Scheme Report of the Independent Expert on the proposed transfer of insurance business from AmTrust Europe Limited to AmTrust International Underwriters DAC and AmTrust Assicurazioni SpA in accordance with Part VII of the Financial Services and Markets Act 2000

For the High Court of Justice of England and Wales

3 March 2020

Prepared by:

Stewart Mitchell FIA

LCP

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1. Executive summary

1.1. The Proposed Transfer

AmTrust Europe Limited (AEL) currently operates across the European Economic Area (EEA) utilising the EEA's Freedom of Services (FofS) and Freedom of Establishment (FofE) arrangements.

Brexit occurred when the UK left the European Union (EU) on 31 January 2020. There is a transition period until 31 December 2020 during which the UK and EU will conduct trade negotiations. The outcome of these negotiations including any decisions about regulatory equivalence between the UK and EU remains highly uncertain. Until 31 December 2020 the current rules remain in place. The Proposed Transfer described in this report is due to complete before 31 December 2020.

In the event of a so called "Hard Brexit" at 31 December 2020 (eg as a consequence of no agreement over trade negotiations) where AEL no longer has FofS or FofE rights, AEL would not legally be able to carry on the non-UK EEA business. For example, AEL would not be able to issue new insurance policies across the EEA and might not legally be able to pay valid claims to existing non-UK EEA policyholders unless AEL obtains appropriate authorisation in all relevant EEA member states.

To provide certainty that the AmTrust Group can continue to carry on EEA business post-Brexit with minimum disruption, AEL is proposing to transfer (the Proposed Transfer) its Italian medical malpractice business to an Italian Company, AmTrust Assicurazioni SpA (AA) and the remaining non-UK EEA business to AmTrust International Underwriters DAC (AIU). AA was acquired by the AmTrust Group in 2019 and has recently started writing new business.

In addition, the aim of the AEL to AA transfer is part of a wider strategic change regarding the medical malpractice business to be written by each of AEL, AIU and AA which is intended to ensure that all Italian medical malpractice business is in one insurer, being AA, supervised by IVASS, the Italian regulator.

The Effective Date of the Proposed Transfer is 1 July 2020.

There will be no change in the ultimate parent company of all entities, Evergreen Parent GP, LLC (Evergreen or the Group).

Other AmTrust transfers

In addition to the Proposed Transfer, AmTrust are preparing to make further transfers as part of their response to Brexit and other strategic changes and transactions. These are summarised below and covered in more detail in Section 2.2:

- The Section 13 transfer of surety business from AIU to Liberty Mutual Insurance Europe SE (LMIE), a third-party outside of the AmTrust Group, with a proposed Effective Date of 31 March 2020.
- The Section 13 transfer of AIU's Italian medical malpractice business to AA, with a proposed Effective Date of 1 July 2020.
- The Part VII transfer of all business from AMT Mortgage Insurance Ltd (AMIL) to AIU with a proposed Effective Date of 1 October 2020.

1.2. My role as Independent Expert

AmTrust have appointed me to act as the Independent Expert (IE) for the Proposed Transfer. The Prudential Regulation Authority (PRA), in consultation with the Financial Conduct Authority (FCA), has approved my appointment.

As IE, my overall role is to assess whether:

- The security provided to policyholders of AEL will be materially adversely affected by the implementation of the Proposed Transfer.
- The security provided to AIU and AA policyholders will be materially adversely affected by the implementation of the Proposed Transfer.
- The Proposed Transfer will have any adverse impact on service standards experienced by policyholders.
- Any reinsurer of AEL providing cover for the transferring business will be materially adversely affected.

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

1.3. Summary of my conclusions

I have set out below my summary conclusions, considering the effect of the Proposed Transfer from six perspectives:

- A: "Non-transferring AEL Policyholders", who will remain with AEL after the Proposed Transfer.
- B: "Transferring AEL to AIU Policyholders", who will transfer from AEL to AIU as a result of the Proposed Transfer.
- C: "Transferring AEL to AA Policyholders", who will transfer from AEL to AA as a result of the Proposed Transfer.
- D: "AIU Policyholders", ie any policyholders of AIU at the time of the Proposed Transfer who will remain with AIU.

- E: “AA Policyholders”, ie any policyholders of AA at the time of the Proposed Transfer who will remain with AA.
- F: Reinsurers whose contracts with AEL are transferring to AIU and AA as part of the Proposed Transfer.

I have considered the various possible permutations of the Proposed Transfer and the other planned AmTrust transfers not completing as expected, or only partially completing. I have considered this from the perspective of the six groups affected by the Proposed Transfer and the three other planned AmTrust transfers. I have set out my conclusions on this at the end of this section.

A: Non-transferring AEL Policyholders

I have concluded that the security provided to Non-transferring AEL Policyholders will not be materially adversely affected by the Proposed Transfer.

Summary rationale:

- The approach and methodology used to calculate insurance provisions and the level of reserves held by AEL are supported by my own independent projections.
- Further support for the level of reserves held by AEL is provided by the results of an independent external reserve review and a further independent external regulatory review.
- AEL has confirmed that the future reserving process and governance for AEL will be materially unchanged post-transfer.
- The SCR coverage ratio for Non-transferring AEL Policyholders is expected to decrease from 178% to 150% as a result of the Proposed Transfer. I do not consider the security provided to Non-transferring AEL Policyholders to be materially adversely affected by this decrease as AEL remains well-capitalised and the coverage ratio remains above AEL’s risk appetite. In addition, AEL’s coverage ratio is expected to return to pre-transfer levels (178%) by June 2021 ie within a year of the Proposed Transfer.
- The level of regulatory capital held on the 1-year standard formula basis is supported by consideration of capital on a 1-year and ultimate basis using an economic capital model, and stress scenarios including reserve deterioration and reinsurer default.

I have concluded that no material impact on service standards is expected for Non-transferring AEL policyholders following the Proposed Transfer.

Summary rationale:

- AEL is not planning any material changes to how the non-transferring business is carried out.
- There are no plans to change how policyholders are serviced.

B: Transferring AEL to AIU Policyholders

I have concluded that the security provided to Transferring AEL to AIU Policyholders will not be materially adversely affected by the Proposed Transfer.

Summary rationale:

- The Transferring AEL to AIU Policyholders will remain within the AmTrust Group and AIU is subject to the same group-wide policies as AEL.
- AmTrust has confirmed that the transferring policies will continue to be reserved in the same way post-transfer as pre-transfer.
- The calculation of the transferring provisions has been performed using the same methodologies as the non-transferring provisions which I consider appropriate.
- The SCR coverage ratio for Transferring AEL to AIU Policyholders is expected to decrease from 178% to 150% as a result of the Proposed Transfer. I do not consider the security provided to these policyholders to be materially adversely affected by this decrease as AIU will be well-capitalised and the coverage ratio remains above AEL and AIU's risk appetite. In addition, AIU's coverage ratio is expected to increase to 170% by December 2021 ie within 18 months of the Proposed Transfer.
- The level of regulatory capital held on the 1-year standard formula basis is supported by consideration of capital on a 1-year and ultimate basis using an economic capital model, and through stress scenarios.
- Transferring AEL to AIU Policyholders which are currently eligible for FSCS protection will retain access to the FSCS in respect of events or circumstances before the Proposed Transfer but may lose access for events or circumstances which arise after the Proposed Transfer eg the insolvency of AIU.
- As access to the FSCS protection will only be required in the event of an insolvency of AEL which is unlikely, I consider that overall the Transferring AEL to AIU policyholders are not materially disadvantaged by the loss of access. Further, any loss of access to the FSCS should be balanced against the detriment a Transferring AEL to AIU policyholder could suffer in the event that AEL could not pay a valid claim to such policyholder following Brexit.

I have concluded that no material impact on service standards is expected for Transferring AEL to AIU Policyholders following the Proposed Transfer.

Summary rationale:

- AEL and AIU, through the AmTrust Group, are planning to minimise any changes as to how the transferring business is carried out, to avoid disruption to the operating model or its customers.
- Although some claims may be handled by AmTrust Group employees in Dublin rather than Nottingham, the AmTrust Group is not planning any material changes to how the Transferring AEL to AIU Policyholders are serviced following the Proposed Transfer.

C: Transferring AEL to AA Policyholders

I have concluded that the security provided to Transferring AEL to AA Policyholders will not be materially adversely affected by the Proposed Transfer.

Summary rationale:

- The Transferring AEL to AA Policyholders will remain within the AmTrust Group and AA will be subject to the same group-wide policies as AEL.
- AmTrust has confirmed that the transferring policies will continue to be reserved in the same way post-transfer as pre-transfer.
- The calculation of the transferring provisions has been performed using the same methodologies as the non-transferring provisions which I consider appropriate.
- The SCR coverage ratio for Transferring AEL to AA Policyholders is expected to decrease from 178% to 150% as a result of the Proposed Transfer. I do not consider the security provided to these policyholders to be materially adversely affected by this decrease as AA will be well-capitalised and the coverage ratio remains above AEL and AA's risk appetite. In addition, AA's coverage ratio is expected to increase to 168% by December 2021 ie within 18 months of the Proposed Transfer.
- The level of regulatory capital held on the 1-year standard formula basis is supported by consideration of capital requirements in comparing the impact of stress scenarios, including reserve deterioration and reinsurer default, both pre- and post-transfer for these policyholders.
- The Transferring AEL to AA Policyholders will benefit from contract certainty in the light of the uncertainty caused by Brexit and the removal of cross-border supervision by alignment with supervision by IVASS, the national regulator.
- Transferring AEL to AA Policyholders which are eligible claimants may lose access to the FSCS for events or circumstances which arise after the Proposed Transfer

eg the insolvency of AA. However, the majority of Transferring AEL to AA Policyholders are hospitals and private clinics and therefore not likely to be eligible for access to the FSCS due to the turnover threshold of £1,000,000.

- As access to the FSCS protection will only be required in the event of an insolvency of AEL which is unlikely, I consider that overall the Transferring AEL to AA policyholders are not materially disadvantaged by the loss of access. Further, any loss of access to the FSCS should be balanced against the detriment a Transferring AEL to AA policyholder could suffer in the event that AEL could not pay a valid claim to such policyholder following Brexit.

I have concluded that no material impact on service standards is expected for Transferring AEL to AA Policyholders following the Proposed Transfer.

Summary rationale:

- AEL and AA, through the AmTrust Group, are planning to minimise any changes as to how the transferring business is carried out, to avoid disruption to the operating model or its customers.
- For example, the AmTrust Group is not planning any changes to how the Transferring AEL to AA Policyholders are serviced following the Proposed Transfer.

D: AIU Policyholders

I have concluded that the security provided to AIU Policyholders will not be materially adversely affected by the Proposed Transfer.

Summary rationale:

- The approach and methodology used to calculate insurance provisions and the level of reserves held by AIU are supported by my own independent projections.
- Further support is provided by the results of an independent external reserve review and a further independent external regulatory review.
- AIU has no plans to change the approach for how insurance provisions are set.
- The reserving process and governance for AIU will be materially unchanged post-transfer.
- The SCR coverage ratio for AIU Policyholders is expected to decrease from 160% to 150% as a result of the Proposed Transfer. I do not consider the security provided to these policyholders to be materially adversely affected by this decrease as AIU will be well-capitalised and the coverage ratio remains above AIU's risk appetite.

- AIU's coverage ratio is expected to return to pre-transfer levels by September 2021, assuming all transfers proceed as planned.
- The level of regulatory capital held on the 1-year standard formula basis is supported by consideration of capital on a 1-year and ultimate basis using an economic capital model, and through stress scenarios.

I have concluded that no material impact on service standards is expected for AIU Policyholders following the Proposed Transfer.

Summary rationale:

- AIU is not planning any material changes to how the business is carried out. In particular, there are no plans to change how AIU Policyholders are serviced following the Proposed Transfer.

E: AA Policyholders

I have concluded that the security provided to AA Policyholders will not be materially adversely affected by the Proposed Transfer.

Summary rationale:

- AA has no plans to change the approach for how insurance provisions are set.
- The reserving process and governance for AA will be materially unchanged post-transfer.
- The SCR coverage ratio for AA Policyholders is expected to increase from 145% to 150% as a result of the Proposed Transfer and projected to stay above this level. AA will be well-capitalised, and the coverage ratio is above AA's risk appetite.
- The level of regulatory capital held on the 1-year standard formula basis is supported by consideration of capital requirements in comparing the impact of stress scenarios including reserve deterioration and reinsurer default.

I have concluded that no material impact on service standards is expected for AA policyholders following the Proposed Transfer.

Summary rationale:

- AA is not planning any material changes to how the business in carried out. In particular, there are no plans to change how AA policyholders are serviced following the Proposed Transfer.

F: Reinsurers

I have concluded that reinsurers of AEL who provide cover for the transferring business will not be materially adversely affected by the Proposed Transfer.

The transferring policies primarily benefit from AEL's previous quota share arrangements with AII and Maiden, both of which are fully collateralised. AII and Maiden will continue to collateralise exposures to AEL and AIU transferring and non-transferring policyholder liabilities post-transfer.

Maiden is in the process of re-domiciling from Bermuda to Vermont in the United States which is a non-Solvency II equivalent territory. The impact of this on AEL and AIU, as a reinsured of Maiden, is to lead to an increase in the SCR and a therefore a reduction in the SCR coverage ratio.

Maiden has agreed an endorsement to its contract with AEL and AIU such that Maiden must provide additional collateral equal to the greater of 120% of the exposure amount of the liabilities, and such additional collateral needed to ensure the SCR coverage ratio is at the same level as it would have been prior to any re-domicile. Therefore, there is no impact on AEL and AIU's SCR coverage ratio, as measured on a 1-year basis using the standard formula.

Consideration of the 1-year SCR coverage ratio in itself is not sufficient as the impact on the capital required to run-off the business to ultimate should also be considered. I have addressed this by the use of stress scenarios for reserve deterioration and default of reinsurers later in this report in section 6.

The form of the collateral is the same as the current collateral arrangement, made up of cash and corporate bonds.

The main live reinsurance policy protecting the transferring business is the quota share reinsurance provided by Swiss Re as of 1 July 2019. The protection provided to the transferring policyholders from this reinsurance will transfer to AIU and AA.

There are also excess of loss reinsurance policies purchased by AEL for certain product lines that will transfer with the underlying policies.

Summary rationale:

- Exposure to claims faced by AEL's reinsurers will not change following the Proposed Transfer and the reinsurers will continue to be required to pay out the same claim amounts in respect of the same events as before the Proposed Transfer.

Further details on my conclusions, and other supporting information, are set out in this report.

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

Permutations of other AmTrust transfers

It is AmTrust's intention that, if any of the other AmTrust transfers or part of the Proposed Transfer does not get sanctioned, AmTrust will go ahead with the sanctioned transfers, or the part of the Proposed Transfer that is sanctioned. I have considered the various permutations of transfers not proceeding as planned and set out my conclusions on this below from the perspective of the six groups of affected parties and the other three planned transfers.

A: Non-transferring AEL Policyholders

If only the AEL to AIU element of the transfer goes ahead, the AEL policyholders would be materially unaffected as AEL's risk profile as a multi-line insurer would remain broadly unchanged as only a relatively small part of the AEL business is transferring to AIU.

If only the AEL to AA element of the transfer goes ahead, then the AEL policyholders would not be exposed to the long tail medical malpractice business but would lose the diversification benefit from this portfolio. Overall these two elements act in different directions.

If neither transfer goes ahead, the AEL Policyholders are unaffected.

B: Transferring AEL to AIU Policyholders

The business transferring from AEL to AIU is similar non-UK European business to that already written by AIU. As such, the risk profile is not expected to change materially for these policyholders whether the transfer goes ahead or not. There will be exposure to Italian medical malpractice business in AIU if the AIU to AA transfer does not proceed, but AEL policyholders are already exposed to this business within AEL pre-transfer.

C: Transferring AEL to AA Policyholders

The business transferring from AEL to AA, and also from AIU to AA, is Italian medical malpractice business, similar to that already written in AA. If this transfer does not go ahead, the transferring policyholders would continue to benefit from diversification being part of a multi-line insurer within AEL.

D: AIU Policyholders

AIU Policyholders are exposed to the AEL and AMIL portfolios transferring in and the surety portfolio transferring out to LMIE. The risk profile of AIU is not expected to change materially in the event of any combination of these transfers as the business transferring is similar to that already written by AIU. I comment further on the transfers affecting AIU Policyholders below.

E: AA Policyholders

AA writes a portfolio of Italian medical malpractice business ie the same business that will be transferred from both AEL and AIU. As such the risk profile of AA as a mono-line insurer is expected to be the same whether either or both the transfers are successful, although the volume of reserves would be different.

If neither transfer goes ahead, the AA Policyholders are unaffected.

F: Reinsurers whose contracts are transferring as part of the transfers

Exposure to claims faced by reinsurers will not change following any partial or full completion of the proposed AmTrust transfers and the reinsurers will continue to be required to pay out the same claim amounts in respect of the same events as before the transfers. Hence, the reinsurers are exposed to the same risks under any combination of the transfers.

AIU to AA transfer

This transfer is expected to complete on 1 July 2020 ie the same date as the Proposed Transfer. The successful completion or otherwise of this transfer affects the AIU and AA Policyholders as described above.

AMIL to AIU transfer

This transfer is expected to complete on 1 October 2020 ie after all the other AmTrust transfers. The business transferring is mortgage insurance which is already written by AIU and is a relatively small amount of business compared to that of AIU overall. Hence, the risk profile of AIU is not expected to change materially. This transfer will only affect AIU and not AEL or AA.

AIU to LMIE transfer

This transfer is expected to complete on 31 March 2020 ie before the other AmTrust transfers. It will not materially impact the other AmTrust Transfers whether it goes ahead or not as the transferring business is already 100% reinsured by LMIE.

2. Introduction

2.1. Background

Part VII - Section 109 of the Financial Services and Markets Act 2000 (FSMA) requires that a scheme report (the Scheme Report) must accompany an application to the High Court of Justice of England and Wales (the Court) to approve an insurance business transfer scheme (Part VII transfer).

The Scheme Report should be produced by a suitably qualified independent person, the Independent Expert (IE), who has been nominated or approved by the Prudential Regulation Authority (PRA) having consulted with the Financial Conduct Authority (FCA). The Scheme Report should address the question of whether any policyholders or reinsurers impacted by the insurance business transfer are adversely affected to a material extent.

AmTrust nominated Stewart Mitchell (I or me) of Lane Clark & Peacock LLP (LCP, we, or us) to act as the IE for the Proposed Transfer of certain insurance business of AEL to AIU and AA under Section 105 of the FSMA. The Proposed Transfer is intended to be effected on 1 July 2020 (the Effective Date).

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

2.2. The Proposed Transfer

AEL currently writes both direct insurance and reinsurance policies in 23 countries across the EEA.

Direct insurance is defined to be insurance policies sold to the insured party. Reinsurance is defined to be insurance policies sold to other insurance companies.

In the event of a so called "Hard Brexit" where AEL no longer has FofS or FofE rights, AEL may not legally be able to carry on the non-UK EEA business. For example, AEL would not be able to issue new insurance policies across the EEA and might not legally be able to pay valid claims to existing non-UK EEA policyholders.

To provide certainty that the AmTrust Group can continue to carry on EEA business post-Brexit with minimum disruption, AEL is proposing to transfer its Italian medical malpractice business (including a non-material amount of related accident and health and legal expenses business) to an Italian Company, AmTrust Assicurazioni SpA (AA); and the remaining non-UK EEA business to AmTrust International Underwriters DAC (AIU), (the Proposed Transfer). AA was acquired by the AmTrust Group in 2019 and has recently started writing new business.

In addition, the AEL to AA transfer is also part of a wider strategic change regarding the medical malpractice business written by each of AEL, AIU and AA which is intended to ensure that all Italian medical malpractice business is in one insurer, being AA, supervised by Istituto per la Vigilanza sulle Assicurazioni (IVASS), the Italian regulator.

The proposed Effective Date of the Proposed Transfer is 1 July 2020.

There will be no change in the ultimate parent company of all entities, Evergreen Parent GP, LLC (Evergreen or the Group).

In this report I have referred to the term ‘Group’ to refer to Evergreen and all subsidiary companies and ‘AmTrust Group’ to all AmTrust entities.

AEL is a wholly own subsidiary of AmTrust International Limited (AIL) which is a UK Limited Company.

AIL, AA and AIU are wholly own subsidiaries of AmTrust International Insurance Ltd (AII), a company incorporated in Bermuda.

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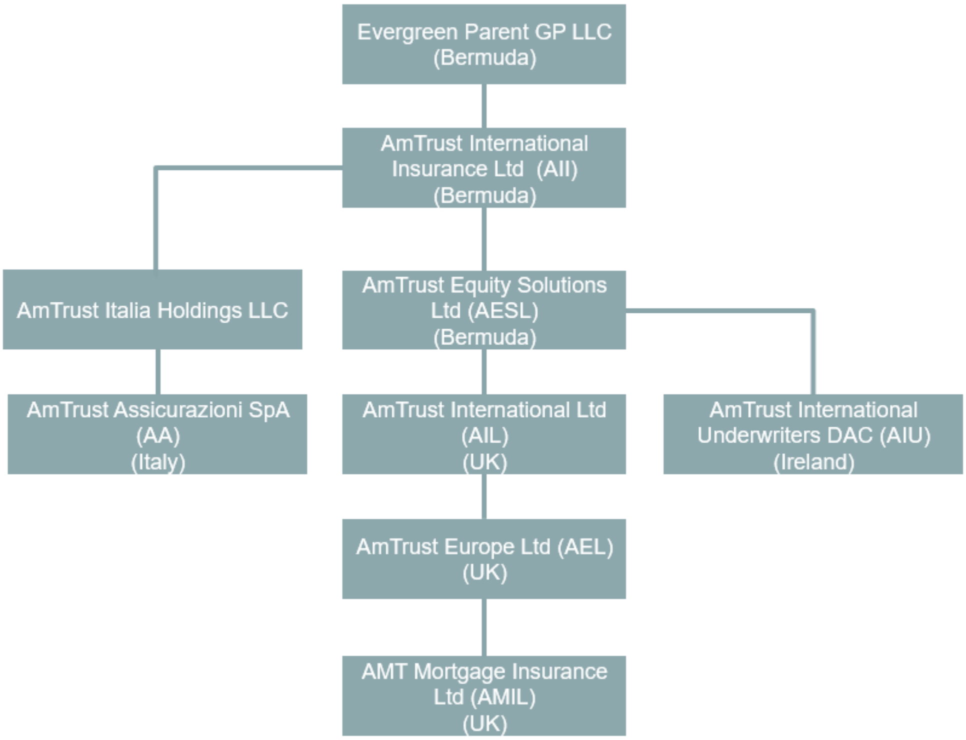
The following diagrams show a simplified structure chart of the Group before the Proposed Transfer and details of the Proposed Transfer. I have also included details of the other proposed AmTrust Group transfers that impact the Proposed Transfer.

Group structure



AmTrust Group transfers

Transfer 1

The Part VII transfer of all business from AMT Mortgage Insurance Ltd (AMIL) to AIU with a proposed Effective Date of 1 October 2020 ie after the Effective Date of the Proposed Transfer. I am acting as the IE for this transfer.

Transfer 2 (the Proposed Transfer covered by this report)

The Proposed Transfer of Italian medical malpractice risks from AEL to AA and other non-UK EEA risks (excluding Italian medical malpractice) from AEL to AIU. As set out in this report, I am acting as the IE for this transfer.

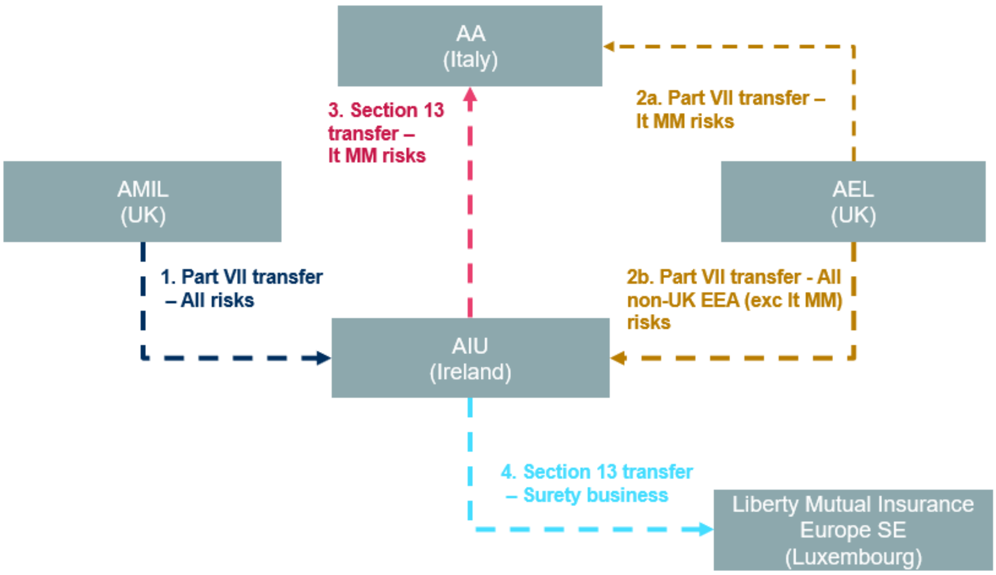
Transfer 3

The Section 13 transfer of AIU's Italian medical malpractice business to AA, with a proposed Effective Date of 1 July 2020 ie the same date as the Proposed Transfer. I am acting as the Independent Actuary for this transfer.

