Mutual International Limited (AMIL)

- 5.7 AMIL was established as a separately capitalised subsidiary of AMIC-ILQ on 14 March 2000 with Company number 03950815. It received permission to underwrite business with effect from February 2002; the business operated for approximately 18 months, closing for new business in July 2003 as a result of emerging problems with its parent and the company has been in run-off since then.
- 5.8 AMIL underwrote Property and Liability business including Employers' Liability, with the objective of:
- Continuing the operations of AMIC-UK, but underwriting directly rather than as a reinsurance of Lombard
 - Taking up business introduced by AMIC-ILQ both for UK risks and European risks under EEA Freedom of Services rules
 - Accepting business from UK regional brokers with previous connections to AMIC-UK
- 5.9 AMIL's short operating period means that relatively little business was underwritten. Table 1 below shows the total premium volumes written over the 18 month operational period, gross of reinsurance, by line of business.

Table 1 - AMIL premium volumes

<u>Line</u>	<u>Premium (£'000)</u>
Material Damage	558
Terrorism	24
Public Liability	43
Employers Liability	51
Business Interruption	165
Total	841

- 5.10 A total of 81 policies were written by AMIL over its 18 month operational period, 2 of which were in respect of EU risks other than the UK and the remainder are UK risks. There are currently no open claims.
- 5.11 AMIL had an outwards reinsurance program in two major subdivisions, covering property related risks and covering liability related risks. I have been provided with a summary structure chart of the reinsurance programme protecting the insured business for the 2002 year and been informed that the 2003 structure was similar. The reinsurance summary shows that the majority of the reinsurance contracts were either shared with AMIC-ILQ or else AMIC-ILQ was itself the reinsurer. Reinsurance of both the property segment and casualty segment consisted of facultative, quota share and excess of loss treaties. I have included the summary structure chart in Appendix 6.
- 5.12 AMIL's last previously open claim settled in 2009. In April 2013 AMIL was advised of a potential hearing loss claim, however this advice did not materialise as a claim. The Compré Group evaluated the circumstances of this case during its due-diligence prior to Bothnia's provision of the whole account reinsurance, this evaluation indicated that AMIL's liability would not exceed £2,000. I have been provided with summary correspondence relating to this and based on the maturity of the portfolio and the absence of other such claims to date, I consider the potential for future claims to be low and this potential does not represent a material adverse factor in forming my opinion.

Bothnia International Insurance Company Limited (“Bothnia”)

- 5.13 Bothnia was founded and registered to operate under Finnish insurance regulation in September 1993 with Finnish business identification number 0947118-3.
- 5.14 Bothnia was purchased by CHL in 2005 and the acquisition completed in June 2006. Bothnia is a member of the Compré Group and is wholly-owned by CHL (Appendix 4 sets out the corporate structure chart).

- 5.15 The majority shareholder of the Compre Group is CBPE Capital.
- 5.16 Bothnia's ORSA report was prepared in line with Bothnia's business plan and was submitted to the Finnish regulators at year-end 2016. The ORSA report submitted included the impact of Bothnia's recent acquisitions and the Compre Group's senior management team have informed me that the FIN-FSA and the Finnish local actuary are fully apprised of these changes. I have independently contacted the local actuary to confirm this. I have also been told by senior function holders of the Compre Group that, in line with the business plan, there are no proposals to accelerate the release of dividend or capital extraction. The ORSA report did not reflect the Bothnia ADC since this was implemented in May 2017 and applied retrospectively from 1 January 2017; separate meetings were held between Bothnia and the FIN-FSA to explain the operation of the Bothnia ADC.
- 5.17 Bothnia engages Compre Services (Finland) Limited, a Finnish subsidiary of CHL, Compre Services (UK) Limited, a UK based subsidiary of CHL, and other Compre Services companies throughout the EU to administer its portfolio. I have collectively referred to these companies as "Compre Services"⁷.
- 5.18 Bothnia is authorised to underwrite and accept new insurance business; its role within the Compre Group is to provide a platform to consolidate other insurance portfolios in run-off which are existing subsidiaries of the Compre Group, and to accept run-off portfolios of third parties. Its business objective is to manage the run-off portfolios at a profit by applying the specialist knowledge and skills of the Compre Group and to achieve economies of scale and capital efficiencies as a result of consolidation to a single entity.
- 5.19 Since its acquisition by CHL, Bothnia has acquired a number of portfolios, the details of which are summarised below:
- In 2007 two run-off companies, Patria Re and ST International were merged into Bothnia; both were existing subsidiaries of CHL.
 - In 2009 Bothnia acquired a portfolio of insurance business in run off from Tryg Vesta (a Danish insurance company).
 - In 2012 two Norwegian portfolios were acquired; the transaction was completed in 2013. The portfolios were in relation to Sparebank 1 Skadeforsikring AS and Unison Forsikring AS.
 - On 12th February 2016 Bothnia entered into the whole account reinsurance contract of RFP. I have explained this further in paragraph 5.26.
 - In 2016 the Boards of Bothnia and Stockholm Re resolved to merge the companies. Bothnia prepared and filed a merger plan, applications for approval of the merger and board and shareholder resolutions with the

⁷ Appendix 4 shows the entities making up the Compre Group including the various service companies.

Swedish and Finnish regulators and the Trade Registry in Finland. The PRA were also informed of the intention to merge the two companies. All necessary approvals for the merger were received prior to 31 December 2016 and the merger was effective at year-end. I have expanded on this in paragraph 5.34.

- In 2016 Bothnia entered into a whole account reinsurance contract and subsequently a legal agreement with two different members of Gibbon. I have explained this further in paragraph 5.36.

5.20 Bothnia is exposed to a number of different types of claim, as illustrated in Table 2 below; claims in respect of Asbestos, Pollution and Health Hazard losses are collectively referred to as “APH”. The currency of the remaining liabilities is dominated by US Dollars and I have shown the mix of outstanding claims by originating currency in Table 3 - the Tables reflect the composition of Bothnia at year-end 2016, including the impact of all of the recent acquisitions.

5.21 Table 2 summarises the composition of Bothnia’s claims provisions according to the major nature of loss

Table 2 - Claims provisions by nature of loss⁸

Reserve Segment	%
Asbestos	57%
Pollution	11%
Health Hazard	5%
Cat	2%
Other Non-APH	23%
Misc	2%
Total	100%

5.22 Table 3 below shows the currency profile of the claims provisions

Table 3 - Currency profile of claims provisions

Currency	%
USD	74%
EUR	15%
GBP	5%
Other	6%
Total	100%

⁸ Other Non-APH refers to Other Non-Asbestos, Pollution and Health Hazard losses

- 5.23 It is clear from the above that the portfolio has a significant US long tail liability content. I have set out my consideration of the level of reserving in paragraphs 7.12 to 7.23.
- 5.24 In 2017 Bothnia purchased a whole account reinsurance which I have referred to as the Bothnia ADC. This reinsurance is placed with a AA rated EU reinsurer and is designed to provide downside reserve risk protection and to optimise its regulatory capital requirement. I have explained this further in paragraph 5.42.
- 5.25 Since Bothnia is already a whole account quota share reinsurer of the Transferors its balance sheet and risk profile include the liabilities of the Transferors and the proposed Transfers have no impact on the risk profile or composition of the portfolio. There are currently no open claims in either of the Transferors and the demands upon the Compré Group's claims handling capabilities are likely to be minimal. The Transfers therefore have no material effect on the existing policyholders of Bothnia.

Ridgwell, Fox and Partners (RFP)

In paragraphs 5.26 to 5.33 I have explained the background to RFP under the following sub-headings:

- RFP business brief
- RFP underwriting pool membership and shares
- QBE's efforts to terminate its participation in RFP
- Wider scope of the RFP pool members to terminate their participation in RFP
- Transfer of the administration from RFPUM to the Compré Group

RFP business brief

- 5.26 RFPUM, on behalf of RFP, underwrote between 1978 and 1991. The portfolio consisted of a worldwide portfolio of excess of loss reinsurance contracts including London Market business and has been in run-off for 26 years. The remaining liabilities of the portfolio consist of claims arising as a result of US Asbestos (34%), Other Non-APH (50%) and Other classes (16%) and the currency of the remaining liabilities is predominantly USD (66%). The overall profile of the business and the nature of the majority of the remaining liabilities has similarities with the existing Bothnia portfolio.

RFP underwriting pool membership and shares

- 5.27 The composition of the underwriting membership is summarised in Table 4 below.

Table 4⁹ - Underwriting member composition of RFP

<u>Entity</u>	<u>% Share</u>
QBE	41%
NZ Re	23%
Moorgate	12%
QBE total	77%
HIR	5%
Wuerttembergische	5%
Allianz	13%
Total	100%

5.28 QBE Insurance (Europe) Limited (“QBE”) participated in RFP and became the dominant participant in the remaining pool liabilities as a result of:

- The acquisition of businesses who had a participation in the pool - in the case of Allstate Reinsurance Company Limited (“ARCO”),
- A Reinsurance to Close of a former participant in the pool - in the case of Gothaer Versicherungsbank (“Gothaer”)¹⁰,
- Through QBE providing a 100% reinsurance to other pool members - in the case of Moorgate Insurance Limited, New Zealand Reinsurance Company UK and New Zealand Insurance Plc

Following the steps undertaken by QBE to consolidate the pool liabilities, QBE represents 76.7% of the remaining share of the pool.

5.29 Moorgate and HIR are wholly owned subsidiaries of the Compre Group.

QBE’s efforts to terminate its participation in RFP

5.30 In 2014 QBE invited run-off specialists to tender for the provision of an exit solution from its obligations as a participant of the pool. The Compre Group carried out a due diligence investigation and Bothnia offered terms for a whole account quota share reinsurance. The terms of the quota share were determined at an aggregate level applicable to RFP as a whole. Individual RFP participants were offered cover on a proportionate basis according to their share in RFP. The reinsurance premium payable by any RFP participant is held as a segregated (or

⁹New Zealand Reinsurance Company (“NZ Re”), Moorgate Insurance Company Limited (“Moorgate”), Hamburger Internationale Rückversicherung AG (“HIR”), Wuerttembergische Feuer (“Wuerttembergische”), Allianz IARD (“Allianz”). The QBE total is subject to rounding error at 1 decimal point.

¹⁰ Gothaer was an RFP member until 1986. Its share was Reinsured to Close by all active members of RFP including QBE

“Ring Fenced”) account; Bothnia and the RFP participant are joint signatories to this account in order to ensure that the reinsurance premium is used only to meet claims under the reinsurance contract. It is the intention that Bothnia’s obligations under the whole account reinsurance will ultimately be subject to an insurance business transfer scheme under FSMA and, if successful, then the whole account quota share reinsurances will be cancelled and the segregation of funds will no longer be applied.

Wider scope of the RFP pool members to terminate their participation in RFP

- 5.31 QBE was the first RFP member to formally accept the terms of the quota share and the transaction was effected on 12 February 2016. The Compré Group have confirmed to me that HIR, Wuerttembergische and Allianz have since accepted the terms¹¹.
- 5.32 HIR and Wuerttembergische are domiciled in Germany where their RFP shares were the subject of European business transfers which were approved by the German Federal Financial Supervisory Authority (“BaFin”) on 7 November 2016 and 28 December 2016 respectively. The Allianz share of RFP is undergoing a European business transfer which is subject to approval by the French regulator, the Autorité de Contrôle Prudential et de Résolution (“ACPR”).

Transfer of the administration from RFPUM to the Compré Group

- 5.33 RFPUM, as pool manager, delegated the pool administration to Aureus Asset Management Limited (“Aureus”). With effect from 1 March 2016, following the implementation of the QBE quota share reinsurance, RFP cancelled its contract with Aureus and has novated all contractual responsibilities, previously held between RFPUM and each of the pool members, to Bothnia who have engaged Compré Services to manage the pool.

Stockholm Re

- 5.34 In 2016 Bothnia and Stockholm Re, a fellow subsidiary in the Compré Group, agreed to merge. The Boards of Bothnia and Stockholm Re determined that the combined entity achieved efficiency gains through risk diversification resulting in an improved Solvency II Capital level on a combined basis. This merger was completed for year-end 2016.
- 5.35 The Stockholm Re portfolio has a similar mix of liabilities to the original Bothnia portfolio; additionally, both of these portfolios, as members of the Compré Group,

¹¹ Gothaer and NZ Re have not agreed to transfer their gross liabilities to Bothnia but they are currently 100% reinsured by the other members of RFP and these reinsurances will transfer to Bothnia.

have been managed consistently and have been subject to the same administration and claims handling processes.

The Gibbon Pools

In paragraphs 5.36 to 5.41 I have explained the background to Gibbon under the following sub-headings:

- Gibbon business brief
- Bothnia's participation in Gibbon
- Administration of the liabilities

Gibbon business brief

- 5.36 The Gibbon Underwriting Pools is business written by RW Gibbon (Underwriting Agencies) Limited and RW Gibbon & Son Limited between 1950 and 1972. The remaining Gibbon liabilities consist primarily of direct and inwards reinsurance APH liabilities. The overall profile of the business and the nature of the majority of the remaining liabilities are largely similar to the existing Bothnia portfolio.

Bothnia's participation in Gibbon

- 5.37 Bothnia is exposed to Gibbon as a result of three transactions involving original members of Gibbon; AG, Swiss Re and AXA.
- 5.38 Bothnia's first participation in Gibbon was via a whole account reinsurance of AG's participation in Gibbon. This reinsurance is on a Funds Withheld arrangement and it is anticipated that the liabilities will subsequently be transferred via an EU Business Transfer Process from Belgium to Finland. AG's motivation for this transfer is to facilitate the closure of their UK branch.
- 5.39 As a result of this transaction with AG, Bothnia was able to enter into a legal agreement (a "discharge and release agreement") with Swiss Re to allow Bothnia to assume the obligations of Swiss Re's participation in Gibbon. The effecting of the discharge and release agreement relied upon Bothnia already being a de-facto participant in Gibbon following the signing of the AG transaction. Swiss Re's motivation for this is to terminate their participation in Gibbon.
- 5.40 The transaction in respect of AXA was agreed on 5 July 2017. The liabilities in respect of AXA's participation in Gibbon are in the region of £50k, in view of this small amount, I have not specifically adjusted my quantitative evaluation for the purposes of this report and I will address the effect of the AXA transaction fully in my supplementary report.

Administration of the liabilities

- 5.41 PRO Insurance Solutions Limited (“PRO”) currently manage Gibbon on behalf of all Pool members. Once acquired, Bothnia envisage management will stay with PRO at least for the short to medium term.

Bothnia ADC

- 5.42 In May 2017 Bothnia entered into a whole account reinsurance contract designed to provide downside reserve risk protection and to optimise its regulatory capital requirement as prescribed under the SF. The reinsurance operates at a whole account level responding to claims in aggregate. The detailed terms of the Bothnia ADC are considered, by Bothnia, to be commercially sensitive and I am therefore not able to provide a complete description of the reinsurance structure in my report. I have confirmed with the Group Actuarial Director that the Bothnia ADC covers potential claims in respect of the Transferring Business both pre- and post-Transfers.
- 5.43 The reinsurer is a highly rated (Standard & Poors AA Rated) EU reinsurance company and the contract applied retrospectively with effect from 1 January 2017. Bothnia discussed the purpose and operation of the reinsurance with FIN-FSA prior to entering into the contract.
- 5.44 In outline, the Bothnia ADC has two sections of cover, which are referred to as in-the-money (“ITM”) and out-of-the-money (“OTM”) sections. The ITM section of the reinsurance pays claims excess of an attachment point up to the level of the undiscounted Best Estimate claims provision – this leads to a reduction in the SF SCR. The OTM section provides additional cover which, together with the newly calculated SF SCR, provides equivalent cover to the SF SCR prior to the application of the Bothnia ADC. The premium for the ITM section is retained by Bothnia on a funds withheld (RFF) basis while the premium for the OTM section is paid annually and is not maintained on a funds withheld basis.
- 5.45 I am familiar with this form of reinsurance from my wider experience in the market. I have been informed by the Group Actuarial Director that the calculation of the claims provisions to be recovered under the ADC is performed each quarter in line with the terms and conditions of the reinsurance agreement. The results of the calculation are included in the Group Actuarial Director's quarterly reserving report which is reviewed by the Bothnia Board.
- 5.46 I have received an explanation of the governance process around the Bothnia ADC from the Group Actuarial Director and am satisfied that these processes are appropriate.
- 5.47 Since the reinsurance structure is relatively new I have carried out my evaluation of the financial security of Bothnia both including and excluding the impact of the

ADC so that its effect on the level of regulatory capital is clearly identified. This is shown in paragraph 7.35.

