Scottish Friendly Assurance Society Limited

Proposed transfer of long-term insurance business from FIL Life Insurance Limited to Scottish Friendly Assurance Society Limited

Initial Report of the With-Profits Actuary of Scottish Friendly Assurance Society

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1 Introduction

Purpose & Background

1.1. Scottish Friendly Assurance Society Limited ("Scottish Friendly" or "the Society"") has agreed to acquire a book of c39,000 closed-to-new-business Section 32 unit-linked pensions policies and c1,000 in-payment annuity policies (the "Transferring Business") from FIL Life Insurance Limited ("FIL").

1.2. The purpose of this report is to review the impact on with-profits policyholders in Scottish Friendly of the proposed transfer of the Transferring Business.

1.3. The proposed transfer to Scottish Friendly will be achieved by a Scheme of Transfer (the "Scheme") under Part VII of the Financial Services and Markets Act 2000. The proposed date of the transfer is 30 September 2026 subject to approval by Scottish Friendly's Delegates and the transfer being sanctioned by the High Court.

1.4. My report considers the potential impact of the Scheme on the security, benefit expectations and servicing of with-profits policyholders in Scottish Friendly Main Fund and the existing sub-funds prior to the transfer (collectively referred to as "SF With-Profits Policyholders" in this report).

1.5. I have considered the potential impact of the proposed Part VIII transfer (Project Meridian, expected to complete in early 2027) where Scottish Friendly will enter into a merger with Family Assurance Friendly Society Limited ("OneFamily") and how those proposals will impact this transfer below. I will also provide a further update in my Supplemental Report as the detail of Project Meridian is finalised.

1.6. This report does not consider the impact of the Scheme on the transferring policyholders, or existing Scottish Friendly policyholders who have no benefits linked to with-profits investments in the Scottish Friendly Main Fund or any Scottish Friendly sub-fund.

Conclusions on the Scheme

1.7. I have produced this report in my role as With-Profits Actuary ("WPA") for Scottish Friendly, to set out the impacts of the proposed Scheme on SF With-Profits Policyholders for the benefit of the Scottish Friendly Board.

1.8. I understand that a copy of my report will accompany the requisite application to the High Court requesting the sanctioning of the Scheme, and accordingly that it may be made available to policyholders and other parties affected by the Scheme.

1.9. In assessing the potential impacts of the Scheme, I have given due consideration to the effects of the planned transfer on the security, administration and benefit expectations of SF With-Profits Policyholders.

1.10. Taking into account the key features of the Scheme, and the discussion of these and other matters contained in this report, it is my view that:

- The terms of the policies held by SF With-Profits Policyholders will be unaffected by the Scheme,
- The Scheme does not have a materially adverse effect on benefit security, benefit expectations, or customer outcomes for SF With-Profits Policyholders, and:
- Affording membership to Transferring Business does not result in any material dilution of the benefits of membership for SF With-Profits Policyholders.

1.11. I therefore conclude that the Scheme will not result in a materially adverse impact on SF With-Profits Policyholders and there is no reason, in those terms, why the transfer should not proceed.

1.12. I am further satisfied that there will be no significant impact on the servicing that policyholders will receive as a result of the Scheme, the proposed approach to communications is appropriate and has paid due regard to the interests of policyholders and the need to treat them fairly.

Status and Disclosure

1.13. I am a Fellow of the Institute and Faculty of Actuaries, having qualified in 2003 and hold a WPA practicing certificate issued by the Institute and Faculty of Actuaries. I am an employee of Scottish Friendly and joined in 2023. Between 1999 and 2023, I worked for Prudential Plc (and subsequently M&G plc following the corporate restructure in 2019). I currently act in the Approved Role of WPA (SMF20a) for Scottish Friendly.

1.14. I confirm that I am not a policyholder of FIL and do not hold shares or have any other financial interest in FIL or any of the companies in the same group. I also confirm that I am not a policyholder of Scottish Friendly.

Reliances, Other Advice & Opinions

1.15. In finalising my report, I have reviewed Mr Scott McNeill's Report as Chief Actuary of Scottish Friendly and Mr John Jenkins's report as Chief Actuary of FIL. A copy of my report has also been provided to Mr McNeill and Mr Jenkins.

1.16. Mr Marc Loh of FTI Consulting has been appointed as Independent Expert and has been approved as such by the PRA who reviewed the appointment. In finalising my report, I have reviewed his report on the terms of the Scheme and considered his conclusions. A copy of my report has also been provided to Mr Loh.

