Report on the Transfer of the UK business from AMT Mortgage Insurance Ltd to AmTrust Europe Ltd

Independent Expert Report of Michael Tripp FIA

25 February 2019

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Contents

1.	Introduction	4
2.	Executive Summary	8
3.	Scope	12
4.	Methodology	14
5.	Background	17
6.	Regulatory background	22
7.	Claims and premium reserves	24
8.	Policyholder security	33
9.	Other considerations	50
10.	Conclusions	58
Appendix A: Glossary		60
Appendix B: Extract from engagement letter		64
Appendix C: My experience		66
Appendix D: Relationships with affected companies		67
Appendix E: Reserving methods		68
Appendix F: Summary of information received		70
Appendix G: Standard Formula Appropriateness for AMIL		72
Appendix H: Reliance and Limitations		73
Appendix I: Methodology		75
Appendix J: Benchmarking		76
Appendix K: Standard Formula Appropriateness for AEL		78
Appendix L: Reserving		83
Appendix M: Analysis of Risks and Risk Mitigants		92
Appendix N: Post-Transfer balance sheet		94

1. Introduction

1.1 Section 109 of Financial Service and Markets Act 2000 ("FSMA") requires that a scheme report must accompany an application to the High Court of England and Wales ("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 approved by the Prudential Regulation Authority ("PRA"), in consultation with the Financial Conduct Authority ("FCA"). The scheme report should address the question of whether any policyholders impacted by the insurance business transfer are adversely affected.

1.2 AMT Mortgage Insurance Limited ("AMIL") and AmTrust Europe Limited ("AEL", "AmTrust") have jointly nominated Michael Tripp ("I", "me") of Mazars UK LLP ("Mazars", "us", "we") to act as the Independent Expert for the proposed insurance business transfer scheme ("the Transfer") of the entire insurance business of AMIL to AEL. The Transfer is intended to be effected on 30 April 2019 ("the Effective Date").

1.3 My appointment was approved by the PRA in consultation with the FCA on 12 December 2017.

1.4 This report describes the proposed Transfer and discusses its possible effects on the policyholders of AEL and AMIL including its effect on policyholder security and levels of service.

1.5 AEL and AMIL are UK registered companies regulated by the PRA.

1.6 AEL was established in 1975 and underwrites general insurance business. The company operates 8 underwriting teams: Liability, Property, Legal Expense, Special Risk, Medical Malpractice, Professional Indemnity, Mortgage & Credit and Accident & Health. The policyholders are a mix of retail consumers, small to medium-sized enterprises ("SME's") and corporates.

1.7 AMIL is a wholly owned subsidiary company of AEL, established in 1991. The entire issued share capital of AMIL was sold by Genworth Mortgage Insurance Corporation to AEL on 9 May 2016. AMIL is the parent company of AMT Mortgage Services Limited ("AMT MSL"), a wholly-owned service company. As AMT MSL is not part of the proposed transfer, I do not consider AMT MSL further in this report.

1.8 AMIL provides mortgage insurance policies which insure mortgage lenders against the risk that a borrower defaults on their mortgage and the secured property is sold at a price which does not cover the value of their mortgage. The policyholders are regulated, financial institutions located around the EU and the UK.

1.9 The terms of my engagement are set out in a letter dated 23 January 2018. An extract of this letter can be found in Appendix B. Please note that on 10 September 2018 AmTrust informed us that the original proposed transfer has been amended, owing to the changing Brexit outlook, for instance, AmTrust does not want to transfer the AMIL's EU risk into AEL only to transfer it out again for Brexit. Therefore, the Transfer only transfers the UK business of AMIL into AEL.

Layout of this report

1.10 My report is structured as follows:

- Section 1 provides an introduction to the Transfer.
- Section 2 is an executive summary of this report and my approach and describes my conclusions.
- Section 3 sets out the scope of this report.
- Section 4 provides a summary of the methodology and my approach to assessing the Transfer.
- Section 5 describes the background and structure of the entities involved.
- Section 6 describes the regulatory background.
- Section 7 describes the claims and premium reserve of the portfolios.
- Section 8 describes the effect of the Transfer on each group of policyholders with regards to security.
- Section 9 provides my assessment of other policyholder considerations.
- Section 10 sets out my conclusions on the Transfer.

Professional experience

1.11 I am a Fellow of the Institute and Faculty of Actuaries ("IFoA") and a member on the Council of the Institute and Faculty of Actuaries.

1.12 I am the Head of Actuarial at Mazars UK LLP and have more than 35 years' experience in general insurance. Prior to joining Mazars in 2013, I was Group Chief Executive Officer at Ecclesiastical Insurance and also held senior roles at E&Y and Watson Wyatt.

1.13 In particular, I have experience in Mortgage Indemnity business, through underwriting it at Guardian Royal Exchange in the 1990s, and Part VII transfers through work as Chair of Ecclesiastical Life Insurance overseeing a transfer to Engage Mutual. Also, I have experience reviewing and advising the audit partners on the adequacy of the actuarial reserves of audit clients who have substantial medical malpractice books both in the UK and Italy, similar to those held by AEL.

1.14 Full details of my experience can be found in Appendix C.

Independence

1.15 I can confirm I have no financial interest in any of the companies involved in the Transfer. I have not previously advised any of the companies involved on any significant project.

1.16 Partners and staff of Mazars have advised, and may advise, the companies on various assignments, for example, tax and delegated authority reviews. However, we have not acted as external auditor or performed any regulatory roles, and have not provided any advice concerning the development of this Transfer.

1.17 I do not believe that any previous assignment would compromise my independence, create a conflict of interest or compromise my ability to report on the proposed Transfer.

1.18 I can confirm that the contribution of AmTrust and its subsidiaries to Mazars' global fee income has not exceeded 1% over the last 3 years.

1.19 The costs associated with my appointment as Independent Expert and the production of this report will be charged to AmTrust Europe Limited.

1.20 Details of the relationships of Mazars with AmTrust are contained in Appendix D to this report. This also sets out why I do not believe any of these relationships to impair my independence to act as the Independent Expert on the Transfer.

Use of this report

1.21 The purpose of this report is to inform the Court of the likely effect of the Transfer upon policyholders. This report is not necessarily suitable for any other purpose.

1.22 A copy of this report will be made available to the Court, the PRA, the FCA and the boards of directors of AEL and AMIL, and any other person entitled to receive a copy under the FSMA Regulations.

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

1.24 In my discussion of the effects of the proposed Transfer on the companies concerned, I use various technical terms. The definitions of these terms as used in this report are contained in Appendix A.

1.25 I make reference throughout this report to financial items or events that are material or immaterial. I consider an event immaterial if the expected impact of the event is very small, such that it would not influence the decisions of a reader, either on its own or in conjunction with other immaterial events.

Professional guidance

1.26 As an Independent Expert reporting to the Court, I am required to act in accordance with Part 35 of the Civil Procedure Rules, Practice Direction 35 and the Guidance for the Instruction of Experts in Civil Claims. Accordingly, this report is prepared for the assistance of the Court and I confirm that I understand my duty to the Court overrides any obligations I have to those instructing me and/or paying my fee. I confirm that I have complied with this duty.

1.27 This report has been prepared under the terms of the Statement of Policy produced by the PRA in April 2015, namely "The Prudential Regulation Authority's approach to insurance business transfers" and the guidance set out in Chapter 18 of the Supervision Manual ("SUP18") contained in the FCA Handbook of Rules and Guidance to cover scheme reports on the transfer of insurance business.

1.28 I have also taken account of the guidance set out in the FCA's final guidance on its approach to the review of Part VII insurance business transfers, FG18/4.

1.29 In my opinion, this report has been produced in line with the requirements of the Technical Actuarial Standards ("TASs") issued by the Financial Reporting Council ("FRC"). In particular, this report has been prepared in accordance with TAS 100: Principles of Technical Actuarial Work and TAS 200: Insurance.

1.30 This report has also been produced in line with the requirements of Actuarial Professional Standard ("APS") X2: Review of Actuarial Work; and APS X3: The Actuary as an Expert in Legal Proceedings produced by the Institute and Faculty of Actuaries. See paragraph 3.12 for more details on the peer review process.

2. Executive Summary

Overview of the Transfer

2.1 This report considers the impact of the Transfer of the UK insurance business of AMIL to AEL.

2.2 The existing policyholders of AEL are a mix of retail consumers, SME's and corporates. The company operates 8 underwriting teams: Liability, Property, Legal Expense, Special Risk, Medical Malpractice, Professional Indemnity, Mortgage & Credit and Accident & Health.

2.3 AMIL provides mortgage insurance policies which insure mortgage lenders against the risk that a borrower defaults on their mortgage and the secured property is sold at a price which does not cover the value of their mortgage. The policyholders are regulated, financial institutions located around the EU and the UK.

2.4 The main aim of the Transfer of the UK business of AMIL in to AEL is to simplify the corporate structure of the AmTrust Group. This is the first step of the overall strategy to simplify the corporate structure. Other steps including the Transfer of the other non-Italian business of AMIL to AmTrust International Underwriters (Ireland), and the Transfer of AMIL's Italian business directly into an Italian entity.

2.5 AEL has permission under Part 4A of FSMA to write insurance business of all the classes of business being transferred in to it. This is confirmed in the Financial Services Register.

2.6 As a consequence of the Transfer, a small portion of the assets and liabilities of AMIL that relates to its UK business will transfer to AEL.

2.7 If the Transfer had taken place on 31 December 2017, AEL would have received net assets on a Solvency II basis with an estimated value of £1.4m from AMIL. The capital coverage ratio of AMIL of 174% remains the same post-Transfer. The value of net assets of AEL on a Solvency II basis as at 31 December 2017 was £352.4m and this would remain the same post-Transfer. Please note that, as AMIL is a subsidiary of AEL, it already contributes to AEL's value. AMIL's net asset value is calculated using the adjusted equity method.

2.8 In addition to the proposed Transfer of the UK business of AMIL in to AEL, AmTrust propose a transfer of Pedigree Livestock Insurance Ltd ("PLI") business in to AEL which it is proposed will be heard by the Court and become effective at or around the same time as the Transfer. PLI is also a wholly owned subsidiary of AEL, however the two transfers are not conditional on one another. The Transfer of PLI is reviewed independently in the report titled "Report on the Transfer of business from Pedigree Livestock Insurance Ltd to AmTrust Europe Ltd". See Appendix N for the combined post-Transfer company balance sheet assuming that the two Transfers happened in parallel.

My approach

2.9 My approach to assessing the likely effects of the Transfer on policyholders is first to:

- Understand the structure of the Transfer and the businesses of the companies involved;
- Identify the groups of policyholders that would be affected; and
- Assess the financial position of the companies involved.

2.10 The above stages are contained in Sections 3 to 7 of the report. Having identified the effects of the Transfer on the various companies and businesses, I consider the following in Sections 8 and 9.

- Consider implications of the Transfer on security provided to the affected policyholders;
- Consider other factors that might affect the policyholders; and
- Consider the implications of the Transfer on reinsurers.

2.11 In order to consider the effect of the proposed Transfer on each of the entities and groups of policyholders concerned, I have been provided with comparative information for each legal entity, including:

- Balance sheet information based on figures as at 31 December 2017;
- Internal actuarial reviews for AEL and AMIL as at 31 December 2017;
- Estimates of the regulatory and economic capital required for each company as at 31 December 2017; and
- Internal management information.

2.12 The baseline data used is that as at 31 December 2017 as this was the most complete audited accounting information. The scope of the proposed Transfer is such that this data remains a valid baseline. The work underpinning this Report has taken place throughout 2018. I have been informed about AMIL's estimated up-to-date financial position and I am satisfied that the arguments and conclusions in this report based on 31 December 2017 data will remain the same.

2.13 I will issue a Supplementary Report prior to the final Court hearing reflecting the most up-to-date financial information available at that time.

Key assumptions

2.14 In conducting my analysis I have assumed the following:

- All existing UK policyholders of AMIL will become policyholders of AEL as a consequence of the Transfer;
- The Transfer is expected to be broadly tax neutral for AEL and AMIL (the "Transfer Companies");

- It is not planned that there will be any reduction in aggregate level of capital held, or any increase in insurance liability or risk exposure as an immediate consequence of the Transfer that would not have occurred were it not to proceed;

- The same level of assets and liabilities will exist within the Transfer Companies in aggregate after the Transfer as before the Transfer, when valued on the same accounting basis; and

- AEL will continue to operate and have no current intentions to cease underwriting.

- The non-UK policyholders of AMIL will remain in AMIL which will continue to operate until the transfers anticipated in paragraph 2.4 complete.

2.15 The above assumptions underlie the analysis and conclusions in this report. If these assumptions were to change, my opinion may also change. At the time of writing this report the above assumptions were the current intentions of the Transfer Companies.

Conclusions

2.16 The conclusions of my report are summarised in this section. The detailed explanation behind these conclusions follows in the body of this report.

2.17 I have identified the following groups of policyholders:

- the transferring UK policyholders from AMIL;

- the remaining other Non-UK policyholders from AMIL; and

- the existing policyholders of AEL.

2.18 With respect to transferring UK policyholders of AMIL, I do not expect any material adverse impact on policyholder security as a result of the Transfer. These policyholders would be moving to a larger entity with sufficient coverage of its capital requirements. I believe that following the Transfer, both AEL and AMIL with Non-UK policyholders will still be sufficiently capitalised such that the chance of insolvency is very low. Please see Section 8 for my analysis. The transferring UK policyholders of AMIL would benefit from access to AEL's credit rating and being a part of a much larger, diversified balance sheet.

2.19 However, I recognise that from an AMIL's UK policyholder security perspective there will be a change in the nature and type of risk to their security which AMIL UK policyholders are exposed. I believe that the greatest risk Pre-Transfer is the risk of a severe downturn in the Italian housing market which is where the majority of AMIL's risk exposure comes from. Post-Transfer, I believe their greatest risk would be a severe increase in claims from AEL's book of Italian medical malpractice business, however, noting that a subsequent Part VII Transfer is anticipated to occur of AEL's Italian medical malpractice business which, if and when completed, will remove this risk. Therefore there would be a change in the nature and type of risk to which AMIL UK policyholders are exposed. However, I do not believe this results in a material adverse impact on their overall security. This is discussed further in paragraphs 8.62 to 8.64.

2.20 With respect to the existing policyholders of AEL and the remaining Non-UK policyholders of AMIL, I do not expect any material adverse impact on policyholder security as a result of the Transfer. Please see Section 8 for my analysis.

2.21 There will be no impact on the pension arrangements for either AEL or AMIL as a result of the Transfer.

2.22 I am not aware of any planned changes to AEL's investment strategy as a result of the Transfer, therefore do not anticipate any adverse impact on the transferring portfolios as a consequence of the Transfer. In addition, governance arrangements such as the investment committee ("IC") are in place to ensure that appropriate decisions are made. Please see paragraphs 9.14 to 9.19 for more details.

2.23 I do not expect any material adverse impact to the three groups of policyholders resulting from changes from ongoing expense levels as a result of the Transfer.

2.24 I do not expect any material adverse impact to any Transferring UK policyholder of AMIL as a result of a change in management and governance framework following the Transfer. The existing AEL Committees and sub-Committees will remain the same post-Transfer. AMIL is a wholly owned subsidiary of AEL and therefore there is some commonality in the governance of the companies involved in the Transfer both in terms of practice and personnel. The existing Non-UK policyholders of AMIL will continue to benefit from the current governance arrangements post Transfer.

2.25 I expect no material adverse impact on the current and historic reinsurers of AMIL and AEL. Reinsurance contracts that cover the UK business of AMIL will novate to AEL from the effective date of the Transfer.

2.26 I conclude that I do not expect any group of policyholders or reinsurers to be materially adversely affected by the Transfer and therefore I see no reason why the Transfer should not proceed.

Expert's declaration

2.27 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 that I have expressed and conclusions that I have drawn represent my true and complete professional opinions on the matters to which they refer.

Michael Tripp FIA

Head of Actuarial, Mazars UK LLP

3. Scope

3.1 I am required as Independent Expert to consider the likely effects of the Transfer on policyholders, including whether the Transfer will result in material detriment to any policyholders affected by the Transfer, relative to their current situation. The purpose of this report is to set out my considerations. For the purposes of this report, policyholders include existing and future claimants.

3.2 Material detriment in the context of this report means any material adverse effect on the security of policyholders' contractual rights and the levels of service provided to policyholders.

3.3 My report considers the effect on the following groups of policyholders:

- the transferring UK policyholders from AMIL;
- the remaining other Non-UK policyholders from AMIL; and
- the existing policyholders of AEL.

3.4 Upon completion of the Transfer, it is expected that the Non-UK policyholders of AMIL will remain within AMIL until the transfers anticipated in paragraph 2.4 complete.

3.5 I am not aware of any alternative arrangements to the Transfer proposed by any party, so I have not considered it necessary to discuss alternative options within this report.

3.6 Shortly before the date of the Court hearing, I will prepare a Supplementary Report covering any relevant matters which have arisen since the date of this report.

Future changes of ownership

3.7 I have not considered any future changes of ownership of any of the companies involved in the Transfer. I am not aware of any proposals to change ownership at the time of writing this report.

Reliance on data

3.8 I have not audited nor have I independently verified the data and information supplied to me. However, I have reviewed it for reasonableness and for internal consistency. I assume AmTrust has been open and honest with me and had disclosed to me any facts and issues that I need to know as the Independent Expert. There is no evidence that there is any information missing.

3.9 I have checked that all the information I have been provided with has been supplied by persons appropriately qualified to provide such information. I had a number of meetings with senior management of AmTrust, including an interview with the Chief Executive Officer. Therefore, I am satisfied that it is reasonable for me to rely on this information.

3.10 A summary of the data provided to me can be found in Appendix F.

Exchange rates

3.11 The figures throughout this report are shown in sterling and, where necessary, have been converted at the following exchange rate:

- £1 = €1.126

This is the rate used by AmTrust as at 31 December 2017.

Peer review process

3.12 In accordance with the internal control processes of Mazars, the work documented in this report has been peer reviewed by a suitably qualified person: an Actuary within my own firm who has considerable experience working in Insurance who has been involved in Part VII Transfer processes and peer review for many years. The peer review process has also included review from a qualified actuary who specialises in the area of General Insurance.

4. Methodology

4.1 In this section, I describe my approach to assessing the Transfer.

4.2 My conclusions have been drawn by undertaking the following activities:

- Review of documentation received from AEL and AMIL;
- Discussions with key personnel at the Transfer Companies; and
- Undertaking my own analysis, where necessary. See Appendix I for a summary of my analysis and references to the relevant sections.

4.3 In particular:

- My view on insurance liabilities of AMIL is based on review of documentation and calculations provided to me by AMIL actuaries and discussions with the relevant individuals at AMIL.
- My view on policyholder security of AMIL is based on review of documentation and calculations provided to me by AMIL actuaries and discussions with the relevant individuals at AMIL as well as market benchmark.
- My view on insurance liabilities of AEL is based on review of documentation and calculations provided to me by AEL actuaries and discussions with the relevant individuals at AEL. This is further supplemented with my own analysis where I see necessary which is detailed in Section 7.
- My view on policyholder security of AEL is based on review of documentation and calculations provided to me by AEL actuaries and discussions with the relevant individuals at AEL as well as market benchmarks. In addition, I have carried out my own analysis where I see necessary which is detailed in Section 8.
- My view on contagion risk is based on review of documentation provided to me by AEL actuaries and discussions with the relevant individuals at AEL.