Atlantic Mutual Insurance Company – in liquidation (“AMIC-ILQ”)

- 5.48 AMIC-ILQ is a long-established New York mutual insurance company which commenced business on 1 July 1842.
- 5.49 Over the years AMIC-ILQ wrote commercial and general liability insurance, including workers’ compensation, surety, auto, property damage, aviation, long-tail liability lines (giving rise to asbestos, environmental and product liability claims), and maritime coverage. AMIC-ILQ wrote in every US state, Puerto Rico, the District of Columbia, Canada, and the United Kingdom through its branch, AMIC-UK.
- 5.50 On 16 September 2010 AMIC-ILQ was placed in rehabilitation, and a formal liquidation commenced on 27 April 2011 in New York. AMIC-ILQ is under the management of the New York Liquidation Bureau (“NYLB”) who is engaged in a programme to crystallise the remaining assets of the company and to settle policy holder and creditor claims as quickly as possible. Under the terms of the liquidation, a US Court sanctioned bar date on the presentation of new claims was set for 15 December 2013 with a limitation for further movement on claims of 16 January 2015. I have been informed by Willkie Farr that this limitation has been followed.
- 5.51 The portfolio contains a large number of workers’ compensation claims and other complex long-tail claims, and the NYLB has advised that the AMIC-ILQ estate will not be in a position to close in the near term. The NYLB has advised me that the potential level of settlement of policyholder and other creditors’ claims cannot currently be determined since the final level of pay-out is subject to its completing further stages of the closure strategy under the terms of the liquidation.
- 5.52 In Table 5 below I have shown the summary balance sheet for AMIC-ILQ for the last 3 calendar year ends. The financial information as at 31 December 2016 has been provided by the NYLB prior to audit final sign-off but I am advised by NYLB that the overall position is representative of the portfolio and is unlikely to change. I have verified that the December 2016 values are consistent with the previous 2 years’ balance sheets and I am therefore satisfied that the information gives a fair representation of the level of balance sheet surplus

Table 5 - Summary balance sheet for AMIC-ILQ

£ 000's	<u>Dec-14</u>	<u>Dec-15</u>	<u>Dec-16</u>
Assets			
Cash and investments	52,034	52,312	59,276
Deposits with credit institutions	30,880	32,789	30,534
Total Assets	82,914	85,101	89,810
Liabilities			
Shareholder surplus	-216,701	-249,725	-300,131
Provision for outstanding claims	189,612	192,514	218,404
Other creditors	110,003	142,312	171,537
Total Liabilities	82,914	85,101	89,810
Total creditor Deficit %	72.3%	74.6%	77.0%

5.53 AMIC-ILQ is financially impaired. I have not examined the priority ranking of other creditors relative to policyholders, but based on the above, if the provision for outstanding claims ranks ahead of all other creditors, then a recovery level in the region of 41% is indicated and if all creditors rank equally then a recovery level in the region of 23% is indicated, based on the December 2016 position. The liabilities of AMIL represent approximately 0.1% of AMIC-ILQ's claims provisions whilst AMIC-UK has no claims provisions. On the basis of the relative scale of AMIC-UK and AMIL to AMIC-ILQ I have not examined the financial condition of AMIC-ILQ further as I did not consider this necessary in forming my opinion.

6. SUMMARY OF THE TRANSFERS

- 6.1 The purpose of the proposed Transfers is to transfer all future income and outgoings arising from the Transferring Business to Bothnia. Liability under the policies issued by the Transferors will be transferred to Bothnia. The Transferring Policyholders will become policyholders of Bothnia and their rights will be exercisable against Bothnia in substitution for the Transferors.

Commercial motivation

- 6.2 All of the affected parties are commercially motivated to effect the Transfers:
- AMIL and AMIC-UK have both been in run-off for a number of years, and neither has any remaining outstanding notified claims. Competitive tenders were invited in 2012 to offer closure solutions for AMIL and AMIC-UK. A number of tender offers were submitted and the terms offered by Bothnia were preferred. Their commercial motivation is that the Transfers will relieve them of the burden of on-going management expenses and Solvency II compliance. If AMIL and AMIC-UK do not wind-up then they will bear the administrative, regulatory capital and reporting requirements as may be applicable under Solvency II. Additionally, the Transfers ensure that any contingent obligations to existing policyholders will be met in full by Bothnia by transferring the liability for these obligations to Bothnia.
 - Bothnia and CHL are specialists in the assimilation and management of portfolios in run-off. The detailed due diligence which was carried out satisfied Bothnia and CHL that the terms of the Transfers represent a profitable commercial opportunity.
 - The NYLB administers AMIC-ILQ and is commercially motivated to effect the Transfers as they will enable the winding-up of AMIL and the closure of the AMIC-UK branch which together represent further steps towards completing the liquidation of AMIC-ILQ.

Transfer of reinsurance assets

- 6.3 The Parties have agreed that the terms of the Transfers are such that certain elements of the original reinsurance protections which AMIL and AMIC-UK procured as active underwriters are not to be transferred. The premium payable under the Bothnia 100% whole account quota share anticipates this condition. The original reinsurances which are not being transferred consist of:
- Contracts of reinsurance where AMIC-ILQ is the reinsurer
 - Contracts of reinsurance which are shared by AMIC-UK or AMIL with AMIC-ILQ and other entities in the Atlantic group of companies

6.4 I have been advised by the Compré Group's due diligence team that all of AMIC-UK's original reinsurance and all of AMIL's liability and high level property reinsurance included AMIC-ILQ as a party. This means that the only original contracts of reinsurance which are being transferred are those in respect of low-layer property reinsurance of AMIL where AMIC-ILQ was not a named party. Appendix 6 summarises the structure of the reinsurance programme.

6.5 The rationale that the Parties adopted in electing to transfer a limited segment of the original reinsurance is that:

For those original contracts where AMIC-ILQ is the reinsurer:

- AMIC-ILQ is financially impaired and in liquidation
- The solvency level is estimated in paragraph 5.53 and since any claims made by AMIC-UK or AMIL would be treated as reinsurance creditors, such claims would rank behind direct policyholders of AMIC-ILQ. This would diminish the recovery rate significantly.
- Under the terms of the liquidation a claims bar date was established, after which no new claims were admitted. Neither AMIC-UK nor AMIL have submitted claims to AMIC-ILQ as a reinsurer

Based on the above, I am satisfied that there is no discernible value associated with these non-transferring original reinsurance contracts.

For those original reinsurance contracts shared in some way by AMIC-UK or AMIL with AMIC-ILQ and other entities in the Atlantic Group:

- NYLB have stated that, administratively, it would not be possible to assign the benefit of the original reinsurance contracts.
- Any recoveries by AMIC-UK would fall to the estate of AMIC-ILQ and be allocated to the entirety of AMIC-ILQ's creditors, with certain creditors being given priority¹². Given the relative scale of AMIC-UK to AMIC-ILQ, in the remote event of a recovery being made any benefit would therefore be likely to be of negligible value to AMIC-UK.
- With respect to recoveries that would in theory be the property of AMIL and not form part of the wider estate of AMIC-ILQ for distribution amongst creditors, I have considered the exposure profile of AMIL and the likelihood of future claims and the actions which NYLB is likely to have undertaken to commute its remaining reinsurance assets.
 - In paragraphs 7.9 to 7.11 I explain that AMIL has no notified outstanding claims. Also, based on my examination of the limited number of issued policies, the fact that AMIL only traded for

¹² See paragraph 8.11 for a high level view of creditor priority under the various regimes.

approximately 18 months (paragraph 5.7) having very limited exposure to the longer-tailed liability classes I have concluded that the possibility of future claims to AMIL is negligible.

- In the remote possibility of AMIL receiving a claim, other conditions must be met in order to effect a reinsurance recovery, for example:
 - The claim must firstly be covered under the contract
 - The reinsurer involved must be solvent
 - The original reinsurance programme should not be compromised as a result of the liquidation process or NYLB having pro-actively commuted such reinsurance
 - The claim would have to breach the reinsurance deductible. The property reinsurance which was shared with AMIC-ILQ had a deductible of \$2.5 million and the liability reinsurance had a deductible of \$10 million. I consider the likelihood of a claim of this magnitude to be extremely remote.

I have considered these factors and I am satisfied that there is no discernible value associated with these non-transferring original reinsurance contracts.

The whole account quota share reinsurance

6.6 The whole account quota share provided by Bothnia in favour of AMIL and AMIC-UK operates as follows:

- Collateral of £1.6 million, representing the premium in respect of the whole account quota share reinsurance, is retained by AMIL in AMIL's bank account (the "Collateral Account") and is used to fund AMIL claims as they arise – a "funds withheld" arrangement.
- The obligation on AMIL to transfer the premium¹³ on the effective date of the Transfers is secured by a fixed and floating charge (the "Charge") over the Collateral Account. The charge was created by a Deed of Charge dated 28 July 2015 between AMIL as chargor and Bothnia as beneficiary (the "Deed of Charge"). The Deed of Charge restricts withdrawals from the Collateral Account for specified purposes, thereby providing Bothnia with security for the payment obligation of AMIL when the Transfers take effect. Specifically, the Deed of Charge requires that any decisions by AMIL to make withdrawals from the Collateral Account require Bothnia's consent, except where such withdrawals are for any of the following purposes:

¹³ Adjusted for claim payments, interest paid on the Collateral Account balance and bank charges associated with maintaining the Collateral Account

- To pay the premium monies to Bothnia when the AMIL transfer takes effect pursuant to an order of the Court;
 - To pay bank charges associated with the Collateral Account; and
 - To pay claims arising out of AMIL's policies, provided the process set out in the whole account quota share reinsurance agreement is followed (which involves consultation with Bothnia).
- Claims arising on the AMIC-UK portfolio which fall under the whole account quota share are recovered directly from Bothnia and are not drawn-down against the collateral fund.

The whole account contract replicates the economic effect on Bothnia of the Transfer being effected. The whole account quota share reinsurance applies to the claims liabilities of AMIL and AMIC-UK after taking credit for the remaining reinsurance protecting AMIL and AMIC-UK. As noted in paragraph 6.3 certain elements of the inuring reinsurance programmes of AMIL and AMIC-UK will not be transferred, this means that the benefit of the existing reinsurances is lower following the Transfers. I have noted in paragraphs 7.7, 7.8 and 7.11 that the likelihood of future claims is low and should a claim occur, there is a high likelihood that the reinsurance contracts which are not being transferred would, in any event, not respond. The theoretical loss in the value of the inuring reinsurance following the Transfer does not therefore affect my opinion.

- 6.7 The separate operation of the whole account quota share as between AMIL and AMIC-UK reflects the financial status of each of the Transferors and separates the reinsurance asset of the solvent subsidiary from that of the branch. The assets of the branch will ultimately fall to the estate of AMIC-ILQ and be apportioned across its entire set of creditors; this includes claims by AMIC-UK under the current whole account quota share arrangement. The effect of the separate operation is to confine any recovery against the collateral deposit held within the subsidiary so that it belongs exclusively to AMIL.
- 6.8 After the effective date of the Transfers the whole account reinsurance will be cancelled and the charge over the Collateral Account will be released. Further consideration of the implications of this are set out in paragraph 6.9.

Considerations following the Transfers

- 6.9 Upon completion of the proposed Transfers, the balance of the £1.6m collateral will revert as cash to Bothnia and the whole account quota share reinsurance will terminate. Therefore following the Transfers, there will be no possibility of the Bothnia whole account quota share benefitting the wider estate of AMIC-ILQ as a result of claims made by AMIC-UK. In sections 7.8 and 7.11 I explain that there is a very low likelihood of material future claims in either AMIL or AMIC-UK. Based on

this evaluation the value of potential recoveries under the AMIC-UK section of the whole account reinsurance and its impact on the wider estate of AMIC-ILQ is negligible. I have concluded that in view of the low likelihood and low value of any recovery and the administrative saving achieved through the Transfers, the effect of this theoretical loss of asset to the wider estate of AMIC-ILQ is outweighed by the resulting benefits and consequently I do not consider that creditors of the AMIC-ILQ estate are adversely affected and this does not affect my overall opinion.

- 6.10 I have set out in paragraph 8.11 a short analysis of the priority of insurance creditors in the event of insolvency in the UK compared with Finland. Should Bothnia become insolvent then, prior to the Transfers, Bothnia's direct policyholders rank above the policyholders of AMIC-UK and AMIL. Following the Transfers, the direct policyholders of AMIL and AMIC-UK become direct policyholders of Bothnia and will rank equally with the existing direct policyholders of Bothnia. These policyholders will rank above the existing reinsurance policyholders of Bothnia and the reinsurance policyholders of AMIL and AMIC-UK, who will become reinsurance policyholders of Bothnia. Following the Transfers, Bothnia's existing reinsurance policyholders experience a marginal worsening in the creditor priority order in the event of insolvency. I do not consider this to be a material disadvantage since the potential claims in respect of AMIC-UK and AMIL are not anticipated to be material.
- 6.11 Following completion of the Transfers, it is the intention of the NYLB to wind-up both AMIC-UK and AMIL and release any residual assets to the estate of AMIC-ILQ.

Consideration if the Transfers do not succeed

- 6.12 The Parties are preparing for the Transfers with the objective that both the AMIL and AMIC-UK Transfers will be effected at the same time and the terms of the whole account reinsurance agreement and the Deed of Charge reflect this shared objective. If none, or only one, of the Transfers is effected, or there are for some reason partial transfers and partial exclusions, the Parties have indicated that they would need to reassess and amend the terms of those transaction agreements. I have considered the following scenarios on the basis of the current terms of the transaction agreements:

- Neither of the Transfers is effected
- One or other of the AMIL or AMIC-UK Transfers is effected

6.12.1 Neither of the Transfers is effected

In this scenario, the whole account quota share reinsurance will continue in force. The Deed of Charge also remains in place because the premium payment obligation under the whole account quota share reinsurance

agreement will only be released when the payment obligation of AMIL to Bothnia is met. This outcome conflicts with the commercial motivation for the Transfers and there would be a strong incentive for the Parties to establish alternative arrangements. If the Transfers do not succeed, then the NYLB will be required to find an alternative means of closing AMIL and winding up AMIC-UK. Under this scenario, NYLB's finalisation of the AMIC-ILQ liquidation will be delayed and this situation is likely to cause a delay in settling creditors' claims and a reduction in the eventual level of pay-out as a result of the increase in costs.

6.12.2 One or other of the AMIL or AMIC-UK Transfers is effected

- The AMIL Transfer succeeds and AMIC-UK does not

I have been advised by the senior function holders of the Compré Group, who have consulted with Willkie Farr, that the transfer agreement does not contemplate the situation of splitting the transfers into two. However if the Transfer of AMIL is effected and AMIC-UK is not, then the Parties would be free to amend the terms of the Transfers. As currently drafted, the transfer agreement contemplates that the cash and assets in the Collateral Account of AMIL, equal to the premium amount¹⁴, would transfer together with the liabilities of AMIL and that the whole account quota share reinsurance would remain in place, covering AMIC-UK only. Upon the satisfaction of the payment obligations of AMIL to Bothnia, the security under the Deed of Charge is discharged at the request of AMIL. The options for AMIC-UK would be considered in the light of the reasons for the failure of the Part VII scheme.

- The AMIC-UK Transfer succeeds and AMIL does not

The whole account quota share reinsurance will continue in force on a funds withheld basis until such time as the Parties agree an alternative course of action. The Deed of Charge remains in place since AMIL has no obligation to transfer assets to Bothnia, which will retain its security under the Deed of Charge. A possibility that has been considered would be the acquisition, by Bothnia, of AMIL. This would be subject to regulatory approvals however and the commercial viability of this option would depend on the reasons for the failure of the AMIL Transfer.

6.13 If the Transfers do not succeed, then, provided that the whole account quota share remains in place, there is no material effect on the policyholders of Bothnia. If the Transfers were not sanctioned and the whole account quota share reinsurance

¹⁴ As adjusted for claims, interest and bank charges

appeared likely to remain in force for an extended period, this would not be consistent with the objectives to wind-up AMIC-UK and AMIL and it is likely that a renegotiation of the terms of the whole account quota share would result but it is not possible to anticipate the effect of such a measure on the policyholders of Bothnia.

- 6.14 I have explained in paragraph 8.2 that AMIL and AMIC-UK have taken no action in relation to compliance with Titles I to III of the Solvency II Directive. It is AMIL and AMIC-UK's strategy to transfer the burden of full Solvency II compliance to Bothnia through the Part VII Transfer mechanism.
- 6.15 Neither AMIC-UK nor AMIL qualify for exemption from Solvency II. In the event that the Transfers were not sanctioned the likely outcome for the Transferors is summarised below:
- Should AMIL not have an alternative plan to wind-up prior to 1 January 2019 it would no longer be able to apply the Transitional Measures and would be subject to full compliance with Titles I to III of Solvency II.
 - As I noted in paragraph 4.21 AMIC-UK is currently in breach of certain regulatory requirements under Solvency II and should the transfer in respect of its liabilities not be sanctioned then the regulatory breach is likely to persist over a longer period and this would increase the likelihood of some form of regulatory intervention.

A likely consequence of the above scenarios is that the costs of the administration of the portfolios would increase, which would be detrimental to existing policyholders since there is no prospect of additional funds from AMIC-ILQ, the ultimate parent company. Additionally AMIC-UK and AMIL would not meet the AMCR (defined in paragraph 4.17) either for a branch or a subsidiary which, in all likelihood, would increase the extent of any regulatory intervention.

7. THE TRANSFERS IN CONTEXT, THEIR SCALE AND POLICYHOLDER SECURITY

7.1 In this section I have considered financial aspects of the proposed Transfers by reference to the statutory financial statements, the Solvency II SCR capital requirements and the level of financial headroom which the balance sheet surplus provides to absorb adverse financial outcomes. I have addressed these aspects under the following sub-headings:

- Comparative balance sheets on a statutory accounting basis (paragraph 7.4)
- The current level of claims in AMIL and AMIC-UK and the scope for further claims (paragraphs 7.5 to 7.11)
- The basis of establishing estimates of outstanding claims in Bothnia, including the impact of RFP, Gibbon and Stockholm Re (paragraphs 7.12 to 7.26)
- The relative scale of the portfolios (paragraph 7.27)
- Solvency positions and stress tests on a statutory accounting basis and on a Solvency II basis (paragraphs 7.28 to 7.39)

7.2 I have carried out a series of stress tests in order to explore Bothnia's financial resilience to adverse variations in circumstances. The stress tests were applied to both the statutory financial statements (paragraph 7.33) and the regulatory, Solvency II based, financial statements (paragraph 7.38). The tests are performed as at 31 December 2016 and I have presented the results both with and without the Bothnia ADC.

