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Case No: CR-2018-001858

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
COMPANIES COURT

Royal Courts of Justice
7 Rolls Building, Fetter Lane,
London, EC4A 1NL

Date: 5 February 2019

Before:

MR JUSTICE SNOWDEN

- -

IN THE MATTER OF THE ROYAL LONDON MUTUAL INSURANCE SOCIETY LIMITED

AND IN THE MATTER OF ROYAL LONDON INSURANCE D.A.C.

AND IN THE MATTER OF PART VII OF THE FINANCIAL SERVICES AND MARKETS ACT 2000

- -

Martin Moore QC (instructed by **Pinsent Masons LLP**)
for **The Royal London Mutual Insurance Society Limited and Royal London D.A.C.**

Tom Weitzman QC for the **Prudential Regulation Authority**

Hearing date: 31 January 2019

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

MR JUSTICE SNOWDEN

MR JUSTICE SNOWDEN :

1. This is an application under Part VII of the Financial Services and Markets Act 2000 ("FSMA") for the Court's sanction of a scheme (the "Scheme") for the transfer of the EEA insurance business of The Royal London Mutual Insurance Society Limited ("Royal London") to a newly formed Irish subsidiary, Royal London Insurance D.A.C. ("RLI"). The transfer of business is proposed in order to deal with the potential problems for Royal London and its EEA policyholders of a "no-deal" Brexit.

2. In common with many other financial institutions, Royal London is concerned that in the event of a "no-deal" Brexit it will lose the "passporting" rights which currently enable it to rely upon its authorisation in the UK to carry out regulated activities to service its policyholders in other EEA Member States. To address this possibility, Royal London wishes to transfer its long-term business with policyholders in the EEA to RLI, which is be authorised and regulated in the Republic of Ireland, and thus able to service the policies concerned after Brexit, whatever form that may take.

3. The board of Royal London has also taken the view, and told its policyholders, that even if an agreement was now reached between the UK and the EU which would permit it to continue to administer the policies from the UK after Brexit, it is now committed to the transfer, which will still take effect as planned.

4. Subject to receiving sanction from the Court, the effective date of the transfer is anticipated to be 7 February 2019. For accounting and reporting purposes only, the transfer will, however, be deemed to have taken effect on 1 January 2019.

Royal London and RLI

5. Royal London is the United Kingdom's largest mutual life and pensions company. It has about 8.8 million policies and funds under management of £114 billion. Royal London maintains five funds, the principal one of which is the Main Fund into which is allocated a variety of books of business. It is the only fund open to new business. All the other funds are closed to new business, save for increments and options derived from existing contracts.

6. Royal London has reached its current state through organic growth as well as a series of acquisitions. For present purposes, the most relevant one was the acquisition in 2011 of Royal Liver Assurance Limited, an incorporated friendly society, and its subsidiaries ("Royal Liver"). Royal Liver itself had earlier acquired portfolios of business written in Ireland by the Caledonian Insurance Company, GRE Life Ireland Limited and Irish Life Assurance plc. Royal Liver also wrote business through its Irish branch. Under the terms of the transfer to Royal London, a Royal Liver Sub-Fund was established, into which was allocated the business carried on by Royal Liver and its subsidiaries.

7. As indicated, Royal London is a mutual life insurance company owned by its members. As at 31 December 2017 there were approximately 1,232,950 members who were policyholders who had effected policies of insurance with the company. Policyholders who effected policies after 25 April 1995 are only members where the policy entitles the policyholder to participate in the profits of Royal London. Thus, policyholders of acquired businesses are not members of Royal London. Separate to membership, Royal London has a concept of a ProfitShare which is a mechanism by which eligible

policyholders can share in its financial performance but at the sole discretion of the directors of Royal London.

8. RLI is a newly incorporated company which received the necessary authorisations to carry on business, including the business to be transferred to it under the Scheme, with effect from 1 January 2019. It has been capitalised by the injection of €40 million in cash from Royal London. Since 1 January 2019, RLI has written a relatively small number of protection policies in Ireland that would, in the absence of the proposed Scheme, have been written by Royal London through its Irish branch.

<u>The Scheme in outline</u>

9. The Scheme is a lengthy and complex document. I shall therefore simply attempt to summarise its more central features.

The Transferring Business

10. There are three blocks of business which are proposed to be transferred under the Scheme:

   i) about 446,000 largely with-profits policies written in Ireland at various times by Royal Liver, Irish Life, Caledonian Insurance Company and GRE Life Ireland. These are currently allocated to the Royal Liver Sub-Fund ("the Royal Liver Transferring Policies"). As at 30 June 2018 gross best estimate of liabilities ("BEL") for these with-profits policies was £737 million. That positive figure means that the anticipated future claims and expenses will exceed the anticipated future inflows from premiums;

   ii) about 55,000 non-profit protection policies sold after June 2011 through Royal London's Irish branch and which are allocated to the Royal London Main Fund ("the Post-2011 Protection Policies"). As at 30 June 2018 the gross BEL for these policies was negative £65 million (i.e. that anticipated future inflows from premiums will exceed anticipated future claims and expenses); and

   iii) about 1,300 bonds sold in Germany under the Scottish Life International brand which are also allocated to the Royal London Main Fund ("the German Bonds"). These bonds are composed of with-profits and unit-linked policies. The holders of the with-profits policies are members of Royal London and are also the only policyholders involved in the transfer who are eligible to participate in the ProfitShare. As at 30 June 2018 the gross BEL for such German Bonds was £105 million (i.e. that the anticipated future claims and expenses will exceed the anticipated future inflows from premiums).

11. Under the Scheme the transferring policies will be transferred from Royal London to RLI, where the blocks of business described above will be allocated to an appropriate sub fund to be established by RLI. Thus, the Royal Liver Transferring Policies will be allocated to the Liver Ireland Sub-Fund, the Post-2011 Protection Policies will be allocated to the Open Fund, and the German Bonds will be allocated to the German Bond Sub-Fund.

12. As well as the transfer of liabilities, under the Scheme Royal London will have an obligation to transfer assets in respect of the Royal Liver Transferring Policies and the German Bonds sufficient to match the gross BEL, Risk Margin and Solvency Capital Requirement ("SCR") required by the recast Directive on the taking up and pursuit of the business of insurance and reinsurance (2009/138/EC) ("Solvency II"), and the Capital Buffer required to capitalise the Liver Ireland Sub-Fund and the German Bond Sub-Fund at 164% in accordance with the RLI capital management framework. No assets will be required to be transferred in respect of the Post-2011 Protection Policies since the BEL for this business is negative.