4.4 My approach to assessing the Transfer has been to perform the following specific activities.

Understand the nature and structure of the Transfer and identify the groups of policyholders that would be affected

4.5 I have discussed the structure and nature of the Transfer with AEL and reviewed the Scheme Document.

Assess the financial positions of AMIL and AEL

4.6 The level of security for policyholders depends on the available capital of the insurance company and the probability that this is sufficient enough to make claim payments as they fall due. Insurers must assess their own risks and solvency needs as well as comparing themselves to regulatory capital requirements. This is discussed further in Section 8.

4.7 I have compared the balance sheets of the companies involved as part of my assessment, on both accounting and regulatory bases as at 31 December 2017. This is discussed in Section 8.

Assess the claims reserves of AMIL and AEL

4.8 I have considered the claims reserves included on the balance sheet for each company as this is generally the largest part of an insurer's liabilities. This is discussed in detail in Section 7. I have focused my analysis on the UK Generally Accepted Accounting Practice ("UK GAAP") reserves as these are the basis of the Solvency II calculation as well as being used in the published financial statements. I have assessed the adequacy of the UK GAAP reserves both with and without margins added to the actuarial best estimate of the claims liability.

Assess the capital modelling undertaken and capital position of AMIL and AEL

4.9 I have considered the appropriate measure to use for assessing policyholder security. The choices available to me are risk capital measures, designed to ensure that an insurer is able to meet its obligations with a probability of at least 99.5% over 1 year, or to ultimate (defined as the time frame until all insurance obligations are paid):

- The Standard Formula ("SF") capital measure, which considers the capital required for AMIL and AEL to meet its obligations with a probability of at least 99.5% over 1 year, based on prescribed rules set by EU regulations (known as Solvency II) – I call it SF1;
- AMIL and AEL's own economic view of the capital required to meet its obligations with a probability of at least 99.5% over 1 year, calculated using their own economic capital model which has not been approved by any prudential supervisor – I call it EC1;
- or AMIL and AEL's own economic view of the capital required to meet its obligations with a probability of at least 99.5% to ultimate, calculated using their own economic capital model which has not been approved by any prudential supervisor – I call it IM ECu.

4.10 I have chosen the Solvency II Solvency Capital Requirement ("SCR") measured by the SF over the 1 year time frame i.e. SF1. I believe that the SF1 is the most suitable measure for assessing policyholder security for both AMIL and AEL. My reasoning is discussed in paragraphs 8.14 to 8.30.

Consider the impacts of the Transfer for the level of security being offered to each group of policyholders

4.11 I have considered the level of security available to each group of policyholders pre and post Transfer. This is discussed in Section 8.

Consider the potential impact on levels of customer service

4.12 I have considered how the level of customer service experienced by each group of policyholders could change following the Transfer, specifically claims handling and policy servicing. These are discussed in Section 9.

Consider other factors that might affect policyholders

4.13 I have considered other factors that might affect policyholders such as pension arrangements, tax implications, governance frameworks, contagion risk, etc. through discussions with AEL and reviews of documentation. These are discussed in Section 9.

Consider the implications of the Transfer for reinsurers

4.14 I have considered the implications of the Transfer on any transferring reinsurers and any existing reinsurers of the involved companies. This is discussed in Section 9.

5. Background

5.1 In this section, I provide background information on the companies involved in the Transfer, the types of business they write and their policyholders.

History of companies

AEL

5.2 AEL was founded in 1975 and is one of the UK registered subsidiaries of the ultimate parent company, AmTrust Financial Services Inc., a Delaware registered US Corporation. AEL's immediate parent is AmTrust International Limited, a holding company for most of the group's European insurance operations.

5.3 AEL underwrites general insurance business in the UK and other European countries. The company operates 8 underwriting teams: Liability, Property, Legal Expense, Special Risk, Medical Malpractice, Professional Indemnity, Mortgage & Credit and Accident & Health.

5.4 AEL has over one million policies in force across 23 European jurisdictions. Policyholders are a mix of retail consumers, SME's and corporates.

5.5 Table 5.1 provides an overview of the annual financial performance of AEL from 31 December 2015 to 2017, taken from the Financial Statements on a UK GAAP basis.

Table 5.1: AEL Annual Financial Performance

AEL (£million)	2017	2016	2015
Net Earned Premium	242.0	204.4	131.9
Profit/(Loss) before tax	68.8	66.6	41.8
Total Liabilities	1,575.8	1,595.3	1,321.1
Total Assets	1,958.2	1,888.4	1,560.2

AMIL

5.6 AMIL was founded in 1991 and is registered in the UK as a non-life insurance company. It is a wholly owned subsidiary of AEL and underwrites business across Europe, insuring mortgage lenders against the risk that a borrower defaults on their mortgage and the secured property is sold at a price which does not cover the outstanding value of their mortgage.

5.7 AMIL, formerly Genworth Financial Mortgage Insurance Limited, was acquired by AEL on 9 May 2016. Since its acquisition by AEL, mortgage insurance as a line of business has been written in AEL and other AmTrust Group companies. Therefore the Transfer of UK policyholders of AMIL in to AEL will lead to greater efficiencies for the group.

5.8 AMIL is the parent company of AMT Mortgage Services Limited ("AMT MSL"), (formerly Genworth Financial Mortgage Services Limited) a service company. The Transfer will have no impact on AMT MSL.

5.9 Table 5.2 provides an overview of the annual financial performance of AMIL from 31 December 2015 to 2017, taken from the Financial Statements on a UK GAAP basis. Figures are converted at the exchange rate given in paragraph 3.11. Assets and liabilities related to the UK business of AMIL will be transferred to AEL upon successful Transfer.

Table 5.2: AMIL Annual Financial Performance

AMIL (£million)	2017	2016	2015
Net Earned Premium	11.6	13.8	13.4
Profit/(Loss) before tax	3.6	0.1	(10.5)
Total Liabilities	81.5	99.6	111.4
Total Assets	153.3	216.9	229.9

5.10 The Transferring portfolio consists of all the UK policies that AMIL underwrote on or before the Transfer date. As at 31 December 2017 on a UK GAAP basis, the transferring portfolio has total liabilities of £4.73m and total assets of £4.51m. Therefore if the Transfer had taken place on 31 December 2017, AEL's net assets would have reduced by £223k.

5.11 On a Solvency II basis, the transferring portfolio has total liabilities of £1.4m and total assets of £2.9m. Therefore if the Transfer had taken place on 31 December 2017, AEL would have received net assets from AMIL with an estimated value of £1.4m. This reconciles with the balance sheet shown in Table 8.1.

5.12 The company is a mono-line insurer and writes solely business-to-business insurance products to lenders of mortgage loans, particularly designed for high loan-to-value mortgages. All policies are mortgage insurance policies which insure multiple loans under each. AMIL offers both "flow" insurance policies (which provide insurance on a loan by loan basis every month as notified to AMIL by the lender) and insurance on a back-book basis for a closed portfolio of loans.

5.13 As at 31 December 2017, AMIL has 11 current policyholders in the UK, of which 8 policyholders are issuing new mortgage loans covered by AMIL. Sums insured total £130m for 8,051 mortgages insured.

5.14 There have been a total of 898 loans benefitting from a claims payment on UK policies with in-force UK lenders. Claims are paid to policyholders either following a loss event such as foreclosure or on an offer of early claims payment by AMIL to the policyholder to settle mortgages in arrears for portions of a portfolio, or to commute an entire portfolio.

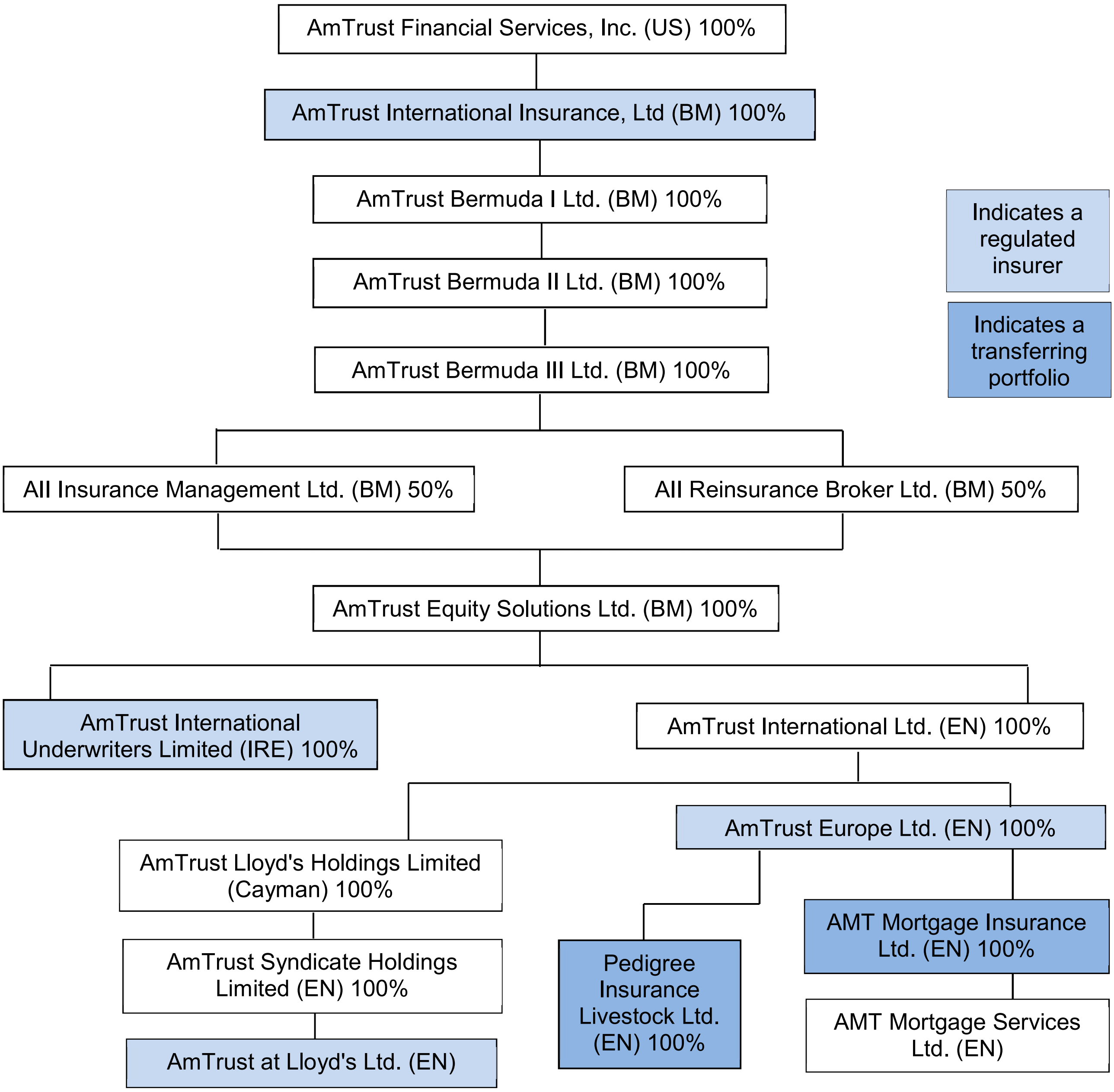
5.15 Total UK claims reserves booked as at 31 December 2017 are £107k net of reinsurance on 34 delinquent loans. Of those 34 delinquent loans, 23 are in respect of a remote excess of loss contract, where the likelihood of attachment is beyond a 1-in-200 year event, and therefore no reserves are held for these policies.

5.16 AMIL currently has two reinsurance programmes in place: a 33.3% quota share programme which is renewed annually by book year since 2011 and aggregate excess of loss arrangements specifically for the Italian book. AMIL's previous excess of loss arrangement covered 2010 and prior book years and was with AmTrust North America. This was put in place prior to the AmTrust acquisition of AMIL and has now lapsed. AMIL's current excess of loss arrangement covers 2011 to 2017 and is written with a third party. Their reinsurance programmes are covered by highly rated reinsurance companies. Reinsurance programmes that cover AMIL's UK business will novate to AEL as part of the Transfer. The impact of the Transfer on reinsurance is discussed further in Section 9.

Overview of structure

5.17 Figure 5.3 illustrates the structure of the business prior to the Transfer, showing relevant entities only. This includes the Transfer of the UK business of AMIL and PLI into AEL. AmTrust Financial Services Inc. is the ultimate parent company of all those involved in the Transfer.

Figure 5.3: Chart showing the structure of AmTrust

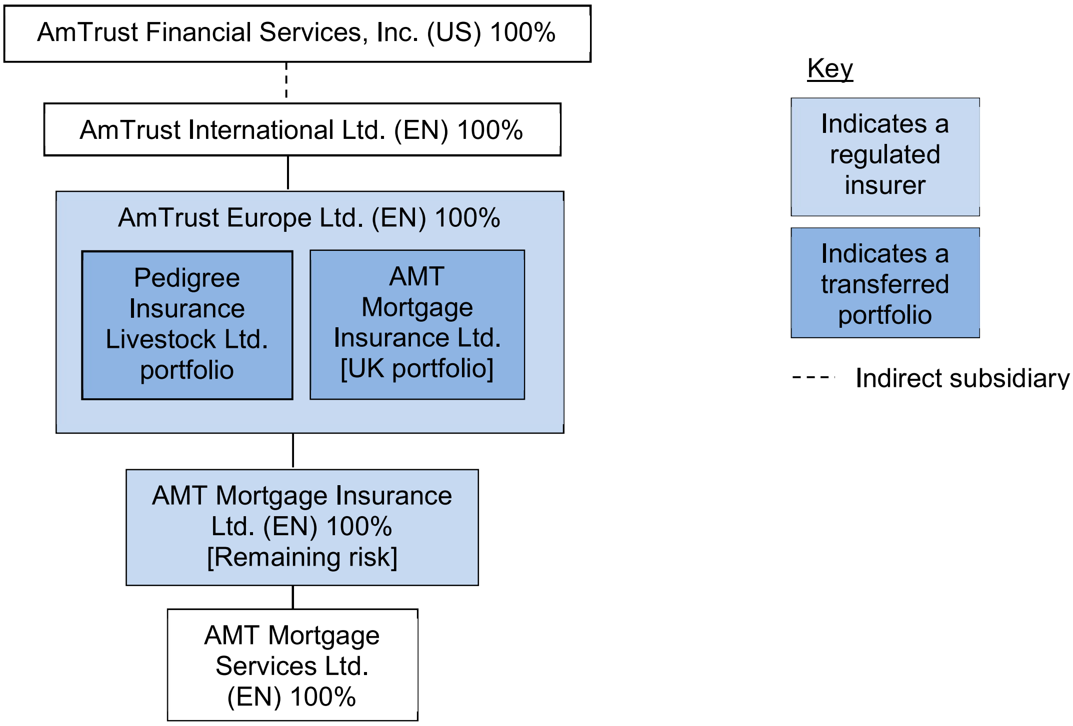


5.18 Some of the management team of AEL have dual roles and oversee both AEL and AMIL. Following the Transfer, the transferred UK business of AMIL will become a business line within AEL i.e. the Mortgage and Credit business line.

5.19 Figure 5.4 illustrates the proposed simplified structure of AmTrust International Ltd. following the Transfer, showing only the relevant companies; this includes the Transfer of the UK business of AMIL and PLI business into AEL, assuming both are successful.

5.20 I understand it is intended that PLI would be dissolved following a successful Transfer and once it has been duly de-authorised.

Figure 5.4: Chart showing the proposed structure of companies post Transfer



6. Regulatory background

6.1 This section provides some background on the regulatory requirements which are relevant to the Transfer.

6.2 The impact of any changes in regulation on the groups of policyholders are discussed in Section 9. However, the opinions provided in this report are based on my own analysis and not the regulators' views of the companies involved.

UK regulation

6.3 UK insurers are regulated by both the Prudential Regulation Authority ("PRA") and Financial Conduct Authority ("FCA"), statutory bodies set up under the Financial Services Act 2012. Prior to this, the Financial Services Authority ("FSA") undertook all regulation of financial services institutions.

6.4 The PRA is part of the Bank of England and regulates banks, building societies, credit unions, insurers and major investment firms. It has a general objective to promote the safety and soundness of the firms it regulates.

6.5 The FCA is a separate organisation with a general objective to ensure that the relevant markets function effectively. The FCA is responsible for conduct supervision and prudential supervision of UK firms. The FCA's main objectives are:

1. Consumer protection;
2. To improve the integrity of the financial system in the UK; and
3. To ensure that the market remains competitive in the best interests of customers.

6.6 The FCA's Principles for Business include the following statements that relate to the fair treatment of customers:

a. **Principle 6:** A firm must pay due regard to the interests of its customers and treat them fairly

b. **Principle 7:** A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading

c. **Principle 8**: A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client

d. **Principle 9:** A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely on its judgement.

Solvency II

6.7 The European Commission developed regulatory requirements for insurance and reinsurance companies within the EU known as "Solvency II" ("SII") and these were implemented on 1 January 2016.

6.8 Solvency II is a principles-based programme set around three pillars:

1. Financial requirements
2. Governance & Supervision
3. Reporting & Disclosure

6.9 Under Solvency II's financial requirements there are two thresholds: Solvency Capital Requirement ("SCR") and Minimum Capital Requirement ("MCR").

6.10 The SCR is the amount of capital required in excess of liabilities that must be held in order to ensure continued solvency over a one year time frame. It can be calculated using Standard Formula, or an Internal Model which has regulatory approval or other ways such as a Partial Internal Model.

6.11 The MCR defines the point of severe supervisory intervention, and is calculated as a linear function of specified variables.

6.12 Insurers are required to calculate the level of capital ("Own Funds") available to meet the SCR, requiring the calculation of a balance sheet according to Solvency II principles. The Own Funds are assessed and allocated into tiers in accordance with the Solvency II rules. Insurers are restricted in their use of lower tier assets to meet the SCR.

6.13 Claims reserves under Solvency II are held on a best estimate basis. This is to say that a provision has to be set up to cover the expected value of future claims. This is true of business where there is no further risk but all claims are not yet paid and also of business where the risk period has not yet expired. Insurers have to set up provisions for all possible future cash-flows (inwards and outwards). This is different to statutory accounting where claims reserves on business where the risk is not expired are held at a minimum of 100% of premium, which is called the unearned premium reserves ("UPR"). Furthermore, where the risk is expired but all claims are not fully paid, claims reserves must be set to cover the claims.

6.14 Under the Solvency II rules concerning governance and supervision, there is an additional requirement for insurers to undertake an annual Own Risk & Solvency Assessment ("ORSA"). This sets out, amongst other things, the company's risk profile, its business plan and the expected level of capital it will require over the next three to five years based on its own assessment of risks.

6.15 I have been provided with the details of the Solvency II SCR and MCR calculations, the balance sheets pre and post Transfer on a Solvency II basis and the ORSA reports for the companies involved with the Transfer.

6.16 The Solvency II SCR and MCR calculations and balance sheets were based on information at the end of Q4 2017 i.e. 31 December 2017.

7. Claims and premium reserves

7.1 AMIL and AEL follow the common market practice in deriving their Solvency II Technical Provisions ("SII TPs"). The starting point of the SII TPs is the claims reserves on a statutory basis ("UK GAAP reserves"), then a series of steps are taken to arrive at the final SII TPs. The steps are as follows:

- UK GAAP reserves
- Remove margins for prudence and reinsurer bad debt
- Recognition of profit or loss in the Unearned Premium Reserve ("UPR")
- Allowance for deferred acquisition costs
- Allowance for future premiums
- Allowance for claims component of net premium provision
- Additional expenses
- Allowance for events not in data ("ENIDS")
- Discounting
- Allowance for a risk margin
- Other adjustments
- Final SII TPs

7.2 In my opinion, the risk of the SII TPs being understated lies with the UK GAAP reserves, i.e. the starting point, for the following reasons:

- The UK GAAP reserves are where the majority of the actuarial judgements and assumptions are exercised.
- The UK GAAP reserves are subject to the highest level of uncertainty in relative and absolute terms compared to other elements of the SII TPs. I have looked at the TP methodology and assumptions and I am comfortable that the non-claims elements of the TP have been assessed suitably.
- The other elements are mostly mechanical in terms of their calculations and the SII TPs and SII balance sheet have been subject to audits as at 31 December 2017. There is some subjectivity in the application of ENIDs and the Risk Margin.

