

**Transfer of business from
Markel International Insurance
Company Limited to Markel
Insurance Societas Europaea**

Scheme Report of the Independent
Expert under Part VII Section 109 of the
Financial Services and Markets Act
2000

6 December 2018

Use of this report

This report has been prepared for the High Court of England and Wales for the purpose of the terms agreed in the letter between Ernst & Young LLP and Markel International Insurance Company Limited, dated 18 September 2018. This report has been prepared to describe the transfer of various insurance business from Markel International Insurance Company Limited to Markel Insurance Societas Europaea, which will be effected under Section 109 of the Financial Services and Markets Act 2000 as amended by the Financial Services Act 2012 (together the 'FSMA').

A copy of this report will be made available to competent regulatory authorities, the High Court of England and Wales, policyholders, and any other person entitled to receive a copy under the FSMA.

I assume no responsibility whatsoever in respect of, or arising out of or in connection with the contents of this report to parties other than those mentioned above. If other parties choose to rely in any way on the content of this report then they do so entirely at their own risk. This report has been prepared solely for the purposes of the FSMA requirements for insurance business transfer schemes and should not be relied upon for any other purposes by any party.

Draft versions of this report and any other interim working papers must not be relied on by any person for any purpose.

Judgements about the conclusions drawn in this report should be made only after considering the report in its entirety as parts read in isolation may be misleading.

The responsibilities of Ernst & Young LLP shall also be limited as stated above

Signatory



Niranjana Nathan
Fellow of the Institute and Faculty of Actuaries
Partner
Ernst & Young LLP

Contents

1. Introduction	1
Purpose of this report	1
Independent Expert appointment	2
Professional guidance	2
Scope of my work	3
Use of data and reports	3
Peer review process	3
Layout of this report	3
2. Executive Summary	5
Background	5
Transfer description	6
Companies involved in the Transfer	7
Purpose of the Transfer	9
Conclusion	10
Key reasons for reaching my conclusion	10
Independent Expert declaration	13
3. Summary of my approach	14
Use of benchmarks in my work	16
4. Assessment of assets and liabilities transferring	17
5. Assessment of Technical Provisions	21
Summary of Technical Provisions for MIICL and the Transferring Policies	22
My review of MIICL and MISE claims reserves	24
6. Assessment of capital requirements	29
Summary of regulatory capital requirements of MIICL and MISE	31
7. Assessment of other issues	38
Impact of Brexit	38
The Financial Services Compensation Scheme	39
Direct and reinsurance policyholders	42
Insolvency procedures in the UK and Germany	42
Customer service	43
Financial Ombudsman Service	43
Policyholder communication strategy	45
Policyholders in jurisdictions outside the EEA	46
Governance	47
Regulatory protection	47
Pension arrangements	48
Tax implications of the Transfer	48
Implications of the Transfer on ongoing expense levels	48
Impact of other portfolio transfers	48
Set off	49
Legal Opinions	49
8. Security provided to policyholders	50
General considerations	50
Considerations for Non-transferring Policies	51
Considerations for Transferring Policies	51
Considerations for Transferee Policies	51
Considerations for Reinsurers of MIICL	52
9. Reliances and limitations	53
Appendix A Glossary	55
Appendix B Extract from EY Terms of Engagement	57
Appendix C Summary of data provided	59
Appendix D Checklist against PRA's Statement of Policy and SPU18 of the FCA Handbook	60
Appendix E Niranjana Nathan experience	62

1. Introduction

Purpose of this report

- 1.1 Markel International Insurance Company Limited ('MIICL') is proposing to transfer various policies of MIICL from MIICL to Markel Insurance Societas Europaea ('MISE') by means of an insurance business transfer scheme (the 'Transfer'). The policies which will transfer (the 'Transferring Policies') all contain some element of insured risk located in the European Economic Area ('EEA'). Please refer to section 2, paragraph 2.6, for a full definition of the policies making up the Transferring Policies, and a full description of the Transfer. After the Transfer is effected, the transferring policyholders of MIICL will become policyholders of MISE.
- 1.2 MIICL and MISE are both a part of the Markel group of companies ('the Markel Group') with the ultimate parent company being Markel Corporation, a company located in Richmond, Virginia and listed on the New York Stock Exchange.
- 1.3 The Transfer will be effected under Section 109 of the Financial Services and Markets Act 2000 as amended by the Financial Services Act 2012 (together the 'FSMA'). The High Court of England and Wales (the 'Court') must approve such insurance business transfer schemes at a sanctions hearing. The FSMA requires that a scheme report must accompany any application to the Court to approve an insurance business transfer scheme. This scheme report should be produced by a suitably qualified independent person (the 'Independent Expert') who has been nominated or approved for this purpose by the Prudential Regulatory Authority ('PRA').
- 1.4 The purpose of this report is to inform the Court, affected policyholders and other relevant parties of the likely effect of the Transfer. This report is not suitable for any other purpose.
- 1.5 The Transfer is intended to be effected on 29 March 2019 (the 'Transfer Date'). This is very shortly after the date of the sanctions hearing of the Transfer, which is currently scheduled for 28 March 2019.
- 1.6 Insurance and reinsurance companies in the UK are authorised to effect and carry out contracts of insurance and reinsurance by the PRA. Insurance and reinsurance companies in the UK are regulated by a combination of the PRA and the Financial Conduct Authority ('FCA'). The PRA and FCA replaced the Financial Services Authority ('FSA') as the regulator of the UK insurance industry on 1 April 2013. In this report the term PRA/FCA shall mean the combination of the PRA and the FCA carrying out their roles as the regulator of the UK insurance industry.
- 1.7 My report considers the effect of the Transfer upon all policyholders of the companies involved in the Transfer, any other group of policyholder (including beneficiaries under the wide definition in the FSMA) which I believe could be affected, or potentially affected, by the Transfer, reinsurers of MIICL whose policies will transfer, and other interested parties.
- 1.8 I will consider various groups of policyholder. In particular:
 - ▶ The policyholders of MIICL which will become policyholders of MISE after the Transfer (the 'Transferring Policyholders').
 - ▶ The policyholders of MIICL which will not transfer to MISE after the Transfer (the 'Non-transferring Policyholders')
 - ▶ The existing policyholders of MISE (the 'Transferee Policyholders').
- 1.9 My report contains a description of the Transfer, the methodology I have used to analyse the Transfer, the opinions I have formed and reasons why I have formed those opinions.

- 1.10 The use of 'I' and 'my' in this report generally refers to the work done by myself and the team operating under my direct supervision during the course of this review. However, when it is used in reference to an opinion, it is mine and mine alone.

Independent Expert appointment

- 1.11 MIICL has nominated Niranjan Nathan ('I', 'me') of Ernst & Young LLP ('EY') to act as the Independent Expert for the Transfer. This nomination has been approved by the PRA in consultation with the FCA. I am a Fellow of the Institute of Actuaries and a partner in the Actuarial Services practice of Ernst & Young LLP. I have more than 19 years' experience in general insurance. I have skills in all areas of general insurance actuarial work (including reserving, capital, Solvency II compliance, pricing, and transactions). Full details of my experience can be found in Appendix E. Ernst & Young LLP is a part of the global network of EY firms.
- 1.12 I confirm that I am aware of the requirements of Part 35 of the Civil Procedure Rules and the Protocol for Instruction of Experts to give Evidence in Civil Claims. As required by Part 35 of the Civil Procedure Rules, I hereby confirm that I understand my duty to the Court, I have complied with that duty and I will continue to comply 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.
- 1.13 I can confirm that I have no direct or indirect connections with MIICL, MISE or the Markel Group that I believe would affect my ability to act as the Independent Expert for the Transfer. In particular, I have never worked on any project involving MIICL, MISE or the Markel Group. I have no shareholding, investment or any other financial connection with any of the parties to the Transfer.
- 1.14 EY have performed some previous work for the parties involved in the Transfer, and related entities, although that work is not related to the subject of the Transfer. My assessment of the Transfer is not in any way affected by this previous work and so I do not believe that this affects my independence for this engagement. The PRA/FCA were aware of the services that EY have performed for the parties involved in the Transfer when approving my appointment as Independent Expert.
- 1.15 The costs of producing this report will be shared between MIICL and MISE.

Professional guidance

- 1.16 This report complies with the applicable rules on expert evidence and with the guidance for Scheme Reports set out by the PRA in the PRA's Statement of Policy and by the FCA in SUP 18 of the FCA Handbook. I have also taken into account the FCA's guidance on portfolio transfers, 'FG18/4: The FCA's approach to the review of Part VII insurance business transfers', issued in May 2018.
- 1.17 This report complies with Technical Actuarial Standards TAS 100: Principles for Technical Actuarial Work and TAS 200: Insurance as issued by the Financial Reporting Council ('FRC'), which is responsible for setting UK actuarial standards. The review performed on this work complies with Actuarial Profession Standard X2: Review of Actuarial Work issued by the Institute and Faculty of Actuaries. The work complies with Actuarial Profession Standard X3: The Actuary as an Expert in Legal Proceedings issued by the Institute and Faculty of Actuaries.
- 1.18 I believe that this compliance has been achieved with no major deviations from the guidelines.

Scope of my work

- 1.19 The scope of my work is detailed in the extract from my terms of reference provided in Appendix B. There are no areas where the actual work performed differs from this agreed scope.
- 1.20 I have not considered any alternative arrangements that could be implemented in place of the Transfer because I have been able to conclude that the Transfer is appropriate, and because no alternative arrangements have been proposed by any party. However, I will consider any consequences to policyholders should the Transfer not go ahead, in particular in relation to Brexit.

Use of data and reports

- 1.21 My analysis is based upon my review of the data and documentation produced by MIICL, MISE and their advisors, and on discussions with representatives from those firms.
- 1.22 I have relied on the completeness of the data provided to me. I have not audited nor have I independently verified the data and information supplied to me. This is because the data relies heavily on financial and internal management accounts which can only be verified by MIICL and MISE themselves, or by their auditors. However, I have reviewed it for reasonableness and for internal consistency. I have also received a specific statement of data accuracy from the management of MIICL and MISE.
- 1.23 I have also placed reliance upon the data insofar as when assessing claims I have not explicitly considered the potential for future causes of new claims that are not seen in the historical data. I consider this approach to be reasonable and in line with accepted actuarial practice.
- 1.24 A summary of the data provided to me can be found in Appendix C.
- 1.25 Most monetary amounts shown in this report are shown in millions of US Dollars. I have chosen this currency for convenience, as it is the financial reporting currency of MIICL, and the majority of communications to date with regulators and policyholders have been stated in US Dollars. Claim settlement amounts and assets held by MIICL and MISE will be in a mixture of different currencies, predominantly USD, GBP and EUR. Where applicable I have converted to US Dollars at the rate of \$1 USD = £0.75 GBP = €0.85 EUR. These are the exchange rates used for the production of the financial statements of MIICL as at 31 December 2017.

Peer review process

- 1.26 In accordance with the internal control processes of EY, the work documented in this report has been peer reviewed by a suitably qualified person (an Actuary within my own firm who has acted as the Independent Expert in other insurance business transfer schemes). The peer review process has included review of the methodology used and discussion of the key elements of the analysis.

Layout of this report

- 1.27 My report is structured as follows:
- ▶ Section 1: Introduction.
 - ▶ Section 2: Executive Summary, including a description of the Transfer, the companies involved, my conclusion, and the key reasons for reaching those conclusions.
 - ▶ Section 3: Summary of the approach I have taken.

- ▶ Section 4: Effects of the Transfer on assets and liabilities. This section includes balance sheets of MIICL and MISE.
- ▶ Section 5: Technical Provision assessment. This section describes the work that I have carried out to assess the claims reserves of MIICL and MISE.
- ▶ Section 6: Capital requirement assessment. This section describes the work that I have carried out to assess the capital modelling of MIICL and MISE.
- ▶ Section 7: Security provided to policyholders. This section summarises my assessment of the policyholder security considerations. It also covers other factors that might affect policyholders.
- ▶ Section 8: Reliances and limitations.
- ▶ Appendix A – Glossary of technical terms.
- ▶ Appendix B – Extract from my terms of engagement letter.
- ▶ Appendix C – List of data and materials reviewed.
- ▶ Appendix D - Checklist against the guidance on scheme reports as set out in the PRA's 'Statement of Policy, the PRA's approach to insurance business transfers – April 2015' ('PRA's Statement of Policy') and Chapter 18 of the Supervision Manual of the FCA Handbook ('SUP18 of the FCA Handbook').
- ▶ Appendix E - cv of Niranjana Nathan.

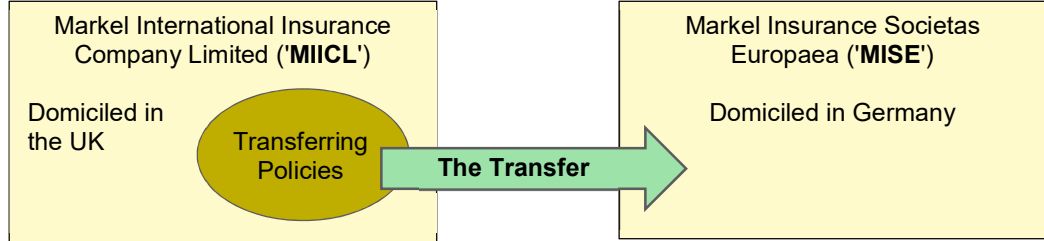
2. Executive Summary

Background

- 2.1 The UK voted to leave the EU on 23 June 2016 and then notified the European Commission of its intention to withdraw from the EU. Under the current terms of the withdrawal, the UK will cease to be a member state of the EU on 29 March 2019 ('Brexit'). An agreement has been made in principle that there will be transitional arrangements in place between the UK and the EU until 31 December 2020, although the nature of these transitional arrangements is currently unknown and I believe are not currently guaranteed.
- 2.2 MIICL currently uses various legislation set out in European law to be able to write and administer insurance policies in the EEA. After Brexit, there is a risk that MIICL will lose the right to carry out these activities. The Transfer is part of a wider reorganisation of the Markel Group, made in response to these challenges arising from Brexit. The reorganisation is designed to enable the Markel Group to continue providing services to their policyholders in the EEA.
- 2.3 MIICL, a UK company, writes insurance business across the EEA using the passporting mechanism of the European Union set out in Solvency II, and implemented in the UK through the Passporting Regulations. This is enabled using:
- ▶ A Freedom of Establishment basis ('FOE'), i.e., setting up branch offices of MIICL across Europe and writing EEA insurance business from those offices. Specifically, MIICL has branch offices in the Netherlands, Germany, Ireland and Spain.
 - ▶ A Freedom of Services basis ('FOS'), i.e., writing EEA insurance business directly from the UK head office of MIICL.
- 2.4 Following the decision of the UK to leave the European Union, the management of MIICL decided to use an alternative model to ensure business continuity, given that there is a risk that the existing model would not be viable after Brexit. Therefore, the Markel Group has carried out, or is carrying out, the following steps:
- ▶ Set up a new company, MISE, domiciled in Germany.
 - ▶ Replicate the branch office structure of MIICL for the new company MISE, so that MISE has a branch office in each of the Netherlands, Ireland, Spain and the UK.
 - ▶ For the affected European business, begin to make live renewals into the new company, MISE, as and when the branch offices of MISE are able to do so.
 - ▶ Transfer the remaining affected European business from MIICL to MISE using an insurance business transfer scheme (i.e., the Transfer). From the Transfer Date all renewals of the affected business would then be made into the new company, MISE.
 - ▶ Close the European branch offices of MIICL.
- 2.5 In summary, the effect of these changes is that all EEA exposures within the Markel business (excluding the UK, except where a policy solely relates to the UK and the EEA) will be insured by MISE.

Transfer description

- 2.6 The Transferring Policies will move from MIICL to MISE as part of the Transfer. After the Transfer the Transferring Policies will be administered by MISE, and MISE would pay claim amounts.



- 2.7 I will first describe which MIICL policies, or parts of policies, are classified as Transferring Policies. As I will explain below, all of the Transferring Policies contain some element of insured risk located in the EEA, although in some cases a policy might be split into two components, with only the risks located in the EEA transferring to MISE. Whether a policy is classified as a Transferring Policy depends on two things:

1. **The branch office through which the policyholder purchased their policy.**
MIICL has branch offices in Germany, the Netherlands, Ireland and Spain. If a policyholder has a policy sold through one of those branch offices then this will be stated on the policy documentation. All other MIICL policies are held with the UK head office of MIICL.
2. **The location of the insured risks covered by the policy.**
There are three relevant geographical groupings:
 - (i) Risks located in the UK.
 - (ii) Risks located in one of the other 30 EEA member states (the 'EEA30').
 - (iii) Risks located elsewhere in the rest of the world ('RoW')

- 2.8 The table below shows a summary of the status of policyholders, with the rows representing the MIICL office location for the policy, and the columns representing the geographical location of the risks insured. Each MIICL policy will belong to one, and only one of the entries in the table.

		Geographical location of risks insured			
		EEA30 only	EEA30 plus some UK	EEA30 plus some in RoW or UK	UK and/or RoW only
MIICL office location	UK Head office	Fully Transfer	Fully Transfer	Only the EEA30 part transfers	Will not Transfer
	Ireland Branch	Fully Transfer	Fully Transfer	Only the EEA30 part transfers	Will not Transfer
	Germany Branch	Fully Transfer	Fully Transfer *	Not Applicable	Not Applicable
	Spain Branch	Fully Transfer	Fully Transfer *	Not Applicable	Not Applicable
	Netherlands Branch	Fully Transfer	Fully Transfer	Not Applicable	Not Applicable

* I understand that there are not likely to be any policies with UK exposure from the branches in Germany and Spain, but if there are any, they will fully transfer.