The New Reinsurance Agreements

13. As only a proportion of the policies currently in the Royal Liver Sub-Fund at Royal London are to be transferred, it would ordinarily be necessary to identify and transfer a fair split of the assets in respect of these policies and thereby to split the Royal Liver Sub-Fund. That would involve taking account of the transferring policyholders' interest in the Royal Liver Sub-Fund's inherited estate (the part of the with-profits fund not allocated to policyholders' liabilities). That is a complex process, and the evidence is that it could not be achieved before Brexit on 29 March 2019. Further, the size of the German Bond business currently allocated to Royal London's Main Fund is so small that it is thought that it could not operate economically as a stand-alone with-profits fund.

14. To address these issues, the Scheme provides that RLI's liabilities in relation to the Royal Liver Transferring Policies and the German Bonds will be immediately reinsured back to Royal London under two new reinsurance agreements (together the "New Reinsurance Agreements"). The premiums for that reinsurance will be offset against Royal London's obligation to transfer assets to RLI under the Scheme, with the consequence that RLI will be left with very few cash assets in the respective new funds, and its regulatory capital in that regard will largely comprise its rights against Royal London under the New Reinsurance Agreements. These rights will also be the subject of a security package that is designed to ensure that, in the event of insolvency of Royal London, the transferring policyholders would be in no worse a position than if they had remained at Royal London.

15. The New Reinsurance Agreements also deal with the maintenance of benefits for the transferring policyholders. While at Royal London, with-profits policies in the Royal Liver Sub-Fund are required to be managed in accordance with certain principles in the instrument of transfer from which the relevant policies were acquired, and more generally Royal London is required to follow specified Principles and Practices of Financial Management ("PPFM"). The Scheme provides that for so long as the New Reinsurance Agreements are in place, RLI will have regard to such relevant principles from the instrument of transfer when managing the Liver Ireland Sub-Fund, and will generally manage the with-profits Royal Liver Transferring Policies and the German Bonds according to two "With-Profits Operating Principles" documents ("WPOP Documents") which will be aligned to the equivalent Royal London PPFM. In particular, the New Reinsurance Agreements set out the governance processes that must be followed when setting Bonuses, allocating units or determining unit prices for the with-profits Royal Liver Transferring Policies and German Bonds. The New Reinsurance Agreements also set out the process that must be followed prior to any material amendments to the terms and conditions of any relevant with-profits policies

of either Royal London or RLI, or Royal London's PPFM. Unless the changes are permitted by the New Reinsurance Agreements they must be agreed by RLI, and there is a mechanism to resolve any disputes by reference to an independent actuarial expert.

16. In essence, the New Reinsurance Agreements are designed to ensure that the holders of the Royal Liver Transferring Policies and the German Bonds can continue to enjoy the same benefits and oversight that they enjoyed at Royal London. As such, the New Reinsurance Agreements form a critical part of the Scheme for transferring policyholders. The terms upon which the New Reinsurance Agreements can be terminated, and the security arrangements in relation to them are therefore also of critical significance.

17. The Scheme makes detailed provision for the circumstances in which the New Reinsurance Agreements can be terminated by Royal London and/or RLI. Prior to termination it is necessary for Royal London and RLI to obtain advice from their respective actuaries and for Royal London to consult and obtain the approval of its Liver Supervisory Committee. In addition, at least 30 days' notice must be given to the regulators in both the UK and Ireland.

18. Termination will trigger an obligation upon the parties to agree or have determined by an independent actuarial expert a termination amount taking into account the BEL of the transferred Royal Liver Transferring Policies and the German Bonds that are still in force. Importantly, termination of the New Reinsurance Agreement in respect of the Royal Liver Transferring Policies cannot take effect unless and until Royal London has paid to RLI the amounts that would be due on a split of the Royal Liver Sub-Fund to reflect the interests of the transferring with-profits policyholders in the Royal Liver Sub-Fund's inherited estate. A similar provision applies under the New Reinsurance Agreement in respect of the German Bonds to reflect the reasonable expectations of the holders of such bonds to future payments of ProfitShare by Royal London.

19. The determination of these amounts due to RLI has to be agreed between Royal London and RLI, which are required to take into account reports from their respective actuaries. The amount in question must then be certified by an independent third-party actuary and notified to the regulators in the UK and Ireland. Importantly, the Scheme also allows the holders of Royal Liver Transferring Policies to apply to the Court to enforce the provisions of the Scheme in this respect.

The Security Package

20. The security arrangements to protect the interests of RLI and its policyholders in the event of the insolvency of Royal London are complex. They are, however, important, because in the absence of such arrangements, if Royal London were to become insolvent, RLI would simply rank as an ordinary unsecured creditor in respect of the New Reinsurance Agreements, and hence RLI's policyholders would in effect rank behind the equivalent policyholders who had been left in Royal London.

21. To deal with this possibility, Royal London will grant RLI "Security Arrangements" consisting of a total of four fixed charges over a specified value of assets held in segregated accounts and a floating charge over its other assets not already subject to other charges (being about £111 billion). The documents comprising the Security Arrangements are subject to English law.

22. The intention of the Security Arrangements, which include certain “equalisation provisions”, is that in the event of the insolvency of Royal London, RLI will recover an amount which will enable it to pay to the relevant transferring policyholders an equivalent amount to that which they would have received had they remained policyholders of Royal London, subject to a minimum recovery of 50% of the BEL of the business reinsured under the New Reinsurance Agreements. In essence, therefore, the Security Arrangements will align the recovery of the policyholders of RLI to those of direct policyholders of Royal London, except in the extreme circumstance that direct policyholders of Royal London recover less than 50% of BEL, in which case the policyholders of RLI will do better.