Transfer 4

The Section 13 transfer of surety business from AIU to Liberty Mutual Insurance Europe SE (LMIE), a third-party outside of the AmTrust Group, with a proposed Effective Date of 31 March 2020 ie before the Effective Date of the Proposed Transfer. I am acting as the peer reviewer for this transfer.

There are different peer reviewers for each of Transfers 1 to 4.



* It MM = Italian Medical Malpractice

2.3. Independent Expert appointment

My appointment

AmTrust has appointed me to act as the IE for the Proposed Transfer. The PRA, in consultation with the FCA, has approved my appointment. AmTrust will bear the costs associated with the production of my report. I note that no costs or expenses of the Proposed Transfer will be borne by policyholders.

My experience

I am a Fellow of the Institute and Faculty of Actuaries (IFoA) and am certified to act as a Signing Actuary for Statements of Actuarial Opinions for Lloyd's.

I am a Partner in the Insurance Consulting practice at LCP and have over 30 years' experience in general insurance.

I have skills in all areas of general insurance actuarial work (including reserving, capital, pricing and transactions), and have been the IE or provided peer review to the IE for seven other insurance business transfer schemes. I have also led the work on Section 166 regulatory reports for the PRA.

Appendix 3 contains my CV with further details of my experience.

Independence statement

I confirm that I have no direct or indirect interests in AEL, either personally or via LCP. In particular:

- I am not, directly or indirectly, a shareholder in AEL or any other company within the Group and I am not a member of any pension scheme under the management of AEL;
- I do not hold any insurance policies issued by AEL.

I have been appointed to act as the IE or the Independent Actuary (IA) for Transfers 1, 2 and 3 and a partner of LCP Ireland has been appointed as the IA for Transfer 4. The IA is the equivalent of the IE for a Section 13 transfer, the Irish equivalent of a Part VII transfer. I do not consider my and LCP's involvement in these transfers to impact my independence in relation to the Proposed Transfer.

I also confirm that LCP does not hold any direct or indirect shareholding in AEL or any other company within the Group.

Based on the above I consider that I am in a position to act independently in my assessment of the Proposed Transfer.

2.4. Scope of this Scheme Report

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

This Scheme Report considers the effect of the Proposed Transfer upon the policyholders of AEL, AIU and AA and those reinsurers whose contracts cover (in whole or in part) the business transferring from AEL to AIU and AA. It contains a description of the Proposed Transfer, the methodology I have used to analyse the Proposed Transfer, the opinions I have formed, and reasons why I have formed those opinions.

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

Despite the UK leaving the EU on 31 January 2020, there remains considerable uncertainty regarding the outcome of the negotiations between the UK and the EU during the transition period up to 31 December 2020. Until 31 December 2020 the current EU rules will apply. The Proposed Transfer is planned to be completed before 31 December 2020. I have considered alternative options in Section 3.4 and key dependencies in Section 3.45.

2.5. Use of this Scheme Report

This Scheme Report has been produced by Stewart Mitchell FIA of LCP under the terms of LCP’s written agreement with AmTrust Management Services Limited. It is subject to any stated limitations (eg regarding accuracy or completeness).

This Scheme Report has been prepared for the purpose of accompanying the application to the Court in respect of the proposed insurance business transfer scheme described in this report, in accordance with Section 109 of the Financial Services and Markets Act 2000. The Scheme Report is not suitable for any other purpose.

A copy of the Scheme Report will be sent to the PRA and the FCA and will accompany the Scheme application to the Court. It will also be made available on the AmTrust Financial website for policyholders and other interested parties at amtrustfinancial.com/amtrustinternational/legal/portfolio-transfers.

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

2.6. Reliances

I have based my work on the data and other information made available to me by AmTrust, AEL, AIU and AA. Appendix 4 contains a list of key data and other information that I have considered. I have also held discussions with the relevant staff of AEL, AIU, AA and their advisors.

I have used a combination of data as at 31 December 2018 and 30 June 2019 for my analysis. Prior to the Sanctions Hearing for the Proposed Transfer, I will prepare a Supplementary Report to confirm and/or update my conclusions in this report, based on updated financial information and any new material or issues that arise.

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

- AEL, AIU and AA will submit witness statements to the Court stating that all information provided to me is correct and complete in all material aspects.
- Each of AEL, AIU and AA have provided a Data Accuracy Statement confirming that the data and information provided to me regarding the Proposed Transfer are accurate and complete.
- AEL, AIU and AA have confirmed to me that there have been no material adverse changes to the financial position of AEL, AIU or AA since that information was provided to me.
- AEL, AIU or AA have read this IE Scheme Report and each has agreed that it is correct in terms of all factual elements of the Proposed Transfer.
- I have conducted basic checks on the data provided to me for internal consistency and reasonableness.
- My checks of the data have not revealed any cause for me to doubt that it is materially appropriate for me to rely on the integrity of the information provided for this report.

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

I have not needed to take any third-party legal advice on any aspects of the Proposed Transfer. AmTrust has confirmed that it has received no specific legal advice relevant to my role as IE for the Proposed Transfer.

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

2.7. Professional standards

This report complies with the applicable rules on expert evidence and with the guidance for Scheme Reports set out by the PRA in their Statement of Policy, the FCA guidance to their approach to review of Part VII transfers issued in May 2018 and by the PRA Rulebook and the FCA Handbook.

This report complies with the following Technical Actuarial Standards issued by the Financial Reporting Council (FRC) in the UK:

- Technical Actuarial Standard 100: Principles for Technical Actuarial Work (TAS 100); and
- Technical Actuarial Standard 200: Insurance (TAS 200).

I have considered The Actuaries' Code as issued by the IFoA when producing this report.

This report has been subject to independent peer review prior to its publication, in line with Actuarial Professional Standard X2: Review of Actuarial Work (APS X2) as issued by the IFoA. This peer review has been undertaken by another Partner at LCP. The peer reviewer was not involved in the production of the report. They have the appropriate experience and expertise to act as peer reviewer of this report and have acted as the peer reviewer for other Part VII transfers.

2.8. Materiality

The FRC considers that matters are material if they could, individually or collectively, influence the decisions to be taken by users of the actuarial information. It accepts that an assessment of the materiality is a matter of reasonable judgement that requires consideration of the users and the context.

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

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

2.9. Definition of "materially adverse"

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

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

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

3. Outline of Proposed Transfer

3.1. The companies involved in the Proposed Transfer

AmTrust Europe Limited

AEL is an insurance company incorporated in England and Wales in October 1975, authorised by the PRA and regulated by the PRA and FCA. It is a wholly owned subsidiary of AIL which is a UK Limited Company. Following a merger transaction on 29 November 2018, Evergreen Parent GP, LLC became the ultimate parent company of AEL owning 100% of the issued share capital.

AEL's current A.M. Best financial strength rating as of 13 August 2019 is "A-" (Excellent).

AEL underwrites general insurance and reinsurance business in the United Kingdom, other European countries and outside of the EEA. AEL writes a varied portfolio of medical malpractice, legal expenses, property, casualty, surety, special risk & warranty and accident & health business.

The Proposed Transfer involves transferring policyholders of non-UK EEA business (excluding Italian medical malpractice business) to AIU and transferring policyholders of Italian medical malpractice business to AA.

AmTrust International Underwriters DAC

AIU is an Irish registered insurance company incorporated in Ireland in January 1991 and is authorised and regulated by the CBI.

AIU's current A.M. Best financial strength rating as of 13 August 2019 is "A-" (Excellent).

The company underwrites multiple lines of business across the EU, EEA and the USA. Its main underwriting activities cover casualty, property, general liability, medical malpractice, surety and specialty business.

AmTrust Assicurazioni SpA

AA is an Italian insurance company. The acquisition of it by the AmTrust Group was approved recently by AA's Italian regulator, IVASS.

The origins of AA followed AmTrust Group's purchase of a 100% stake in the share capital of BancAssurance Popolari Danni SpA (BAP) on 15 May 2019. Prior to this, BAP had transferred its portfolio to Cargeas Assicurazioni SpA in early November 2018. A single policy for each line of business was retained in order to keep BAP's insurance licences. These policies expired between July and September this year ie before the expected Effective Date of the Proposed Transfer of 1 July 2020.

New business began to be written into AA during Q3 2019. As at mid-November 2019, c. €4m of gross premiums had been written in respect of medical malpractice business. This is expected to increase to between €25m and €30m by 31 December 2019. The majority of this is expected to be medical malpractice business (€20m to €25m depending on renewals from AIU to AA), together with some legal protection and professional indemnity business. I will comment on the amount of business written to date and the updated business split forecast at the Effective Date of the transfer in my Supplementary Report.

AmTrust International Insurance Ltd

AmTrust International Insurance Ltd (AII) was incorporated in Bermuda in August 1982. It is a Group reinsurance company providing reinsurance to subsidiaries within the Group, including AEL and AIU and AA.

AII's current A.M. Best Financial Strength Rating as of 13 August 2019 is "A-" (Excellent).

3.2. Description of the Proposed Transfer

Transferring policies

If sanctioned by the Court, the Proposed Transfer will move the following business written by AEL and its branches to AIU and AA:

- All non-UK EEA (excluding Italian medical malpractice) business written by AEL will transfer to AIU; and
- All Italian medical malpractice business written by AEL will transfer to AA.

All rights and obligations of AEL relating to the transferring policies will also be transferred to AIU and AA. AmTrust has already started renewing AEL's non-UK EEA business into AIU and writing Italian medical malpractice business into AA and it will continue to do so following the Effective Date.

As at 30 June 2019, the transferring policies represent 47% of booked provisions of £225.6m net of reinsurance compared to total booked provisions for AEL of £480.7m. Further detail is provided in Section 5.5 of this report.

AEL expect that all policies they plan to transfer to AIU and AA will be able to transfer at the Effective Date. Should this not be possible for any reason, there are provisions in the Scheme Document to allow for the transfer of such policies at a later date.

Reinsurance

Reinsurance is an arrangement with another insurer to share or pass on risks. Reinsurance contracts may be underwritten by an external reinsurer or by a reinsurance entity in the same group.

Quota share is a common type of reinsurance arrangement, where an insurer shares a set proportion of premiums and claims with the reinsurer.

Excess of loss reinsurance is another type, where the portion of claims above a certain defined level is passed onto the reinsurer.

Reinsurance is purchased on a group basis and allocated to individual companies in line with their business plans. This is a centralised function managed under the service agreement with AIL.

AEL has three primary quota share reinsurance arrangements:

- **AII** – this whole account reinsurance arrangement expired on 30 June 2019 ie new risks that incepted on 1 July 2019 were no longer covered under this arrangement. Originally 70% of the business was ceded (over 90% for medical malpractice business) but this reduced over a number of years and was 20% prior to the expiry. The arrangement is fully collateralised.
- **Maiden** – this arrangement only covered the Italian medical malpractice business relating to hospitals written or renewed between 3 April 2011 and 31 December 2018. The original cession was 40%, reducing down to 20% by the end of 2018. The arrangement requires Maiden to fully collateralise its exposure.
- Maiden is in the process of re-domiciling from Bermuda to Vermont in the United States which is a non-Solvency II equivalent territory. The impact of this on AEL, as a reinsured of Maiden, is to lead to an increase in the SCR and a therefore a reduction in the SCR coverage ratio.
- Maiden has agreed an endorsement to its contract with AEL and AIU such that Maiden must provide additional collateral equal to the greater of 120% of the exposure amount of the liabilities, and such additional collateral needed to ensure the SCR is at the same level as it would have been prior to any re-domicile. Therefore, there is no impact on AEL and AIU's SCR pre- or post-Transfer nor their SCR coverage ratio. The form of the collateral is the same as the current collateral arrangement, made up of cash and corporate bonds.
- **Swiss Re** – the main live reinsurance policy protecting the transferring business is the quota share reinsurance provided by Swiss Re that incepted on 1 July 2019. It is a whole account programme for a 50% share on a number of lines of business, including Italian medical malpractice business. The coverage is on a policy

attachment basis ie only policies underwritten within the twelve-month period of the policy are covered.

In addition, there are several targeted excess of loss reinsurance arrangements covering specific product lines. These excess of loss reinsurance policies respond to reinsured liabilities before the quota share reinsurance.

Following the Proposed Transfer, the cover under the reinsurance policies that protect the transferring policyholders will transfer to AIU and AA. New business underwritten by AA will be covered by the Swiss Re quota share policy.

Other related transfers planned to take place before the Proposed Transfer

Section 2.2 described a transfer of a portfolio of surety business written through AIU to Liberty Mutual Insurance Europe SE (LMIE) (Transfer 4). This transfer is being separately considered by another IA, also a Partner at LCP.

The Effective Date of Transfer 4 is 31 March 2020 ie before the Proposed Transfer. Unless otherwise stated, pre- and post-transfer results for AIU, in the context of the Proposed Transfer, are presented assuming Transfer 4 has taken place.

The transferring surety portfolio, as at 31 March 2019, accounts for only c. 6% of the total AIU claims reserves net of reinsurance and is expected to lead to a non-material increase in AIU's projected Solvency Capital Requirement (SCR) coverage ratio as the business is already reinsured by LMIE.

As such, my conclusions regarding the AEL to AIU transfer would not be affected whether or not Transfer 4 has taken place by the Effective Date of the Proposed Transfer.

I will confirm in my Supplementary Report if Transfer 4 has or has not taken place and will consider the consequences if not.

3.3. Purpose of the Proposed Transfer

The purpose of the Proposed Transfer is to simplify the business currently written across the AmTrust Group in Europe in response to Brexit, providing certainty that the AmTrust Group can continue to carry on non-UK EEA business post-Brexit with minimum disruption to its operating model and its customers.

In addition, the aim of the AEL to AA transfer is part of a wider strategic change regarding the medical malpractice business to be written by each of AEL, AIU and AA which is intended to ensure that all Italian medical malpractice business is in one insurer, being AA, supervised and regulated by IVASS.

3.4. Alternative options considered

The Proposed Transfer originally assumed a hard Brexit where AEL no longer has FofS or FofE rights for existing or new policyholders. It also assumed that any transitional Brexit arrangement would unlikely be long enough to run-off the book given the long-tailed nature of the liabilities of the business written.

The UK has now left the EU although there remains uncertainty regarding the outcome of trade negotiations between the UK and the EU during the transition period up to 31 December 2020. For example, under a Hard Brexit, AEL may not legally be able to pay valid claims to existing EEA policyholders.

It is AmTrust's intention to continue with the Proposed Transfers regardless of any trading arrangements which may be agreed between the UK and the EU. This is because the transfers are part of a wider strategic change regarding the business to be written by each entity going forward, in particular so that all Italian medical malpractice business is in one insurer, being AA, supervised by IVASS, the Italian regulator.

It is AmTrust's intention that, if any of the transfers or part of the Proposed Transfer does not get sanctioned, AmTrust will go ahead with the sanctioned transfers, or the part of the Proposed Transfer that is sanctioned.

The impact on policyholders through the solvency position and the SCR coverage ratio for each combination of transfers or part of a transfer not being implemented is described in section 6.

AmTrust has confirmed to me that capital will be allocated to group entities to ensure that the SCR coverage ratios for the receiving and transferring entities are maintained in the event that not all of the transfers proceed. The mechanism by which this will be achieved is as follows:

- AEL and AIU will transfer assets to AA equal to the technical provisions and other net liabilities related to the Proposed Transfer.
- AEL and AIU will also pay dividends to their parent companies equal to any capital in excess of 150% of their SCR after taking into account the Proposed Transfers. These dividends will then be used, as needed, by the Group to fund the capital needs of AA up to a 150% SCR coverage ratio following the execution of the transfers.

3.5. Key dependencies

The key dependencies of the Proposed Transfer are as follows:

- Court approval required for the Proposed Transfer – the Directions Hearing is scheduled for 11 March 2020 and the Sanctions Hearing is expected to be 24 June 2020. The Court will take into account whether the PRA and FCA have any objections to the Proposed Transfer.
- Any objections raised by policyholders, reinsurers or non-UK EEA regulators after the Directions Hearing – I will comment on these (if any exist) in my Supplementary Report.
- The PRA must provide the Court with the required certificates under Schedule 12 of FSMA in relation to its consultation with EEA regulators and the necessary solvency certificates from the CBI and IVASS in respect of AIU and AA (respectively).
- The Effective Date of the Proposed Transfer is 1 July 2020 and current EU rules will apply during the transition or implementation period up that date and beyond until 31 December 2020. As such the Proposed Transfer is not dependent on the outcome of the trade negotiations between the UK and the EU during the transition period.
- IVASS has requested an external review of the impact under Italian GAAP of transferring AEL and AIU medical malpractice portfolios to AA. The first draft of this review has not yet been provided but I will comment on the final results of this review in my Supplementary Report.
- AIU is in the process of applying to the CBI for some additional class licences and passporting rights for legal expenses and Italian motor liability business which will need to be approved by the Effective Date in order for such business to transfer to AIU on the Effective Date under the Proposed Transfer. To the extent that any applications for such licences are required and remain outstanding as at the Effective Date, the policies for which such licenses are required by AIU and/or AA (as applicable) will be “Residual Policies” under the terms of the Scheme Document and will transfer at such point that the licenses are granted.
- AA will be submitting an application for a licence in San Marino in respect of an insured hospital situated in this jurisdiction. This is expected to be submitted by 4 March 2020.

4. My approach as IE

As IE, my overall role is to assess whether:

- The security provided to Non-transferring and Transferring policyholders of AEL, AIU policyholders and AA policyholders will be materially adversely affected by the implementation of the Proposed Transfer.
- The Proposed Transfer will have any adverse impact on service standards experienced by policyholders.
- Any reinsurer of AEL covering the transferring business will be materially adversely affected.

To make these assessments, I have considered the effect of the Proposed Transfer from the perspectives of each of:

- Existing AEL policyholders, who will remain with AEL after the Proposed Transfer.
- Transferring policyholders, who will transfer from AEL to AIU and AA as a result of the Proposed Transfer.
- Any policyholders at AA at the time of the Proposed Transfer who will remain with AA.
- Any policyholders at AIU at the time of the Proposed Transfer who will remain with AIU.
- Reinsurers whose contracts with AEL are transferring to AIU and AA.

My approach to assessing the Proposed Transfer has been to perform the following five steps analysing evidence provided by AmTrust to support the Proposed Transfer:

Step 1: Assessing the provisions of AEL, AIU and AA

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

Therefore, I have assessed the appropriateness of the provisions included on AEL's, AIU's and AA's balance sheet and the approach to be used for the calculation of provisions for AEL, AIU and AA pre- and post-transfer. Details of this step are set out in Section 5.

Step 2: Assessing the capital positions of AEL, AIU and AA

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

For AEL, AIU and AA, the level of capital required is set under the European Solvency II standard. A key metric under Solvency II is the Solvency Capital Requirement (SCR). This is an estimate of capital required to ensure that an insurer can meet its obligations over the next 12 months with a probability of at least 99.5%.

I have assessed the appropriateness of the projected capital requirements of AEL, AIU and AA. Details of this step are set out in Section 6.

Step 3: Assessing overall policyholder security

Under this step, I have considered the level of provisions and capital (from steps 1 and 2) in the context of the assets held by each of AEL, AIU and AA and other forms of security such as reinsurance.

For this analysis, I have considered the current balance sheet of AEL and the post-transfer pro-forma balance sheets for each of AEL, AIU and AA. Details of this step are set out in Section 7.

Step 4: Assessing policyholder communications

I have assessed the appropriateness of AEL's communication strategy to inform policyholders and other stakeholders of the Proposed Transfer.

The key focus of my assessment was whether the policyholders and other stakeholders are to be provided with sufficient and clear enough information so that they can understand how the Proposed Transfer may affect them. Details of this step are set out in Section 8.

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

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

5. Reserving considerations

5.1. Introduction to insurance reserving

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

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

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

5.2. Introduction to reserving bases

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

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

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

- UK Generally Accepted Accounting Principles (GAAP) – these are the accounting standards used to set the provisions underlying the published financial accounts of AEL. GAAP provisions are relevant for policyholders as they are used as a reference point when setting provisions to cover future claims and other costs.
- Solvency II technical provisions – these are calculated in line with the European Solvency II regulations that came into effect in both UK and Ireland with effect from 1 January 2016. These provisions are relevant for policyholders as they are the basis for calculating the capital required and assessing solvency, for AEL, AIU and AA.

5.3. My considerations relating to reserving

As IE, my overall assessments related to reserving are:

- whether an appropriate level of provisions is maintained for both non-transferring and transferring policyholders;
- whether an appropriate level of provisions is maintained for the receiving entities post transfer; and
- whether any aspects of the reserving may lead to policyholders being materially adversely affected by the Proposed Transfer.

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

- Appropriateness of provisions (Section 5.5);
- Key uncertainties when setting the provisions (Section 5.6);
- Current AEL and AIU reserving process and governance (Section 5.7);
- Future reserving process and governance for AEL, AIU and AA (Section 5.8); and
- Setting of case estimates (Section 5.9).

Within these areas, I have also considered any expected differences in the reserving approach between AEL, AIU and AA to understand how this may affect non-transferring and transferring policyholders.

Further details on each of these considerations are set out below, and I have stated my overall conclusion related to reserving in Section 5.10.

5.4. Approach to my review

I have reviewed several documents provided by AEL, AIU and AA relating to the setting of provisions, including the reserving process and governance. In addition, I have had meetings to discuss the information provided and any questions I have had on the approach. A list of the key data and documentation reviewed is provided in Appendix 4.

5.5. Appropriateness of provisions

The following table shows the level of booked provisions as at 30 June 2019 (the latest available figures at the time of my writing of my report) for AEL, split between the non-transferring and transferring business. The transferring provisions represent 47% of the total provisions, net of reinsurance. The transferring policies, as at 30 June 2019, represent approximately 10% of the total number of policies issued by AEL (c.2.6m out of c. 25m). When considering only live policies (being policies which have not expired), this proportion reduces to 8% (c. 0.5m out of c. 6.4 m).

Summary of GAAP booked provisions for AEL at 30 June 2019

£m	Gross of reinsurance	Net of reinsurance
Non-transferring AEL	479.4	255.1
Transferring to AIU	145.1	62.9
Transferring to AA	614.4	162.7
Total AEL	**1,238.9**	**480.7**

Source: AEL, figures include OS, IBNR and UPR

Over 60% of AEL booked provisions as at 30 June 2019 will be transferring to AA and AIU.

The Italian medical malpractice business transferring to AA represents 72% of the transferring business on a net of reinsurance basis. Business written to date in AA is predominantly medical malpractice business, with a small amount of associated legal expenses and professional indemnity business. AA is effectively a mono-line insurer writing almost exclusively Italian medical malpractice business.

The business transferring to AIU relates to non-UK EEA business (excluding Italian medical malpractice) and is predominantly made up of miscellaneous financial loss (eg warranty and structural defects business) and surety business.

The non-transferring business remaining in AEL will be mainly After The Event legal cover, Professional Indemnity, Warranty and Structural Defects business. Each of these classes of business accounts for between 17% and 25% of the booked provisions of the non-transferring business.

My assessment of the appropriateness of provisions

I have considered the appropriateness of the following:

- Booked provisions for AEL, AIU and AA;
- Calculation of the transferring provisions; and
- Solvency II technical provisions for AEL, AIU and AA.

Central reserving oversight function

The reserving process is performed by actuarial teams at the entity level for AEL and AIU. However, overall oversight of the analysis and a review of the provisions is performed by AmTrust's Chief Actuary and this will not change post-transfer.

The team currently reserving the Italian medical malpractice business that will transfer to AA will be replaced by a local team in Italy. This is expected to be completed in advance of the Effective Date of the transfer. Therefore, no change in the reserving function is expected pre- and post-transfer. Although the Chief Actuary will provide oversight of the reserving process, responsibility for setting AA's reserves will sit with AA.

Independent projections for AEL by the IE

I have performed my own independent projections on a sample of AEL's business, covering key classes including medical malpractice. These classes accounted for c. 70% of AEL's booked reserves as at 31 December 2018.

My projections were based on paid and incurred claim triangles provided to me by AEL. I derived my own paid and incurred development patterns based on this data and supplemented this with wider benchmark data to inform my tail selections. I used a number of widely accepted actuarial methods such as the chain ladder and Bornhuetter-Ferguson methods and derived expected loss ratios for more recent underwriting years. This was based on averages across the more developed prior underwriting years.

My estimate of gross of reinsurance claims reserves for these classes of business were c. 2% higher than AEL's gross actuarial best estimates. There is subjectivity around the selection of assumptions; particularly around the derivation of paid and incurred development patterns including any tail factors, expected loss ratios and the amount of reliance to place on trends emerging in the claims data. Therefore, the level of reserves could easily be higher or lower than my or AEL's estimates. I consider the difference of c. 2% to be within a range of reasonable best estimates.