Therefore, I have focused my detailed independent review on the UK GAAP reserves of AMIL and AEL, and considered the implications for the Solvency II technical provisions.

7.3 In this section, I discuss the claims reserve strength on a statutory basis, i.e. UK GAAP basis, of the portfolios. I discuss the portfolios in the following order:

- AMIL's portfolio as a whole;
- the transferring UK business from AMIL;
- the remaining non-UK business in AMIL; and
- the existing portfolio in AEL.

7.4 Throughout this section it should be noted that there is a limitation upon the accuracy of any estimate of claims reserves owing to intrinsic uncertainty in any estimate of future liabilities. This is due to the fact that the claims will be subject to the outcome of events yet to occur, such as judicial decisions, legislative actions, the economic environment, claim management, and changes in inflation. As a result, it should be recognised that future claims emergence will likely deviate, perhaps materially, from any estimated claims reserves.

AMIL portfolio

7.5 AMIL provides two types of Mortgage Insurance ("MI"):

- cover at loan-level, where individual loans are insured from the loan origination by the mortgage lender; and
- structured MI, where a portfolio of loans is insured, often after the date of origination.

7.6 With loan-level MI, AMIL insures the lender against losses arising from a mortgage loan. AMIL takes a first-loss position on the mortgage exposure down to an attachment point defined at the start of the MI contract. For example, if the attachment point is 75% loan to value ("LTV") and the loan is a 90% LTV mortgage, then for a property purchased for £88.8k (€100k), AMIL will insure the first £13.3k (€15k) of losses incurred by the lender if the mortgage defaults and the full loan value cannot be recovered. The £13.3k (€15k) cover is known as the Maximum Claim Amount ("MCA").

7.7 With structured MI, AMIL insures the lenders of pools of mortgages, with the inception of insurance coverage often post origination. Such insurance coverage often has structured insurance features such as a first loss deductible (lender retained risk) and an aggregate loss cap after which point the risk is retained by the lender.

7.8 The AMIL actuarial team has provided me with the following information:

- Claims reserving and earned premium methodology;
- Details of earned premium patterns used and the calculations for Q3 2017, i.e. an insurer "earns" a portion of a policy's premium as time elapses during the policy period in accordance with the expected pattern of risk emergence and earned premium patterns give the proportion "earned" at the end of each accounting period;

- Quarterly reserve reviews for Q1 to Q4 2017 (reports and presentations to the Board);
- Minutes of the Board meetings for Q1 to Q3 2017;
- A glossary of terms related to mortgage insurance;
- List of active and run-off policies, including current risks in force; and
- Historic claims development records at Q3 & Q4 2017.

7.9 I have reviewed the documentation provided by AMIL regarding their claims reserving and earned premium methodology as well as a document explaining the review done by an independent actuarial firm, regarding the earned premium patterns.

7.10 The claims reserves are split between case reserves and incurred but not reported ("IBNR") reserves. Case reserves are estimated for reported delinquencies, i.e. loans with arrears. AMIL's reserving methodology for Mortgage Indemnity insurance business is based on the work of an external consultant with experience in this field. The methodology captures the key risks of the business in terms of frequency and severity of loss given the specifics of the policies written. There are several items which need to be parameterised. The key ones are the loss in the event of a notified default, the rate of default delays and the case reserve to be applied to the loss. The case reserve itself is taken account of by looking at claims frequencies, severities and the maximum claim under the policy considering the limits and circumstances that the policy was written in. Geographical differences between mortgage markets and economic conditions are taken account of in the parametrisations and segmentation is appropriate on geographical grounds. AMIL's parameters are updated quarterly. The history of the case estimates is tracked against reality and the analysis of this forms the IBNR, methodology is documented and detailed. IBNR is calculated for the last two quarters only owing to the length of likely reporting delay.

7.11 There is sufficient detail in these documents for me to understand the methodology used and to conclude that the methodology and assumptions are consistent with generally accepted actuarial techniques and appear reasonable. While there have not been any papers published recently on the subject by an actuarial body, nothing based upon my own knowledge or contained within the articles published by the Institute and Faculty of Actuaries and the Casualty Actuarial Society would lead me to believe the methodology used by AMIL is not appropriate.

7.12 The unearned premium reserve is equal to 100% of the unearned premium. This is dictated by accounting legislation. In the case where losses are expected to exceed the written premium an additional provision is required. After reviewing AMIL's claims reserves and the methodology used to derive these reserves I conclude that no additional reserve is required due to the loss ratio being lower than 100%. I have reviewed the premium provision under the Solvency II basis, I concluded that the loss ratios used were reasonable.

7.13 I understand that the earned premium pattern used for Italy has been reviewed and AMIL actuaries consider that the earned premium proportions applied at the end of each accounting period are higher than the emerging experience. From Q4 2017, a new pattern in line with the incurred experience has been used. I have reviewed it and it is in line with the observed proportions of claim numbers notified at the end of each accounting period compared with total expected number of claims in a year.

7.14 The internal actuarial team of AMIL reviews the assumptions used to calculate the claims reserves on a quarterly basis. The key assumptions are in respect of the proportions of delinquencies that will become a claim, the maximum foreclosure periods and the severities (proportions applied to outstanding loan value). I have noted that those responsible for the reserves estimates are suitably qualified actuaries.

7.15 We have been provided with the quarterly reserve reports, the presentations made to the Board and the minutes of the Board meetings. The claims and business developments as well as the findings of the team that could affect the assumptions are explained in detail in the quarterly reserve reports. Any change to these assumptions is discussed and approved by the Board.

7.16 Assumptions are not amended on a frequent basis which is in line with my expectations given how infrequently economic changes which would affect this book occur.

7.17 There is sufficient detail in these reports for me to understand the process used and the key areas of reserves uncertainty.

7.18 I have checked that the reserves booked by the Board are in line with actuarial recommendation.

7.19 I have compared the risk margin component of the SII TPs with market benchmark, 2016 SFCR data, and it is within a reasonable range. As few companies write Mortgage Indemnity Guarantee business, a comparison was made to the whole UK non-life insurance market. AMIL's ratio of Risk Margin to the SII TP's is within the interquartile range of the market, sitting at the median which is where we would expect given their tail length and risk of business under the Standard Formula. See Table J3 in Appendix J for the results of this analysis.

Analysis of gross claims reserves at Q4 2017

7.20 In order to assess the reserve strength of AMIL, I have carried out a review of the key assumptions and methodologies used by AMIL reserving actuaries.

7.21 I have understood the methodology and assumptions behind the UK and Non-UK claims reserves but not re-calculated AmTrust estimates. I am satisfied that the reserving process around this business is a suitable approach. I believe this as the data appears suitably detailed for projection and the methodology and assumptions follow common actuarial techniques.

7.22 I understand that there is a strong link between economic conditions and the ability of mortgagees to make their mortgage payments. This results in the cyclical nature of mortgage insurance and the fact that development patterns shown by claims triangles in such circumstances might not be stable.

The earned results of AMIL's estimates

7.23 On earned business, the length of time taken for a delinquency to be known is very short so cyclicality over multiple year time horizon does not have a strong impact. Any cyclicality in the economic environment which drives claims would not have time to establish itself on earned business.

7.24 An economic event is likely to manifest over a period of time rather than occurring instantaneously.

7.25 Even if there was an instantaneous shift in the environment, a delinquency could still take several months to manifest once the borrower has exhausted their financial means of repayment.

7.26 The tail is driven by reporting delays as losses are relatively well known once one occurs.

7.27 The tail is limited by the fact that AMIL insures only the 'top' part of the mortgage (say 95% LTV to 80% LTV, below this has zero loss) and the bank will foreclose after a set amount of missed payments.

The unearned results of AMIL's estimates

7.28 On unearned business, I have reviewed AMIL's estimate of unearned losses.

7.29 I understand from AMIL that the estimate of losses on unearned business contains an allowance for cyclicality.

7.30 There is uncertainty in the probability/frequency calculation given the limited history of large market events, I understand that AMIL is able to analyse the ones which have occurred and their impact on the mortgage market and make reasonable allowance for the historical deteriorations.

7.31 I do not see a need to change any balance sheet figures for AMIL as a result of my review described above.

Conclusions on the value of AMIL liabilities

7.32 Based on my review described above, I have concluded that the methodologies and assumptions of the underlying reserve analysis carried out by AMIL actuaries are reasonable. The methodologies and assumptions have remained stable over several years and I have seen no strong indication of over or under reserving systematically, only deviations from estimated values which is to be expected. Therefore, I do not believe that the reserve strength of AMIL has been understated.

AMIL transferring portfolio

7.33 In paragraphs 7.5 to 7.31, we considered the strength of AMIL's reserves as a whole. However, only the UK business is transferring to AEL.

7.34 Table 7.1 shows the split by country of the UK GAAP reserves as at 31 December 2017. AMIL currently writes business in Germany, Italy and the UK. Business from the other countries included in Table 7.1 is in run-off.

Table 7.1: Gross reserves split by country as at 31 December 2017

AMIL (%)	Case reserves	IBNR	Loss Adjustment Expenses	UPR	Total
Finland	1%	3%	0%	0%	0%
Germany	1%	11%	0%	13%	9%
Ireland	12%	39%	0%	0%	5%
Italy	85%	41%	87%	78%	80%
Portugal	1%	5%	3%	0%	0%
Spain	1%	1%	3%	0%	0%
Sweden	0%	1%	3%	0%	0%
UK	0%	1%	3%	8%	5%
Total	100%	100%	100%	100%	100%

7.35 It can be seen in Table 7.1 that the transferring UK business only comprises 5% of AMIL's gross reserves as at 31 December 2017. Given the small proportion of AMIL's reserves that are transferring to AEL, we consider the analysis performed in respect of AMIL's whole portfolio to be sufficient.

7.36 The conclusions in paragraph 7.32 are still appropriate when only considering the proportion of reserves that are transferring. Therefore, I conclude that I do not believe that the reserve strength of AMIL for transferring policyholders has been understated.

AMIL remaining portfolio

7.37 The non-UK remaining portfolio of AMIL comprises 95% of the gross reserves. I consider the analysis performed in paragraphs 7.5 to 7.31 in respect of AMIL's portfolio as a whole to be appropriate

7.38 The conclusions in paragraph 7.32 are still appropriate when only considering the proportion of reserves that are remaining. Therefore, I conclude that I do not believe that the reserve strength of AMIL for remaining policyholders has been understated.

AEL existing portfolio

7.39 AEL underwrites general insurance business in the UK and other European countries. The company operates 8 underwriting teams: Liability, Property, Legal Expense, Special Risk, Medical Malpractice, Professional Indemnity, Mortgage & Credit and Accident & Health. The largest line of business in terms of gross claims reserves is Medical Malpractice, representing 70% of the total booked reserves as at 31 October 2017. Most of the Medical Malpractice class is underwritten in Italy. The second and third largest lines are Professional Indemnity and Legal Expenses; they represent about 8% and 5% of the reserves respectively. The Legal Expenses book consists of Personal and Commercial After The Event ("ATE") and Before The Event ("BTE") policies.

7.40 The AEL actuarial team has provided me with the following information:

a. Quarterly reserving reports for Q1 to Q4 2017;

b. Minutes of Reserving committees for Q1 to Q3 2017;

c. Reserving report at year-end 2016 (TAS compliant);

d. Actuarial recommendations at Q1 2018 for Medical Malpractice;

e. Summaries of analysis at Q4 2017 by line of business; and

f. Historic claims development records at December 2017 for earned premium, paid and incurred claims, and claim counts.

Table 7.2 provides a breakdown of the AEL reserves split by line of business.

Table 7.2: AEL reserves by line of business

AEL: Booked Reserves by Reserving Group as at 31 October 2017	
Reserving Group	**% of Total Booked Reserve**
Property	1.9%
Professional Indemnity	8.4%
Liability	2.9%
Medical Malpractice	69.7%
Legal Expenses - Personal	3.0%
Legal Expenses - Commercial	2.2%
Accident & Health	1.5%
Bonds	0.9%
Electrical Consumer	1.4%
Motor Related Products	0.7%
Structural Defects	3.4%
Trade Guarantees	0.4%
Other Speciality Risks	1.2%
Legal ATE Tranters	0.0%
Legal ATE RI	0.0%
BTE & Excess Protection	2.5%

7.41 The internal actuarial team of AEL estimates the reserves on a quarterly basis. I have noted that those responsible for the reserves estimates are suitably qualified actuaries.

7.42 The reserves are discussed quarterly with the underwriters. AEL holds a quarterly Reserving Committee which includes the Managing Director, Chief financial Officer, Chief Risk Officer and the Head of Actuarial, in which reserves are discussed and agreed.

7.43 For classes of business with sufficient historical data, the actuaries use widely accepted actuarial methods in conjunction with expected loss ratios from AEL's business plan. Where historical data is not available or not considered as sufficient by the actuaries, they rely on benchmark development factors and the expected loss ratios. The benchmark development patterns are discussed further in Appendix L.

7.44 AEL's philosophy is to book reserves on a slightly conservative basis under UK GAAP standard, this is evidenced in the comparison of booked and actuarial best estimate reserves where a prudent margin is added to the actuarial best estimate, for instance on a gross basis, the ultimate loss ratios ("ULRs") booked for Q4 2017 are slightly higher than the actuarial best estimate ULRs (The difference is shown in Table L1 of Appendix L).

Medical Malpractice

7.45 Given the size of the Medical Malpractice ("MedMal") reserves, I have undertaken a high level analysis to estimate the gross outstanding claims reserves as at Q4 2017 (the valuation date was 31 December 2017, the data was as at 31 October 2017).

7.46 I have projected paid and incurred claims using a number of widely accepted actuarial methods, i.e. loss development factors for paid and incurred claims as well as Bornhüetter-Ferguson ("BF") method. My gross claims reserves are within a reasonable range of the AEL calculated numbers.

7.47 Across the underwriting years of this portfolio I have projected loss ratios based upon the current and historic claims data. In most instances, AEL actuaries had projected a higher loss ratio than my own. For the 2014 and 2017 underwriting years I have projected a higher loss ratio of 0.7% and 2.5% respectively (The difference is shown in Table L1 of Appendix L). Over all underwriting years, the AEL estimate exceeds my estimate of the reserves required to settle future liabilities. For this reason, I believe the claims reserves set by AEL to be adequate for this line of business.

7.48 There are areas of subjectivity in any reserving analysis. Within the analysis I carried out, one such area would be the estimation of an initial loss ratio for each underwriting year. This initial expected loss ratio ("IELR") is used to drive some projection methodologies, especially the methodologies used to estimate losses in recent underwriting years (2015 to 2017). In order to derive the IELRs I used, I calculated an average based on prior, more mature underwriting years ultimate losses. While the final losses will differ from this estimate, I am comfortable that the estimate is reasonable as the policies written recently were written in the same legal environment and the same market. Historically the legal environment has changed in Italy with the introduction of the Milan tables in 2011 which are used for calculating compensation awards. I have made an allowance for this and this pre-dates the underwriting years from which the IELRs were derived.

7.49 The claims reserves have reinsurance. In estimating the impact of reinsurance on this account, AEL applies the quota share percentage to the gross reserve. This approach is commonly applied in the market and a reasonable way of performing the calculation.

7.50 In 2015, an external review of the Medical Malpractice reserves was undertaken and concluded that AEL estimates were reasonable. In my opinion, the AEL estimate was reasonable given the methodologies implemented and the alignment of the results.

7.51 For the other classes of business, the analysis I have performed to satisfy myself that the gross claims reserves are consistent with my expectations for insurance business of this nature includes the review of the following:

- the Q4 2017 quarterly reserves report & summaries;
- the year-end 2016 report; and
- the methods used to estimate the reserves compared with industry best practice.

See Appendix L for more details on the work I have undertaken. I have no reason to believe that the reserves for AEL lie outside a range of reasonable estimates.

7.52 I have compared the risk margin components of the SII TPs with market benchmarks and it is higher than market benchmarks. This does not look unreasonable given that AEL mainly writes business with long tail liabilities that have shown significant volatility in the past. I note that a higher risk margin actually increases the policyholders' security as this will increase the SII TPs. When looking at the size of the risk margin I have compared the AEL figure to the range of risk margins in the market. I would expect AEL to have a larger ratio of Risk Margin to Technical Provisions than the mean given they write long tail liability business which will increase the Risk Margin for this line of business. I have been able to compare the AEL result to where I would expect them to be in the market. AEL were towards the upper end of the range of market data. This is in line with what I expect.

7.53 The results of this benchmarking can be found in Table J3 in Appendix J. From conducting this analysis I am satisfied that the AEL risk margin is a reasonable estimate.

Conclusions on the value of the existing liabilities

7.54 Based on my review described above I have concluded that the methodologies and assumptions of the underlying reserve analysis carried out by AEL actuaries are reasonable (see Appendix L) and I also have an independent view on the reserve amounts for the MedMal class. The methodologies and assumptions have remained stable over several years and I have seen no strong indication of over or under reserving systematically.

7.55 I have looked at historic actual versus expected analyses for the AEL classes of business and noted the differences that have arisen historically. This historic experience provided context for my other pieces of analysis but did not directly drive my conclusions. The basis of my conclusions have been formed from the work I have performed in carrying out my own independent projections of claims data and analysis of the methodologies and assumptions carried out. Consequently, I do not believe that the reserve strength of the UK GAAP reserves or the Solvency II Technical Provisions of AEL are understated.

8. Policyholder security

8.1 In this section, I describe the effect of the Transfer on each group of policyholders with regards to security. I set out my conclusions at the end of the section and explain throughout how I have reached those conclusions.

8.2 I assess policyholder security through consideration of the balance sheet and the various measures of capital adequacy under Solvency II, such as the SCR measured by the standard formula over 1 year, the capital measure produced by AEL's and AMIL's economic capital models i.e. their internal model over 1 year time horizon and over the ultimate time horizon. See Section 6 of this report for more discussion on Solvency II regulations and the SCR.

8.3 I distinguish between three groups of policyholders:

- the transferring UK policyholders from AMIL;
- the remaining non-UK policyholders from AMIL; and
- the existing policyholders of AEL.

8.4 Only the UK policyholders of AMIL are transferring to AEL. Table 8.1 shows the Solvency II balance sheet of AMIL, split in to the transferring UK risk and the risk remaining post-Transfer.

Table 8.1: Solvency II Balance sheet of AMIL as at 31 December 2017 prior to Transfer, split by UK transferring and remaining risk (£m)

	AMIL	AMIL (UK)	AMIL (remaining)
Assets:			
Cash	3.8	0.0	3.8
Investments	116.2	2.6	113.6
Value of subsidiaries	3.9	-	3.9
Reinsurance assets	6.1	0.2	5.9
Other assets	4.3	0.1	4.2
Total Assets	**134.3**	**2.9**	**131.4**
Liabilities:			
Insurance liabilities	55.8	1.4	54.4
Other liabilities	3.4	0.0	3.4
Total Liabilities	**59.2**	**1.4**	**57.8**
Equity	**75.1**	**1.4**	**73.6**

8.5 In my opinion, policyholders are secure if their incurred and future claims can be paid by the insurance company as they fall due. This will be the case if the insurance company holds sufficient excess realisable assets over its liabilities so it can pay claims in full at the time payment falls due in a range of adverse conditions. This requires me to consider policyholder security before and after the Transfer.