Other provisions

23. In addition to clauses giving effect to the transfer of the business and the other matters described above, the Scheme contains conventional provisions for the continuity of proceedings, mandates and other matters. It also deals with the establishment, maintenance, merger, division of funds and closure of the Liver Ireland Sub-Fund and the German Bond Sub-Fund and the allocations to such funds of the Royal Liver Transferring Policies and the German Bonds and their respective policies, assets and liabilities. The Scheme also contains detailed provisions for the circumstances in which capital support might be required for the Liver Ireland Sub-Fund and the German Bond Sub-Fund from other funds of RLI.

24. One effect of the Scheme is that holders of German Bonds will lose their membership of Royal London. Membership is only likely to be of value in the context of a de-mutualisation. No such event is anticipated, but a provision has been included in the Scheme to the effect that if Royal London demutualises within 5 years of the Effective Date any person then holding a German Bond will be entitled to the same compensation as any other member of Royal London is to receive.

Loss of FSCS protection

25. A notable consequence of the transfer of policies from Royal London to RLI is that about 22% of the transferring policyholders who would be entitled to the protection of the UK’s Financial Services Compensation Scheme (“FSCS”) in the event of insolvency of Royal London, will be likely to lose access to the FSCS in respect of post-transfer events. Ireland (in common with other EEA States) does not have an equivalent compensation scheme. I shall return to consider that matter below.

Part VII Transfers

26. Section 104 FSMA provides that no insurance business transfer scheme is to have effect unless an order sanctioning it has been made under section 111(1).

27. Sections 105(1) and 105(2)(a) FSMA provide in relevant part,

> “(1) A scheme is an insurance business transfer scheme if it-
>
> (a) satisfies one of the conditions set out in subsection (2);

> (b) results in the business transferred being carried on from an establishment of the transferee in an EEA State; and
>
> (c) is not an excluded scheme.
>
> (2) The conditions are that -
>
> (a) the whole or part of the business carried on in one or more member States by a UK authorised person who has permission to effect or carry out contracts of insurance ("the transferor concerned") is to be transferred to another body ("the transferee")."

It is clear on the facts of the instant case that the Scheme is an insurance business transfer scheme as defined.

28. Section 111(1) FSMA sets out the conditions which must be satisfied before the court may make an order sanctioning an insurance business transfer scheme. The conditions are that all of the appropriate certificates and authorisations to conduct the transferring business shall have been obtained from the relevant regulators (section 111(2)) and that the court considers that, in all the circumstances of the case, it is appropriate to sanction the scheme (section 111(3)).

29. Section 112 then provides for the making of orders to give effect to the transfer of the business, including as to the transfer of property, rights and liabilities (section 112(1)(a)), the continuation by and against the transferee of pending legal proceedings by and against the transferor (section 112(1)(c)), and such incidental, consequential and supplementary matters as are necessary to secure that the scheme is fully and effectively carried out (section 112(1(d)).

30. The approach to the exercise of the Court's discretion under section 111(3) FSMA is now well established. It follows the approach adopted under the predecessor of Part VII FSMA, namely Schedule 2C to the Insurance Companies Act 1982. The principles were conveniently summarised by Evans-Lombe J in Re AXA Equity & Law Life Assurance Society plc and AXA Sun Life plc [2001] 1 All ER (Comm) 1010 at 1011-1012 as follows,

> "(1) The 1982 Act confers an absolute discretion on the court whether or not to sanction a scheme but this is a discretion which must be exercised by giving due recognition to the commercial judgment entrusted by the company's constitution to its directors.
>
> (2) The court is concerned whether a policyholder, employee or other interested person or any group of them will be adversely affected by the scheme.
>
> (3) This is primarily a matter of actuarial judgment involving a comparison of the security and reasonable expectations of policyholders without the scheme with what

> would be the result if the scheme were implemented. For the purpose of this comparison the 1982 Act assigns an important role to the independent actuary to whose report the court will give close attention.
>
> (4) The FSA by reason of its regulatory powers can also be expected to have the necessary material and expertise to express an informed opinion on whether policyholders are likely to be adversely affected. Again the court will pay close attention to any views expressed by the FSA.
>
> (5) That individual policyholders or groups of policyholders may be adversely affected does not mean that the scheme has to be rejected by the court. The fundamental question is whether the scheme as a whole is fair as between the interests of the different classes of persons affected.
>
> (6) It is not the function of the court to produce what, in its view, is the best possible scheme. As between different schemes, all of which the court may deem fair, it is the company's directors' choice which to pursue.
>
> (7) Under the same principle the details of the scheme are not a matter for the court provided that the scheme as a whole is found to be fair. Thus the court will not amend the scheme because it thinks that individual provisions could be improved upon.
>
> (8) It seems to me to follow from the above and in particular paras (2), (3) and (5) that the court, in arriving at its conclusion, should first determine what the contractual rights and reasonable expectations of policyholders were before the scheme was promulgated and then compare those with the likely result on the rights and expectations of policyholders if the scheme is put into effect."

31. The role of the "independent actuary" referred to by Evans-Lombe J is now fulfilled under section 109 FSMA by a report from an "independent expert" (invariably an actuary) and the role of the FSA is now fulfilled by the Financial Conduct Authority ("FCA") and Prudential Regulation Authority ("PRA") together.

32. The approach of the Court to the report of the independent expert and the views of the Regulators was described by Briggs J in Re Pearl Assurance (Unit Linked Pensions) Limited [2006] EWHC 2291 (Ch) at paragraph 6,

> "6. Notwithstanding that detailed perusal of a proposed Scheme both by an independent expert and by the [Regulators] are conditions precedent to the exercise of the court's discretion to sanction it, the discretion remains nonetheless one of real importance, not to be exercised in any sense by way of rubber stamp…. The relevant principles are concisely summarised in

> the following passage from the judgment of Mr. Justice Rimer in Re Hill Samuel Life Assurance Limited [1998] 3 All ER176, at177:
>
> > "Ultimately what the court is concerned with is whether the scheme is fair as between different classes of affected persons, and in arriving at a conclusion as to whether or not it is, amongst the most important material before the court is material which the Act requires to be before it, namely the report of an independent actuary as to his opinion on the scheme.""

