Scottish Widows Limited & Rothesay Life Plc

Summary Report of the Independent Expert on the proposed Scheme to transfer certain long-term insurance business from Scottish Widows Limited to Rothesay Life Plc

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1 The proposed transfer

1.1 The Independent Expert

1.1.1 Scottish Widows Limited (SWL) and Rothesay Life Plc (Rothesay) have proposed a scheme (the Scheme) to transfer certain long-term insurance business (the Transferring Business) from SWL to Rothesay. I am the Independent Expert for the Scheme. I am required to provide a report on the Scheme.

1.1.2 The Transferring Business contains non-profit annuity policies, residual risk policies and longevity insurance agreements (together the Transferring Policies), and associated assets and liabilities.

1.1.3 I give a description of the Transferring Policies in paragraphs 1.3.4 to 1.3.14.

1.1.4 SWL and Rothesay (the Companies) have appointed me as the Independent Expert. The Prudential Regulation Authority (PRA), after consulting with the Financial Conduct Authority (FCA), approved my appointment.

1.1.5 The High Court of Justice of England and Wales (the Court) must approve (also called "sanction") the Scheme for the transfer to happen. My role is to consider the likely impact of the Scheme on the policyholders of the Companies and to set out my conclusions in a report. The report is primarily for the Court. The report is also for policyholders and any other parties affected by the Scheme. This is a summary of my full report (my Report) which is available on the Companies' web sites:

- www.scottishwidows.co.uk/bulk-annuities
- www.rothesay.com/scottish-widows-transfer

1.1.6 My Report contains additional information and analysis on the aspects of the transfer discussed in this summary report. This summary report is subject to the same regulation, guidance and professional standards as those set out in sub-section 1.4 of my Report. This summary report has been independently peer reviewed by a senior actuary, Kim Durniat. I will also prepare a supplementary report for the Court (my Supplementary Report). I will prepare this closer to the date of the Court hearing at which the Scheme will be considered. I will update my conclusions in my Supplementary Report, taking into account events that occur after the date of my Report.

1.2 The companies involved in the transfer

1.2.1 SWL is a UK insurance company. It writes a range of insurance, pensions and investment business. As at 30 June 2024 SWL had approximately 6.5m in-force policies and valued its liabilities for these policies at £164bn.

1.2.2 Rothesay is a UK insurance company. Rothesay writes a limited range of products that provide pension benefits or pension-related benefits to individuals, the trustees of UK occupational pension schemes and other insurance companies. As at 30 June 2024 Rothesay had in-force policies covering approximately 1.0m lives and valued its liabilities for these policies at approximately £58bn.

1.3 The proposed transfer

1.3.1 In 2023 SWL decided to sell the Transferring Business and subsequently entered into an agreement to transfer the Transferring Business to Rothesay, a leading specialist insurer in the management of the types of policy included in the Transferring Business. The Scheme is the legal process to enable the transfer.

1.3.2 If the Court approves the Scheme, the effective date of the Scheme (the Scheme Effective Date) is expected to be 11 June 2025. From that date, holders of the Transferring Policies will become policyholders of Rothesay and Rothesay will be responsible for the administration of the Transferring Policies and payment of all benefits falling due under them.

1.3.3 In advance of the legal transfer of the Transferring Business to Rothesay, SWL has entered into a reinsurance agreement (the Reinsurance Agreement) with Rothesay. This agreement transfers most of the economic risk and reward (profits or loss) on the Transferring Business from SWL to Rothesay with effect from 1 January 2024.

The Transferring Policies

1.3.4 The Transferring Policies (as at 30 June 2024) are:

- 28 bulk purchase annuity buy-in policies issued by SWL to 21 UK pension scheme trustees.
- 6,739 individual annuity policies issued by SWL to, or in respect of, individual pension scheme members and/or contingent beneficiaries[1] from nine bulk purchase annuity buy-in policies previously issued by SWL to pension scheme trustees that have since moved to buyout.
- Two residual risk policies issued by SWL to pension scheme trustees in connection with the bulk purchase annuity policies issued to such trustees.
- Four longevity insurance agreements entered into between SWL and Lloyds Banking Group (LBG) Pensions Trustees Limited (the Ambrosia Policies).