8.6 Standard solvency measures in use such as the SCR aim to measure the extent to which the company will be able to maintain excess assets over its liabilities following a severe adverse event. Solvency II defines the SCR as the amount of excess assets required now in order for there to be a less than 0.5% chance that assets will be less than liabilities over a 1 year timeframe. That is the company should be able to withstand a 1-in-200 year event over a 1 year timeframe.

8.7 One measure of security is to consider the actual excess of assets over the liabilities of the company compared with the regulatory SCR: this is often termed “the coverage ratio”. A coverage ratio of over 100% means that the actual excess assets are greater than the SCR. Conversely, a coverage ratio of less than 100% means that actual excess assets are smaller than the SCR.

8.8 I first consider the SCR, coverage ratios and other metrics in this section. Then I show further analysis I have performed to support my conclusions. Finally, my conclusions are shown in each of the sub-sections regarding the impact of the security on the three groups of policyholders at the end of this section of the report.

Impact of the Transfer on the balance sheets of the affected companies

8.9 Table 8.2 shows simplified Solvency II balance sheets before and after the Transfer. The amounts shown for the positions before the Transfer are based on the balance sheets as at 31 December 2017.

8.10 The actual balance sheets before and after the Transfer will be different to that represented in Table 8.2 due to the actual experience of the companies between 31 December 2017 and the Transfer date.

8.11 I will issue a Supplementary Report prior to the final Court hearing after reviewing the most up-to-date information.

Table 8.2: Solvency II Balance sheets of AMIL and AEL as at 31 December 2017 prior to and post Transfer (£m)

	Prior to transfer		Post transfer	
	AMIL	**AEL**	**AMIL**	**AEL**
	[A]	[B]	[C]	[D]
Assets:				
Cash	3.8	54.8	3.8	54.8
Investments	116.2	377.8	113.6	380.4
Value of subsidiaries	3.9	135.4	3.9	134.0
Reinsurance assets	6.1	665.3	5.9	665.5
Other assets	4.3	203.1	4.2	203.2
Total Assets	**134.3**	**1,436.4**	**131.4**	**1,437.9**
Liabilities:				
Insurance liabilities	55.8	963.0	54.4	964.5
Other liabilities	3.4	121.0	3.4	121.0
Total Liabilities	**59.2**	**1,084.0**	**57.8**	**1,085.5**
Equity	**75.1**	**352.4**	**73.6**	**352.4**

8.12 The key movements are listed below:

a. After the Transfer, AMIL's balance sheet in column [C] shows the remaining assets and liabilities for the non-UK policyholders who are remaining in AMIL.

b. As shown in Table 8.1, £2.9m of AMIL's total assets and £1.4m of AMIL's total liabilities are transferred with the UK policyholders into AEL.

c. Assets and liabilities of UK policyholders of AMIL transfer to AEL line-by-line to arrive at column [D], the only exception being removing the £1.4m of AMIL's equity transferred over from the value of AEL's subsidiaries.

8.13 A key aspect of the balance sheets is that AEL has £665.5m of reinsurance assets post-Transfer; £0.2m or 0.03% of which relates to the UK business of AMIL. More than 80% of this is in respect of collateralised quota share reinsurance with Maiden Reinsurance Company ("Maiden"), and AmTrust International Insurance Limited ("AIIL") which is intra-group. The collateral provided is investment grade. There were two forms of collateral – funds withheld and trust account. The collateral is managed by JP Morgan for AIIL and State Street for Maiden. This arrangement provides additional security for AEL policyholders.

Risk capital measures – AMIL

8.14 I have considered the appropriate measure to use for assessing policyholder security. The choices available to me are risk capital measures, designed to ensure that an insurer is able to meet its obligations with a probability of at least 99.5% over

1 year, or to ultimate (defined as the time frame until all insurance obligations are paid):

- The Standard Formula ("SF") capital measure, which considers the capital required for AMIL and AEL to meet its obligations with a probability of at least 99.5% over 1 year, based on prescribed rules set by EU regulations (known as Solvency II) – I call it SF1;

- AMIL and AEL's own economic view of the capital required to meet its obligations with a probability of at least 99.5% over 1 year, calculated using their own economic capital model which has not been approved by any prudential supervisor – I call it EC1;

- or AMIL and AEL's own economic view of the capital required to meet its obligations with a probability of at least 99.5% to ultimate, calculated using their own economic capital model which has not been approved by any prudential supervisor – I call it ECu.

8.15 AMIL currently uses the Standard Formula approach to calculate its SCR. The Standard Formula is a method for calculating regulatory SCR prescribed by the EU Solvency II regulation (as discussed in Section 6 of this report). It aims to provide a consistent basis for comparing different companies across Europe.

8.16 As part of my independent expert work I have considered the risks to which AMIL is exposed and how these compare to the risks specified in the Standard Formula. For risks that are not included in the Standard Formula I have considered whether there are appropriate risk mitigants put in place by management in order to not require any capital to be held against these risks. In my opinion, the Standard Formula sufficiently captures the risks facing AMIL. Further details of my analysis are shown in Appendix M.

8.17 Under the Standard Formula, the SCR is calculated to a one-year time horizon. I have also considered the capital requirement to alternative time horizons, for example the ultimate time horizon which allows for the projection of future policyholder claims until these no longer need to be paid. In order to calculate a risk measure for the ultimate time horizons, I have considered AMIL's economic capital model for ORSA. I consider the one-year time horizon to be appropriate for AMIL for the purpose of assessing policyholder security. My consideration for the appropriateness of using EC1 can be found in Appendix G.

8.18 I have also considered the relative size of AMIL's Own Funds in excess of its SCR compared to other insurance companies in Section 8.33 for benchmarking. The Own Funds represent the level of available capital held to meet capital requirements under Solvency II (see paragraph 6.12). I believe it is important to carry out this benchmarking exercise in order to assess the level of AMIL's policyholder security relative to the UK market pre and post Transfer.

8.19 The Standard Formula is designed to be applicable to all insurers and is therefore based on the insurance risks within the "average" company. Therefore, it will not reflect the risk profile of AMIL perfectly as it is not tailored to its particular circumstances, as an economic capital model would be. I have carried out analysis of AMIL's economic capital model for ORSA and compared it to the SF and still consider the SF to be an appropriate measure of policyholder protection. AMIL's economic capital model has not been approved by any prudential supervisor. See

Appendix G for more information on my analysis carried out on AMIL's economic capital model and Standard Formula.

8.20 Despite this limitation, I believe the Standard Formula is an appropriate approach for assessing policy holder security for AMIL for the following reasons:

- as set out in my analysis above and in Appendix M, the Standard Formula is sufficiently comprehensive in capturing the material risks facing AMIL; and

- as set out in my analysis above and in Appendix G, the Standard Formula does not understate the risks facing AMIL when compared with the economic model used by AMIL for ORSA.

8.21 In addition SF1 has the following advantages over ECu:

- It is easy to compare SF1 across the industry as it is publicly available (for benchmarking analysis, see Appendix J), while, ECu is not publicly available;

- SF1 has been audited hence it has been subject to a higher level of external scrutiny than ECu.

8.22 I conclude that the SF1 is the most suitable measure for assessing policyholder security at AMIL for the reasons given above. In summary, through my investigations, I have not identified any reason to believe that the calculated SF1 materially understates or overstates the capital required by AMIL for the purpose of assessing policyholder security for AMIL policyholders.

8.23 The above analysis is appropriate for both transferring UK policyholders and remaining non-UK policyholders. The transferring UK policyholders comprise a small proportion of AMIL's risk. Following the Transfer, AMIL's coverage ratio remains the same at 174% which is still comfortably above their target of 120% (discussed in paragraph 8.45).

Risk capital measures - AEL

8.24 AEL currently uses the Standard Formula approach to calculate its SCR. In my opinion the use of the Standard Formula is reasonable for AEL as the wide mix of business written by AEL is captured adequately. The Standard Formula has been carefully calibrated to be an effective measure of risk for a diverse range of portfolios.

8.25 As part of my independent expert work I have performed an assessment of the Regulatory Solvency Capital Requirement i.e. SF1 as a suitable measure for assessing policyholder security. The full details of this assessment are given in Appendix K; only a summary and the conclusion are shown here.

8.26 I have also considered the risks which AEL is exposed to and how these compare to the risks specified in the Standard Formula. For risks that are not included in the Standard Formula I have considered whether there are appropriate risk mitigants put in place by management in order to not require any capital to be held against these risks. Further details of this are shown in Appendix M.

8.27 I have also reviewed AEL's Own Risk and Solvency Assessment ("ORSA") and Solvency and Financial Condition Report ("SFCR"), and their assessment of the appropriateness of Standard Formula for AEL, which conclude that the SF1 is suitable for AEL.

8.28 I have also considered AEL's economic capital model on both a one-year timeframe and to ultimate timeframe. AEL's economic capital model has not been approved by any prudential supervisor. I have performed a comparison of the capital requirements from this model and how this compares to the Standard Formula measure.

8.29 For the same reasons described in paragraphs 8.14 to 8.21 for AMIL, I believe the SF1 is an appropriate measure for assessing policyholder security for AEL.

8.30 In summary, through my investigations, I have not identified any reason to believe that calculated SF1 materially understates or overstates the capital required by AEL for the purpose of assessing policyholder security for both pre and post the Transfer.

Impact of the Transfer on the solvency positions of the affected companies

8.31 I have considered the SCR for AMIL and AEL at 31 December 2017 and how the SCR for the two companies may have looked if the Transfer had taken place at that time. I have performed my own high level checks on these calculations and found no reason to believe there were any inaccuracies in them. The impact of the PLI transfer into AEL has no impact on my view as described in this section.

Table 8.3: Solvency positions of AMIL and AEL as at 31 December 2017, prior to and post Transfer (£m)

	Prior to transfer		Post transfer	
	AMIL	AEL	AMIL	AEL
Own Funds / Equity	75.1	352.4	73.6	352.4
SCR	43.2	232.3	42.4	232.3
Coverage ratio	174%	152%	174%	152%
Excess capital	**31.8**	**120.1**	**31.2**	**120.1**

8.32 The actual excess capital in the post-Transfer AEL is £120.1m which is the same as AEL's pre-Transfer position. The Own Funds remain at £352.4m as shown in Table 2. The coverage ratio of AEL post-Transfer is the same as pre-Transfer.

a. Comparing AEL pre and post-Transfer, the coverage ratio and SCR both remain materially the same; the SCR actually increases by £23k post-Transfer. I have performed a high level check on the SCR calculations in order to understand why they remain the same and do not believe there to be any material inaccuracies.

b. Comparing AMIL pre-Transfer and AEL post-Transfer, AEL had a lower coverage ratio than AMIL however neither have moved as a result of the

Transfer. The selection of assets that transfer with AMIL's UK liabilities has been designed in such a way that this is the case, ensuring that the Transfer has no effect on the coverage ratio of either company.

8.33 The actual impact of the Transfer will be different from that presented above due to the actual experience of the companies between 31 December 2017 and the Transfer date.

Benchmarking

8.34 I have performed benchmarking of coverage ratios against the wider UK general insurance market in order to put into context the current solvency position of AMIL and AEL. In my opinion, the coverage ratio is a good indicator of the financial strength of a UK general insurer.

8.35 I understand that every company in the wider UK general insurance market has its own idiosyncrasies and different lines of business will have different characteristics and levels of risk, for example the expected length of liabilities. I believe the coverage ratio takes these differences into account to a reasonable extent because SCRs are calibrated to 1-in-200 events over one year which reflect the risk profiles of the (re)insurers, and the coverage ratio is relative to the SCR (the SCR is higher for more volatile business). We note that some firms may choose to hold a multiple of the SCR to protect themselves from events that emerge over multiple years.

8.36 However the SCR is a one year measure of risk and so it may be that firm with longer tailed liabilities may consider it appropriate to hold higher multiples of the SCR in order to protect themselves from events that emerge over multiple years. There is no formal calibration beyond the SCRs i.e. covering 1-in-200 events, for example in the next section of the report, I show that one cannot be certain what return period events a (re)insurer with a 141% coverage ratio can withstand. Therefore, in my opinion, excess over SCR should be gauged by considering the wider market.

8.37 I have used publically available data on Own Funds and SCR for the UK general insurance market as at 31 December 2017. My market benchmark only considers companies that are actively writing business, i.e. I have excluded run-off companies as they are not relevant for comparison with AMIL and AEL.

8.38 I believe that my benchmark gives a good representation of the UK general insurance market including 97 companies.

8.39 Table J1 found in Appendix J shows the deciles of the coverage ratio in my market benchmark. On this list AMIL is currently in the 6th decile, AEL is in the 5th decile and the post-Transfer companies would not move from these positions.

8.40 I further divided insurers into three groups based on their size and repeated my analysis. I did this in order to show the relationship between solvency ratio and the size of the company. I defined my groups as follows:

- Small: SCR less than £20m.
- Medium: SCR between £20m and £100m. AMIL falls in this group.

- Large: SCR greater than £100m. AEL falls in this group.

I chose these groupings for simplicity and because this splits my dataset of 97 companies into roughly equal groups, with 29, 31, and 37 companies in the Small, Medium and Large groups respectively. Table J2 found in Appendix J shows the deciles of the coverage ratio for the three groups.

8.41 Were I to compare AMIL to other companies of similar size to it (i.e. Medium companies), its coverage ratio pre-Transfer of 174% would fall in the 5th decile (i.e. between 40th and 50th percentile of the distribution of coverage ratios ranging from the lowest to the highest). Post-Transfer, AMIL's position would not change.

8.42 Were I to compare AEL to other companies of similar size to it (i.e. Large companies), its coverage ratio pre-Transfer of 152% would fall in the 7th decile. Post-Transfer, AEL's position would not change.

8.43 There is a trend for smaller companies to have higher coverage ratios, shown in Table J2. Taking this into account, AMIL and AEL have similar financial strength when compared with their relevant market benchmark.

8.44 I conclude that the post-Transfer coverage ratios of AMIL and AEL are not out of line with the market.

AmTrust's risk appetite

8.45 AEL has a target coverage ratio of 140% and AMIL has a target coverage ratio of 120%, as defined in the risk appetite statements used by their respective management teams to track financial performance. I believe these target coverage ratios are beneficial to policyholder security, For example, this target has the following implications:

- If the coverage ratio of AEL falls below 140%, management of AEL will seek capital injections from the parent company AIIL.
- If the coverage ratio of AMIL falls below 120% pre-Transfer, AMIL would seek a capital injection from its parent AEL.

Stress and scenario testing

8.46 I have performed stress and scenario tests for both AEL and AMIL pre-Transfer. These tests have been carried out on the coverage ratio for the Standard Formula SCR over 1 year time frame. It should be noted first and foremost that these scenarios have a very remote chance of occurring. It is however still useful to consider them as they help to illustrate what the position of AEL and AMIL policyholders would be under these extreme scenarios.

8.47 My stress and scenario tests consider the following two events. I have chosen these two events as I believe they give a reasonable view of the key risks to AMIL and AEL both pre and post the Transfer.

[a] **Mortgage indemnity stress:**
a severe deterioration in the Italian housing markets where AMIL operates. The deterioration is calibrated to a 1-in-200 event using the standard formula. It leads to a large increase in foreclosures, which in turn causes a substantial increase in claims to AMIL.

[b] **Medical malpractice stress:**
a severe deterioration in the medical malpractice class of business of AEL. The ultimate loss ratio is stressed up to 128% for 2010-2017. The loss ratio of 128% was reverse-engineered to reach a 1-in-200 reserve deterioration, where the 1-in-200 is calibrated using the Mack method (see Appendix E for details) for the reserve deterioration on an ultimate time horizon.

[c] **AEL Reinsurer financial difficulty stress:**
Financial difficulties at both Maiden and AEL's parent, AmTrust International Insurance Limited ("AIIL"). Maiden and AIIL are both reinsurers of AEL. Under this stress scenario, the financial difficulties lead to AEL not being able to receive any reinsurance recoveries, owing to [b], beyond the current collaterals held. The chance of both Maiden and AIIL encountering financial difficulties and no reinsurance recoveries being paid to AEL is remote. The chance of this occurring will be beyond a 1-in-200 event.

8.48 The table below shows the impact on the balance sheet of AMIL of the event described in [a], pre-Transfer.

Pre-transfer	**Mortgage indemnity stress [a]**	
	AMIL	
	Pre-deterioration	**Post-deterioration**
Assets:		
Cash	3.8	3.8
Investments	116.2	116.2
Value of subsidiaries	3.9	3.9
Reinsurance assets	6.1	6.1
Other assets	4.3	4.3
Total Assets	**134.3**	**134.3**
Liabilities:		
Insurance liabilities	55.8	83.9
Other liabilities	3.4	3.4
Total Liabilities	**59.2**	**87.3**
Own Funds	**75.1**	**47.0**
SCR	**43.2**	**50.2**
Coverage ratio	**174%**	**94%**

8.49 The key movements are:

AMIL's gross insurance liabilities would increase by £28.1m due to event [a].

AMIL's coverage ratio would fall to 94% as its liabilities have increased. AMIL would therefore require additional capital from its parent AEL in this scenario.

8.50 The table below shows the impact on the balance sheet of AMIL of the event described in [a], post-Transfer.

Post-transfer	**Mortgage indemnity stress [a]**	
	AMIL	
	Pre-deterioration	**Post-deterioration**
Assets:		
Cash	3.8	3.8
Investments	113.6	113.6
Value of subsidiaries	3.9	3.9
Reinsurance assets	5.9	5.9
Other assets	4.2	4.2
Total Assets	**131.4**	**131.4**
Liabilities:		
Insurance liabilities	54.4	82.5
Other liabilities	3.4	3.4
Total Liabilities	**57.8**	**85.9**
Own Funds	**73.6**	**45.5**
SCR	**42.4**	**48.1**
Coverage ratio	**174%**	**95%**

8.51 The key movements are:

AMIL's coverage ratio falls to 94% as its liabilities have increased. AMIL would therefore require additional capital from its parent AEL in this scenario, in order to ensure the company is sufficiently capitalised relative to its own risk appetite.

The deterioration affects the remaining non-UK policyholders of AMIL in the same way that they would have been affected pre-Transfer. The Transfer of UK policyholders to AEL does not affect the impact of this stress.

8.52 The table below shows the impact on the balance sheet of AEL if event [b] occurred, pre-Transfer.

Pre-transfer	**Medical malpractice stress [b]**	
	AEL	
	Pre-deterioration	**Post-deterioration**
Assets:		
Cash	54.8	54.8
Investments	377.8	377.8
Value of subsidiaries	135.4	135.4
Reinsurance assets	665.3	665.3
of which AIIL	427.8	427.8
of which Maiden	190.1	190.1
of which other	47.4	47.4
Other assets	203.1	203.1
Total Assets	**1,436.4**	**1,436.4**
Liabilities:		
Insurance liabilities	963.0	1,136.9
Other liabilities	121.0	121.0
Total Liabilities	**1,084.0**	**1,257.9**
Own Funds	**352.4**	**178.5**
SCR	**232.3**	**266.5**
Coverage ratio	**152%**	**67%**

8.53 The key movements are:

AEL's gross insurance liabilities would increase by £174m due to event [b].

AEL's coverage ratio falls to 67% as its liabilities have increased. AEL would therefore require additional capital from its parent AIIL in this scenario.