My estimate of gross claims reserves for the medical malpractice business is less than 1% lower than AEL's estimate. My experience of medical malpractice portfolios is that a wide range of best estimate of reserves of between -10% to +15/20% of reserves could be supported.

I understand that over 2019 there was further deterioration in AEL's ULR estimates of the medical malpractice business for older underwriting years of between 5-9%. As such, I stressed some of the assumptions made in my analysis to understand how far they would need to move by before reaching the upper and lower end of the range.

If I assumed a 10% slower claims development pattern (ie a particular year is 30% developed rather than 40% developed), my estimate for the medical malpractice business would be c. 20% higher than AEL's estimates ie towards the upper end of what I consider a reasonable range of best estimates to be.

I have reviewed how AEL's ULR's have changed over time. Historical deteriorations in AEL's ULR estimates have been of the order of c. 20% for the older years in the period from 2014 to 2019. However, more recent years have performed much better and shown improvements over time. Changes in the mix of business eg no single doctors or hospitals business written, rate increases and increased deductibles have led to better results. Overall the total ULR for all years of account has remained stable over the last five years.

If I assumed a similar level of deterioration to that seen historically in the older poorer performing years in my gross ULR estimates on the 2017 and 2018 underwriting years, this would increase my estimate of the reserves on these years by c. 20%, again towards the upper end of what I consider a reasonable range of best estimates to be.

The potential for future deterioration in this class of business is there given the long-tailed nature of this class of business meaning uncertainty when setting case reserves and the potential for long delays in claims settlement. Stressed scenarios around reserve deteriorations, and their impact on the SCR coverage ratios, have been considered and are described in section 6.8.

My review of AEL's booked provisions

In this section I have reviewed the process by which AEL calculate their booked provisions.

AEL perform quarterly-reserving exercises. Analysis is performed on an early-close set of data eg as at 31 October 2018. Actual claims experience in the two months to period close (in this example 31 December 2018) is then compared to expectations when setting year-end provisions.

AEL have been writing many of the accounts included within the transferring business for several years meaning there is a large amount of historical claims experience on which to rely on when setting provisions. Provisions are generally set by using AEL's own claims experience supplemented by benchmarks for some classes of business.

The key assumptions used are the patterns to estimate the development of claims and initial expected loss ratios. The approach taken uses standard actuarial techniques such as the chain ladder, expected loss ratio and Bornhuetter-Ferguson methods (defined in Appendix 1) for most classes.

Alternative techniques are used for other classes where standard approaches are not appropriate. For example, AEL apply a "state transition model" for their legal expenses account, which means considering probabilities of claims being made and the success rate of those claims.

For the Italian medical malpractice business, AEL rely more on its own experience and data rather than using benchmarks as the incurred development of this business is different to that typically seen in market benchmarks. This business is not fully run-off and as such judgement is applied in setting the tail claim development. This factor is derived following detailed discussions with the claims team in Milan and varies by claim type.

For non-Italian medical malpractice business, the reliance on benchmarks by AEL has reduced over time as they now rely more heavily on their own claims experience for projection purposes.

AEL now only use market benchmarks where their own experience is not fully developed, eg professional indemnity where benchmarks are provided by an external consultant, and also for classes which are in run-off and are not material to the overall reserves.

The booked provisions are not discounted for the "time value of money". To the extent that claims will be paid out some time in the future, there is an argument that having no discounting provides an additional element of prudence in the provisions. This is due to the ability to earn investment income up to the point the claims are paid.

The focus of my assessment of the AEL approach to setting provisions was a review of the documents provided to me by AEL relating to the calculated provisions as at 31 October and 31 December 2018 (the latest date that full audited results were available), and my discussions with key members of AEL's reserving team.

The provisions calculated by the AEL actuarial team are on a best estimate basis ie with no implicit or explicit margin. AEL then hold a management margin within the booked provisions. The margin is considered on a class by class basis, the size of which varies depending on the degree of uncertainty of the underlying claims experience.

As at 31 December 2018, the overall margin was c. 4% of the net best estimate gross earned reserves. This level of management margin is in line with my experience of the wider market where a margin of up to 5-8% of reserves would be typical, although there are examples of higher margins.

The best estimate provisions ie before the addition of the management margin, will transfer to AIU and AA. AIU and AA will then set a management margin in line with their respective policies to recognise the specific uncertainties within the post-transfer portfolios.

Historically, AEL and others have experienced reserve deteriorations following worse than expected claims experience for Italian medical malpractice business. Whilst my independent estimates and the results of external independent reviews would suggest AEL's booked provisions are reasonable on a best estimate basis, there is a risk that they could ultimately prove to be insufficient.

As noted earlier, the Italian medical malpractice business has observed deteriorations in ULRs over time. Since 2014, the ULRs on the 2010 to 2013 underwriting years have increased by between 16% and 21%. The 2013 and 2014 underwriting years saw an improvement over the same period of c.14%. Whilst this is attributable to worse than expected claims experience, following discussions with AEL's actuarial team, I understand a secondary driver for the deterioration was an initial reliance on broker data which proved to be, over time, inadequate. AEL now has 10 years' worth of own data to inform their projections. Following the adverse experience, AEL has made changes to the mix of business and level of deductibles, in addition to rate increases. I consider the risk of similar level future deteriorations to be lower as a result of these changes, although there is uncertainty around this.

AEL has considered the risk of reserve deteriorations through a formal stress scenario as part of their annual ORSA process through a reverse stress scenario. The scenario considered is a severe reserve deterioration that would be significant enough to lead to insolvency of AEL and therefore the risk of policyholders not being paid. This scenario is based on output from AEL's economic capital model (ECM) at a 1 in 500 year event. I consider this to be extremely remote even given the historical reserve deteriorations observed on the Italian medical malpractice business.

A less severe reserve deterioration scenario has also been considered as part of AEL's wider Solvency II public reporting (Solvency and Financial Condition Report). This scenario is equivalent to a 25% increase in total claims provisions. This is broadly equivalent to a 10% increase in ULR. Although the ULR for earlier years in respect of medical malpractice business have deteriorated by up to c. 20%, more recent years have improved. Therefore, I consider a 10% increase in ULR for the overall portfolio to be a reasonable stress scenario.

External independent review - AEL

Following the historical poor performance of Italian medical malpractice business, AEL were requested by the PRA to appoint a skilled person to perform an independent, external review of the Italian medical malpractice and French structural defects portfolios written by AEL. This was performed by an external consultancy firm. In respect of the medical malpractice portfolio, the review covered an independent review of the claim reserves as at 30 September 2018.

The external estimate of gross of reinsurance claims reserves for medical malpractice was c. 7% higher than AEL's actuarial estimate. Reinsurance reduced the deficit to c.3%

on a net of reinsurance basis or c. €5m. AmTrust management hold a total margin on reserves of €19.6m. If we assume that c. 57% of this margin is allocated to the medical malpractice book (this book accounts for c. 57% of AEL's net earned reserves), this would lead to an overall surplus of c. €6m for this class.

Note that the total margin accounts for 6.6% of the whole account net of reinsurance earned reserve of €297.8m (€19.6m / €297.8m).

I consider a reasonable range around a best estimate of reserves, as noted earlier, to be -10% to +15/20% of reserves and so have concluded that AEL's level of medical malpractice reserves is reasonable. In addition, the management margin of 6.6% held is in line with the range of 5% to 8% of reserves that I observe for other insurers.

The external review notes the significant degree of uncertainty in the medical malpractice reserve estimates, particularly around the typically long delays in claims settlement. I agree with the findings of this review as they are consistent with my own views for this portfolio and my wider experience of portfolios like this for other insurers. I have considered these when coming to my conclusions around the appropriateness of the booked provisions.

Although I have not adopted the external third parties' reserve estimates and views, they provide additional evidence to support the conclusions I reached based on my own independent projections of the appropriateness of the provisions booked by AEL.

Conclusion on AEL's booked provisions

Based on my own independent projections of the provisions for AEL, I concluded that the level of booked provisions for AEL was reasonable and I did not identify any concerns around the appropriateness of the provisions.

My conclusion was supported by my review of AEL's approach and methodology, and the level of provisions indicated by other independent reserve reviews.

Independent projections for AIU by the IE

I have performed my own independent projections on a sample of AIU's business, covering key classes including Italian and French medical malpractice, US General Liability and US Commercial Credit. These classes accounted for c. 70% of AIU's booked claim reserves as at 31 December 2018. I applied triangular-based reserving methodologies to these key classes deriving my own assumed development patterns, making use of benchmark data to inform my selected assumptions where I believed this was necessary.

In aggregate, my independent projections were c. 2% higher than AIU's gross actuarial best estimates. I consider this to be well within a range of reasonable best estimates given the type of business written by AIU and my wider experience of insurers' writing similar business.

My review of AIU's booked provisions

AIU's approach to setting provisions is similar to AEL with a quarterly-reserving exercise performed. At year-end 2018, detailed analysis was performed on an early-close set of data as at 30 September 2018 and the assumptions derived applied to data as at 31 October 2018. Actual claims experience in the two months to 31 December 2018 was then compared to expectations and taken into consideration when setting year-end provisions.

As for AEL, the booked provisions are not discounted for the "time value of money".

The focus of my assessment of AIU's approach to setting provisions was a review of the documents provided to me by AIU relating to the calculated provisions as at 31 December 2018 (the latest date that full audited results were available), and my discussions with key members of AIU's reserving team.

The provisions calculated by the AIU actuarial team are on a best estimate basis. A small management margin is held in the booked provisions in respect of reserve uncertainty. As at 31 December 2018, the overall margin was c. 1% of the net best estimate gross claim reserves. This is not a material amount.

The level of management margin for AEL is higher than AIU. I consider the relative difference in margin to be reasonable given medical malpractice business, where there is a considerable degree of uncertainty, forms a larger proportion of AEL's reserves than for AIU. I am satisfied that the transferring policyholders will not be materially adversely impacted by the Proposed Transfer, as any future management margin is expected to reflect the specific uncertainties within each entity eg the relative amount of longer tail business written. For example, the management margin for AA would be expected to be higher post-transfer than for AEL or AIU given the concentration of long tail medical malpractice written by AA.

The use of benchmarks is limited for AIU. Projections for the Surplus Lines general liability and professional indemnity classes are performed by AmTrust USA at an individual programme level. London Market Association benchmarks are used at an aggregate level for this business to provide a sense check against the more granular level of the underlying projections. The benchmarks are based on risk codes which I consider appropriate eg E3, E5, E7 and E9 for the professional indemnity class and NA and UA for the general liability class.

External independent review - AIU

AIU has commissioned an independent review of AIU's best estimate reserves gross and net of reinsurance from an external actuarial consultancy (being a different consultancy firm to that which performed the AEL review referred to above). The most recent review I considered in my assessment was at 31 December 2018. The approach taken uses standard actuarial techniques such as the chain ladder, expected loss ratio and Bornhuetter-Ferguson methods. These are techniques I would expect to see for business of this type.

This report indicates that the total best estimate gross and net of reinsurance provisions calculated by the actuarial consultancy were c. 1% higher than the total best estimate provisions booked by AIU. This is not materially different and within what I consider a range of reasonable best estimates.

The range around both the best estimate gross and net provisions indicated by the independent review was -13% to +24% of the best estimate. Whilst the range is wider than my experience would indicate, I believe it is reasonable given the inherent uncertainty in the business written and that a wide range of alternative, but plausible, best estimate assumptions could be justified.

My review of the external independent review, in addition to my own independent projections, provides additional evidence of the appropriateness of the booked provisions.

Similar to the skilled persons review undertaken in respect of AEL, a regulatory independent review was also performed for AIU, by the same external actuarial consultancy firm which performed the review for AEL. The review focussed on the Italian and French medical malpractice, surety and US commercial credit business written by AIU. In respect of the medical malpractice portfolio, the review covered an independent review of the claim reserves as at 30 September 2018.

Overall, the level of reserves estimated in the regulatory review by the external actuarial consultancy firm were effectively the same as AIU's best estimate on a net of reinsurance basis. A management margin is also held in on top of AIU's actuarial best estimate.

Although I have not adopted the external third parties' reserve estimates and views, they provide additional evidence to support the conclusions I reached based on my own independent projections of the appropriateness of the provisions booked by AIU.

Conclusion on AIU's booked provisions

Based on my own independent projections of the provisions for AIU, I concluded that the level of booked provisions for AIU was reasonable and I did not identify any concerns around the appropriateness of the provisions.

My conclusion was supported by my review of AIU's approach and methodology, and the level of provisions indicated by two further independent reserve reviews.

Booked provisions for AA

In the context of the Proposed Transfer, AA's GAAP provisions to date are small. As such, I have not performed an assessment of the provisions similar to those for AEL and AIU. However, AmTrust has confirmed that the reserving approach taken will be in line with AEL and AIU and overseen by AmTrust's Chief Actuary.

Therefore, I do not have any concerns around their reasonableness at this stage. The volume of business to be written is expected to increase by the time of the Proposed Transfer and so I will consider this matter further in my Supplementary Report.

Calculation of the transferring provisions

For the purpose of the Proposed Transfer, the approach taken to calculate the transferring provisions is no different to the non-transferring provisions. As I consider the overall provisions to be appropriate, based on my review of the overall methodology taken, I also consider the calculation of transferring provisions to be appropriate.

Solvency II technical provisions for AEL, AIU and AA

The starting point for the calculation of the Solvency II technical provisions (TPs) is the booked GAAP provisions, and I have reviewed the approach taken by AEL and AIU to convert the booked GAAP provisions into the TPs. My review has focussed on the areas which involve a degree of subjectivity and, in my experience, are the areas of greatest interest to an independent reviewer. This included Events Not in the Data (ENIDs) and the Risk Margin.

For both AEL and AIU an allowance for ENIDs is made within the TPs as the data used to estimate GAAP provisions does not typically include experience from rare events. Given the potentially large range around what the best estimate of reserves could be, in this context, ENIDS are not a material component of the TPs. The use of a truncated distribution is a common approach where an assumption is made as to the level of claims from such rare events. This approach has been used to calculate the ENID load for AEL and AIU.

AEL and AIU's ENID loads, as at 31 December 2018, are c. 3% and c. 5% respectively of the total net best estimate technical provisions. In my experience, I consider these implied loadings to be in line with that typically held by other diversified insurers writing similar classes of business.

The risk margin within the TPs under Solvency II represents the potential costs of transferring insurance obligations to a third-party should an insurer fail. The Solvency II guidelines allow four simplifications to the calculation of the risk margin. AEL and AIU use 'Method 2' where an entity's SCR runs off in line with the best estimate TPs ie excluding the risk margin.

Whilst this is an approach I have seen in my wider market experience; market practice is moving towards assuming a slower run-off pattern than implied by the TPs. Therefore, it could be argued that the Risk Margin, and therefore Solvency II TPs is understated, due to a lower projected SCR at each future point in time.

However, there is an offsetting element of prudence given items within an entity's SCR would usually be expected to reduce more quickly than the rate implied by running off in line with the best estimate TPs eg:

- Catastrophe risk – one would expect the majority of this to disappear after one year; and
- Other Credit risk – one would expect broker balances to be mostly paid within a year.

The length of the run-off pattern implied by the net best estimate TPs is around 30 years which I consider to be sufficiently long given the nature of the business written by AEL, the impact of increasing the length of the run-off pattern would not be expected to be material.

I have reviewed the validation work performed by AEL in support of their risk margin calculation. This shows that the impact of running off elements of the SCR (eg operational risk) in a non-linear way does not lead to a material difference in the risk margin and is even less material in the context of the overall technical provisions.

AEL's risk margin as at 31 December 2018 is approximately 4% and 11% of the best estimate gross and net technical provisions respectively. The difference between the gross and net proportion reflects the relatively large proportion of AEL's liabilities that are reinsured away (c. 65%), compared to what is more typical across the market. The majority of AEL's technical provisions relates to general liability and miscellaneous financial business, accounting for c. 90% of total best estimate gross technical provisions.

LCP's market review of Solvency II reporting as at 2018 year-end, based on 100 of the largest non-life insurers in the UK and Ireland, showed that for this type of business, the risk margin is typically c. 5% and c. 10% of best estimate gross and net technical provisions respectively. AEL's risk margin is broadly in line with the rest of the market, although just below the typical range.

AIU's risk margin as at 31 December 2018 is c. 4% of the best estimate gross technical provisions. 85% of AIU's total best estimate gross technical provisions relate to general liability and miscellaneous financial business, for which a typical risk margin based on LCP's market review is c. 5% of best estimate gross technical provisions. I consider AIU's risk margin, as a percentage of best estimate gross technical provisions, to be broadly in line with the rest of the market, although just below the typical range.

On a net basis, AIU's risk margin is higher reflecting the increased volatility due to the relatively high level of reinsurance, as at 31 December 2018 85% of AIU's booked reserves were reinsured.

Overall, I believe the approach taken and results are materially appropriate for AEL and AIU.

My overall conclusion is that AEL and AIU's approach used to calculate the TPs is appropriate. I have not sought to re-perform the calculation of the TPs or verify the calculations performed by AEL or AIU.

As noted above for booked provisions, AmTrust has confirmed that the technical provisions approach for AA will be in line with AEL and AIU. Therefore, I do not have any concerns around their appropriateness at this stage. I will consider this further in my Supplementary Report.

5.6. Key uncertainties when setting provisions

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

There are several uncertainties in setting provisions for the classes of business written by AEL, AIU and AA:

- Several of the classes of business written by AEL, AIU and AA can have claims that are only finally agreed and paid many years after the original incident date eg medical malpractice and casualty lines of business.
- The medical malpractice business is written on a claims made basis meaning once the policy terminates no new claims can be made under the policy terms. However, existing claims notified within the policy term can continue to experience adverse development and can take a long time to settle. This is because it can take many years for the full consequences of any negligence to become apparent

and for the final claim payments to be established. Hence inflation and the cost of future claims is a key uncertainty. However, I believe this delay to be shorter than if the business were written on a loss occurring basis where the potential further delay from a claim incident to an insurer being notified can also increase the delay in settlement.

- In addition, potential disputes over liability and the complexity of settlement negotiations can lead to further delays. AEL and AIU have specialist claims handling teams and insist on full control throughout the claims settlement process.
- Several classes of business written are small in volume with limited historical data meaning that claims experience is likely to be volatile. Given this volatility, AEL and AIU have judgementally selected tail development factors or used benchmark development factors to inform and sense check these selections. These classes will be subject to greater than usual uncertainty.
- AEL and AIU use benchmarks to help inform and validate some of their selected development patterns. Whilst there is uncertainty to the extent that these benchmarks are appropriate to the business written by AEL and AIU, the reliance on these benchmarks has reduced over time and are mostly used for liability classes where benchmarks are provided by an external consultant and classes which are in run-off and are not material to the overall reserves.

Reinsurance is used to mitigate the impact of these key uncertainties and also a risk margin is held within the Solvency II technical provisions. AEL and AIU also use data from elsewhere within the AmTrust Group to supplement their analysis.

5.7. Current reserving process and governance

AEL and AIU reserving processes

The reserving process for AEL and AIU is based on the group-wide process, with quarterly Reserving Committees held.

AEL and AIU use standard actuarial techniques and the approach is in line with standard market practices to calculate provisions for the types of insurance cover. They have used commercially available reserving software, together with Excel spreadsheets, to calculate their provisions.

They now perform their calculations in Excel spreadsheets only given the relatively small proportion of the analysis that was performed in the commercial software. This approach is also in line with typical market practice, and I did not identify any material concerns with the appropriateness of the processes used.

AmTrust's Chief Actuary makes a recommendation on the ultimate loss ratios to the Reserving Committee(s). Formal approval for the decisions taken by the AEL Reserving Committee is provided by the Executive meeting that immediately follows. The AIU

Reserve Committee makes the final ULR selections. The overall responsibility for reviewing, challenging and recommending the level of provisions to hold and incorporate within the financial statements lies with the board of each entity.

The external regulatory reviews for AEL and AIU included a detailed assessment of the reserving process and highlighted some areas of improvements that AEL/AIU will be addressing over the next six to twelve months. These range from applying a wider range of methodologies in estimating reserves to improving the reliability of the data used and the efficiency of the overall process.

My own review reconciles with the key findings from these external reviews. I believe that addressing these recommendations will only benefit policyholders and lead to more robust estimation of reserves and potentially reduce the risk of unexpected reserve deteriorations in the future. The findings from the external pricing review included a recommendation for more regular review of trends in the claims data to mitigate the impact of significant pricing risk and I agree with the recommendation and believe it will further improve the robustness of reserve estimates.

I have seen AEL's draft management response to these recommendations which have been reviewed by the AEL board and shared with the PRA. The recommendations included the proposal to use further alternative reserving methods. Whilst these may not lead to a materially different level of reserves, it could support the selected level of reserves based on the current methodology.

The findings of the AIU review have not yet been finalised and so AIU's management response is not yet available. Action is being taken by AEL and AIU to address the recommendations made and to improve the overall reserving process.

I will consider more fully AEL and AIU's progress against the recommendations made in the external reports and the implementation of any proposed actions in my Supplementary Report.

Wider stakeholder involvement in the reserving process

The AEL and AIU Reserving Committees are attended by a wide group of members, including representation from the Chief Executive Officer, actuarial function, key underwriters and the claims team. Papers are circulated in advance of the Reserving Committee and members are encouraged to challenge the results. I have reviewed the papers circulated to the Reserving Committee and have concluded they provide sufficient detail for appropriate decisions to be taken.

Actions from the Reserving Committee and any changes recommended are recorded in the minutes and circulated to attendees.

Reserving process governance

There is evidence of internal peer review of AEL and AIU's reserving analysis. I have seen evidence of this whilst reviewing the calculation spreadsheet files provided to me. I have also seen evidence of clear minutes from committees involved in the reserving process, including post-meeting email discussions to agree outstanding points and actions.

There are terms of reference in place for the various committees involved in the reserving process. Each of these is evidence of appropriate governance around the reserving process.

The external regulatory reviews of AEL and AIU noted improvements were needed around the documentation of the methodologies used and the assumptions applied in the reserving process. AEL management have provided responses to the recommendations, together with timescales for implementation of their proposed actions. The AIU review is yet to be finalised. I will comment on progress on AEL and AIU's management responses, and the implementation of the proposed actions, in my Supplementary Report.

Given the significant uncertainty around the medical malpractice portfolio in particular, it was also recommended that the risk function increases its focus on reserving risk, ie the risk that reserves will be inadequate, in modelling capital requirements.

AEL and AIU, as part of their wider governance, comply with the requirements set out in the Sarbanes-Oxley Act (Sarbox) of 2002. Sarbox holds CEOs responsible for their company's financial statements with stringent auditing standards in place.

AA reserving process

I have reviewed the draft Reserving Policy for AA which indicates that the reserving approach for AA is expected to be in line with those of AEL and AIU. I will consider this again in my Supplementary Report.

5.8. Future reserving approach and governance

Beyond the improvements recommended from the external regulatory reviews of AEL and AIU, AmTrust has confirmed there are no planned changes in the reserving approach for either GAAP or Solvency II provisions for AEL and AIU post-transfer.

There will also be no change to the governance process for reserving, beyond the improvements recommended from the external regulatory reviews.

5.9. Setting of case estimates

Claims handlers assess claims as they are notified to an insurer and use their judgement and experience to estimate the likely cost of each claim. This is known as setting a "case estimate".

Typically, these case estimates would be a key input into the reserving process as a basis for projecting the estimated costs of future claims, ie those that have not yet been reported and the additional cost of settling those that have been reported.

The provision for these future claims is known as IBNR (incurred but not reported). The IBNR includes estimated developments to existing open claims, ie those that have been reported but not fully settled. The provision for these open claims is called IBNER (incurred but not enough reported). Depending on the type of insurance being considered, and the claims handling approach, both the IBNR and IBNER can be either positive or negative.

A memo provided to me by AmTrust describes how claims are handled across the AmTrust operating companies under a group service arrangement with AmTrust International. The AmTrust Group claims structure ensures that the claims strategy, including claims and reserving philosophy, is consistent across the companies.

AEL does not have its own formal claim policy around the setting of case estimates but from the memo provided and following conversations with AmTrust, the approach is in line with the wider AmTrust Group approach. In addition, the same claims team that currently handle AEL and AIU Italian claims will transfer across to a dedicated claims function within AA and the same individuals will continue to handle these claims for AA. Overall governance of the process will be maintained by AA. AIU aim to "establish a reserve figure which reflects the probable exposure" and is expected to be paid "based on all of the facts available".

AmTrust has confirmed to me that there will be no change in the approach to setting case estimates following the transfers.

5.10. Overall conclusion: Reserving considerations

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

Non-transferring AEL Policyholders

I have concluded that the Non-transferring AEL Policyholders will not be materially adversely affected by the reserving aspects of the Proposed Transfer.