The need for the Scheme

33. On 21 December 2017 the European Insurance and Occupational Pensions Authority ("EIOPA") issued an opinion on service continuity in insurance in light of the withdrawal of the UK from the EU. EIOPA's opinion was that, in the absence of a political agreement between the EU and the UK, UK insurance undertakings would lose their right to conduct business in the Member States of the EU by way of freedom of establishment and freedom to provide services under Solvency II. EIOPA stated that in such a situation, unless UK insurance companies took "mitigating actions" before Brexit, they would usually not be able to ensure the continuity of their services with regard to cross-border insurance contracts concluded prior to the date of the UK's withdrawal from the EU. One of the options suggested by EIOPA to ensure service continuity was the transfer of insurance contracts of UK undertakings with policyholders in the remaining 27 EU Member States to an insurance subsidiary established in an EU27 Member State.

34. Against the background of that opinion from EIOPA and the continuing uncertainty over the terms of Brexit during 2018, the board of Royal London concluded that in the absence of an agreement between the EU and the UK as regards the provision of financial services post-Brexit, the best option to ensure continuity of service for its policyholders would be to transfer its EEA business to RLI. The evidence also confirmed that the board of Royal London has kept this rationale under consideration in the context of the continuing political situation with regard to Brexit, and that it has maintained that view.

35. In essence, as Mr. Moore QC put it in argument, the board of Royal London consider that they have been forced into making a decision as to how best to protect the interests of their EEA policyholders against the risk that Royal London would be unable to service such policies in the event of a Brexit which made no provision for financial services. Mr. Moore QC submitted that Royal London and its policyholders required certainty, and a commercial decision therefore needed to be taken and implemented.

36. The PRA also addressed Brexit in its evidence and submissions. The PRA report stated,

> "The PRA is conscious of the fact that the transfer is driven by the UK's exit from the European Union on 29 March 2019, with associated time constraints. The PRA has no desire to delay progress of the Scheme in the circumstances."

37. In his submissions on behalf of the PRA, Mr. Weitzman QC reiterated that the PRA accepted that Royal London was not acting in order to obtain a business advantage, but was attempting to deal with the uncertainty caused by Brexit. He made the following statement of the PRA's position,

> "In the absence of an EU/UK withdrawal agreement, UK firms' passporting rights to other EEA jurisdictions will end at the point of the UK's exit from the EU – which is currently scheduled to be on 29 March 2019.
>
> In the absence of such passporting rights, there is uncertainty as to whether UK firms can lawfully continue to carry on insurance business in such other EEA jurisdictions, which uncertainty extends to the payment of claims.
>
> Having regard to such uncertainty, it is reasonable for UK firms to takes steps to achieve certainty, including the carrying out of Part VII transfer schemes.
>
> ….
>
> In the absence of an EU/UK agreement, there is uncertainty as to whether any UK Part VII transfer scheme taking place after the UK leaves the EU will be recognised by other EEA states.
>
> Having regard to the above, the PRA's view is that it is not unreasonable for Royal London to take the view that the time has now been reached when it should proceed with the present Part VII transfer in order to achieve certainty."

38. In common with its approach in other similar schemes, the FCA's report stated,

> "Whilst we are unable to opine on the likely outcome of the UK-EU negotiations, and whilst it remains unclear as to what the impact of the UK's withdrawal from the EU will be, the FCA generally expects applicants and the Independent Expert to have properly and fully considered the potential implications and risks to policyholders associated with the UK's withdrawal in the context of the proposed transfer. Where the analysis shows that there are risks and that the policyholder position could be materially affected, we expect the applicants and Independent Expert to have given proper and full consideration to possible mitigations and solutions to minimise any policyholder detriment arising from the Scheme."

39. The PRA took a similar approach and had reviewed the other "potential mitigations" suggested by the Independent Expert. The PRA concluded that such steps were not otherwise necessary for Royal London's business, would be very costly, and might not work. In the circumstances, the PRA did not dispute the Independent Expert's conclusion that it is reasonable that Royal London should not take such steps.

The impact of Brexit on the exercise of discretion by the Court

40. In re AIG Europe Limited [2018] EWHC 2818 (Ch), after referring to the approach in the London Life and AXA cases, I considered the effect of Brexit upon the discretionary decision of the Court in the context of an insurance business transfer scheme. I said, at [44]-[46],

> "44. … in considering whether the protections for policyholders are sufficient, it should be borne in mind that the current background is not the one that has often been considered in the past, where the independent expert, the Regulators and the Court are considering a transfer of insurance business which is being undertaken by the company concerned for entirely commercial reasons within its own control. The current situation is different.
>
> 45. The evidence of [the transferor] is that the uncertainty over the Brexit negotiations means that if it delayed further and did nothing, there is a real risk that substantial numbers of policyholders would be materially prejudiced in event of a "hard" Brexit by the loss of [the transferor's] EU passporting rights, and a resultant inability of [the transferor] to continue to service policies through its overseas branches or even pay policyholders' claims in other EU jurisdictions. The concerns expressed by [the transferor] seem genuine and reasonable, and in the absence of any objection or contrary evidence from the Regulators, I am not in a position to second-guess the directors of [the transferor] in this respect.
>
> 46. The consequence is that, in applying the tests in the authorities to which I have referred above, I must balance the risk of prejudice to a large body of policyholders in the EEA … if the Scheme were not to be sanctioned, against any potential risk of prejudice to individual policyholders under the terms of the proposed Scheme. In that regard, as was made clear by Evans-Lombe J in the AXA case, the fundamental question is whether the proposed Scheme as a whole is fair as between the interests of the different classes of persons affected. The current uncertainty over Brexit means that there may be no perfect solution for the holders of the policies being transferred …, and the possibility that some individual policyholders or groups of policyholders may be adversely affected in certain respects does not mean that the Scheme necessarily has to be rejected by the Court. It is also worth reiterating that it is not my function to produce what, in my view, is the best possible scheme: as between different schemes, all of which the Court might deem fair, it is the directors' choice which [the transferor] should pursue."

41. I applied the same approach in relation to a further insurance transfer scheme in The Prudential Assurance Company Limited [2018] EWHC 3811 (Ch) and in relation to a banking business transfer scheme in Barclays Bank plc [2019] EWHC 129 (Ch).

42. Mr. Moore QC, who appeared for Royal London, endorsed this approach. Given the importance of this issue in the current climate, I gave the PRA the opportunity to express its view of the approach that I had taken. That resulted in a written statement that the PRA's view is that the Court is entitled to take account of the uncertainties referred to in paragraph 37 above when assessing a Part VII scheme and whether policyholders are materially adversely affected by the scheme. The statement added that the PRA was "aware" of my judgments in AIG and Prudential and "does not seek to challenge" the approach which I had adopted. I take that to mean that the PRA does not disagree with my approach and, perhaps just as importantly, had no alternative to offer me in the instant case.