7.3 I have also referred to the requirement to perform a supplementary review shortly before the Transfer scheme sanction hearing in order to update the Court on any matters in the intervening period that might affect my opinion.

Comparative balance sheets on a statutory accounting basis

7.4 Table 6 shows the comparative balance sheets of the Parties pre- and post-Transfers. Additionally, I have shown the Bothnia balance sheet pre and post the impact of the Bothnia ADC.

Table 6 – Pre- and Post- Transfers balance sheets of the Parties

Comparative balance sheet positions as at 31 December 2016 (GBP 000's)

	Pre- Transfer				Post- Transfer			
	Bothnia	Post-ADC	AMIL	AMIC-UK	Bothnia	Post-ADC	AMIL	AMIC-UK
Assets								
Investments :								
Equities	0	0			0	0		
Bonds and short term deposits	46,704	46,704			46,704	46,704		
Deposits with credit institutions	0	0			0	0		
Deposits with cedants	1,152	1,152			1,152	1,152		
Cash at bank and in hand	24,182	23,835	2,286	1,553	25,812	25,465	656	1,553
Reinsurer share of outstanding claims	13,671	29,174	250		13,671	29,174		
Debtors								
Arising out of reinsurance operations	13,048	13,048			11,418	11,418		
Other debtors	3,823	3,823	5		3,823	3,823	5	
Tax	0	0			0	0		
Accrued Interest	360	360			360	360		
Other debtors	297	297			297	297		
Total Assets	103,237	118,393	2,542	1,553	103,237	118,393	661	1,553
Liabilities								
Subscribed capital	3,260	3,260	2,500		3,260	3,260	2,500	
Invested Unrestricted Equity Fund	7,505	7,505			7,505	7,505		
Profit / loss brought forward	10,113	10,818	-1,908		10,113	10,818	-1,908	
Shareholder surplus	20,877	21,583	592		20,877	21,583	592	
Provision for outstanding claims	62,724	62,724	250		62,724	62,724	0	
Equalisation provision	4,120	4,120			4,120	4,120		
Creditors								
Arising out of reinsurance operations	7,796	22,070	1,631		7,796	22,070	0	
Other creditors	5,711	5,711		65	5,711	5,711		65
Home office balance	0	0		1,488	0	0		1,488
Accrued Liabilities	2,008	2,184	69		2,008	2,184	69	
Total liability	103,237	118,393	2,542	1,553	103,237	118,393	661	1,553

Notes on the above:

- The Bothnia ADC affects the statutory financial statements in the following areas:
 - Bothnia's Cash at Bank is reduced by the amount of the premium in respect of the OTM section.
 - The Reinsurer share of outstanding claims increases, reflecting the recovery under the Bothnia ADC in line with the level of claims to which the programme is subjected.
 - The overall Shareholder Surplus increases which reflects the amount by which the benefit under the OTM section exceeds the reinsurance premium. A potential tax liability arises which is reflected in the increase in the Accrued Liabilities.
 - The Creditor item arising out of reinsurance operations increases, reflecting the funds withheld premium for the ITM section.

- There is no change to the total liabilities or assets of Bothnia Pre- and Post-Transfers. Post-Transfers, Bothnia's Debtors Arising out of Reinsurance Operations has reduced by £1,630k with a corresponding increase in cash; the complementary change is reflected in AMIL's cash balances and reinsurance creditor item. This reflects the reinsurance premium payable under the whole account quota share.
- The balance sheet of AMIC-UK does not change.
- The balance sheet of AMIL changes in order to reflect the removal of the whole account quota share and the funds withheld balances. The balance sheet surplus does not change.

Current claims in AMIL and AMIC-UK and the scope for further claims

- 7.5 The Compre Group provided me with a summary of the investigation that they conducted in their due-diligence review of AMIL and AMIC-UK prior to Bothnia issuing the whole account quota share reinsurance. I have reviewed the procedures adopted and I consider the approach to have been thorough. I have also been provided with current information with respect to developments on claims notifications made to the Transferors.

With respect to AMIC-UK

- 7.6 I am advised that there are no current outstanding claims nor any loss advices of a precautionary nature. The Compre Group have confirmed that the position has remained unchanged since at least December 2012.
- 7.7 In order to consider the possibility of a material exposure to the late emergence of claims, I have reviewed a schedule of all contracts issued by AMIC-UK other than those terminated under the WFUM pool Scheme of Arrangement. The conclusion of my examination is set out below, firstly for the remaining WFUM pool UK EL exposures and secondly for the remainder of the portfolio:
- WFUM pool potential UK EL exposures:
 - 1041 contracts appear on the policy register and the industry groups underwritten are, in my opinion, low-risk with respect to latent claim emergence. The earliest policy commenced in January 1978 and the final contract expired in February 1989.
 - I have carried out a high-level examination of the policy listing. Based on my experience of portfolios with UK EL exposure and similar exposure periods, it is in my view likely that at the current level of maturity of the portfolio, any latent claims would by now have begun to emerge. The fact that there have been no claims for at least 4 years,

only an enquiry on ELTO which has not resulted in a formal claim to date, indicates that the nature of the portfolio is low-risk with respect to the potential for late-emerging claims. I am satisfied that the potential for the late emergence of claims of any material degree is extremely small.

- All other contracts issued by AMIC-UK
 - 255 contracts are recorded on the policy register; the last contract expired in December 2002. I have not examined the contract terms in detail, but based on my high level view of the descriptions of the original insured parties, I am satisfied that the potential for the late emergence of claims to any material degree is extremely small.

7.8 Whilst the portfolio has no current open claims and the nature of the exposures appears to be relatively low-risk with respect to the potential for late-emergence claims, nevertheless it remains a possibility that late emergence claims from the UK EL section may occur in the future. I am satisfied that the risk is small because AMIC-UK offered relatively small limits of coverage with short durations of continuous coverage provided to the underlying policyholders (80% of policyholders were insured for 3 years or less); these factors will tend to limit the scale of individual claims. Any claims that arise will be recoverable under the whole account reinsurance prior to the Transfers and following the Transfers will become part of the Bothnia portfolio. Emergent claims will be subject to assessment by Bothnia and Compre Services and subject to actuarial estimation and appropriate reserves will be established as the need arises.

With respect to AMIL

7.9 I am advised that claims activity is minimal - the last formal notified claim was closed by December 2009. Since that time there has been 1 informal enquiry of a potential claim, in 2013, in respect of an industrial deafness case under a UK EL insurance policy. I have been provided with summary correspondence in relation to this. The Compre Group have investigated the claim during its due-diligence prior to Bothnia's provision of the whole account quota share reinsurance and found that the period of coverage is limited and that there are a number of details missing in the information provided – the maximum loss to AMIL was considered unlikely to exceed £2,000 should the claim be formally lodged and found to be valid.

7.10 Industrial deafness claims have seen a significant increase in the UK over the last few years and the common experience of insurers is that a high proportion are found to be invalid (up to 80%) for various reasons. Having only had 1 case intimated 4 years ago, and given the general experience of UK EL insurers in the UK, it is in my opinion unlikely that AMIL will experience a material level of future claims. AMIL is carrying a contingent provision of £250k for IBNR which, based on my

understanding of the claims pattern and the exposure base of the policy register, is highly conservative.

- 7.11 I have also considered the possibility of future claims by examining the policy register, consisting of 81 issued policies. The final policy expired in October 2004 and, based on the industry classifications and the coverage periods involved, I consider the portfolio to have a very low-risk profile as far as the possibility of late notice claims. However, as is the case for AMIC-UK, there is a possibility of late-emergence claims on the UK EL contracts. As noted in paragraph 7.8, in the event that latent claims emerge, then they will be subject to appropriate evaluation by Bothnia and technical provisions will be established on a basis consistent with Bothnia's reserving policy.

The basis of establishing estimates of outstanding claims in Bothnia

- 7.12 I have discussed the basis of establishing the provisions for future claims with the senior function holders of Bothnia and the Compre Group, and with Mr Ruohonen. The senior function holders include Compre's Group Actuarial Director and Bothnia's external appointed actuary. FIN-FSA requires that every Finnish insurance company has an appointed actuary, whose local qualification is granted by the Ministry of Social Affairs and Health. For larger insurers, the appointed actuary is usually internally employed, but this is not a legal requirement and smaller companies (including Bothnia), tend to use the services of external independent consulting actuaries.
- 7.13 Based on my discussions with the senior function holders, and on the explanations provided to me regarding the operations of the claims service provided by Compre Services, I am satisfied that the establishment of case reserves for claims is consistent with the basis that is generally adopted by London market insurance companies, with which I am familiar. As noted in paragraph 5.34 Bothnia merged with Stockholm Re, a Compre Group company. As members of the same group, both underwent a similar reserving process and the Group Actuarial Director prepared an actuarial reserve review for the combined entity as at 31 December 2016.
- 7.14 I have sought explanations from the relevant senior function holders of the approach taken regarding the establishment of contingent provisions for IBNR, which I have summarised below:
- Bothnia establishes IBNR by applying a series of benchmark factors to the notified case reserves. I am familiar with this approach and it is not uncommon for run-off portfolios, particularly portfolios with substantial US asbestos and pollution reserves.
 - As the issues driving many of the underlying claims are being resolved, reserve estimates for an increasing number of segments of the portfolio have moved

away from the benchmark method to a more contract-specific basis. In recognition of this Compré Services, on behalf of Bothnia, reviews significant deviations between the IBNR: Case reserves ratios expected at the start of the year and the implied updated ratios at quarter end. This approach is viewed as allowing Bothnia to identify early on whether any part of its portfolio is developing significantly differently to expectations. Whilst the establishment of IBNR is being targeted towards specific contracts, I have been advised by Compré Services that Bothnia has maintained an unallocated, “bulk”, IBNR provision in the statutory accounts at such a level that gives an overall portfolio IBNR broadly consistent with the earlier benchmarking method.

- Independent external actuarial reviews of the claims provisions were carried out as at December 2013 and December 2014. As at December 2016 external consultants performed an independent validation check on the Group Actuarial Director’s in-house reserve review. The external reviews at December 2014 and December 2016 were both performed by the same firm of highly experienced and reputable actuaries and consultants, and prepared in accordance with the relevant professional standards as adopted by the Institute and Faculty of Actuaries, this gives me confidence that it is reasonable to rely on the work as background in forming my opinion.
- The internal actuarial review includes a statistical range of estimates around the Group Actuarial Director’s best estimate. Based on the estimated ranges, the statutory reserves are at a level equivalent to the 90th percentile, which is considerably in excess of the statistical expected value, namely circa the 60th percentile. The statistical expected value, or mean outcome, is referred to as the “best estimate” and forms the basis of the technical provisions for the purposes of the regulatory returns under Solvency II.

Bothnia Actuarial review – approach

- 7.15 The purpose of Bothnia’s actuarial review was to establish a best estimate basis of the claims provisions. In addition, a key output of the analysis was to place Bothnia’s statutory held reserves into a statistical range around the best estimate. The methodological approach taken and the key assumptions are explained below.
- 7.16 The claims database was analysed and the portfolio was segmented into a number of categories with broadly similar characteristics, reflecting the:
- Original underwriting class of business (e.g. aviation, casualty, marine, motor, credit, property)
 - Nature of the contract (e.g. direct business, non-proportional or proportional reinsurance)
 - Major territory associated with the claims (e.g. UK, US or other)

- Underwriting year grouping (e.g. 1970& prior, 1971-80, 1981-85, 1986-90, 1991-2000, 2000&later)
- Type of loss (e.g. asbestos, health hazard, pollution, various other)

Each claim is ascribed a combination of the above characteristics.

7.17 Benchmark factors have been used in the actuarial review which reflected the different combinations in a coherent and consistent manner. The benchmark factors consisted of:

- Ratio of IBNR: Case reserves. This method applies a factor to outstanding loss reserves to project IBNR. The factors are judgemental, supported by industry data.
- Survival ratios (applied to paid or incurred claims). This method applies a factor to the averaged calendar movements in paid and incurred claims over the previous 5 years. The ratios are based on judgment, considering selected industry projected ultimate values, historical industry payments and take account of trends in the pattern of the individual claims.
- Redundancy analysis. This method considers business segments with very low numbers of new claims being reported. The degree to which case reserves have historically tended to be overstated or understated was evaluated by comparing the historical level of movement in case reserves as claims have been settled. The proportionate reduction in the case reserve as a result of claim settlements was available as a cross check on other methods.

7.18 The approach considered most appropriate was applied to the claims database and cross-checks applied to ensure that, for example, sub-portfolios which had been active in the past 5 years but where there was no current advised case reserve were allocated an IBNR using the survival ratio benchmark whereas the IBNR:Case loading ratio would have produced a nil estimate.

7.19 Further ad-hoc adjustments were applied to claims in respect of well-known market events and where the actuaries were familiar with the particular circumstances of loss which would lead to the IBNR allocation method producing results which were inconsistent with their wider knowledge. A small number of claims were considered in isolation and the specific circumstances of the claims reflected in the IBNR estimate, in consultation with the claims department.

Key assumptions

7.20 Asbestos

- The benchmark factors are based on the wider experience of the Group Actuarial Director and the factors used by external actuaries in previous

external reserve reviews based on their broader experience on a wide range of portfolios. The factors were considered to be relevant for the Bothnia US asbestos portfolios since much of the Bothnia portfolio is assumed reinsurance made up of exposures from many underlying insureds.

- The choice of factors reflects the delays that might be expected in processing direct US asbestos claims through into the international reinsurance and retrocessional market.
- The IBNR to case reserve ratios also reflect differential features between underwriting years; those underwriting years which have been heavily exposed to claims were considered to have a higher level of underlying policy limit exhaustion than later groups of years (particularly 1970 – 1985) where there is likely to be more coverage remaining.
- Consideration is then given to a more granular identification of IBNR potential reflecting specific matters of insurance policy coverage.
- No IBNR for US asbestos losses is assumed from the 1986 underwriting year onwards since asbestos claims were generally excluded from direct insurance policies in the US from 1986.
- Certain classes were deemed too remote to be exposed to asbestos claims (e.g. credit insurance).
- The Compré Group Actuarial Director has considered a publication by AM Best which set out its revised assessment of the potential for Asbestos and Pollution related insured losses in the US insurance market. A key conclusion of the AM Best report, issued in November 2016, is that claims reserves held by US insurers are potentially understated by approximately 18%. The view held by the Compré Group Actuarial Director, following consultation with the claims department, is that the AM Best analysis is not directly comparable with the Bothnia portfolio since the AM Best study is focused on the reserves of US primary insurers whereas Bothnia's US asbestos exposures are mainly through inwards reinsurance risks and are subject to Bothnia's reserving practices. Further, I have been informed by the Group Actuarial Director that Bothnia has not seen any emerging evidence of a shortfall in Bothnia's best estimate reserves. Consequently, whilst the AM Best publication provided informative background information, it did not lead to a direct impact to the approach taken in the Group Actuarial Director's review.

7.21 Pollution and health hazard

- Pollution and health hazard is not a significant element of the exposure and IBNR was based on an IBNR to case reserve loading without adjustment for lags and underwriting year bands.

7.22 Other claim types

- In deriving an estimate, the claims database was interrogated and sub-divided into loss types which were ascribed IBNR factors consistent with their respective natures of loss.
- Large specific losses were considered individually on their merits.

7.23 RFP and Gibbon

- For each of these relatively recent acquisitions, the same general actuarial methodology was adopted as for the balance of the portfolio.
- In the case of RFP I note:
 - This was the first occasion on which an in-house actuarial review was performed in full. An external actuarial review had been carried out prior to the acquisition of the portfolio as part of the due diligence process. The external consultants are the same as those who carried out the December 2016 actuarial validation and therefore the external actuarial validator had continuity of knowledge of RFP.
- In the case of Gibbon I note:
 - A detailed in-house actuarial review has not been carried out as at 31 December 2016. A detailed due-diligence analysis was carried out by the Group Actuarial Director as at 31 December 2015 and, in addition, an external actuarial IBNR review was prepared at the same time. The methods used for these reviews are consistent with the methods currently adopted for IBNR estimation within Bothnia.
 - The IBNR methodology as at 31 December 2016 took the IBNR loading factor derived from the December 2015 detailed studies and applied that to the corresponding case reserves as at December 2016. This approach was considered reasonable since there had not been significant paid claims or other loss developments which affected the risk profile of Gibbon since the due diligence exercise.

Conclusion on the actuarial review

- 7.24 The approach taken is, in my opinion, reasonable and in line with good market practice. I have satisfied myself that the overall IBNR levels are consistent with benchmark levels within my own experience by comparing the overall IBNR to Case reserve ratios of the major business segments with the levels with which I am familiar and for companies with a broadly comparable mix of claim categories. The conclusion of the external actuarial validation as at 31 December 2016 was that Bothnia's actuarial best estimate reserves are reasonable both gross and net of external reinsurance.

- 7.25 The provisions in the statutory accounts, summarised in Table 6, contain implicit margins of conservatism and are not discounted for the time value of money. This means that the statutory shareholder surplus is likely to be an understatement of the true, economic value. In the regulatory returns, under Solvency II, the provisions for outstanding claims are measured on a best estimate basis and are calculated with allowance for the time value of money; therefore the balance sheet surplus on a regulatory basis is a more accurate economic representation.
- 7.26 Based on my review of the portfolio, the actuarial review and on the explanations provided to me by the relevant senior function holders, I did not consider it necessary to conduct an in-depth actuarial analysis of the claim statistics of Bothnia. I am satisfied that the claims reserves carried by Bothnia are established at a conservative level and that the actuarial best estimates reflect a reasonable view of the most likely outcome. However it must be noted that the reserves are estimates based on current knowledge and reserving philosophy and may change materially should emerging circumstances prove to be different to the underlying reserving assumptions.