- 2.9 From this we can see that where a policy only has exposure in the EEA30 or has exposure in both the EEA30 and the UK, then the policy will fully transfer to MISE. The situation is slightly more complicated for policies from the UK head office and the branch office in Ireland where a policy also has exposure to RoW. Those policies are split into two components, with only the component of the risk in the EEA30 classified as being a Transferring Policy. There are no policies classified as a Transferring Policy where the risks are only located in the UK or RoW; those policies will not transfer. I have marked 'Not Applicable' where an entry in the table does not include any policyholders (for example, there are no UK or RoW risks for any policyholders from the branch office in the Netherlands).
- 2.10 The policies of the UK head office are from three different sources depending on how MIICL acquired the policy, although for the purpose of the definition of Transferring Policies they are all treated as UK head office. The three main sources are:
- (a) Policies written by MIICL on a freedom of services basis in accordance with the Passporting Regulations.
 - (b) Policies in MIICL as a result of MIICL's merger with Markel Europe Plc on 1 July 2015.
 - (c) Policies reallocated from MIICL's former branch offices in Belgium and Sweden, following the closure of those branches.
- 2.11 MISE is in the process of setting up branch offices in the Netherlands, Ireland, Spain and the UK. As part of the Transfer, the Transferring Policyholders will move to the corresponding branch office of MISE. In due course, MIICL will close its branch offices in Ireland, the Netherlands, Germany and Spain.
- 2.12 The policies of the branch office of MIICL in Ireland which do not Transfer to MISE will be reallocated, in due course, to the UK head office of MIICL and administered from there until all claims are settled. There is no agreed timetable for this reallocation, which will happen after the Transfer at a time when it is practical for MIICL to do so. This reallocation from Ireland to the UK is not a part of the Transfer but I have considered the effect of the Transfer on those policies.
- 2.13 On the Transfer Date, the relevant assets and liabilities of MIICL will transfer to MISE. The majority of the transferring assets are made up of cash, short duration bonds and reinsurance assets. I describe the effect of the Transfer on the balance sheets of MIICL and MISE in section 4.
- 2.14 The third party reinsurers of MIICL will be transferred to MISE as part of the Transfer, covering the same risks as they were covering prior to the Transfer. A large part of the reinsurance recoverable is from other reinsurers in the Markel Group. From the reinsurers' perspective, there will be no change to the risks that they reinsure. In particular, where a MIICL policy is split (with a part of the policy transferring to MISE and a part remaining with MIICL) the reinsurance will continue to operate as usual, with a part of any reinsurance allocated to each of MISE and MIICL as appropriate.

Companies involved in the Transfer

Markel International Insurance Company Limited ('MIICL')

- 2.15 MIICL is an insurance company incorporated in England and Wales on 20 November 1969 as Terra Nova Insurance Company Limited. It changed its name to Markel International Insurance Company Limited on 4 November 2002. MIICL is a part of the Markel Group.
- 2.16 MIICL is authorised by the PRA and regulated by the PRA/FCA in the UK, and has permission to carry on certain classes of general insurance business. Additionally, MIICL has branch offices in the Netherlands, Germany, Ireland and Spain and is authorised and regulated by the regulatory authorities in those countries.

- 2.17 MIICL holds surplus lines licenses and is an accredited reinsurer in most US states. It is also able to write general insurance in a number of other territories. The main areas of business written by MIICL are:
- ▶ Global Insurance – includes a wide range of commercial risks, but is mostly focused on General Liability and Professional Liability for large accounts and complex risks often with high attachment points.
 - ▶ Specialty & Financial – the largest components are Professional Liability, Trade Credit, Equine and Livestock but this also includes other specialty lines of business (e.g., Personal Accident and Contingency).
 - ▶ Reinsurance – includes a wide variety of global reinsurance, written on a per-claim, proportional, and catastrophe event basis. A large component is written via the Markel operations in South America.
 - ▶ Marine & Energy – includes various property and liability risks for vessels and energy installations.
 - ▶ UK National Markets - includes UK legal expenses, commercial insurance of small and medium UK businesses covering Professional Liability, Property and General Liability.
 - ▶ Branch office business – written from Ireland, Germany, the Netherlands and Spain – the business is mostly Professional Liability, General Liability, Directors and Officers Liability and Personal Accident.
 - ▶ Sweden – this is the discontinued business of the old branch office in Sweden. The remaining risks are mostly Professional Indemnity and Marine from Nordic countries.
 - ▶ Other MIICL – various intra-group reinsurance exposures.
- 2.18 MIICL writes around \$0.6bn of gross of reinsurance premium per year and has \$1.0bn in net of reinsurance technical provisions as at 31 December 2017. The annual amount of premium written in respect of the Transferring Policies is approximately \$0.1bn.

Markel Insurance Societas Europaea ('MISE')

- 2.19 MISE is an insurance company incorporated in Germany in 2018 as Markel Insurance Societas Europaea. MISE is a part of the Markel Group.
- 2.20 MISE is authorised and regulated by Bundesanstalt für Finanzdienstleistungsaufsicht ('BaFin') in Germany, and has permission to carry on certain classes of general insurance business. Additionally, MISE is in the process of setting up branch offices in the Netherlands, Ireland and Spain, and will be regulated by the regulatory authorities in those countries.
- 2.21 Concurrent with the Transfer, MISE is planning to establish a UK branch office on an FOE basis in the UK from where it will write new business and administer the policies of the Transferring Policies from the UK head office of MIICL after the Transfer. MISE is planning to convert the UK EEA branch to a third country branch post-Brexit (by means of an application for full UK authorisation under FSMA) either after the expiry of the transitional period, if one is agreed, or during the three year period of the UK's proposed temporary permissions regime. MISE is in the process of developing these plans in consultation with the PRA. The PRA cannot legally authorise a third country branch of an EEA insurer until after Brexit, or if there is a deal and a transition period for passporting (as the current regime for FOE branches under the Passporting Regulations will continue to apply), the authorisation will be formally given as the transition period expires. There is currently no requirement for firms to apply for a third country branch by the Brexit date but the UK government and the PRA and FCA have

set out details of a temporary permissions regime that will apply in the event no withdrawal treaty is agreed with the European Union.

- 2.22 I have been informed that MISE has all licences required to assume the Transferring Policies (except that MISE is in the process of securing a license to write legal expenses business in Germany). I understand that by the Transfer Date all branches of MISE will be functioning, and all the necessary licenses will have been obtained.
- 2.23 MISE was established by the Markel Group in July 2018 as the main insurance carrier for risks located in the EEA30. As and when the relevant policies of MIICL expire, the policyholders will be offered to renew their policy with MISE rather than MIICL. In this way, MISE is a continuation of the EEA30 business written by MIICL. After the Transfer, the liabilities in respect of the expired policies will have moved to MISE, so that all EEA30 policies (old and new) will be provided by, and administered by, MISE. MISE began accepting business on 1 October 2018. So far, MISE has only written a small amount, all from its head office in Germany.
- 2.24 MISE will have a significant intra-company reinsurance arrangement (the 'Bermuda QS') with Markel Bermuda Limited, who will reinsure 90% of all business written by MISE on a quota share basis following the Transfer. The Bermuda QS will cover the future business of MISE on a quota share basis, and will also cover 90% of the settlement value of the Transferring Policies. The Bermuda QS will be in place on, or prior to the Transfer Date. For further details on the Bermuda QS, refer to paragraph 4.17.

Markel Bermuda Limited

- 2.25 MBL is an insurance company incorporated in Bermuda as Limited ('MBL'). MBL is authorised and regulated by the Bermuda Monetary Authority in Bermuda and has permission to provide diversified specialty insurance and reinsurance products to corporations, public entities and property and casualty insurers. MBL is registered as both a Class 4 commercial insurer and Class C long-term insurer under the insurance laws of Bermuda.
- 2.26 MBL writes approximately \$1.3bn of gross of reinsurance premium per year and has \$1.8bn in available capital on a US accounting basis as at 31 December 2017.

Purpose of the Transfer

- 2.27 The purpose of the Transfer is to reorganise the European operations of the Markel Group in such a way as to comply with the relevant insurance regulations. There is considerable uncertainty in the UK with regard to the future regulatory landscape as a result of Brexit. In particular, I believe that it is unlikely that MIICL would be able to continue to use FOS and FOE, in its current form, as a means of writing insurance business in the EEA. There is also uncertainty for the status of the existing EEA30 policyholders of MIICL, where MIICL would be required to administer the remainder of the policy and make any claim payments due; the regulations governing this process after Brexit are unclear. I will discuss the issue of Brexit in more detail in paragraph 7.2.
- 2.28 Therefore, the Markel Group has elected to place all EEA30 risks into a European insurance carrier, MISE, so that continuity of operations can be guaranteed. This will enable the Markel Group to service the existing European client base, and also to write new business.

Conclusion

- 2.29 I have considered the Transfer and its likely effects on the policyholders of MIICL and MISE. I confirm that I understand my duty to the Court.

I conclude that the security provided to policyholders will not be materially adversely affected after the Transfer, that no group of policyholders would be adversely affected to a material extent by the Transfer, that the level of customer service provided to policyholders would be unaffected by the Transfer, and that therefore there is no reason that the Transfer should not go ahead.

Materiality

- 2.30 As Independent Expert, I have considered the effect of the Transfer on the policyholders involved, and in particular, I have considered whether any group of policyholders is adversely affected to a material extent by the Transfer. I will explain below what I mean by a “material extent”.
- 2.31 Firstly, it is important to note that an insurance business transfer can have different effects on different groups of policyholder. There may be some effects of a transfer that are positive to a particular policyholder, and some effects that are negative (i.e., adverse). If some of the effects of a transfer are adverse, this does not necessarily mean that the transfer is unfair, because the adverse effect might be insignificant or it might be outweighed by other positive effects.
- 2.32 Secondly, my conclusions are partly based on various statistical estimates of future events, and those estimates will always be subject to some uncertainty (because they are estimates of future, unknown events). I have used my professional judgement to weigh up the conclusions from those statistical estimates, bearing in mind the uncertainties involved.
- 2.33 For the purpose of this report, I consider that a matter is material if it could, either individually or collectively, influence the decision to be taken by the user of the report. Assessing this materiality requires reasonable judgement on the context of the work and the way in which it is reported. I have considered the overall effect of the Transfer on each group of policyholders, after considering the aggregate effect of all of the various issues.
- 2.34 There might be some matters described in this report which are not material, but which I believe would be of interest to policyholders.

Key reasons for reaching my conclusion

- 2.35 I set out below the key reasons for reaching my conclusions. This is not an exhaustive list of the issues I have addressed, but rather a summary of the parts that I believe are most relevant to policyholders.
- 2.36 There are four main topics I will discuss below:
- ▶ The sufficiency of the technical provisions of MIICL and MISE.
 - ▶ The level of capitalisation of MIICL, MISE and MBL, and the associated financial strength of those firms.
 - ▶ The considerations of changes to the servicing of policies.
 - ▶ The impact of Brexit.

Sufficiency of technical provisions

- 2.37 The technical provision is the money set aside by an insurance company to pay future claim amounts. It is an important part of the security offered to policyholders; it is important that an insurance company has sufficient money available to pay these future claims. I have reviewed the technical provisions of MIICL and MISE pre and post transfer.
- 2.38 My review has included an assessment of the approach, methodology and governance that are used to determine the technical provision levels. I have also assessed key assumptions used in determining the technical provisions and also carried out a benchmark review for the most material and uncertain aspects of the technical provisions.
- 2.39 I have concluded that the technical provisions are set on an appropriate and consistent basis for both MIICL and MISE, both before and after the Transfer.

Capitalisation position of entities post transfer

- 2.40 I have reviewed the regulatory capital position of MIICL and MISE pre and post the Transfer. Post Transfer, both entities would meet regulatory capital requirements by a large margin. The regulatory capital is calibrated at a 1 in 200 level of sufficiency. This suggests that the overall level of security provided to the policyholders of both MIICL and MISE is good.
- 2.41 Both MIICL and MISE are rated 'A' by both Standard & Poor and A.M. Best, and I would expect that this would be maintained after the Transfer. This suggests a good level of financial strength.
- 2.42 A significant proportion of the assets held by MISE will be in the form of a reinsurance asset with MBL. This will increase the counterparty default risk for MISE, but will be a strong source of security for MISE, given the size and financial strength of MBL. MBL is also rated 'A' by both Standard & Poor and A.M. Best.

Servicing of policyholders

- 2.43 There will be no changes to the way that policies are administered and claims paid, and I do not anticipate any changes to the level of customer care provided.

The impact of Brexit

- 2.44 Brexit has introduced or exacerbated a number of risks for insurers operating in the UK, particularly for those that trade across EU borders. There is also the potential that after Brexit, UK insurers lose the ability that currently exists to insure and service risks in the EU (outside of the UK) without being authorised by local regulators. Not proceeding with the Transfer gives the potential, depending on the outcome of ongoing Brexit negotiations, of policyholders not legally being able to have their claims paid or policies serviced.
- 2.45 There are some Brexit risks which cannot be avoided in any practical way; however, I believe that the most material risks, relating to how services can be provided to EEA policies, can be mitigated by transferring those policies or parts of policies to MISE (i.e., by effecting the Transfer).

Effect on specific policyholder groups

2.46 The table below shows a summary of the reasons for reaching my conclusion, for each of the groups of policies. A policyholder might hold a policy in one or more of the three categories.

Type of policy	Summary of the reasons for my conclusion
<p>Non-transferring Policies</p> <p>These MIICL policies will remain with MIICL after the Transfer</p>	<p>There will be minimal change to the balance sheet and financial strength of MIICL after the Transfer because the Transferring Policies are only approximately 15% of the overall MIICL business.</p> <p>Based on my review, I conclude that the technical provisions of MIICL are set on a reasonable basis, and that MIICL would meet its regulatory capital requirement after the Transfer.</p> <p>The policyholders will belong to the same legal entity, with exactly the same governance structure, regulatory framework, policy terms and conditions, and their policies will be serviced in the same manner as prior to Transfer.</p>
<p>Transferring Policies</p> <p>These MIICL policies will move from MIICL to MISE as part of the Transfer</p>	<p>The policies will move from MIICL and MISE; based on my review, I conclude that the both MIICL and MISE are both strongly capitalised companies, and that they provide a broadly equivalent level of security.</p> <p>Based on my review, I conclude that the technical provisions of MISE are set on a reasonable basis, and that MISE would meet its regulatory capital requirement after the Transfer.</p> <p>The policy terms and conditions will be the same, and the policies will be serviced in the same manner as prior to Transfer. The policyholders will belong to a different legal entity; but the governance structure and regulatory framework is not materially different.</p> <p>Without the Transfer, I believe that there are some key risks related to Brexit; in particular, that MIICL could be prevented by law from paying claims and servicing policies. This would be detrimental to policyholders.</p>
<p>Transferee Policies</p> <p>These MISE policies will remain with MISE after the Transfer</p>	<p>Based on my review, I conclude that MISE will be strongly capitalised and provide high level of security.</p> <p>Based on my review, I conclude that the technical provisions of MISE are set on a reasonable basis, and that MISE would meet its regulatory capital requirement after the Transfer.</p> <p>The policyholders will belong to the same legal entity, with exactly the same governance structure, regulatory framework, policy terms and conditions, and their policies will be serviced in the same manner as prior to Transfer.</p>

Effect on other parties

2.47 I did not identify any other parties that would be materially affected by the Transfer.

Supplementary report

- 2.48 My conclusions are based on the information available to me at the time of writing this report. I will produce a Supplementary Report prior to the Transfer Date, and this will comment on the most recent information available. I expect that this will include details of movements in claims paid and claims incurred since 31 December 2017. There may be other data that I will request for the purposes of the Supplementary Report, depending on the circumstances and any changes to the financial positions of the companies involved.

Independent Expert declaration

- 2.49 In reaching the conclusions set out below, I have applied the following principles. I have sought to adhere to:
- a. Exercise my judgement in a reasoned and justifiable manner;
 - b. Describe the impact on all classes of beneficiaries (principally the policyholders of MIICL and MISE) and the reinsurers of MIICL whose contracts will form part of the Transfer;
 - c. Indicate how the Transfer might lead to any changes in the material risks to the benefits of different classes of beneficiaries;
 - d. Indicate (in broad terms) the impact on the actuarial information of adopting alternative plausible assumptions;
 - e. Assess the impact on all classes of beneficiaries;
 - f. Indicate the proposed rationale for the Transfer to proceed;
 - g. Include (in summary) the most material information on which my opinion is based; and,
 - h. Describe the rationale for my opinion.
- 2.50 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 and conclusions I have drawn represent my true and complete professional opinions on the matters to which they refer.
- 2.51 As required by Part 35 of the Civil Procedure Rules, I hereby confirm that I understand my duty to the Court, I have complied with that duty and I will continue to comply with that duty.
- 2.52 I do however consider it necessary that I review the most recent information, up to the date of the Transfer, when this becomes available later in the year, before confirming my opinion and conclusions.

3. Summary of my approach

3.1 The section below sets out my approach for assessing the Transfer.

Gain a thorough understanding of the Transfer and identify the groups of policyholders that would be affected.

3.2 This was achieved through discussions with MIICL, MISE, and their advisors to understand the Transfer, together with reviewing the documents agreed between the parties for the implementation of the Transfer. This includes the scheme document, being the legal document which effects the Transfer, the policyholder communication materials, and the witness statement of Andrew John Davies made on behalf of MIICL and MISE. In Appendix C I have set out the materials I have reviewed.

Review of the claims reserves of MIICL and MISE

3.3 The claims reserve of an insurance company is an estimate of the amount of money that the company will need to pay out to its policyholders as claim payments in the future. It is an unknown amount of money (because future claim amounts are unknown and uncertain) but it can be estimated by the company by using various statistical methods.

3.4 An important question when considering the security provided to policyholders of a company is whether the estimation of the claims reserves has been carried out in an appropriate way. This is because there is a risk that the company has underestimated the amount of money that it will need to pay future claim amounts to policyholders, and therefore a risk that it will not be able to pay those claim amounts.

3.5 Therefore, I have considered the adequacy of significant parts of the claims reserves of MIICL and MISE. This is described in section 5.

Review of the assets and capital requirements of MIICL and MISE

3.6 A second important aspect of the modelling work I have reviewed relates to the uncertainty in the amount of the future claim amounts. The amount of capital in an insurance company is the difference between the value of the assets of the company (e.g., investments, cash and amounts due from debtors), and the value of the liabilities of the company (e.g., future claim payments and amounts due to creditors). This amount is also sometimes referred to the amount of 'available capital' or the amount of 'surplus' of a company. It is one measure of the financial strength of the company.

3.7 Insurance regulators require that an insurance company has at least a certain minimum amount of capital (i.e., so that it has a level of buffer to help make future claim payments). The capital requirement is needed because the future amount of the claim payments is uncertain; the insurance company and the regulator wish to be confident that the company is able to meet all future claim payments, even in an unlikely adverse scenario. However, this does not mean that a company will be able to meet all claim payments in all circumstances; only that there is a higher probability of being able to do so.