43. In the circumstances I consider that I am justified in continuing to adopt the same approach that I outlined in AIG to the exercise of my discretion in this case.

Satisfaction of the statutory requirements in this case

44. Without going into detail, I am satisfied that, subject to one point, all of the detailed requirements of FSMA and the Regulations as regards advertisements, notifications, certificates and regulatory permissions have been satisfied.

45. In particular, the PRA approved the form of the advertisements and the FCA has confirmed that it is satisfied that the way in which communications to policyholders have been conducted. I have also read a sample of the short letters and longer booklets sent to Royal London's policyholders which clearly explain the features and potential effect of the Scheme for the policyholders. In particular, the booklets clearly explained, in summary form, the New Reinsurance Agreements and the Security Arrangements, how the RLI funds will be managed after the transfer, and the procedure that would apply for payment of a fair proportion of the Royal Liver Sub-Fund's inherited estate and an amount in respect of future ProfitShare to RLI for the benefit of the relevant transferring with-profits policyholders in the event of termination of those arrangements.

The appropriate certificates

46. The one procedural point that has arisen relates to the "appropriate certificates" required by section 111(2) and Schedule 12 FSMA. Before dealing with the facts of the instant case I should briefly summarise the relevant statutory and EU provisions.

47. For the purposes of the Scheme relating to Royal London, which is authorised in the UK under Article 14 of Solvency II, the appropriate certificates are potentially those identified by the following provisions of paragraph 1 of Schedule 12,

> "(1) For the purposes of section 111(2) the appropriate certificates, in relation to an insurance business transfer scheme are -
>
> (a) a certificate under paragraph 2;
>
> (b) if sub-paragraph (2) applies, a certificate under paragraph 3;

(ba) if sub-paragraph (2A) applies, a certificate under paragraph 3A;

…..

(2) This sub-paragraph applies if–

(a) the transferor concerned is a UK authorised person which has received authorisation under Article 14 of the Solvency II Directive from the appropriate regulator; and

(b) the establishment from which the business is to be transferred under the proposed insurance business transfer scheme is in an EEA State other than the United Kingdom.

(2A) This sub-paragraph applies if—

(a) the transferor concerned is a UK authorised person which has received authorisation under Article 14 of the Solvency II Directive from the appropriate regulator; and

(b) as regards any policy which is included in the proposed transfer and which evidences a contract of insurance (other than reinsurance), the contract was concluded in an EEA State other than the United Kingdom."

The remaining sub-paragraphs 1(3), 1(4) and 1(5) of Schedule 12 deal with transferors which have been authorised under Article 162 of Solvency II. That Article relates to branches of insurers with head offices outside the EU and is therefore not applicable to Royal London.

48. Paragraph 2 of Schedule 12 FSMA is a certificate as to the margin of solvency of the transferee, to be given by the appropriate regulator and taking into account the scheme. In the instant case, such a certificate was duly given by the Central Bank of Ireland in relation to RLI on 11 January 2019.

49. Paragraphs 3 and 3A of Schedule 12 provide for the provision of certificates as to consultation and consent respectively.

"*Certificates as to consultation*

3. A certificate under this paragraph is one given by the appropriate regulator and certifying that the host State regulator has been notified of the proposed scheme and that—

(a) that regulator has responded to the notification; or

(b) that it has not responded but the period of three months beginning with the notification has elapsed.

> *Certificates as to consent*
>
> 3A. A certificate under this paragraph is one given by the appropriate regulator and certifying that in respect of each contract concluded in an EEA State other than the United Kingdom the authority responsible for supervising persons who effect or carry out contracts of insurance in the EEA State in which that contract was concluded has been notified of the proposed scheme and that –
>
> (a) the authority has consented to the proposed scheme; or
>
> (b) the authority has not responded but the period of three months beginning with the notification has elapsed."

50. These provisions should be read against the background of Article 39 of Solvency II, the relevant part of which provides,

> "*Transfer of portfolio*
>
> 1. Under the conditions laid down by national law, Member States shall authorise insurance and reinsurance undertakings with head offices within their territory to transfer all or part of their portfolios of contracts, concluded either under the right of establishment or the freedom to provide services, to an accepting undertaking established within the Community.
>
> Such transfer shall be authorised only if the supervisory authorities of the home Member State of the accepting undertaking certify that after taking the transfer into account the accepting undertaking possesses the necessary eligible own funds to cover the Solvency Capital Requirement referred to in the first paragraph of Article 100.
>
> 2. In the case of insurance undertakings paragraphs 3 to 6 shall apply.
>
> 3. Where a branch proposes to transfer all or part of its portfolio of contracts, the Member State where that branch is situated shall be consulted.
>
> 4. In the circumstances referred to in paragraphs 1 and 3, the supervisory authorities of the home Member State of the transferring insurance undertaking shall authorise the transfer after obtaining the agreement of the authorities of the Member States where the contracts were concluded, either under the right of establishment or the freedom to provide services.
>
> 5. The authorities of the Member States consulted shall give their opinion or consent to the authorities of the home Member State of the transferring insurance undertaking within three months of receiving a request for consultation. The

> absence of any response within that period from the authorities consulted shall be considered as tacit consent."

51. Apart from the certificate of solvency required by Article 39(1), the only requirement for consent from the authorities of other Member States arises under Article 39(4). That requirement for consent only applies to the authorities of other Member States in which the contracts were concluded, either under the right of establishment or the freedom to provide services. In context, this must refer to the conclusion of the contracts which are to be transferred by the transferor. The added requirement in Article 39(3) to consult the authorities of the Member State of a branch of the transferor which is transferring contracts does not, of itself, lead to any requirement for consent independently of Article 39(4). On any view, therefore, there is no requirement to obtain the consent of the authorities of Member States where no transferring contracts have been concluded by the transferor.

52. Article 39(5) is designed to provide a timeframe of three months for the giving of an opinion by a regulator of a branch which is consulted under Article 39(3), and the giving of consent as required by Article 39(4). But because Article 39(3) does not of itself require any consent to be given by the foreign regulator of a branch, the provision as to tacit consent in the last sentence of Article 39(5) must be limited to the requirement for consent under Article 39(4).