The relative scale of the portfolios

- 7.27 As noted in paragraphs 7.6 and 7.9, the Transferors have no notified claims reserves; AMIL is carrying a contingent provision for IBNR of £250k on its statutory accounts, which represents approximately 0.4% of Bothnia's total gross claims provisions. AMIC-UK has a zero claims provisions. The quantum of reserves being transferred is relatively small in relation to Bothnia's overall portfolio.

Solvency positions and stress tests on a statutory accounting basis and on a Solvency II basis

- 7.28 An objective test of the security afforded policyholders is the level of balance sheet surplus in relation to the policyholder liabilities. This gives a measure of the financial resilience of the insurance company to withstand unexpected adverse movements in claims, investment performance or other losses.
- 7.29 I have shown below the level of available balance sheet surplus and the impact of a series of financial stresses on both the statutory accounts' surplus (paragraphs 7.31 to 7.33) and on the Solvency II basis Capital Ratios (paragraphs 7.34 to 7.39).
- 7.30 The stress tests that I have applied to both statutory and regulatory balance sheets are similar in nature, however since the accounting treatment of certain balance sheet items differ between the two bases, I would not expect a completely consistent pattern of results. The objective of the stress tests is to evaluate the sensitivity of the balance sheet surplus under each of the accounting bases.

Statutory accounting basis

7.31 Tables 7 and 7a below set out a measure of Bothnia’s surplus in relation to the level of technical provisions as reported on its statutory accounts pre and post-Bothnia ADC. Beneath the table I have commented on the values and summarised or commented upon the results of a limited number of stress tests applied to key aspects of the balance sheet in order to evaluate the resilience of the balance sheet to different shocks.

Table 7 - Balance sheet surplus relative to technical provisions as at December 2016 pre-Bothnia ADC

	<u>Bothnia</u>	<u>AMIL</u>	<u>AMIC-UK</u>
Per statutory accounts			
Surplus to gross claims provisions	40%	237%	N/A
Surplus to net claims provisions	51%	N/A	N/A
Liabilities to net present value			
Surplus to gross claims provisions	46%		
Surplus to net claims provisions	58%		

Table 7a – Balance sheet surplus relative to technical provisions as at December 2016 post-Bothnia ADC

	<u>Bothnia</u>	<u>AMIL</u>	<u>AMIC-UK</u>
Per statutory accounts			
Surplus to gross claims provisions	41%	237%	N/A
Surplus to net claims provisions	77%	N/A	N/A
Liabilities to net present value			
Surplus to gross claims provisions	45%		
Surplus to net claims provisions	84%		

7.32 Notes to Table 7 and Table 7a:

- The ratios measure the headroom that the balance sheets provide to absorb adverse movements in the claims provisions. The balance sheet surplus is available to meet adverse contingencies in respect of all operational aspects of the business, including movements in claims. For these purposes, Bothnia’s Equalisation Provision¹⁵ is treated as surplus.

¹⁵ Equalisation provisions are funds required, under local insurance regulations, to be separately held and not treated as pure shareholder funds under normal circumstances. The funds are a Finnish regulatory required internal safety net which cannot be paid out as dividends but are available to meet adverse contingencies. I have summarised various aspects of Finnish Insurance customer protection in Appendix 5.

- Bothnia's surplus ratio, net of reinsurance, increases significantly following the implementation of the Bothnia ADC.
- The circumstances of the Parties are very different and a direct comparison of the above ratios is not strongly indicative of relative strength and my principal focus in evaluating the strength of Bothnia's balance sheet is on the absolute level of security provided by Bothnia.
- The relatively high surplus ratio for AMIL reflects the small residual IBNR (there are no recorded open claims) and its status as a small portfolio of relatively low-risk business which has had an extended period of run-off with minimal claims activity. I explained in paragraph 6.6 that AMIL has agreed a Deed of Charge in favour of Bothnia over the funds in the Collateral Account. The funds available to AMIL are therefore subject to a legal encumbrance. However, for the purposes of calculating AMIL's surplus ratios in Tables 7 and 7a I have not applied a restriction arising from this encumbrance to the level of surplus. I did not consider this necessary since:
 - AMIL has an established procedure with Bothnia to ensure that running costs and normal business expenses are promptly agreed and processed through the Collateral Account; and
 - If claims payments out of the Collateral Account equal or exceed the premium amount then the secured obligation under the Deed of Charge will be zero and Bothnia shall, at AMIL's request, release the Collateral Account as security making the surplus freely available to AMIL.

The net liability for AMIL is zero.

- As a branch operation of an insolvent company, the surplus ratio for AMIC-UK is not a meaningful measure and it may be considered as being insolvent; in section 8.11 I have outlined the way in which insolvency proceedings may be applied.
- I have also shown the surplus ratios for Bothnia reflecting the net present value of the claims provisions. This is a more economically correct representation than the pure statutory accounting position since this recognises the time-value of money over the settlement duration of the claims and places the valuation of the liabilities on a consistent footing with the assets. In performing this calculation I have made certain assumptions regarding the average duration of the cash flows associated with the various segments that make up the reserves and the appropriate interest rate for discounting based on my experience of other portfolios with broadly similar

exposures¹⁶. I also verified my assumptions against the cash flow assumptions used by Bothnia in their Solvency II SCR calculations.

- The surplus ratios for Bothnia are identical pre- and post- Transfers since the whole account quota share provided by Bothnia already reflects the risks of AMIL and AMIC-UK together with the transfer premium.
- The investment portfolio of Bothnia includes an unsecured interest bearing loan to its parent, CHL of Euro 3.6 million (GBP 3.1 million). The loan was issued in July 2014, with further funds being issued in 2015 and 2016, and is repayable on demand subject to 10 days' notice. The loan to parent is not a material factor in forming my opinion since it represents approximately 10.5% of CHLs surplus funds and is well covered, but I have considered the effect on the balance sheet surplus in the event of a 100% write-off, which I consider to be an extreme stress (Test #5 below).

7.33 As a check on the resilience of Bothnia (pre and post-Bothnia ADC) on the statutory accounting basis I have applied a series of stress tests and recalculated the balance sheet surplus ratios shown in Table 7 and Table 7a. I have judgementally ascribed a probability to each stress scenario; the investment driven scenarios (Tests #1 and #2) represent a 1-year view while the other tests represent an ultimate view. The tests are:

- **Test #1** = A 30% equity market shock
- **Test #2** = 5% interest rate shock
- **Test #3** = 50% loss of reinsurance asset
- **Test #4** = Provisions for asbestos claims increase by 25%
- **Test #5** = Write off 100% of Bothnia's loan to parent

Table 8 below shows the results of these tests

Table 8 – Balance sheet surplus ratios under stressed scenarios

	Pre-ADC		Post-ADC	
	Gross	Net	Gross	Net
Test 1	40%	51%	41%	77%
Test 2	30%	38%	31%	58%
Test 3	29%	32%	29%	45%
Test 4	22%	29%	34%	67%
Test 5	35%	45%	36%	67%

¹⁶ Mean terms (years) Asbestos = 6, Pollution / Health / Non-APH = 4, CAT / Misc = 2 with an overall mean term of 5.1 years and interest rate of 1.5% pa

- Test #1: 30% equity market shock {Probability ~ 1.5%};
 - No change, Bothnia has minimal equity investment exposure.
- Test #2: +5% interest rate shock leading to a 13% reduction in bond values {Probability ~ 1%};
 - The bond portfolio is relatively short dated, which mitigates the impact of interest rate shocks. The capital coverage falls, but on a statutory basis remains solvent. The assets being received as part of RFP and Gibbon are held as cash in a Bothnia bank account and their value is not affected under this scenario.
- Test #3: Loss of 50% of the reinsurance asset {Probability ~ <0.5%};
 - The reliance on reinsurance is primarily in respect of a specific reinsured section of the portfolio, WSAK17. This section is reinsured by National Indemnity Company, a Standards and Poors AA rated subsidiary of Berkshire Hathaway.
 - This test is performed without stressing the reinsurance asset in respect of the ITM section of the Bothnia ADC since the ITM operates on a funds withheld basis which introduces a high degree of risk mitigation.
- Test #4: Provisions for asbestos claims increase by 25% {Probability ~ 2%};
 - I consider this to be a relatively extreme scenario given the strength of the reserving basis.
- Test #5: Write off 100% of Bothnia loan to parent {Probability ~ <0.5%};
 - The loan of Euro 3.6 million represents approximately 10.5% of the shareholder funds of CHL – the shareholder funds in CHL give a coverage level of approximately 10 times the loan amount. A 100% write off is therefore an extreme scenario but serves to show that the loan to parent does not present a material risk to Bothnia's solvency.

Solvency II basis

7.34 In paragraphs 7.35 to 7.39 I have shown the regulatory capital requirements and the available assets which Bothnia has to meet these requirements. In addition I have tested the extent to which Bothnia's SCR and MCR are covered under a series of financial stress scenarios.

¹⁷ WASA SAK Försäkringsaktiefbolag (publ), a company within the WASA Group from 1990 – 1995. The portfolio is protected by two Aggregate Stop Loss contracts which have been in place since. Administration of the portfolio has been handled by Resolute Management since 1998. WSAK became part of the Bothnia portfolio during the merger with Stockholm Re.

7.35 In paragraph 4.15 I noted that Bothnia is subject to the SF for the purposes of its regulatory capital requirement, the SCR. Table 9 below shows the SCR at year end 2016. In it I show:

- The position for Bothnia, excluding the effect of all RFF
- The RFP position under the RFF restriction
- The Gibbon position under the RFF restriction
- Bothnia's position at year-end 2016, reflecting all aspects of RFF, including the application of RFF restrictions on the Bothnia whole account reinsurance in favour of AMIL and AMIC-UK
- The final column shows the position for Bothnia following the completion of the Transfers (i.e. removing the RFF restriction on the AMIL and AMIC-UK whole account reinsurance)

Table 9a shows the equivalent values adjusted to reflect the impact of the Bothnia ADC.

7.36 In my evaluation of the solvency position of Bothnia, I have focussed on its financial position post-Transfers; the stress tests in Tables 10 and 10a have been performed on this basis.

Table 9 - Summary of the Year End 2016 Solvency II capital requirement for Bothnia pre-Bothnia ADC

GBP 000's	<u>AMII/AMIC-UK on RFF Basis</u>				<u>Post-Transfers</u>
	<u>Bothnia</u>	<u>RFP</u>	<u>Gibbon</u>	<u>Total</u>	<u>Total</u>
MCR	3,154			5,257	5,257
SCR	9,541	7,978	1,794	19,312	19,312
Available assets (Solvency II basis)	23,384	3,682	1,669	28,735	30,365
Capital Ratio	245%	46%	93%	149%	157%

Table 9a - Summary of the Year End 2016 Solvency II capital requirement for Bothnia post-Bothnia ADC

GBP 000's	<u>AMII/AMIC-UK on RFF Basis</u>				<u>Post-Transfers</u>
	<u>Bothnia</u>	<u>RFP</u>	<u>Gibbon</u>	<u>Total</u>	<u>Total</u>
MCR	3,154			3,471	3,471
SCR	6,566	5,942	1,375	13,883	13,883
Available assets (Solvency II basis)	24,129	4,654	1,375	30,158	31,788
Capital Ratio	368%	78%	100%	217%	229%

7.37 Notes to Table 9 and Table 9a:

- Bothnia's Solvency II capital calculations have been prepared by the Compré Group Actuarial Director. I have applied my own cross-checks to the calculations and discussed the basis adopted in arriving at their evaluation and I am satisfied that the approach is reasonable.
- Bothnia's SCR reduces materially following the inclusion of the Bothnia ADC.
- For the segment of Bothnia's portfolio associated with Gibbon, the SCR following the Bothnia ADC reduces to a level below the ring fenced assets associated with this portfolio. For the reasons noted in paragraph 4.18, Bothnia is restricted in the amount for which it may take credit for regulatory solvency purposes in its available assets.
- Bothnia has surplus capital, on a regulatory basis, 57% higher than the SCR before the Bothnia ADC and 129% higher than the SCR after the Bothnia ADC.
- In paragraph 4.17 I explained that the SCR calculated using the SF is based on the application of a series of risk loading factors which are not necessarily representative of the true risk profile of an individual business. The experience of mature portfolios with extensive US liability and asbestos exposure can be mixed with respect to the inherent risk. Increasingly for US asbestos assureds, agreements are being reached with the trusts representing the insured asbestos-exposed policyholders (a significant number of whom are in a form of protected bankruptcy with their assets, including the benefit of insurance coverages, held in trust on behalf of injured parties). The settlement agreements typically include the capping of liabilities – thus for many US asbestos exposed insurers operating as excess and surplus lines underwriters, it is increasingly likely, in my opinion, that the funnel of doubt will narrow and that for a portfolio in run-off the standard formula is likely to become increasingly inappropriate as the factors driving the uncertainties reduce. Notwithstanding this view, the nature of the underlying liabilities is long-tailed and is undoubtedly uncertain.
- I noted in paragraphs 5.30 and 5.38 that Bothnia will ultimately seek to effect an insurance business transfer of RFP and Gibbon. A consequence of this is that the RFF restriction on these portfolio segments will be removed, leading to an improvement in the overall solvency levels on a Solvency II basis. I did not consider it necessary for the purposes of my opinion to quantify the improvement and my assessment is based on the current RFF status of RFP and Gibbon.

7.38 In order to test the resilience of the balance sheet on a Solvency II basis, Bothnia have, under my instruction, produced 5 sensitivity tests which examine the impact of

variations in the level of technical provisions, the exposure to reinsurance counterparties and a test focusing on the economic environment. The tests are:

- **Test #1** = A 20% increase in all claims reserves
- **Test #2** = A 2-grade deterioration in counterparty ratings
- **Test #3** = Combination scenario #1 + #2
- **Test #4** = 25% increase in asbestos reserves
- **Test #5** = Interest rate shock, +2% on all durations

7.39 I have performed these tests by instructing the Compré Group Actuarial director to change the opening position of the Solvency II balance sheet as required for each test and then re-calculate the SCR using the SF. Table 10 below sets out the impact of these various stress tests on a pre-Bothnia ADC basis, Table 10a sets out the impact on a post-Bothnia ADC basis.

Table 10 – Solvency II SCR capital calculations under stress scenarios pre-Bothnia ADC

GBP 000's	Base Case	Test 1	Test 2	Test 3	Test 4	Test 5
Solvency II SCR	19,312	23,305	28,880	32,711	22,226	16,520
Solvency II MCR	5,257	6,308	7,220	8,178	6,021	4,593
Own Funds	30,365	23,049	30,188	22,863	25,331	33,340
Capital Ratio	157%	99%	105%	70%	114%	202%

Table 10a – Solvency II SCR capital calculations under stress scenarios post-Bothnia ADC

GBP 000's	Base Case	Test 1	Test 2	Test 3	Test 4	Test 5
Solvency II SCR	13,883	17,159	23,798	26,990	16,226	12,700
MCR	3,471	4,311	5,950	6,748	4,057	3,175
Own Funds	31,788	28,489	31,979	28,197	29,941	31,563
Capital Ratio	229%	166%	134%	104%	185%	249%

Notes:

- **Test #1:**
 - Pre-Bothnia ADC this leads to a breach of the SCR. This reflects the fact that the reserve risk is a dominant risk and that the SF SCR responds to these tests in a multiplicative manner.
 - Post-Bothnia ADC there is no SCR breach.
- **Test #2:**

- This leads to an increased counterparty risk, this reflects the requirement for additional provisions against a default by counterparties. The most material counterparties relate to the “cash at bank” being held in respect of the RFF arrangements for RFP and Gibbon and the reinsurance counterparty in respect of WSAK.
- There is no additional counterparty risk in respect of the ITM section of the Bothnia ADC as this has been written on a funds withheld basis.
- Test #3 is a combination of Tests #1 and #2:
 - This leads to a breach of the SCR on the pre-Bothnia ADC basis.
 - On the post-Bothnia ADC basis the SCR is still being met.
- Test #4:
 - This leads to a significant increase in the SCR but does not lead to a breach on either a pre or post-Bothnia ADC basis.
- Test #5:
 - This improves the Solvency II capital position since the favourable effect of discounting on the liabilities exceeds the adverse impact of higher interest rates on the valuation of the bond portfolio.

In each of the above scenarios the MCR is exceeded by margin of at least 250% pre-Bothnia ADC and 400% post-Bothnia ADC.

The scenarios which lead to a SCR breach are circumstances where there is a material underestimation of the technical provisions. I consider such a significant degree of underestimation to be highly unlikely based on the detailed level of analysis applied in evaluating and monitoring the portfolio. Bothnia’s ORSA contemplates such circumstances and identifies that contingency measures in order to raise additional capital would be necessary in the event that the SCR is breached. I have discussed with the Compre Group’s senior management the most likely method that Bothnia would use to raise additional capital. I have been advised that shareholder support would be in the form of a Shareholder Contribution, which would qualify as Tier 1 Capital. I note that there are no formal guarantees in place for the provision of additional capital, however I am satisfied through my conversations with senior function holders of the Compre Group that, given the importance of Bothnia to the further development of the Compre Group, additional capital would be provided.

Based on the low likelihood of significant under-provisioning, the ability of the existing funds to exceed the MCR and the ability of Bothnia to raise additional funds, I do not consider the results of these tests to have identified a material risk to the security of the Transferring Policyholders.