1.17. In producing this report, I have placed reliance on the following information (amongst other information):

- Advice provided by external life insurance tax expert

Compliance with Actuarial Standards

1.18. This report and the underlying preparatory work that has been carried out is, in my opinion, compliant with the relevant Technical Actuarial Standards issued by the Financial Reporting Council ("FRC") for members of the Institute and Faculty of Actuaries ("IFoA") in all material respects. The relevant standards include:

- Technical Actuarial Standard 100: General Actuarial Standards v2.0
- Technical Actuarial Standard 200: Insurance

1.19. TAS 200 Provision 4. Insurance transformations specifically sets out the actuarial standards applicable to technical actuarial work related to insurance transformations, which includes providing an opinion on Part VII transfers.

1.20. I have also considered the relevant professional standards issued by the IFoA, the guidance issued by the regulator in FG 22/1 and the PRA policy statement (2022) on their approach to insurance business transfers and believe that this work is in line with those requirements. In particular, this report has been peer reviewed by Alan Rankine, FFA and is considered to be compliant with APS X2.

1.21. The Actuarial Profession has published a series of risk alerts requiring all actuaries to consider, and communicate clearly, the impact of climate change and sustainability issues or risks within their actuarial work and demonstrate an understanding of the limitations and uncertainties when evaluating and communicating climate related financial risks. Climate change is explicitly considered within this report as part of the consideration of the impact of the proposed transfer on the risk profile of Scottish Friendly.

2 Impact of the Scheme in relation to SF With-Profits Policyholders

Background to Scottish Friendly and Outline of the Scheme

2.1. As Chief Actuary of Scottish Friendly, Mr McNeill has documented a full background of Scottish Friendly in Section 3 of his report as a well as an outline of the Scheme in Section 4. In the interests of brevity, I have not reproduced this detail in my report.

Impact on SF With-Profits Policyholder security

2.2. It is useful to consider the reported solvency and risk appetite position of Scottish Friendly before and after the transfer to assess whether there is any material adverse impact to the security of SF With-Profits Policyholder benefits.

Pillar 1

2.3. The table below is taken from the SF Chief Actuary's report showing the estimated impact of the transfer on Pillar I basis as at 30 June 2025:

Pillar 1 position as at 30 June 2025	Pre-transfer (£m)	Post-transfer (£m)
Own funds	141.7	156.9
SCR	62.7	87.6
Solvency ratio	**226%**	**179%**

2.4. The impact of the transfer is to reduce the capital cover from 226% to 179% at 30 June 2025.

2.5. This shows that Scottish Friendly is expected to be able to meet its Pillar 1 capital requirements immediately after the Scheme, and that the business will remain comfortably above the solvency appetite trigger level[1].

Pillar 2

2.6. Pillar 2 results are not publicly available although the solvency ratio on a Pillar 2 basis is above the equivalent Pillar 1 position both before and after the Scheme is implemented. The impact of the Scheme is broadly commensurate with the Pillar 1 basis with similar drivers.

2.7. Further, Pillar 2 solvency is expected to remain in excess of solvency trigger levels meaning that there would be no immediate need to consider action in response to the Scheme to strengthen the solvency of the Society.

[1] Approved Pillar 1 trigger level is 160%

Management of additional Market Risk

2.8. The transfer is not expected to introduce new risks the Society is not already exposed to but will result in an increased exposure to existing risks. As the Transferring Business is predominately unit-linked in nature, the Society has an exposure to the fall in the value of assets backing those unit-linked policies, when in turn reduce the value of future charge income from those policies. This is the primary driver of the increased market risk the Society and reduced solvency position shown in 2.3 above.

2.9. The Society has many actions available to manage solvency which would be informed by the Board approved Capital and Financial Management Framework. Those actions could include the reduction of bonus rates, additional reinsurance and/or hedging as well as reducing investment risk in asset shares. Some of these directly impact future with-profits policyholder outcomes which I consider in further detail below.

2.10. The SA Chief Actuary notes in paragraphs 5.28-5.31 of his paper that one action to manage this increase in market risk and therefore improve solvency would be hedging of the equity component of market risk which, if implemented, has been estimated to improve the Pillar 1 solvency position by c.25%.

2.11. I note that this would remain an action which could be taken to reduce exposure to market risk in the future, should it ever be required.

Impact on Benefit Expectations of SF With-Profits Policyholders

2.12. This section contains further detail around the financial impact of the Scheme on SF With-Profits Policyholders. For the avoidance of doubt – There will be no change to the terms of the policies held by SF With-Profits Policyholders and I do not envisage any change to the governance of the with-profits business as a result of the proposed transfer.