53. As I see it, therefore, paragraph 3 of Schedule 12 FSMA has gone further than required by Article 39(3) of Solvency II, in not only requiring the PRA to certify that the foreign regulator of a branch which is transferring policies has been consulted, but also requiring it to certify whether or not a response has been given within three months.

54. So far as paragraph 3A of Schedule 12 FSMA is concerned, as I read it, the PRA certificate is only required to deal with the giving of consent or the absence of a response from Member States in which transferring contracts have been concluded by the transferor. Obviously, the giving of express consent would satisfy paragraph 3A(a). I also consider that the PRA would be entitled to treat a response which implicitly consented to a scheme as falling within paragraph 3A(a).

55. As far as the provision deeming the absence of any response to be tacit consent is concerned, I consider that this should be read purposively to mean that tacit consent can be inferred where there has been no response addressing the question of consent. Specifically, a mere acknowledgment of receipt of the notification (whether by email or letter) would not, of itself, amount to a response within the meaning of paragraph 3A(a).

56. In forming my views of the interpretation of paragraphs 3 and 3A, my attention was drawn to the decision of Norris J in Commercial Union Life Assurance Co [2009] EWHC 2521. At paragraphs [90]-[91] Norris J held that the fact that a foreign regulator was still consulting within its own jurisdiction as regards a transfer scheme did not prevent the FSA from giving the appropriate certificate under paragraph 4(b) of Schedule 12 to the effect that the regulator had been consulted, and the period of three months from the giving of the notification had elapsed and the authority concerned had not refused its consent. As I read it, Norris J's decision turned on the specific wording of paragraph 4 which is in different terms to the wording of paragraphs 3 and 3A of

Schedule 12. I therefore do not gain any assistance from that decision in the instant case.

The inquiries and replies

57. Turning to the facts of the instant case, the PRA has provided a certificate pursuant to paragraph 3 of Schedule 12 to the effect that it has notified the supervisory authority in Ireland of the proposal to transfer certain long-term insurance business of Royal London pursuant to the Scheme and the Irish supervisory authority has responded. To the extent that the Scheme proposes to transfer policies of the Irish branch of Royal London, that certificate plainly satisfies paragraph 3.

58. So far as paragraph 3A of Schedule 12 is concerned, it appears that the PRA wrote to all EEA regulators more than three months ago, notifying them of the proposed Scheme and seeking their consent to it. Mr. Weitzman QC told me that this is the PRA's standard practice where it cannot be certain of the place where each of the transferring policies were concluded.

59. The result was that a number of the regulators wrote back, consenting to the Scheme; this category included in particular Ireland and Germany. Others did not respond in any way, shape or form. In relation to each of these categories, the PRA gave a certificate under sub-paragraphs (a) or (b) of paragraph 3A. If paragraph 3A was engaged on the facts in relation to those Member States, that certificate clearly satisfied the statutory requirement.

60. The issue that has arisen (which Mr. Weitzman QC told me was not uncommon where the PRA adopts its standard practice of contacting every EEA regulator), is that the remaining regulators replied in a variety of ways and the PRA has not provided any certificate under paragraph 3A in relation to such Member States. In particular,

    i) two of the regulators (Finland and Iceland) wrote back simply acknowledging notification had been received, but no further communication was received;

    ii) the Italian regulator wrote back to the effect that it could not express an opinion on the Scheme but awaited confirmation that it had been sanctioned;

    iii) the Romanian regulator wrote back, observing that if Romania was the State of the commitment underlying the insurance contract, then it would give its consent provided that the interests of policyholders, contracting parties and beneficiaries were fully protected, and asking that the PRA inform it of the Scheme being sanctioned; and

    iv) the Spanish regulator expressed the opinion that its consent was not necessary because neither Royal London or RLI were authorised to operate in Spain, and that although it appeared that some of the policyholders now lived in Spain, the policies in question were subject to UK law.

61. The correspondence with the French regulator was more extensive. The French regulator first wrote back to the PRA to note that RLI was not registered on its database and that it was waiting for notification from the Central Bank of Ireland to register RLI. It then referred to Article 39(5) of Solvency II and stated,

> "Please note that our consent to this transfer is conditional on your answers. We believe that the 3-month period is not running at the moment.
>
> We consider that this period of 3 months doesn't begin to run until we have had the necessary clarifications from you on this transfer operation; the deadline is therefore suspended for the moment."

62. Subsequently, the French regulator wrote another email referring to a provision as to profit-sharing imposed upon French life insurers under the French Civil Code and stating that it would wish to see RLI comply with this provision as regards contracts written with French policyholders after the transfer.

63. The PRA responded,

> "The company would like to know whether having written no business in your jurisdiction and with no intention to write business there in the future, but with some transferring policyholders now having an address there, will it be necessary for RLI to apply for a passport?"

64. The French regulator then responded that as it understood matters, the transfer would include "French commitments" and that RLI therefore needed to apply for a passport. As a result, the Central Bank of Ireland wrote to the French regulator on 29 January 2019 notifying it in accordance with Article 148(1) of Solvency II, of the intention of RLI to write class 1 and 3 insurance business on a freedom of services basis in France.

Analysis

65. Taking these six replies together, as an overarching point I simply do not think that paragraph 3A of Schedule 12 is engaged in relation to any of these Member States. Whatever might have been the PRA's reason for writing to every EEA regulator, there is simply no evidence to suggest that any of the policies being transferred under the Scheme were concluded in any of these six Member States. The evidence is that the transferring policies were all written from the Irish or German branches of Royal London, or by one of its predecessors in those jurisdictions. Although it might be that some policyholders have addresses in other Member States, that is not the test for the application of paragraph 3A. It might, for example, simply reflect the fact that the policyholder moved after taking out his policy.

66. I therefore do not require any additional certificate from the PRA under paragraph 3A in relation to the six member States referred to above.

67. In any event, even if paragraph 3A were applicable, I ought to record that on the basis of my interpretation of paragraph 3A, I consider that it could have been satisfied in relation to each of the six Member States referred to above.