Conclusion with respect to financial aspects of the Transfers

- 7.40 Based on the above I have concluded that Bothnia is a solvent Well Capitalised entity prior to the Bothnia ADC and Very Well Capitalised post-Bothnia ADC.
- 7.41 I have considered the basis of setting reserves and discussed the methodologies with the Compré Group Actuarial Director and, independently, with Bothnia's external actuary. I have reviewed the independent actuarial analysis produced as at December 2013 and December 2014, and the independent validation work performed by the external consultants as at December 2016. I have also conferred with Mr Ruohonen regarding Bothnia's reserving practices.
- 7.42 I am satisfied that Bothnia is sufficiently well reserved, with sufficient surplus capital on a statutory and regulatory basis to ensure that no parties are materially adversely affected by the Transfers. I am satisfied that the Bothnia ADC leads to an improvement in the level of regulatory capital coverage; it is designed to be adjusted in line with the scale of Bothnia's portfolio as it engages in further acquisitions and therefore it is not possible to anticipate, over the life-time of the portfolio, the precise outcomes of the Bothnia ADC as at 31 December 2016. In view of this, I have formed my opinion on the basis of both the pre- and post-Bothnia ADC positions and I am satisfied that on either basis my overall conclusion is the same in the context of the Transfers.
- 7.43 Bothnia's role within the Compré Group is to provide a platform to consolidate other insurance portfolios in run-off which are existing subsidiaries of the Compré Group, and to accept run-off portfolios of third parties. Its business objective is, ultimately, to manage the run-off portfolios at a profit. I have reviewed Bothnia's most recent ORSA report which sets out projected balance sheets over the next 3 years and contemplates contingency arrangements for the provision of additional capital should the anticipated level of profitability of the forecast financial statements not be met. I am satisfied that the underwriting disciplines and controls around the due-diligence process in relation to portfolio acquisitions are appropriate, I am also satisfied that Bothnia has the capability to quickly test the impact on the regulatory capital requirement of alternative scenarios for any acquisition. Based on this I do not consider that Bothnia's pursuit of future new business adversely affects any of the Parties.

Supplementary report

- 7.44 My evaluation is based on the financial statements as at 31 December 2016, with an adjustment to reflect the impact of the Bothnia ADC. The circumstances surrounding claims and investment markets are subject to daily fluctuations; in addition, Bothnia is actively seeking additional portfolios to assimilate. I have been

advised that the Compré Group is frequently invited to tender for portfolio acquisition opportunities whose preferred carrier would be Bothnia.

- 7.45 I will produce a supplementary report shortly prior to the sanction hearing. The purpose of the supplementary report is to advise the Court on factors which occurred after the financial data that I have relied upon in forming my opinion was produced, and which may affect my opinion.

8. OTHER CONSIDERATIONS

I have set out below a number of other factors not addressed earlier in my report. These factors are largely of a non-financial nature that I have considered when forming my opinion, these are set out under the following headings:

- Systems of control and governance and the transfer of regulatory responsibility from the PRA to FIN-FSA
- Compliance with the requirements of Solvency II
- Standard of service provided to policyholders
- Possible impairment of reinsurance asset values as a consequence of the scheme
- Financial Services Compensation Scheme ("FSCS")
- Financial Ombudsman Service ("FOS")
- Maintenance of records under the Employers' Liability Tracing Office ("ELTO")
- Guarantees to third parties and funds held in trust
- Implications of the Transfers to policyholders in different jurisdictions
- Tax implications of the Transfers
- Considerations regarding the impact of insolvency of the Parties
- Policyholder communication strategy
- The impact of the UK EU Referendum result

8.1 Systems of control and governance and the transfer of regulatory responsibility from the PRA to FIN-FSA

Prior to the Transfers the Transferring Business falls under the UK regulatory regime as implemented by the PRA and FCA and applied to AMIL and AMIC-UK. The PRA and the FCA are statutory bodies set up under the Financial Services Act 2012. The PRA and FCA are required to co-ordinate with each other in advance of insurance business transfers under Part VII of FSMA.

The PRA is part of the Bank of England and is responsible for:

- Prudential regulation of banks, building societies and credit unions, insurers and major investment firms;
- Promoting the safety and soundness of the firms it regulates, seeking to minimise the adverse effects that they can have on the stability of the UK financial system; and

- Contributing to ensuring that insurance policyholders are appropriately protected.

The FCA is a separate institution and is responsible for:

- Ensuring that its regulated markets function well;
- Conduct regulation of all financial firms; and
- Prudential regulation of those financial services firms that are not supervised by the PRA

Following the Transfers the Transferring Business falls under the Finnish regulatory regime as implemented by the FIN-FSA and applied to Bothnia.

FIN-FSA is responsible for the conduct and prudential regulation of financial institutions in Finland and is organised into three main departments, namely:

- Institutional Supervision,
- Prudential Supervision,
- Supervision of Markets and Conduct of Business

FIN-FSA operates within the Finnish Insurance Companies Act, which has been modified in order to accommodate the implementation of the Solvency II Directive and members of FIN-FSA are represented on the major boards of the European system of financial supervision in a similar manner to senior staff of the PRA / FCA.

The scale of operations of FIN-FSA is considerably smaller than that of the PRA / FCA, with approximately 50 non-life insurance entities under its supervision, some of which are members of the same larger group.

I have summarised in Appendix 5 the most significant aspects of consumer protection as applied in Finland. The overall objectives and general structure of the protection measures are similar in both the UK and Finland and Solvency II has led to further harmonisation of insurance regulation and regulatory capital standards across the EU.

The FCA has set out its Principles for Businesses. These principles include the following that relate to the fair treatment of customers:

- Principle 6: A firm must pay due regard to the interests of its customers and treat them fairly

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

The FIN-FSA applies similar concepts of fair play in its regulatory ethos. Its forward-looking strategy for 2017 to 2019 sets out its objectives with respect to high quality customer and investor protection which are:

- That service providers' internal procedures take account of the requirements of customer and investor protection.
- The provision of high-quality information to investors and reporting procedures that support this.
- A widened scope of stock exchange trading supervision via European cooperation.
- To enhance the reach of customer information.

FIN-FSA's strategy regarding the conduct of insurance business is also set out in its Code of Conduct and Regulatory Outline.

Both the FCA and FIN-FSA have clearly established objectives regarding the conduct of business and fair treatment of policyholders under their respective jurisdictions.

Based on the above, I do not consider that the change in regulator will have a material adverse impact on the Transferring Policyholders and claimants; there is no impact on Bothnia's existing policyholder base.

I noted in paragraph 3.4 that the Parties' legal advisors produced summaries of the legal frameworks in the UK and in Finland and I have included these in full in Appendix 7 together with my own synopsis of the advice obtained. I have compared their analyses and considered the respective regulatory regimes from the following perspectives:

- Prudential regulation;

- Conduct of business issues;
- Complaints handling;
- Supervisory intervention;
- Approval of controllers of regulated entities; and
- Processes for rejecting claims

Based on my evaluation of the comparative analysis of the regulatory arrangements I am satisfied that none of the affected parties is adversely affected as a result of the Transfers.

8.2 Compliance with the requirements of Solvency II

I have confirmed with the senior function holders of the Compre Group that, with respect to their management responsibilities to Bothnia, full compliance with Titles I to III of the Solvency II Directive since adoption on 1 January 2016 has been achieved and will continue to be achieved in the future. I have reviewed the Solvency II planning schedule for on-going reporting and I am satisfied that significant resources are being deployed to meet the requirements; the resources consist of internal actuarial and finance staffing. I have also confirmed with the Compre Group Actuarial Director that all regulatory submissions to the FIN-FSA have been fully completed and submitted on time. I have also been advised that Bothnia maintains a regular dialogue with FIN-FSA in order to ensure that satisfactory compliance with all Solvency II requirements is continued.

I have also confirmed with the Compre Group that internal controls and governance policies and processes have been implemented which are consistent with the new regulatory requirements. I have not reviewed the documentation relating to those internal policies and processes but on the basis of the information that I have been provided with, together with the additional questions that I have raised and the responses that I have received, I am satisfied that appropriate measures are in place.

I have reviewed Bothnia's 2015 ORSA document which was submitted to FIN-FSA in 2016 based off year end 2015 data. I have also reviewed the ORSA which was completed for mid-year 2016 which was submitted to the FIN-FSA in 2017. In my view these documents properly addressed the requirements, FIN-FSA have provided limited feedback and commented that the documents were "professionally prepared". I will review the status with respect to further regulatory feedback in my supplementary report.

AMIC-UK and AMIL have taken minimal action towards compliance with Titles I to III of the Solvency II Directive. AMIC-UK and AMIL have informed the PRA of their status with respect to Solvency II compliance, which I explained in paragraphs 4.16 and 4.21.

Based on the above I have concluded that, with respect to on-going regulatory controls and governance, the Transfers have no impact on the existing Bothnia policyholders and have a positive outcome on any policyholder obligations that may arise in respect of AMIL and AMIC-UK in the future.

8.3 **Standard of service provided to policyholders**

Bothnia is administered by Compre Services. I have confirmed with the senior function holders of the Compre Group that there will be no change to the general administration of the portfolio, claims handling nor in the dealings with policyholders post Transfers.

Willkie Farr have been appointed by the NYLB to advise on English law matters relating to the Transferors and Willkie Farr's address is being used as the registered office for AMIL, it is also noted on the UK Financial Services Registers as the address to which claims, complaints and other correspondence in respect of the Transferors should be directed. The Transferors do not currently have a formal claims handling or operational system in place, however in the event of a claim it is expected that the NYLB would engage Willkie Farr, who would liaise closely with the Compre Group under the terms of the whole account quota share reinsurance, to assist with the investigation, adjustment and settlement of any such claim. There are no formal notified claims in either of the Transferor entities and following the Transfers, should claims emerge, then the claims handling protocols adopted by the Compre Group will apply.

I conclude that the service provided to Transferring policyholders would not be materially affected by the Transfers. I am also satisfied that the Transfers will have no impact on the standards of service of existing Bothnia policyholders. There is no impact on AMIC-ILQ.

8.4 **Possible impairment of reinsurance asset values as a consequence of the scheme**

I have considered the potential impact on the value of the reinsurance asset attributable to the Parties arising as a direct result of the Transfers.

I explained in paragraph 6.3 that the only original reinsurance contracts included in the Transfers are the low level property reinsurance contracts of AMIL. The Transfers have no impact on Bothnia's ability to effect recoveries under these contracts of reinsurance following the Transfers.

With respect to those original reinsurance contracts not being transferred, I explained in paragraph 6.5 that their economic value is negligible and I do not consider the loss of such reinsurances to be a material impairment to the Parties.

In paragraph 6.8 I explained that upon completion of the Transfers, the whole account quota share reinsurance provided by Bothnia will be cancelled. Claims arising from the transferred policyholders will be met from Bothnia's funds in common with its other policyholders. As noted in section 7, Bothnia is Well Capitalised and satisfies the regulatory capital requirements under Solvency II. A consequence of the cancellation of the whole account reinsurance is that AMIC-ILQ has no possibility of benefitting under this reinsurance. I explained this effect in paragraph 6.9 and concluded that this did not represent a material impairment to any of the Parties nor to AMIC-ILQ.

The Transfers have no impact on the existing reinsurance arrangements of Bothnia since they do not interact with the historically placed reinsurance programmes of Bothnia and its acquired portfolios, and the liabilities associated with the Transferors are already included within the scope of the Bothnia ADC.

Whilst the Transfers lead to a theoretical loss of certain parts of the original reinsurance contracts of AMIL and AMIC-UK, in reality the economic value of these contracts is negligible and I am satisfied that the changes to the various reinsurance arrangements following the Transfers have no material impact on any of the Parties, including AMIC-ILQ.

8.5 Financial Services Compensation Scheme ("FSCS")

The FSCS, established under FSMA is described as a "statutory fund of last resort" and is intended to provide compensation to customers of authorised financial services firms in the event of their insolvency.

The FSCS provides protection for policyholders of relevant persons or, where applicable, successor firms¹⁸ in circumstances where the relevant person or successor firm is unable, or likely to be unable, to satisfy protected claims against it. The direct policyholders of the Transferors are included within the scope of the FSCS.

In order to qualify as a successor firm and to obtain complete continuity of coverage for the Transferring Policyholders under the FSCS, Bothnia has obtained the relevant regulatory permissions to provide insurance services on a cross-border basis from Finland to the UK, under the EU Freedom of Services regime (a process

¹⁸ Successor firms are defined as persons who have assumed responsibility for liabilities arising from acts or omissions of predecessor relevant persons (in this context a "person" means an insurer)

referred to as “passporting services”). I am therefore satisfied that the Transfers have no material impact on the Transferring Policyholders’ rights under the FSCS.

Following the result of Brexit there is uncertainty with regards to the continuation of the UK’s involvement in the EU Freedom of Services regime and Bothnia’s ability to passport services into the UK may be subject to change. If this occurs then the protection afforded Transferring Policyholders by the FSCS may be subject to variation. However, given the low likelihood of a claim on the Transferring Business and the Well Capitalised status of Bothnia, I do not consider this potential change to materially impact the Transferring Policyholders. I have further discussed the potential impact of Brexit in paragraph 8.13.

8.6 Financial Ombudsman Service (“FOS”)

FOS provides private individuals and micro enterprises with a free independent service for resolving disputes with financial services companies, including insurers. In the context of insurance, the policy in connection with which the dispute arises must be or have been administered from within the UK, although the claimant does not have to be based in the UK.

Bothnia, as a Finnish insurer is not covered under FOS’s compulsory jurisdiction for its own acts or omissions in respect of the Transferring Policies or its existing policies, pre- or post-Transfer. After the Transfer, Bothnia would be subject to FOS’s compulsory jurisdiction in respect of AMIL and AMIC-UK’s acts and omissions which are already subject to FOS’s compulsory jurisdiction prior to the Transfer. FOS has an optional voluntary jurisdiction for those insurers which do not automatically fall under its scope but who wish to provide their UK policyholders with access to FOS’ services. Bothnia was admitted to this voluntary jurisdiction on 30 October 2015. By submitting itself to FOS’s voluntary jurisdiction, Transferring Policyholders who are eligible claimants will be able to take any complaints they may have regarding Bothnia’s conduct post-Transfers to FOS. The voluntary jurisdiction is a contractual agreement between the insurer and FOS Ltd. (the company that administers the ombudsman scheme), the standard terms of which are set out in DISP19 4, I have summarised these terms below.

Bothnia has agreed for the following rules and guidance to apply, except where the context requires otherwise:

¹⁹ DISP refers to the Dispute Resolution section of the FCA Handbook

- DISP 1 (Treating Customers Fairly), except
 - DISP 1.9 (Complaints record rule)
 - DISP 1.10 (Complaints reporting rules)
 - DISP 1.10a (Complaints data publication rules) and
 - DISP 1.11 (Lloyd's)
- DISP 2 (Jurisdiction of the Financial Ombudsman) except
 - DISP 2.3 (Compulsory Jurisdiction)
- DISP 3 (Complaint handling procedures of the Financial Ombudsman Service)

Additionally, Bothnia has agreed that FOS maintains the same powers to make determinations and awards under the voluntary jurisdiction as under the compulsory jurisdiction (DISP 4.2.4) and, under both the compulsory jurisdiction (DISP 3.7.13) and the voluntary jurisdiction (DISP 4.2.5), awards made by FOS may be enforced through the courts. I understand that, in practice, such a situation has not arisen to date and I consider the likelihood of this occurring with respect to the Transfers to be remote.

Under the rules governing FOS's voluntary jurisdiction, there is scope for participants to withdraw. The process for withdrawing is set out in DISP 4.2.7 and requires that:

- The voluntary jurisdiction participant has submitted to FOS Ltd a written plan for:
 - Notifying its existing customers of its intention to withdraw and
 - Handling complaints against it before its withdrawal
- The voluntary jurisdiction participant has paid the general levy for the year in which it withdraws and any other fees payable and
- FOS Ltd has approved in writing both the voluntary jurisdiction participant's plan and the date of the withdrawal (which must be at least six months from the date of the approval of the plan)

In the event that Bothnia were to withdraw their participation from voluntary jurisdiction, having had the withdrawal plan approved by FOS, any Transferring Policyholder seeking redress would have to go through the Finnish Financial Ombudsman Bureau ("FINE").

FINE handles disputes in which one of the parties is a financial service provider established in Finland (i.e. Bothnia), having a branch or subsidiary in Finland or which has agreed to submit to FINE's jurisdiction. FINE and FOS are both members of the Financial Dispute Resolution Network (FIN-NET), a European wide collaboration of financial ombudsman schemes designed to improve cross border collaboration and assist claimants in contacting the correct ombudsman. When entering this agreement, ombudsman schemes need to prove that they comply with certain minimum standards. Upon reviewing a complaint, the FINE Boards will issue a recommendation to the financial service provider being examined. According to FINE the financial sector generally complies with the recommendations given, and according to FINE's 2014 and 2015 annual reports up to 99% of recommendations were complied with. Although the awards are issued in the form of recommendations, non-compliance would result in significant bad-will in the market and within the supervising authorities.

Given all of the above I do not consider it likely that there will be any material change to the rights of policyholders of AMIL and AMIC-UK to bring complaints to FOS pre- and post-Transfer. Additionally, given the nature of the Transfer and the communication I have had with the Parties, as well as the historically high level of market compliance with FINE's recommendations, I do not consider the possibility of a change in ombudsman to be materially disadvantageous to the Transferring Policyholders.