3.8 I have considered the approach taken by MIICL and MISE in calculating their regulatory capital requirements. I discuss this in section 6.

Consider the level of security offered to each group of policyholders, assuming existing arrangements, and assuming the Transfer is effected

3.9 I have considered the balance sheets of MIICL and MISE, both before and after the Transfer, as part of my assessment of their relative financial positions, including the net assets of the companies and the level of capital. This is discussed in section 4.

Consider the potential impact of the Transfer on levels of customer service

- 3.10 I have considered how the level of customer service provided to each group of policyholders could change following the Transfer. This is described from paragraph 7.30

Consider any other factors that might affect policyholders (for example, ongoing expense levels, pension arrangements etc.)

- 3.11 These are set out in section 7:

- ▶ Impact of Brexit
- ▶ The Financial Services Compensation Scheme
- ▶ Direct and reinsurance policyholders
- ▶ Insolvency procedures in the UK and Germany
- ▶ Customer service
- ▶ Financial Ombudsman Service
- ▶ Policyholder communication strategy
- ▶ Policyholders in jurisdictions outside the EEA
- ▶ Governance
- ▶ Regulatory protection
- ▶ Pension arrangements
- ▶ Tax implications of the Transfer
- ▶ Implications of the Transfer on ongoing expense levels
- ▶ Impact of other portfolio transfers
- ▶ Set off

Materiality

- 3.12 Throughout my work I have applied the concept of materiality, as set out from paragraph 2.30 above.

Use of benchmarks in my work

- 3.13 At various points in my review I have used 'benchmarks' to test the assumptions used in the Markel claims reserving and capital modelling analysis. This includes claim development patterns (i.e., the assumptions used to calculate the level of future claim payments) and loss ratio picks (i.e., the profitability of the business being written by Markel). These benchmarks are derived from the data and analysis of other firms or groups of firms in the insurance market. This is a valuable exercise because it compares the assumptions used by Markel to those used by other firms in the wider insurance market.
- 3.14 As part of claims reserving and capital modelling work it is useful, in the first instance, to consider the firm's own data, and the results of the analysis using that data. This is because this data, by definition, relates entirely to the firm's own business and is relevant to the firm's own specific characteristics (in terms of the exact type of business written and the way that the firm manages and pays claims). It is then useful to compare the assumptions and results with benchmarks from the wider market.
- 3.15 The benchmarks I have used are split by line of business. The applicability of these benchmarks to a line of business varies according to the number of firms included in the sample:
- ▶ Including all of the market data (or a very wide range of firms) in the sample will give a more generic view of the insurance market. This is a useful comparison to make because the sample will have a large volume of market data (and so will have greater credibility) and will show how Markel compares to the market as a whole.
 - ▶ Including a small sample of firms that we believe are similar to Markel will give a benchmark which is specific to the portfolio of business written by Markel – this is an advantage. However, this benchmark sample will contain fewer firms and less data, and might therefore have lower credibility than the market-wide sample.
- 3.16 For my review I have used a combination of the above two approaches (i.e., market-wide and specific benchmarks). The benchmarks I have used are based on an aggregation of data from across the insurance clients of my firm. This includes a large number of firms operating in the London Insurance Market including 15 firms writing more than \$0.5bn of premium per year (and so of a comparable size to, or a larger size than MIICL). This sample also includes approximately 40% of all the business written in the Lloyd's of London insurance market, a large part of which is similar to the business written by MIICL. Some of my benchmarks are also based on an analysis of publicly available market wide data.
- 3.17 I believe that the benchmarks I have used are appropriate for my analysis of MIICL and MISE because they are based on a wide range of firms, which are of a similar size to MIICL, and which write similar types of business to MIICL and MISE.

4. Assessment of assets and liabilities transferring

- 4.1 In order to show the effect of the Transfer on the assets and liabilities I have reviewed the balance sheets of MIICL and MISE. These balance sheets are based on a scenario where the Transfer was notionally effected on 31 December 2017. This is not the Transfer Date; however, it is instructive to consider the financial positions at 31 December 2017 because this is the most recent date at which audited financial information is available for MIICL. I believe that this is the most appropriate basis to view the Transfer, because it is based on the most recent set of audited financial statements.
- 4.2 The starting balance sheet for MIICL is based on the audited UK GAAP (the Generally Accepted Accounting Principles) financial statements as at 31 December 2017. This is the standard basis for the preparation of accounts of UK insurance companies.
- 4.3 MISE is a new company, and was set up with an amount of \$48m in assets, injected from the parent company of the Markel Group. For the purpose of this balance sheet comparison I have produced a notional starting balance sheet for MISE, with that starting amount of capital. I believe that this will show the best currently available view of the Transfer on the balance sheet of MISE.
- 4.4 I expect that the normal activities of MIICL and MISE will continue in the period between 31 December 2017 and the Transfer Date (for example, paying policyholder claims and writing or renewing policies). The actual position of MIICL and MISE will be different to that represented below due to the actual experience between 31 December 2017 and the Transfer Date. However, I believe that this gives the best currently available picture of the Transfer. I will produce a Supplementary Report prior to the Transfer Date, and this will comment on the most recent information available. I expect that the updated financial information will be based on data as at 30 September 2018.

Effect of the Transfer on MIICL balance sheet

- 4.5 The table below shows the balance sheets for MIICL, both before and after the Transfer. As described above, I have constructed this balance sheet information to be on an equivalent UK GAAP basis. For clarity, I have not shown the detailed balance sheets, and have grouped together various line items.

Table 4a: MIICL balance sheets – 31 December 2017 - \$Ms.

	MIICL		
	Pre Transfer	Effect of Transfer	Post Transfer
Investments	1,358	(136)	1,222
Reinsurers' share of technical provisions	544	(73)	471
Deferred acquisition costs	50	(6)	44
Other debtors	210	(31)	178
Assets	2,162	(246)	1,915
Technical provisions	1,574	(235)	1,339
Other Creditors	45	(7)	38
Available capital	543	(4)	539
Liabilities	2,162	(246)	1,915

MIICL assets

- 4.6 The investments held by MIICL are mostly cash and short term bonds (approximately 75% of the total), with the remainder held as equity type investments. I understand that this is in line with the MIICL policy for the distribution of the asset mix, and that there are no plans to change the mix of assets held by MIICL. The MIICL policy is to hold assets in a mixture of

currencies which match the currencies of the underlying claim liabilities (this avoids the exchange rate risk which might arise if there were a mismatch between assets and liabilities). MIICL periodically adjusts the balance of assets held in different currencies as and when the mix of liabilities changes.

- 4.7 The assets transferring from MIICL consist of the reinsurance asset in respect of the transferring business and investments. There is also a small amount of other debtors, which is mainly in respect of amounts of premium owed by policyholders. The investments transferring are in the form of cash and short term bonds. The amount of assets transferring is relatively small relative to the overall asset size, and would not materially change the mix of assets held by MIICL.
- 4.8 I have reviewed the MIICL Own Risk and Solvency Assessment which sets out the management's view on the main risks to the company (this document was dated 27 February 2018). The relevant parts on the investment risk sections set out the downside scenarios for investment risk, including liquidity risk, for MIICL. In section 6, I also describe my review of the MIICL internal model which estimates market risk in conjunction with the other risks to the firm.
- 4.9 I am satisfied that the mix of assets held by MIICL is appropriate for a firm of this type, and that the Transfer will not materially affect the level of market and liquidity risk.

MIICL Liabilities

- 4.10 The balance sheet of MIICL as at 31 December 2017 shows gross technical provisions of \$1,574m and a reinsurance asset of \$544m (and so technical provisions net of reinsurance of \$1,030m). These amounts reconcile to the technical provisions shown in table 5a in paragraph 5.4.
- 4.11 The liabilities transferring from MIICL consist mainly of the technical provisions (discussed in section 5) in respect of the transferring business. Approximately 16% of the technical provision amount would transfer. There is also a small amount of other creditors, which is mainly in respect of amounts owing to brokers and reinsurers.
- 4.12 MIICL had available capital of \$543m. There will be a small reduction in the level of available capital after the Transfer, based on these estimates.

Effect of the Transfer on MISE balance sheet

- 4.13 The table below shows the balance sheets for MISE, both before and after the Transfer. As described above, I have constructed this balance sheet information to be on an equivalent UK GAAP basis. For clarity, I have not shown the detailed balance sheets, and have grouped together various line items.

Table 4b: MISE balance sheets – 31 December 2017 - \$Ms.

	MISE			
	Pre Transfer	Effect of Transfer	Bermuda QS	Post Transfer
Investments	48	136	(146)	38
Reinsurers' share of technical provisions	0	73	146	219
Deferred acquisition costs	0	6	0	6
Other debtors	0	31	0	31
Assets	48	246	0	294
Technical provisions	0	235	0	235
Other Creditors	0	7	0	7
Available capital	48	4	0	52
Liabilities	48	246	0	294

MISE assets

- 4.14 The notional balance sheet of MISE as at 31 December 2017 only shows one entry: the starting amount of assets of \$48m, which is held as cash and short term bonds.
- 4.15 As described above in paragraph 4.7, the assets (other than reinsurance asset and debtors) will mostly be cash and bonds. The longer term investment strategy of MISE will be to hold a portfolio of assets similar to MIICL. Therefore, there would be no change to the investment strategy of the insurer of the transferring Policies, and this does not affect my conclusion on the Transfer. The MISE policy on the currency of assets held is the same as the policy for MIICL; i.e., to hold assets in a mixture of currencies which match the currencies of the underlying claim liabilities. The claim liabilities for MISE are predominantly in EUR and GBP. MISE periodically adjusts the balance of assets held in different currencies as and when the mix of liabilities changes.

MISE Liabilities

- 4.16 After the Transfer the balance sheet of MISE shows gross technical provisions of \$235m and a reinsurance asset of \$219m (and so technical provisions net of reinsurance of \$16m). The available capital of MISE is \$52m.

Bermuda QS

- 4.17 The Bermuda QS will be effected on, or prior to the Transfer Date. This would immediately cede 90% of all of the transferring claim liabilities (net of all other reinsurance) to MBL. It will also apply to 90% of the value of the future business written by MISE. The Bermuda QS will apply to the claim liabilities net of all other reinsurance, including any reinsurance exhaustion or non-recovery (i.e., bad debt). This means that the Bermuda QS will effectively provide 90% cover for the MISE calendar year net underwriting result.
- 4.18 The reinsurance asset transferring from MIICL already has a large component with MBL (approximately \$50m on a best estimate basis). This reinsurance asset, along with the addition of the Bermuda QS, would mean that the overall percentage of the gross technical provision ceded from MISE to MBL is approximately 92%. Transferring liabilities will be gradually settled, and I would expect that the total percentage ceded to MBL would reduce over time, and would eventually reach 90% (i.e., only the Bermuda QS).

Premium payable by MISE to MBL

- 4.19 A premium will be payable by MISE to MBL in respect of the Bermuda QS. This is currently estimated to be \$146m, which is equal to the amount of the reinsurance technical provision amount on the contract, as recognised by MISE on a GAAP basis. This means that on a GAAP basis the Bermuda QS has a neutral effect on the available capital of MISE (MISE will pay a premium of \$146m to MBL but this will be offset by an equal and opposite amount of additional reinsurance asset from the Bermuda QS). If claims are settled in line with the assumptions of the GAAP basis, then over time MBL will pay an amount of \$146m to MISE in the form of reinsurance recoveries. This pricing mechanism is in line with the Markel Group's own policies and procedures for placing intra-group reinsurance. The premium will be paid immediately by MISE to MBL. Further payments on the contract would be made by MISE to MBL from time to time, as profits (or losses) emerge.
- 4.20 There is a small amount of conservatism in the estimation of the reinsurance recoveries on the Bermuda QS due to the prudent reserving philosophy used by MIICL and MISE on GAAP basis (as I will explain in paragraph 5.33, the financial statement basis is set on a conservative basis). On a realistic best estimate basis (i.e. without the conservatism in the claim reserve estimates), the level of reinsurance payments from MBL to MISE would be slightly less than the \$146m premium paid from MISE to MBL. However, based on the information I have available to date I believe that the premium payable by MISE for the Bermuda QS is set at a fair and reasonable level. This is because there will be much less downside risk in MISE with the Bermuda QS in place (since MBL will meet the cost of settling 90% of the value of all claims regardless of their value).

Finalisation of the terms of the Bermuda QS

- 4.21 At the time of writing this report, the terms of the Bermuda QS (including the premium payable on the contract) are only available in draft. The contract wording will be agreed prior to the Transfer Date. Markel will also provide me with final documentation on the calculation of the premium amount payable by MISE. From my discussions with Markel I do not anticipate any material changes to the draft terms of this contract between now and the Transfer Date. I will review the terms of the contract and the premium payable when they are agreed, and will comment on this in my Supplementary Report.

5. Assessment of Technical Provisions

- 5.1 The technical provision amount is the money set aside by an insurance company to pay future claim amounts. It is an important part of the security offered to policyholders; it is important that an insurance company has sufficient money available to pay these future claims. A firm will carry out some form of actuarial analysis to estimate the amount of the technical provisions required. I have carried out a review of this analysis. I have reviewed the technical provisions of MIICL, and the technical provisions associated with the Transferring Policies (which will become the technical provisions of MISE after the Transfer).
- 5.2 I will use the term technical provisions to refer to the total provision set aside for all of the future claim payments on a GAAP basis. Some of the intermediate calculations in the actuarial work will not be on a GAAP basis and in those circumstances I will use, for convenience, the term 'claims reserve'. In the table below I will show a reconciliation of the claims reserve to the total technical provision shown in the GAAP financial statements.
- 5.3 I will use the term 'best estimate' when referring to an estimate of the claims reserve, where that estimate has no intended margin for prudence or optimism, and where it is a reasonable estimate of the claims reserve given the data and information available. There are inherent risks in insurance business, and there are uncertainties when estimating a claims reserve amount. The methods used by actuaries to estimate a claims reserve often involve subjective judgements. Given that there is a range of assumptions that can be reasonably justified, there is also a range of best estimates that can be considered to be reasonable.

Summary of Technical Provisions for MIICL and the Transferring Policies

- 5.4 I provided a narrative of the business written by MIICL in paragraph 2.17. The table below shows a breakdown of the technical provisions, gross and net of reinsurance, in respect of MIICL and the Transferring Policies as at 31 December 2017.

Table 5a: MIICL Technical Provisions - 31 December 2017 - \$Ms

		MIICL Pre- Transfer	Transfer Amount	MIICL Post- Transfer	Transfer % of Total
Head office	Global Insurance	355	53	301	15%
	Specialty & Financial Lines	204	21	183	10%
	Reinsurance	186	0	186	0%
	Marine & Energy	147	12	135	8%
	Other MIICL	206	0	206	0%
	Sweden	12	12	0	100%
Branches	Ireland	108	9	99	8%
	Spain	28	28	0	100%
	Netherlands	37	37	0	100%
	Germany	11	11	0	100%
Gross Total		1,293	183	1,110	14%
GAAP adjustment		141	33	108	23%
Outwards reinsurance		(544)	(73)	(471)	13%
Reserve Margin		139	19	120	14%
Net Technical Provision		1,030	162	868	16%

- 5.5 The first column of the table shows a breakdown of the technical provision amount for MIICL as at 31 December 2017. The first block of figures shows the gross claims reserve for the UK head office business (which represents the majority) and the second block shows the claims reserve for the branch offices. In order to reconcile to the technical provision in the financial statements (in table 4a in paragraph 4.5) I have also shown various other adjustments: (i) The 'GAAP adjustment' is necessary to convert the basis calculated by the actuaries to one which is consistent with UK GAAP; notably, an adjusted treatment of unearned profits and the inclusion of other claim handling costs, (ii) The allowance for the outwards reinsurance asset, and, (iii) The inclusion of the reserve margin. As described below in paragraph 5.33, the MIICL technical provision shown in the GAAP financial statements includes a margin amount, over and above the best estimate amount. The total MIICL net technical provision is \$1,030m.

- 5.6 The second column shows the corresponding amounts transferring to MISE as part of the Transfer. All branch liabilities will transfer (except for a part of the branch office in Ireland), and parts of the Global Insurance, Specialty & Financial Lines, and Marine & Energy. In total on a net of reinsurance GAAP basis, \$162m will transfer to MISE. This represents 16% of the total net technical provision.

MIICL outwards reinsurance

- 5.7 MIICL has a number of outwards reinsurance arrangements in place, including catastrophe event covers, per claim event protection and proportional reinsurance. A large proportion of this outwards reinsurance asset is to be collected from MBL. There is also a substantial amount of reinsurance in place to protect the company in extreme downside scenarios where the level of the gross claims is higher than expected. This program is predominantly placed with third party reinsurers external to the Markel Group.
- 5.8 I have reviewed the outwards reinsurance program in place for MIICL and believe that it is appropriate for the company; this is because I believe that the reinsurance program provides an adequate level of protection in extreme downside scenarios (for example, in scenarios

where there are new large catastrophe events). The reinsurance program is also broadly consistent with other peer group insurers (comparing against other insurance clients of my firm, which are of a similar size to MIICL and which write similar types of business).