68. Finland and Iceland simply made no substantive response on the question of consent, so the presumption of tacit consent would apply to them given the passage of over three months since notification. The same can, I believe, be said of the Spanish regulator,

which, after (correctly) pointing out that its consent was not necessary, made no other substantive response.

69. The Italian regulator can be taken implicitly to have consented to the Scheme given its request to be notified when the Scheme had been sanctioned, as did the Romanian regulator having indicated that it would consent if the interests of policyholders, contracting parties and beneficiaries were protected: that requirement is satisfied by the Part VII process.

70. Finally, taken as a whole, I consider that the communications with the French regulator amount to the giving of implicit consent to the Scheme. The French regulator essentially indicated that its consent was conditional upon being satisfied as to the ability of RLI to service what it described as the "French commitments" which were being transferred. As I understand matters, the Central Bank of Ireland has now done all that is necessary under Article 148(1) for RLI to perform such activities under the freedom of services basis with any transferring policyholders who are now resident in France. To the extent that the French regulator referred to what it would like to see written into policies concluded by RLI with French citizens after the transfer, that is obviously not a matter that relates to the giving of consent for the transfer of existing policies and can, I consider, therefore be ignored for the purposes of paragraph 3A.

The reports of the Independent Expert

71. The Independent Expert in this case is Mr. Tim Roff, a partner at Grant Thornton LLP and is a Fellow of the Institute and Faculty of Actuaries. He has over 30 years' experience in the life assurance sector including acting as Independent Expert on a number of Part VII transfers. His appointment as Independent Expert has been approved by the PRA, as has the form of his reports.

72. Mr. Roff has produced a very detailed and impressive report, together with a supplementary report and up-date letters in which he has examined the effect of the Scheme on the security of benefits, benefit expectations, regulatory governance and service standards of the three groups of policyholders concerned – those transferring to RLI, those remaining at Royal London, and those who have taken policies out recently with RLI in Ireland.

73. I do not consider it necessary to summarise the reasoning in Mr. Roff's reports in any detail in this judgment. I will simply say that I see no reason to doubt any of his conclusions which are conveniently summarised in an executive summary as follows:

> "1.16 I am satisfied that the implementation of the proposed Scheme with the New Reinsurance Arrangements and Security Arrangements will not have a material adverse effect on the security of the benefits or the future benefit expectations of Transferring Policyholders, Remaining Policyholders or Existing Policyholders.
>
> 1.17 It is also my opinion that the Transfer will have no material adverse effect on the governance or service standards experienced by the Transferring Policyholders, the Remaining Policyholders, or the Existing Policyholders.

1.18 In forming these conclusions, I have taken into account the loss of the FSCS protection that many policyholders in the Transferring Business benefit from. The FSCS provides protection to policyholders in the event of insolvency or default of UK based insurers or EEA branches of UK based insurers. After the Transfer, the policyholders of the Transferring Business will hold policies with an Irish based insurance company and therefore those that are currently entitled to FSCS protection will lose this entitlement. There is no equivalent to the FSCS in Ireland for long-term insurance business. The purpose of the Scheme is to effect the transfer of the transferring Business from Royal London to RLI, in order to enable the continued servicing (e.g. receiving premiums and paying claims) of the Transferring Business, regardless of the outcome of the Brexit negotiations. In my opinion, having certainty that policies in the Transferring Business can continue to be serviced lawfully after Brexit is very important. The loss of FSCS protection is an unavoidable consequence of achieving this certainty. In addition, I have considered that the FSCS provides protection to covered policyholders following an insolvency or default event. Given that RLI will be well capitalized and will be required to comply with the Solvency II Directive ("Solvency II") in EU law, the likelihood of default or insolvency of RLI is, in my opinion, remote….

1.19 The New Reinsurance Agreements and Security Arrangements form an important part of the Transfer as they are being put in place to ensure that the Scheme does not result in the need to split the Royal Liver Sub-Fund or manage the German Bond Business in a way which is materially different to the current management of these policies. It is my opinion that the New Reinsurance Agreements allow the with-profit policyholders in the German Bond Business and Ireland Liver Business to continue to benefit from the funds to which their policies are currently allocate. Further, the Security Arrangements provide appropriate security for RLI in the unlikely event that Royal London fails to meet its obligations under the Reinsurance Arrangements or becomes insolvent. The New Reinsurance Agreements also largely align RLI's interests with those of the direct policyholders of Royal London in relation to the distribution of assets in the extremely unlikely event that Royal London becomes insolvent.

1.20 In the event that the New Reinsurance Agreements are terminated in future, I am satisfied that the Scheme, the New Reinsurance Agreements and the Security Arrangements provide adequate protection to policyholders, to ensure that they will be treated fairly.

> 1.21 I am also satisfied that there will be no material adverse effect as a result of the Transfer on the reinsurers of Royal London whose contracts cover the Transferring Business."

Policyholder communications

74. In excess of 612,740 policyholder packs were sent out in addition to the other publicity for the Scheme. As of a few days ago, 60,672 communications had been received in response, but only 16 (or 0.2% of communications from policyholders) could be categorised as voicing any objection. No policyholders appeared at the hearing to object to the Scheme. I should, however, deal with the broad themes of the concerns expressed by policyholders.

75. The majority of policyholders were concerned about the financial stability of RLI and the loss of FSCS protection. These were matters dealt with extensively by Mr. Roff in his reports, leading to his conclusions which were summarised in paragraphs 1.18 and 1.19 of his first report (above).

76. As I have indicated above, the New Reinsurance Agreements and Security Agreements will form the basis for RLI's ability to meet (and exceed) its relevant SCR and other metrics under Solvency II. It is therefore essential that those arrangements are legally and commercially robust.

77. When I inquired into those arrangements at the hearing, I was told by Mr. Weitzman QC that the PRA was aware that the documents comprising the New Reinsurance Agreements and Security Arrangements had been reviewed by the Central Bank of Ireland in its capacity as Irish regulator of RLI, because, as I have indicated above, the obligations owed to RLI under such arrangements represent the bulk of RLI's regulatory capital for Solvency II purposes. Mr. Weitzman QC also told me that the arrangements had been reviewed in-house by the PRA.