2.13. In the main, existing Scottish Friendly customers are not directly impacted by the transfer. Whilst there is an increased exposure to risk, in particular market risk, this is aligned to the return seeking nature of with-profits business and the transfer is expected to be value adding for the Society as a whole. I note that there a potential for the transfer to have an impact in the following areas for SF With-Profits Policyholders:

- Expenses and expense allocation
- Society profit available for distribution
- Asset Share Investment strategy

2.14. I consider each of the points above in turn:

Expenses and Expense Allocation

2.15. Direct costs of the transfer are not expected to have an impact on existing policyholders' benefits. While the costs borne by Scottish Friendly will be met from the estate of the Main Fund, those costs have been allowed for in full in the pricing of the acquisition such that an acceptable rate of return is expected to be achieved for Society members on the investment.

2.16. Ongoing costs of the transferring business have the potential to change the expense base and the expense allocation of the Society in future. These costs were considered in detail in the original pricing of the transaction and are in the process of being validated by the project team working on the transfer.

2.17. The Chief Actuary also notes in Paragraph 6.17 of his paper that there will be no changes to the expense allocation methodology as a result of the transfer.

2.18. Given these points, I believe it is unlikely the transfer will have a material impact on the expense allocation and resulting benefit expectations of SF With-Profits Policyholders.

Society Profit Available for Distribution

2.19. The Transferring Business is expected to generate income in excess of the original consideration paid to FIL and the expenses incurred with the initial consideration recovered in a relatively short period of time. This profit generation will increase the security of existing benefits and/or enhance benefit expectations of SF With-Profits Policyholders.

2.20. The recovery of the initial consideration over a relatively short period of time is important in confirming the transaction is value adding for the current generation of participating policyholders, satisfying the requirements of COBS 20.2.60 (1)[2] and by extension COBS 20.2.28.

2.21. This additional profit will be included in the miscellaneous surplus assessment going forward, which supports the level of profits available for distribution to eligible members.

Asset Share Investment Strategy

2.22. There will be no changes to the current investment strategy for SF With-Profits Policyholders as a result of the transfer.

2.23. However, as discussed in paragraph 2.8 above, the increased market risk the Society is exposed to has the potential to impact future asset share investment strategy decision making.

2.24. In the event of a future market stress, solvency of the Society may reduce and reach the agreed trigger level earlier than otherwise would have been the case due to the additional market risk exposure. At that point a range of actions would be considered in accordance with the Capital and Financial Management Framework which could include a more conservative investment strategy for SF With-Profits Policyholders.

2.25. However, as discussed in paragraphs 2.10 & 2.11, a key management action available is to reduce the additional market risk exposure the Society is exposed to as a result of the transfer. I believe this mitigates most, if not all, of the potential impact the transfer has on the future investment strategy for SF With-Profits Policyholders.

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[2] *If non-profit insurance business is written in a with-profits fund, a firm should take reasonable steps to ensure that the economic value of any future profits expected to emerge on the non-profit insurance business is available for distribution during the lifetime of the with-profits business.*

Conclusion on Benefit Expectations

2.26. On balance, I do not believe there is any material adverse effect on the benefit expectations for existing with-profits policyholders. In practice, SF With-Profits Policyholders could reasonably expect to benefit from the additional income from the transferring business through increased ProfitShare distributions going forward.

Society Membership

2.27. It has been recommended that the Transferring Business is granted membership to the Society on a basis consistent with other non-profit and unit linked policyholders in the Main Fund as well as all policyholders in the sub-funds.

2.28. Given the value of membership to the Transferring Business is in practice negligible, I do not consider that affording membership results in any material dilution of the benefits of membership for SF With-Profits Policyholders.

Conclusions on the Impact of the Scheme

2.29. I am satisfied that, taking into account the Capital and Financial Management Framework of Scottish Friendly, the Society will remain capitalised to a level where the transfer will not lead to a materially adverse impact on the security or benefit expectations of SF With-Profits Policyholders

2.30. SF With-Profits Policyholders will benefit from the transfer which will continue to support the ProfitShare distributed to them as part of their final bonuses.

2.31. Further, I am satisfied that the Society has appropriate management actions in place to facilitate recover of its solvency position after significantly adverse events.

2.32. I will continue to monitor the solvency and risk position of the Society and will, if necessary, provide an update in a Supplementary report prior to the final Sanction Hearing court date.