Claims reserving approach used by MIICL and MISE

- 5.9 The claims reserving work is carried out by a team of Markel actuarial staff based in the UK. They are responsible for various actuarial activities, including claims reserving and capital modelling for various parts of the business. The Markel Group operates its insurance business as a single global brand, and writes policies in a number of subsidiary companies. The key subsidiaries operating in Europe include MIICL and MISE; the Markel Group also operate a managing agent in the Lloyd's of London insurance market, with business written through Syndicate 3000. The Markel business is organised by 'division', and a client would purchase a policy from one of the available Markel insurance platforms depending on their location and preference. In this way there is some overlap in the business written by MIICL, MISE and Syndicate 3000
- 5.10 The work carried out by the actuarial team includes, but is not limited to, the claims reserving for MIICL and MISE. The claims reserving work is carried out on a quarterly basis. There is a common methodology and integrated IT data systems for various Markel subsidiary companies, so that the claims reserving process for MISE will be carried out in exactly the same way as for MIICL (in the same way that MIICL and Syndicate 3000 currently use common processes). Where there is overlap between the business written by legal entities, and the class is sufficiently similar, then that class would typically be projected as an aggregate amount, and the amounts are then apportioned between the legal entities.
- 5.11 The analysis is carried out on a gross of reinsurance basis by line of business. The first part of the analysis is carried out on 'attritional claims' which excludes any particularly large claim events which might distort the data patterns. The methods used are standard actuarial methodologies including the Chain Ladder Method, the Bornhuetter-Ferguson Method and the Expected Loss Ratio Method (these methods are described at the foot of the Glossary in Appendix A). The assumptions used in the models are based on analysis of the historical data and on actuarial judgement as appropriate. They also separately use industry data to derive industry wide benchmarks, as a cross check against their own analysis, and as an assumption for those cases where Markel has only limited data history.
- 5.12 Actuarial judgement is also applied to select estimates where these methods are not appropriate (for example, where there is a change in the underwriting, claim patterns or legal environment). The actuaries review the results of the various methods, based on both paid claim and incurred claim data, and select the most appropriate estimate based on judgement.
- 5.13 There is a separate analysis of claims reserves for large losses, which is based on a gross of reinsurance basis, using a frequency-severity type methods in conjunction with the standard actuarial methods as appropriate. The actuarial team consults with the Markel claims team as appropriate, in particular for these large loss events.
- 5.14 The net reserves are calculated from the gross reserves by deducting the calculated reinsurance recoveries for known claims and making relevant assumptions about the reinsurance recoveries on potential future claims. For some specific unusual events, the actuarial team has built models to calculate the reinsurance recoveries explicitly.

Changes to the in reserving process after the Transfer

- 5.15 There will be no change to the reserving process itself after the Transfer. The same team of actuaries will be performing the analysis, and there will be no changes to the existing claims reserving process.

My review of MIICL and MISE claims reserves

My approach and materials reviewed

- 5.16 I have held meetings with the Markel actuarial team to understand the claims reserving process. I have also been provided with, and reviewed their own report on the claims reserves as at 31 December 2017. This report complies with the relevant professional actuarial standards, and includes a full description of the reserving methodology, main assumptions used, and main uncertainties. I have also obtained additional claim and premium data on parts of the portfolio on which I could carry out my own analysis.
- 5.17 I have not independently audited the data provided to me. I have, however, carried out reconciliation checks to the reported audited accounts and have carried out various diagnostics on the data. This has led me to believe that the data is appropriate for the purposes of my exercise.
- 5.18 My approach was then to carry out testing on the key parts of the claims reserves. This included a review of the key assumptions in the Markel analysis; I checked those assumptions for consistency with the historical data, and also compared them against my own market benchmarks.

My comments

Markel actuarial team

- 5.19 I believe that the Markel actuarial team has a sufficient level of experience and expertise to carry out the necessary activities. This is because:
- ▶ I have reviewed their organisational chart, comparing this with the knowledge I have of other peer group companies (comparing against other insurance clients of my firm, which are of a similar size to MIICL and which write similar types of business). The level of actuarial resource is at a level that I would expect for firms of a similar size and complexity to MIICL and MISE.
 - ▶ The standard and depth of work that I have reviewed is at a level that I would expect for firms such as MIICL and MISE. My interactions with the actuarial team suggest to me that they have the required level of competence.

Overall methodology and process

- 5.20 The overall methodology is based on standard actuarial methods which I believe are appropriate for these type of liabilities. The type, and range of methods used, is as I would expect for MIICL and MISE.

Categorisation of business

- 5.21 The business is reviewed in approximately 50 lines of business (with some analysis carried out for sub-classes as appropriate). I have reviewed the class of business categorisation for reserving purposes, and am satisfied that this is an appropriate basis. In particular, it provides a sufficient level of granularity by type of business, and has sufficiently homogeneous categories, with sufficient volume of data in each category.
- 5.22 The branch office business has separate lines of business for reserving purposes, and so after the Transfer the reserving process for that business will not change.
- 5.23 For some other Transferring Policies, the business, when transferred to MISE, will be projected in aggregate along with other MIICL and Syndicate 3000 business. The claim reserve for MIICL, MISE and Syndicate 3000 will then be split out in proportion to premiums or claims as appropriate. By projecting the business in aggregate, it is possible to make a more robust projection, with larger volumes of data. This is a valid approach provided that the underlying business has similar characteristics (and as I describe above, I believe that this is the case).

- 5.24 I believe that there are two issues to consider here. The first is the data used for individual claims and premiums for the reserving process for MIICL, MISE and Syndicate 3000. This data is already flagged for legal entity in the case of MIICL and Syndicate 3000, and after the Transfer this will include MISE. I understand that this will involve minimal adjustments to data systems, because the mechanism is already used to split data between other legal entities. I believe that it will provide a sufficiently robust split of premium and claim data by legal entity, and that this will enable a review of the financials for each line of business by legal entity.
- 5.25 Secondly, I believe that the overall approach for allocating claims reserves between legal entities is appropriate, and is in line with the methods that I would expect. I understand that the review process of the claims reserves includes an analysis of loss experience for each claim type (attritional, large and catastrophe) separately by legal entity (for a common line of business) and that any anomalies are investigated and adjustments made if necessary. I have reviewed the loss ratios for different components of the business (transferring and non-transferring) and discuss this below in paragraph 5.29.

Case reserves

- 5.26 I have considered the process used by the Markel claims team to set the level of case reserves for individual claim events. It is important that this process is on a consistent basis from year to year because this data is used in the actuarial methods to make projections for the future claim development. From my discussions with the actuarial team and from reading their report, I am not aware of any material changes to the way that case reserves have been set. From my review of the claim development patterns described below, and from diagnostics of paid and incurred claim data I did not identify any issues.

Review of material assumptions

- 5.27 I have identified and reviewed what I believe to be the key assumptions in the claims reserving analysis. The key areas are the assumptions used for the future claim development and the assumption for the loss ratio on the later underwriting years.
- 5.28 I have reviewed the future claim development pattern for a sample of five classes of business, predominantly those classes with the largest claims reserves and with the most uncertainty (these classes are: Marine Energy, Netherlands Liability, Netherlands Professional Indemnity, Netherlands Professional & Managements Risk and Spain Construction Professional Indemnity). This included transferring business and non-transferring business and made up 45% of the transferring business. I have checked that these assumptions are consistent with the historical claim development data of MIICL. I have also checked these against benchmark claim development patterns from my own wider experience of these type of liabilities (see paragraphs from 3.13 for an explanation of the source of these benchmarks). I have therefore concluded that these assumptions are set on an appropriate basis.
- 5.29 I have reviewed the assumed loss ratio for the latest underwriting year for the most material classes of business, making up 65% of the total claims reserve of MIICL. I have cross checked these assumptions are consistent with the historical loss ratios of MIICL. I have also checked these against benchmark loss ratios from my own wider experience of these types of liabilities (see paragraphs from 3.13 for an explanation of the source of these benchmarks). I have also checked loss ratios for the total MIICL and transferring business components, to check that there are no material differences except in a few cases where a difference is justified by the claims experience. I therefore concluded that these assumptions are set on an appropriate basis.

- 5.30 Given all of the above, I believe that the methodology and assumptions used are reasonable, and that the actuarial best estimate of the claims reserve is set on a reasonable basis. This applies to MIICL as a whole, and to the component in respect of the Transferring Policies.

Current MISE claims reserve

- 5.31 The review I carried out was based on data as at 31 December 2017. At that time, MISE had not written any business, and so necessarily had zero technical provisions. MISE starting

writing business in October 2018, although so far, only from the head office in Germany. The amount of business written by the Transfer Date is likely to be quite small; I will however, review this as part of my Supplementary Report and consider the materiality of those liabilities relative to the transferring liabilities.

Reserve margin and Technical provisions presented in the financial statements

- 5.32 The discussion in the preceding sections considers the best estimate of the claims reserve. This is the estimate that is used, after an appropriate conversion, as the basis for demonstrating regulatory solvency under Solvency II (see section 6).
- 5.33 The technical provision included in the financial statements includes a margin for prudence, which is effectively an additional buffer for uncertainty, added by the management of MIICL. The additional margin added has two components:
 - ▶ The actuarial team carry out a parallel claims reserving exercise which uses more prudent assumptions than the best estimate basis. There is therefore a margin between this basis and the best estimate view.
 - ▶ In the booked technical provision there is an additional margin included, equivalent to 0.06% of the earned premium (i.e., increasing the loss ratio by 0.06%).
- 5.34 The total margin for MIICL, as at 31 December 2017 was \$139m (representing 13% of the net technical provision amount).

Key uncertainties in the claims reserves

- 5.35 As part of my review I have considered the uncertainties in the estimation of the claims reserve and in the range of possible values for the eventual settlement cost of those claims reserve liabilities.
- 5.36 The first way of quantifying these uncertainties is to consider the results of the MIICL capital model (which is described later in this report from section 6). This model estimates the range of possible outcomes for the settlement of the claims reserve, and the likelihood of each of those values. The model considers all of the individual reserving related risks to which MIICL is exposed, and combines these risks (allowing for diversification) to give an overall distribution of the possible outcomes. This model shows that at a 1 in 200 level, the claims reserve would be settled at a value which is 36% higher than the best estimate amount, equivalent to an additional \$260m of claims cost. This overall range of values is what I would expect for a company with the characteristics of MIICL.
- 5.37 A second way to consider the uncertainty is to identify any material specific reserving issues, and consider the range of possible values that could be assigned to those specific items. In particular, I have reviewed the key parameters in the reserving work, and considered alternative reasonable values for those parameters to test how this affects the overall conclusion of the reserving analysis (this type of analysis is 'sensitivity testing'). I set out below the seven areas of specific material uncertainty I have identified and reviewed:

(i) Liability risks

- 5.38 A large proportion of the portfolio is for liability risks. The claims may be settled a long time into the future, and so there is a corresponding higher degree of uncertainty in that settlement cost.
- 5.39 As described above in paragraph 5.28, I have reviewed the claims development pattern assumptions for the largest classes of business (incorporating the largest five classes and 45% of the transferring liabilities). I further tested those assumptions by applying alternative values to the parameters: I increased the claim development pattern by 3% for the 2008 and post underwriting years, effectively applying an additional 3% of future claims to each of those years. This increased the net claims reserve for those classes from \$107m to \$113m (i.e., an increase of \$6m, equivalent to 5.7% of the net of reinsurance claims reserve for

those classes and 0.7% of the overall net claims reserve). This sensitivity test is consistent with the Markel Internal Model assessment of reserve risk and is also consistent with my own expectation of the change in the settlement cost for such a change in the value of the parameter.

(ii) Loss ratio for the most recent underwriting year

- 5.40 There is uncertainty for the most recent underwriting year because the claims are at an early stage of development. MIICL mitigates this risk by managing its exposure to large losses through reinsurance arrangements. MIICL also holds a margin within the claims reserves to provide for additional security.
- 5.41 As described above in paragraph 5.29, I have reviewed the loss ratios for the most recent underwriting year for the most material classes of business (making up 65% of the total claims reserve of MIICL). As a sensitivity test I increased the loss ratio parameter for the 2017 underwriting year by 5%. This increased the net claims reserve for those classes by \$24m (i.e., an increase equivalent to 2.6% of the total claims reserve). This sensitivity test is consistent with the Markel Internal Model assessment of reserve risk and is also consistent with my own expectation of the change in the settlement cost for such a change in the value of the parameter.

(iii) Latent claims

- 5.42 The MIICL claims reserves do not include any explicit allowance for future new latent claim types arising (although there is an implicit allowance in the estimates). A new 'latent' claim type affecting the insurance market could be similar, say, to the unforeseen insurance claims arising from exposure to asbestos. Whilst I believe that this is very unlikely, as much of the portfolio is short-tailed or written on a claims made basis, should a new latent claim issue arise then this could increase the overall claim settlement cost.
- 5.43 The assumption made by MIICL (in their own pricing analysis) suggests that there could be a deterioration, at the 1 in 200 level, of \$70m for such a new latent claim type. Given the volume of liability business written by MIICL, and the size of the claims reserve, I believe that this is a reasonable estimate for a new latent claim type, and that this is consistent with the findings of the MIICL capital model.

(iv) Bodily injury claims and Periodical Payment Orders (MIICL only)

- 5.44 For MIICL only, the UK Motor Treaty business has exposure to large motor bodily injury claims, including settlement through long term Periodical Payment Orders. There are currently projected to be 26 such claims.
- 5.45 I believe that 26 Periodical Payment Order claims is a reasonable number, given the size of the MIICL motor portfolio (this is based on a comparison against five other large underwriters of UK Motor Treaty business that I have reviewed). I have checked that the claim reserving basis used by MIICL is consistent with the current commonly used valuation principles for these types of claims. I also checked the range of reserve estimates specifically for the Motor Treaty class. The MIICL best estimate reserve for Periodical Payment Order is \$26m and the 1 in 200 amount (per the MIICL capital model) is \$59m (i.e., an increase of 126% of the claims reserve). This is broadly consistent with the assumptions by the other UK Motor Treaty insurers in my benchmark sample.

(v) Growing business in South America (MIICL only)

- 5.46 For MIICL only, the South American reinsurance business is relatively new and some classes are still in the process of expansion. This brings additional levels of uncertainty to the estimation of claims reserves. However, the premium written in South America is still relatively small (around \$35m in the last five years) and 70% of the business is property and other short tail lines which have less uncertainty. Recently, the mix has changed with longer tail Surety premium growing from \$5m to \$9m. If the MIICL Surety loss ratio doubled on the

2015 to 2017 underwriting years the impact would be \$15m. Given the above, I am satisfied that the assumptions used in the analysis are set on an appropriate basis.

(vi) MISE portfolio will be smaller than MIICL

- 5.47 MISE is a smaller company than MIICL when measured by the size of the claims reserve; this means that there will be less diversification, other things being equal, for MISE compared to MIICL, and the reserve risk is likely to be greater as a proportion of the claims reserve. However, as I will discuss in section 6, the overall capital in MISE is at an adequate level, and I believe that this compensates for the additional risk.

(vii) General risks

- 5.48 In addition, I believe that they are uncertainties that would be typical for insurance firms such as MIICL and MISE. For any insurance company, the future financial position will depend on the outcome of future unknown events. I do not believe that there is any particular uncertainty which should preclude the Transfer from being effected. I believe that the methods used to quantify the claims reserves are appropriate and these uncertainties do not affect the conclusion I reached on the level of the claims reserve.

Supplementary Report

- 5.49 I will issue a supplementary report prior to the final Court hearing after reviewing the most recent information on claims reserves, including commentary on any significant movements in the claims reserves or changes arising from claims settlements.

6. Assessment of capital requirements

6.1 A key consideration is whether the companies involved in the Transfer are sufficiently secure, and whether that level of security changes as a result of the Transfer. The level of security provided to the policyholders of an insurance company depends on the available assets of the company, and in particular on the probability that this level of assets is sufficient to make all claim payments as they fall due.

6.2 One measure of this security is the level of the regulatory capital requirement, and the extent to which the available capital of the firm is greater than that capital requirement. The European Commission has developed the regulatory requirements for insurance and reinsurance undertakings within the EU (known as 'Solvency II'). Both MIICL and MISE are currently subject to the regulatory requirements of Solvency II.

6.3 In this section I will:

- ▶ Set out some background on Solvency II.
- ▶ Explain the regulatory capital position for MIICL and MISE.
- ▶ Explain the review I have undertaken on the capital amounts.
- ▶ Explain the impact of the Bermuda QS on the capital position, and my review of MBL.
- ▶ Explain my overall conclusion on the capital strength of MIICL and MISE.

Background to Solvency II

6.4 The key metric to trigger regulatory intervention under Solvency II is the Solvency Capital Requirement ('SCR'). This is determined as the economic capital to be held by an insurance firm in order to ensure that the probability of not meeting their obligations in the coming year is less than 1 in 200. It is intended to represent a normal target level of capital for the insurer, and capital falling below this level would trigger a response from the insurer's regulator. This '1 in 200' level would represent a relatively remote event, and an insurer with that level of capital can be considered to have a very good level of security.

6.5 Insurers can choose one of three methods on which to base their SCR calculations; a Standard Formula approach, an Internal Model approach or a Partial Internal Model approach:

- ▶ The Standard Formula approach entails a prescribed basis for calculation and a prescribed set of parameters to use in working out the capital requirement.
- ▶ The Internal Model approach involves the insurer using their own capital model to calculate their regulatory capital requirement. Both the approach to calculating available capital (via the Solvency II balance sheet) and the approach to calculating the capital required are different to the Standard Formula approach.
- ▶ The Partial Internal Model approach is a mixture of the Standard Formula approach and the Internal Model approach. An Internal Model is used to calculate parts of the regulatory capital, and the Standard Formula to calculate the remainder.

6.6 The choice of which of these three approaches to use is made by the insurer themselves; however, the form and structure of Internal Models and Partial Internal Models are subject to approval by the relevant regulator (generally the regulator in the home country of the insurer). In cases where the regulator does not approve an Internal Model or Partial Internal Model, the Standard Formula will be applied by default.

- 6.7 In my discussion of the capital requirements I will refer to the individual components of the risks; namely:
- ▶ Insurance Risk: The risks relating to the upcoming year of insurance business and the uncertainties relating to the claims reserves (i.e., the uncertainty that the cost of settling these liabilities could be higher or lower than the booked reserve amount). The firm will need to pay some insurance claims to their policyholders over the coming years, but the amount of those payments and the timing of those payments is uncertain. There is a risk that the amount to be paid is more than expected.
 - ▶ Market Risk: This describes the risk of loss or of adverse change in the financial situation resulting, directly or indirectly, from fluctuations in the level and in the volatility of market prices of assets, liabilities and financial instruments. This includes the uncertainties relating to investments performance (the investment return achieved and the value of the assets held by the firm could go up or down, and the amount by which they go up or down is uncertain). This risk type is further subdivided into interest rate risk, equity risk, property risk, currency risk and concentration risk.
 - ▶ Counterparty Default Risk: The risk of any defaults of counterparties or reinsurers. This includes any institution or individual that is a debtor to firm, and in particular, the reinsurers of the firm.
 - ▶ Operational Risk: This includes uncertainties relating to failures in operational procedures. For example, IT systems failure or fraud.
- 6.8 The basis for calculating the value of the available capital is slightly different between Solvency II and UK GAAP. I will refer to the amount of available capital on a Solvency II basis as 'Solvency II Own Funds'. The amount of available capital as shown on the balance sheets in paragraph 4.5 and 4.13 is really the same concept as Solvency II Own Funds, but calculated using a different set of rules.
- 6.9 It is important to note that even if an insurer does not have sufficient eligible Solvency II Own Funds to meet the required capital level then this does not necessarily mean that it would not be able to settle all its claims in full. In those circumstances the balance sheet strength of the insurer would be sufficient to pay its liabilities, even though the regulatory capital amount would not be met.
- 6.10 The insurer is also required to submit an Own Risk and Solvency Assessment ('ORSA') to the regulator, which sets out their own views on the risk of the firm and the appropriateness of the SCR calculation.