The key reasons for reaching my conclusions for Non-transferring AEL Policyholders are as follows:

- The calculation of provisions has been performed using techniques and approaches in line with standard market practice.
- My own independent projections and those of an external actuarial consultancy firm support the level of provisions held by AEL.
- AEL has confirmed that the future reserving process and governance for AEL will be materially unchanged post-transfer, other than for those actions agreed as a result of the external regulatory review.

Transferring AEL to AIU and AEL to AA Policyholders and AA Policyholders

I have concluded that the Transferring AEL to AIU and AEL to AA Policyholders and the AA Policyholders will not be materially adversely affected by the reserving aspects of the Proposed Transfer.

The key reasons for reaching my conclusions for the Transferring AEL to AIU and AEL to AA and AA Policyholders are as follows:

- The calculation of provisions for AIU has been performed using techniques and approaches in line with standard market practice.
- My own independent projections and those of two external actuarial consultancies support the level of provisions held by AIU.
- The AIU and AA reserving processes are in line with the wider AmTrust Group process.
- AIU has confirmed that the future reserving process and governance for AEL will be materially unchanged post-transfer, other than for those actions agreed as a result of the external regulatory review.

6. Capital considerations

6.1. Introduction to insurance capital setting

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

An insurer's "capital coverage ratio" is calculated as the available capital in excess of provisions divided by the capital required under regulations. The coverage ratio is a measure of capital strength and, whilst it does not capture all aspects of policyholder protection, all else being equal, a higher coverage ratio provides more protection. A higher ratio indicates there is more capital available per £ of capital required. Under Solvency II, the level of available capital is referred to as "own funds".

For the purposes of this report, I describe a company as having "sufficient capital" (relative to the regulatory capital requirement under consideration) if the coverage ratio is above 100%. I describe a company as "well-capitalised" if the coverage ratio is between 150% and 200% and "very well-capitalised" if the coverage ratio is more than 200%.

6.2. Calculating capital requirements

For AEL, AIU and AA, the level of capital required is set under the European Solvency II standard.

A key metric under Solvency II is the SCR. This is an estimate of capital required to ensure that an insurer can meet its obligations over the next 12 months with a probability of at least 99.5%.

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

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

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

AEL, AIU and AA use the standard formula without USPs to calculate their SCR. AEL and AIU do have an, unapproved, internal model which is also considered for wider capital management purposes. AA only use the standard formula and do not have an alternative economic capital model.

Capital requirements beyond a “1-year” view

The SCR is a “1-year” view of risk as it focuses on risks that an insurer faces over the next 12 months. Consideration of the 1-year SCR coverage ratio in itself is not sufficient as the impact on the capital required to run-off the business to ultimate should also be considered.

As part of their overall capital management, insurers typically also consider an “ultimate” view of risk that considers the risks faced over the period until the business is fully run-off. I have used stress scenarios, including reserve deterioration and default of reinsurers, later in this section to consider uncertainty beyond the 1-year view.

AEL, AIU and AA use the standard formula which does not give an estimate of the SCR on an ultimate view. The standard formula only gives an estimate of the SCR over the 1-year time horizon. However, AEL and AIU have considered risk beyond the 1-year view within their 31 December 2018 Own Risk and Solvency Assessment (ORSA). They considered this through a number of scenarios beyond the next 12 months including risks that are not covered within the standard formula.

This included a forward-looking assessment of capital requirements. This showed that AEL’s and AIU’s SCR coverage ratio is expected to stay above 146% and 158% respectively through to 2021, before taking into account the Proposed Transfer or any other changes in the structure of the business.

Both AEL and AIU use economic capital models (ECM) to set their internal measures of capital. Although these models are not approved for regulatory purposes, they provide an alternative view of capital requirements over the ultimate time horizon as well as over 1-year.

For AEL, I compared the 1-year and ultimate SCR as at 31 December 2018 derived under the ECM. I note that the 1-year SCR (£190.2m) is higher than on an ultimate basis (£151.0m). On an undiversified basis, the 1-year SCR is lower than the ultimate basis. A comparison by the main risk categories is shown below:

Comparison of 1-year and Ultimate AEL ECM results (£m)

Risk	ECM - 1-year basis	ECM – Ultimate basis
Insurance Risk	170.1	189.4
Credit Risk	31.4	63.0
Market risk	112.6	67.7
Operational risk	40.2	55.0
Undiversified SCR	354.3	375.1
Diversified SCR	**190.2**	**151.0**

The key drivers for the lower SCR on an ultimate basis compared to the 1-year basis are as follows:

- **Market risk** – AEL's approach to market risk on an ultimate basis is to assume that, after one year, all assets will be sold and a portfolio of ultra-low risk government bonds will be purchased. Ultimate market risk is therefore lower than 1-year market risk as it includes this expected investment profit, with limited additional risk beyond the first year.

  This is a common approach to modelling market risk on an ultimate basis. A common approach within the market is to show insurance risk on a discounted basis, and to have no investment income beyond the first year. AmTrust has instead elected to show insurance risk on an undiscounted basis and allow for the discount benefit by showing investment income beyond the first year. I consider this approach to be reasonable, as the assumptions made are consistent and do not include any element of double-counting of investment returns.

  AmTrust has confirmed that, once expected profit is removed, ultimate risk is greater than 1-year risk. The relevant figures for this are £138.9m (1-year) and £170.0m (ultimate). This is in line with my expectations, as the longer time horizon should intuitively allow more time for risks to emerge.

  Note that AmTrust has revised the methodology for market risk during 2019, which has resulted in a narrowing of the difference between 1-year and ultimate market risk.

- **Insurance risk** – has two elements; premium risk, which increases on an ultimate basis, and reserve risk, which is lower on an ultimate basis. I have challenged AmTrust around the reasonableness of reserve risk being lower on an ultimate basis. There are two main differences between 1-year and ultimate reserve risk:

- The ECM first models ultimate reserve risk, and then produces 1-year reserve risk by determining a proportion of a proportion of the ultimate risk to be "recognised" in the first year.
- On a 1-year basis, reserve risk includes potential movements in the risk margin over one-year. On an ultimate basis, the risk margin is fully released, and reserve risk can be offset by the amount of the starting risk margin.

I consider the amount of risk recognised in the first year to be relatively conservative given the long-tailed nature of the risks written by AEL. From my review of their parameterisation of the ECM, AEL take the highest assumption from the various methods considered and so are potentially overstating the 1-year risk. In particular, they are recognising 75% of medical malpractice reserve risk within year one. I consider this to be a conservative assumption, based on my wider experience of modelling this class of business.

In addition, the methodology for assessing the movement in risk margin used by AEL is somewhat conservative. The risk margin is calculated based on a constant factor of liabilities. During extreme scenarios, the liabilities will be materially higher at the end of the year than they were at the beginning. The use of a constant factor will tend to overstate the risk margin after one year, which in turn overstates the increase in one-year reserve risk.

Overall, the reduction in reserve risk from 1-year to ultimate is more than offset by the increase in premium risk, leading to an overall increase in insurance risk for AEL from 1-year to ultimate.

- **Diversification allowance** – the diversification allowance shown above appears to be larger on an ultimate basis than on a 1-year basis. However, this is a knock-on effect from the market risk issues described above, whereby results are distorted by changes to the expected profit. Considering risk excluding this impact shows that the allowance for diversification is slightly lower on an ultimate basis than on a 1-year basis. This is in line with my expectations.

The ECM models insurance risk for more than 30 years into the future. No future investment returns are allowed for beyond 8 years as assets and liabilities are assumed to be perfectly matched and the unwinding of the discounting will offset investment returns. These are potentially prudent assumptions since if the modelling period was extended beyond 8 years, this would lead to a reduction in market risk and an increase in own funds ie increases in the SCR coverage ratio. I consider the assumptions made to be reasonable.

Credit risk (split between reinsurance credit and non-reinsurance credit risk) is higher on an ultimate basis than a 1-year basis. This is reasonable as, given the nature of the business written by AEL, it takes a long time for claims to be fully paid. Therefore, reinsurance credit risk exposures (the main driver of credit risk) is expected to emerge slowly as well. The emergence of non-reinsurance credit risk would be expected to emerge more quickly as it relates to amounts owed over a shorter time frame. As such, there would be no material difference in non-reinsurance credit risk over 1-year and ultimate.

I took additional comfort around the results of AEL's ECM through:

- the relative stability of the ratio of 1-year to ultimate SCR under the ECM and the 1-year SCR under the standard formula and ECM over the last few quarters;
- a review of the findings from an external validation review performed by an external consultancy firm in 2017 on the 1-year results of the AEL ECM. The review focused on all key risk types, with a focus on insurance risk, particularly in respect of medical malpractice business. The validation was performed by a firm independent of the model build and parameterisation. This review concluded that the modelling methodologies were reasonable and appropriate for the business and broadly in line with market practice. I agreed with the findings based on my own wider experience of validating capital models; and
- the degree of validation testing that AmTrust perform on this model, as described in the external validation review report, which I consider to be proportionate and in line with the level of testing I have seen for other insurers.

I have performed a similar comparison of AIU's 1-year and ultimate SCR as at 31 December 2018 derived under the ECM.

Comparison of 1-year and Ultimate AIU ECM results (€m)

Risk	ECM - 1-year basis	ECM – Ultimate basis
Insurance Risk	131.2	82.4
Credit Risk	58.1	145.1
Market risk	55.4	45.5
Operational risk	22.3	22.3
Undiversified SCR	267.0	295.3
Diversified SCR	**170.4**	**131.8**

For similar reasons as AEL, the 1-year SCR (€170.4m) is higher than on an ultimate basis (€131.8m).

For AIU, the reduction in reserve risk due to the unwinding of the risk margin is larger than the increase for premium risk on an ultimate basis and so the SCR decreases overall for insurance risk. I am satisfied with the reduction in AIU's reserve risk from a 1-year to ultimate basis. For similar reasons as AEL, I consider AIU's 1-year emergence factor assumptions and methodology for assessing the movement in risk margin to be somewhat conservative.

The reduction in market risk from 1-year to ultimate is smaller than for AEL which reflects that AIU has a greater proportion of assets invested in bonds, and no equities. As such, the assumed change in volatility over 1-year compared to ultimate is less significant compared to that for AEL.

For similar reasons as AEL, credit risk is higher on an ultimate basis than a 1-year basis as it is expected to emerge slowly over time.

Note that for AIU, operational risk in the ECM model is calculated using the standard formula and is assumed to be the same on a 1-year and ultimate basis.

Minimum Capital Requirement

Another key measure of capital under Solvency II is the Minimum Capital Requirement (MCR). This is a simpler calculation than the SCR and typically a less onerous requirement.

Both AEL and AIU are projected to be very well-capitalised on this measure. The MCR capital coverage ratios as at 31 December 2018 were 397% and 533% respectively. Therefore, I have not considered the MCR further as part of my assessment of capital considerations post-transfer, and my primary focus is on the SCR.

6.3. Components of capital requirements

The key components of the SCR common to AEL, AIU and AA are:

- *Insurance risk*, which is made up of:
  - *Premium r*isk: the risk that may arise from an inaccurate assessment of the risks associated with writing an insurance policy or from uncontrollable factors. As a result, the insurer's costs may significantly exceed premiums.
  - *Reserving risk*: the risk that the value of insurance claims proves to be higher than expected. For example, this covers the risk of deterioration in reserves or other catastrophe events, and uncertainties related to existing liabilities.
- *Credit (Counterparty default) risk*: the risk of defaults or downgrades by counterparties that either owe the insurer money or hold money on its behalf. For example, this covers the risk of the failure of a reinsurer or a broker.
- *Market risk*: the risk of changes in each insurer’s financial position due to changes in the market value of assets, liabilities and financial instruments. For example, this covers the risk of falls in the value of assets that are being held to make future claims payments.
- *Operational risk*: the risk of losses caused by failures in an insurer’s operational processes, people and systems, or from events that are external to the insurer. For example, this would cover the risk of fraud or IT failure.

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

The most material component of the SCR for AEL and AIU is non-life insurance risk, which represents 49% and 46% of the undiversified SCR respectively, as reported in AEL’s and AIU’s Solvency and Financial Condition Report as at 31 December 2018 (as calculated using the standard formula). This is expected given that insurance is the core business of AEL and AIU. The next material component of the SCR is market risk, representing 33% and 22% of the undiversified SCR for AEL and AIU respectively

Based on the calculations provided as at 30 June 2019, non-life insurance risk is also the most material component of the SCR for AA, accounting for c. 95% of the undiversified SCR. Whilst this proportion is projected to reduce over time, non-life insurance risk is still expected to be the most material component of the SCR for AA.

6.4. My considerations related to capital

As IE, my overall assessments related to capital are:

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

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

- The capital policy for each of AEL, AIU and AA (Section 6.6);
- SCR appropriateness for AEL, AIU and AA (Section 6.7);
- The SCR under stressed scenarios for AEL and AIU (Section 6.8);
- The planned capital structures for AEL, AIU and AA (Section 6.9); and
- Projected SCR coverage ratios (Section 6.10).

6.5. Approach to my review

I have reviewed several documents provided by AEL relating to the calculation of capital requirements and projected coverage ratios. A list of the key data and documentation reviewed is provided in Appendix 4.

I have also independently calculated selected aspects of the standard formula SCR calculation for AEL, AIU and AA using LCP's standard formula model and compared my results to those produced by AEL, AIU and AA.

6.6. The capital policy for each of AEL, AIU and AA

I have reviewed the capital policy for AEL and AA and the Risk Appetite Statement for AIU (as I understand there is no formal capital policy). There are no material differences between them. The risk appetite for the solvency coverage ratio is broadly consistent across all three entities with AEL and AIU targeting a 140% level and AA targeting 145%.

Insurers with a more diversified portfolio that write a number of classes of business that are not strongly positively correlated with each other, may benefit from the poor claims experience in one class of business being offset by favourable experience in another.

A mono-line insurer, like AA, potentially misses out on this benefit and could face a greater level of risk than had they written a more diversified range of business compared to writing almost exclusively Italian medical malpractice business. This is the main driver for AA targeting a higher SCR coverage ratio than AEL and AIU.

Being effectively a mono-line insurer could potentially lead to an insufficient level of reserves to meet AA's future claims or capital to support its business needs. This risk is actively considered in AA's assessments eg in the calculation of premium and reserving risk within the standard formula, AA benefit from a much smaller diversification credit than other insurers writing multiple classes of business would.

In my view, I believe it is appropriate that that AA is targeting a higher risk appetite SCR coverage ratio than AEL and AIU given the mono-line nature of the business written.

6.7. SCR appropriateness for AEL and AIU

I have considered the SCR appropriateness for AEL and AIU considering two aspects: the appropriateness of using the standard formula; and calculating my own independent estimates of the SCR.

Appropriateness of the standard formula for AEL

AEL has reviewed the appropriateness of the standard formula for calculating the SCR. A detailed review of the appropriateness of the standard formula was performed by AEL as part of the 2016 ORSA and not repeated in 2017 given there had been no material change in AEL's business.

I have reviewed AEL's ORSA and the justification for the use of standard formula and concluded that the use of standard formula appropriately captures the material risks that AEL is exposed to. I have compared each risk of the capital requirement derived under the standard formula and that under the ECM. There are risks that are not captured within the standard formula, but AEL regularly monitors these non-quantifiable risks. These include:

- Liquidity risk – AEL regularly reviews its liquidity position. In addition, this risk is mitigated as AEL's assets are mainly invested in relatively liquid corporate and government bonds.
- Group risk – AEL regularly monitor the failures or downgrades of the Parent Company and/or any other entity in the Group. AEL maintains a level of own funds ensuring it meets its agreed risk appetite. They also consider this risk explicitly as part of their ORSA.
- Legal and Regulatory risk – AEL mitigates this risk through consulting with their internal Group Legal and Compliance Function and external consultants and advisors as necessary.
- Strategic risk – AEL's strategy and business plan are reviewed annually in their ORSA and business performance is reviewed monthly.

AEL concluded that no adjustments or additional capital loads were required in addition to the SCR calculated using the standard formula. Based on my review of the description of the monitoring of non-quantifiable risks within AEL's ORSA I concluded that these risks were mitigated so that no adjustments were required to the SCR as calculated by the standard formula.

A further standard formula appropriateness review was performed in Q2 2019 by an external management consultancy firm. The findings of this assessment showed that if allowances were made in the standard formula for AEL's specific risk profile, ie by using USPs, the SCR would be c. 11% lower ie the SCR as calculated by the standard formula is conservative overall given AEL's risk profile.

I reviewed the methodology used by AEL's actuarial department in estimating volatility parameters specific to AEL's risk profile for premium and reserve risk. AEL used the prescribed approach set out by EIOPA for calculating USPs. I consider this to be reasonable and in line with how other insurers calculate USPs, either for use in the standard formula or in their own internal models. In addition, since the expert judgments applied by AEL in the parameterisation are back-tested against historical experience by line of business, this would implicitly reflect AEL's historical reserve deteriorations. Therefore, I am satisfied that AEL's USPs give due consideration to AEL's actual claims experience.

The analysis showed the volatility parameters for the medical malpractice business was lower than the standard formula parameters. A key reason for this was that the standard formula, for certain lines of business, does not allow for non-proportional reinsurance recoveries whilst AEL does have this type of reinsurance protection in place. In addition, where an adjustment non-proportional reinsurance is applied for certain lines of business in the standard formula, it is smaller than would be applied were AEL's own specific arrangements considered.

In addition, AEL's parameters are regularly validated through back-testing and scenario testing. For example, AEL performed scenario analysis in order to derive an alternative estimate of their general liability (predominantly medical malpractice) catastrophe SCR. It showed that an alternative approach led to a less than 0.5% increase in total diversified SCR compared to the standard formula SCR.

I am satisfied that the standard formula parameters are appropriate for the medical malpractice business as they indicate the standard formula was not understating the capital requirements for this line of business.

In 2018, an assessment of standard formula appropriateness was made by comparing the results of the standard formula SCR to that of AEL's own ECM. This model is based on the AmTrust syndicate model which is subject to Lloyd's validation requirements.

Lloyd's has been centrally reviewing the validation of the 80 or so syndicates in the Lloyd's market on an annual basis for 10 years and provides feedback on areas for improvements back to syndicates as part of their annual review. Their feedback to individual syndicates, including the AmTrust syndicate, helps to support and improve model methodology, the overall parameterisation process and model governance but not the specific parameters selected. Given this, I take some comfort that the ECM model can be used to provide limited support to the results of the standard formula SCR but have not placed too much reliance on this.

The 2018 assessment showed the standard formula SCR was higher than that based on AEL's ECM. Capital charges for some risks were higher and some lower when comparing across the two methods, but the resulting aggregation of risks meant that the SCR was higher overall under the standard formula compared to the ECM.

The ECM produces a lower aggregate capital requirement than the standard formula, mainly due to greater levels of assumed diversification. The ECM applies a number of correlation assumptions, for example between classes, types of losses and key risks. The standard formula has less correlation assumptions which are prescribed and have limited flexibility for insurers to adjust these for their own circumstances and views of the dependencies between risks.

Based on the assessment as at 31 December 2018, the 1-year SCR under the ECM (£190.2m) was c. 30% lower than under the standard formula (£266.6m). A comparison across risks is set out in the following table:

Comparison of 1-year SCR between the standard formula and AEL ECM (£m)

Risk	Standard Formula	ECM
Insurance Risk	166.2	170.1
Credit Risk	30.9	31.4
Market risk	105.8	112.6
Operational risk	30.9	40.2
Undiversified SCR	333.8	354.3
Diversified SCR	**266.6**	**190.2**

Across each risk type, the capital charge under the standard formula is lower than under the ECM. However, once risks are aggregated and diversification allowed for, the standard formula SCR is higher than the ECM over the 1-year time horizon.

There is more diversification in the ECM than the standard formula for the following reasons:

- there is less correlation assumed between the different risks than under the standard formula which leads to more diversification credit; and
- operational risk is diversified against other risks whereas it is added directly onto the SCR in the standard formula with no diversification credit allowed for. The approach under the standard formula is prudent.

Differences in the degree of diversification credit between the ECM and standard formula arise since the modelling approaches are different.

The ECM contains a number of implicit correlation assumptions (eg dependency between insurance and market risk through inflation) and explicit correlation assumptions applied through a copula approach with tail dependency (eg correlations between types of losses within a class and between classes in premium and reserving risk). The explicit correlation assumptions are based on AEL's judgment on the degree of dependency between risks.

The standard formula allows for diversification between sub-risk in each main risk category (eg 25% correlation between currency and interest rate risk within market risk) and between each main risk category (eg 25% correlation between non-life insurance and market risk). These correlations are prescribed with limited flexibility for adjustment to reflect own views of the degree of dependency.

Differences in the capital charges for the key risk types arise since the ECM models the risks differently to the standard formula.

- **Insurance risk** – under the ECM, premium and reserve risk are modelled on an ultimate time horizon with emergence factors applied to derive the risk over one year. This compares to the standard formula where prescribed risk factors are applied to premium and reserve volumes.
- **Market risk** – under the ECM, an economic scenario generator (ESG) is used to estimate market risk. The ESG allows for more granular modelling of the sub-risks that make up market risk than the standard formula.
- **Operational risk** – under the ECM, operational risk is set using a scenario-based approach, specific to AEL's risk exposure. The standard formula capital uses a factor-based approach which is applied to the earned premiums and technical provisions and then added on directly to the Basic SCR, with no diversification allowance made.

The ECM has been through independent external validation in 2017 which concluded that, although some areas for improvement were identified. I have reviewed the findings from this validation review, in particular the recommended areas of improvement, and compared this to my wider experience of validating capital models. I agreed with the findings of the review, in that, taken individually none of the improvements were considered to lead to a material mis-statement of the overall SCR. I concluded that the results of the ECM support the level of 1-year SCR calculated by the standard formula as this is not understated in comparison to the ECM SCR.

Conclusion on the appropriateness of the standard formula for AEL

I have reviewed the standard formula appropriateness assessments provided by AEL and the supporting analysis and I am satisfied that the standard formula is an appropriate basis for calculating the SCR for AEL for the following reasons:

- I believe the standard formula sufficiently captures the risks that AEL is exposed to. For risks that are not captured by the standard formula, these are regularly monitored and mitigated by AEL.

- The findings of the 2019 assessment show that AEL's SCR is conservative when allowing for AEL's specific risk profile.
- Based on the analysis as at 31 December 2018, the standard formula gives a higher capital requirement than both the 1-year and ultimate requirements as calculated by AEL's own ECM which has been externally validated, indicating that the standard formula was not understating the capital requirements.
- The standard formula results are broadly consistent each quarter which gives some assurance around the stability of the results.
- There are several uncertainties underlying the business written by AEL which could limit the appropriateness of AEL's own data to parameterise an internal model or apply USPs in the standard formula. These uncertainties include the lack of development history for some of the longer-tailed classes of business eg medical malpractice and the potentially volatile claims experience because of the small volume of some of the classes of business written.
- However, I am still satisfied to rely on analysis based on AEL's own data in forming my opinion because AEL's own incurred development for Italian medical malpractice business is different to that typically seen elsewhere and the allowance for development in claims beyond the data available is based on detailed discussions between the AmTrust actuarial team and the claims team in Milan and varies by claim type.

Independent calculation of the SCR for AEL

I have also performed an independent calculation of the material aspects of the standard formula SCR for AEL and compared my results to those produced by AEL. This is based on LCP's own standard formula model using data supplied by AEL.

My independent estimates support my conclusion that the standard formula SCR for AEL has been calculated materially correctly.

Appropriateness of the standard formula for AIU

AIU's most recent Actuarial Function Report (AFR) and other SCR comparison documentation, both dated December 2018, provides a summary of the actuarial function's view on the appropriateness of the standard formula for the purpose of calculating the SCR. The actuarial function concluded that the standard formula represents a conservative approach to setting capital.

I have reviewed AIU's AFR and the justification for the use of standard formula and concluded that the use of standard formula appropriately captures the material risks that AIU is exposed to. I have compared each main risk category of the capital requirements using the standard formula and using the ECM. For this review, I have relied on discussions with members of AmTrust's capital team and a review of the supporting documentation.

As for AEL, non-quantifiable risks that are not captured within the standard formula are regularly monitored by AIU. AIU concluded that no adjustments or additional capital loads were required in addition to the SCR calculated using the standard formula. Based on my review of the description of the monitoring of non-quantifiable risks within AIU's ORSA I concluded that these risks were mitigated so that no adjustments were required to the SCR as calculated by the standard formula.

A standard formula appropriateness review for AIU was performed in 2019 by an external consultancy firm. The findings of this assessment showed that if allowances were made in the standard formula for AIU's specific risk profile, through the use of USPs, the SCR would be at least 10% lower ie the SCR as calculated by the standard formula is conservative overall given AIU's risk profile. AIU's parameters are regularly validated through back-testing and scenario testing giving me comfort that they are reasonable. As for AEL, the rationale for the lower USPs is due to the allowance for non-proportional reinsurance which is not allowed for certain lines of business in the standard formula and so not reflective of AIU's specific risk profile.