With respect to the existing Bothnia policyholders, FINE provides a complaints service in respect of Finnish policyholders. I am satisfied that there will be no effect on the ability of any policyholders to bring their complaints under their respective existing ombudsman facilities.

I have further commented on the consumer protection services and standards provided in Finland in Appendix 5.

8.7 **Maintenance of records under the Employers' Liability Tracing Office ("ELTO")**

The FCA's Insurance: Conduct of Business sourcebook ("ICOBS") requires insurers underwriting employers' liability business to maintain a searchable register including details of employers' liability policies underwritten or renewed after 1 April 2011, and details of any employers' liability policy under which a claim has been made after that date. Insurers may comply with these obligations by becoming a member of the Employers Liability Tracing Office ("ELTO"), which maintains an electronic

database of members' new and renewed employers' liability policies (the "ELTO Database").

The ELTO Database facilitates the identification of Employers' Liability insurers. Its primary purpose is to assist victims of workplace negligence and their advisors in the pursuit of compensation against former employers.

I have discussed this matter with senior representatives of Compre Services who provide administrative services to Bothnia, with senior function holders of AMIL and AMIC-UK and the representatives of AMIC-ILQ. Compre Services supplies information to ELTO according to Bothnia's requirements and is familiar with the process. Willkie Farr have, on behalf of AMIL and AMIC-UK, entered data to ELTO in respect of the majority of the potentially exposed contracts and have advised the Compre Group of the progress that has been made. I have been advised that Compre Services will complete the loading of ELTO information as required Post-Transfers.

8.8 Guarantees to third parties and funds held in trust

I have confirmed with the senior function holders of the Parties that neither of the Transferors, nor the Transferee has any guarantee commitments or funds held in trust relating to the business subject to the Transfers.

8.9 Implications of the Transfer for policyholders in different jurisdictions

I have reviewed the policy register provided in respect of AMIL and AMIC-UK and I have not identified any contracts falling outside of the EEA.

8.10 Tax implications of the Transfers

I have discussed the tax implications of the Transfers on Bothnia with the Chief Financial Officer of the Compre Group. He has advised me that he does not foresee any additional tax impact arising for Bothnia as a consequence of the Transfers; he has arrived at this conclusion following his consideration of the fact that the economic result of the Transfers has been realised in Bothnia in 2014 following the establishment of the Whole Account Quota Share Agreement. Based on this opinion, and since the financial statements have been subjected to statutory audit at year end 2014, 2015 and 2016 and no tax issues were identified, I am satisfied that the Transfers have no impact on the tax position of Bothnia and I did not consider it necessary to obtain external tax advice.

I have been provided with a letter from NYLB's Chief Financial Officer which summarised the advice obtained by the NYLB from its tax advisors and their Finance Department regarding the potential tax implications to AMIL, AMIC-UK or AMIC-ILQ arising from the Transfers. The advice that has been received is that there are no tax implications arising.

8.11 Considerations regarding the impact of insolvency of the Parties

Within this section I have compared the relative priorities of creditors in the event of a winding-up under the UK and Finnish regimes in order to form a view as to whether policyholders of the Transferors or of the Transferee are materially disadvantaged as a result of the change from UK to Finnish regulation. Within this context, I have also examined the effect of the Transfers on the direct and reinsurance policyholders of Bothnia should it become insolvent.

I have also considered the likely circumstances to which policyholders of the Transferors would be exposed should the Transfers not succeed. This is because the Transfers form part of the wider chain of events relating to the liquidation of AMIC-ILQ. In Appendix 9 I have included a synopsis of the liquidation process and creditor priority order under US law as applicable to AMIC-ILQ - the synopsis was provided to me by the NYLB.

Comparative analysis of creditor priorities under the Finnish and UK regimes

In the UK, the winding up of an insurance undertaking is governed by the Insurers (Reorganisation and Winding Up) Regulations 2004 ("the Winding up Regulations"). Under these regulations, insurance claims take precedence over other claims on the insurance undertaking with the exception of certain preferential claims (e.g. claims by employees, rights in rem) with respect to the whole of the insurance undertaking's assets. Therefore, direct policyholders have equivalent rank and rank above inwards reinsurance policyholders and all other unsecured/non-preferential creditors in the event that an insurer is wound up.

Under Finnish winding up rules, private customers are afforded preferential treatment over other creditors. The winding up and liquidation rules are stipulated in the Finnish Insurance Companies Act and the legal advice that I have obtained with respect to the priority ranking of creditors is summarised, in order, as:

- Administrative expenses incurred after the bankruptcy, including wages (referred to as "mass-debts")

- Certain secured debts (holders of real estate mortgages)
- Policyholders' claims (and holders of chattel mortgage)
- Other secured debts
- Unsecured debts (including, inter alia, taxes and wage expenses incurred before the bankruptcy)
- Claims of low preference (including, inter alia, tax penalties and certain other sanctions imposed by authorities)
- Preference shareholders
- Equity shareholders

Based on my understanding of the comparative priorities of the different classes of creditors, I do not consider the treatments under Finnish versus UK practice to materially disadvantage any Transferring Policyholders as a result of the Transfers and this aspect does not affect my conclusion.

Should Bothnia become insolvent then, prior to the Transfers, Bothnia's direct policyholders rank above Bothnia's reinsurance policyholders (which include AMIL and AMIC-UK). Following the Transfers, the direct policyholders of AMIL and AMIC-UK become direct policyholders of Bothnia and will rank equally with existing direct policyholders of Bothnia and above reinsurance policyholders of Bothnia.

This change would represent a marginal worsening in the position, post-insolvency, of Bothnia's existing direct and reinsurance policyholders; however, given the scale of the Transfers when compared to Bothnia's existing liabilities, I consider any disadvantage to not be material.

Considerations of the potential effect of the US liquidation procedure

Since both AMIL and AMIC-UK are associated with AMIC-ILQ, which is subject to US liquidation proceedings, I have considered the likely impact on policyholders of AMIC-UK and AMIL of the liquidation should the proposed Transfers not proceed.

AMIL, as a separately capitalised UK subsidiary is governed by the Winding up Regulations should it become subject to winding up. Policyholders of AMIL are

therefore not directly subject to the outcome of the liquidation proceedings of AMIC-ILQ.

AMIC-UK, as a UK branch of an insurance undertaking which is headquartered outside of the EU, is also subject to the Winding up Regulations. However its treatment under a liquidation may differ from that of AMIL. I have summarised the procedure and alternative outcomes below:

- Where a non-EU insurance undertaking is in liquidation in its country of incorporation, a winding-up order can be made in England in respect of the UK branch of that company. Such an order will be an “ancillary” liquidation which will run in parallel to the main liquidation proceedings in the foreign country.
- The English court has discretion to order an ancillary winding-up and whether it chooses to make such an order or not depends on all of the facts at the relevant time.
- Instead of ordering an ancillary winding-up, the English court may decide that it is more appropriate to recognise the authority of the foreign liquidator to deal with the UK branch’s assets and creditors in England.
- If an ancillary winding-up order is made, then the Winding up Regulations will apply as if it were a UK insurer but the powers of the English liquidator may be limited by the court to collecting in the assets of the UK branch located within England. Once the English assets have been collected in they will be remitted to the foreign liquidator for distribution to all of the company’s creditors in accordance with foreign law.
- Alternatively, if the foreign and the UK liquidators agree that, on the facts, it would be best for each liquidator to distribute to creditors in accordance with the relevant foreign and UK laws, then such conduct can be authorised by the English court.
- If distributions are made to creditors in accordance with UK law then the priority of payments under the Winding up Regulations will apply.

Based on my evaluation of the liquidation procedures applicable to AMIL and AMIC-UK, I consider AMIL policyholders likely to be unaffected directly by the liquidation of AMIC-ILQ. Since the US liquidation rules can be applied to AMIC-UK, it is more likely to be included within the liquidation process of AMIC-ILQ as this route is potentially the least costly and therefore most beneficial to the estate of AMIC-ILQ.

8.12 Policyholder communication strategy

The Parties have set out the following strategy with respect to publicising the Transfers:

- Letters have been drafted which set out the purpose of the Transfers. The letters identify the Parties and give guidance on the action to be taken should the addressee have concerns over the Transfers. It is proposed that the letters will be sent to:
 - Direct policyholders of AMIL and AMIC-UK, for whom address details are available
 - Reinsurance policyholders of AMIC-UK, for whom address details are available
 - Reinsurers of AMIL and AMIC-UK who are subject to the Transfer
 - Insurance brokers to AMIL and AMIC-UK
- The Transfers are to be advertised in the London, Edinburgh and Belfast Gazettes and in the Times and Insurance Day. The Compré Group will establish a website onto which the scheme document, notices, the IE Report and the IE supplementary report will be available until the effective date of the Transfer. FIN-FSA have advised Bothnia that they do not require Bothnia to publish notice of the Transfers in the Finnish press.

The Parties intend to request the Court to grant waivers from the following requirements:

- With respect to notifying the policyholders and cedants of AMIL and AMIC-UK, it is proposed to send individual correspondence only to those policyholders and cedants for whom contact details are available
- With respect to publicity in EEA states, other than Finland and the UK it is proposed that public notices are waived.
- With respect to notifying the existing policyholders of Bothnia, it is proposed that no individual policyholder notifications are issued.

The above waivers are sought on the basis that the costs of publicity are disproportionate to the likely benefits to affected parties. Additionally, for Bothnia, the existing policyholders are already exposed to the risks arising in respect of the AMIL and AMIC-UK portfolios as a result of the existing whole account quota share reinsurance provided by Bothnia.

As noted above, the Transfers are to be advertised in the London, Edinburgh and Belfast Gazettes and in the Times and Insurance Day. On the grounds that Insurance Day may not fall into the category of national newspaper, the Parties also intend to request the Court to grant a formal waiver from the requirement that notice be published in two national newspapers. The Parties also intend to request a waiver from the requirement to formally send a notification to Bothnia, which is technically a third-party reinsurer whose reinsurance contract is to be transferred under the scheme, because Bothnia is already aware of the scheme and the content of the notice by virtue of it being the Transferee under the scheme.

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

8.13 **The impact of the UK EU Referendum result**

On 23 June 2016, the UK held a referendum and voted to leave the EU (“Brexit”).

The process to leave the EU is governed by Article 50 of the Treaty of Lisbon. The Article 50 process was triggered on 29 March 2017 meaning that the UK is scheduled to leave the EU on or before 29 March 2019. As part of the Brexit process the UK will be required to renegotiate its treaties with each of the member nations of the EU. Brexit and the subsequent renegotiation may lead to changes in UK law although it seems likely that certain elements of EU legislation will be incorporated into UK law. With respect to EU directives and regulations relating to insurance companies, the UK played a prominent role in the development and implementation of Solvency II and insurance entities supervised by the PRA have been subject to Solvency II since 1 January 2016. Since the financial services sector represents a significant proportion of the UK economy and the City of London would wish to maintain its pre-eminent position as a financial centre it seems reasonable to assume that the UK will seek to maintain an equivalence with Solvency II going forwards. Also, the principles of risk based capital which are embodied within Solvency II are being widely adopted in many jurisdictions world-wide which would further suggest that, if the UK is to remain a significant participant in the global financial services market, it is unlikely to take a stance on insurance regulation materially different to Solvency II.

The eventual impact of Brexit is highly uncertain. However the Transferee will remain in the EU and this means that post-Transfers the policyholders of both AMIL and AMIC-UK will experience continuity with respect to the regulatory

capital requirement regime to which they are currently subject and as such are immunised from any changes which Brexit may produce should the UK eventually leave the EU.

An important facet of the Brexit negotiation will be the extent to which UK financial services entities may offer services on a cross-border basis in the EU and likewise the extent to which EU entities may offer services in the UK. I note in paragraph 5.17 that Compré Services has responsibility for the administration of the Bothnia portfolio and that this includes a UK service company, these services are of an administrative and advisory nature, are not regulated activities and are expected to continue to be offered following the UK's exit from the EU. Post-Transfers, managing and paying a UK claim would be considered a regulated activity taking place in the UK, this means that the post-Brexit regime would need to allow EEA insurers with UK policies to manage such claims. While the eventual outcome of Brexit cannot be predicted with complete accuracy, it is reasonable to assume that an acceptable mechanism to fulfil such pre-existing cross-border contractual obligations will form a significant aspect of the Brexit negotiation.

The Transferors are in run-off and the Transferee operates portfolios in run-off and so no issues arise in relation to cross-border selling. I am not aware of any reason why the enforceability of any existing contract relating to the Transferring Business would be affected by Brexit.

I note again that the final result of Brexit is highly uncertain. However based on my consideration of the Pre- and Post- Brexit regulatory capital requirement and the effect of cross-border provision of services, it appears highly unlikely that Brexit of itself will have an adverse impact on the Parties.

9. OPINION

9.1 Based on:

- The level of security provided by Bothnia
- The fact that Bothnia is already exposed to the claims of AMIL and AMIC-UK through the whole account quota share reinsurance arrangement, leading to no net economic impact on Bothnia
- The fact that there is no material change in the administration of the business
- The overall improvement in the system of control and governance afforded the affected policyholders of AMIL and AMIC-UK
- The fact that the Transfers meet the objectives of the NYLB in connection with its management of AMIC-ILQ and its creditors and policyholder liabilities

I have reached the opinion that the security of the transferring AMIL and AMIC-UK policyholders, and the existing policyholders of Bothnia, will not be adversely affected by the Transfers and that the Transfers will not adversely affect the service levels provided to any of those groups of policyholders. I have also reached the conclusion that there is no material adverse effect on the policyholders and creditors of AMIC-ILQ nor on the reinsurers of the Transferors.



Dewi James FIA
Moore Stephens LLP

16 October 2017

Appendix 1 - Professional experience D James

Dewi James

Fellow of the Institute and Faculty of Actuaries, qualified 1988. Practising Certificate holder for Lloyd's Statements of Actuarial Opinions.

Work experience

1980 – 1983	Government Actuary's Department – Insurance supervision
1983 – 1984	Anglo American Life – 1 year running a small pensions unit in Johannesburg
1983 – 1985	Mercer life and pensions
1985 – 1988	Sturge Lloyd's Agent reserving, syndicate planning and establishment , reinsurance security assessment
1988 – 1992	Ernst & Young wide range of consulting assignments
1992 – 1995	Alexander Howden – took over Clay & Partners (actuarial consultancy). Various reserving and pricing assignments
1995 – 2001	Zurich Insurance - corporate / chief actuary Zurich Re (UK), chief actuary Turegum, chief actuary CMGL, pricing actuary and chief actuary for Zurich Global Energy (London / Europe).
2001 – 2017	Set up James, Brennan & Associates . Assignments include : <ul style="list-style-type: none"> • A project intended to offer a solution to the LMX property Catastrophe spiral claims • Various reserve reviews and investigations of Lloyd's syndicates • US Statements of Actuarial opinion for London companies, part of the NAIC returns • Various London market and mass market pricing analyses • Joint venture to develop a Dynamic Financial Analysis and statistical simulation package and other technical software • Various pricing work and other financial modelling in the London market • FSA reporting expert for portfolio transfers under the UK Financial Services and Markets Act, 2000 • Independent vote valuer on solvent schemes of arrangement and claims adjudicator on solvent schemes • ICA, Internal and Partial internal financial modelling for a number of entities
2017 -	Moore Stephens LLP – appointed Head of Actuarial Practice

Various publications and presentations – most relevant are

Books:

“Modern Actuarial Theory and Practice” published 2000, 2004 (2nd edition)

“Part VII Transfers a practical guide” published 2007

For 2 years gave an actuarial course in Bratislava Economics University

Presented 10 week lecture series on general insurance at City University London

August 2005 – Reinsurance Summer School presentation on Dynamic Financial Analysis

Other research etc. on:

- US Savings and Loans,
- US legal system working party,
- Member of ABI commutations working party (2001),
- Mitigation of reinsurance credit risk using debt assignment and set-off
- Financial structures for commutation deals

Appendix 2 - Professional experience M Ruohonen

Matti Juhani Ruohonen

Qualified Actuary, 1984, granted by the Finnish Ministry of Social Affairs and Health
Ph. D., University of Turku, 1976

Work experience

1979 – 1980	University of Vaasa - associate professor of statistics
1980 – 1983	University of Turku - associate professor of applied mathematics
1984 – 2001	Sampo Insurance Group – various responsibilities including Corporate development, Actuarial department controller Member of the management team of the Sampo group Chief actuary of Sampo Mutual Insurance Company (Non-Life)
2001 - 2007	Veritas life insurance Company Ltd Managing director Veritas reinsurance Company Ltd Managing director Member of the management team of Veritas Group
2007	Aktia Savings Bank – senior advisor
2009 – 2013	Finnish Ministry of Social Affairs and Health - secretary to two working groups focused on the implementation of Solvency II into the Finnish regulatory environment
2008 –	Fennia Life Insurance Company Ltd – vice chairman of the board Blue White Alternative Investments Ltd – board member
2014 -	Finnish Mutual Insurance Company for Pharmaceutical Injury Insurance – board member