Summary of regulatory capital requirements of MIICL and MISE

- 6.11 The table below shows a summary of the regulatory capital requirements at 31 December 2017, as if the Transfer was effected on that day. The first column shows the MIICL IM SCR. The next three columns show the MIICL SF SCR, both before and after the Transfer (with the difference also shown). The last column shows the corresponding MISE SF SCR after the Transfer. I will discuss these calculations in further detail in the following paragraphs.

Table 6a: MIICL Solvency II capital requirements – 31 December 2017 - \$Ms

	Internal Model	Standard Formula			
	MIICL pre-Transfer [A]	MIICL pre-Transfer [B]	MIICL post-Transfer [C]	Change [D]	MISE post-Transfer [E]
[1] Insurance Risk	265	303	281	(22)	5
[2] Counterparty Default Risk	106	28	26	(2)	8
[3] Operational Risk	42	31	25	(5)	4
[4] Market Risk	212	166	158	(8)	2
[5] Diversification	(310)	(129)	(122)	7	(3)
[6] Pension Risk charge	32	32	32	0	0
[7] One year adjustment	(18)	0	0	0	
[8] SCR	329	431	401	(31)	16
[9] Solvency II Own Funds	642	642	599	(43)	50
[10] Capital Adequacy Ratio	195%	149%	150%	1%	319%

- 6.12 The first four rows in the table shows the part of the total capital requirement relating to each of the components of risk for Insurance, Counterparty, Operational and Market. So for example, we can see that Insurance Risk is the largest component of risk for MIICL pre-Transfer, with a contribution of \$265m to the total. Row [5] is the effect of the diversification between those risks. Not all adverse events are likely to happen all at once, and so there is an effect of pooling the risk together so that the total capital requirement is less than the sum of the parts (the diversification amount is shown as a negative). Row [6] is one further amount included, which is the Pension Risk for MIICL, which is added on as an additional loading for the risk emerging from the pension fund. Row [8] is a further adjustment needed for the Internal Model to make the basis of the calculation equivalent to the Solvency II requirement of a one year time horizon. The totals of lines [1] to [7] makes up the SCR. Comparing this with the Own Funds amount in line [9] gives a comparison of the amount by which the firm meets the regulatory capital requirement, shown a percentage in Row [10].

MIICL regulatory capital assessment

- 6.13 MIICL is regulated by the PRA in the UK and falls under the Solvency II capital regime. MIICL has elected to use an Internal Model basis for the purpose of the Solvency II capital requirement. The MIICL SCR is calculated using an Internal Model. This model has been approved by the PRA. Prior to the Transfer, MIICL meets that capital requirement by a large margin, with a 195% coverage ratio. At the moment, there is not an available calculation of the IM SCR for MIICL after the Transfer.
- 6.14 MIICL also calculates the SF SCR. The pre-Transfer SF SCR for MIICL is higher than the IM SCR. This is because the Internal Model estimate captures some additional features of the business which is not allowed for in the Standard Formula calculation. In particular, the assumptions for variability in the Internal Model are based on data which is specific to MIICL, rather than industry average parameters.

- 6.15 After the Transfer, the SF SCR for MIICL would reduce slightly, and there would also be a small reduction in Own Funds. This is as I would expect, because there is only a small, 15% reduction in technical provisions, and a corresponding small reduction in the value of the assets. The overall coverage ratio on the SF SCR basis increases by a very small amount from 149% to 150%. On this basis, the capital strength is practically the same.
- 6.16 At the time of writing this report, MIICL have not yet re-performed the IM SCR calculation on the post-Transfer basis. They are currently working out a timetable to do this, and I expect that this will be available for me to review as part of my Supplementary Report. I do not believe that it is of value here to carry out proxy calculations for this IM SCR post Transfer. However, I can say with some certainty the IM SCR amount would reduce following the Transfer, given that 15% of the reserve amount is effectively removed from the balance sheet with only a small drop in the value of the assets. So by assuming a constant IM SCR of \$329m (the pre Transfer IM SCR) and the reduced Own funds of \$599m, we will have a lower bound for the coverage ratio. This gives a coverage ratio of 182%, which is still a very high ratio, and shows that MIICL would continue to meet that capital requirement after the Transfer.
- 6.17 I will describe my review of the calculation of the SF SCR and the IM SCR in paragraph 6.27.

MISE regulatory capital assessment

- 6.18 MISE is regulated by BaFin in Germany and falls under the Solvency II regime. The MISE SCR will be calculated using the Standard Formula approach rather than an Internal Model (at least in the foreseeable future). Approval to use the Standard Formula has been granted by BaFin.
- 6.19 There will only be a relatively small number of policyholders in MISE at the time of the Transfer. Despite this, MISE was set up with a very large amount of 'seed capital' (in particular, this large starting capital was needed to obtain certain US regulatory permissions which will be used at a later date). For these reasons I do not believe it is instructive to review the starting capital assessment of MISE, except to say that MISE would meet that capital requirement by a very large margin. This is because, just before the Transfer Date, MISE is likely to hold a very large amount of capital (approximately \$48m) and only have a small technical provision amount (this will probably not be more than \$40m on a gross of reinsurance basis, and \$4m on a net of reinsurance basis).
- 6.20 After the Transfer the MISE SF SCR is estimated to be \$16m. The corresponding Solvency II Own Funds amount is \$50m, which gives a Capital Adequacy Ratio of 319%.
- 6.21 I believe that the Standard Formula approach is an appropriate basis for calculating the regulatory capital requirement for MISE. The Standard Formula approach for MISE has been agreed by BaFin (indeed, I understand that there are only five firms in Germany with approved internal models, and those firms are all much larger than MISE). The fact that MISE uses the Standard Formula rather than an Internal Model does not affect my conclusion on the Transfer. I reached this conclusion because the Standard Formula basis covers all of the material risks of MISE, including Insurance, Counterparty Default, Market, and Operational Risks. I have also considered the complexity of the risks inherent in MISE and whether the Standard Formula basis will capture those risks in an appropriate way. For each of Insurance, Counterparty Default, Market, and Operational Risks I consider that there is nothing unusual in the risk profile of MISE that would invalidate the Standard Formula approach. So, for example:
- ▶ Insurance Risk: There are no lines of business written by MISE which I would expect to have a materially higher level of risk compared to the market average.
 - ▶ Market Risk: MISE does not hold any unusual types of investments (e.g., derivative instruments) that would give higher levels of risk than estimated by the Standard Formula.

- ▶ Counterparty Default Risk: MISE does not have any material counterparty default risk issues that would invalidate the Standard Formula approach.
- ▶ Operation Risk: I do not believe that there are any particular operational risks for MISE that would mean that MISE would have a higher than average level of operational risk.

6.22 The split of risk types for MISE after Transfer is as I would expect, with a large contribution from insurance risk. MISE has proportionately less market risk than MIICL because MISE does not, at present, invest in equity type investments. MISE also has a larger contribution from counterparty default risk due to the materiality of the Bermuda QS. There is no pension risk in MISE.

UK third country branch office

6.23 There may be certain prudential capital requirements placed on the UK branch office of MISE. For example, a requirement to hold an amount of capital specifically in the UK. The details of any such requirement are not yet formalised by the PRA. However, MISE meets the SF SCR requirement by a very large margin and I believe would be able to meet any requirement to hold specific capital in the UK. Indeed, MISE could hold an amount of capital equal to the SF SCR in both the UK and in Germany. For this reason, the possibility of further UK prudential capital requirements for MISE does not affect my conclusion on the Transfer.

Comparison of regulatory capital requirements

6.24 The table below shows an overall comparison of the Capital Adequacy Ratios and Solvency II Own Funds of MIICL and MISE.

Table 6b: Capital Adequacy Ratios for MIICL and MISE

	Solvency II Own Funds	Coverage Ratios	
		Standard Formula	Internal Model
MIICL pre-Transfer	642	149%	195%
MIICL post-Transfer	599	150%	Not available
MISE post-Transfer	50	319%	Not applicable

6.25 Based on these Solvency II capital requirements the Non-Transferring Policyholders will have a similar level of Capital Adequacy Ratio after the Transfer (with a slight increase from 149% to 150% on a Standard Formula basis. The portfolio transferring is a relatively small proportion of the total, so I would not expect any significant change to the risk profile. MIICL is relatively large insurance firm, and will remain so even after transferring the Transferring Policies.

The Transferring Policyholders would be moving to a firm with a higher SF SCR coverage ratio. The Transferring Policies would be moving from a firm regulated on the basis of an internal model SCR to one regulated using a standard formula SCR. However, the principles underpinning those two bases are the same, so I would not expect there to be any material disadvantage to policyholders in respect of this change.

6.26 The policyholders of MISE after the Transfer will have a high Capital Adequacy Ratio after the Transfer (319%). This is higher than the Capital Adequacy Ratio of MIICL.

My review of Standard Formula calculations for MIICL and MISE

6.27 Markel provided me with the data and key inputs used in their SF SCR calculation for MIICL and MISE. I have performed my own independent calculation of the SF SCR of MIICL and MISE for the most material areas of risk (I consider these to be premium and reserve risk, interest rate risk, equity risk, lapse risk and currency risk for MIICL; and, premium and

reserve risk, interest rate risk, currency risk and counterparty default risk for MISE). The results of my calculations are consistent with the Markel analysis. In addition, I have reviewed the approach and any other assumptions made for each element of the calculations of the SF SCRs for MIICL and MISE, and consider these to be reasonable and proportionate to the scale and complexity of their operations. Therefore, I am satisfied that the SF SCRs produced for MIICL and MISE are appropriate.

- 6.28 I have reviewed documentation on the production of the MIICL and MISE SF SCR and am satisfied that the methodology used is appropriate. I have also reviewed the calculations underlying the production of the MIICL and MISE Solvency II Own Funds amount, and am satisfied that this calculation has been performed appropriately.

My review of Internal Model calculations for MIICL

- 6.29 In order to test the appropriateness of the MIICL Internal Model for calculating the MIICL IM SCR I have carried out the following procedures:
- ▶ I have received and reviewed the documentation of the Internal Model and received and reviewed the most recent set of model results. The documentation was sufficient for me to get an understanding of the methodology and key assumptions of the model.
 - ▶ I have received and reviewed the most recent validation report for the Internal Model. This sets out and documents the company's own testing and validation of the model, which is a requirement for ongoing use of the model. This also sets out the key assumptions and expert judgements in the modelling work. As part of the validation procedures MIICL carries out more than 130 standard annual tests covering all individual components of the model. A range of validation tools have been used for these tests (including analysis of change, sensitivity testing, stress and scenario testing and reverse stress tests). The range of testing carried out is as I would expect.
 - ▶ I have carried out my own benchmarking exercise of the Internal Model results. This involves comparing key metrics (e.g., ratios of capital to premium and technical provisions) against peer group companies and to the equivalent Standard Formula measures (comparing against other insurance clients of my firm, which are of a similar size to MIICL and which write similar types of business). The MIICL IM SCR was within the benchmark range of the peer group companies, but in the upper quartile in terms of required capital relative to premium and reserves. This is as I would expect, given that MIICL writes proportionately more liability business and has a larger amount of assets held as equities, with a corresponding higher insurance risk and market risk.
- 6.30 Based on my review I am satisfied that the methodology and assumptions used are appropriate. I note that this model has been approved by the PRA for the purposes of using the model as the basis to assess regulatory capital.
- 6.31 In my opinion, the validation work performed by MIICL is appropriate. It has focused on the most material areas of the Internal Model and provided comprehensive coverage for individual component of the risks.

Approach adopted by MIICL to model each component of the risks

- 6.32 I have summarised below the approach adopted by MIICL to model the various components of the risks, as described in paragraph 6.7.

Insurance risk

- 6.33 For the risks relating to the settlement of claims reserves, the gross settlement amounts are generated by class of business and then reinsurance is applied (either as ratio adjustments on older years or by using the explicit reinsurance program for the latest year's business).

Attritional and large losses are modelled separately using the aggregated volatility and frequency severity modelling approaches respectively. Natural catastrophes are modelled separately using either an external catastrophe model or an event loss table for areas that are not covered by the external catastrophe model.

- 6.34 The reinsurance component models the reinsurance contracts across the latest prior year and future years, along with the reinstatement premium calculations. Third-party contracts and inter-group contracts are modelled separately.

Market risk

- 6.35 This relates to the risk of loss or adverse changes in MIICL's financial position caused by economic volatilities. This component is estimated using third-party simulation models purchased from third parties. These models provide economic scenarios for equity returns, exchange rates, and interest rates by bond type.

Counterparty Default Risk

- 6.36 This models the financial impact of MIICL's reinsurers being unable to meet their obligations (e.g., due to insolvency). It uses a transition matrix to simulate the evolution of the credit ratings (and hence the possibility of default) of reinsurers over the future reserving run-off period. The module also models the risk of default by brokers and cover holders.

Operational Risk

- 6.37 An operational risk charge is based on a series of possible adverse events, with severity and frequency assumptions applied. These are selected and parameterised by MIICL's risk management team.

Pension risk charge

- 6.38 An amount is added for the risk arising from the MIICL pension fund, based on the estimates provided by the pension specialists valuing that fund. I have not reviewed those calculations, but the amount of the pension fund liabilities is relatively small in the context of MIICL as a whole, and this amount of risk would not change after the Transfer.

Diversification

- 6.39 The model allows for diversification between risk categories, and lines of business with risk categories using standard statistical techniques.

Rating Agency assessment

- 6.40 Another estimate of financial strength of an insurer can be obtained from ratings provided by credit rating agencies. Standard & Poor ('S&P') and A.M. Best provide a credit rating for the Market Group as a whole, and for each of MIICL and MISE individually. The rating provided to each entity is 'A' which signifies "Strong" and "Excellent", respectively on S&P and A.M. Best scales. This suggests that both MIICL and MISE are both strongly capitalised.

Impact of the Bermuda QS on security

- 6.41 Concurrently with the Transfer the Bermuda QS will be effected, which will cede 90% of all insurance risk (which includes all past and new business) to MBL. This changes the characteristics of the security provided to the policyholders compared to the situation in MIICL, because a greater proportion of the assets held by MISE will be in the form of a single reinsurance asset. This means that MISE would pay the claims initially, and then would be reimbursed for 90% of the amount by MBL. Therefore, the ability of MISE to make claim payments is closely linked to the financial strength of MBL. There would clearly be an additional counterparty default risk, depending on the financial strength of MBL. Given the materiality of the Bermuda QS I have carried out analysis on the financial strength of MBL, including a review of the business written, regulatory capital requirements and technical provisions.

MBL - Background and business written

- 6.42 MBL is a very large Bermudian reinsurer with available capital of \$1.7bn and gross written premium for 2017 of \$1.3bn. MBL writes a wide range of reinsurance of both property and liability exposures on a global basis, with a large weighting towards catastrophe exposed reinsurance in North America. It also writes high excess insurance of general casualty business. There is also run-off exposure of a large book of annuity and whole life business from Ireland and the US.

Capital requirements

- 6.43 MBL has a capital requirement, for the 2017 year, in Bermuda of \$959m and an available capital on this basis of \$2,051. This gives a coverage ratio of 214%. I have consulted with the insurance team of my firm based in Bermuda, with experience of that local market, and I understand that this a high coverage ratio relative to the peer group of MBL.
- 6.44 Underwriting is the largest risk, with a 40% contribution to the overall capital, with catastrophe risk making up 30% of that amount. This is what I would expect given the large amount of catastrophe exposure business written. The Markel Group has a consistent approach, across all group companies, for capital modelling and catastrophe aggregate monitoring. I have received and reviewed the output of the catastrophe scenario modelling. This shows that the 1 in 250 year catastrophe loss amount is \$395m. This compares to the available capital (on an equivalent basis) of \$1,946m; this shows that MBL is well capitalised, and would remain solvent after a rare catastrophe event of that size.
- 6.45 Market risk is also one of the largest risks, with a 35% contribution to the capital. This is not surprising given the large amount of assets held in respect of the life insurance business. This does, however, also provide good diversification away from the underwriting risk.
- 6.46 Reserve risk is relatively small, other things being equal, with a contribution of 20% to the overall capital. A large proportion of the business is relatively short tail, with less uncertainty. Some high excess business and casualty reinsurance does, however, have greater reserve risk.
- 6.47 Standard & Poor ('S&P') and A.M. Best provide a credit rating for MBL of 'A' which signifies "Strong" and "Excellent", respectively on S&P and A.M. Best scales. This suggests that MBL is strongly capitalised

Technical provisions

- 6.48 I received and reviewed a copy of the report on claims reserves from the external actuaries of MBL. That report supported the technical provisions shown in the financial statements of MBL as at 31 December 2017. That analysis used methodologies that I consider to be appropriate for the types of business written by MBL. The report complied with the professional standards I would expect. Therefore, I have no reason to suppose that the technical provision amount is unreasonable.

Overall conclusion on MBL security

- 6.49 Given all of the above I am satisfied that MBL has a strong balance sheet and provides a high level of security. My conclusion from this analysis, is that MBL provides a high level of security to MISE, and as a consequence, a high level of security to the policyholders of MISE.

Overall conclusion on capital strength

- 6.50 I believe that MIICL and MISE will both have a strong balance sheet after the Transfer, and that the probability of either firm becoming insolvent or otherwise unable to pay policyholders' claims is remote. I reached this conclusion because:
- ▶ Both MIICL and MISE meet the regulatory capital requirements by a large margin, both before and after the Transfer. The regulatory capital is calibrated at a 1 in 200 level of sufficiency over a one year period. The fact that MIICL and MISE meet that

requirement by a large margin suggests that there is a very high probability that the policyholders would have claim payments made as they fall due.