8.54 The table below shows the impact on the balance sheet of AEL if event [b] occurred, post-Transfer.

Post-transfer	Medical malpractice stress [b]	
	AEL	
	Pre-deterioration	Post-deterioration
Assets:		
Cash	54.8	54.8
Investments	380.4	380.4
Value of subsidiaries	134.0	134.0
Reinsurance assets	665.5	665.5
of which AIIL	427.8	427.8
of which Maiden	190.1	190.1
of which other	47.6	47.6
Other assets	203.2	203.2
Total Assets	**1,437.9**	**1,437.9**
Liabilities:		
Insurance liabilities	964.5	1,138.3
Other liabilities	121.0	121.0
Total Liabilities	**1,085.5**	**1,259.3**
Own Funds	**352.4**	**178.5**
SCR	**232.3**	**266.5**
Coverage ratio	**152%**	**67%**

8.55 The key movements are:

AEL's coverage ratio falls to 67% as its liabilities have increased. AEL would therefore require additional capital from its parent AIIL in this scenario, in order to ensure the company is sufficiently capitalised relative to its own risk appetite.

Post-Transfer, the transferred UK policyholders from AMIL would be adversely affected by this deterioration.

The deterioration affects the existing AEL policyholders in the same way that they would have been affected pre-Transfer. The Transfer of UK policyholders to AEL does not affect the impact of this stress.

8.56 We now consider the impact of events [b] and [c] happening together, a severe reserves deterioration in the medical malpractice class of business and both AEL's reinsurers facing financial difficulty to the extent that AEL will receive no reinsurance recoveries from them.

8.57 The table below shows the impact on the balance sheet of AEL if the events described in [b] and [c] both occurred, pre-Transfer.

Pre-transfer	**Medical malpractice stress + AEL reinsurers financial difficulties (i.e. [b] and [c] together)**	
	AEL	
	Pre-deterioration	**Post-deterioration**
Assets:		
Cash	54.8	54.8
Investments	377.8	377.8
Value of subsidiaries	135.4	135.4
Reinsurance assets	665.3	718.0
of which AIIL	427.8	454.3
of which Maiden	190.1	216.3
of which other	47.4	47.4
Other assets	203.1	203.1
Total Assets	**1,436.4**	**1,489.2**
Liabilities:		
Insurance liabilities	963.0	1,458.6
Other liabilities	121.0	121.0
Total Liabilities	**1,084.0**	**1,579.6**
Own Funds	**352.4**	**- 90.4**
SCR	**232.3**	**266.5**
Coverage ratio	**152%**	**-34%**

8.58 The key movements are:

AEL's insurance liabilities would increase by £495m which is the gross impact of event [b]. There are no reinsurance recoveries due to event [c].

AEL's reinsurance assets would increase by £53m which is the impact of excess reinsurance collateral held by AEL as at 31 December 2017.

AEL's coverage ratio falls to negative 34% as its liabilities have increased. AEL would therefore require a significant capital injection from their parent in order to ensure the company is sufficiently capitalised.

8.59 The table below shows the impact on the balance sheet of AEL if the events described in [b] and [c] both occurred, post-Transfer.

Post-transfer AEL	Medical malpractice stress + AEL reinsurers financial difficulties (i.e. [b] and [c] together)	
	AEL combined company	
	Pre-deterioration	Post-deterioration
Assets:		
Cash	54.8	54.8
Investments	380.4	380.4
Value of subsidiaries	134.0	134.0
Reinsurance assets	665.5	718.3
of which AIIL	427.8	454.3
of which Maiden	190.1	216.3
of which other	47.6	47.6
Other assets	203.2	203.2
Total Assets	**1,437.9**	**1,490.6**
Liabilities:		
Insurance liabilities	964.5	1,460.1
Other liabilities	121.0	121.0
Total Liabilities	**1,085.5**	**1,581.1**
Own Funds	**352.4**	**-90.4**
SCR	**232.3**	**266.5**
Coverage ratio	**152%**	**-34%**

8.60 The key movements are the same as the pre-Transfer movements:

AEL's insurance liabilities would increase by £495m which is the gross impact of event [b]. There are no reinsurance recoveries due to event [c].

AEL's reinsurance assets would increase by £53m which is the impact of excess reinsurance collateral held by AEL as at 31 December 2017.

AEL's coverage ratio falls to negative 34% as its liabilities have increased. AEL would therefore require a significant capital injection from their parent in order to ensure the company is sufficiently capitalised.

Post-Transfer, the transferred UK policyholders from AMIL would be adversely affected by this deterioration.

The deterioration affects the existing AEL policyholders in the same way that they would have been affected pre-Transfer. The Transfer of UK policyholders to AEL does not affect the impact of this stress.

8.61 In summary, my stress and scenario test shows that under these scenarios there is no material adverse impact to any group of policyholders as a result of the Transfer.

- Pre-Transfer the UK policyholders of AMIL would be adversely affected by event [a] whereas post-Transfer they would be adversely affected by events [b] and [c] as part of AEL.
- The non-UK policyholders of AMIL would be adversely affected by event [a] to the same extent pre and post-Transfer.

- The existing policyholders of AEL would be adversely affected by event [b] to the same extent pre and post-Transfer.
- The existing policyholders of AEL would be adversely affected by events [b] and [c] combined to the same extend pre and post-Transfer.

In all stresses, capital would be required from their respective parent company in order to get the regulatory solvency ratio to the required level. The Transfer does not impact the extent of capital which would be required as a result of the stresses.

Reverse stress testing for AEL

8.62 I also performed additional high-level reverse stress tests as summarised in the paragraphs below to support my conclusions regarding the sufficiency of AEL's SCR post-Transfer.

8.63 The value of reinsurance assets post-Transfer as at 31 December 2017 is £665.5m. In order to reduce the coverage ratio to an insufficient level, i.e. below 100%, AEL would need to experience a default of more than 18% of its assets. I consider the probability of this occurring to be very low. This is because the majority of the reinsurance assets are in respect of quota share agreements which are fully collateralised.

8.64 The value of AEL's investments post-Transfer as at 31 December 2017 is £380.4m. In order to reduce the coverage ratio to an insufficient level, i.e. below 100%, AEL would need to experience a decrease in the value of its investments by more than 31%. I consider the probability of this occurring to be very low given AEL's cautious investment strategy.

8.65 A severe deterioration in the medical malpractice class of business of AEL. For example, AEL's gross insurance liabilities would increase by £174m due to event [b].

8.66 I conclude that AEL is able to withstand a variety of stresses post transfer. The stress testing therefore further supports my conclusions that AEL has sufficient Own Funds for policyholder security purpose.

Guarantee from ANA to AMIL

8.67 AMIL policyholders currently benefit from a guarantee from AmTrust North America ("ANA").The terms of the guarantee are such that ANA promises to pay claims to AMIL once ultimate claims are in excess of an agreed amount.

8.68 Pre Transfer, I believe that this guarantee is of benefit to both AMIL and AEL policyholders. This is because in case of problems local to AMIL or AEL, a third party can provide additional funds and hence in some situations provide an additional layer of security for AMIL policyholders through enhanced ability to receive claim payments, and for AEL policyholders through protecting the value of its subsidiary.

8.69 Post-Transfer, the UK policyholders of AMIL will no longer directly benefit from this guarantee. However, the chance of UK policyholders requiring this additional layer of security is remote. The main risk within AMIL lies with the Italian mortgage indemnity portfolio, as demonstrated in Table 7.1. I therefore believe that the Transfer does not materially disadvantage the UK policyholders of AMIL.

Change in risk profile for UK AMIL policyholders

8.70 When considering policyholder security my conclusion is that the level of security for UK policyholders of AMIL remains broadly the same before and after the Transfer.

8.71 As discussed in paragraph 2.19, from a policyholder security perspective, I believe the greatest risk for the UK policyholders of AMIL before the Transfer is the risk of a severe downturn in the Italian housing market. Post-Transfer, I believe that due to increased diversification within AEL the greatest risk would be a severe increase in claims from AEL's book of medical malpractice business. Therefore there would be a change in the nature and type of risk to which the UK policyholders of AMIL are exposed.

8.72 While the risks are different, my work on benchmarking, and stress scenarios [a] and [b] show that the UK policyholders of AMIL are not disadvantaged as a result of the Transfer as they are adequately protected pre and post the Transfer and they are subject to a similar level of risks pre and post the Transfer albeit the risks are different but they are not subject to materially greater risks post-Transfer.

Impact on the security of transferring UK policyholders of AMIL

8.73 Should the Transfer become effective, the transferring UK policyholders from AMIL would be moving to a significantly larger entity which is sufficiently capitalised relative to its regulatory capital requirements. Although the coverage ratio would fall (since AEL's coverage ratio is lower than AMIL's both pre and post-Transfer) I believe the coverage ratio of AEL is in line with the market given its size

8.74 Following the Transfer, the transferring UK policyholders of AMIL have direct access to the capital of AEL. They will however lose direct access to the capital in AMIL.

8.75 My opinion is that I do not expect the transferring UK policyholders of AMIL's financial security to be materially disadvantaged by the Transfer in terms of their security for the following reasons:

- They would be transferring into a company that is sufficiently capitalised in respect of its regulatory capital requirements. The sufficiency is demonstrated by Table 8.2.
- They would be transferring from a company without a credit rating to a company with a credit rating of A (Excellent) from A.M. Best.
- They would be transferring into a company with a best estimate level of reserves, as discussed in Section 7.
- AEL and AMIL come under the same regulatory regime, so there would be no change in the level of regulatory protection. This applies to the payment of dividends to parent companies. Approval would be required from the PRA both prior to and after the Transfer.

- Although the risk profile for the UK policyholders of AMIL has changed qualitatively (such that the UK policyholders of AMIL are now exposed to medical malpractice business), in my opinion, because the level of security remains quantitatively the same the UK policyholders of AMIL are not materially disadvantaged. This is discussed in paragraphs 8.62 to 8.64.

Impact on the security of remaining non-UK policyholders of AMIL

8.76 Should the Transfer become effective, the remaining non-UK policyholders of AMIL will benefit from the same coverage ratio as pre-Transfer, 174%.

8.77 As a result of the Transfer, the remaining non-UK policyholders of AMIL will experience reduced geographical diversification as the UK policyholders are transferred to AEL. However, since the UK policyholders comprise only 5% of the gross reserves (see Table 7.1) the impact on security is not significant.

8.78 Therefore, I conclude that the Transfer will not materially disadvantage the non-UK policyholders remaining in AMIL in terms of their security.

Impact on the security of existing AEL policyholders

8.79 Should the Transfer become effective, the existing AEL policyholders would share their capital with the UK policyholders of AMIL.

8.80 Post-Transfer, the coverage ratio of AEL will remain at 152% and the Own Funds position remains the same.

8.81 My opinion is that I do not expect the AEL policyholders to be materially disadvantaged by the Transfer in terms of their security for the following reasons:

- There is no reduction in coverage ratio.

- The Transfer is from a 100% owned subsidiary of AEL. Therefore in reality no new risks are being taken into AEL as a result of the Transfer. AEL policyholders are already exposed to the risk of AMIL liabilities being more than expected through their 100% ownership of AMIL, and this risk does not change post-Transfer.

9. Other considerations

9.1 In this section, I discuss the following topics:

a) Changes in regulatory jurisdiction
b) Customer service
c) Complaints process
d) Transfer of employees
e) Pension scheme considerations
f) Tax implications
g) Investment strategy implications
h) Implications under insolvency
i) Liquidity position
j) “Brexit”
k) Financial Services Compensation Scheme
l) Financial Ombudsman Service
m) Impact on reinsurers
n) Governance and management framework
o) Should the Transfer not become effective
p) Communication strategy
q) Contagion risk

Changes in regulatory jurisdiction

9.2 There will be no changes in regulatory jurisdiction as a result of the Transfer of the UK policyholders of AMIL into AEL. All companies involved are regulated by the FCA and PRA and this will not change post Transfer. Therefore, I conclude that no group of policyholders will be adversely affected as a result of the Transfer in relation to this.

Customer service

9.3 The claims handling for the UK policyholders of AMIL will operate in the same manner as it currently does, i.e. the same employees that serve the existing AMIL policyholders will serve them post-Transfer. Please note that AEL does handle similar claims for its mortgage indemnity guarantee (“MIG”) class. Day to day operations will remain the same for claims up to a €100,000 threshold.

9.4 Claims above €100,000 will require approval from the head of AEL’s claims team post Transfer. However these claims are unusual and AEL have only experienced two such claims to date – in 2006 and 2010. The head of AEL’s claims team would take counsel from experts within the MIG team should such a claim arise.

9.5 Arguably, stronger governance around claims handling is positive for policyholder’s general security. Avoiding claims faults and paying claims unnecessarily will free additional resource for genuine claims.

9.6 I conclude that the claims handling process for the UK policyholders of AMIL will not be adversely affected as a result of the Transfer to AEL.

9.7 The remaining policyholders of AMIL will experience no change with regards to claims handling as a result of the Transfer. Therefore, I conclude that the remaining policyholders of AMIL will not be adversely affected.

Complaints process

9.8 AMIL has no formal complaints team as their sales are business-to-business. Complaints are reported to the business relationship manager within the AMIL team and escalated as necessary.

9.9 Post-Transfer, the complaints process will remain unchanged, except the point of contact for UK policyholder complaints will be from AEL. The complaints process for remaining policyholders will remain unchanged.

9.10 I conclude that the complaints process for the UK policyholders of AMIL will not be adversely affected as a result of the Transfer to AEL.

Transfer of employees

9.11 No employees will be transferred from AMIL to AEL as a result of the Transfer. Policies will be managed by the Mortgage and Credit division of AmTrust Post-Transfer in the same say existing non-AMIL mortgage policies are currently managed.

Pension scheme considerations

9.12 AMIL operates a defined benefit scheme for its employees in Germany, Italy and Spain. However, no pension scheme liabilities will be moved to AEL after the Transfer.

Tax implications

9.13 As the Transfer is an intra-group transaction, AmTrust does not believe there to be any significant tax implications as a result. I am not aware of any tax implications as a result of the Transfer.

Investment strategy implications

9.14 AEL's Investment Policy states that they aim to maximise the return on the investment portfolio for the longer term with a low/medium risk appetite whilst taking into consideration the requirements with respect to liquidity, relevant prudential regulations and capital adequacy. The policy sets out their investment guidelines, requirements and restrictions. A low/medium risk asset is defined as bearing the following characteristics:

- Safety of principal;
- Stability in value;
- Appropriate levels of liquidity for the overall portfolio;
- Diversification with respect to types of investment, individual and geographical concentrations, industry and duration;
- Mitigation of counterparty risk; and
- Maintenance of risk appetite within tolerance limits as agreed by the Board.

9.15 AMIL and AEL have almost identical investment management guidelines and the same in-house investment team located in New York.

9.16 Investments of AEL are actively managed by an Investment Committee ("IC") comprising of the CFO, Financial Controller and one representative from the Risk function. Investment managers are also invited to attend. The IC advises the Board of Directors of AEL and AMIL with respect to investment strategy and performance as well as approving large transactions.

9.17 I conclude that I do not expect AEL's investment strategy to have a significant adverse effect on the transferring UK policyholders of AMIL because AEL will still have a substantial amount of assets to invest following the Transfer. In addition, governance arrangements such as the IC are in place to ensure that appropriate decisions are made.

9.18 I am not aware of any planned changes to AEL's investment strategy as a result of the Transfer, therefore, do not anticipate any adverse impact on the transferring portfolios as a consequence of the Transfer.

9.19 I am not aware of any planned changes to AMIL's current investment strategy as a result of the Transfer, therefore do not anticipate any adverse impact on the remaining policyholders of AMIL as a consequence of the Transfer.

Implications under insolvency

9.20 In the event of insolvency of AEL post-Transfer, the UK policyholders of AMIL would rank alongside the existing policyholders of AEL. There would therefore be insolvency situations, where, had the Transfer not happened, there would not have been any impact on the UK policyholders of AMIL. However this has to be considered alongside the situation in which AMIL as a standalone entity would have become insolvent but AEL would not. In my opinion these two situations would offset.

9.21 As described in Section 8, I expect the probability of insolvency of AEL and AMIL to be remote post-Transfer, just as the probability of insolvency for AEL and AMIL was remote pre-Transfer, although the circumstances of the insolvencies would be different. I do not anticipate any material adverse impact as result of the Transfer for either the current AEL policyholders or the transferring UK policyholders of AMIL in case of insolvency.

Liquidity position

9.22 I do not anticipate any change to the liquidity position of AEL as a result of the Transfer. In my opinion, the amount of cash or cash equivalents available to pay liabilities post-Transfer will be more than sufficient.

"Brexit"

9.23 On 23 June 2016 the UK voted to leave the EU. On the 29 March 2017 the European Commission were officially notified of UK's intentions to withdraw from the EU. The UK is due to leave the EU on 29 March 2019 and it will therefore take some time for the full implications of this vote to become clear.

9.24 There are a number of risks for insurers in the UK. Some areas of potential concern are exchange rate volatility, contract uncertainty and a changing regulatory environment.

9.25 AEL has prepared a detailed Brexit contingency plan outlining potential strategies in the event that no agreement is reached between the UK and EU on administering European run-off risks concluded prior to the withdrawal date. Dependent on when a decision is reached and the extent of any transitional arrangements, AEL has a number of options including a portfolio transfer of impacted business to its Irish carrier.

9.26 This Brexit contingency plan has been submitted to the PRA and is a topic that is regularly discussed with the PRA and other European regulators. I have reviewed this memorandum and the proposed strategy.

9.27 Despite these risks to the insurance market as a whole, I do not believe that changes in the insurance market or UK regulatory environment resulting from Brexit will affect my conclusions contained in this report. However, if the Transfer was to take place to another entity incorporated/regulated in the EEA, I would need to reassess my conclusions.

9.28 My reasons for believing my conclusions will be unaffected are:

a. The transferring UK policyholders of AMIL fall under UK legislation, FSMA, therefore Brexit will not impact the transferring policyholders regardless of the Transfer.

b. AEL have future plans to transfer and/or renew business in to other European companies. For example European clients who are worried about Brexit are renewed in to AmTrust International Underwriters Limited (registered in Ireland) at their request.

Financial Services Compensation Scheme

9.29 The Financial Services Compensation Scheme ("FSCS") was set up under the FSMA to protect consumers when financial services firms fail. It applies to customers of UK-authorised financial services firms, mainly assisting private individuals but also some small businesses.

9.30 The FSCS will pay 100% of any claim incurred for compulsory insurance and 90% for non-compulsory insurance, without any limit on the amount payable, if a financial services firm is unable to.

9.31 In the case of a Transfer of insurance business, the policyholders will continue to be covered by the FSCS as long as the transferee is also a UK-authorised insurer.

9.32 The policyholders of AMIL are not entitled to the FSCS as they are mortgage lenders rather than private individuals or small businesses. The mortgagees have no ability to pursue AMIL in relation to compensation as they are neither a party to the mortgage insurance policy or a beneficiary of the cover.

9.33 Therefore, I conclude that the Transferring policyholders are not adversely affected with regards FSCS coverage as their position remains the same pre and post Transfer.

Financial Ombudsman Service

9.34 The Financial Ombudsman Service ("FOS") was set up as an independent public body to resolve individual disputes between financial services businesses and consumers. It is accessible for insurance policies administered from within the UK.

9.35 Eligible claimants are defined to be:

- Consumers;
- Micro-enterprises;
- Charities with an annual income less than £1 million; and
- Trustees of a trust with net asset valueless than £1 million.