1.3.5 Under a bulk annuity buy-in contract, the pension scheme pays the insurer a lump sum. In return, the insurer pays to the pension scheme trustee a specific portion of the benefits that the pension scheme pays to its members or other beneficiaries. The pension scheme trustees become a policyholder of the insurer. The pension scheme trustees remain responsible for paying benefits to members and other beneficiaries of the pension scheme.

1.3.6 Under a buyout contract, the pension scheme pays the insurer a lump sum. In return, the insurer becomes liable for the benefits payable to the relevant members or other beneficiaries of the pension scheme. The individuals receiving benefits from the pension scheme become policyholders of the insurance company. The insurance company issues these individuals with individual insurance policies setting out the benefits that will be paid by the insurance company. These polices are called individual annuity policies.

1.3.7 An individual annuity policy pays a regular amount of benefit to the policyholder, usually until the death of the policyholder.

1.3.8 An annuity can be in payment or in deferment. In payment means that regular payments to the beneficiary have started. When an annuity is in deferment, it is called a "deferred annuity". This means that the regular payments will start later, usually the policyholder's planned retirement date.

1.3.9 The annuity policies included in the Transferring Policies are "non-profit". This means that the benefits of the annuity are defined when the policy is taken out. Apart from as set out immediately below, SWL has no discretion in the amount of benefit paid.

[1] Contingent beneficiaries are persons entitled to receive benefits upon the death of the pension scheme member, such as a spouse.

1.3.10 In certain situations, the beneficiary of an annuity may choose to exchange some or all of their annuity income (the regular payment) for a lump sum payment (called a commutation). This applies to beneficiaries of individual annuities and the beneficiaries of pension schemes insured under the bulk annuity buy-in contracts. Beneficiaries of deferred annuities may also ask to:

- move the value of their policy to a different pension provider (called a transfer, with the amount transferred called a transfer value); or
- have payments started earlier or later than planned. In this case the insurer will reduce or increase the annuity income amount respectively to reflect the change in the expected payment period.

1.3.11 These policyholder choices are referred to as optional benefits or, simply, options. The insurer uses its discretion to set the factors used to convert defined benefits to optional benefits. When setting these factors, the insurer must comply with the relevant policy terms and conditions. Later in this summary report I refer to the amount of benefit calculated when converting defined benefits to a different form of benefit as the "discretionary benefit".

1.3.12 The only other circumstance in which discretion is exercised is in some cases when a beneficiary dies, a pension becomes payable to the beneficiary's spouse, and there is a larger than usual age gap between the beneficiary and their spouse. If the spouse is younger, the pension payable to them may be reduced as the larger than usual age difference means the spouse's pension is likely to be paid over a longer period than would normally be expected. For some policies, the insurer uses its discretion to set the factors used to reduce the pension payable to the spouse. Again, when setting these factors, the insurer must comply with the relevant policy terms and conditions.

1.3.13 Residual risk policies provide extra protection to pension scheme trustees that have entered into a buyout contract. The policy covers certain risks that may not be covered by the buyout contract. These risks could include claims from scheme members that they have a right to a higher level of benefit than those insured under the buyout policy because of either data or benefit errors.

1.3.14 The four longevity insurance agreements (referred to above in 1.3.4 as the Ambrosia Policies) transfer some of the longevity risk from the insured pension schemes to SWL. Longevity risk is the risk that pension scheme members live longer than expected and, therefore, that member pensions are paid for longer than expected.

1.4 My considerations with respect to the proposed transfer

1.4.1 I have primarily considered the effects of the Scheme on the following three classes of policyholders:

- Transferring Policyholders: The holders of the Transferring Policies and any other individuals who are or may become entitled to receive benefits under these policies.
- SWL Non-Transferring Policyholders: The holders of existing SWL policies as at the Scheme Effective Date that will not transfer to Rothesay under the Scheme (the SWL Non-Transferring Policies) and any other individuals who are or may become entitled to receive benefits under these policies.
- Rothesay Existing Policyholders: The holders of existing Rothesay policies (including reinsurance policies, where Rothesay is acting as reinsurer) as at the Scheme Effective Date (the Rothesay Existing Policies) and any other individuals who are or may become entitled to receive benefits under these policies.

1.4.2 My key considerations in respect of each class of policyholders are the effects of the Scheme on:

- the security of policyholders' benefits, which is dependent on the relevant insurance company's financial strength and the risks to which they are exposed
- the reasonable expectations of policyholders in respect of their benefit expectations, service standards, management and governance.