- ▶ The credit ratings provided by the rating agencies also suggest that MIICL and MISE are strongly capitalised.

- 6.51 As a new company MISE has an unusually high level of capitalisation, simply because the company has only just begun trading, and does not yet have many policyholders.
- 6.52 At the time of writing this report I am not aware of any dividend amounts to be paid by MIICL or MISE in the period up to and immediately after the Transfer Date. If there are any dividends agreed then I will review this as part of my Supplementary Report, and will consider the dividend in the context of the updated balance sheets as at 30 September 2018 for MIICL and MISE.

7. Assessment of other issues

7.1 In this section I will set out the issues relevant to each group of policyholder. I will first describe some issues that are common to various combinations of policyholders.

Impact of Brexit

7.2 Brexit has introduced or exacerbated a number of risks for UK insurers conducting business across the EU. In particular, there is also a potential risk that after Brexit, UK insurers lose the ability to conduct such business through the loss of passporting rights (which remove the need to be authorised by local European regulators). Some potential areas of concern are market volatility with a particular emphasis on exchange rate volatility, a higher risk of negative interest rates in the future, and the impact of a changing regulatory environment.

7.3 This is currently a significant amount of interaction between MIICL and the other Markel offices and clients located in the EEA, with different services moving across the border between the UK and the EEA. I set out below some of the main areas that I have identified; this is not an exhaustive list, but does cover, I believe, the most important areas of activity:

- (i) MIICL providing services to policyholders, where those policyholders are located in the EEA or have a part or all of their risk located in the EEA. These activities include, for example, paying claims, receiving and paying premium, dealing with customer queries and complaints, policy amendments and lapses, and liaising with insurance brokers. This also includes advertising and selling new policies.
- (ii) Markel personnel and other resources in the UK providing services to other branch offices and Markel sister companies in Europe (for example, providing underwriting, finance, actuarial and claims handling expertise). This also applies vice-versa from the EU to the UK.
- (iii) Data sharing (for example, of customer data) between MIICL and other Markel offices based in the EU.
- (iv) Markel staff working and moving between office locations.

7.4 Most of those activities are regulated to some extent; the question is, to what extent those activities will still be permitted after Brexit. It is not currently clear what the outcome of the Brexit negotiations will be. However, it appears likely that passporting will not continue in its current form and so MIICL is unlikely to be able to conduct regulated activities in the EEA post-Brexit. There may be a deal reached between the EU and the UK in respect of existing contracts (known as 'contract continuity'). However, the EU and the European Insurance and Occupational Pensions Authority's public positions to date have been that existing EEA business should plan on the basis that existing business cannot be serviced from the UK post-Brexit.

7.5 In the absence of a wider deal, it may be unlawful for MIICL to provide services to Transferring Policyholders. The ability of MIICL to provide services (including payment of claims or policy amendments etc.) in respect of the Transferring Policies is of vital importance to such policyholders. MIICL being unable to provide these services to policyholders would clearly be detrimental to those policyholders. By effecting the Transfer, I believe that the Markel Group will achieve some certainty in this area because these activities will be performed by a legal entity domiciled in the EU (i.e., MISE). MISE would be legally able to provide those services to policyholders regardless of the outcome of the future relationship between the EU and the UK.

7.6 Many of the risks associated with Brexit are either unavoidable for insurance firms, or could only be avoided with an unreasonable amount of time and resources, given the current state of knowledge. For example, post-Brexit, depending on the nature of the deal reached with the EU, there is a risk that employees of Markel from EU member states would not be permitted

to work in the UK. Given the current state of knowledge of the arrangements post Brexit, I think it would be unreasonable to expect MIICL to immediately begin contingency planning for this eventuality. Furthermore, this is risk to MIICL regardless of whether the Transfer is effected. Dependent on the nature of the deal, there are other activities that might not be permitted and it is possible that this could cause disruption to the Markel Group and have some negative effect on policyholders. For example, there might be additional restrictions on sharing policyholder data between offices in the UK and offices in the EU. However, the problem will arise regardless of whether the Transfer is effected; indeed, the problem of data sharing will actually be much worse in a scenario without the Transfer. For these reasons I believe that no policyholder will be made materially worse off due to the effect of these other Brexit related risks.

- 7.7 I have considered the overall approach taken by MIICL in respect of Brexit. The primary course of action has been to effect the Transfer, which as I described above, will ensure continuity of service for those risks located in the EEA. I do not believe that it is reasonable at this stage to expect that MIICL has effected other detailed plans to remedy other Brexit risks. I expect that MIICL would be able to address some of those risks should they arise. I believe that this is consistent with the approach taken by other peer group companies of MIICL with operations across the EEA, and this does not affect my conclusion on the Transfer.
- 7.8 There are some Transferring Policies which include risks located in both the EEA30 and the UK. MISE will have a branch office in the UK from which MISE will be able to provide the necessary policy and claim settlement services to policyholders. As I discussed in paragraph 7.6, there might be other Brexit related risks which cannot be avoided; however, I do not believe that these policyholders are made any worse off with respect to these risks after the Transfer.
- 7.9 There are some policies of the MIICL branch office in Ireland which will not Transfer to MISE, but will instead remain with MIICL. Those policies will, in due course, be reallocated to the UK head office of MIICL where they will be administered until all claims are settled. I believe that these policies are not materially affected by any Brexit issues because all of the risks associated with the policies are located outside of the EEA30.
- 7.10 I discussed the issues relevant to the UK third country branch application in paragraph 6.23 and this does not affect my conclusion on the Transfer.
- 7.11 At this stage of the consultation, I am not aware of anything to suggest that MISE would not be able to establish this branch office in the UK. I will comment further on this issue in my Supplementary Report.
- 7.12 Given all the above arguments, I believe that the most pragmatic solution to the Brexit related issues is to effect the Transfer. There are some Brexit risks which cannot be avoided in any practical way. However, I believe that the most material risks, relating to how services can be provided to EEA policies, can be mitigated by transferring those policies or parts of policies to MISE.

The Financial Services Compensation Scheme

Background to the FSCS

- 7.13 Consumer protection is provided by the Financial Services Compensation Scheme ('FSCS') in the UK. This is a statutory 'fund of last resort' which compensates customers in the event of the insolvency of a financial services firm. Insurance protection exists for private policyholders and small businesses (with annual turnover of less than £1 million) in the situation where an insurer is unable to meet its liabilities. The FSCS will pay 100% of any claim incurred for compulsory insurance (e.g., motor third party liability insurance or professional indemnity insurance) and 90% of the claim incurred for non-compulsory insurance (e.g., home insurance), without any limit on the amount payable. The FSCS is funded by levies on firms authorised by the PRA. No protection is available for Goods in Transit, Marine, Aviation and Credit Insurance. Contracts of reinsurance are also not

protected. The FSCS covers risks located in the UK and EEA for insurance companies authorised in the UK.

The effect of a transfer on FSCS protection

- 7.14 The PRA has recently issued a consultation paper (*Consultation Paper CP26/18: UK withdrawal from the EU: Changes to PRA Rulebook and onshored Binding Technical Standards*) setting out a proposed approach for its rules following Brexit, including those relating to the FSCS.
- 7.15 This paper proposes that equivalent FSCS protection will be provided to transferring policyholders who transfer from a UK insurer to a “successor firm” (i.e., an insurance firm covering the policyholders following a transfer) if certain conditions are met. The same FSCS protection for eligible policyholders will be provided if the successor firm is a “relevant person”. A “relevant person” may be loosely summarised in this context as an insurer with UK authorisation. Even if the successor firm is not a relevant person, the paper proposes that the transferring policyholders would retain some FSCS rights: specifically, claims arising from insured events which occur prior to the date of the transfer would be covered by the FSCS, but not claims arising from insured events occurring after the date of the transfer. In summary, the following cases would be covered by the FSCS after a transfer:
- (i) If a policy is eligible for FSCS protection before the transfer, and the policy transfers to a successor firm which is a relevant person, then a claim on the policy would be eligible for FSCS protection after the transfer.
 - (ii) If a policy is eligible for FSCS protection before the transfer, and the policy transfers to a successor firm which is not a relevant person, then a claim on the policy is eligible for FSCS protection after the transfer only if the insured event which gave rise to the claim occurred before the date of the transfer.

Transferring Policies affected

- 7.16 I will describe in this section my understanding of how the FSCS protection regulations would apply to different groups of Transferring Policies. In order to assess any relevant changes to FSCS rights I have considered the FSCS rights currently available to the Transferring Policies; I have then considered, for each group of Transferring Policies, how those FSCS rights would change after the Transfer, based on my understanding of the relevant regulations.
- 7.17 Some, but not all, Transferring Policies currently benefit from the protection of the FSCS. Markel has carried out a survey, and approximately 20% of Transferring Policies, by number, appear to benefit from the FSCS (the remainder of the policies are either for policyholders who are not considered to be eligible, or lines of business which are not, under the regulations, eligible).
- 7.18 For those Transferring Policies with current FSCS protection, the situation after the Transfer depends on the branch office of MISE to which the policy transfers.

Transferring Policies which transfer to the UK branch office of MISE

- 7.19 As described in paragraph 2.21, MISE will apply to the PRA to convert its current EEA passporting branch in the UK into a third country branch in the UK; after this process MISE would be authorised in the UK under the FSMA. Any new policies written by MISE, after this conversion, would be covered by the FSCS. Given that MISE would be authorised in the UK I believe that MISE will have the status of a ‘relevant person’ in respect of the policies of its UK branch office. Therefore, the Transferring Policies which transfer to the UK branch office of MISE will fall under category (i), as set out above in paragraph 7.15. If a policy is eligible for FSCS protection before the Transfer, then a claim on the policy would be eligible for FSCS protection after the Transfer.

Transferring Policies which transfer to the head office of MISE (in Germany) or a branch office of MISE in the Netherlands, Ireland or Spain

7.20 I believe that there is some uncertainty about whether MISE will be classed as a relevant person for the purpose of its policies administered in the head office in Germany or branch offices in the Netherlands, Ireland and Spain. There is an argument that MISE will be classified as a relevant person, as a consequence of MISE having a UK branch office authorised in the UK. On the other hand, after the Transfer those other branch offices will in some sense 'lose' the connection to the UK because the underlying risks are located outside the UK, and the policies are also administered outside of the UK. The only connection to the UK would be that MISE incidentally has a UK branch office and that the policies were originally written by a UK firm. Given this uncertainty in the application of the new regulations, I believe that there is some risk that MISE would not be treated as a relevant person with respect to these policies. If MISE is not treated as a relevant person in these circumstances then the Transferring Policies which transfer to these branch offices will fall under category (ii), as set out above in paragraph 7.15. If a policy is eligible for FSCS protection before the Transfer, then a claim on the policy is eligible for FSCS protection after the Transfer only if the insured event which gave rise to the claim occurred before the Transfer Date.

Other compensation schemes available

7.21 My understanding is that the Transferring Policyholders might have other compensation schemes available, depending on their location, but that these are not likely to offer equivalent protection to the UK FSCS:

- ▶ There is no equivalent corresponding scheme applied in Germany. The compensation scheme in Germany is supervised by BaFin, and covers life insurance and substitutive health insurance only (being insurance which is in whole or part a substitute for statutory health insurance), which does not form part of the Transfer.
- ▶ In the Netherlands, there is no compensation scheme available to cover non-life insurance policies.
- ▶ In Spain, the compensation scheme only applies to Spanish insurers and hence will not be applicable to MISE policyholders.
- ▶ In Ireland, there is a scheme operated by the Insurance Compensation Fund (ICF) as a fund of last resort. The ICF only applies to risks situated in Ireland. Any payments from the ICF are subject to approval from the court, and not all policyholder liabilities are covered by the ICF, with exclusions including health, dental, and life policies. Payments made by the ICF are limited to the lesser of 65% of the sum due to the policyholder and €825,000, and so are lower than potential payments from the FSCS. Commercial policyholders are not covered by the ICF unless the claim is in respect of a liability to an individual. Although the scheme might be available, I believe that it is unlikely that many of the Transferring Policies would be eligible; this is because the business written through the branch office in Ireland is mostly for international business and therefore does not contain many Irish-situated risks (i.e., the Irish branch business is very different to the branches in Germany, the Netherlands and Spain, which are more focused on their local markets). Moreover, approximately 85% of the Transferring Policies as a whole is commercial business. The effect of these circumstances is that it is unlikely that there will be many Transferring Policies that could benefit from ICF protection.

Conclusion for Transferring Policyholders

7.22 I believe that there is a risk that some Transferring Policyholders could lose some of their right to claim FSCS compensation following the Transfer. Specifically, this applies to the Transferring Policies which transfer to the head office of MISE or a branch office of MISE other than the UK. These policies might not be eligible for FSCS protection for claims arising

after the Transfer Date, although this depends on the exact implementation of the new regulations for the FSCS. The loss of this part of the FSCS protection is effectively a 'worst case' scenario; the 'best case' scenario is that MISE is indeed treated as a relevant person and the full FSCS protection would be preserved after the Transfer for these policies.

7.23 As described above, there are no alternative schemes available that would provide equivalent protection. However, I am satisfied that those Transferring Policyholders who are currently eligible are not materially disadvantaged for the following two reasons:

- ▶ The right to compensation arises only when an insurance company becomes insolvent. I describe in paragraph 6.50 the reasons why I consider that this is a remote possibility. Therefore, I believe that the scenario of needing to claim compensation under the FSCS or any other statutory compensation scheme is also remote.
- ▶ The Transfer is taking place in response to Brexit. There are other Brexit risks which potentially have a greater impact than the loss of FSCS rights. However, without the Transfer those same policyholders would still be MIICL policyholders, and would have the corresponding Brexit risks as set out in paragraph 7.2. Of course, it is not possible to say with any certainty which of the many Brexit risks will materialise and which will turn out to be benign. But this does show that Brexit gives rise to advantages and disadvantages to both the Transfer and the status quo position; i.e., there are Brexit risks to various policyholders regardless of whether the Transfer is effected.

7.24 I have therefore concluded that these policyholders are not materially adversely affected by the Transfer in relation to the FSCS arrangements.

Direct and reinsurance policyholders

7.25 A 'direct policyholder' is a corporate firm or an individual person who is insured by an insurance company. A 'reinsurance policyholder' is an insurance company which reinsures a part of their risks to a reinsurer.

7.26 A changing mix of direct and reinsurance policyholders might have an impact on an insurance business transfer scheme because the ranking of creditors in the event of an insolvency is different for direct and reinsurance policyholders. In particular, direct policyholders would usually rank ahead of reinsurance policyholders. However, I believe that this is not an issue for the Transfer because:

- ▶ None of the Transferring Policyholders or Transferee Policyholders are reinsurance policyholders. As part of MISE, they would therefore all rank equally (with respect to this Direct/Reinsurance split) in the event of an insolvency of MISE.
- ▶ There are some reinsurance policyholders in MIICL, but because the volume of business transferring from MIICL is relatively small, there will not be any significant change to the split between direct and reinsurance policyholders.
- ▶ As discussed in paragraph 6.50, I consider it a remote possibility that MISE becomes insolvent.

7.27 For the above reasons, my conclusion on the Transfer is not affected by the split of direct and reinsurance policyholders.

Insolvency procedures in the UK and Germany

7.28 In the event of an insolvency of an insurer, the ranking of the policyholders in the ordering of its creditors is important, because a higher ranking in that ordering would mean that other things being equal, the policyholders would have a greater chance of their claims being paid. The rules governing this ordering of creditors is different in the UK and Germany, the states in

which MIICL and MISE, respectively, are authorised. The broad difference is that in the UK, policyholders have slightly more protection, because they have priority over a larger part of the assets of the insurer.

- 7.29 This could have an effect on the security provided to Transferring Policies. However, I do not believe that this is a material issue because: (i) As discussed in paragraph 6.50, I consider it a remote possibility that MISE becomes insolvent, and (ii) as described in 7.23, the other Brexit risks associated for the Transferring Policies have a potentially greater impact.

Customer service

- 7.30 I have considered how the level of customer service, specifically claims handling and policy servicing, experienced by each group of policyholders could change after the Transfer.
- 7.31 Services such as systems, staff and physical assets are currently provided to MIICL by a service company, Markel International Services Limited ('MISL'). Subject to the completion of the appropriate employee consultation procedures, the employment contracts of those employees currently acting on behalf of the branch offices of MIICL will transfer on 1 January 2019 from MISL to Markel Holdings GmbH. MISL will also transfer to Markel Holdings GmbH certain systems and physical assets. Some services, systems, staff and physical assets will remain in MISL and be supplied to both MISE and MIICL. In the end state, MISE will receive the same services, systems, staff and physical assets from a combination of Markel Holdings GmbH and MISL as MIICL previously received. MISE will therefore provide the same standard of service to policyholders as is currently delivered by MIICL as it will be using the same personnel in the same offices using the same systems.
- 7.32 The head office business of MIICL and the Irish branch business of MIICL will be serviced in the same manner as prior to the Transfer by employees of MISL
- 7.33 I do not anticipate any material adverse impact to any group of policyholders following the Transfer as a result of claims handling and policy servicing. This is because:
- ▶ The same personnel will be providing the same types and levels as before the Transfer, from the same office locations.
 - ▶ This is an intra-group transfer scheme, and there are no new policies or claims (in the sense that what appears in one firm is taken away from the other), so no additional resources should be required to provide an equivalent level of customer care.
 - ▶ As I discussed in the section on Brexit, the consequences on customer care in the case of a hard Brexit without the Transfer are much more serious. By effecting the Transfer I believe that those risks are mitigated.