9.36 The policyholders of AMIL are not eligible to refer complaints to the FOS as they are mortgage lenders.

9.37 Therefore, I conclude that neither the transferring UK policyholders of AMIL nor the remaining policyholders of AMIL are adversely affected with regards FOS coverage, as their position remains the same pre and post completion of the Transfer.

Impact on reinsurers

9.38 I have discussed the reinsurance arrangements which will be in place post-Transfer and note that there are no planned changes from the current coverage. There is a potential uncertainty regarding enforceability of reinsurance arrangements governed by the laws of non-EEA countries.

9.39 However, reinsurance programmes that cover AMIL's UK policyholders will novate to AEL on the effective date of the Transfer. I therefore conclude that there will be no likely effect of the Transfer on reinsurers covering companies affected by the Transfer. I will provide an update in my Supplementary Report.

Governance and management framework

9.40 AEL's Governance Manual outlines the legal and regulatory framework within which the company operates and the role of the Board and Committees.

9.41 The Board retains ultimate authority for all strategic issues and management decisions of AEL. AEL has the following Committees and sub-Committees to which Board powers are delegated:

- Remuneration and Nominations Committee
- Executive Committee
    - i. Reserving Committee
    - ii. Underwriting Committee

    iii. Product Governance Committee
    iv. Data Governance Management Committee
    v. Investment Management Committee
    vi. Deal Review Committee
- Risk and Compliance Committee
- Audit Committee

9.42 AEL's Risk and Compliance Committee is supported by the Risk Management function, assisting the Board in formulating the company's risk appetite, risk management strategies, policies and limit structures.

9.43 AMIL's Board has the following Committees and sub-Committees:
- Investment and Capital Committee
- Audit, Risk and Compliance Committee
    i. Risk Committee
    ii. Internal Model Steering Committee
- Remuneration Committee

9.44 AMIL is a wholly owned subsidiary of AEL and therefore there is already some commonality in the governance of the companies involved in the Transfer both in terms of practice and personnel. Therefore, the transferring UK policyholders of AMIL will continue to benefit from similar governance arrangements post Transfer.

9.45 I conclude that there is no significant risk of any material adverse impact arising as a result of the Transfer in regards to a change of governance and management framework. The existing AMIL and AEL Committees and sub-Committees will remain the same post Transfer.

Should the transfer not become effective

9.46 I have considered the likely effects on all groups of policyholders should the Transfer not become effective.

9.47 In my opinion, the impact of the Transfer not going ahead to the policyholders of AMIL (both transferring and remaining) is limited. If the Transfer were not to proceed:

- I understand from AEL that AMIL would remain a 100% subsidiary.
- The SCR coverage ratio enjoyed by the UK policyholders of AMIL would be higher in the short run by remaining as a separate entity.

9.48 If the Transfer were to not proceed, there would be no impact on the existing policyholders of AEL compared to the current position.

9.49 The Transfers of AMIL's UK business and of PLI (as referred to in paragraph 2.8) are not dependent on one another. One group of policyholders could transfer while the other group remains as AMIL or PLI policyholders. For more information refer to Appendix M.

Communication strategy

9.50 I understand that AmTrust is seeking a waiver from the requirement to notify AEL policyholders on the following basis:

- The transfer of 11 UK policyholders of AMIL (all commercial entities) will be immaterial to the AEL policyholders.

- The cost will be disproportionate at around £8m assuming the costs involved in the communication are around £1 per policy.

9.51 In my opinion, it is reasonable for AEL to seek this waiver given the immaterial size of the Transfer in comparison to AEL's existing business and the anticipated costs of communication.

9.52 AMIL intend to write to all 11 UK policyholders. Other proposed forms of communication regarding the Transfer of AMIL UK insurance business to AEL include the following:

- Notices in the Financial Times (international edition);

- Notices in two UK newspapers, The Times and The Sun, in compliance with the regulations and in order to target AEL's consumer policyholders;

- Notices in the London, Edinburgh and Belfast Gazettes; and

- Notice in Insurance Day, aiming to target AEL's reinsurance customers.

9.53 In addition, AMIL intends write to all reinsurers and seek confirmation of their agreement to the Transfer.

9.54 I understand that there will also be a notice on both AmTrust International (the website used by AEL) and AMIL's websites which include the letter sent to AMIL policyholders, the summary of the scheme and this report, the Scheme Document(s) setting out the terms of the Transfers, legal notices and a Q&A document setting out frequently asked questions about the Transfer for the UK policyholders of AMIL and other interested parties as well as a copy of the full version of this report and the report on the Transfer of PLI to AEL.

9.55 I have reviewed the draft letter to be sent to AMIL policyholders. In my opinion, this letter is clear, provides a fair representation of the Transfer, and is not misleading:

- The letter clearly indicates the aim and implications of the Transfer and how the policyholders' interests are being protected

- Access to other documentation available including this report is outlined

- Sufficient information on when and how the policyholders can exercise their right to object is provided

9.56 I have reviewed the draft text to be published on the websites. In my opinion, it is not misleading and sufficient. Access to other documentation available including this report is outlined.

9.57 I have reviewed the draft letter to be sent to AMIL reinsurers. In my opinion the letter is clear, gives a fair representation of the Transfer, and is not misleading:

- The letter describes the proposed Transfer in detail
- Access to other documentation available including this report is outlined
- Sufficient information on when and how the reinsurers can exercise their right to object is provided

9.58 In my opinion, both the summary of the scheme and report and the legal notice are clear and effective.

9.59 I conclude that in my opinion, the proposed communication strategy is efficient and proportionate given the size and implications of the Transfer. In my view, their strategy is fair and the proposed documentation is clear and not misleading.

Contagion risk

9.60 Contagion risk is the risk that losses or liabilities from the activity of one part of the AmTrust Group business might deplete or divert financial resources held to meet liabilities from AEL post-Transfer.

9.61 Should the AmTrust Group get into financial difficulties there are several controls that would restrict its ability to access funds in AEL. Dividends or transfers would need Board and regulatory approval; as indeed would any change in risk appetite affecting the minimum SCR coverage or holdings of illiquid assets. Comparing the position of AMIL now with that of AEL post-Transfer, the same controls would, in effect, apply. Alongside this, the regulator will continue to be involved and consulted, as appropriate.

9.62 Based on my review of this issue, which included holding discussions with the management team of AEL and reviewing the relevant governance policies, I have concluded that the position for AMIL is no worse after the Transfer than before.

9.63 A separate report explaining my review of the contagion risk of AEL in more detail is available to the PRA, the FCA and the Court on request.

10. Conclusions

10.1 I have considered the Transfer and its likely effects on both the transferring and remaining policyholders of AMIL and the existing policyholders of AEL.

10.2 In reaching the conclusion below, I have applied the following principles as set out in relevant professional guidance. I have sought to:

- Exercise my judgement in a reasoned and justifiable manner;
- Describe and assess the impact on all classes of beneficiaries (for the purpose of this report, being the transferring UK policyholders of AMIL, the remaining non-UK policyholders of AMIL and the existing policyholders of AEL);
- Indicate how the Transfer might lead to any changes in the material risks to the benefits of the classes of beneficiaries;
- Assess the impact on all the classes of beneficiaries;
- Indicate the proposed rationale for the Transfer to proceed;
- Include (in summary) the most material information on which my opinion is based; and
- Describe the rationale for my opinion.

10.3 I have concluded that there will be no material change to the service provided to the transferring or remaining policyholders of AMIL, and no material adverse impact on the security provided to them. Therefore, I do not expect that the policyholders of AMIL would be materially adversely affected by the Transfer.

10.4 I have concluded that there will be no material change to the service provided to the existing policyholders of AEL and no material adverse impact on the security provided to them. Therefore, I do not expect that the existing policyholders of AEL would be materially adversely affected by the Transfer.

10.5 In addition, reinsurers of UK policyholders of AMIL will not be adversely affected by the Transfer as all reinsurance contracts covering these policyholders will be transferred to AEL via novation. As a result, exposure to claims faced by AMIL's reinsurers will not change as a result of the Transfer.

10.6 Further to this, I have concluded that the existing reinsurers of AEL will not be materially adversely affected by the Transfer.

10.7 Given the above, I do not expect any group of policyholders or reinsurers to be materially adversely affected by the Transfer and therefore I see no reason why the Transfer should not proceed.

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

10.9 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.

10.10 I do however consider it necessary that I review the most recent information up to the effective date of the Transfer, when this becomes available, before confirming my conclusions and opinions in my Supplementary Report.

Appendix A: Glossary

AEL	AmTrust Europe Limited
AIIL	AmTrust International Insurance Limited
AMIL	AMT Mortgage Insurance Limited
AMT MSL	AMT Mortgage Services Limited, a service company whose parent is AMT Mortgage Insurance Limited
ANA	AmTrust North America
ATE	A type of insurance covering legal expense costs or advice for the bringing or defence of a court case where the policyholder has already decided to take or defend a legal action and wants to insure against the risk of losing and having to pay the other side's costs
APS	Actuarial Professional Standard
BF method	Bornhüetter-Ferguson method (see Appendix E for details)
BTE	A type of insurance covering legal expense costs or advice for the bringing or defence of a court case in case a future legal action has to be fought or defended
Capital requirements	The level of funds that an insurance or reinsurance undertaking is required to hold
Claims reserve	Funds held for the payment of future claims
Claims triangles	Historic claims development records
Delinquency	Mortgage loan where the borrower has failed to make a scheduled mortgage payment under the terms of the mortgage and remains in arrears
Earned premium	An insurer "earns" a portion of a policy's premium as time elapses during the policy period in accordance with the expected pattern of risk emergence
Effective Date	The date at which the Transfer becomes legally binding
EU	European Union
FCA	UK Financial Conduct Authority
FRC	UK Financial Reporting Council
FSA	UK Financial Services Authority, which regulated insurers before the PRA and FCA were formed

FSCS	UK Financial Services Compensation Scheme
FSMA	Financial Services and Markets Act 2000
FOS	Financial Ombudsman Service
Gross	Excluding the effect of reinsurance arrangements. For example, 'gross insurance liabilities' refers to insurance liabilities before taking in to account any offsetting reinsurance assets
IBNR	Incurred But Not Reported - A reserve that represents the estimated losses for claims that have occurred prior to a reporting period end date, but have not yet been reported to the insurer
IELR	Initial Expected Loss Ratio
IFoA	Institute and Faculty of Actuaries
Independent Expert	The suitably qualified person appointed to produce an independent report on the Transfer, in accordance with FSMA
Internal Model	A bespoke model developed by an insurance or reinsurance undertaking to calculate its SCR under Solvency II. All insurers are required to calculate their SCR using either an Internal Model or the Standard Formula
LAE	Loss adjustment expenses - Reserves allocated to cover expenses related to claims reserves
Legal expenses	Legal expenses insurance is purchased to fund the costs of legal advice and/or the costs of bringing or defending a court case. Legal expenses insurance can be bought: • "before the event" - in case a future legal action has to be fought or defended; or • "after the event" - where the policyholder has already decided to take or defend a legal action and wants to insure against the risk of losing and having to pay the other side's costs.
Mack method	See Appendix E for details
Maiden	Maiden Reinsurance Company
MIG	Mortgage Indemnity Guarantee – a type of credit insurance where a mortgage lender is insured against a loss due to a default of the borrower
MCA	Maximum Claim Amount – the maximum claim payable per loan, per the policy terms
MCR	Minimum Capital Requirement, a formulaic calculation of the capital requirement as part of the European Solvency II regulations for insurers

ORSA	Own Risk & Solvency Assessment, a reporting requirement where management consider their own assessment of risks and associated economic capital needs as part of the European Solvency II regulations for insurers
Own Funds	Available capital to meet capital requirements under Solvency II
PLI	Pedigree Livestock Insurance Limited
PRA	Prudential Regulation Authority
Reinsurance	An arrangement with another insurer or reinsurer whereby risks are shared
Risk Margin	The risk margin is the cost of providing an amount of capital necessary to support the obligations, on the assumption that they are transferred to a "reference undertaking" in accordance with the approach set out in the Delegated Acts.
Run-off	A line of insurance business that no longer accepts new business but continues to provide coverage for claims arising on its policies still in force, and that makes payments for claims that have occurred on policies that have expired
SCR	Solvency Capital Requirement, amount of capital insurers are required to hold under European Solvency II requirements. If an insurer's capital falls below the SCR, it will trigger regulatory intervention with the intention of remedying that position
SFCR	Solvency and Financial Condition Report
SME	Small or Medium sized Enterprise
Solvency II or SII	An updated set of regulatory requirements for EU insurers which apply from 1 January 2016
Standard Formula	A standardised calculation for the SCR and MCR of an insurance undertaking, as prescribed under Solvency II
SUP 18	Chapter 18 of the Supervision Manual from the FCA Handbook
TAS	Technical Actuarial Standards
the Transfer	The insurance business Transfer of the UK policyholders of AMIL from AMIL to AEL
Transfer Companies	AEL, UK policyholders of AMIL and PLI
TP	Technical provisions
TUPE	Transfer of Undertakings (Protection of Employment) regulations
UK	United Kingdom

UK GAAP	UK Generally Accepted Accounting Practice
ULR	Ultimate Loss Ratio
UPR	Unearned Premium Reserve

Appendix B: Extract from engagement letter

Specific Service Agreement

Description

The terms of the Engagement are subject to our General Terms and Conditions of Business and our Engagement Letter, copies of which are enclosed (together the "**Engagement Pack**").

Our Understanding

We understand that AmTrust International is in the process of undertaking two general insurance portfolio transfers under Part VII of the Financial Services and Markets Act 2000 from two UK regulated entities into AmTrust Europe Limited ("AEL") and is looking to appoint an independent expert ("IE") for each portfolio transfer.

The two Part VII transfers include:

1. The transfer of a pet insurance portfolio from Pedigree Livestock Insurance Ltd (PLI) to AEL
2. The transfer of a mortgage indemnity guarantee portfolio from AMT Mortgage Insurance Limited ("AMIL) to AEL*

Scope of Work

The scope of our work would include the provision of the Report which would consider the terms of the Transfer generally and the effects which it will have on the policyholders of policies of the companies involved, including the effects on their security and levels of service. The areas that will be reviewed and covered in our report are explained in the next section. The Report would be used in Court Applications.

In preparing the Report, we would need to have regard to the duty that we would owe to assist the Court on those matters within the expertise of the Independent Expert. This duty overrides any obligations to the companies involved.

Our Review

1. Consideration of the regulatory background in the UK and the specific background of the Transferor and Transferee companies.
2. Consideration of the terms of the scheme and a review of the transfer schemes for AMIL into AEL.
3. The possible impact of the Transfer, including effects on security of policyholder benefits and levels of service, on the different policyholders, as well as those remaining in each company, involved in the Transfer. These factors are contrasted to the position which will apply after the completion of the proposed transfer.
4. An assessment of the appropriateness, in nature and amount, of the assets being transferred.
5. An assessment of the capital position and reinsurance programme of each company prior to and after the Transfer.
6. A review of the effects of the Transfer on any mechanisms implemented to provide financial support in any of the Companies.

7. A review of, and opinion on, the adequacy of the communications made to policyholders concerning the Transfer.
8. An assessment of the operational plans and changes to assets and liabilities up to the effective date.
9. Any other matters drawn to the attention of the Independent Expert by the regulators or required by the regulators to be addressed within the Reports.

The nature of advice we will give will necessarily depend on both the amount of detail provided to us and the time scale within which the advice is required. We will rely on the information provided to us as being correct and complete and will not audit it for purposes of Engagement. If advice of a general nature is provided, the applicability of this will depend on the particular circumstances in which it is applied by you (of which we might not be aware) and should therefore be viewed accordingly.

Should we agree to vary the scope of our work once this letter has been signed by you, we will issue a supplemental Specific Service Agreement clarifying the nature and extent of any agreed variations. In the absence of such a supplemental Specific Service Agreement, the terms set out herein shall apply.

We reserve the right to discuss and agree with you changes to the scope of our work should they become necessary following a change in legislation.

* *Note: Since this Specific Service Agreement was issued and signed, the scope of our services has changed. The Part VII Transfer now only transfers the UK policyholders of AMIL in to AEL.*

MAZARS

Appendix C: My experience

My professional experience is set out below:

- I have worked in the general insurance industry for over 35 years, gaining experience both as a senior executive and a consultant.
- From 2007 to 2013, I was Group Chief Executive Officer of Ecclesiastical Insurance, and before that a partner with E&Y and Watson Wyatt. In the 1990's, I led GRE's UK Personal lines business and in the 1980's its Strategic Planning activity.
- I have been in charge of the underwriting of Mortgage Indemnity Guarantee business for a major British composite. Furthermore, in my time at Ecclesiastical, I was involved in the Part VII Transfer of the life business.
- I have also had experience in the pet insurance industry, having worked on the premium rating process for a pet insurer. In addition, I have run claims operations.
- I have experience reviewing and advising the audit partners on the adequacy of the actuarial reserves of audit clients who have substantial medical malpractice books both in the UK and Italy, similar to those held by AEL.
- I am currently Head of Actuarial at Mazars UK LLP after joining the firm in 2013. I ensure that all actuarial aspects contribute effectively to the running and strategic development of insurance enterprises.
- I am a member of the Council of the Institute and Faculty of Actuaries.
- I am a PRA/FCA skilled person.

Appendix D: Relationships with affected companies

Not including the preparation of this Independent Expert Report, Mazars has proposed to undertake the following additional projects for the AmTrust Group in 2018:

- AmTrust Europe Limited – Taxation review for Part VII Transfer;
- AmTrust at Lloyd's – Sciemus; and
- AmTrust at Lloyd's – Marintec Srl.

The combined revenue generated by Mazars from these three projects amounts to less than £30k. I do not believe that these projects create a conflict with my acting as the Independent Expert on the proposed Transfer as they account for a very small proportion of Mazars' income. In addition, neither I nor any member of our actuarial team have any involvement in these projects and no member of the teams involved in these projects have been involved in the Independent Expert assignment.

Appendix E: Reserving methods

This appendix contains a brief description of the actuarial projection techniques used to estimate ultimate claims, in particular:

- Claim development method (paid/incurred claims, claim counts);
- Expected loss ratio method;
- Bornhüetter-Ferguson method (paid or incurred claims);
- Frequency/Severity or Average Cost per Claim (ACPC); and
- Mack method.

Claim development method, also known as Chain ladder method or Link Ratio method

In this method, the historical period-to-period development factors for each claims cohort are used to select appropriate period-to-period development factors for future projection. These are then used to project the incomplete cohort to ultimate claim figures.

Any anomalous development factors are removed from the construction of the complete triangle development factors. Removal of these anomalous development factors is made by inspection of the relevant development patterns.

Expected claim ratio method

The ultimate claims for a given claims cohort can be determined by applying an expected loss ratio to the ultimate premiums. The expected loss ratio is the loss ratio that it is anticipated that will be realised when claims ultimately settle. This expected loss ratio is commonly determined at the time the business is written. It should be noted that the expected loss ratio method is based entirely on initial expectations and ignores claims experience. In practice, this is most commonly used in early development periods where there may be limited data which does not enable other standard actuarial methods to be used or reduces the appropriateness of these methods.

Bornhüetter-Ferguson method

The BF method is a traditional actuarial reserving method that requires an initial estimate of the ultimate liability for each claim submission period cohort. This is usually calculated using a weighted combination of the development patterns observed in historical claims and technical input from experts. This initial estimate is then adjusted by the experience observed to date. This method is particularly useful for more recent submission periods as there is less development and less data within these periods, making the chain ladder estimates less credible.