Other relevant experience

Chairman of the Actuarial Association of Finland from 1991 – 1996

Member of the IAA Council 1991 – 1996

Chairman of the Finnish Insurance Association 2002 – 2008

Appendix 3 - Schedule of key information provided

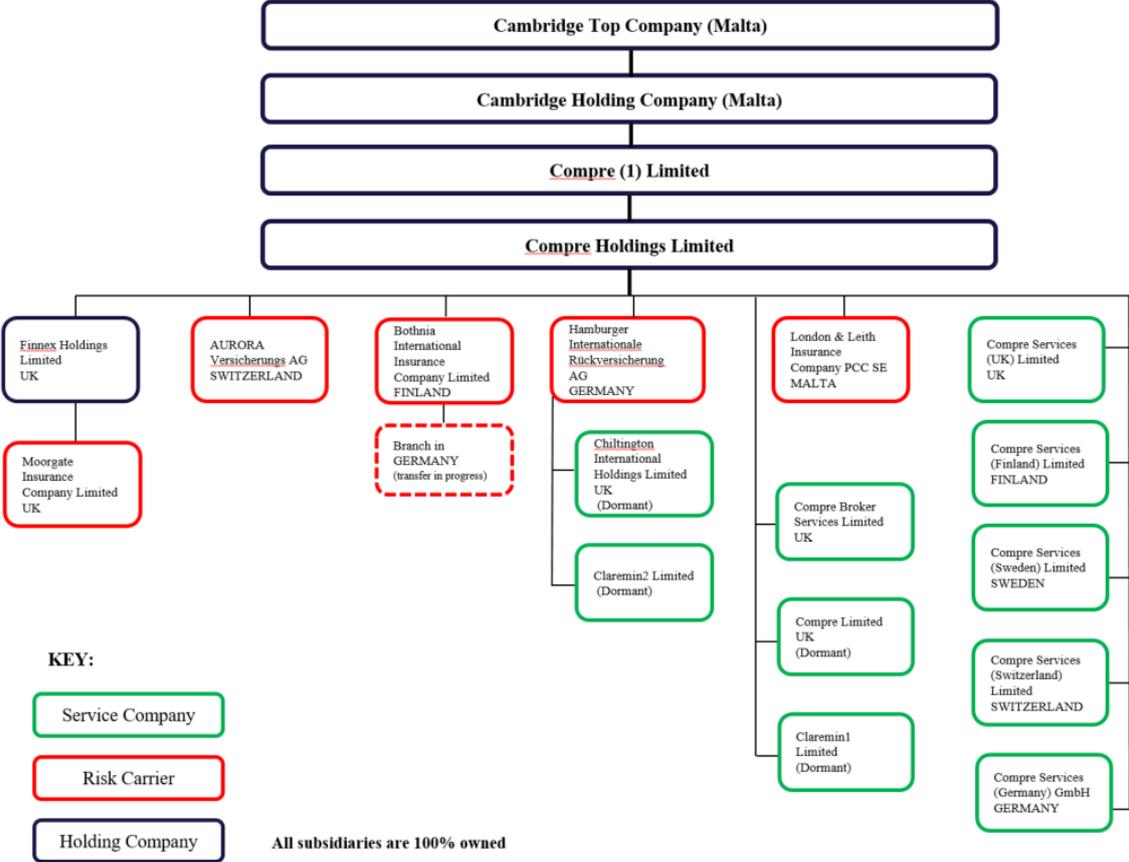
Financial statements

- Bothnia financial statements as at 31 December 2016
- AMIL financial statement as at 31 December 2016 (unaudited)
- AMIC-ILQ financial statements as at 31 December 2016 (unaudited)
- AMIC-UK financial statement as at 31 December 2016 (unaudited)

Other items

- AMIC Certificate of completion of the WFUM scheme
- Policy registers - AMIL and AMIC-UK
- 2014 Solvency II implementation plan - Bothnia
- Bothnia Solvency II Standard Formula regulatory capital requirement calculation as at 31 December 2016
- Bothnia Solvency II regulatory balance sheet as at 31 December 2016 with reconciliation to the statutory accounts
- Bothnia external actuarial reserve review as at 31 December 2012 (issued November 2013)
- Bothnia external actuarial reserve review as at December 2013, December 2014 and December 2016
- Bothnia ORSA reviews as at December 2014, December 2015 and June 2016
- Correspondence relating to the intimation of a deafness claim against AMIL
- Compré Group structure chart
- Deed of charge relating to funds withheld by AMIL in respect of the Bothnia whole account quota share reinsurance
- Amended quota share reinsurance agreement between AMIL, AMIC-UK and Bothnia
- Loan agreement between Bothnia and Compré Holdings Ltd
- Witness statements of Kari Maki, Jon Lloyd, Scott Fischer and Ted Coopersmith
- Draft communication notices of the proposed Transfers addressed to policyholders of AMIC-UK, policyholders of AMIL, reinsurers of AMIL and AMIC-UK
- Bothnia policyholder and waiver proposal
- Summaries of the UK and Finnish legal and regulatory frameworks, prepared by the Parties' respective legal advisors
- Compré Group capital management policy
- Compré internal due-diligence evaluation report on RFP
- Compré internal actuarial comparative analysis of regulatory surplus pre/post RFP
- Independent External Actuarial review of RFP
- Compré internal due-diligence evaluation report on Gibbon
- Compré high level due-diligence evaluation on the Swiss Re and AG elements of Gibbon
- Bothnia internal actuarial reserve review as at 31 December 2016
- Bothnia Solvency II report as at 31 December 2016
- Bothnia Solvency II Quantitative Reporting Template as at 31 December 2016

Appendix 4 – Compre Group structure chart



Appendix 5 – A brief overview of insurance customer protection in Finland

Legislation

The Insurance Companies Act regulates the insurance industry in Finland. It has been renewed on implementation of the Solvency II regulation into Finnish legislation. The Solvency II Directive is embedded in the Finnish Insurance Companies Act. The amendments took effect on 1 January 2016 and concurrently, the Delegated Acts, EIOPA Rules and Recommendations came into force.

Finland has maintained its requirement for equalisation provisions, which has been in use since the early 1950s. This system is meant to enhance the solvency of insurance companies and to protect the policyholders and claimants. Under Solvency II however, Finnish Equalisation provisions will generally be accepted as Tier 1 capital.

From 1 January 2016 the Finnish regulatory framework is the same as in the EU.

Customer protection is a major focus of the Finnish Insurance Contracts Act. This legislation regulates the contents of insurance contracts and the information to be given by the insurer to the policyholder. One of the key paragraphs is Chapter 2 Section 9 that states that “If the insurer or its representative has failed to provide necessary information or has given incorrect or misleading information to the policyholder when marketing the insurance, the insurance contract is considered to be in force to the effect understood by the policyholder on the basis of the information given.” The basis enforcing drafting in favour of the customer exists in the Finnish insurance sector and has not yet been extended to the banking sector.

Authorities and advisory bodies

The supervising authority in Finland is the Financial Supervising Authority (FIN-FSA). It is the authority that licences undertakings to underwrite insurance business in Finland and which gives consent to portfolio transfers. FIN-FSA supervises the service providers’ code of conduct and the legality and sound practice of contractual terms in policy wording, marketing and other contacts with customers.

Policyholder protection in Finland has been addressed through high solvency requirements (including the equalisation provisions) and through the practice of requiring that distressed companies be merged with stronger entities. In Finland the policyholders do not have a similar scheme as the Deposit Guarantee Fund for the banks.

Finland operates a special authority to help dissatisfied customers of insurance industry. The customer may turn to the Financial Ombudsman Bureau (FINE). The bureau provides information and advice to insurance company customers and handles disputes on behalf of the customer with the insurance company concerned. Disputes may be handled by a court of law, or by the Insurance Complaints Board. The board examines disputes related to insurance relationship as well as to the interpretation of legislation and insurance terms and conditions. The board does not examine any issues related to statutory insurance such as worker’s compensation (i.e. employers’ liability). For this purpose there is separate body

called the Employment Accidents Appeal Board. The Insurance Complaints Board will not take up any issues concerning foreign insurance companies with no branch office in Finland.

In addition to insurance specific bodies, Finland operates a more general mechanism to raise complaints through the Consumer Ombudsman or Consumer Disputes Board who are also empowered to pursue insurance related cases on behalf of claimants and policyholders.

Employers' liability

Worker's compensation insurance has its own special rules. There is a joint liability of all companies underwriting this insurance. It is explicitly stated in the Employment Accidents Insurance Act Chapter 3 Section 38c that "If the liability for compulsory insurance under this Act remains in part or altogether unsecured because of liquidation or bankruptcy of the insurance company after the policyholders' duty to pay supplementary premiums is implemented, the insurance companies underwriting said insurance are jointly accountable for the liability or part of it."

In the event of liquidation or bankruptcy of a Finnish insurance company, the Federation of Accident Insurance Institutions sees to compensation payments after the insurance portfolio and the corresponding assets have been transferred to the Federation.

Liquidation and bankruptcy

In case of liquidation and bankruptcy there is a special protection for private customers. This is regulated in the Insurance Companies Act. The receivables of private customers have a preference over other receivables. It is stated that the private person's receivables have the same preference as a holder of a chattel mortgage.

Appendix 6 – Summary structure chart of the reinsurance programme for AMIL

Atlantic Mutual International Limited.

Property Reinsurance structure before Transfer

Property Catastrophe Excess of Loss for AMIC-ILQ, AMIL, CIC,ASIC USD 150m xs \$20m for each occurrence Provided by Open Market		
Property Per Risk Excess of Loss for AMIC-ILQ, AMIL, CIC,ASIC USD 47.5m xs \$2.5m Provided by Open Market		
AMIL has a USD \$4M Stop Loss over all accounts provided by AMIC-ILQ		
Property Buffer R/I provided by AMIC-ILQ Difference between GBP 1m and USD 2.5m		
65% Property GBP1m QS R/I to Open Market	20% Property GBP 1m QS R/I to AMIC-ILQ	AMIL 15% Retention on Property
Specific Reinsurances of individual acceptances R/I to the Open Market.		

Property – Terrorism

Property Terrorism Excess of Loss for AMIC-ILQ, AMIL, CIC,ASIC USD 47.5m xs \$2.5m Provided by Open Market

Workers Compensation Act

WCA Excess of Loss for AMIC-ILQ, AMIL, CIC,ASIC USD 40m xs \$10m Provided by Open Market

Casualty

Casualty Excess of Loss for AMIC-ILQ, AMIL, CIC,ASIC USD 40m xs \$10m Provided by Open Market	
AMIL has a USD 4M Stop Loss over all accounts provided by AMIC-ILQ	
90% Casualty Quota Share USD1m or GBP 666.667 for AMIL provided by AMIC-ILQ	10% AMIL retention

Notes :

- | |
|------------------------|
| Transferring contracts |
|------------------------|
- Property-terrorism, Workers Compensation Act and Casualty reinsurance programmes are not being transferred
- CIC = Centennial Insurance Company (insolvent)
- ASIC = Atlantic Specialty Insurance Company
- AMIL, CIC and ASIC are subsidiaries of AMIC-ILQ

Appendix 7 – A brief comparison of insurance regulations in the UK and Finland

I obtained legal advice from separate firms in the UK (Willkie Farr & Gallagher (UK) LLP) and in Finland (Krogerus) which outlines the regulatory environments in the UK and Finland respectively. Appendix 7.1 reproduces the memorandum provided by Willkie Farr & Gallagher (UK) LLP and Appendix 7.2 reproduces the memorandum provided by Krogerus.

I have summarised the relative merits of the two systems below under the major headings of:

- Prudential Regulations
- Conduct of business
- Complaints handling
- Supervisory intervention
- Approval of controllers of a regulated entity
- Process for rejecting claims

Prudential Regulations

As a result of the change in jurisdiction prudential regulation over the policies will transfer from the PRA to the FIN-FSA. Both of these bodies operate within the EEA and there is a high degree of parity between the two systems (as indicated in paragraph 8.1). The degree of convergence has increased under the Delegated Acts which are being adopted with the implementation of Solvency II.

Conduct of Business Issues

Both the UK and Finnish regulators publish a set of rules and “Best Practices” setting out codes of expected conduct. In the UK the FCA applies ICOBS to the direct contracts of insurance written by AMIL and AMIC-UK. The high level rules that insurers must follow are that claims must be handled promptly and fairly, reasonable guidance must be provided to a policyholder to help them make a claim, no claim can be unreasonably rejected and claims must be settled promptly when terms are agreed.

In Finland good insurance practice is not defined to the level of detail set out in ICOBS; however the FIN-FSA has been vested with the power to enforce correct practices to ensure that insurance companies within its jurisdiction comply with not only the rules regarding insurance, but also that any conduct which is contrary to good insurance practice or otherwise unfair towards the policyholder is not practiced.

Complaints Handling

As AMIL and AMIC-UK are in run-off, having no infrastructure of their own, they do not have a separate complaints handling department. Bothnia is compliant with EIOPA’s Guidelines of Complaints Handling by Insurance Undertakings (EIOPA-BoS-12/069). Any complaints which cannot be handled internally can be referred to the respective financial ombudsman, FOS in the UK and FINE in Finland. Given Bothnia’s submission to FOS’s voluntary jurisdiction there will be no material change in the ability of AMIL and AMIC-UK policyholders to bring complaints to FOS and so there will be no noticeable change in the complaints handling procedure pre- and post-Transfer.

Supervisory Intervention

In both the UK and Finland regulators have been provided with a number of supervisory tools with which to implement their respective regulatory powers. There is a high degree of parity between the two systems, both providing the regulatory authorities with the ability to impose fines, demand inspections or reviews, orders to cease underwriting or withdraw authorisation. In both territories these powers are defined by clear and well documented Acts.

Approval of Controllers of a Regulated Entity

Both the UK and Finnish regimes are subject to European legislation regarding the approval of Controllers. In both cases Board Members and persons in a comparable position are subject to a suitability assessment in accordance with the Solvency II Directive (Fit and Proper).

Process for Rejecting Claims

Both the UK and Finland have strict guidelines relating to the process for rejecting a claim. In the UK these are included within ICOBS and stipulate that a rejection is unreasonable except where there is evidence of fraud, through breach of contract, non-disclosure of relevant information or otherwise.

In Finland the process is set out in the Insurance Contracts Act (543/1994), which similarly limits the rejection of a claim to incidences where there has been fraud and requires that the reasons for the rejection must be provided to the policyholder in writing.

In both cases, if the policyholder feels their claim has been unfairly rejected they may bring a complaint to the relevant ombudsman for arbitration.

Appendix 7.1 – A brief synopsis of insurance regulations in the UK

WILLKIE FARR & GALLAGHER_{(UK) LLP}

MEMORANDUM

TO: Dewi James, Independent Expert, Moore Stephens LLP

FROM: Nick Bugler, Willkie Farr & Gallagher (UK) LLP

RE: UK Insurance Regulation

DATED: 13 July 2017

This memorandum sets out a high level overview of some of the key aspects of UK Insurance Regulation. You are the Independent Expert to the proposed insurance business transfer schemes of Atlantic Mutual Insurance Company's UK branch (AMIC UK) and Atlantic Mutual Insurance Limited (AMIL) (together, the "Atlantic companies") pursuant to which portfolios of insurance contracts will be transferred to Bothnia International in Finland. You have been asked to consider the respective insurance regulatory regimes in the UK and Finland in the context of the proposed insurance business transfers and the impact on policyholders and other stakeholders of the transfers from insurers subject to the UK regulatory regime to an insurer that is subject to the Finnish regulatory regime. This memorandum is intended to assist you in assessment.

Prudential Regulation

AMIL is subject to the prudential regulation of the Prudential Regulation Authority (PRA). AMIL has informed the PRA that it is applying the Transitional Provisions under Title VI of the Solvency II Directive (the "Transitional Provisions"). This means that the PRA is obliged to ensure that the minimum solvency requirements that are set out in the Solvency I Directives are applied to AMIL. While Titles I, II and III of the Solvency II directive will not apply to AMIL for as long as it avails of the Transitional Provisions, AMIL remains subject to Titles IV, V and VI of the Solvency II Directive. Prudential regulation is also applied to the UK branch of AMIC purely in relation to the business that was conducted through that branch. These are minimum standards that would apply across the European Economic Area. AMIC UK is unable to avail of the Transitional Provisions and is subject to the entirety of the Solvency II directive as it has been implemented into UK law and regulation. AMIC UK is therefore obliged to comply with Solvency II minimum solvency requirements.

Conduct of Business Issues

In the UK, conduct of business regulation is set out in the Insurance Conduct of Business (ICOBS) module of the FCA's rulebook. Conduct of business rules apply to the carrying on of the business of effecting or carrying out contracts of insurance, amongst other things, by a firm from an establishment in the UK. Therefore it would apply to the Atlantic companies. However, it does not apply to contracts of reinsurance. As the Atlantic companies are in run-off and have been for many years, the most relevant rules in ICOBS are contained in Chapter 8 on claims handling. The high level rules that insurers must follow are that the insurer must:

- handle claims promptly and fairly;
- provide reasonable guidance to help the policyholder make a claim and appropriate information on its progress;
- not unreasonably reject a claim (including by terminating or voiding a policy); and
- settle claims promptly once settlement terms are agreed.

There are further rules concerning what constitutes an unreasonable rejection of a claim for a policyholder who is a consumer, which reflect changes to the law introduced by the Consumer Insurance (Disclosure and Representations) Act 2012. Basically, these rules modify the common law remedies that an insurer may have to avoid or terminate a policy where there have been misrepresentations or non-disclosure or a breach of warranty. The modifications in ICOBS cut back the insurer's ability to avoid claims on ground of non-disclosure when it was not reasonable to expect the policyholder to make a disclosure or on the grounds of misrepresentation when that misrepresentation was not negligent. The common law right of an insurer to avoid a claim on the grounds of any breach of warranty is also modified such that it would not be reasonable to avoid the claim if the breach of warranty did not relate to the claim.

There are also rules concerning motor insurance but these will not be applicable to the Atlantic companies as they do not write motor insurance.