Financial Ombudsman Service

- 7.34 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. It is not necessary for the private individual or micro enterprise to live or be based in the UK for a complaint regarding an insurance policy to be dealt with by the Financial Ombudsman Service. However, it is necessary for the insurance policy concerned to be, or have been, administered from within the UK and/or issued from the UK.
- 7.35 Following the Transfer, certain Transferring Policyholders who are currently eligible to refer a dispute with MIICL to the UK FOS will lose such rights. However, based on MIICL's analysis of the Transferring Policies, very few policyholders will be impacted due to the following reasons:

- ▶ Where the Transferring Policies were written and administered entirely out of one of the branch offices in Germany, the Netherlands and Spain, the policyholders are not eligible to bring a complaint under the UK FOS due to the lack of the UK connection. We understand that MIICL considers that this is the case for the majority of the Transferring Policies written by those branches.
- ▶ We understand that MIICL considers the Transfer to comprise largely of non-consumer business (with only 15% of policyholders estimated to be consumers), and so only a minority of affected policyholders are likely to be eligible to make a complaint more generally (i.e., even if their policy was written in or administered from the UK, which is not the case for the policyholders of the Dutch, German and Spanish branch offices as set out above).

7.36 I have however discussed with Markel the possible alternative measures that could be put in place, and any available ombudsmen scheme in the local branch jurisdictions. I understand that the following is the position in the relevant branch jurisdictions:

- ▶ There is a voluntary ombudsman scheme in Germany, the German Insurance Ombudsmann Association (Versicherungsbund e.V.) to which policyholders whose insurer is a member can make a complaint. Only consumers and micro-enterprises are eligible under the scheme. I understand from Markel that MISE will register to become a member of this scheme prior to the Transfer. Transferring Policyholders may also post-Transfer address complaints to BaFin.
- ▶ There is a scheme in the Netherlands known as the Financial Services Complaints Board (Klachteninstituut Financiële Dienstverlening) ('Kifid'). The Kifid only applies to policyholders who are consumers. MIICL is currently a member of Kifid. We understand that MISE intends to apply for membership prior to the Effective Date. The Dutch Foundation for Consumer Complaints Board also provides services to consumers or businesses to help resolve disputes out of court. The services provided are alternative dispute schemes which are acknowledged by both the Dutch Government and the European Commission.
- ▶ The ombudsman scheme in Spain is not available to policyholders of non-Spanish insurers. However, policyholders will be able to make complaints about MISE in respect of its activities in Spain to the Spanish regulator.
- ▶ In Ireland, complaints against a financial services firm can be made through the Financial Services and Pensions Ombudsman ('FSPO'). The FSPO is a statutory officer who deals independently with unresolved complaints from consumers about their individual dealings with all financial service providers. The financial services provider must be registered and authorised by the CBI. FSPO is able to make decisions that are binding on the insurer in relation to the complaints it considers, these decisions can include redress and remediation.

7.37 I do not believe that any policyholders will be materially disadvantaged by the Transfer in relation to the Financial Ombudsman Service due to the following reasons:

- ▶ I understand from the witness statement of Andrew John Davies on behalf of MIICL and MISE that the number of historical cases referred to the UK FOS is small. Since 2014, on average only five referrals annually have been made to the UK FOS by MIICL policyholders. In addition, MIICL's records indicate that each of these referrals has been made by persons resident in the UK and hence there is only a small chance that any such referrals have been made by policyholders of policies similar to the Transferring Policies. Therefore, I believe that the loss of such a right is unlikely to have a material impact on the Transferring policyholders.
- ▶ As set out above, there are a number of alternative schemes which Transferring Policyholders can benefit from, depending on the jurisdiction in which they are situated.

- ▶ MISE has committed in the scheme document to reduce the impact of the loss of such a right by complying with the following:
 - (a) The relevant provisions of DISP Dispute Resolution: Complaints chapter of the FCA handbook of rules and guidance ('DISP') that would apply to the handling of any complaints brought to the UK Financial Ombudsman Service that fall under its jurisdiction.
 - (b) Any other relevant sections of the handbook of rules and guidance issued by the FCA from time to time pursuant to FSMA where the application of local law is likely not to result in the same outcome for the Transferring Policyholders.
 - (c) Any valid judgment, settlement, order or award (or relevant part thereof) of the UK Financial Ombudsman Service, made under its jurisdiction as set out in DISP 2.
 - (d) MISE will also notify BaFin of the undertakings set out in the scheme document and request that BaFin takes these into account in its supervision of MISE.

Policyholder communication strategy

- 7.38 The regulations under the FSMA require that a communication is sent to every policyholder of the parties of an insurance business transfer scheme, unless the Court waives this requirement. Consideration is usually given to the practicalities and cost of this process, whilst having in mind the relevance of the scheme to policyholders. Ultimately, it is for the Court to grant these waivers.
- 7.39 MIICL propose to undertake procedures to notify policyholders and other interested parties of the Transfer. I have reviewed the material to be distributed to these parties, and am satisfied that this documentation is appropriate and that it includes sufficient detail on the Transfer. I understand that the following actions will be undertaken by MIICL:
1. Notify the policyholders of the Transferring Policyholders via post using a communication pack, either directly (where MIICL has the contact details) or through a broker. Where a broker is used then MIICL has made arrangements with the broker that they receive regular updates on which policyholders have been notified. I believe that this is an appropriate method of notifying these policyholders.
 2. Notify the relevant reinsurers via email using a communication pack, either directly or through a broker. Where a broker is used then MIICL has made arrangements with the broker that they receive regular updates on which reinsurers have been notified. I believe that this is an appropriate method of notifying these reinsurers.
 3. Make relevant information, including this report, available on its website.
 4. Advertise in the press.
- 7.40 MIICL intends to request that the Court grants certain waivers in relation to the notification requirements. In considering these requests I have considered the relevance of the Transfer to the policyholder, the extent to which they might be disadvantaged by not receiving further notification, the extent to which they might be inconvenienced by the notification, and the practicalities and costs of making the notification. The most material waivers requested are: for:
1. Policyholders who will not Transfer. They represent approximately 90% of MIICL's policyholders. They will remain policyholders of the same legal entity, with exactly the same governance structure, regulatory framework, policy terms and conditions and their policies will be serviced in the same manner as prior to Transfer. For this reason I believe that this waiver is reasonable.

2. "Non-active" policyholders, with Transferring Policies on older years of account where the policy has expired and there is not projected to be any real prospect of a future claim being made. The waiver would apply to years of account prior to a "cut off" year, where that cut off year varies according to the line of business. The assumption for the cut off year is consistent with the MIICL claims reserving analysis (so that there are not any projected future payments on those years of account in respect of claims which are currently unreported). I have reviewed the cut off year applied to each line of business and believe that they are appropriate. I believe that this is a reasonable approach since it would be impractical to notify all of these policyholders, and they are very unlikely to have to make further insurance claims on those policies.
3. Certain groups of beneficiaries and other groups where MIICL does not have contact details: including (without limitation) Employer's Liability beneficiaries and co-insurers (MIICL wrote some business on a co-insurance basis). The details of these parties are unknown and cannot be notified. I would not expect MIICL to hold the contact details of these parties and I do not believe that there is any practical way of identifying them. Therefore, I believe that this is a reasonable approach.
4. Reinsurers with whom MIICL (or a reinsurance broker on its behalf) has placed reinsurance prior to 2001. That information is not available from the due diligence work currently carried out by MIICL. However, the year 2001 is prior to the "cut off" date used for all of the classes of business (see point [2] above), and we believe that it is very unlikely that any further reinsurance recoveries would be recovered from those reinsurance policies. Therefore, I believe that this is reasonable approach.
5. A general waiver in respect of reinsurers for whom MIICL does not have contact details. This waiver is not now needed because MIICL has collated all contact details of the reinsurers they intend to notify.

7.41 I also note that the Markel contact details which policyholders should use will not change after the Transfer, and that MIICL has agreed to pass on to MISE any relevant communications from policyholders in relation to the Transferring Policies.

7.42 Markel intends to place advertisements in a range of publications, which covers all of the territories where there is a location of risk for the Transferring Policies. The strict requirement is for MIICL to notify in two national newspapers in each EEA state in which a risk is situated. I understand that in Belgium, France, Germany, Ireland, Italy, the Netherlands and Spain, Markel will advertise solely in the Financial Times (International Edition). I understand this newspaper is widely circulated in these jurisdictions. I believe that this is a reasonable approach.

7.43 For the above reasons I am satisfied that the policyholder communications strategy for the Transfer is reasonable and does not materially affect any policyholder.

Policyholders in jurisdictions outside the EEA

7.44 All of the risks associated with the Transferring Policies are located in the EEA. However, some of the Transferring Policyholders will be domiciled in non-EEA countries, and as a result, the governing law of their policies is relevant to the enforceability of the contract. All policies will transfer as a matter of English law. The question is whether, to the extent any policies are governed by the laws of another state, such policies will transfer as a matter of local law.

7.45 Firstly, I have had discussions with Markel and their legal advisors to understand the number of policyholders which could potentially be affected by this issue. Markel considers that substantially all policies of the branch offices in Germany, the Netherlands and Spain are governed by the law of an EEA state, and that generally the policies of the UK head office and Irish branch will be English law or the law of an EEA state. For the policies governed by English law or the law of an EEA state there should be no issues of enforceability. Markel cannot rule out that there may be some policies of the UK head office or the branch office in

Ireland which are governed by the law of a non- EEA state. Generally, the issue to consider in respect of non-EEA law governed policies is the risk that the underlying policyholders may argue that the Transfer is not effective. This might be the case where a policyholder would object to the Transfer based on the financial strength of the transferee or its reputation. Given the context of this Transfer, I consider it unlikely that any of the policyholders who could take this approach would do so, as MIICL is unlikely to be able to service their policy post-Brexit (absent agreement between the UK and the EU on contract continuity) (i.e., there is a risk their claim could not be paid). In addition, as set out in paragraph 6.50 of this report, MISE is well capitalised and the likelihood of insolvency is remote.

- 7.46 Markel is currently undertaking a sampling exercise of those policies to ascertain the number of such policies. Given the above, I do not expect that there is a large number of policyholders potentially affected by this issue and, as a result, I do not expect there to be a material concern around the effectiveness of the UK court order sanctioning the Transfer. However, I will review the findings of the exercise carried out on the Irish branch office and will comment on this in my Supplementary Report.

Governance

- 7.47 I have been provided with and have reviewed the governance framework and policy documents for each of MIICL and MISE. These documents describe the system of governance underpinning the management of MIICL and MISE.
- 7.48 For MIICL, the document sets out the principles of governance, roles and responsibilities, governance structure, controls in place and escalation procedures. In my opinion, the governance framework for MIICL contains all of the key elements that I would expect, and I consider this framework to be adequate for a company of this size and complexity. The governance structure for MIICL will not change after the Transfer, except that those specific requirements for the branch offices will not be required from the point at which those offices are closed.
- 7.49 For MISE, the governance structure is similar; from my discussions with Markel, this is as I would expect because there are similarities across the processes used across the Markel subsidiary companies. Some of the key differences between the MIICL and MISE frameworks are:
- ▶ There are fewer Key Function Holders and Board Reporting Committees for MISE. However, given the smaller size and scope of MISE compared to MIICL, I consider this to be reasonable.
 - ▶ The regulatory framework aspects of the governance structure are tailored to the requirements of BaFin rather than PRA, which is as I would expect.
- 7.50 The governance frameworks for MIICL and MISE are as I would expect for firms of this size and complexity, and I did not identify any material differences between the two frameworks. Therefore, this does not affect my conclusion on the Transfer.

Regulatory protection

- 7.51 MIICL is currently regulated by the PRA and the FCA in the UK, and MISE is regulated by BaFin in Germany.
- 7.52 The prudential regulatory regime, Solvency II, is the same in the UK and in Germany. I note that Solvency II is written into UK Law and therefore, immediately following Brexit, the regulatory regimes in the UK and Germany will continue to be equivalent. While it is possible that amendments could be made to the UK prudential regulatory regime following Brexit, in my view the prudential regulatory protection provided by Solvency II within the UK will remain aligned with the prudential regulatory protection provided in Germany in the foreseeable future.

- 7.53 MIICL currently follows each of the local conduct regulations where risks are located and the location from which the business is carried out. Following the Transfer, neither the location of risk nor the location from which the business is carried out will change. This is because the branch office structure of MISE will mirror the branch office structure of MIICL, and policies will be allocated to the corresponding MISE branch office. This means that for each Transferring Policy there will be no change to the insurance regulator responsible for conduct regulation. I understand that MIICL and MISE will continue to follow the same local conduct standards after the Transfer. Therefore, this does not affect my conclusion on the Transfer.

Pension arrangements

- 7.54 MIICL has a defined benefit pension scheme for employees, which is now closed to new members and closed for the accrual of new benefits. As at 31 December 2017 the estimated amount of liabilities of the pension scheme pension liability, on a discounted basis, is \$197m. In the MIICL IM SCR this pension liability attracts a capital charge of \$32m. The pension scheme will not transfer to MISE, and MISE does not have any pension schemes.
- 7.55 This does not affect my conclusion on the Transfer because:
- ▶ I believe that appropriate allowance for the risk is made in the MIICL IM SCR and MIICL meets that overall capital requirement, both before and after the Transfer.
 - ▶ The pension scheme does not transfer as part of the Transfer, and so there is no change to the amount of pension risk in MIICL or MISE.

Tax implications of the Transfer

- 7.56 I have discussed the tax implications of the Transfer with the tax team of MIICL and have also consulted with tax specialists from my own firm on this matter.
- 7.57 There may be some small additional amounts of corporation tax to pay as part of the Transfer, but I do not expect that those amounts are material to the Transfer. The ongoing tax charges for MISE might also be slightly higher than the corresponding MIICL amounts, but again, I do not expect that those amounts are material to the Transfer.
- 7.58 I do not expect that there will be any material tax implications from the implementation of the Bermuda QS, but will review this as part of my Supplementary Report, once the terms of that contract are finalised.
- 7.59 For the above reasons, I do not believe that any issues relating to tax have any effect on my conclusion on the Transfer.

Implications of the Transfer on ongoing expense levels

- 7.60 Other than the initial costs of the Transfer, the ongoing expenses of MIICL and MISE are not anticipated to materially increase after the Transfer, as all claims handling and policy administration will be performed by the same personnel. I therefore do not anticipate that this will create any adverse impact to the MIICL or MISE policyholders.

Impact of other portfolio transfers

- 7.61 I understand that MIICL is currently planning to transfer its business written through a branch office in Switzerland to MISE, pursuant to a separate portfolio transfer to be undertaken in due course, in accordance with Swiss Law. This timetable for this transfer is not yet agreed. The amount of business transferring is relatively small (with a net of reinsurance technical provision amount of approximately \$2m). Furthermore, the business transferring has similar to the business that will be included in MISE. For this reason, the business transferring from the Swiss branch of MIICL does not affect my conclusion on the Transfer, regardless of when the Swiss transfer is effected.

Set off

- 7.62 '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 do not believe that there are any material set-off rights that can be exercised by cedants or reinsurers. I have not identified any set-off issues as part of my work, and so this does not affect my conclusion on the Transfer.

Legal Opinions

- 7.63 There are no areas of my work where I have needed to obtain an independent legal opinion. I have discussed the following issues with the legal advisors of MIICL:
- ▶ The options available in EEA states as a replacement for the UK FSCS and Financial Ombudsman Scheme.
 - ▶ The effect of the Transfer on Transferring Policyholders located outside of the EEA.
- 7.64 I did not deem those issues to be sufficiently material to require an independent legal opinion. The legal advisors have a good professional reputation and I am relying on their own professional independence. For that reason I am comfortable with the conclusions I have reached for the matters set out above.

8. Security provided to policyholders

- 8.1 In this section I will summarise the reasons for reaching my conclusion. I will first set out some general considerations, and then consider each of the three groups of policyholder.

General considerations

Sufficiency of technical provisions assessment

- 8.2 The technical provision is the money set aside by an insurance company to pay future claim amounts. It is an important part of the security offered to policyholders; it is important that an insurance company has sufficient money available to pay these future claims. I have reviewed the technical provisions of MIICL and MISE pre and post transfer.
- 8.3 My review has included an assessment of the approach, methodology and governance that are used to determine the technical provision levels. I have also assessed key assumptions used in determining the technical provisions and also carried out a benchmark review for the most material and uncertain aspects of the technical provisions of MIICL and the transferring business.
- 8.4 The technical provisions in MISE at the time of the Transfer are likely to be small compared to the size of the transferring liabilities. Also, the technical provisions of MISE will be valued using the same process, methodology and assumptions that are currently used for the transferring business.
- 8.5 Therefore, I have concluded that the technical provisions are set on an appropriate and consistent basis for both MIICL and MISE, both before and after the Transfer. I will provide an update to the technical provision assessment in the Supplementary Report.

Capitalisation position of entities post transfer

- 8.6 I have reviewed the regulatory capital position of MIICL and MISE pre and post the Transfer. Post Transfer, both entities would meet regulatory capital requirements by a large margin. The regulatory capital is calibrated at a 1 in 200 level of sufficiency. This suggests that the overall level of security provided to the policyholders of both MIICL and MISE is good.
- 8.7 Both MIICL and MISE are rated 'A' by both Standard & Poor and A.M. Best, and I would expect that this would be maintained after the Transfer. This suggests a good level of financial strength.
- 8.8 A significant proportion of the assets held by MISE will be in the form of a reinsurance asset with MBL. This will increase the counterparty default risk for MISE, but will be a strong source of security for MISE, given the size and financial strength of MBL. MBL is also rated 'A' by both Standard & Poor and A.M. Best. I conclude that MBL would provide a high level of security to MISE after the Transfer.

Servicing of policyholders

- 8.9 From the policyholders' perspective, there will be no changes to the way that policies are administered and claims paid, and I do not anticipate any changes to the level of customer care provided.

The impact of Brexit

- 8.10 Brexit has introduced or exacerbated a number of risks for insurers operating in the UK, particularly for those that trade across EU borders. There is also the potential that after Brexit, UK insurers lose the ability that currently exists to insure and service risks in the EU (outside of the UK) without being authorised by local regulators. Not proceeding with the Transfer gives the potential, depending on the outcome of ongoing Brexit negotiations, of policyholders not legally being able to have their claims paid or policies serviced.

- 8.11 I believe that the most pragmatic solution to the Brexit related issues is to effect the Transfer. There are some Brexit risks which cannot be avoided in any practical way; however, I believe that the most material risks, relating to how services can be provided to EEA policies, can be mitigated by transferring those policies or parts of policies to MISE.

Other issues

- 8.12 I have considered various other issues, as set out in section 7 of this report. None of those other matters affects my conclusion on the Transfer.