Frequency/Severity or Average Cost per Claim (ACPC)

This method considers separately the two key elements of total claim amounts, i.e. the number of claims and the average cost of a claim.

This method requires development tables for both total claim amounts and claim numbers. A third development table, of the average claim amounts, is then formed by dividing the figures in the corresponding cells of the first two tables. The next stage is the projection of figures in the average claims and number of claims tables, using either grossing-up factors or development factors. Finally, the projected ultimate claims can be calculated by multiplying together for each accident/underwriting period the projected figures for the average claim amounts and claim numbers. A reserve can then be calculated by subtracting all payments to date in respect of claims.

There are different types of frequency/severity methods which focus on a review of the number of anticipated claims and the anticipated claims severity. These methods can be used for most risks but are often used to provide insight in the analysis of long-tailed risks.

Mack method

This method produces standard errors for both individual origin periods and for all periods combined and then uses past claims data to derive estimates of the mean and variance of the total claims arising from each origin period.

The Mack method specifies only the mean and standard deviation of a distribution, not the full distribution itself so a full distribution and hence percentiles are derived by fitting a log normal distribution with the same mean and variance.

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Appendix F: Summary of information received

Information provided by AmTrust

AEL

- Company structure chart for AmTrust Group
- Financial statements on a UK GAAP basis for the year ended 31 December 2017
- Balance sheets on a SII basis as at year-end 2017
- Financial statements post-Transfer
- Year-end Review of Reserves as at 31 October 2016
- Reserving reports at 1Q, 2Q, 3Q and 4Q 2017
- AFH report for 2017
- ORSA reports pre-Transfer 2017, 2016 and 2015
- SFCR reports and QRTs for the year ended 31 December 2017
- Business plan 2018, 2016 and 2015
- Claims triangles for year-end 2017
- Board and Committee meeting minutes
- Governance Manual
- Investment Management Guidelines
- Risk Management Policy
- Reserving methods
- SCR Q3 2017 and Q4 2018
- Information on reinsurance arrangements
- Communications with PRA
- SCR Analysis of Change and Comparison with Standard Formula
- Brexit Contingency plan
- Standard Formula appropriateness assessment
- Internal model methodology and specification document

AMIL

- Financial statements on a UK GAAP basis for the year ended 31 December 2017
- Balance sheet on a SII basis as at year-end 2017
- Balance sheet on a SII basis of the transferring UK business as at year-end 2017
- Reserving reports at 1Q, 2Q, 3Q and 4Q 2017
- Reserving methodology and glossary of terms
- ORSA reports pre-Transfer 2017
- SFCR reports and QRTs for the year ended 31 December 2017
- Business plan 2018, 2016 and 2015
- Claims, delinquency and reserves triangles for year-end 2017
- Policy information and details of pending claims
- Earnings patterns as at Q3 2017
- Presentation provided to the FCA/PRA regarding the Transfer
- Board and Committee meeting minutes
- Details of governance structure and composition
- Internal Operational Procedures report
- Economic Capital Model and SII Valuation Methodology & Assumptions report
- Pension liability information

- Policyholder communication strategy
- Economic Capital Model and Solvency II Valuation Methodology & Assumptions
- Standard Formula appropriateness assessment
- Internal model methodology and specification document

Draft legal documentation provided

- A witness statement for the Directions Hearing on behalf of both AEL and AMIL
- Legal Notice
- Scheme and Report Summary
- Claim form
- Scheme Document
- Letters to reinsurers
- Letter to transferring AMIL policyholders
- Letter to brokers of AMIL policies

Appendix G: Standard Formula Appropriateness for AMIL

As discussed in paragraph 8.15, AMIL currently uses the Standard Formula approach to calculate its SCR. AMIL has also developed an Economic capital model which allows for a projection of future policyholder claims until these no longer need to be paid (known as "to ultimate"). AMIL does not use this Economic capital model for regulatory reporting purposes, but maintains the model for internal capital management purposes.

AMIL has carried out analysis on the appropriateness of using the Standard Formula for setting regulatory capital by comparing the Standard Formula results to those calculated by its Economic capital model. AMIL's analysis has concluded that it is appropriate to use the Standard Formula. The PRA has not objected to the conclusion reached by AMIL as no capital add on has been issued.

I have investigated AMIL's Economic capital model at a high level to form my own independent view. I understand that for its Own Risk and Solvency Assessment ("ORSA") and for internal capital management purposes, AMIL has developed an alternative model for the components of the SCR which represent Operational Risk (the risk that some operational failing of the Company leads to detriment), Premium Risk (the risk that the premiums changed are insufficient for the risks borne by the company), and Reserve Risk (the risk that on-going claims are settled at a higher value than previously expected) using internal calculation methodologies. These models are for management use only, not for setting the regulatory SCR. These models aim to measure underlying drivers of risk at a more granular level than that considered by the Standard Formula. I have reviewed these alternative models at a high level and consider them to be reasonable.

These alternative models are used by AMIL to produce an Alternative SCR (the "Alternative SCR" or "ASCR") which is used to sense check the SCR produced by the Standard Formula. They result in an Alternative SCR that is within 10% of the Standard Formula SCR in the last 8 quarters. The fact that these alternative models give results in a close range compared with the Standard Formula SCR gives me further comfort that the Standard Formula is appropriate for AMIL for the purpose of assessing policyholder security.

Appendix H: Reliance and Limitations

Events following the modelling date

The conclusions in this report are based on analyses that have been undertaken on data as at different points in time (typically 31 December 2017). 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 Supplementary Report 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.

The balance sheets shown in this report are based on data as at 31 December 2017. I would expect some changes to have taken place between then and the date of this report.

Reliance on other parties

In developing the conclusions in this report, I have relied on the data and accompanying explanations provided to me by and on behalf of AmTrust. I have not specifically reviewed the data for accuracy and completeness, but I have reviewed it for reasonableness.

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 and capital requirements. For AMIL, I have performed a review of assumptions and methodologies of the gross claims reserves for all the reserving class of business. Similarly, my review of AMIL's capital position in order to assess policyholder security has not amounted to a full re-estimation of the capital position. Therefore, I have relied on the calculations and documentation provided to me. I believe this is reasonable given the testing that I have done and the relatively simplistic nature of these calculations for a business of its size. The reviews that I have carried out give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.

In addition, for AEL, I have independently carried out my own estimation of the reserves for the largest reserving class of business Medical Malpractice, for the remaining reserving classes I have carried out high-level review. My review of AEL's capital position in order to assess policyholder security has not amounted to a full re-estimation of the capital position. I believe this is reasonable given the experience and professional qualifications of the authors of reserving and capital documents provided to me by AEL, the testing that I have done and the materiality of the classes which have not been re-calculated. The reviews that I have carried out give no indication of any significant deficiency and I believe that appropriate methodologies have been adopted throughout.

I have also relied on discussions that I have had with the managements of AmTrust. Where appropriate, I have sought documentation from them to evidence the assertions made to me in those discussions.

Other

The underlying numbers contained in this report are calculated to many decimal places. In the presentation of the figures in the various tables, there may be reconciliation differences due to the effect of rounding.

In my judgement, the results and conclusions contained in this report are reasonable given the information made available to me.

However, there is a limitation upon the accuracy of any estimate of claims reserves or capital requirements in that there is an inherent uncertainty in any estimate of future liabilities. This is due to the fact that the claims will be subject to the outcome of events yet to occur, such as judicial decisions, legislative actions, claim consciousness amongst potential claimants, claims management, claims settlement practices, changes in inflation and economic decisions. As a result, it should be recognised that future claim emergence will likely deviate, perhaps materially, from any estimate of claims reserves. In addition, it should be recognised that the actual capital required will likely deviate, perhaps materially from any estimate of the capital requirements.

Appendix I: Methodology

In my analysis in Section 7, I have performed the following:

- Reviewed AMIL's claims reserving and earned premium methodology, see paragraphs 7.5 to 7.32;
- Independently projected paid and incurred claims for the Medical Malpractice reserving class for AEL, see paragraphs 7.40 to 7.47;
- Reviewed the assumptions and methodologies adopted by AEL for the remaining reserving classes, see Appendix L.
- Compared AMIL and AEL's risk margin components of the SII TPs with market benchmarks, see paragraph 7.48 and Appendix J

In my analysis in Section 8, I have performed the following:

- Reviewed AMIL and AEL's use of the Standard Formula approach to calculate its SCR, see Appendix K for more information for AEL only;
- In order to compare the SF SCR over 1 year time frame with the SCR over the ultimate time frame, I reviewed an external actuarial report on AEL's economic capital model, AMIL's internal methodology document (high level) for its economic capital model, ORSA for AEL and AMIL, and SFCR documentation for AEL.
- Reviewed the impact of the Transfer on the solvency position of the involved companies, comparing the balance sheets pre and post Transfer, see paragraphs 8.9 to 8.33;
- Benchmarking of coverage ratios against the wider UK general insurance market, see paragraphs 8.34 to 8.44; and
- Stress testing which shows realistic disaster scenarios for both AEL and AMIL, see paragraphs 8.46 to 8.61.

Appendix J: Benchmarking

Table J1: Coverage ratio benchmarking

Decile	Percentile range	Coverage ratio	Company in decile
1st	0% - 10%	< 124%	AXA Insurance UK plc
2nd	10% - 20%	124% - 134%	Allianz Insurance plc
3rd	20% - 30%	134% - 142%	Travelers Insurance Company Ltd
4th	30% - 40%	142% - 151%	Liberty Mutual Insurance
5th	40% - 50%	151% - 171%	**AEL pre and post-Transfer,** Admiral Insurance Company Ltd
6th	50% - 60%	171% - 197%	**AMIL pre and post-Transfer,** Royal & Sun Alliance Insurance plc
7th	60% - 70%	197% - 233%	Aviva Insurance Ltd
8th	70% - 80%	233% - 279%	Berkshire Hathaway Int. Ins. Ltd
9th	80% - 90%	279% - 358%	Endurance Worldwide Ins. Ltd
10th	90% - 100%	> 358%	Sompo Japan Ins. Company

Table J2: Coverage ratio benchmarking

Decile	Percentile range	Small companies Coverage ratio	Medium companies Coverage ratio	Large companies Coverage ratio
1st	0% - 10%	< 140%	< 132%	< 108%
2nd	10% - 20%	140% - 171%	132% - 144%	108% - 125%
3rd	20% - 30%	171% - 196%	144% - 148%	125% - 130%
4th	30% - 40%	196% - 213%	148% - 163%	130% - 134%
5th	40% - 50%	213% - 261%	163% - 177%	134% - 140%
6th	50% - 60%	261% - 293%	177% - 204%	140% - 150%
7th	60% - 70%	293% - 321%	204% - 237%	150% - 155%
8th	70% - 80%	233% - 279%	237% - 271%	155% - 181%
9th	80% - 90%	279% - 358%	271% - 477%	181% - 217%
10th	90% - 100%	> 358%	> 477%	> 217%

Table J3: Risk Margin/Net TP Best Estimate benchmarking

Class	Min	LQ	Median	Mean	UQ	Max	AEL	AMIL
General Liability	2%	6%	9%	15%	18%	180%	**22%**	**N/A**
Credit & Suretyship	2%	8%	12%	15%	18%	45%	**22%**	**9%**
Total UK Non-Life	1%	6%	9%	17%	16%	266%	**22%**	**9%**

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Appendix K: Standard Formula Appropriateness for AEL

Comparison of capital by main risk category: AEL

I have performed a comparison by main risk category between the capital requirements using the Standard Formula and the AEL economic capital model based on a one year view and the ultimate view. My conclusion is that the Standard Formula gives the highest overall capital requirement and is therefore the most appropriate for assessing policyholder security.

I have reviewed the economic capital model at a high level to understand the differences against the Standard Formula. For my review, I have relied on discussions with the AEL capital team; the report of an external actuarial consultant who has performed validation on the methodology, approach and parameterisation of the economic capital model; and review of other documents provided to me. The documents I used are shown at the end of this section.

AEL as at Q4 2017

Risk	Standard Formula	economic capital model (1 year view)	economic capital model (ultimate view)
Market Risk	66.2	50.7	66.2
Credit Risk	41.3	37.8	52.7
Insurance Risk	155.9	198.3	150.9
Operational Risk	27.9	39.9	53.2
Undiversified Total	291.1	326.7	323.0
Total SCR	236.4	186.9	109.0

Below is a high level explanation for the largest differences. Full explanations of these and explanations for the smaller differences are given in detail in the rest of this appendix.

- Insurance Risk
    - The economic capital model ultimate view is lower than the 1 year view, mainly due to the release of the Risk Margin from the ultimate view which is not reflected in the 1 year view. The difference between the Standard Formula and economic capital model 1 year view is due to multiple differences in the method for calculating the two views. These are explained in more detail in the Insurance Risk section of this Appendix.

- Total SCR
    - The Standard Formula SCR is higher than the economic capital model 1-year view, mainly due to how aggregation in the Standard Formula differs from the Economic capital model, in particular the approach for aggregating Operational Risk and differences in the correlations used.
    - The economic capital model ultimate view SCR is a lot lower than the 1 year view due to the allowance for future profits from investment, which is significant on the ultimate time horizon.

Market risk

Considering the differences in methodology: the economic capital model uses an ESG provided by Moody's to create consistent paths for asset prices, currencies, and interest rates and applies these to AEL's balance sheet over 8 years (for the ultimate risk) and for a single year (for the 1-year risk). The paths are ranked by the impact on the balance sheet and the 99.5th percentile impact is selected as the risk. The Standard Formula on the other hand uses shocks applied to different risk categories such as interest rate risk, spread risk, currency risk etc. and uses a correlation matrix to aggregate the risks.

The Standard Formula market risk is higher than the 1-year Economic capital model market risk by £15.5m. This is for a number of reasons:

- An Economic Scenario Generator (Moody's) drives the market risk in the Economic capital model. This is a more granular approach than adopted in the Standard Formula and will by its nature lead to different results.
- In the economic capital model, the treatment of discounting is different from in the Standard Formula. In the Standard Formula, the impact of discounting (which reduces the liabilities) is allowed for in the Insurance Risk. In the Economic capital model, the discounting credit is captured as part of risk free investment income in the Market Risk module.

Comparing the 1-year economic capital model market risk with the to-ultimate economic capital model market risk: I would expect the to-ultimate risk to be much higher as there is more time for market risks to emerge. However the economic capital model ultimate view of market risk is only slightly higher. This is because it takes into account many years of investment income. This reduces the market risk in the ultimate model as most future years will show a positive investment return which acts to reduce the risk.

Credit risk

Comparing the credit risk from the economic capital model (1 year time horizon) and the Standard Formula, the economic capital model has a slightly lower risk charge.

Credit risk may be split into reinsurance credit risk (RI credit risk) and non-reinsurance (non-RI) credit risk. Both are higher in the economic capital model than in the Standard Formula before allowing for diversification. However, the economic capital model assumes less correlation between the two than in the Standard Formula, leading to a slightly lower charge overall.

Comparing the ultimate time horizon and the 1 year time horizon on the economic capital model, the ultimate time horizon risk is much higher for RI credit risk. This is reasonable as it takes a long time for the insurance risk that is being reinsured to run-off, and so the emergence of the RI credit risk is slow. For the Non-RI credit risk, the ultimate time horizon risk and the 1 year time horizon risk are the same. This is also reasonable as the emergence of this risk would be expected to be very quick as the amounts owed are short-term.

Insurance risk

Comparing the insurance risk from the economic capital model (1 year time horizon) and the Standard Formula, the economic capital model has a higher risk charge. This is partly because in the economic capital model the insurance risk is on an undiscounted basis. The discounting credit is captured in market risk rather than insurance risk. If the discounting credit were allocated to insurance risk, the 1-in-200 insurance risk would be £184.6m, which is still higher than the standard formula 1-in-200 of £155.9m. However, I believe this is reasonable and I explain why below.

Insurance risk may be split into premium risk and reserve risk. The approach of the economic capital model to calibrating both of these is very different from the standard formula.

Considering reserve risk: in the economic capital model, the reserve risk is modelled on the ultimate time horizon first. Then, emergence factors are used to derive the risk over a 1-year time horizon. I understand that AmTrust has carried out back-testing on the derived 1-year volatilities in order to validate the assumptions used which gives me further comfort. In the standard formula on the other hand, the 1-year reserve risk is parameterised directly using multiplicative risk factors applied to reserve volumes. In the economic capital model, the reserving classes used align with those used in the business whereas the standard formula uses Solvency II classes of business. Given these differences, one would expect a reasonable degree of difference between the approaches.

Considering premium risk: in the economic capital model, the premium risk is modelled on the ultimate time horizon first. Then, emergence factors are used to derive the risk over a 1-year time horizon. In addition, the future provisions related to unearned exposures are modelled stochastically through a credibility factor to reflect changes in technical provisions given experience in the first year. I understand that AmTrust has carried out back-testing on the derived 1-year volatilities in order to validate the assumptions used which gives me further comfort. In the standard formula on the other hand, the 1-year premium risk is parameterised directly using multiplicative risk factors applied to premium volumes. In the economic capital model, the classes of business used align with those used in the business whereas the standard formula uses Solvency II classes of business. Given these differences, one would expect a reasonable degree of difference between the approaches.

In the economic capital model, the medical malpractice line of business makes up a large proportion of the overall reserve risk and premium risk. In the standard formula the medical malpractice line of business makes a smaller relative contribution to the overall SCR, with more contribution from other lines of business. On this particular issue, I believe the economic capital model to be closer to reflecting the true risks, however, I note that when considering the overall calibration, the Standard Formula SCR is higher, and hence not inappropriate for the purpose of assessing policyholder security.

Comparing the ultimate time horizon and the 1 year time horizon on the economic capital model, the ultimate time horizon risk is much lower for insurance risk. This looks unusual but is due to the movements in the risk margin on a 1 year time horizon and the unwinding of the Risk Margin over the longer term horizon. The Risk Margin held at time 0 may be released or strengthened at time 1, whereas it is no longer required and released at ultimate and hence is deducted from the ultimate risk. Without deducting the Risk Margin, the insurance risk at the ultimate time horizon is higher than the 1 year time horizon.

Operational risk

Comparing the operational risk from the economic capital model (1 year time horizon) and the Standard Formula, the economic capital model has a higher risk charge. The main driver of the difference is a difference in approach to calculating the capital requirement. The operational risk in the economic capital model is set using a scenario based approach, which has been set specific to AEL's risk exposure. This represents an operational risk charge before diversification with other risk categories.

The Standard Formula capital uses a factor-based approach which is applied to the earned premiums and technical provisions. This is added on directly to the Basic SCR.

Overall the higher capital requirement in the economic capital model is not highly material and is offset by the diversification allowance between operational risks and other risks in the Economic capital model, which is not allowed for in the Standard Formula.

Comparing the ultimate time horizon and the 1 year time horizon on the economic capital model , the ultimate time horizon risk is higher. This is reasonable given that the ultimate time horizon looks at the operational risk over a longer time frame than the 1-year view, and therefore captures a higher exposure to risk.

Diversification

The Standard Formula allows for diversification between sub-risks within a single main risk category (e.g. interest rate risk, equity risk etc., which are part of market risk), and then overall diversification between the main risk categories (e.g. market risk, credit risk, etc.).

This approach differs from the economic capital model where there are a number of:

- Implicit correlation assumptions, for example
    - correlation between classes within insurance risk due to reinsurance application,
    - correlation between insurance risk and market risk due to inflation risk and other market risk from the ESG,
    - correlation between modelled reinsurance recoveries and their exposure to reinsurance credit risk.
- Explicit correlations applied through a hierarchical copula approach:
    - between attritional and large losses within a class,
    - between classes within premium risk and within reserving risk,
    - between premium risk and reserving risk
    - between insurance risk, operational risk and credit risk.