As for AEL, in 2018 AIU performed an assessment of standard formula appropriateness by comparing the results of the standard formula SCR to that of AEL's own unapproved ECM. The AIU model is based on the AmTrust syndicate model which is subject to Lloyd's validation requirements. The model has been designed to reflect AIU's specific risk profile.

As for AEL, I take some comfort that the ECM model can be used to provide limited support to the results of standard formula SCR but have not placed too much reliance on this.

I consider it reasonable to use the results of the model as evidence to support the appropriateness of the use of the standard formula.

Based on the assessment as at 31 December 2018, the 1-year SCR under the ECM (€170.4) was c. 2% higher than under the standard formula (€167.7m) which I do not consider materially different. A comparison across key risks is set out in the following table:

Comparison of 1-year SCR between the standard formula and AIU ECM (€m)

Risk	Standard Formula	ECM
Insurance Risk	101.1	131.2
Credit Risk	41.5	58.1
Market risk	46.6	55.4
Operational risk	22.3	22.3
Undiversified SCR	211.5	267.0
Diversified SCR	**167.7**	**170.4**

The ECM produces a slightly higher aggregate capital requirement than the standard formula. Some elements of the ECM rely on the standard formula to calculate the capital requirement. For example, operational risk under the ECM is assumed to be equal to that derived using the standard formula. A future improvement is being considered where the ECM models operational risk based on risk scenarios specific to AIU. As operational risk is a relatively small driver of the SCR and would give more diversification credit if calculated in the ECM, I believe this is a reasonable approach.

The degree of diversification allowance is greater under the ECM than the standard formula. This is for similar reasons as for AEL. However, this is not enough to offset the higher level of capital, primarily in respect of insurance risk, under the ECM than under the standard formula. The reason for this difference is attributable to the modelling differences between how ECM models insurance risk compared to the standard formula.

A secondary driver for the difference is that for insurance risk, the ECM assesses the movement in the risk margin over the one year. However, the standard formula keeps the risk margin constant in the stressed scenario, as set out in Article 83 of the Delegated Act which governs Solvency II. Therefore, a more like-for-like comparison between the ECM and standard formula would be to exclude the risk margin movement from time 0 to time 1 from the ECM result. On this basis the SCR of €170.4m would reduce to €116.2m, driven by a reduction in insurance risk.

This reduction is overstated since the methodology for assessing the movement in risk margin used by AIU is somewhat conservative in that the risk margin is calculated based on a constant factor of liabilities. In the event of a stressed scenario, the liabilities will be materially higher at the end of the year than they were at the beginning, and so the use of a constant factor will tend to overstate the risk margin after one year and therefore the movement from time 0 to time 1.

Even with a much smaller reduction in the risk margin movement, the 1-year SCR under the standard formula would be greater than the 1-year SCR under the ECM. In addition, the 1-year SCR under the standard formula is also greater than the ultimate SCR under the ECM.

The re-domiciling of Maiden could mean that the use of the standard formula is less appropriate for calculating reinsurance credit risk. However, as noted earlier, Maiden has agreed an endorsement to its contract ensuring the SCR is at the same level as it would have been prior to any re-domicile. Therefore, with no change in reinsurance credit risk (and SCR), whether the standard formula is appropriate to calculate reinsurance credit risk post transfer is not relevant.

The standard formula still leads to a higher capital estimate than the ultimate ECM estimate, which is the basis to consider when looking at a transfer of these types of liabilities.

Conclusion on the appropriateness of the standard formula for AIU

I have reviewed the standard formula appropriateness assessments provided by AIU and the supporting analysis and I am satisfied that the standard formula is an appropriate basis for calculating the SCR for AIU for the following reasons:

- I believe the standard formula sufficiently captures the risks that AIU is exposed to. For risks that are not captured by the standard formula, these are regularly monitored and mitigated by AIU in a similar way to AEL.
- The findings of the 2019 assessment show that AIU's SCR is conservative when allowing for AIU's specific risk profile.
- Based on the analysis as at 31 December 2018, the standard formula gives a higher capital requirement than both the 1-year (after the risk margin allowance) and ultimate requirements as calculated by AIU's own ECM, indicating that the standard formula was not understating the capital requirements.
- The standard formula results are broadly consistent each quarter which gives some assurance around the stability of the results.
- The AIU model is based on a model for AmTrust Group's Lloyd's syndicate, which is subject to Lloyd's validation requirements. As for AEL, I take some comfort that the ECM model can be used to provide limited support to the results of the standard formula SCR but have not placed too much reliance on this.

Independent calculation of the SCR for AIU

I have performed an independent calculation of the material aspects of the standard formula SCR for AIU and compared my results to those produced by AIU. This is based on LCP's own standard formula model using data supplied by AIU.

My independent estimates support my conclusion that the standard formula SCR for AIU has been calculated materially correctly.

Appropriateness of the standard formula for AA

AA use the standard formula to calculate the SCR. I am not aware of any plans to develop an internal model in the short to medium term. Given the relative infancy of AA, and the potentially volatile claims experience because of small premium volumes and a lack of development history, this limits the use of AA's own data to parameterise an internal model or apply USPs in the standard formula without the need for significant expert judgement. I believe the use of the standard formula to calculate the SCR is materially appropriate.

Independent calculation of the SCR for AA

I have also performed an independent calculation of the material aspects of the standard formula SCR for AA and compared my results to those produced by AA. This is based on LCP's own standard formula model using data supplied by AA.

My independent estimates support my conclusion that the standard formula SCR for AA has been calculated materially correctly.

6.8. SCR scenario analysis

Within the 2018 ORSA for AEL, AIU and AA, several scenarios have been considered to understand the impact on the SCR coverage ratio, including combinations of scenarios. These scenarios do not take into account the impact of the various planned transfers.

In addition, the stresses between AEL, AIU and AA cannot be compared on a like-for-like basis due to the different risks each entity faces and that, post-transfer, the relativity of these risks changes.

AEL scenarios

For AEL, the key scenarios are:

1. **Lehman stress** – a fall in investment values in Q4 2018 comparable to that experienced following the collapse of Lehman in 2008.
2. **UK windstorm and flood** – a severe winter season across the South East of the UK and Northern Europe combined with two floods in the UK.
3. **Economic downturn** – a combination of a £30m investment value shock, 4% increase in claims reserves due to inflationary pressure and a reduction in new business volumes of 10% from 2019.
4. **Parent downgrade** – a downgrade in AmTrust Financial Services, Inc (AEL's ultimate holding company prior to the merger transaction with Evergreen Parent, GP on 29 November 2018).
5. **Yield curve up shock and inflationary strain –** considers the knock-on effects of an economic shock.
6. **Cyber-attack –** a cyber-attack that leads to three sources of loss including a regulatory fine of 5% of turnover, compensation payments and incurred costs remedying the causes of the attack.
7. **Reserve deterioration –** an increase in reserves that would be so severe to cause AEL to become insolvent.
8. **Reinsurer default** – default of Maiden and AII, two key reinsurers for AEL.

A summary of the impact of each scenario is set out below:

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AEL's risk appetite
1. Lehman stress	Leads to a reduction in the SCR (market risk) and eligible own funds. The SCR is not particularly sensitive to the scenario given market risk is not a key driver of AEL's capital position.	Whilst this scenario leads to a reduction in the SCR coverage ratio from the base scenario, it does not lead to a breach of AEL's risk appetite.

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AEL's risk appetite
2. UK windstorm and flood	Leads to a reduction in the SCR (non-life underwriting risk) and eligible own funds. Much of the loss would be reinsured through AEL's XoL programme and internal quota share arrangements with AII.	Whilst this scenario leads to a reduction in the SCR coverage ratio from the base scenario, it does not lead to a breach of AEL's risk appetite.
3. Economic downturn	Leads to a reduction in the SCR (market and non-life underwriting risk) and eligible own funds due to a fall in investments and premiums.	Over 2019 the solvency coverage ratio would reduce below AEL's tolerated risk appetite but then improve back during 2020.
4. Parent upgrade	A reduction in rating would lead to a reduction in new business volumes and therefore a reduction in non-life underwriting risk. AEL's counterparty default risk would increase as the downgrade would impact AII's rating. Eligible own funds would initially increase due the lower level of new business written.	Due to the increase in eligible own funds relative to a reduction in SCR, this would lead to an increase in AEL's coverage ratio.
5. Yield curve shock and inflationary strain	Would lead to an increase in reserves and therefore an increase in default risk and non-life underwriting risk. There would also be a reduction in market risk following the reduction in asset values. The level of eligible own funds would reduce.	The scenario would lead to an immediate reduction in the SCR coverage ratio to below AEL's risk appetite. Whilst this ratio is projected to increase from 2019, it would still be below AEL's risk appetite over this period, albeit only slightly by 2021 (139% versus 140%).
6. Cyber attack	Would lead to a larger reduction in the eligible own funds compared to the SCR.	The scenario would lead to an immediate reduction in the SCR coverage ratio to below AEL's risk appetite. The ratio is projected to increase back to AEL's risk appetite threshold from 2020.

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AEL's risk appetite
7. Reserve deterioration	This would lead to an immediate increase in the SCR, driven by reserve risk. There would also be a significant drop in eligible own funds, driven by the increase in technical provisions, and in AEL's SCR coverage ratio. This would lead to AEL's insolvency with no new business to be written.	The likelihood of an event of this size occurring is expected to be very remote, only once every 500 years. The SCR coverage ratio drops well below AEL's tolerated risk appetite which is not unexpected given the severity of the event.
8. Reinsurer default	The default of Maiden and AII would significantly increase non-life underwriting risk due to the increase in technical provisions. This would also lead to a fall in eligible own funds.	This scenario leads to a reduction in the SCR coverage ratio to below AEL's tolerated risk appetite. Whilst it does not lead to insolvency for AEL, it is not expected this ratio will increase back to base levels over the next three years. The reinsurance is collateralised.

I consider the scenarios modelled by AEL to be reasonable for the following reasons:

- The scenarios focus on the key risks that drive AEL's capital position.
- The impact of each scenario on the SCR and level of eligible own funds, relative to the base scenario, is directionally as expected.
- The impact of each scenario is considered beyond the next 12 months.
- In most scenarios, the solvency coverage ratio is expected to be above the risk appetite level by 2021 with the exception of Scenario 5 (only slightly below the risk appetite level), Scenario 7 (which is considered to be very remote) and Scenario 8 (which is also considered to be remote). I consider Scenario 8 to be remote on the basis of the respective financial strength of AII and Maiden and the collateralisation of the reinsurance. The planned re-domestication of Maiden also means they are legally required to provide additional collateral for its liabilities due to AEL. Management actions to address the failure of Maiden, and therefore the collateral, are described in AEL's Recovery Plan. These could include putting certain lines of business or the whole business into run-off and/or the suspension of dividend payments to manage the recovery back to risk appetite levels.
- The insolvency causing event (reverse stress test – scenario 7) for AEL is expected to be very remote. Despite the frequency of reserve deteriorations observed historically on the Italian medical malpractice business, I consider a deterioration across all classes of business of the size necessary to lead to

insolvency to be very remote. Based on AEL's ECM output, this has a 0.2% chance of occurring ie once every 500 years.

As part of AEL's 2018 year-end Solvency and Financial Condition Report (SFCR), a less severe reserve deterioration scenario was also considered. It showed a 25% increase in total claims provision leads to a c. 8% increase in AEL's 2018-year end SCR from £267m to £288m and a decrease in own funds from £347m to £280m. Overall, this led to a reduction in the 2018 year-end SCR coverage ratio from 130% to 97%.

I calculate this scenario to be broadly equivalent to a 10% increase in the total ULR at the whole account level. Although the ULR for earlier years in respect of medical malpractice business have deteriorated by up to c. 20%, more recent years have improved and the overall ULR for medical malpractice has remained broadly stable.

Given historically the Italian medical malpractice business has been the main source of reserve deteriorations, and that across all years combined the ULR has been broadly stable, I consider a c. 10% increase in the ULR for the whole account to be a reasonable stress scenario relative to AEL's own claims experience.

I expect the risk of future reserve deteriorations for AEL to be smaller post-transfer since the Italian medical malpractice business (the main source of historical reserve deteriorations) will transfer to AA. However, this risk would transfer to AA which I consider further under stress scenarios for AA. All else being equal, the Transferring AEL to AA Policyholders are more materially exposed to future reserve deteriorations (if past experience is an indicator of the future) than they would have been if they remained with AEL, since AA is a less diversified insurer than AEL.

Downside scenarios in respect of the medical malpractice book have been considered in the external regulatory review for AEL.

Most of the scenarios considered led to an increase in reserves which would be at the upper end of a range of reasonable best estimate of reserves. More extreme scenarios were considered but these relate to a series of less likely events.

Additional reserve deterioration and reinsurer default scenarios for AEL

I asked AmTrust to run some additional stress scenarios that consider:

- Strengthening of the Italian medical malpractice reserves;
- default of the reinsurance with Maiden and AII together with a default ('haircut') on the collateral of both Maiden and AII; and
- various combinations of these two scenarios with differing severities.

The stress scenarios are reverse stress scenarios in that they target various combinations of the level of reserve strengthening and reduction in collateral required to exhaust AEL's own funds and result in the SCR coverage ratio falling from 178% at Day 0 (30 June 2020) to 0%. At this point claims can still be paid in full as AEL's asset and liabilities are equal.

The results of the key scenarios are summarised in the table below.

	Reserve deterioration	Maiden and AII default	Collateral haircut	SCR coverage ratio
Base	**0%**	**No**	**0%**	**178%**
Scenario 1	229%	No	0%	0%
Scenario 2	104%	Yes	0%	0%
Scenario 3	7%	Yes	100%	0%
Scenario 4	56%	Yes	50%	0%

Scenario 1: In the event of no default, it would need to take a significant deterioration (229%) in the level of reserves on the Italian medical malpractice book to lead to exhaustion of the level of own funds. This deterioration would result in a level of reserves that I would consider to be significantly outside a range of reasonable best estimates and is much more severe than AEL's own historical experience. As a result, I consider Scenario 1 to be a very severe, and extremely remote, stress.

Scenario 2: In the event of default by Maiden and AII, but no haircut or reduction in the collateralised recoveries, the level of reserve deterioration necessary is smaller than in the event of no default but still significant (104%). This deterioration would result in a level of reserves that I would still consider to be materially outside a range of reasonable best estimates and AEL's own experience. As a result, I consider Scenario 2 to also be a very severe, and remote, stress.

Scenario 3: Should the full amount of the collateralised recoveries not be available, it would only require a 7% deterioration in the level of reserves in the event of default by Maiden and AII to lead to an exhaustion of the level of own funds. The form of the collateral is a mixture of cash and corporate bonds, is ring-fenced and held in trust by State Street for the sole benefit of AEL. Therefore, I consider it remote that no collateralised recoveries would be available if called upon.

Scenario 4: This considers a more realistic, if still unlikely, scenario where a 56% deterioration in reserves is combined with reinsurer default and a 50% collateral haircut.

The severity of the stresses considered above lead me to conclude that even in the event of an extreme or unlikely combined scenario where there is a severe deterioration in reserves and/or default by Maiden and AII with loss of collateral still allows all claims to be met by AEL. Scenarios 2 to 4 are particularly strong to the extent that they assume no recoveries from AII and Maiden above the level of collateral held.

I have considered the impact of a similar combination of stress scenarios on AA on Day 1 and note that less severe stresses are required to lead to a drop in AA's SCR coverage ratio to 0%, than for AEL on Day 0. This is to be expected given AA is a less diversified insurer than AEL and so the offsetting benefit of experience on other classes of business is limited. I consider this further below where I discuss the results of the AA post-transfer scenarios.

AIU scenarios

For AIU, the key downside scenarios are:

1. **Reserve deterioration** – An increase in reserves equivalent to a 1 in 10-year event. This represents the risk that AIU's provisions turn out to be inadequate.
2. **Economic downturn** – a combination of an increase in incurred claims equivalent to a 1 in 5-year event, a 5% loss on debtors and a discontinuation of mortgage business.
3. **Reinsurer default** – default of Maiden and AII, two key reinsurers for AIU. This is a reverse stress test for AIU ie a what-if scenario to assess what level of reinsurer default could threaten solvency.

A summary of the impact of each scenario is set out below:

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AIU's risk appetite
1. Reserve deterioration	The scenario leads to an increase in the non-life underwriting risk. This is partially offset by a reduction in market risk due to the reduction in net asset values. Overall this leads to an increase in the SCR. The level of eligible own funds also reduces in this scenario.	The scenario would lead to a reduction in the SCR coverage ratio in 2020 and 2021 relative to the base scenario. It is expected to only just fall below AIU's tolerated risk appetite level in 2020 before improving in 2021.
2. Economic downturn	The increase in SCR is driven by an increase in counterparty default risk. Similarly, the scenario leads to a reduction in the level of eligible own funds.	Whilst the scenario would lead to a reduction in the SCR coverage ratio relative to the base scenario, it is still above AIU's tolerated risk appetite level.

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AIU's risk appetite
3. Reinsurer default	The default of Maiden and AII would significantly increase non-life underwriting risk due to the increase in technical provisions. This would also lead to a significant fall in eligible own funds. This would lead to AIU's insolvency with no new business to be written.	The likelihood of this event occurring is expected to be very remote. The SCR coverage ratio drops well below AIU's tolerated risk appetite which is not unexpected given the severity of the event and AIU's dependency on its reinsurance arrangements.

I consider the scenarios modelled by AIU to be reasonable for the following reasons:

- The scenarios focus on the key risks that drive AIU's capital position. The Reserve and Economic stresses are reasonably likely representing, respectively, 1-in-10 and 1-in-5 year events.
- The impact of each scenario on the SCR and level of eligible own funds, relative to the base scenario, is directionally as expected.
- The impact of each scenario is considered beyond the next 12 months. In each scenario, the solvency coverage ratio is expected to be above the risk appetite level by 2021.
- The insolvency causing event (reverse stress) for AIU is expected to be very remote. I consider this to be reasonable on the basis of the respective financial strength of AII and Maiden and the collateralisation of the reinsurance. AIU's ORSA describes the management actions in the event of reinsurer default. Management would place AIU into solvent run-off.

AA scenarios

For AA, the key downside scenarios are:

1. **Reserve deterioration** – an increase in reserves equivalent to a 10% increase in loss ratio across all lines of business.
2. **Economic downturn** – a c. 7% reduction in market values of all assets held in 2020.
3. A combination of the two scenarios above.
4. **Reverse stress** – four reverse stress scenarios were considered:

4.1 A deterioration in loss ratio on the medical malpractice business that leads to a reduction in the SCR coverage ratio to 100% (equivalent to an increase in loss ratio from 65% to 200% and a simultaneous increase in the retained portion per claim increasing from €2.5m to €5.0m).

4.2 No recoveries from the excess of loss reinsurance treaty.

4.3 An increase in AA's retention of each claim from €2.5m to €10.0m.

4.4 An increase in premium income in 2020 from €90m to €135m without an increase in own funds.

A summary of the impact of each scenario is set out below:

Scenario	Impact on SCR/eligible own funds relative to base scenario	Impact on AA's risk appetite
1. Reserve deterioration	This scenario leads to a gradual reduction in the SCR coverage ratio driven primarily by a reduction in the level of own funds through to 2021. The SCR also increases over the period, driven primarily by an increase in insurance risk.	The SCR coverage ratio decreases from AA's risk appetite level of 145% to 117% by 2021.
2. Economic downturn	This scenario leads to a gradual reduction in the SCR coverage ratio driven primarily by a reduction in the level of own funds through to 2021. The SCR also reduces over the period driven primarily by a reduction in market risk.	The SCR coverage ratio decreases from AA's risk appetite level of 145% to 130% by 2021.
3. Combined reserve deterioration and economic downturn	This combined scenario leads to a greater proportionate reduction in the level of own funds than in the SCR.	The SCR coverage ratio decreases from AA's risk appetite level of 145% to 113% by 2021. This reduction in SCR coverage ratio is greater than Scenarios 1 and 2 individually given the greater proportionate reduction in the level of own funds than the SCR.
4.1. Reverse stress test	A reduction in level of own funds from €50.9m to €42.1m and an increase in the SCR from €35.1m to €42.0m.	This leads to a reduction in AA's SCR coverage ratio from 145% to 100%.
4.2. Reverse stress test	No change in the level of own funds but an increase in the SCR from €35.1m to €56.1m.	This leads to a reduction in AA's SCR coverage ratio from 145% to 91%.
4.3. Reverse stress test	A reduction in level of own funds from €50.9m to €48.1m and an increase in the SCR from €35.1m to €61.3m.	This leads to a reduction in AA's SCR coverage ratio from 145% to 78%.
4.4. Reverse stress test	No change in the level of own funds but an increase in the SCR from €35.1m to €44.7m.	This leads to a reduction in AA's SCR coverage ratio from 145% to 114%.

I consider the scenarios modelled by AA to be reasonable for the following reasons:

- The scenarios focus on the key risks that drive AA's capital position. Given the potential range of best estimate reserves for medical malpractice business and associated uncertainty, Stress 1 and 4.1 focus on the potential for deterioration in claims experience from different perspectives.

For stress 1, a 10% increase in loss ratio across all lines of business is effectively equivalent to a 10% increase in loss ratio for Italian medical malpractice business. An increase in overall loss ratio across the book would be more severe than what AEL has historically observed on its Italian medical malpractice book (recognising older underwriting years have deteriorated whilst more recent years have improved). Therefore, I consider this scenario to be reasonable.

For stress 4.1, an increase in loss ratio of this magnitude would be significantly greater than what AEL has historically observed. I consider the likelihood of this occurring to be remote but as demonstrated, pre-transfer, it only leads to a drop in AA's SCR coverage to 100%.

- The impact of each scenario on the SCR and level of eligible own funds, relative to the base scenario, is directionally as expected.
- The impact of each scenario is considered beyond the next 12 months and, apart from the reverse stress tests, leads to an SCR ratio in excess of 100%.
- The insolvency causing events (reverse stress tests) are expected to be extremely remote.

I consider that AEL, AIU and AA have demonstrated resilience to reasonably severe shocks which are designed to capture the risks that each entity faces.

Post-Transfer scenarios

AEL scenarios

AEL, as part of their 2019 ORSA, have considered scenarios to understand the potential impact on the post-transfer SCR coverage ratio of specific risks. The description and results of the key scenarios that have a material impact on the coverage ratio are as follows:

- **Yield curve and inflation shock** - risk-free yields increase by 1% pa for Sterling and Euro and an increase in claims inflation of 2.24% pa.
- **Swiss Re termination** – Non-renewal of the Swiss Re quota share programme from 1 July 2020 with no alternative reinsurance in place.
- **Reinsurer default** – all reinsurers default with no replacement from 1 January 2020.
- **Insurance market crisis** – assumes all AEL's reinsurers default from 1 January 2020 and a further reduction in investment of c. £391m.
- **Combined scenario** – this assumes a combination of three separate impacts:

- Non-renewal of the Swiss Re quota share programme from 1 July 2020 with no alternative reinsurance in place.
- Increase in loss ratios for the after the event (ATE) business at a 75% confidence level.
- Cyber loss of £120m on 1 January 2020.

As noted earlier, there is no impact on AEL of default of Maiden post-transfer since Maiden only covered Italian medical malpractice business which would have already transferred to AA.

	Q2 2020	Q4 2020	Q4 2021	Q4 2022
Base	**150%**	**161%**	**179%**	**185%**
Scenarios				
Yield curve and inflation shock	133%	142%	159%	166%
Swiss Re termination	150%	156%	149%	146%
Reinsurer default	129%	136%	148%	151%
Insurance market crisis	39%	45%	60%	73%
Combined scenario (as above)	150%	152%	143%	142%
Movement from base				
Yield curve and inflation shock	(17%)	(19%)	(20%)	(18%)
Swiss Re termination	0%	(5%)	(30%)	(39%)
Reinsurer default	(21%)	(25%)	(31%)	(33%)
Insurance market crisis	(111%)	(116%)	(119%)	(112%)
Combined scenario (as above)	0%	(8%)	(36%)	(43%)

These scenarios are used for tracking against business plan expectations during 2020. As a result, the base results are not exactly comparable to the capital projections derived when assessing the impact of the transfers on SCR coverage ratios. However, I still believe these ORSA scenarios to be materially appropriate for use in my assessment of the impact of the stresses on AEL on a post-transfer basis.

The insurance market crisis leads to SCR coverage ratios significantly below the 100% level and a breach of AEL's MCR ie insolvency. The management actions upon resolution have not been modelled in this scenario, as such the SCR coverage ratio continues to remain below AEL's risk appetite level by 2022. I consider this scenario to be extremely remote given the relative financial strength of AEL's reinsurers. In addition, due to AEL's fairly cautious investment strategy, a reduction in investments of that size would be unlikely.

All other scenarios lead to less notable reductions in the SCR coverage ratio post-transfer. In order to ensure AEL is sufficiently capitalised relative to its own risk appetite level of 140%, additional capital would be required from AEL's parent in respect of the yield curve and inflation shock and reinsurer default scenarios.

The increase in yields leads to a decrease in technical provisions and investments, whilst claims inflation leads to an increase in loss reserves and loss ratios on unearned and new business. The overall increase in technical provisions would lead to an increase in the SCR and reduction in own funds.