78. Draft opinion letters have also been prepared which are addressed to RLI and to the Central Bank of Ireland by Pinsent Masons in respect of the validity and effectiveness of the Security Arrangements under English law, and by Matheson, Solicitors in Dublin, as to their recognition and enforceability under Irish law. The PRA was also provided with a copy of the draft letter from Pinsent Masons. The draft opinion letters will, I was told, be signed and delivered when the Scheme and relevant documents are sanctioned and executed in final form; and for my part I proceed on the basis that this will be done. The Security Arrangements were also the subject of advice given to the Independent Expert by Barry Isaacs QC, who concluded that, although untested in an insolvency event, he was satisfied that the relevant provisions would operate as intended.

79. I have seen no reason in the materials to question any of these opinions or to doubt the basis upon which it is intended that the New Reinsurance Agreements and Security Arrangements will operate. I therefore do not consider it necessary (or practical on a hearing such as this) to investigate such matters further.

80. So far as the loss of FSCS protection for some 22% of the transferring policyholders is concerned, it appears to me that this is most unlikely to lead to any material prejudice

in practice. For the reasons that I have set out, and Mr. Roff explains at length in his reports, the prospect of Royal London or RLI becoming insolvent is remote. The possibility that some transferring policyholders might lose FSCS protection in that remote situation is more than outweighed by the risk of real and immediate prejudice to transferring EEA policyholders if the Scheme were not to be implemented and there were to be a "no-deal" Brexit with the result that such policies could not be serviced (which might include claims not being paid). In essence, therefore, I accept the opinion of the Independent Expert on this point. For its part, the PRA also accepted that it was "not unreasonable" for Mr. Roff to take this view, and pointed out that there was no alternative jurisdiction in the EEA to which the policies might be transferred that offered any equivalent protection to the FSCS.

81. Three policyholders apparently complained that the Scheme did not allow them to opt-out, so that their policies would not be transferred. The result would be that they would thereby take the risk that their policies would not be capable of being administered in the event of a "no-deal" Brexit. A fourth suggested that the transfer should not go ahead at all whilst there was still uncertainty over the terms of Brexit or even whether it would happen at all.

82. In my view Mr. Moore QC provided the answer to these points. He submitted, and I accept, that it would not have been possible (or at least would have been highly impracticable) to design a scheme, for RLI to apply for its necessary authorisations in Ireland, and for RLI to make the necessary arrangements for the conduct of its future business, if it were uncertain what proportion of EEA policyholders would be transferring and which would not be transferring due to the availability of an opt out.

83. Mr. Moore also submitted that it was a reasonable and responsible approach for Royal London to have decided not to wait any longer to implement the Scheme given the current uncertainties. That was also the view of the Independent Expert and the PRA. Mr. Roff commented,

> "Given that there are no certainties over the terms of Brexit, it is important that Royal London take steps to ensure that they are certain that the Transferring Business can be lawfully serviced post-Brexit. Given the length of time it takes to implement Part VII transfers it is not possible to wait and see what the outcome of the Brexit negotiations are, and Royal London has been required to take steps in advance of the terms of Brexit becoming clear."

And, as set out above, the PRA stated that,

> "...it is not unreasonable for Royal London to take the view that the time has now been reached when it should proceed with the present Part VII transfer in order to achieve certainty."

84. Other objections concerned the allocation of a disproportionately large part of the costs of the Scheme to the Royal Liver Sub-Fund and the potential impact of the Scheme on the future profits of the transferring policies.

85. The one-off costs of the Scheme are estimated to be £21 million, and it is proposed that this sum be allocated approximately equally between the Royal Liver Sub-Fund (£9.6 million) and the Royal London Main Fund (£11.4 million). The incremental ongoing costs will be about €2.1 million higher, of which €2 million will in essence be shared between the remaining Royal Liver Sub-Fund and the Liver Ireland Sub-Fund, and €0.1 million relating to the German Bond business to the Royal London Main Fund.

86. I am satisfied, as was the Independent Expert, that, though high, these costs of the Scheme are an unavoidable consequence of the need to provide service continuity for transferring policyholders post-Brexit. I am also satisfied that the basis for their allocation between policyholders (both transferring and non-transferring) is fair and in accordance with the PPFM for Royal London's relevant funds.

87. As to the potential impact of the Scheme on future profits, I have explained that the New Reinsurance Agreements are designed essentially to produce the same results for the with-profits policyholders in the transferred business as if they had not left Royal London, and the Independent Expert has concluded, after a thorough analysis that there should be no material change for transferring policyholders so far as financial benefits is concerned. The Independent Expert has also opined that the future ProfitShare rates for eligible holders of German Bonds will not be materially affected as a consequence of the transfer, and I see no reason to doubt his conclusion.

Conclusion

88. Returning to the principles that I set out above as regards the exercise of discretion, it is worth reiterating that this is not a Scheme that Royal London has chosen to implement for its own commercial purposes. It has been forced to do so by the continued uncertainties over Brexit. In the absence of any agreement between the UK and the EU in relation to the ability of UK institutions to conduct financial services business in the EEA after Brexit, the board of Royal London have taken the entirely reasonable decision to propose the Scheme to be certain that their EEA policyholders will be able to be serviced after the UK leaves the EU. That is obviously a vital consideration for those transferring policyholders, many of whom bought their policies in Ireland in the first place.

89. As I said in AIG, the current uncertainty over Brexit means that there may be no perfect solution for the holders of the policies being transferred. The possibility that some individual policyholders or groups of policyholders are required to run a risk of being adversely affected in certain respects does not mean that the Scheme necessarily has to be rejected by the Court. The fundamental question is whether the proposed Scheme, as a whole, is fair as between the interests of the different classes of persons affected.

90. On the evidence, the transferee, RLI, is duly authorised, and has the benefit of reinsurance and security from Royal London to enable it to carry on the business to be transferred to it in Ireland. I have the assurance of a detailed and comprehensive series of reports from the Independent Expert that the Scheme will cause no material prejudice to transferring policyholders, to those who are left behind in Royal London or to the existing policyholders of RLI. In particular, and in common with the Independent Expert and the PRA, I regard the potential loss of FSCS protection for some transferring policyholders as being a largely theoretical risk, as against the very real prejudice that

all EEA policyholders would face in the event of a “no-deal” Brexit if the Scheme were not implemented.

91. In conclusion, the statutory requirements have been met, and having regard to all the circumstances that I have outlined, I am satisfied that Scheme is one that I should exercise my discretion to sanction.