1.4.3 The test I have applied in considering this Scheme is whether the position of any class or sub-group of policyholders is, in the round, "materially adversely affected". The word "material" is not uniquely defined and so, where there are adverse changes, I have attempted to give some context as to their size or likelihood of occurring. If a potential effect is very unlikely to happen and does not have a large impact, or if it is likely to happen but has a very small impact, I do not consider it material.

1.4.4 My assessment of whether any class or sub-group is materially adversely affected includes consideration of the Companies' application of discretion in determining the amount and form of benefits payable to policyholders. In assessing this impact on policyholders, I consider whether the Companies' approaches to the use of discretion are, in my opinion, consistent, aligned with policy terms and conditions and fair to policyholders.

1.4.5 In most respects, the interests of all Transferring Policyholders are similar. Therefore, I mainly consider the Transferring Policyholders as a class as a whole. There are some cases where I have different considerations for particular sub-groups of policyholders. For these purposes, I will refer to the following sub-groups:

- The Transferring Annuities, which are the 28 bulk purchase annuity buy-in policies and the 6,739 individual annuity policies referred to in the first two bullets of paragraph 1.3.4. I refer to the holders of these policies and any other individuals who are or may become entitled to receive benefits under these policies as the Transferring Annuitants.
- Other Transferring Policies, which are the two residual risk policies and the four longevity insurance agreements referred to in the third and fourth bullets of paragraph 1.3.4. I refer to the holders of these policies and any other individuals who are or may become entitled to receive benefits under these policies as the Other Transferring Policyholders.

2 The effect of the Scheme on the Transferring Policyholders

2.1 Summary

2.1.1 I am satisfied that the Scheme will have no material adverse effect on the Transferring Policyholders.

2.1.2 To arrive at my conclusions, I have considered the following:

- the impact of the Scheme on the security of the benefits of the Transferring Policyholders
- the impact of the Scheme on the reasonable expectations of the Transferring Policyholders, including benefit expectations, service standards, management and governance.

2.1.3 I expand on these points below.

2.2 Benefit security of Transferring Policyholders

2.2.1 It is important that Transferring Policyholders' benefits are paid as they fall due. The continuing ability of an insurer to pay benefits depends upon it holding:

- sufficient assets to pay the expected amount of future benefits and expenses as they fall due
- additional assets in case the actual amount of future benefits and expenses it needs to pay is greater than expected.

2.2.2 I have investigated the security of Transferring Policyholders' benefits by comparing the sources of security and the profile of risks to which the Transferring Policyholders will be exposed pre- and post-Scheme.

2.2.3 I am satisfied that the Scheme will have no material adverse effect on the benefit security provided to the Transferring Policyholders.

2.2.4 I have formed this opinion taking into account, amongst other things, that:

- both SWL and Rothesay are subject to the same regulatory solvency regime, meaning that the minimum amount of capital (assets in excess of liabilities) that they must hold offers a similar level of security
- both SWL and Rothesay have reasonably similar targets in respect of excess capital (capital above the minimum capital requirement), such that the probability of either company being unable to meet its obligations to its policyholders, including the Transferring Policyholders is, in my opinion, remote.

2.3 Reasonable expectations of Transferring Policyholders

2.3.1 In my opinion, the Transferring Policyholders' reasonable expectations in respect of their policies are that:

- they receive their benefits as guaranteed under the policy, on the dates specified
- to the extent that benefits rely on discretion, that such discretion is exercised fairly
- the administration, management and governance of the policies are in line with the contractual terms under the policy and applicable conduct regulation (how firms treat their customers)
- the standards of service received are as good as those they currently receive.

2.3.2 Transferring Policyholders may also expect an appropriate degree of consumer protection with regards to their fair treatment, the ability to escalate complaints to an independent body where they feel that they have been treated unfairly, and access to any industry compensation scheme. The proposed transfer will not alter the consumer protection framework that applies to Transferring Policyholders (or any other SWL or Rothesay policyholders) and, therefore, I do not consider it further in this summary report.

2.3.3 I have investigated the factors listed in paragraph 2.3.1 by looking separately at benefit expectations, policy administration and servicing, and management and governance.

2.3.4 As there are differences in approach, I consider policy administration and servicing for the Transferring Annuitants separately to policy administration and servicing for the Other Transferring Policyholders.

Benefit expectations

2.3.5 I am satisfied that the Scheme will have no material adverse effect on the reasonable benefit expectations of Transferring Policyholders.