Reinsurer default leads to a notable increase in SCR, driven by an increase in premium and reserve risk through a lack of reinsurance recoveries that would have otherwise been available. The increase in level of own funds is more than offset by the increase in SCR.

The termination of the Swiss Re quota share programme would lead to an increase in own funds relative to the base scenario as expected profits are no longer ceded to Swiss Re. However, this is more than offset by the increase in SCR following an increase in net exposures.

For similar reasons as for the pre-transfer scenarios modelled for AEL as part of their 2018 ORSA, I consider the scenarios modelled here to be reasonable. I consider that AEL has demonstrated resilience to reasonably severe shocks, designed to reflect the key risks it faces, post-transfer.

AIU scenarios

AIU, as part of their 2019 ORSA, have considered scenarios to understand the potential impact on the post-transfer SCR coverage ratio of specific risks. The description and results of the key scenarios that have a material impact on the coverage ratio are as follows:

- **Swiss Re termination** – In this scenario, the quota share with Swiss Re is not renewed at the scheduled date of 1 July 2020 and is not replaced by any additional cover over the remainder of the projection period.
- **Wider insurance stress** – The wider insurance stress consists of an increase in ultimate loss ratios (ULRs) in line with the 80th percentile of the AIU economic capital model. There is also a downgrade of the credit rating for all reinsurance partners.
- **Deterioration in medical malpractice experience** – This scenario, includes an increase in the ULRs for the Italian Medical Malpractice business line equivalent to the 80th percentile worst result. In this scenario the portfolio transfer of the Italian Medical Malpractice business is delayed by one year and takes place on 1 July 2021.

- **Lehman asset shock** – This scenario involves a shock to investments in line with the stresses that occurred following the default of Lehman Brothers in 2008. The haircut to assets impacts both the investments held on AIU's balance sheet and the collateral held against the reinsurance exposures to Maiden and AII.
- **Cyber stress** – The cyber stress scenario, consists of a single operational loss of €101m on 1 July 2020.
- **Reverse stress** – The reverse stress, takes the form of the loss of the Swiss Re quota share reinsurance from 1 July 2020 and an operational shock of €101m from a cyber event occurring at the same time.

There is no impact on AIU of default of Maiden post-transfer since Maiden only covers Italian medical malpractice business which would have transferred to AA.

	Q2 2020	Q4 2020	Q4 2021	Q4 2022
Base	**150%**	**150%**	**154%**	**154%**
Scenarios				
Swiss Re termination	146%	140%	129%	127%
Wider insurance stress	108%	129%	135%	136%
Deterioration in medical malpractice experience	124%	119%	144%	145%
Lehman asset shock	144%	145%	148%	150%
Cyber stress	150%	112%	115%	116%
Reverse stress	146%	103%	95%	95%
Movement from base				
Swiss Re termination	(4%)	(10%)	(25%)	(27%)
Wider insurance stress	(42%)	(21%)	(19%)	(18%)
Deterioration in medical malpractice experience	(26%)	(31%)	(10%)	(9%)
Lehman asset shock	(6%)	5%)	(6%)	(4%)
Cyber stress	0%	(38%)	(39%)	(38%)
Reverse stress	(4%)	(47%)	(59%)	(59%)

As for AEL, these scenarios are used for tracking against business plan expectations during 2020. As a result, the base results are not exactly comparable to the capital projections derived when assessing the impact of the transfers on SCR coverage ratios. However, I still believe these ORSA scenarios to be materially appropriate for use in my assessment of the impact of the stresses on AIU on a post-transfer basis.

The reverse stress test leads to SCR coverage ratios below the 100% level but not a breach of AIU's MCR ie insolvency. It demonstrates AIU's relative resilience to losses of this size and nature.

All other scenarios lead to smaller reductions in the SCR coverage ratio post-transfer. To ensure AIU is sufficiently capitalised relative to its own risk appetite level of 140%, additional capital would be required from AIU's parent in respect of a number of these scenarios.

The wider insurance stress would lead to a notable reduction in SCR coverage ratio as at Q2 2020. This is not unexpected given the relative severity of the deterioration in claims experience equivalent to a 1-in-5-year event which would reduce the level of own funds and increase in SCR. The increase in SCR would be driven by an increase in reserve risk and counterparty default risk as a result of the downgrade in the credit ratings of reinsurers.

The termination of the Swiss Re quota share programme would lead to an increase in own funds relative to the base scenario as expected profits are no longer ceded to Swiss Re. However, this is more than offset by the increase in SCR following an increase in net exposures.

The deterioration in medical malpractice experience, leading to a delay in the transfer of one year, would lead to a notable reduction in coverage ratio in 2020 driven by a decrease in own funds and increase in SCR. However, AIU's SCR coverage ratio is expected to increase to above risk appetite levels by the end of 2021.

The Lehman shock has a relatively small impact on AIU's coverage ratio which is not unexpected given AIU's fairly cautious investment strategy limiting their potential exposure.

The cyber shock would lead to a notable reduction in AIU's SCR coverage ratio through a reduction in level of own funds. However, this is partially offset by a corresponding reduction in the tax liability.

For similar reasons as for the pre-transfer scenarios modelled for AIU as part of their 2018 ORSA, I consider the scenarios modelled here to be reasonable. I consider that AIU has demonstrated resilience to reasonably severe shocks, designed to reflect the key risks it faces, post-transfer.

AA scenarios

Additional reserve deterioration and reinsurer default scenarios

I asked AmTrust to perform similar scenarios for AA on Day 1 to those AEL on Day 0 to compare the risks faced by the Transferring AEL to AA Policyholders pre- and post-transfer.

Again, the stress scenarios were set to a level of severity that would lead to the exhaustion of all the own funds for AA ie a drop in the level of own funds from €332.4m to zero and an SCR coverage ratio from 150% to 0%.

The results of these stresses are summarised in the table below.

	Reserve deterioration	Maiden and All default	Collateral haircut	SCR coverage ratio
Base	**0%**	**No**	**0%**	**150%**
Scenario 1	138%	No	0%	0%
Scenario 2	48%	Yes	0%	0%
Scenario 3	0%	Yes	68%	0%
Scenario 4	30%	Yes	25%	0%

Comparing the impact of these scenarios on AA post-transfer to AEL pre-transfer, the level of stress required to lead to full exhaustion of AA's level of own funds is lower ie the impact of similar stresses is higher. The risks face by the Transferring AEL to AA Policyholders are higher post-transfer than pre-transfer. This is to be expected given AA is a less diversified insurer than AEL and so the offsetting benefit of experience on other classes of business is limited.

Scenario 1: A 138% reserve deterioration in AA's Italian medical malpractice reserves is required to lead to exhaustion of own funds compared to a 229% deterioration for AEL pre-transfer.

Scenario 2: A 48% deterioration in reserves for AA, combined with Maiden and AII default, but no haircut or reduction in the collateralised recoveries, is necessary to lead to a 0% SCR coverage ratio. This compares to a 104% deterioration in reserves for AEL. A 48% reserve deterioration is above that seen historically and I consider such a deterioration to be unlikely.

Scenario 3: A 0% deterioration in reserves for AA, combined with Maiden and AII default and a 68% haircut on collateral, is necessary to lead to a 0% SCR coverage ratio. This compares to a 7% deterioration in reserves, and a 100% haircut on collateral, for AEL.

Scenario 4: For AA 30% deterioration in reserves combined with reinsurer default and a 25% collateral haircut reduces own funds to zero compared to 56% and 50% respectively for AEL. A 30% reserve deterioration would be outside what I consider a range of reasonable best estimates and is beyond that seen historically but is a plausible level of deterioration to consider as a stress scenario.

Scenarios 2 to 4 are particularly strong to the extent that they assume no recoveries from AII and Maiden above the level of collateral held.

In these scenarios, Transferring AEL to AA Policyholders would be disadvantaged by the Proposed Transfer. However, I believe this disadvantage is offset by the benefits of the Proposed Transfer to Transferring AEL to AA Policyholders. These include the removal of uncertainty of not having claims paid due to unsuccessful trade negotiations by the end of the Brexit transitional period. Further, it is my view that the Transferring AEL to AA Policyholders would prefer to be supervised by IVASS, their national regulator, rather than an overseas regulator.

Existing AA policyholders are also disadvantaged by the Proposed Transfer as they are now exposed to the risk of default by Maiden whereas pre-transfer they are not. However, I consider the risk to be remote given that the collateral will be ring-fenced for the benefit of AA and held in trust.

6.9. The planned capital structures for AEL, AIU and AA

No material change is planned to AEL's and AIU's capital structure post-transfer. Virtually all of AEL's and AIU's own funds were classified as unrestricted tier 1, ie the highest quality. Less than 6% of AIU's own funds sat in a restricted ring-fenced fund. A solvency coverage ratio of 150% is targeted for AEL and AIU post-transfer, higher than the current risk appetite for both entities of 140%.

For AA, a higher risk appetite solvency coverage ratio of 145% is targeted reflecting the concentration of medical malpractice business within this entity. However, post-transfer a solvency coverage ratio of 150%, in excess of the risk appetite, is targeted.

AEL has confirmed that they will look to maintain targeted capital coverage levels across each entity post-transfer.

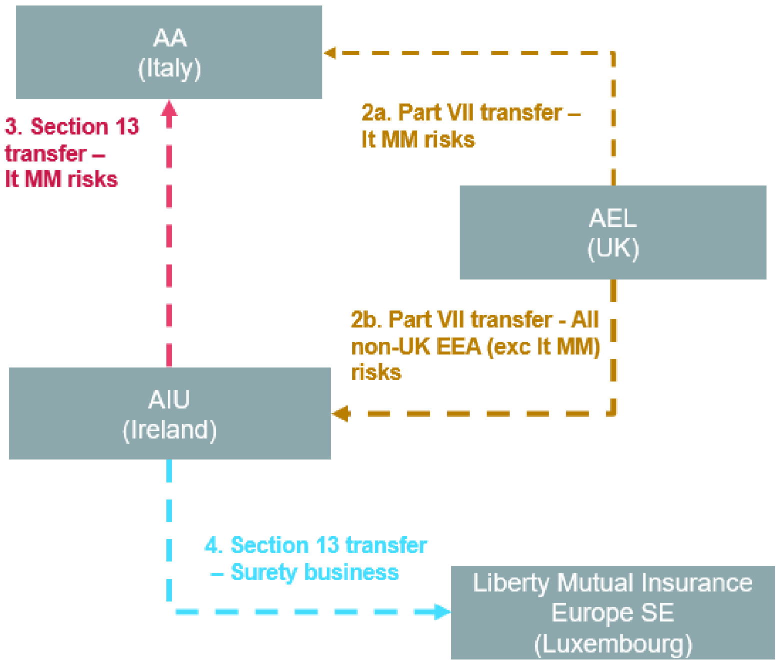
AEL and AIU will transfer to assets to AA equal to the technical provisions and other net liabilities related to the Proposed Transfer.

AEL and AIU will also pay dividends to their parent companies equal to any capital in excess of 150% of their SCR after taking into account the various planned transfers. These dividends will then be used, as needed, by the Group to fund the capital needs of AA up to a 150% SCR coverage ratio following the execution of the transfers.

6.10. Projected SCR coverage ratios

The following tables set out the SCR coverage ratios for AEL, AIU and AA pre- and post-the Proposed Transfer. Day 0 is the day before the Effective Date of the Proposed Transfer (1 July 2020) ie pre-transfer and Day 1 is the day after the Effective Date ie post-transfer.

The first table below represents the expectation that both parts of Transfer 2 ie the Proposed Transfer (2a: AEL to AA and 2b: AEL to AIU) and Transfer 3 (AIU to AA) proceed on the Effective Date, as set out in the following diagram. Please refer to Section 2.2 for more detail on these transfers.



* It MM = Italian Medical Malpractice

Note that in the figures presented below, Transfer 4 is assumed to have already taken place given it has an Effective Date of 31 March 2020 ie before the Effective Date of the Proposed Transfer.

The figures below are projections, and I will comment on any updates to the figures in my Supplementary Report.

SCR and coverage ratios pre- and post- the Proposed Transfer and Transfer 3

	SCR coverage ratio	Change in coverage ratio	Own funds (£m)	SCR (£m)	Own funds less SCR (£m)
Day 0 – pre-Transfer					
AEL	178%		381.2	213.8	167.5
AIU	160%		233.0	145.3	87.7
AA	145%		107.0	73.8	33.2
Day 1 – post-Transfer					
AEL (2a ☑, 2b ☑)	150%	(28%)	229.4	153.2	76.2
AIU (2b ☑, 3 ☑)	150%	(10%)	207.5	138.5	69.0
AA (2a ☑, 3 ☑)	150%	+5%	286.7	191.5	95.2

Source: AmTrust. Figures converted assuming £1 = €1.16.
Key: ☑ - transfer expected to take place, ☒ - transfer not expected to take place

In summary:

- AEL: the SCR coverage ratio of Non-transferring AEL Policyholders is projected to decrease from 178% to 150%. However, AEL is still projected to be well-capitalised (as defined in Section 6.1) and this level of coverage is above AEL's risk appetite. In addition, AEL's coverage ratio is expected to return to pre-transfer levels (178%) by June 2021 ie within a year of the Proposed Transfer.
- AIU: the SCR coverage ratio for AIU Policyholders is expected to decrease from 160% to 150%. However, AIU is still projected to be well-capitalised (as defined in Section 6.1) and this level of coverage is above AIU's risk appetite. In addition, AIU's coverage ratio is expected to increase to 170% (assuming the transfer from AMIL to AIU takes place as planned) by December 2021 ie within 18 months of the Proposed Transfer.
- AA: the SCR coverage ratio for AA Policyholders is expected to increase from 145% to 150%, ie above AA's risk appetite level of 145%. AA becomes well-capitalised (rather than having sufficient capital) as a result of the Proposed Transfer. In addition, AA's coverage ratio is expected to increase to 168% by December 2021 ie within 18 months of the Proposed Transfer. Whilst the AEL and AIU policyholders transferring into AA will be moving from more diversified insurers to a predominantly monoline insurer, I am satisfied they are not materially

disadvantaged as I consider AA to be a well-capitalised insurer like AEL and AIU. Furthermore, the AEL and AIU policyholders transferring into AA Italian medical malpractice insurance cover, may prefer to be supervised by IVASS, the Italian regulator, and benefit from the reduced uncertainty around contract continuity after the Brexit transitional period.

- The SCR coverage ratio for Transferring AEL to AIU Policyholders and Transferring AEL to AA Policyholders is projected to decrease from 178% to 150%. For the same reasons as the Non-Transferring AEL Policyholders, I have concluded that they will not be materially adversely affected.
- AmTrust Financial Services, Inc, (AFSI) will provide such capital injections/measures as are necessary into AA from outside of the AmTrust European Group to support the Proposed Transfer and fund the post-transfer SCR coverage ratios of 150% after taking into account, transfers of capital from other European entities and other capital measures such as reinsurance available to AA. If no reinsurance or other capital measures are executed prior to the transfer date, the Group would provide, based on current capital projections, capital injections as follows:

Injection	€m	Timing
Into AA	66.0	On or before 31 March 2020
Into AA	25.9	On or before 30 June 2020
Into AEL	10.0	On or before 30 September 2020
Total	**102.0**	

An update on the cash injections and other measures will be detailed in my Supplementary Report.

In section 7.2 we show how the total assets and total liabilities on a GAAP basis are expected to change as a result of the Proposed Transfer from Day 0 to Day 1. The capital injection into AA of €66.0m will not be reflected in a comparison of Day 0 and Day 1 movements as it takes place before Day 0. Similarly, the €10.0m injection takes place after Day 1 and so is not reflected in the movement between Day 0 and Day 1.

Of the €25.9m injection on or before 30 June 2020, only €9.3m of this relates to the Proposed Transfer and the balance will be injected regardless of whether the Proposed Transfer takes place or not. This broadly equates to the difference, after converting to Sterling, of c. £6m in total assets on a GAAP basis for AEL, AIU and AA combined between Day 0 to Day 1 (see section 7.2 for more detail).

After the conversion from GAAP TPs to Solvency II TPs, the increase in the combined level of own funds is from £721.2m at Day 0 to £723.5m at Day 1, ie £2.3m (c. 1%).

AEL's SCR coverage ratio is projected to increase from 142% as at 30 June 2019 to 148% as at 31 December 2019 to 178% at Day 0 ie the point of the Proposed Transfer. The increase is primarily driven by a reduction in the SCR over the period and, to a lesser extent, an increase in level of own funds. I am satisfied that this increase is reasonable for the following reasons:

- A projected reduction in SCR over the period due to:
  - a reduction in non-life insurance risk following a reduction in earned premium as AEL, over the course of 2019, has put a number of poorer performing accounts into run-off. This is a key input into the standard formula calculation; and
  - a reduction in operational risk caused by a reduction in the gross TPs as they focus on writing more of the better performing lines of business. Again, this is a key input into the standard formula calculation.
- An increase in own funds due to a decrease in business on lines that now no longer contribute to business strain and also profit from the run-off of the remaining lines of business.
- The introduction of the 50% quota share arrangement with Swiss Re from 1 July 2019 which also reduces new business strain.

A quantitative breakdown of the key drivers of the change in coverage ratio is set out in the table below.

	Movement %	SCR coverage ratio %
SCR coverage ratio as at Q2 2019		**142%**
Impact of:		
Lower technical provisions	24%	
Reduction in earned premiums	20%	
Swiss Re contract	9%	
Other (reduction in own funds and increase in market risk)	(16%)	
Projected SCR coverage ratio as at Q2 2020		**178%**

The Day 0 SCR coverage ratio is sensitive to changes in the level of reserves and stresses to asset values. Based on Day 0, a 10% increase in reserves would lead to a reduction in the coverage ratio from 178% to 160%. Similarly, a £30m reduction in asset values (approximately 8% of own funds) would lead to a reduction in coverage ratio from 178% to 165%.

AIU's SCR coverage ratio is projected to increase from 146% as at 31 December 2019 to 160% at Day 0 ie the point of the Proposed Transfer. As for AEL, the increase in coverage ratio is primarily driven by a reduction in the SCR over the period and, to a lesser extent, an increase in level of own funds. For similar reasons for AEL, I am satisfied the increase is reasonable.

Market comparison of SCR coverage ratio

LCP perform an annual market review of Solvency II reporting across the UK and Ireland. I have compared the targeted coverage ratio of 150% for each AmTrust entity against, firstly, the full sample of insurers analysed and, secondly, by insurer type.

In the market review, we classified each insurer according to whether more than 50% of their gross written premiums were written in a single Solvency II line of business. If not, they were classified as multi-line insurers. The split of AEL and AIU's gross written premiums by material Solvency II line of business as at 31 December 2018 is as follows:

Solvency II line of business	AEL
Miscellaneous financial loss	32%
General Liability	31%
Legal Expenses	17%
Fire and damage	7%
Other	12%
Total	**100%**

Solvency II line of business	AIU
General Liability	39%
Miscellaneous financial loss	31%
Credit and suretyship	17%
Fire and damage	8%
Other	5%
Total	**100%**

On this basis, based on 2018 year-end figures, both AEL and AIU would be classified as multi-line insurers but with a focus on miscellaneous financial loss and general liability business respectively. We consider this classification to be appropriate for benchmark comparison purposes given no Solvency II line of business dominates their respective business.

We would classify AA as a general liability insurer.

The key results from this market review are set out below:

	2018 SCR coverage ratio		
Type of insurer	**Average**	**25th – 50th percentile**	**50th – 75th percentile**
All	**206%**	**138% - 162%**	**162% - 208%**
General liability	218%	128% - 174%	174% - 305%
Miscellaneous financial loss	204%	140% - 149%	149% - 221%
Multi	165%	132% - 151%	151% - 183%

Source: LCP – Financial strength improves despite increasing risk – Solvency II reporting across the UK and Ireland (July 2019)

AEL and AIU's post-transfer SCR coverage ratios of 150% would be close to the 50th percentile of other multi-line insurers.

If we were to classify AEL and AIU based on the Solvency II line of business they write most business (on the basis they will be less diversified post-transfer), AEL would be a miscellaneous financial loss insurer and AIU a general liability insurer. AEL's target SCR ratio would be slightly above the 50th percentile for other miscellaneous financial loss insurers whilst AIU's would be around the 40th percentile for general liability insurers.

This analysis gives me comfort that the post-transfer coverage ratios of AEL and AIU are not out of line with the market.

Although the market analysis was based on UK and Irish insurers, there is benefit in comparing AA's post-transfer SCR coverage ratio to other general liability insurers in the review. AA's coverage ratio of 150% would be around the 40th percentile for general liability insurers sampled in the review. Therefore, I consider AA's post-transfer coverage ratio not to be out of line with the wider UK and Irish markets, albeit it is in the second quartile of the capital coverage ratios.

Reduction in SCR coverage ratio for AEL pre- and post-transfer

A 100% coverage ratio equates to the estimate of capital required to ensure that an insurer can meet its obligations over the next 12 months with a probability of at least 99.5%.

A coverage ratio of over 100% therefore corresponds to a risk of less than 0.5% or 1 in 200 that an insurer cannot meet its obligations over the next 12 months.

AEL has performed some analysis in their capital model on the difference in the level of risk between a coverage ratio of 178% and 150% and this was summarised in a paper provided to me. The analysis highlighted the post-transfer coverage ratio was still in excess of AEL's risk appetite. The results of the analysis showed that the drop from 178% to 150% was equivalent to an increase in the probability of policyholders not receiving all claim payments of less than 0.01% on an ultimate basis. This conclusion was reached through the use of AEL's ECM. There were no modelled scenarios in their internal model where, at these capital coverage levels, the losses within a year would exceed the own funds.

Given this small increase in probability of policyholders not receiving all claim payments, I am satisfied that policyholders are unlikely to be materially adversely affected by this fall in coverage ratio.

Risk beyond a 1-year basis is considered through scenario testing, looking at the impact of plausible and extreme events on the SCR coverage ratio beyond the next 12 months. This is in addition to a forward-looking assessment of capital requirements of the base scenario before considering the Proposed Transfer or any other changes in the structure of the business. In addition, AEL and AIU consider an ultimate view of capital through their internal model.

Conclusion

Based on my analysis, I do not expect there to be any material adverse changes in the strength of capital protection for any group of policyholders.

Contingencies

AmTrust has confirmed that the Proposed Transfer and Transfer 3 will go ahead irrespective of any trading arrangements agreed between the UK and EU following Brexit. They have also confirmed that, if for any reason one particular transfer, or part of a transfer, does not go ahead, all other transfers, or parts of transfers, will proceed.

I have considered the various permutations of transfers not proceeding as planned and set out my conclusions on this below from the perspective of the six groups of affected parties and the other three planned transfers. My conclusions in this regard are set out in the Executive Summary.

I have considered this further through assessing the impact of each permutation of transfers on SCR coverage ratios. Under all of these permutations, the projected SCR coverage for all entities is 150% ie well-capitalised. In addition, as demonstrated below, even without the transfer from AIU to AA (ie 2b ☑, 3 ☒), the projected SCR coverage for AIU and AA is expected to be 150% post the transfer of business from AEL to AIU and AA.

Hence the conclusions I drew earlier in this section remain appropriate. The various permutations of transfers are summarised in the table below:

SCR and coverage ratios pre- and post- transfer – other permutations

	SCR coverage ratio	Change in coverage ratio	Own funds (£m)	SCR (£m)	Own funds less SCR (£m)
Day 0 – pre-Transfer					
AEL	178%		381.2	213.8	167.5
AIU	160%		233.0	145.3	87.7
AA	145%		107.0	73.8	33.2
Day 1 – post-Transfer					
AEL (2a ☒, 2b ☑)	150%	(28%)	293.5	196.0	97.5
AEL (2a ☑, 2b ☒)	150%	(28%)	243.1	162.0	81.1
AIU (2b ☒, 3 ☑)	150%	(10%)	178.2	118.9	59.3
AIU (2b ☑, 3 ☒)	150%	(10%)	248.2	165.6	82.6
AA (2a ☒, 3 ☑)	150%	+5%	188.9	126.1	62.8
AA (2a ☑, 3 ☒)	150%	+5%	203.8	136.2	67.6

Source: AmTrust. Figures converted assuming £1 = €1.16.
Key: ☑ - transfer expected to take place, ☒ - transfer not expected to take place

In my assessment of the potential impact on policyholders of the various permutations of the transfers, I have considered the change in SCR coverage ratios. However, these are based on a 1-year regulatory view of capital and not a view of the capital required to run-off the business to ultimate.

I have also considered the results of AEL's and AIU's economic capital models, which indicate a level of ultimate capital lower than the 1-year standard formula view, and the use of stress scenarios for AEL, AIU and AA to help form my conclusions.

6.11. Overall conclusion: Capital considerations

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

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

- **The projected capital requirements for AEL, AIU and AA have been calculated appropriately for both non-transferring and transferring policyholders.**
- **Following the Proposed Transfer, I do not expect there to be any materially adverse changes in the strength of capital protection for any group of policyholders.**

7. Policyholder security

7.1. My considerations relating to policyholder security

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

- whether the likelihood of valid policyholder claims being paid is maintained following the Proposed Transfer for both non-transferring and transferring policyholders.
- whether any change in policyholder security results in policyholders being materially adversely affected by the Proposed Transfer.