3 Customer Outcomes

3.1. Ongoing compliance with the requirements of Consumer Duty is overseen by the Scottish Friendly's Board, with day-to-day compliance delegated to relevant Executives. The Board formally reviews and agrees an assessment of Scottish Friendly's compliance with Consumer Duty annually.

3.2. The transfer is not expected to have any adverse impact on Scottish Friendly's ability to comply with the requirements of Consumer Duty in respect of Existing Policies.

4 Other Considerations

Taxation

4.1. Scottish Friendly engaged an external expert in life insurance taxation to support the transfer who confirmed there is not expected to be any adverse impact to the tax position of Scottish Friendly, and by extension the SF With-Profits Policyholders, as a result of executing the Scheme.

Policyholder Administration

4.2. As set out in paragraph 6.24 of the Chief Actuary's report, there are no changes planned to the administration or operational processed for existing policies as a result of the transfer. Further, there are plans in place to ensure there is sufficient additional resource in the business to support the Transferring Policies meaning there should be no change to the servicing of the existing Scottish Friendly policies.

Communications to Policyholders

4.3. The Chief Actuary summarises the regulations governing Part VII transfers in his report which require that, unless the Court agrees otherwise, all policyholders in all affected companies should be informed of the proposed transfer in writing.

4.4. I am supportive of the proposed application to the court for a waiver from mailing all Scottish Friendly policyholders given that the transfer is not expected to materially adverse impact on the security, servicing or benefit expectations of SF With-Profits Policyholders.

4.5. I would further note the material cost of mailing all policyholders would directly impact the solvency of the Society and reduce the benefits that will be realised from the transfer.

4.6. I believe the proposed approach, whereby the delegates will vote on the transfer and notices will be placed in the national press and on the FIL and Scottish Friendly websites provides existing policyholders with an appropriate level of information about the transfer.

Effect of the Proposed Part VIII Transfer (Project Meridian)

4.7. Project Meridian is the proposal for Scottish Friendly to merge with OneFamily, subject to regulatory approval with completion anticipated to be early 2027. I note this follows the implementation of this Scheme and as such the Transferring Business will subsequently transfer to OneFamily when the Part VIII Transfer completes.

4.8. The Part VIII transfer will be subject to a separate regulatory approval process which will consider the impact of that transfer on all Scottish Friendly policyholders, including the Transferring Business. That transfer will be separately considered by an Independent Actuary, the regulators and Scottish Friendly's Chief Actuary and With-Profits Actuary.

4.9. Whilst the detail of the Part VIII transfer in the process of being finalised, I would note the following areas which will likely be relevant for any future With-Profits Actuary report:

- No changes are proposed to any Scottish Friendly policyholder terms and conditions and therefore no changes to policyholder benefit expectations are anticipated.
- All Scottish Friendly policyholders (including the Transferring Business) will become a member of OneFamily which will include similar benefits of membership that they currently have as Scottish Friendly members.
- As described in the Chief Actuary report (Section 8) there is no reason to believe that the benefit security of Scottish Friendly policyholders will be adversely impacted.
- Any emerging value from this Scheme is to be included in the assessment of value attributable to SF With-Profits Policyholders under the Part VIII Transfer. Whilst part of a separate regulatory process, I would note this approach should ensure the conclusion I reach above in paragraphs 2.19 to 2.21 remains reasonable.

5 Conclusion

5.1. I have produced this report in my role as WPA for Scottish Friendly, to set out the impacts of the proposed Scheme on SF With-Profits Policyholders. I will also provide a further update in my Supplemental Report as the detail of Project Meridian is finalised.

5.2. In assessing the potential impacts of the Scheme, I have given due consideration to the effects of the planned transfer on the security, administration and benefit expectations of SF With-Profits Policyholders.

5.3. Taking into account the key features of the Scheme outlined above, and the discussion of these and other matters contained in my report, it is my view that:

- The Scheme does not have a materially adverse effect on benefit security, benefit expectations, or customer outcomes for SF With-Profits Policyholders, and:
- Affording membership to Transferring Business does not result in any material dilution of the benefits of membership for SF With-Profits Policyholders.

5.4. I therefore conclude that the Scheme will not result in a materially adverse impact on SF With-Profits Policyholders and there is no reason, in those terms, why the transfer should not proceed.

5.5. I am further satisfied that there will be no significant impact on the servicing that policyholders will receive as a result of the Scheme, the proposed communications plan is appropriate and has paid due regard to the interests of policyholders and the need to treat them fairly.

Signed electronically

Callum Stuart FFA

With-Profits Actuary of Scottish Friendly Assurance Society Limited
16 March 2026