2.3.6 I have formed this opinion taking into account that:

- most benefits, the vast majority of which are regular annuity payments, are contractually defined and do not rely on discretion
- where discretion is applied, it mainly impacts only a subset of Transferring Annuitants when they choose to do something other than take their contractually defined benefit, such as take a cash lump sum, transfer the value of their policy to another pension provider or have payments started earlier or later than planned (as described in paragraphs 1.3.10 and 1.3.11), where:
    - the amount of the benefit calculated, the discretionary benefit, is not guaranteed
    - Rothesay will use methods consistent with those currently used by SWL
    - the methods and assumptions that Rothesay will use are, in my opinion, aligned with policy terms and conditions and fair to Transferring Annuitants
    - any future changes to Rothesay's methods and assumptions will be subject to Rothesay's internal governance and its requirement to meet the FCA's conduct rules which are, in my opinion, comparable to SWL's internal governance and its requirement to meet the same conduct rules.

- the only other circumstance in which discretion is exercised affects a very small number of Transferring Annuitants when a spouse's pension[2] becomes payable on the death of a Transferring Annuitant and there is a larger than usual age gap between the Transferring Annuitant and their younger spouse, which I refer to as a "young spouse pension", where:
    - Rothesay will usually take a simplified approach that typically leads to a level of benefit similar to that calculated by SWL; and
    - for the small subset of cases where the spouse is significantly younger than the Transferring Annuitant, Rothesay will review the simplified calculation and adjust it, if necessary, to ensure the benefit meets the relevant policy terms and conditions.

2.3.7 That said, the assumptions Rothesay will use to calculate discretionary benefits and young spouse pensions differ from those currently used by SWL. Rothesay's use of different assumptions will lead to changes in the level of discretionary benefits and young spouse pensions. Based on calculations performed by the Companies, these changes are expected to be broadly neutral overall. Where discretion is exercised, some of the Transferring Annuitants may receive higher benefit amounts while others may receive lower amounts. Where the Transferring Annuitants may receive lower amounts, the FCA has asked the Companies to consider whether additional measures could be taken to mitigate the impact of the differences. The Companies have committed to addressing this request and are currently developing their approach to implementing appropriate additional measures. I will report on the outcome in my Supplementary Report. Guaranteed benefit amounts, including any applicable inflationary increases, will not be affected.

Policy administration and servicing

2.3.8 In my opinion, the Scheme will have no material adverse effect on the policy administration and service standards experienced by the Transferring Policyholders.

2.3.9 I discuss the position for the Transferring Annuitants separately to that for the Other Transferring Policyholders as different considerations apply to each group.

2.3.10 For the Transferring Annuitants, I have formed this opinion taking into account, amongst other things, that:

- Transferring Annuities will continue to be administered by the same outsourced service provider using the same administration platform and the same staff immediately after the Scheme is implemented, with the exception of contact centre staff that deal with initial telephone enquiries (where a change is intended to provide a better level of service to the Transferring Annuitants)
- the Companies and the outsourced service provider have comprehensive plans (a Separation Plan and supporting documents) to ease the transition from SWL to Rothesay
- service standards after the Scheme is implemented will be at least as good as those that are currently applied by SWL.

[2] A spouse's pension is a pension payable to the spouse of a Transferring Annuitant upon the death of the Transferring Annuitant. Where the spouse is significantly younger than the Transferring Annuitant, the pension payable to the spouse may be reduced, to reflect that it is likely to pe paid over a longer period than expected.

2.3.11 For the Other Transferring Policyholders, I have formed this opinion taking into account, amongst other things, that:

- Rothesay will administer the Ambrosia Policies using its own system that it uses for similar contracts, and which it is already using to replicate the administration and calculations currently in place
- there are currently no administration requirements for the residual risk policies as no claims have yet been made under these policies and Rothesay, and its outsourced service providers, have expertise in administering any benefits that may become payable under this type of contract.

2.3.12 As at the date of my Report, the Companies' work on the Separation Plan is underway. The Separation Plan contains activities that have completed, activities that are work in progress and activities that are planned to be carried out between the date of my Report and the Scheme Effective Date. While this is a common position in a transfer of insurance business, the Companies need to be confident that they will successfully implement the Separation Plan before the Scheme Effective Date. This is recognised by the Companies and they have taken into account the timeline for successfully implementing the Separation Plan in setting the Scheme Effective Date.