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

- The GAAP balance sheets of AEL, AIU and AA (Section 7.2)
- The solvency positions of AEL, AIU and AA (Section 7.3)
- Access to the FSCS and other applicable compensation schemes (Section 7.4)
- Access to an Insurance Ombudsman Service (Section 7.5)
- Reinsurance arrangements with reinsurers (Section 7.6)
- Insurance regulation (Section 7.7)

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

7.2. Impact on the balance sheets of AEL, AIU and AA

I have based my analysis on projected balance sheets, immediately pre- and post- the Proposed Transfer, on the anticipated Effective Date of 1 July 2020.

I will also prepare a Supplementary Report ahead of the Sanctions Hearing for the Proposed Transfer, which will include an update of my conclusions in that report.

Note for the purpose of the comparison below, I have assumed that all other transfers that are due to take place either before or on the Effective Date of the Proposed Transfer, as described in Section 2.2, will have taken place.

GAAP balance sheets of AEL, AIU and AA pre- and post- the Proposed Transfer (£m)

	AEL £m Day 0	AIU £m Day 0	AA £m Day 0	AEL £m Day 1	AIU £m Day 1	AA £m Day 1
Investments and cash	691	417	137	343	391	516
Deferred acquisition costs	78	23	7	67	25	15
Reinsurers recoverables	620	549	30	270	451	478
Insurance and int. receivables	312	95	20	296	90	40
Other assets	164	35	0	164	35	0
Total Assets	**1,866**	**1,118**	**193**	**1,141**	**992**	**1,049**
Technical provisions	1,120	747	67	598	635	702
Technical creditors	207	56	17	191	66	23
Other liabilities	88	59	0	84	63	(2)
Total Liabilities	**1,415**	861	**84**	**873**	763	**722**
Total Equity	**451**	**257**	**109**	**268**	**229**	**327**

Source: AmTrust. Figures converted assuming £1 = €1.16.

The table above shows simplified GAAP balance sheets for AEL, AIU and AA pre- and post- the Proposed Transfer. The impact of the transfer is relatively material for AEL given that c. 47% of the net GAAP provisions, based on figures as at 30 June 2019, will be transferred out.

Note that the AA figures are not on an Italian GAAP basis. This does not allow credit to be taken for policy deductibles until the underlying claim has actually been paid. I do not expect the Transferring AEL to AA Policyholders to be materially disadvantaged by this accounting treatment since it will, all else being equal, lead to a higher level of booked provisions than under UK GAAP. This does not have an impact on a Solvency II basis and so the projected SCR coverage ratios are unchanged.

AmTrust have had preliminary discussions around the implications of this accounting issue and potential solutions with their Italian advisers, auditors and with IVASS. The main option being considered is the possibility of booking an intangible asset (or goodwill) representing the difference in valuations under UK/Ireland GAAP and Italian GAAP bases. This option would be enhanced if a third party, through a reinsurance agreement or financial guarantee, supported this asset. I will provide an update on this issue in the supplementary report.

As expected given the Proposed Transfer, the key movements in the balance sheet for AEL are the reduction in technical provisions, together with the corresponding reduction in reinsurer recoverables, and the reduction in investments and cash.

AA's balance sheet increases significantly due to the receipt of the transferring AEL and AIU business. AIU's balance sheet reduces less significantly as the business transferring out to AA is more significant than that transferring in from AEL.

Overall, across all three entities combined, total assets increased from £3,177m to £3,183m, an increase of £6m.

Based on current capital projections, capital injection into AA of €66m will take place on or before 31 March 2020. This will not be reflected in the movement above as this is before Day 0. Of the €25.9m injection, on or before 30 June 2020, €9.6m of this relates to the transfer and the balance will be injected whether the transfer takes place or not. The difference to the increase in assets, after converting to Sterling, relates to differences in timing and rates of corporation tax between Ireland and Italy.

Total liabilities decreased only slightly from £2,360m to £2,359m. I am satisfied that this reduction does not materially adversely impact policyholders given the size of the reduction and that the level of total available assets increases from £817m to £824m. I also consider all three entities to be well-capitalised post transfer.

7.3. Impact on the solvency positions of AEL, AIU and AA

The solvency positions of AEL, AIU and AA pre- and post-transfer are summarised in the following table. This assumes all other proposed transfers in the AmTrust Group that are due to take place before or on the Effective Date of the Proposed Transfer will have taken place.

Solvency positions of AEL, AIU and AA pre- and post- the Proposed Transfer (£m)

	AEL £m Day 0	AIU £m Day 0	AA £m Day 0	AEL £m Day 1	AIU £m Day 1	AA £m Day 1
Own Funds	381.2	233.0	107.0	229.4	207.5	286.7
SCR	213.8	145.3	73.8	153.2	138.5	191.5
SCR coverage ratio	**178%**	**160%**	**145%**	**150%**	**150%**	**150%**

Source: AmTrust. Figures converted assuming £1 = €1.16.

AEL and AIU are both well-capitalised immediately before and after the Proposed Transfer (as described in Section 6.1 and 6.10). AA has sufficient capital before the Proposed Transfer and is well-capitalised after the Proposed Transfer.

7.4. Access to a Compensation Scheme

The Financial Services Compensation Scheme (FSCS) in the UK provides consumer protection. This statutory “fund of last resort” compensates customers in the event of the insolvency of a financial services firm. Insurance protection exists for individuals and small businesses in the situation where an insurer is unable to meet its liabilities for direct policyholders only (ie reinsured policyholders are not covered). For certain insurance that is compulsory in the UK (eg motor third-party liability insurance), insurance protection also exists for direct policyholders whether they are individuals or small businesses (being business with an annual turnover of less than £1,000,000).

The FSCS will pay 100% of any claim incurred for compulsory insurance (eg motor third-party liability insurance) and 90% of claims incurred for non-compulsory insurance (eg home insurance), without any limit on the amount payable. No protection is available for Goods in Transit, Marine, Aviation and Credit Insurance.

Following the Proposed Transfer, eligible Transferring AEL to AIU Policyholders will retain access to the FSCS in respect of events or circumstances arising before the Proposed Transfer but would lose access for events or circumstances which arise after the Proposed Transfer as set out in the PRA’s Policy Statement PS5/15 ‘ Policyholder protection’.

AEL has estimated that 80% of the unexpired c. 520,000 transferring policies are likely to be held by policyholders eligible for access to the FSCS. As AEL does not hold information on the turnover of individual policyholders, these estimates are based on the number of policies in classes primarily written for consumer and SME policyholders. The classes of business that are considered to be affected include accident & health, affinity schemes, liability, legal expenses, mobile phone and motor business.

AIU and AA will not be establishing a UK (third country) Branch and so these policyholders, if eligible, may lose access to the FSCS as a result of the Proposed Transfer in respect of claims arising after the Effective Date (including during the transitional period that expires on 31 December 2020, as neither AIU nor AA are authorised in the UK on a FofE basis). Establishing a third country branch would maintain access to the FSCS and so eligible policyholders would not be adversely affected by loss of access.

The other 20% of unexpired transferring policies are held by policyholders not expected to be eligible for FSCS protection due to the nature of the coverage (e.g. policyholders of surety policies).

The majority of Transferring AEL to AA Policyholders are public and private hospitals and clinics and therefore not likely to be eligible for access to the FSCS due to the turnover threshold.

The drop in SCR coverage ratio for Transferring AEL to AIU and AEL to AA Policyholders from 178% to 150% in each case indicates these policyholders are more likely to require access to a compensation scheme post-transfer.

I have concluded that, due to the financial strength of AIU and AA, which I have considered in more detail in the previous section, an insolvency scenario which would be required to trigger FSCS protection is unlikely. Therefore, losing access to the FSCS is unlikely to have a materially adverse effect on the transferring policyholders. The scenario in which the loss of FSCS becomes a materially adverse effect is the insolvency of AIU or AA.

In addition, the Transferring AEL to AIU and AEL to AA Policyholders may value the certainty that valid claims can be lawfully paid in a Hard Brexit to the loss of access to the FSCS which only benefit them in the unlikely event of the insolvency of AIU or AA.

In Ireland there is an Insurance Compensation Fund, but this scheme is designed to facilitate compensation only in relation to risks situated in Ireland. In Italy a compensation scheme is only available for a small number of specific classes of business (such as the Guarantee Fund for Victims of Road Accidents). Therefore, the majority of Transferring AEL to AIU and AEL to AA policyholders are unlikely to have access to such schemes.

A further difference between the UK and Irish compensation schemes is that FSCS cover relates to eligible policies irrespective of where the risk is situated whereas the Insurance Compensation Fund only covers risks situated in Ireland.

7.5. Access to an Insurance Ombudsman Service

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

The FOS was extended on 1 April 2019 to also cover small businesses. Small businesses are defined in this context to be businesses with less than £6.5m turnover and either fewer than 50 employees or a balance sheet total of less than £5m.

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

The Transferring AEL to AIU and AEL to AA Policyholders will retain access to the FOS in respect of pre-Effective Date acts or omissions by AEL but may lose access to the FOS in respect of acts and omissions taking place after the Effective Date.

However, AIU and AA have confirmed they will voluntarily comply with the FCA rules (set out in DISP, the Dispute Resolution: Complaints part of the FCA Handbook) that apply to the handling of complaints brought to the FOS and any award or direction made or given by the FOS (and this is also set out in the Scheme Document). The provisions of the Scheme Document permit transferring policyholders to enforce such undertakings directly against AIU and AA (as applicable).

I have therefore concluded the transferring policyholders are not materially disadvantaged from loss of access to the FOS.

In Ireland there is a Financial Services and Pensions Ombudsman's Scheme. In Italy there is no generic national ombudsman although there are schemes operating on a regional basis.

7.6. Reinsurance arrangements with reinsurers

Reinsurance is purchased on a group basis. AEL has three primary quota share reinsurance arrangements:

- **AII** – this whole account reinsurance arrangement expired on 30 June 2019 ie new risks that incepted on 1 July 2019 were no longer covered under this arrangement. Originally 70% of the business was ceded (over 90% for medical malpractice business) but this reduced over a number of years and was 20% prior to the expiry. The arrangement is fully collateralised.
- **Maiden** – this arrangement only covered the Italian medical malpractice business relating to hospitals written or renewed between 3 April 2011 and 31 December 2018. The original cession was 40%, reducing down to 20% by the end of 2018. The arrangement requires Maiden to fully collateralise its exposure.

  Following Maiden's intention to re-domicile from Bermuda to Vermont in the United States (ie from a Solvency II equivalent to non-Solvency II equivalent territory), Maiden has agreed an endorsement to its contract with AEL and AIU such that Maiden must provide additional collateral equal to the greater of 120% of the exposure amount of the liabilities, and such additional collateral needed to ensure the SCR is at the same level as it would have been prior to any re-domicile. Therefore, there is no impact on AEL and AIU's SCR pre- or post-Transfer nor their SCR coverage ratio. The form of the collateral is the same as the current collateral arrangement, made up of corporate bonds.
- **Swiss Re** – the main live reinsurance policy protecting the transferring business is the quota share reinsurance provided by Swiss Re that incepted on 1 July 2019. It is a whole account programme for a 50% share on a number of lines of business, including Italian medical malpractice business. The coverage is on a policy attachment basis ie only policies underwritten within the twelve-month period of the policy would be covered.

In addition, there are several targeted excess of loss reinsurance arrangements covering specific product lines. The excess of loss reinsurance responds before the quota share reinsurance.

All of AEL's reinsurance that provides cover for the transferring business will transfer to AIU and AA. Similarly, reinsurance arrangements providing cover for non-transferring business will remain with AEL.

New business risks at AA will be covered by the existing Swiss Re quota share. AA, as indicated in its business plan submission to IVASS, will purchase excess of loss cover to protect its catastrophe liability exposures.

Existing AA policyholders are currently protected by the Swiss Re policy, but post-transfer will be exposed to Maiden and AII. Whilst this represents a new risk for AA policyholders, I do not believe they are materially adversely affected due to the relative financial strength of both entities and their respective parent companies. Also, Maiden will be required to post additional collateral equal to the greater of 120% of the exposure amount of the liabilities, and such additional collateral needed to ensure the SCR is at the same level as it would have been prior to any re-domicile.

7.7. Insurance regulation

Prudential regulation

Prudential regulation requires financial firms to control risks and hold adequate capital to ensure regulated firms are being run in a safe and sound way.

The UK, Ireland and Italy are currently regulated under Solvency II. Solvency II covers the prudential regulation of insurers, including risk management and capital requirements. The position regarding UK insurance regulation in the medium to long term after 31 December 2020 is currently unclear. However, the expectation is that the UK will seek to maintain equivalence with Solvency II.

Based on the above considerations, I do not expect transferring policyholders to be materially adversely affected by the changes in prudential insurance regulation governing their policies when transferring from a UK insurer to an insurer in Ireland or Italy (as applicable).

Conduct regulation

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

There is currently less harmonisation in conduct regulation across the EEA compared to prudential regulation. However, a number of existing EU Directives govern consumer regulation across the EEA, and so currently apply to the UK, Ireland and Italy. For example, the Insurance Mediation Directive (IMD) aimed to ensure appropriate levels of protection for customers.

The Insurance Distribution Directive (IDD), which replaced the Insurance Mediation Directive (IMD) across EEA member states on 1 October 2018, strengthened and consolidated the existing rules of the IMD covering the distribution of insurance and reinsurance, and also the administration and performance of an insurance policy once it has been written. As for Solvency II, the position regarding the compliance with IDD in the UK in the medium to long term after 31 December 2020 is currently unclear.

Therefore, the key relevant comparison is between the conduct regulations in the UK and those in Ireland and Italy. If these were materially different, this could potentially affect transferring policyholders where the business is currently carried out in the UK and post-transfer will be carried out in Ireland and Italy.

There is access to similar mechanisms in terms of conduct regulation in Ireland and Italy to those in the UK for the transferring policyholders based on EU Directives.

Conclusions on regulation

Based on the above considerations, I do not expect transferring policyholders to be materially adversely affected by the change in insurance regulation governing their policies moving from the UK to Ireland or Italy.

7.8. Overall conclusion: Policyholder security

Based on the work and rationale described above, I have concluded that the security provided to transferring policyholders will not be materially adversely affected by the Proposed Transfer.

8. Policyholder communications

8.1. My considerations relating to policyholder communications

I have assessed the appropriateness of AEL's proposed communication strategy to inform policyholders and other stakeholders of the Proposed Transfer.

The key focus of my assessment was whether the policyholders and other stakeholders are to be provided with sufficient and clear enough information so that they can understand how the Proposed Transfer may affect them.

8.2. Overview of communications strategy

AEL has developed a communication strategy to notify affected parties of the Proposed Transfer and to allow time for affected parties to raise objections to the Court. I have summarised the main points of the communications strategy below:

- *Non-transferring AEL Policyholders:* It is not proposed to issue individual notifications to the Non-transferring AEL Policyholders. A dispensation is being sought in this regard.
- *Transferring AEL to AIU and AEL to AA Policyholders:* AEL will notify transferring policyholders, subject to the dispensations sought as discussed in Section 8.3.
- *AIU Policyholders:* It is not proposed to issue individual notifications to existing AIU Policyholders. A dispensation is being sought in this regard.
- *AA Policyholders:* AmTrust will notify all current AA policyholders, subject to the dispensations sought as discussed in Section 8.3.
- *Reinsurers*: For reinsurance contracts placed through a reinsurance broker, AEL will provide a communication pack to the broker and request they send this to the lead reinsurer for each treaty. They will also request written confirmation this has taken place. For reinsurance contracts written directly with reinsurers, AEL intends to send a communication pack to such reinsurers, except where such reinsurance is written on a co-insurance basis, it will send the communication pack to the lead reinsurer only.
- *Intermediaries and other parties (including brokers, managing general agents (MGA) and commercial partners which operate schemes)*: AEL will directly notify those who have placed transferring business for the transferring policyholders and will ask such persons to notify policyholders on AEL's behalf.
- *Third party claimants*: AEL intends to notify persons who are not policyholders of AEL but currently have an open claim in respect of a transferring policy (e.g. where there is a third party claimant under an AEL motor liability policy). AEL intends to notify such persons directly where claims are managed in-house and via third party administrators (TPAs) where TPAs handle the relevant claims.

For any policyholders with policies relating to the Proposed Transfer incepting after the Directions Hearing, who will not have been notified via the planned mail shot with links to the communications pack, the following approach will be taken:

- subject to applicable law and regulation, the policy terms and conditions of the relevant products will be updated prior to issuance to include a term highlighting AEL's intention to carry out the Proposed Transfer and giving AEL the right to carry out the Proposed Transfer under Part VII FSMA in order to continue servicing the policy after Brexit; and
- A letter, email or SMS will be provided explaining the Proposed Transfer and directing these policyholders to the website for additional information instead of sending the full communications pack.
- This approach is expected to be taken for a mobile phone product, certain delegated property business and legal expenses business (as AIU does not yet hold the licence currently, as explained in more detail in section 3.5).

IE conclusion

I am satisfied that the communications strategy as described in this section, together with the dispensations sought as described in section 8.3, will ensure that those who will be affected by the Proposed Transfer will be informed appropriately, including new policyholders with policies incepting after the Directions Hearing and prior to the Effective Date of the Proposed Transfer.

8.3. Planned dispensations and rationale

AEL intends to request that the Court grant a dispensation from the need to directly notify the Non-transferring AEL Policyholders.

AEL has provided a rationale to support their request for dispensation with indirect reference to the judgement of Norris J in the Directions Hearing in Re Aviva International Insurance Limited [2011] EWCH 1901 (Ch.) (the Aviva Judgement). The Aviva Judgement summarised the following factors as a rationale for granting a dispensation:

1. the impossibility of contacting policyholders;
2. the practicality of contacting policyholders;
3. the utility of contacting policyholders;
4. the availability of other information channels through which notice of the application can be made available;
5. the proportionality of strict compliance and the impact of collateral commercial concerns; and
6. the likely impact of the Proposed Transfer on policyholders.

Non-transferring AEL Policyholders

AEL does not intend to notify Non-transferring AEL Policyholders. AEL's rationale for the dispensation sought for Non-transferring AEL Policyholders is as follows (I have included in brackets the reference to the factors from the Aviva Judgement where applicable):

AEL's view is that Non-transferring AEL Policyholders will have access to the information from the publications in the UK, and so will have the opportunity to be made aware of the Proposed Scheme without direct notification (availability of other information channels).

AEL also believe the cost of direct notification of all Non-transferring AEL Policyholders is disproportionate to the benefit received from direct notification, particularly given the Non-transferring AEL Policyholders are not materially disadvantaged by the Proposed Transfer and the Proposed Transfer is primarily being undertaken to respond to the potential impact of Brexit (proportionality and impact).

Moreover, AEL do not consider that notifying the Non-transferring AEL Policyholders that their policies are remaining with the same insurer and that nothing is changing for them in terms of: (i) their insurer's governance structure and regulatory framework; (ii) their policy terms and conditions; and (iii) their security of benefits is necessary (utility).

Transferring AEL to AIU and AEL to AA Policyholders

Transferring AEL to AIU and AEL to AA Policyholders will be notified individually through a communication pack (the component parts of which I have reviewed).

Given transferring policies have been issued through a broker, agent or other third party, AEL intend to notify the policyholders through these third parties rather than directly. The rationale is that these third parties are more likely to have the most relevant and up-to-date policyholder contact details and that policyholders are accustomed to receiving communications from the third parties than from AEL.

AmTrust has requested the following dispensations:

- they will not notify transferring policyholders of claims made policies whose policies expired on or before 31 December 2019 (ie six months prior to the Effective Date); and
- they will notify transferring policyholders of claims occurring policies whose policies incepted on or after a specific cut-off date. The cut-off date is set for each line of business as the 90th percentile of observed historical delays from policy inception to claim load date and rounded back to the nearest half year.

The intention is to notify all policyholders other than those who can no longer make a claim or those who are very unlikely to make a claim based on AEL's review of historic claims patterns. The rationale for claims occurring policyholders is that by applying the

90th percentile of delays, rather than the say the average, AmTrust will be taking a more conservative view of the potential delay in claim notifications. All else being equal, this would lead to an earlier cut-off date and therefore more policyholders would qualify for notification.

AIU policyholders

A dispensation is being sought from the requirement to notify existing AIU policyholders for similar reasons to those for Non-transferring AEL Policyholders (availability of other information channels, proportionality, impact and utility).

AA policyholders

AEL will notify these policyholders as is required under UK law but will seek that this is through third parties for the same reasons as set out for transferring policyholders.

Third party claimants

As set out above, AEL intends to notify persons who are not policyholders of AEL but currently have an open claim in respect of a transferring policy via third party administrators (TPAs) where such persons handle the relevant claims for the same reasons as it intends to notify policyholders through third parties.

Policyholders (General)

A general dispensation is requested in respect of transferring policyholders and AA policyholders, on the basis that there may be changes in the identity of policyholders (e.g. by way of assignment) or contact details that are not notified to AEL or the policies themselves do not identify all holders of the policy or any beneficiaries under such policies (impossibility).

Following reinsurers

A general dispensation is requested in respect of following reinsurers, as AEL will not always have the relevant contact details for all reinsurers, e.g. in respect of non-lead reinsurers or where reinsurers have changed their contact details without giving notice to AEL (impossibility).

IE conclusion

I am satisfied with the rationale for the various dispensations sought, as information regarding the Proposed Transfer is available from other sources and my conclusions support that all groups of policyholders and reinsurers are not materially disadvantaged by the Proposed Transfer.

8.4. Planned notices

AEL will comply with the regulation and place a notice of the Proposed Scheme in:

- the London, Edinburgh and Belfast Gazettes; and
- two national newspapers in the UK (and AEL proposes to publish an additional notice in a third national UK newspapers (being The Sun) to increase the breadth of the UK advertising).

AEL intends to request that the Court grants a dispensation from the requirement to place notices in two national newspapers and one business newspaper in each non-UK EEA states on the following grounds:

- AEL proposes publishing the notice in the Financial Times (International Edition) and one additional quality and/or business publication in each non-UK EEA state as it is considers that this achieves an appropriate balance between local press and international press. AEL also intends to advertise in Insurance Day as it considers that its cedant clients are likely to read this publication;
- the cost of advertising in an additional national newspaper in every non-UK EEA state is considered to be disproportionate relative to the number of policyholders who might be reached by such publication (proportionality). However, to ensure that the Proposed Transfer is widely advertised, AEL proposes to advertise in an additional newspaper in those non-UK EEA states where the Financial Times (International Edition) has a circulation of less than 2,000 and where there are more than 200 live policies in such non-UK EEA state; and
- AEL will, through third parties, seek to notify all transferring policyholders subject to the requested dispensations. Non-transferring AEL Policyholders are based in the UK so will have access to the notices referenced above (availability of other information channels).

IE conclusion

As AEL will be notifying all Transferring AEL to AIU and AEL to AA Policyholders, through third parties subject to the proposed dispensations, and I have concluded that Non-transferring AEL Policyholders and transferring policyholders are not disadvantaged by the Proposed Transfer, I am satisfied with the proposed approach to advertisements.

8.5. Translation of key documents

All publication notices and major documents (including this report) will be provided in English, save that where a third party or TPA deals with a transferring policyholder or AA policyholder whose policy is in a language other than English, AmTrust will provide that third party or TPA with a local language translation of the communication pack to provide to policyholders or third-party claimants. Such translated versions will also be available on the AmTrust website.

Readers of such translations should rely on AEL and not myself or LCP to ensure that the translations into each language are accurate.

8.6. Clarity of communication

I have reviewed drafts of both the proposed letters, the summary of the Scheme Document and the Q&A booklet to be provided to policyholders explaining the background to the Proposed Transfer and the transfer process.

IE conclusion

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

8.7. Overall conclusion: Communication strategy

Based on my review of the communication strategy, I have concluded the planned communications strategy will ensure adequate coverage of affected parties. AEL is applying for a number of dispensations from communicating to some affected parties. I have concluded that these are appropriate.

I have also concluded that the planned communication is sufficiently clear for policyholders to understand the effects of the Proposed Transfer.

9. Customer service and other considerations

9.1. Customer service

AmTrust has confirmed that there will be no material changes to policyholder administration and claims handling for Non-Transferring AEL Policyholders and Transferring AEL to AIU and AEL to AA Policyholders as a result of the Proposed Transfer.

In addition, AmTrust expect to maintain previous contact details for policyholders regarding claims and servicing policies and will forward any policyholder correspondence to AIU and AA. I will provide an update in my Supplementary Report.

In-house claims handling will move from the UK to Dublin after the AEL transfer to AIU. However, there will be no change in the claims philosophy or strategy since this is set and managed at the level of the AmTrust Group's European operations.