Considerations for Non-transferring Policies

- 8.13 Non-Transferring Policies are currently covered by a strongly capitalised company (i.e., MIICL) and would continue to be insured by the same legal entity after the Transfer.
- 8.14 The transferring liabilities and risks are small in comparison to the current overall size of MIICL. The technical provisions transferring represent approximately 15% of the MIICL total technical provisions. The business transferring is also of the same general type of risk. Therefore, the mix of insurance risks in MIICL after the Transfer will not be materially different to the situation before the Transfer (except that the size of the business will be reduced by 15%).
- 8.15 For the above reasons I conclude that the security provided to the Non-transferring Policies of MIICL will be equivalent after the Transfer.

Considerations for Transferring Policies

- 8.16 Transferring Policies are currently covered by a strongly capitalised company (i.e., MIICL) and would transfer to another strongly capitalised company (i.e., MISE).
- 8.17 This is the group of policies which could, potentially, be materially affected by Brexit if the Transfer did not go ahead. In particular, there is the potential that after Brexit, UK insurers lose the ability that currently exists to insure and service risks in the EU (outside of the UK) without being authorised by local regulators. I believe that this would be detrimental to these policyholders.
- 8.18 The type of security provided to the Transferring Policyholders would be different after the Transfer because this security would come from different sources. MISE is a relatively large, well-capitalised insurer, writing a very diverse range of insurance products. Although MISE is also well-capitalised, but the absolute size is much smaller than MIICL and the range of business written is narrower. However, MISE does benefit from the Bermuda QS, which is backed by the security of MBL. MBL is a very large, strongly capitalised reinsurer. On balance, it is my view that the overall strength of the level of security provided by these two approaches is broadly equivalent.
- 8.19 For the above reasons I conclude that the security provided to the Transferring Policies of MIICL will be equivalent after the Transfer.

Considerations for Transferee Policies

- 8.20 Transferee Policies are currently covered by a strongly capitalised company (i.e., MISE) and would continue to be insured by the same legal entity after the Transfer.
- 8.21 I have reviewed the wider communications plan put in place by Markel, and am satisfied that this plan is appropriate.
- 8.22 The Transferee Policyholders will belong to the same legal entity, with exactly the same governance structure, regulatory framework, policy terms and conditions, and their policies will be serviced in the same manner as prior to Transfer

- 8.23 For the above reasons I conclude that the security provided to the Transferee Policies of MIICL will be equivalent after the Transfer.

Considerations for Reinsurers of MIICL

- 8.24 I have considered any possible effect on the reinsurers of MIICL, where the underlying business is transferred to MISE. The amount payable by those reinsurers to MIICL and MISE in respect of that reinsurance would not change as a result of the Transfer. I did not identify any set off rights. Therefore, I conclude that these reinsurers are not materially affected.

9. Reliances and limitations

Events following the modelling date

- 9.1 The conclusions in this report are based on various analyses that have been carried out on data as at different points in time (typically 31 December 2017). I have been informed by MIICL that there have been no material changes between the modelling dates and the date of this report. However, future events could occur between the date of this report and the effective date of the Transfer that could change my conclusions. I will provide a letter prior to the sanction of the Transfer to update the Court on whether there have been any material changes since the issue of this report.
- 9.2 The balance sheets shown in this report are based on data as at 31 December 2017 for both MIICL and MISE. I would expect some changes to have taken place between then and the date of this report.

Reliance on other parties

- 9.3 In developing the conclusions in this report I have relied on the data and accompanying explanations supplied to me by and on behalf of MIICL and MISE. I have received specific statements of data accuracy from MIICL and MISE. I have not specifically reviewed the data for accuracy and completeness but I have reviewed it for reasonableness.
- 9.4 I have carried out investigations, as detailed in this report, to gain comfort on the appropriateness of the methodology and conclusions for the most significant liabilities. However this has not amounted to a full re-estimation of every class of business, so by definition I have relied upon the reserving work performed on behalf of MIICL and MISE for some components of the claims reserves. I believe that this is reasonable given the experience and professional qualification of the authors of the documents and the testing that I have carried out. The reviews that I have carried out on the reserves give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.
- 9.5 I have also relied upon discussions that I have had with the management of MIICL and MISE. Where appropriate, I have sought documentation from them to evidence the assertions made to me in these discussions.
- 9.6 Additionally, draft versions of this report have been reviewed by the management of MIICL and MISE, and challenged appropriately where they believed this report did not capture structural or contractual information in sufficient detail or clarity. The comments received are available for review if required.

Use of benchmarks

- 9.7 As well as analysing the trends of the historical claims development, I have also relied upon benchmarks from wider market experience. Whilst MIICL and MISE's own development can be expected to vary from the benchmarks based on individual circumstances, I believe that the benchmarks are an appropriate check. However, benchmarks are revised periodically as new information and trends emerge, and it is likely that individual accounts will differ from the average. Therefore, it is possible that these benchmarks will not be predictive of the future claim reporting of MIICL and MISE.
- 9.8 I have also used other benchmarks based on my wider market experience to assess the appropriateness of some of the assumptions used within the reserve estimations and capital modelling performed for MIICL and MISE.

Other reliances

- 9.9 The underlying numbers contained in this report are calculated to many decimal places and so totals and summaries are subject to rounding differences.

- 9.10 In my judgement, the results and conclusions contained in this report are reasonable given the information made available to me. However, the actual cost of settling future claims and those still outstanding as at the valuation date is uncertain as, amongst other things, it depends on events yet to occur such as future court judgments. It could be different from the estimates shown in this report, and possibly materially so. Such differences between the estimated and actual outcome could possibly have a material impact upon the balance sheet strength of the companies involved, and therefore upon the Transfer.
- 9.11 I do not believe that there are any matters that are relevant to the policyholders' consideration of the scheme which I have not taken into account.

Appendix A Glossary

I have used the following defined terms or technical terms in this report.

Term	Definition
BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht, the regulator of the insurance industry in Germany
Bermuda QS	MISE will have an intra-company reinsurance arrangement with Markel Bermuda Limited, who will reinsure 90% of all business written by MISE on a quota share basis following the Transfer. This will also include the transferring liabilities.
Best Estimate	An estimate prepared with no margin for either prudence or optimism included
Brexit	The UK voted to leave the EU on 23 June 2016 and then notified the European Commission of its intention to withdraw from the EU. Under the current terms of the withdrawal, the UK will cease to be a member state of the EU on 29 March 2019.
Counterparty Default Risk	The risk of any defaults of counterparties (i.e. any institution or individual that is a debtor to the undertaking)
Court	The High Court of England and Wales
Direct policyholders	Policyholders that are not insurers or reinsurers
DISP	Dispute Resolution: Complaints chapter of the FCA handbook of rules and guidance
EEA	The European Economic Area
EEA30	The geographical area covering the 30 EEA member states, excluding the UK
EU	European Union
External reinsurance	Reinsurance cover, in this context, purchased from reinsurers that are not a part of the Markel Group
FCA	The Financial Conduct Authority, one of the regulators of the insurance industry in the UK (in conjunction with the PRA)
FOE	Freedom of Establishment basis
FOS	Freedom of Services basis
FRC	The Financial Reporting Council, the body responsible for setting actuarial standards in the UK
FSCS	Financial Services Compensation Scheme, the consumer protection scheme in the UK
FSMA	Financial Services and Markets Act 2000
FSPO	Financial Services and Pensions Ombudsman
IBNR	Incurred but not reported. Refers to the amounts an insurer will have to pay for claims that are reported in the future but relate to events that have already occurred. Often used to refer to any amounts insurers must pay over and above existing case reserves and hence also includes IBNER (as defined below). Where it does not include IBNER, it is sometimes referred to as 'Pure IBNR'
IBNER	Incurred but not enough reported. Refers to the amounts an insurer will have to pay over and above existing case reserves for claims that have already been reported, i.e., the estimated cost of any anticipated future development on known claims. This is often included within IBNR
Independent Expert	The suitably qualified person appointed by the court to produce an independent report on the Transfer, in accordance with the FSMA
Insurance Risk	Risks relating to insurance policies sold, i.e., the risk that the cost of claims for which the insurer is responsible proves to be higher than expected

Term	Definition
Kifid	Klachteninstituut Financiële Dienstverlening, a dispute resolution scheme for consumers in the Netherlands
Market risk	Risks relating to investment performance and changes in the value of investments
MCR	Minimum Capital Requirement, a formulaic calculation of the capital requirement as part of the existing European Solvency II regulations for insurers
Non-transferring Policyholders	The policyholders of MIICL which will not transfer to MISE after the Transfer.
Operational risk	Risks relating to failure of operational procedures
ORSA	Own Risk and Solvency Assessment
Own Funds	Available capital to meet the capital requirements under Solvency II
Passporting Regulations	Financial Services and Markets Act 2000 (EEA Passport Rights) Regulations 2001 (SI 2001/2011)
PRA	The Prudential Regulatory Authority, one of the regulators of the insurance industry in the UK (in conjunction with the FCA)
PRA's Statement of Policy	PRA's approach to insurance business transfers
RoW	The geographical area covering all locations outside of the EEA.
S&P	Standard & Poor, a credit rating agency.
SCR	Solvency Capital Requirement. The amount of capital insurers are required to hold under Solvency II regulations. If an insurer's capital (i.e., 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 II	An updated set of regulatory requirements for insurers that operate in the EU. These requirements apply to insurers from 1 January 2016
Standard formula	A prescribed approach under Solvency II for the calculation of capital based on an insurer's financial information (e.g. premium, claims reserves, etc.)
SUP18 of the FCA Handbook	Chapter 18 of the Supervision Manual of the FCA Handbook
TAS 100	The Technical Actuarial Standard issued by the FRC which should be applied to all aspects of technical actuarial work.
TAS 200	The Technical Actuarial Standard issued by the FRC relating to matters where there is a high degree of risk to the public interest.
Transfer	The proposed insurance business transfer of the business of MIICL to MISE
Transfer Date	The date on which the Transfer becomes effective, currently expected to be 29 March 2019
Transferee Policyholders	The policyholders of MISE, before the Transfer
Transferring Policies	The policies that will be transferred as part of the Transfer.
Transferring Policyholders	The policyholders who hold a Transferring Policy
UK GAAP	Generally Accepted Accounting Principles, the accounting basis used by insurers in the UK
Underwriting Risk	The risks relating to the upcoming year of insurance business to be written, unexpired policies at the balance sheet date, and the uncertainties relating to the claims reserves at the balance sheet date

Appendix B Extract from EY Terms of Engagement

Scope of services

This engagement will cover the appointment of Niranjana Nathan as Independent Expert for the MIICL to Markel Insurance SE part VII transfer (the "Transfer"). We note that the primary duty of the Independent Expert in an insurance business transfer in the UK is to the High Court of England and Wales ("the Court").

We will:

- ▶ Analyse work you have carried out on the companies and portfolios of policies involved in the Transfer, including (but not limited to) the adequacy of the claims reserves and capital modelling analysis (under solvency rules) for each of the groups of policyholders who are affected by the Transfer.
- ▶ Supplement this with such additional calculations and investigations as the Independent Expert believes are necessary to enable him to form a view on the implications of the Transfer on the policyholders involved and communicate this to the Court.

We will prepare the following reports (together the "Reports"):

- ▶ A report (the 'Report') providing the Independent Expert's conclusions on the Transfer and explanation of those conclusions, to be presented in draft to the PRA and FCA (together the "UK financial regulators") on a date agreed with the UK financial regulators and then updated as required following the feedback from both the UK financial regulators and then delivered to the Court in sufficient time prior to the initial directions hearing.
- ▶ A supplementary report (the 'Supplementary Report') to supplement the Report, to be presented to the Court at the final court hearing to consider the sanction of the Transfer. The Update Letter will discuss issues that have arisen between preparation of the Report and the final court hearing that the Independent Expert considers material to the Transfer, as well as any impact on his conclusions.
- ▶ A summary report (the 'Summary Report'). In accordance with the Financial Services and Markets Act 2000 and subordinate regulations, a summary of the Independent Expert's report will be provided to affected policyholders and any other person entitled to receive a copy to assist them with assessing the Transfer.
- ▶ Such further reports as may be required by the Court, the UK financial regulators or by you in connection with the Transfer, it being acknowledged that the preparation of such reports may incur additional costs which (if relevant) will be agreed in advance of the relevant work being undertaken.

We will ensure that the Reports comply with the requirements of the Financial Services and Markets Act 2000, PRA's Statement of Policy – "The Prudential Regulation Authority's approach to insurance business transfers", applicable case law, relevant professional guidance and requests made by the UK financial regulators and Part 35 of the Civil Procedure Rules (each as amended, supplemented or replaced from time to time). This includes any obligations we may have thereunder to evaluate and verify any information which you have provided to us in connection with the provision of the Services or the preparation of the Reports.

In performing the Services, we will use the skill, care, expertise and competence that could reasonably be expected from a highly reputable international consultancy firm or company providing to major multinational corporations the same or similar Services to those provided under the Agreement (including the particular skill and expertise of the Independent Expert selected for appointment to the Transfer).

Where the Independent Expert determines that he will require legal support in relation to any issues relating to the Transfer we will endeavour to use information produced by your legal advisors wherever possible. Where we do need to obtain an independent legal opinion on any matter we will agree with you the instructions for this legal advice and associated fees in advance.

As part of this engagement Niranjan Nathan will be responsible for providing the report in his role as Independent Expert. In that role Niranjan will be undertaking the work on behalf of EY and EY takes responsibility for the work undertaken by its partners and employees. Specifically in the context of clause 4 within Appendix B of this statement of work Niranjan will be personally responsible for the report but that EY also takes responsibility for this work as a result of Niranjan being employed by EY.

Appendix C Summary of data provided

Data area	File(s)
Financial information	MIICL Actuarial Function report as at 31 December 2017
	MIICL Actuarial SAO report as at 31 December 2017
	MIICL Reserving exhibits as at 31 December 2017
	External actuarial report as at 30 June 2018
	MBL Actuarial report as at 31 December 2017
	MBL Financial Statement as at 31 December 2017
	MBL Financial reports as at 31 December 2017
	MIICL Financial Statements from 2016-2018
	MIICL Financial reports as at 31 December 2017
	MIICL Internal Model and Standard Formula SCR outputs as at 31 December 2017
	MISE Business plan
	Schedules showing the impact of the Transfer on the reserves and balance sheets of MIICL and MISE as at 31 December 2017
	MIICL 2018 investment plan
	MIICL capital and dividend policy documents
	Reinsurance
MISE reinsurance contract with MBL	
MIICL transferring reinsurance policyholders	
Capital and Risk	Standard Formula inputs
	Internal model documentation
	MIICL ORSA, dated 27 February 2018
Legal documents	Scheme document
	Witness statement
	Financial Ombudsman Service memorandum
Operational information	MISE governance map
	MIICL governance map
	MISE organisational structure document

Appendix D Checklist against PRA's Statement of Policy and SPU18 of the FCA Handbook

The table below shows the relevant section references in this report where I have addressed each point in the guidance from Chapter 18 of the Supervision Manual of the FCA Handbook and the PRA's 'Statement of Policy - The PRA's approach to insurance business transfers – April 2015' with regards to the scheme report.

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	1.11, 1.15
PRA 2.30 (2) FCA 18.2.33 (2)	Confirmation that the independent expert has been approved or nominated by the PRA (or appropriate regulator);	1.11
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;	1.11, Appendix E
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;	1.13 to 1.14
PRA 2.30 (5) FCA 18.2.33 (5)	The scope of the report;	1.19 to 1.20, Appendix B
PRA 2.30 (6) FCA 18.2.33 (6)	The purpose of the scheme;	2.27 to 2.28
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;	2.6 to 2.14
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;	1.21 to 1.23, Appendix C
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;	1.22 to 1.23, 7.64, 9.3 to 9.7
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;	1.22 to 1.23, 9.4 to 9.5
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;	2.46, Section 8
PRA 2.30 (12) FCA 18.2.33 (11 A)	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;	2.14

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	9.11
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.	Section 8 and throughout the report
PRA 2.33 (1) FCA 18.2.36 (1)	Include a comparison of the likely effects if it is or is not implemented;	4.13, 5.4, 6.11, 6.24
PRA 2.33 (2) FCA 18.2.36 (2)	State whether they considered alternative arrangements and, if so, what;	1.20
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; and	2.46, Section 8
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.	Section 7
PRA 2.35 (1) FCA 18.2.38 (1)	For any mutual company involved in the scheme: Describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders;	N/A
PRA 2.35 (2) FCA 18.2.38 (2)	State whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights; and	N/A
PRA 2.35 (3) FCA 18.2.38 (3)	Comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without	N/A

Appendix E Niranjan Nathan experience

Background

- ▶ Over 19 years' general insurance experience
- ▶ Qualified as a Fellow of the Institute & Faculty of Actuaries in 2004
- ▶ Joined Ernst and Young in 2016 and prior to this worked with Swiss Re and Tillinghast, Towers Perrin

Skills

- ▶ Extensive experience in advising clients in the London & other international markets
- ▶ Specialised in risk, actuarial pricing, reserving and capital management
- ▶ Experience in M&A transaction assessment and integrations

Professional Experience

- ▶ Niranjan is a partner and leads the EY UK P&C actuarial team
- ▶ Previously he was at Swiss Re where he was a managing director and the Chief Risk Officer (CRO) of their global commercial insurance division responsible all risk management and actuarial reserving activity globally.
- ▶ At Swiss Re, Niranjan has also led the UK P&C actuarial pricing team and been a senior member of the group strategy and development team. Prior to Swiss Re, he was a consultant at Tillinghast, Towers Perrin.
- ▶ Niranjan has over 18 years of experience as a professional in the general insurance industry with experience across several global markets. His experience spans risk, actuarial pricing, reserving, risk capital, portfolio and business monitoring, strategy development and implementation monitoring.
- ▶ Niranjan leads several engagements supporting clients develop their Brexit strategies and implementation plans including planning for Part VII transfers.
- ▶ He has been extensively involved in the structuring and pricing of several large and complex reinsurance structures including leading transactions which include Part VII portfolio transfers.
- ▶ He has been involved in several merger / acquisition situations and integration work streams across the UK and internationally for personal and commercial line business.
- ▶ He has managed the reserving processes for several London Market companies, Asia Pacific Reinsurance companies, Insurance clients and Australian State Schemes.