2.3.13 At the date of my Report, work on implementing the Separation Plan is progressing to plan and I have no reason to be concerned that the activities will not be completed successfully.

2.3.14 I have asked the Companies to keep me informed of progress against the Separation Plan and I will provide an update in my Supplementary Report.

Management and governance

2.3.15 In my opinion, the Scheme will have no material adverse effect on the management and governance of the Transferring Policies.

2.3.16 I have formed this opinion taking into account, amongst other things, that:

- Rothesay's governance structure is comparable to that of SWL's and is, in my opinion, appropriate
- the same regulatory requirements, including the Consumer Duty (as described below), apply to both SWL and Rothesay.

2.3.17 The Consumer Duty is regulation on how firms must act. The Companies must act to deliver good outcomes for retail customers. SWL applies the Consumer Duty to all of the Transferring Policies and Rothesay applies the Consumer Duty to all of its business.

3 The effect of the Scheme on the SWL Non-Transferring Policyholders

3.1 Summary

3.1.1 I am satisfied that the Scheme will have no material adverse effect on the SWL Non-Transferring Policyholders.

3.1.2 To arrive at my conclusion, I have considered the following:

- the impact of the Scheme on the security of the benefits of the SWL Non-Transferring Policyholders
- the impact of the Scheme on the reasonable expectations of the SWL Non-Transferring Policyholders, including benefit expectations, service standards, management and governance.

3.1.3 I have formed my opinion taking into account, amongst other things, that:

- the impact of the Scheme on SWL's financial position is not material
- there will be no changes for SWL Non-Transferring Policyholders, because of the Scheme, to:
  - the way benefit amounts are calculated and paid
  - the level of charges or the way charges are determined
- there will be no changes for SWL Non-Transferring Policyholders to SWL's administration, management or governance arrangements because of the Scheme.

3.1.4 Given the limited impact of the Scheme on the SWL Non-Transferring Policyholders, I include no further analysis in this summary report.

4 The effect of the Scheme on the Rothesay Existing Policyholders

4.1 Summary

4.1.1 While SWL is a Rothesay Existing Policyholder (because of the Reinsurance Agreement), the considerations in this section do not apply to it, as it is a party to the Scheme. If the Scheme is implemented SWL will cease to be a policyholder of Rothesay. In the remainder of this section, readers should interpret Rothesay Existing Policyholders as excluding SWL.

4.1.2 I am satisfied that the Scheme will have no material adverse effect on the Rothesay Existing Policyholders.

4.1.3 To arrive at my conclusion, I have considered the following:

- the impact of the Scheme on the security of the benefits of the Rothesay Existing Policyholders
- the impact of the Scheme on the reasonable expectations of the Rothesay Existing Policyholders, including benefit expectations, service standards, management and governance.

4.1.4 I have formed my opinion taking into account, amongst other things, that:

- the impact of the Scheme on Rothesay's financial position is not material
- there will be no changes for Rothesay Existing Policyholders, because of the Scheme, to the way benefit amounts are calculated and paid
- there will be no changes for Rothesay Existing Policyholders to Rothesay's administration, management or governance arrangements because of the Scheme.

4.1.5 Given the limited impact of the Scheme on the Rothesay Existing Policyholders, I include no further analysis in this summary report.

5 Conclusions

5.1.1 I am satisfied that the Scheme will not have a material adverse effect on:

- the security of the benefits of the policyholders of SWL and Rothesay, including the Transferring Policyholders
- the reasonable expectations of the policyholders of SWL and Rothesay in respect of their benefit expectations, service standards, management and governance, including the Transferring Policyholders.

5.1.2 Based on the analysis above, and the more detailed information in my Report, I am satisfied that the Scheme is fair to all classes and sub-groups of SWL and Rothesay policyholders, although as noted in paragraph 2.3.7, where discretion is exercised in determining the level of benefits payable, some of the Transferring Annuitants may receive higher (non-guaranteed) benefit amounts while others may receive lower amounts. Where the Transferring Annuitants may receive lower amounts, the Companies have committed to addressing a request of the FCA to take additional measures to mitigate the impact of the differences. The Companies are currently developing their approach to implementing appropriate additional measures and I will report on the outcome of this work in my Supplementary Report. Guaranteed benefits are not affected.

5.1.3 My Supplementary Report will provide an update on my conclusions considering any significant events that happen after the date of my Report.