The same claims handlers will continue to handle all AEL Italian claims (including medical malpractice claims) from the Italian office post-transfer as pre-transfer. The only change post-transfer is that claims over €1m, that were previously approved by AIU and AEL, will now be approved by AA. Policyholders will not be impacted by this change to the claims handling process.

Other non-UK EEA claims are mainly managed externally by TPAs and coverholders and this will not change.

As such, I do not expect that policyholders will receive a materially different level of customer service following the Proposed Transfer.

9.2. Tax implications

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

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

Therefore, there are no tax implications of the Proposed Transfer on transferring or non-transferring policyholders.

9.3. Investment management implications

AEL and AIU's investment strategies are approved by their investment committees with oversight by their boards. Each committee adheres to similar governing principles and guidelines set at the Group level.

- As at 31 December 2018, the vast majority of AEL's invested assets were in either corporate or government bonds. A small proportion is invested in property, cash and holdings in other undertakings.
- Similarly, the majority of AIU's invested assets were in corporate or government bonds. A small proportion is invested in bank deposits, collateralised securities and collective investment vehicles.

Investment management is outsourced to specialists within the AmTrust Group. The management of AEL and AIU's bond portfolio is outsourced to the same dedicated team of investment managers in another AmTrust Group company.

The investment strategy of AA follows the wider strategy of the AmTrust Group and is managed in a similar manner to AEL and AIU.

No changes to AEL's or AIU's investment strategy are planned as a result of the Proposed Transfer.

Therefore, I do not anticipate any materially adverse impact to the non-transferring or transferring policyholders in terms of investment management as a consequence of the Proposed Transfer.

9.4. Implications on ongoing expense levels

All costs and expenses incurred relating to the Scheme will be borne by AEL, AIU and AA and will not be borne by policyholders. One-off costs associated with the Proposed Transfer are expected to be modest relative to the size of the transferring business and existing portfolios of AEL, AIU and AA.

Therefore, there are no impacts on transferring or non-transferring policyholders as a result of any changes to ongoing expense levels.

9.5. Impact on liquidity position

The liquidity position of a company represents its ability to meet all claim payments and other obligations as and when they fall due. Both AEL and AIU monitor asset liquidity as part of their ORSA processes. AA will follow the same process. Both AEL and AIU invest mainly in government bonds and corporate bonds which are normally readily convertible into cash. As AEL, AIU and AA write new business, liquidity is also available from premium income.

Therefore, I do not anticipate any materially adverse impact on the liquidity position for the non-transferring or transferring policyholders as a consequence of the Proposed Transfer.

9.6. Set-off

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

I have not identified any material set-off rights as part of my review. Therefore, I do not believe considerations around set-off impact my conclusions.

9.7. Overall conclusions: Customer service and other considerations

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

10. Conclusions and Statement of Truth

I have considered the Proposed Transfer and its likely effects on the Non-transferring AEL Policyholders, the Transferring AEL to AIU and AEL to AA Policyholders, AIU Policyholders, AA Policyholders and the reinsurers of the transferring business.

In reaching the conclusions set out below, I have applied the principles as set out in relevant professional guidance, being the Technical Actuarial Standards (TASs) TAS 100: Principles for Technical Actuarial Work and TAS 200: Insurance.

I have concluded that:

- **The security provided to Non-transferring AEL Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for Non-transferring AEL Policyholders following the Proposed Transfer.**
- **The security provided to Transferring AEL to AIU Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for Transferring AEL to AIU Policyholders following the Proposed Transfer.**
- **The security provided to Transferring AEL to AA Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for Transferring AEL to AA Policyholders following the Proposed Transfer.**
- **The security provided to AIU Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for AIU Policyholders.**
- **The security provided to AA Policyholders will not be materially adversely affected by the Proposed Transfer. No material impact on service standards is expected for AA Policyholders.**
- **Reinsurers whose contracts with AEL are transferring to AIU and AA as part of the Proposed Transfer will not be materially adversely affected by the Proposed Transfer.**

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10.1. Issues to highlight

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

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

- Any changes to the final details of the Proposed Transfer.
- Any reinsurer and policyholder objections received.
- Updated financial information and capital projections.
- AA's reserving policy.
- Progress on AEL's management responses to the final recommendations from the AEL external regulatory review and the implementation of the proposed actions.
- Progress on AIU's management response to the final recommendations from the AIU external regulatory review and the implementation of the proposed actions.
- Updated details on business written by AA prior to the Proposed Transfer.
- The potential consequences if Transfer 4 has not taken place.
- Findings from the review of the transferring Italian medical malpractice portfolios requested by IVASS.
- The accounting treatment of unpaid deductible recoveries under Italian GAAP.
- Update on AIU and AA's licence applications which are expected to be submitted by 4 March 2020.
- An update on the proposed cash injections and other measures to fund the Proposed Transfer.

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

10.2. IE duty and declaration

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

I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.

I confirm that I am aware of the requirements of Part 35 of the Civil Procedure Rules, Practice Direction 35 and the Protocol for Instruction of Experts to give Evidence in Civil Claims.

10.3. Sign-off

S. Mitchell

Stewart Mitchell FIA
Partner

3 March 2020

95 Wigmore Street
London W1U 1DQ
www.lcp.uk.com

The use of our work

This work has been produced by Lane Clark & Peacock LLP under the terms of our written agreement with AmTrust Management Services Limited. It is subject to any stated limitations (eg regarding accuracy or completeness).

This Scheme Report, which is our work, has been prepared for the purpose of accompanying the application to the Court in respect of the insurance business transfer scheme described in this report, in accordance with Section 109 of the Financial Services and Markets Act 2000. The Scheme Report is not suitable for any other purpose.

A copy of the Scheme Report will be sent to the Prudential Regulatory Authority, the Financial Conduct Authority and will accompany the Scheme application to the Court.

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

Professional Standards

Our work in preparing this document complies with Technical Actuarial Standard 100: Principles for Technical Actuarial Work, together with Technical Actuarial Standard 200: Insurance.

Appendix 1 - Glossary

Term	Definition
Best estimate	An estimate prepared with no margin for either prudence or optimism included.
Bornhuetter-Ferguson (BF) method	A blend of the Chain Ladder Method and the Expected Loss Ratio Method (defined later in this glossary). The weighting given to each is dependent on how developed the claims are for a particular policy year.
Brexit	The expected exit of the UK from the EU following the referendum on continuing membership held in the UK in June 2016.
Capital Cover Ratio	The Capital Cover Ratio is the ratio of Available Capital to Required Capital. This is a measure of the capital strength of the insurer – the higher the ratio, the stronger the insurer. Also referred to as the SCR coverage ratio.
Central Bank of Ireland (CBI)	The regulator of the insurance sector in Ireland.
Chain Ladder method	An actuarial method for estimating future payments or numbers by using the historical pattern of past payments or numbers to estimate a development profile, which can be used to extrapolate future payments or numbers.
Core Tier 1	Under Solvency II, capital is categorised into 3 tiers based on the permanence and loss absorbency of the form of capital. Tier 1 capital is the highest quality.
Counterparty Default Risk	The risk of defaults or downgrades by counterparties that either owe an insurer money or hold money on its behalf. For example, this covers the risk of the failure of a reinsurer or a broker.
Court	The High Court of Justice of England and Wales.
Direct policyholders	Any policyholders that are not insurers or reinsurers.
European Economic Area (EEA)	The EEA Agreement established the EEA on 1 January 1994. The EEA unites the 28 EU member states with Iceland, Liechtenstein, and Norway into an internal market governed by the same basic rules. These rules aim to enable goods, services, capital, and persons to move freely about the EEA in an open and competitive environment, a concept referred to as the four freedoms.
Effective Date	The effective date of the Proposed Transfer, expected to be 1 July 2020.
European Union (EU)	The EU prior to Brexit, ie the 28 member states. Post-Brexit the EU will consist of 27 member states ie excluding the UK.
Events not in data (ENIDs)	An estimate of possible future events or developments that are not in existing data. Insurers need to make allowance for ENIDs in their Solvency II technical provisions.

Appendix 1 (cont)

Term	Definition
Excess of Loss Reinsurance	A type of reinsurance in which the reinsurer indemnifies the ceding company for losses that exceed a specified limit (in respect of individual claims or the aggregate cost of claims). Excess of loss reinsurance is a form of non-proportional reinsurance.
Expected Loss Ratio method	An actuarial method for estimating future payments or numbers based on combining an exposure measure and an assumed rate per unit of exposure (the "initial expected loss ratio") for the written business.
Financial Conduct Authority (FCA)	The UK regulatory agency that focuses on the regulation of conduct by retail and wholesale financial services firms. The FCA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
Financial Ombudsman Service (FOS)	Set up by the UK Parliament, the FOS is the UK's official expert in sorting out problems with financial services. Parliament set up the FOS and has legal powers in the UK to address unresolved complaints between a business and a customer relating to financial services.
Financial Reporting Council (FRC)	The body responsible for setting actuarial standards in the UK. The FRC also regulates auditors and accountants and sets the UK's Corporate Governance and Stewardship Codes.
Freedom of Establishment (FofE)	Under the EU Insurance Directives and Insurance Mediation Directive, insurance companies have the right to provide business services through a permanent presence within the EEA under the principle of FofE utilising the "passporting" system in place between EEA regulators.
Freedom of Services (FofS)	Under the EU Insurance Directives, insurance companies have the right to provide business services on a cross-border basis within the EEA under the principle of FofS utilising the "passporting" system in place between EEA regulators.
Financial Services Compensation Scheme (FSCS)	The FSCS is the compensation fund of last resort for customers of UK authorised financial services firms. This covers insurance for individuals and some insurance for small businesses.
Financial Services and Markets Act 2000 (FSMA)	The legislation under which Part VII governs the transfer of (re)insurance business between (re)insurance undertakings.
Generally accepted accounting principles (GAAP)	A collection of commonly-followed accounting rules and standards for financial reporting. GAAP specifications include definitions of concepts and principles, as well as industry-specific rules.

Appendix 1 (cont)

Term	Definition
Hard Brexit	A scenario where AEL no longer has FofS or FofE rights and may not legally be able to carry on with non-UK EEA business. For example, AEL would not be able to issue new insurance policies across the EEA and might not legally be able to pay valid claims to existing EEA policyholders.
Incurred but not enough reported (IBNER)	See definition of IBNR
Incurred but not reported (IBNR)	The provision for claims that are reported in the future but relate to events that have already occurred. This includes provision for estimated developments to existing open claims, ie those that have been reported but not fully settled. The provision for these open claims is called IBNER (Incurred But Not Enough Reported). Depending on the type of insurance being considered and the claims handling approach, both the IBNR and IBNER can be either positive or negative.
Independent Expert	A suitably qualified person appointed by the Court to produce an independent report on an insurance business transfer scheme, in accordance with the FSMA. The Independent Expert's primary duty lies with the Court, and the opinion of the expert is independent of those of the sponsoring companies involved in the Transfer and the PRA.
Insurance Compensation Fund (Ireland)	The Insurance Compensation Fund is primarily designed to facilitate payments to policyholders in relation to risks in the State where an Irish authorised non-life insurer or a non-life insurer authorised in another Member State goes into liquidation.
Institute for Insurance Supervisions or IVASS	The regulator of the insurance sector in Italy
Market risk	The risk of changes in an insurer's financial position due to changes in the market value of assets, liabilities and financial instruments. For example, this covers the risk of falls in the value of assets that are being held to make future claims payments.
Minimum Capital Requirement (MCR)	A formulaic calculation of the capital requirement as part of the existing European Solvency II regulations for insurers. Breaching the MCR defines the point of intensive regulatory intervention. The calibration of the MCR is to be the capital required to give an 85% confidence level of sufficient capital to last one year. The MCR is a simpler calculation than the SCR and is typically a less onerous requirement.
Operational risk	The risk of losses caused by failures in an insurer's operational processes, people and systems, or from events that are external to the insurer. For example, this would cover the risk of fraud or IT failure.

Appendix 1 (cont)

Term	Definition
Own funds	The capital in excess of provisions available to meet the SCR capital requirements under Solvency II.
Prudential Regulation Authority (PRA)	The part of the Bank of England that carries out the prudential regulation of financial firms in the UK, including banks, investment banks, building societies and insurance companies. The PRA operates as part of the regulatory framework implemented under the Financial Services Act 2012.
PRA's Statement of Policy	The Statement of Policy issued by the PRA entitled "Statement of Policy – The PRA's approach to insurance business transfers – April 2015"
Proposed Transfer	The proposed insurance business transfer of AEL to AIU and AA under Section 105 of the FSMA.
Quota share reinsurance	A reinsurance contract in which the insurer and reinsurer share both claims and premiums in the same proportion. The reinsurer usually pays a commission to the insurer to allow for their costs of selling and administering the policy.
Required capital	The amount of capital an insurer must hold in order to meet its regulatory capital requirements (ie the SCR).
Reinsurance	An arrangement with another insurer to share or pass on risks. For example, in the case of the Proposed Transfer, AEL is transferring underwriting (insurance) risk to AII using a reinsurance quota share arrangement.
Reinsurance bad debt	Reinsurance bad debt is a provision for amounts that are owed by reinsurers but which may not be paid, eg due to the insolvency of the reinsurer.
Risk Appetite	A framework of boundaries within which an insurer operates. The framework captures the risks to which the company is exposed and sets risk-specific and aggregate limits within which to manage the organisation.
Scheme Document	A document submitted to the Court setting out details of the Scheme or Proposed Transfer.
Scheme Report	This report prepared by me, as the Independent Expert, for submission to the Court.
Section 13 transfer	The Irish equivalent of a UK Part VII transfer, regulated by the CBI.
Solvency Capital Requirement (SCR)	The amount of capital insurers are required to hold under Solvency II regulations. This is an estimate of capital required to ensure that an insurer is able to meet its obligations over the next 12 months with a probability of at least 99.5%. If an insurer's capital (ie the excess of its assets over its liabilities) falls below the SCR, it will trigger regulatory intervention, with the intention of remedying that position.
Solvency Financial Condition Report (SFCR)	Solvency II requires each insurer to publish an SFCR annually that contains certain qualitative and quantitative information.

Appendix 1 (cont)

Term	Definition
Solvency II	The system for establishing (among other things) minimum capital requirements for EEA (re)insurers under the Solvency II Directive 2009/138/EC.
Standard Formula	A prescribed approach under Solvency II for the calculation of capital based on an insurer's financial information (eg premiums and claims provisions).
TAS 100	The FRC issued Technical Actuarial Standard 100: Principles for Technical Actuarial Work (TAS 100) which applies to all actuarial work produced after 1 July 2017.
TAS 200	The FRC issued Technical Actuarial Standard 200: Insurance (TAS 200) which applies to all actuarial work produced after 1 July 2017.
Technical provisions	Under Solvency II, the technical provisions cover the ultimate costs of settling all claims arising from events occurring up to the balance sheet date plus the provisions for future claims (and premiums) arising on unexpired periods of risk.
Transferee	The insurer to which the business is being transferred, being AmTrust International Underwriters Designed Activity Company (AIU) in the case of AEL's non-UK EEA policies (other than Italian medical malpractice business) and AmTrust Assicurazioni SpA (AA) in the case of AEL's Italian medical malpractice business.
Transferor	The insurer from which the business is being transferred, AmTrust Europe Limited (AEL).
Unallocated Loss Adjustment Expenses (ULAE)	Unallocated Loss Adjustment Expenses are expenses relating to the handling of claims that are not allocated to specific claims, eg claim handlers' salaries and office space.
Underwriting risk	The risk that the value of insurance claims proves to be higher than expected.
Unearned Premium Reserve (UPR)	A provision for the unexpired portion of insurance policies and appears as a liability on the insurer's balance sheet, since the premium would be paid back upon cancellation of the policy.

Appendix 2 – Extract from Terms of Reference

LCP has been appointed by AmTrust Management Services Limited on behalf of AEL, AIU and AA.

Summary of agreed scope of work

I, Stewart Mitchell will act as IE to support your planned Part VII transfer of AmTrust Europe Limited (AEL) business into AmTrust International Underwriters (AIU) and AmTrust Assicurazioni SpA (AA).

Your primary requirement is for the IE to act in line with Section 109 of the Financial Services Markets Act 2000.

The key deliverables from the work will be:

- The main and supplementary IE reports;
- Input as required to address any issues arising;
- Presenting my findings as IE to the Court and responding to any queries and additional court requests; and
- A summary report to support policyholder communications.

Appendix 3 – CV of Stewart Mitchell FIA

I am a Partner in LCP's Insurance Consulting practice and a Fellow of the Institute of Actuaries (qualified in 2004). I hold an MBA from City University Business School and qualified as an ACII with the Chartered Institute of Insurance.

I joined LCP in 2016, and prior to this was a Director at Ernst & Young LLP. I have 20 years' experience as a general insurance actuarial consultant, and a further 10 years' experience working in the insurance industry prior to joining Ernst & Young LLP.

Professional experience

I have a broad experience of actuarial engagements over the last 20 years. This experience covers reserving, capital, pricing, reinsurance and transactions.

I have been the IE and supported or provided peer review to the Independent Expert for seven other insurance business transfer schemes. I have also led the work on Section 166 regulatory reports for the PRA.

I hold a Lloyd's Signing Actuary practicing certificate and am currently the Signing Actuary for four Lloyd's syndicates. I have performed this role for many Lloyd's syndicates in the past, signing the opinions for up to nine Lloyd's syndicates in a single year-end.

I have previously been appointed by the Bermuda Monetary Authority as a Loss Reserving Specialist for Bermudian insurance companies and the Appointed Actuary for Lichtenstein insurance companies.

I have provided opinions on the adequacy of claims reserves for US regulators of UK based insurance companies and for HMRC for UK insurance companies.

I have extensive experience in independent reviews of claim liabilities for general insurance companies. I have also led capital modelling projects and reviews of Solvency II technical provisions.

I have worked with many insurers in reviews of claims liabilities and capital requirements for the purpose of mergers and acquisitions.

Appendix 4 – Summary of data provided

The following is a list of the key data items I have requested and received in assessing the Proposed Transfer. All data I have requested has been provided to me. AEL has provided a Data Accuracy Statement confirming that the data and information provided to me regarding the Proposed Transfer are accurate and complete.

1. Draft Court and regulatory documents prepared by AEL for the Proposed Transfer, including:

- AEL Scheme Document (draft dated 3 December 2019)
- AEL First Witness Statement (draft dated 3 December 2019)
- AIU First Witness Statement (draft dated 3 December 2019)
- AA Witness Statement (draft dated 3 December 2019)
- Legal notice (draft dated 25 November 2019)
- Directions Order (draft dated 25 November 2019)

2. Draft proposed communication plan and communication prepared by AEL:

- Template letters to policyholders, intermediaries, reinsurers and third parties (drafts dated 25 November 2019)
- Policyholder Q&A Booklet (draft dated 25 November 2019)
- Summary of the Scheme Document (draft dated 25 November 2019)

3. Documents relating to provisions and reserving processes, including:

- AEL and AIU Internal Reserve Review Reports 2018
- AEL and AIU External Reserve Review Reports 2018
- AIU Actuarial Report on Technical Provisions 2018
- AEL and AIU Audit and Reserve Committee Meeting Notes 2018
- AEL and AIU Internal Audit Reports 2018
- AEL and AIU Draft Terms of Reference 2018
- AEL, AIU and AA Draft Reserving Policy

4. Documents relating to capital and related processes, including:

- Solvency and Financial Condition Report (SFCR) for AEL and AIU year ending 31 December 2018
- AEL and AIU 2018 Own Risk and Solvency Assessment (ORSA) report
- AA ORSA Policy

- AEL and AA Capital Management Policy 2018
- AIU Risk Appetite Statement
- AEL, AIU and AA Business Plan
- AEL and AIU Standard Formula calculations
- AEL Standard Formula appropriateness assessments
- Various additional stress scenarios for AEL and AA

5. Other evidence prepared by AEL to support the Proposed Transfer, including:

- Draft projections of future balance sheets and capital requirements up to 31 December 2021 for AEL and AIU
- Details of the impact of the Proposed Transfer on contact points and service standards
- Details of the tax, investment and liquidity implications of the Proposed Transfer

6. Data Accuracy Statement

- For each of AEL, AIU and AA

Appendix 5 – Mapping to requirements

The table below shows the relevant section references in the Scheme Report where I have addressed each point in the guidance from:

- FCA x.x: Chapter 18 of the Supervision Manual of the FCA Handbook; and
- PRA x.x: the PRA's "Statement of Policy - The PRA's approach to insurance business transfers – April 2015".

I have included references from the UK regulators, the PRA and FCA.

Guidance reference	Guidance	Scheme report reference
PRA 2.30 (1) FCA 18.2.33 (1)	Who appointed the independent expert and who is bearing the costs of that appointment	2.3 (page 18)
PRA 2.30 (2) FCA 18.2.33 (2)	Confirmation that the independent expert has been approved or nominated by the appropriate regulator (the PRA)	2.3 (page 18)
PRA 2.30 (3) FCA 18.2.33 (3)	A statement of the independent expert's professional qualifications and (where appropriate) descriptions of the experience that makes them appropriate for the role	2.3 (page 18) Appendix 3
PRA 2.30 (4) FCA 18.2.33 (4)	Whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest	2.3 (page 18)
PRA 2.30 (5) FCA 18.2.33 (5)	The scope of the report	2.4 (page 19)
PRA 2.30 (6) FCA 18.2.33 (6)	The purpose of the scheme	3.3 (page 26)
PRA 2.30 (7) FCA 18.2.33 (7)	A summary of the terms of the scheme in so far as they are relevant to the report	3 (page 23)
PRA 2.30 (8) FCA 18.2.33 (8)	What documents, reports and other material information the independent expert has considered in preparing the report and whether any information that they requested has not been provided	Appendix 4

Appendix 5 (cont)

Guidance reference	Guidance	Scheme report reference
PRA 2.30 (9) FCA 18.2.33 (9)	The extent to which the independent expert has relied on: (a) information provided by others; and (b) the judgement of others	2.6 (page 20)
PRA 2.30 (10) FCA 18.2.33 (10)	The people the independent expert has relied on and why, in their opinion, such reliance is reasonable.	2.6 (page 20)
PRA 2.30 (11) FCA 18.2.33 (11)	Their opinion of the likely effects of the scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between: (a) transferring policyholders; (b) policyholders of the transferor whose contracts will not be transferred; and (c) policyholders of the transferee	Executive summary (page 4) 10 (page 107)
PRA 2.30 (12) FCA 18.2.33 (11A)	Their opinion on the likely effects of the scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the scheme.	Executive summary (page 4) 10 (page 107)
PRA 2.30 (13) FCA 18.2.33 (12)	What matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in their opinion, be relevant to policyholders' consideration of the scheme.	10 (page 107)
PRA 2.30 (14) FCA 18.2.33 (13)	For each opinion that the independent expert expresses in the report, an outline of their reasons	Reserving: 5.10 (page 47) Capital: 0 (page 88) Policyholder: 7.8 (page 97) Communication: 8.7 (page 103) Other: 9.7 (page 106)
PRA 2.32 (1) FCA 18.2.35 (1)	A description of any reinsurance arrangements that it is proposed should pass to the transferee under the scheme	3.2 (page 24)
PRA 2.32 (2) FCA 18.2.35 (2)	A description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred	3.2 (page 24)
PRA 2.33 (1) FCA 18.2.36 (1)	Include a comparison of the likely effects if it is or is not implemented	3.4 (page 27)

Guidance reference	Guidance	Scheme report reference
PRA 2.33 (2) FCA 18.2.36 (2)	State whether they considered alternative arrangements and, if so, what	3.4 (page 27)
PRA 2.33 (3) FCA 18.2.36 (3)	Where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences they consider may be material to the policyholders	Executive summary (page 4) 7.4 (page 93)
PRA 2.33 (4) FCA 18.2.36 (4)	Include their views on: (a) the effect of the scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer; (b) the likely effects of the scheme on matters such as investment management, new business strategy, administration, claims handling, expense levels and valuation bases in relation to how they may affect: (i) the security of policyholders' contractual rights; (ii) levels of service provided to policyholders; or (iii) for long-term insurance business, the reasonable expectations of policyholders; and (c) the cost and tax effects of the scheme, in relation to how they may affect the security of policyholders' contractual rights, or for long-term insurance business, their reasonable expectations	(a) Executive summary (page 4) 7.4 (page 93) (b) and (c) 9 (page 104)

The Proposed Transfer does not involve any mutual companies or long-term insurance business. As such, PRA 2.35 and PRA 2.36 (FCA 18.2.38 and FCA 18.2.39) do not apply.

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Lane Clark & Peacock LLP
London, UK
Tel: +44 (0)20 7439 2266
enquiries@lcp.uk.com

Lane Clark & Peacock LLP
Winchester, UK
Tel: +44 (0)1962 870060
enquiries@lcp.uk.com

Lane Clark & Peacock Ireland Limited
Dublin, Ireland
Tel: +353 (0)1 614 43 93
enquiries@lcpireland.com

Lane Clark & Peacock Netherlands B.V.
(operating under licence)
Utrecht, Netherlands
Tel: +31 (0)30 256 76 30
info@lcpnl.com