In relation to employers' liability insurance, there is an obligation on firms to ensure the requisite information regarding employers' liability is put on to an Employers' Liability Register. This is an aid to potential claimants who need to trace insurance policy covering an employer under which a claim for employers' liability may be made. This does apply to companies in run-off and does apply to the Atlantic companies.

As regards the common law position, the starting point will be to examine the terms of the contract regarding the procedure for a policyholder to make a claim. The issues for the insurer will be to assess whether or not a claim is within the terms of the coverage of the policy and, if so, what is the quantum of the claim that the policyholder is entitled to receive.

Other than for consumer contracts, insurers may have grounds for voiding a policy if, for example, there has been non-disclosure, misrepresentation or a breach of warranty. These rights will be available to reinsurers but for insurers these rights are modified as described above in relation to policies issued to consumers.

There is a general overlay under the PRA and FCA rules with relation to the principles for business. These require authorised firms in the UK, amongst other things, to treat customers fairly, and to ensure that they manage any potential conflicts of interest that might arise.

The Insurance Act 2015 came into force in the UK on August 12, 2016 and is a major reform to UK insurance contract law. The Atlantic companies will generally be unaffected by the new regime which impacts upon contracts of insurance entered into on or after 12 August 2016, long after the Atlantic companies stopped writing business.

Complaints Handling

The Atlantic companies, being in run-off and having no infrastructure of their own, do not have a separate complaints handling department. However, if a claim were to be rejected, then a policyholder would be entitled to take a claim to the Financial Ombudsman Service, as these companies are within the compulsory jurisdiction of FOS.

Supervisory Intervention

Regulators in the UK have a variety of tools at their disposal in relation to companies they supervise. For example, they can request expert reports into a particular matter of a company. They could require a company not to take action without notifying or obtaining consent from the regulators. They could take disciplinary or enforcement action in relation to breaches of their rules which could result in censures or fines, or indeed banning orders in relation to individuals. They could require companies to cease underwriting and ultimately they could withdraw authorization. They can give capital guidance which effectively requires insurers to ensure that they have sufficient capital to meet the guidance.

Approval of Controller of a Regulated Entity

As part of the prudential supervision of insurance companies, a person who is deemed to be a controller of such company is subject to approval of the regulators. This requirement derives from European legislation known as the Acquisitions Directive and will be the same across the Member States of the European Economic Area. Broadly speaking, any person who has 10% shareholding or 10% voting power in an insurance or reinsurance company or in its parent company will be required to be approved prior to obtaining that interest.

Nick Bugler

Willkie Farr & Gallagher (UK) LLP

Appendix 7.2 – A brief synopsis of insurance regulations in Finland

Krogerus

MEMORANDUM

To: Vakuutusosakeyhtiö Bothnia International ('Bothnia')
From: Sami Martola, Tuulia Tanskanen
Date: 11 November 2015
Subject: Brief description of the Finnish insurance regulatory scheme in connection with Project Olympic

1. Assignment

Bothnia has asked Krogerus to draft a brief and non-exhaustive summary of the key regulations concerning insurance business in Finland. The purpose of this memorandum is to provide background information when assessing the impact of a planned insurance portfolio transfer from the UK to Finland. The memorandum focuses on topics relevant to the transaction at hand and regulatory issues which are most likely to differ in the two countries.

2. Prudential Regulation

On a general level it can be stated that the majority of Finnish insurance regulation is based on EU law. In addition the Finnish prudential regulation of insurance companies is based on the harmonised framework for insurance companies in the EU. The Solvency II Directive²⁰ has been implemented into Finnish legislation through 27 legislative acts and through amendments to the Finnish Financial Supervisory Authority's ('FIN-FSA') Regulations and Guidelines concerning bookkeeping, financial reporting and annual reports of insurance companies (14/2012). The main legal provisions regarding the solvency of insurers are included in the Insurance Companies Act (521/2008). Moreover, detailed rules and recommendations on the implementation of the Solvency II Directive have been set out in the FIN-FSA Regulations and Guidelines 1/2015.

3. Conduct of Business Issues

The FIN-FSA publishes Regulations and Guidelines which contain provisions of binding nature as well as quasi-binding recommendations regarding the code of conduct of insurance companies. The FIN-FSA also publishes more detailed regulations, such as, for

²⁰ Directive 2009/138/EC of 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II directive)



instance, Regulations and guidelines 10/2012, which contain detailed rules and recommendations regarding disclosure of expenses and returns of insurance policies.

Nevertheless, good insurance practice has not been defined expressly in Finnish insurance legislation. However, certain principles are generally considered to be inherent to good insurance practice, namely *fair and equitable treatment* of policyholders and respect of fundamental rights, including *equal treatment* and *non-discrimination*. Pursuant to the Act on the Financial Supervision Authority (878/2008) the FIN-FSA has been vested with the power to supervise that insurance companies within its jurisdiction comply with not only rules regarding marketing and insurance terms and conditions, but also any *conduct which is contrary to good insurance practice or otherwise constitutes unfair or inappropriate conduct towards the customer, that is, the policyholder*.

Moreover, insurance companies' conduct is regulated by the Finnish consumer protection legislation, which applies to consumers and consumer-like persons, such as employees. Pursuant to the Consumer Protection Act (38/1978), clauses which are unreasonable to consumers (or employees, for example) can be adjusted or disregarded. Likewise, the general rules regarding good marketing practice also apply to insurance companies.

In addition to the Insurance Contracts Act (543/1994), in which *inter alia* the insurers' and policyholders' obligations are regulated, also the general Contracts Act (228/1929) is applicable to insurance policies. The Contracts Act contains a provision according to which any unreasonable agreement can, in principle be adjusted or disregarded. The threshold for applying this provision to an insurance policy is, however, much higher than that of the Consumer Protection Act.

4. Complaints Handling

All Finnish insurance companies must, pursuant to the FIN-FSA Regulations and Guidelines 3/2013 apply the complaints handling procedure as set out in the European Insurance and Occupational Pensions Authority's ('EIOPA') *Guidelines on Complaints-Handling by Insurance Undertakings* (EIOPA-BoS-12/069, 14 June 2012).²¹ Bothnia complies with the said guidelines, including, *inter alia*, the guidelines regarding complaints management policy, registration and reporting of complaints, internal follow-up and procedures for responding to complaints.

Moreover, Bothnia's policyholders can submit complaints to the insurance ombudsman institutions both in the UK, to FOS (Bothnia has submitted itself to the voluntary jurisdiction of FOS) and in Finland, to FINE. Policyholders who qualify as consumers or

²¹ Downloadable from the following site:
https://eiopa.europa.eu/Publications/Guidelines/EIOPA_Complaints_Handling_GL_EN.PDF#search=EIOPA%20complaints%20handling%20gl



consumer-like persons (e.g. employees) can also file complaints to the consumer ombudsman, and the consumer ombudsman can take the matter before a district court. The consumer ombudsman may also lodge class actions on behalf of consumers, provided that the consumers have opted in to the action.

5. Supervisory Intervention

According to Chapter 25 Section 1 of the Insurance Companies Act, the FIN-FSA is responsible for supervising insurance companies and ensuring their compliance with the insurance laws and good insurance practice in particular as regards the companies' solvency and governance. The FIN-FSA has been granted substantial competence to supervise insurance companies, including the right to information and inspections, implementation ban and demand for rectification accompanied by the conditional imposition of a fine. The FIN-FSA powers cannot be limited by reasons relating to the protection of business secrets or personal information.

The FIN-FSA regularly inspects the entities that it supervises, inter alia, by carrying out assessments of the adequacy of the supervised entities internal control and supervision. Moreover, the FIN-FSA can use external assistance in inspecting insurance companies' books. In case an insurance company has neglected its solvency obligations, the FIN-FSA may restrict its activities or cancel its license entirely. In addition, the FIN-FSA can restrict management's powers for a definite period of time and assign an authorized representative to act on behalf of the insurance company.

Moreover, pursuant to the provisions of Chapter 29 of the Insurance Companies Act (521/2008), a person acting in violation of certain provisions of the said Act or the Companies Act (624/2006) can be sentenced for an insurance company crime subject to a fine or imprisonment of maximum one year. Moreover, less aggravated violations of the Insurance Companies Act may be sentenced as insurance company offenses, which are subject to a fine.

6. Approval of Controllers of a Regulated Entity

The Managing Director, the Board Members of an insurance company and persons in a comparable position with the aforementioned are subject to a suitability assessment and approval by the FIN-FSA. The persons in question must undergo a suitability assessment (fit and proper) in accordance with the Solvency II Directive, as implemented the Insurance Companies Act (521/2008). Detailed guidance regarding the approval proceedings is set out in the FIN-FSA's Regulations and Guidelines 7/2014.

7. Process for Rejecting Claims

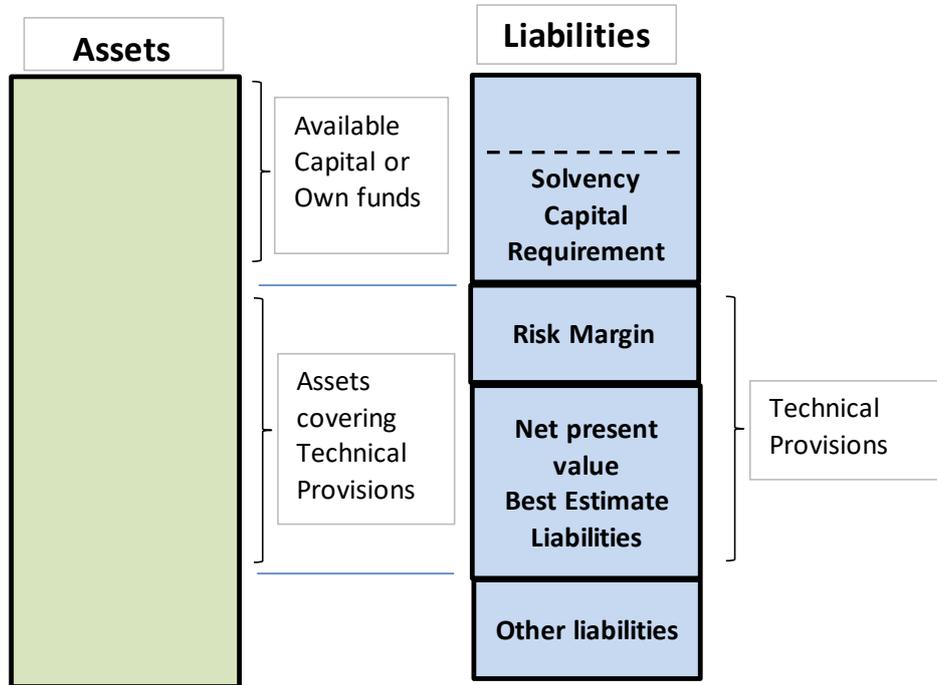
The process of reviewing and rejecting claims is set out in the Insurance Contracts Act (543/1994). The insurance company must make a decision on accepting or rejecting the

claim within one month after receiving the information necessary to make the decision. The claim payment accrues interest in accordance with the statutory rules regarding interest. A decision rejecting a claim must normally include information on the available means of redress.

Although the Act does not contain specific provisions on disclosure of the grounds for the decision, it is nevertheless required by good insurance practice that sufficient grounds be stated in the decision, at least where the claim is rejected or the amount payable is modified. FINE has drafted recommendations concerning the information to be given to claimants in case of rejecting claims. Said Recommendation has been submitted to all members of the Federation of Finnish Financial Services.

Appendix 8 – Basic principles of the Solvency II balance sheet

The schematic below illustrates the structure of the Solvency II balance sheet



The Solvency II balance sheet is intended to be a tool for management to assess an entity’s solvency and is an important consideration for significant decisions. It is also a tool for regulators to assess the solvency of an insurer.

A key consideration for management in making significant decisions will be the excess of assets over Technical Provisions, other liabilities and the SCR. This excess of Own Funds over the SCR will determine the capacity of an entity to assume additional risks into its portfolio, and may similarly restrict an entity from pursuing growth or indeed indicate that a de-risking strategy should be pursued. The level of Own Funds may also impact the credit rating of an entity.

The Technical Provisions are a direct input to the balance sheet, and are a fundamental determinant of the SCR.

Solvency II requires the Technical Provisions to be determined using a market consistent valuation of the liabilities. Technical Provisions are estimated as a ‘best estimate’ of the liabilities with allowance for the time value of money and supplemented by a risk margin. The Technical Provisions are made up as follows of *Claims provision + Premium provision + Risk margin*. For Bothnia the Premium provision is nil since it does not underwrite live business and there are no unexpired risks.

The risk margin (‘RM’) represents the margin that another insurer taking on the liabilities at the valuation date would require over and above the discounted ‘best estimate’. Under Solvency II, the RM is calculated using a cost-of-capital (‘CoC’) approach where the RM is the net present value of the cost of the future capital required to support the portfolio as it runs-off. The principle of the calculation is set out in the formula below:

$$RM = CoC \times \sum_{t \geq 0} \frac{SCR(t)}{(1 + r_{t+1})^{t+1}}$$

Where:

SCR(t) consists of Underwriting risk (with respect to existing business); Counterparty risk (e.g. reinsurance); Operational risk; and Market risk (if unavoidable, i.e. not hedge-able); and;

r_t is the risk-free discount rate at time t as provided by EIOPA for all major currencies.

CoC is currently prescribed by the EU regulation 2015/35 at 6% pa

Appendix 9 – Synopsis of US liquidation proceedings applicable to AMIC-ILQ

Background

The New York Liquidation Bureau (“NYLB”) carries out the duties of the Superintendent of Financial Services of the State of New York (“Superintendent”) in his or her capacity as receiver (“Receiver”) of impaired or insolvent domestic insurance companies (“Domestic Estate”), under New York Insurance Law (“Insurance Law”) Article 74. For each Domestic Estate, the Superintendent is appointed Receiver by the Supreme Court of the State of New York (“Receivership Court”). Thereafter, the NYLB’s actions as the Receiver’s agent are subject to the Receivership Court’s approval. Acting on behalf of the Receiver, the NYLB marshals and maximizes the assets and resolves the liabilities of the insurer in an effort either to rehabilitate or to liquidate the Domestic Estate. Rehabilitation can be used to remedy an insurer’s impairment and can include, subject to court approval, a plan to reduce or resolve the insurer’s liabilities and avoid liquidation (“Rehabilitation”). If the Superintendent believes further attempts to rehabilitate the insurer would substantially increase the risk of loss to policyholders or the public, the company will be liquidated. Upon liquidation, the assets of the Domestic Estate are distributed to policyholders and creditors in accordance with statutory priorities.

Distribution of Assets

The Receiver recommends and seeks court approval regarding distributions from any Domestic Estate in Liquidation. Distributions are made in a manner that assures the proper recognition of priorities and a reasonable balance between the expeditious completion of the liquidation and the protection of non-adjudicated claims.

New York State Insurance Law Section 7434 set forth a comprehensive list of nine classes of creditor claims in specific order of priority of distribution. The statute provides that no distribution can be made to a class of creditors until each claim in the preceding class had been paid in full. This amendment applied to any proceeding under Insurance Law Article 74 as to which an order of liquidation had been entered on or after June 29, 1999. In 2005, the scheme of distribution of assets provided in Insurance Law Section 7434 was applied retroactively. The list of creditor classes in order of priority as set forth by Insurance Law Section 7434 is as follows:

- (i) **Class One – Administrative Claims**
Claims with respect to the actual and necessary costs and expenses of administration incurred by the liquidator or rehabilitator.
- (ii) **Class Two – Claim and Related Costs**
All claims under policies including claims of federal, state or local government for losses incurred, third party claims, claims for unearned premiums, and all claims of security funds or guaranty associations, but excluding claims under reinsurance contracts.
- (iii) **Class Three – Federal Government Claims**
Claims of the federal government, except those stated above in Class two.
- (iv) **Class Four – Employee Claims**
Claims for wages owing to employees of an insurer against whom an Article 74 proceeding is commenced and claims for unemployment

insurance contributions required by Article 18 of the New York Labor Law.

- (v) Class Five – State and Local Government Claims
Claims of state and local governments, except those stated above in Class two.
- (vi) Class Six – General Creditor Claims
Claims of general creditors, including, but not limited to, claims arising under reinsurance contracts.
- (vii) Class Seven – Late Filed Claims
Claims filed late or any other claims other than claims stated in Class eight or Class nine below.
- (viii) Class Eight – Section 1307 Shareholder’s Loans
Claims for advanced or borrowed funds made pursuant to Insurance Law Section 1307.
- (ix) Class Nine – Shareholder Claims
Claims of shareholders or other owners in their capacity as shareholders.

Provided below is a detailed description of the creditor classes.

Class One – Administrative Claims

Claims with respect to the actual and necessary expenses of administration incurred by the Receiver. Included in administrative claims are accruals for vacation benefits and post-retirement medical benefits that have been allocated among the Combined Domestic Estates in Liquidation.

Class Two – Claims and Related Costs

All claims under policies including such claims of federal, state or local government for losses incurred, third party claims, claims for unearned premiums, and all claims of Security Funds or Guaranty Funds, but excluding claims under reinsurance contracts.

Class Three through Class Nine – Subordinate Class of Creditor Claims

Should there be sufficient assets after paying Class two claims, these subordinate classes of creditor claims will be thoroughly investigated and recommended for allowance prior to dividend distribution. The NYLB’s policy is not to incur additional costs on claims not expected to be paid. Therefore, these subordinate classes of creditor claims will not be handled until such time as assets are available to pay such claims. Prior to the 2005 amendment to Insurance Law Section 7434, certain Domestic Estates in Liquidation made distributions to creditors that are currently classified as Class three through Class six. These claims received court approval for each distribution.