As these approaches are fundamentally different, one would expect the economic capital model diversification to be different from those set in the Standard Formula.

Comparing the diversification in the standard formula with that in the economic capital model over a 1-year time horizon, there is more diversification in the economic capital model. This is for a number of reasons:

- Operational risk diversifies against other risks in the economic capital model whereas it is added directly onto the SCR in the standard formula (i.e. no diversification)
- There is less correlation assumed (hence more diversification) between the different risk types in the economic capital model: between premium risk and credit risk for example, or between premium risk and market risk.

Comparing the diversification in the economic capital model over a 1-year time horizon with the ultimate time horizon, there is more diversification in the ultimate time horizon. This is for a number of reasons:

- There is diversification between the different years which can be allowed for in the ultimate time horizon which is not present in the 1-year time horizon.

- The risk margin is no longer required at ultimate and is hence deducted from the ultimate insurance risk whereas as over the 1-year time horizon, it may need to be strengthened and hence makes a contribution to the 1-year SCR.

Documents used

- AEL 2018 SCR AoC and Comparison with SF v5
- WTW report AmTrust Europe Limited - PhaseII – FINAL
- AEL 2017 ORSA Report
- Email correspondence with AmTrust capital team
- Discussions with AEL and AMIL actuaries

Appendix L: Reserving

Medical Malpractice class of AEL

Across the underwriting years of this portfolio I have projected loss ratios based upon the current and historic claims data. In most instances, AEL actuaries had projected a higher loss ratio than my own. For the 2014 and 2017 underwriting years I have projected a higher loss ratio of 0.7% and 2.5% respectively (The difference is shown in Table L1 below). Over all underwriting years, the AEL estimate exceeds my estimate of the reserves required to settle future liabilities. For this reason, I believe the claims reserves set by AEL to be adequate for this line of business.

There are areas of subjectivity in any reserving analysis. Within the analysis I carried out, one such area would be the estimation of an initial expected loss ratio for each underwriting year. This initial expected loss ratio ("IELR") is used to drive some projection methodologies, especially the methodologies used to estimate losses in recent underwriting years (2015 to 2017). In order to derive the IELRs I used I calculated an average based on prior, more mature underwriting years' ultimate loss ratios. While the final losses will differ from this estimate I am comfortable that the estimate is reasonable as the policies written recently were written in the same legal environment and the same market. Historically the legal environment has changed in Italy with the introduction of the Milan tables which are used for calculating compensation awards. I have made an allowance for this.

AEL segment the claims data for this class into its various territories in order to provide homogeneity in the claims. The projections are carried out using link ratio and other standard methodology.

The claims reserves have reinsurance. In estimating the net of reinsurance reserves, AEL allow for the quota share recoveries by applying the rate of the quota share percentage to the gross reserve. This approach is commonly applied in the market and a reasonable way of performing the calculation.

Table L1: Comparison of Ultimate Loss Ratios

Underwriting Year	AEL Actuarial loss ratio	AEL Booked loss ratio	Mazars loss ratio	Difference (AEL Actuarial - Mazars)	Difference (AEL Booked - Mazars)
2009	146.0%	145.1%	146.0%	0.0%	-0.9%
2010	97.4%	97.0%	97.4%	0.0%	-0.4%
2011	99.0%	98.4%	98.9%	0.1%	-0.5%
2012	97.8%	98.6%	97.7%	0.1%	0.9%
2013	98.3%	98.9%	98.1%	0.2%	0.8%
2014	77.7%	79.4%	78.4%	-0.7%	1.0%
2015	82.7%	86.9%	74.9%	7.8%	12.0%
2016	82.4%	87.3%	78.3%	4.1%	9.0%
2017	87.5%	92.4%	90.0%	-2.5%	2.4%

In addition to my independent projections of AEL's medical malpractice book, I have performed a series of diagnostics for the medical malpractice book, in order to understand the development of these claims in greater detail. The key findings of this analysis were the following:

- AEL's actuaries for reserving purposes believe that claims on the earliest underwriting year (2009) are not fully settled, and thus have made allowance for this through the use of a tail factor. I have sought to test the adequacy of AEL's implied tail factor against appropriate benchmark data (sourced from the Lloyd's risk code) for similar medical malpractice business as provided by AEL. Based on this, the tail factor calculated by AEL actuaries on both a paid and incurred basis is higher compared to the market benchmark and thus I conclude it to be reasonable.
- Paid to incurred ratios in particular have shown that there has been a change in characteristics of claims on more recent years. I have discussed with the actuaries of AEL, who have confirmed that in the middle of 2013, there was a change in underwriting moving from aggregate deductibles to individual deductibles and self-insured retentions, which has had the impact of increasing the overall level of deductibles. AEL have also confirmed that there has been no material changes to the case reserving philosophy historically for this particular business.

Non-Independently Projected Classes of Business

AEL: Booked Reserves by Reserving Group as at 31 October 2017	
Reserving Group	% of Total Booked Reserve
Property	1.9%
Professional Indemnity	8.4%
Liability	2.9%
Legal Expenses - Personal	3.0%
Legal Expenses - Commercial	2.2%
Accident & Health	1.5%
Bonds	0.9%
Electrical Consumer	1.4%
Motor Related Products	0.7%
Structural Defects	3.4%
Trade Guarantees	0.4%
Other Speciality Risks	1.2%
Legal ATE Tranters	0.0%
Legal ATE RI	0.0%
BTE & Excess Protection	2.5%

These classes were not re-projected in full owing to their materiality levels but work was carried out to better understand the adequacy of the reserves set for these classes. I have carried out analysis in many cases using high level projection methodologies. In my analysis I have considered the methodologies around the reserving carried out at the reserving class of business level which is more granular than the reserving group shown in the table above. The work carried out is listed below.

Property

- I have compared benchmark claims development patterns to AEL implied development pattern. I have used benchmarks from other market participants, the resulting ultimate claim estimates differed from the AEL estimate by 0.3%. I view this difference to be well within a reasonable range.
- I have assessed grouping of claims and segmentation. This reserving class contains residential let, caravan, commercial property, commercial buildings, commercial package, household and household flood.
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed for this class of business and I am happy that AEL use generally accepted actuarial techniques. In particular, I believe AEL's methodology is appropriate to this line of business given its short tail nature. There is the features of the claims data which have changed over time, following an increase in the range of property cover provided. However, this does not give rise to a material concern given the size of the older years' reserves against the total.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is no non-proportional cover for this class. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business, within this reserving class, owing to a lack of sufficient historical claims data, development patterns were based on patterns from other property lines of business within this class where there was larger volume of claims data. I view this to be a reasonable methodology given the absence of statistically reliable claims volumes.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Professional Indemnity

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from London market data and PRA returns, the resulting ultimate claim estimates differed from the AEL estimate by 6.0%. I view this difference to be within a reasonable range given the level of uncertainty associates with the different mix of business underlying the benchmarks.
- I have assessed grouping of claims and segmentation. Prior to 2013 this reserving class contained a mix of business (large proportion from financial advisers). Over more recent periods this class has become largely dominated by solicitors' professional indemnity.
- I have discussed methodology with AEL, I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its long/medium tail nature. There are features of the claims data which have changed over time, following a change in the mix of business from predominantly financial advisors to solicitors. This does not give rise to a material concern given that the change was made 5 years ago.
- AEL have used benchmark development factors in conjunction with discussions with the Underwriters and the Claims department, particularly with respect to the known

claim notifications. I view this to be a reasonable methodology given the absence of statistically reliable claims volumes. Benchmark development patterns are chosen from London Market data with similar risks.

- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is non-proportional cover for this class, AEL does not assume recoveries for IBNR which is a reasonable approach. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the small lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Liability (including Greek Motor)

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from London market data, the resulting ultimate claim estimates differed from the AEL estimate by 0.7%. I view this difference to be well within a reasonable range.
- I have assessed grouping of claims and segmentation. This reserving class consists of direct liability business written in UK, Europe and the US, with the exposure in the US minimal, and Greek motor business.
- I have discussed methodology with AEL, I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its long/medium tail nature. There are features of the claims data which have changed over time following a growth of the Greek motor line and a change in the underwriter in 2014. AEL has used suitable methodology in their reserving for these features.
- Due to the change in the mix of the business as detailed above, AEL have used benchmark development factors in conjunction with discussions with the Underwriters and the Claims department, particularly with respect to the known claim notifications. I view this to be a reasonable methodology given the absence of statistically reliable claims volumes.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is non-proportional cover for this class, no recoveries are assumed for the IBNR, which is a reasonable approach.

ATE Legal Expenses (Personal)

- I have discussed methodology with AEL and I have understood how the reserve estimates have been formed for this class of business using a model which models the rate of settlement and method of settlement of claims. I am comfortable that the methodology used by AEL is appropriate to this line of business given its long/medium tail nature and the features of the claims.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.

ATE Legal Tranters and Ellite

- I have discussed methodology with AEL and assessed reasonableness. I do not include specifics of AEL methodology here but I have understood how the reserve estimates have been formed for this class of business and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its long/medium tail nature and the features of the claims data which have remained stable over time.
- Both the Tranters and Ellite lines of business are in run-off, and hence the ultimate losses for this class has been determined using a judgemental approach. I view this to be a reasonable and proportional approach given that relatively low volumes have been written, no new business is being written and claims are well developed.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.

ATE Legal Expenses (Commercial)

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from other market participants. I view the AEL's assumed development pattern to be reasonable.
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed using a stochastic model which models the win/loss rates and the expected timing of settlements for the unfunded business, with a judgemental approach for funded business due to insufficient data volumes for this class of business. I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its long/medium tail nature and the features of the claims data.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For funded business within this reserving class, an ultimate loss is selected based upon the business plan which is higher than the pricing loss ratio. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

BTE and Excess Protection

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from other market participants, the resulting ultimate claim estimates differed from the AEL estimate by +1.2%. I view this difference to be well within a reasonable range.
- I have assessed grouping of claims and segmentation. This reserving class contains before the event ("BTE"), excess protection, ARAG legal expense and Italian branch legal protection insurance. ARAG is a UK provider of legal expense insurance and assistance products for insurers, intermediaries and solicitors.
- I have discussed methodology with AEL and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its short/medium tail nature.

- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Accident & Health

- I have assessed grouping of claims and segmentation. This reserving class contains personal accident, travel, critical illness, Swedish dental, best doctors, medical insurances, Yvellin and accident, death & cancer ("ADAC").
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed for this class of business and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its short tail nature and the features of the claims data.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is non-proportional cover for this class, no recoveries are assumed for IBNR claims, which is a reasonable approach.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Bonds

- I have assessed grouping of claims and segmentation. This reserving class contains bonds & guarantees, surety RI and surety bonds (UK, Spanish, Italian and French (Verspieren).
- I have discussed methodology with AEL and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its short tail nature and the features of the claims data which have changed historically but remained stable over the most recent 7 underwriting years.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is non-proportional cover for this class, no recoveries are assumed for the IBNR claims which is a reasonable approach. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Electrical Consumer

- I have assessed grouping of claims and segmentation. This reserving class contains brown & white goods, brown & white insured, electrical warranties, mobile phones, gadgets and bicycles.
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed for this class of business and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its claims features.
- Owing to the fact that there is no historic data for most of the lines of business within this reserving class, AEL has used benchmark development factors in order to determine the ultimate claims level. I view this to be a reasonable methodology given the absence of statistically reliable claims volumes.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Motor Related Products

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from other market participants, the resulting ultimate claim estimates differed from the AEL estimate by 1.0%. I view this difference to be well within a reasonable range.
- I have assessed grouping of claims and segmentation. This reserving class contains car hire, GAP, CVT (Italian motor), motor DTI, motor warranties and other miscellaneous motor insurance.
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed for this class of business and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given the features of the claims data.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Structural Defects

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from other market participants. I view the AEL's assumed development patterns to be reasonable.

- I have assessed grouping of claims and segmentation. This reserving class contains structural defects, Norwegian home warranty, Nordic structural and Decennial French construction business.
- I have discussed methodology with AEL. I have understood how the reserve estimates have been formed for this class of business. Following this, I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its long tail nature. There are features of the claims data changed significantly over time, due to the growth in the Norwegian and structural defects lines of business. AEL has used appropriate reserving methodologies to address these features.
- Due to the changing mix of business within this class as detailed above and the fact there is only 6-7 years of historical claims data for this class means AEL have determined the ultimate claims through MDIS benchmarks or benchmarks provided by their auditor.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is non-proportional cover for this class, no recoveries are assumed for IBNR claims which is a reasonable approach. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Trade Guarantees

- I have assessed grouping of claims and segmentation. This line of business contains construction (including French), trade guarantees (IBG's), performance bonds & specialist trade credit insurance (Equinox).
- I have discussed methodology with AEL and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its short tail nature and the features of the claims data.
- Owing to low volumes of claims data for this reserving class, AEL have made use of loss ratios based on the business plan in order determine the ultimate loss. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history. I view this to be a reasonable methodology given the absence of statistically reliable claims volumes.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some of the smaller lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Other Speciality Risks

- I have compared benchmark claims development patterns to AEL implied development patterns. I have used benchmarks from other market participants and London market data, the resulting ultimate claim estimates differed from the AEL estimate by +0.3%. I view this difference to be well within a reasonable range.
- I have assessed grouping of claims and segmentation. This line of business contains Boiler Breakdown, Equine, Furniture Warranties, Rental Guarantees, Mortgage Indemnity, Payment Protection, Plant & Equipment, Political Risks and Credit Card add on sold via banks.
- I have discussed methodology with AEL and I am happy that they are generally accepted actuarial techniques and appropriate to this line of business given its short/medium tail nature and the features of the claims data. There is a change in business mix in relation to the mortgage indemnity class which has since been commuted.
- For some smaller lines of business within this class, there is insufficient volumes of claims data within AEL and hence in such cases ultimate loss ratios have been judgmentally selected. I have discussed the approach used to derive such estimates and I view this to be a reasonable methodology given the absence of statistically reliable claims volumes.
- I have discussed the methodology for allowing for the impact of reinsurance with AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.
- For some small lines of business within this reserving class, an ultimate loss is selected based upon the business plan. On a quarterly basis AEL assesses how losses are tracking against ULR. If losses are running higher than expected then the loss ratio is adjusted, if not then it is maintained. This is an approach which is suitable for classes with little or no claims history.

Mortgage Indemnity

- AEL began writing mortgage indemnity insurance in 2017, AEL estimates the ultimate loss using loss ratios as per the business plan. 2017Q4 is the first quarter that AEL has reviewed this class of business and intend on carrying out a full review at 2018 Q1 when there is further claims experience. I view this to be a reasonable approach.
- I have discussed the methodology for allowing for the impact of reinsurance for AEL. There is quota share insurance in place which is allowed for using an appropriate methodology.

Appendix M: Analysis of Risks and Risk Mitigants

I have considered AEL and AMIL's main risk exposures in comparison to the Standard Formula.

The main components of AEL and AMIL's risk exposures are shown below.

- Underwriting Risk
  - Premium and reserve risk
- Market Risk
  - Interest rate risk
  - Spread risk
  - Currency risk
  - Equity risk arising from strategic equity investments.
- Credit Risk
  - Exposures to reinsurers, banks and bond counterparties
- Operational Risk
- Other Risks
  - Legal & Regulatory Risks
  - Strategic Risk
  - Governance risk
  - Other Group risks
  - Liquidity Risk.

The above material risks have been captured in the Standard Formula, with the exception of the risks listed as 'Other Risks'.

My approach is based on my understanding of the materiality of the different risks facing insurance companies, and what mitigants one could reasonably expect to be in place. I have assessed AEL's approach to mitigating these 'Other Risks' that are not included in the Standard Formula. My analysis of these risks and whether there is a requirement to hold capital against these risks is set out below. I consider AEL's approach to mitigating these risks to not require additional capital to be held to cover these risks. In addition, I have reviewed the ORSA and there is a process for internal review of the emerging risks in place.

Risk	Definition	AEL's approach to risk mitigation	AMIL's approach to risk mitigation
Liquidity Risk	The Company's potential inability to meet all payment obligations when they become due and the risk stemming from the lack of marketability of an investment security that cannot be bought or sold quickly enough to realize cash.	AEL regularly monitors its liquidity ratio (current assets compared to liabilities).	AMIL regularly monitors its liquidity ratio (current assets compared to liabilities) and performs cashflow analysis.
Legal & Regulatory Risk	The risk of non-compliance with regulation and legislation.	AEL mitigates this risk through its corporate governance and internal control mechanisms.	AMIL mitigates this risk through its corporate governance and internal control mechanisms.
Strategic Risk	Risks arising from failure to sufficiently define the direction and objectives of the entity, together with the resourcing and monitoring of the achievement of the same.	AEL produces a business strategy and plan as part of its ORSA, identifying its objectives and future plans. Projections are carried out to assess the impact on the future balance sheet.	AMIL produces a business strategy and plan as part of its ORSA, identifying its objectives and future plans. Projections are carried out to assess the impact on the future balance sheet.
Governance Risk	Risks arising from the failure to demonstrate independent and proper stewardship of the affairs of the entity in	AEL uses a 'three lines of defence' governance model, incorporating review from Risk	AMIL uses a 'three lines of defence' governance model, incorporating review

	order to safeguard the assets of the entity's shareholders and the overall interests of its stakeholders.	& Compliance, and Internal Audit. Monitored as part of the ORSA.	from Risk & Compliance, and Internal Audit. Monitored as part of the ORSA.
Group Risks	The risks arising from other parts of its group, through parental influence, changes in overall AM Best Rating, or direct contagion.	AEL have considered this risk as part of their ORSA scenario testing. The impact on the SCR coverage ratio is assessed not to be material.	AMIL considers a Group risk scenario as part of its ORSA, the assessment shows there is no additional capital required to cover this risk. This risk is also covered as part of AMIL's Group operational risk policy.
Solvency Risk	The risk that the entity fails to maintain adequate levels of capital resources of sufficient quality and quantity in order to carry out its business objectives and in order to meet all domestic and international regulatory considerations regarding the capital resource requirements.	AEL sets its risk appetite at 140% SCR coverage ratio. This metric is monitored regularly as part of the ORSA and in business planning.	AMIL's risk appetite is set based on solvency ratio. This metric is monitored regularly as part of the ORSA and in business planning.
Reputational Risk	The risk relates to potential losses resulting from damages to the Company's reputation, which could be manifested in terms of lost revenue; increased operating, capital or regulatory costs; or destruction of shareholder value.	AEL manages reputational risk by operating to high standards across its business activities, and continuously monitoring feedback from its key stakeholders, including customers and regulators.	AMIL manages reputational risk by operating to high standards across its business activities, and continuously monitoring feedback from its key stakeholders, including customers and regulators.

Based on the above assessments, I consider that both AEL and AMIL have appropriate mitigants in place to not require capital to be held for these additional risks and that the Regulatory SCR is sufficient to cover the capital requirement for both a 1 year time horizon and the ultimate time horizon.

Appendix N: Post-Transfer balance sheet

Given below is the simplified Solvency II balance sheet of the post-Transfer combined company, based on the balance sheets as at 31 December 2017, assuming that the Transfer of AMIL UK insurance business to AEL is successful in parallel to the Transfer of PLI insurance business to AEL (as referred to in paragraph 2.8).

	Prior to transfers			Post transfers		
	AMIL	**PLI**	**AEL**	**AMIL**	**PLI**	**AEL**
Assets:						
Cash	3.8	3.9	54.8	3.8	-	58.8
Investments	116.2	-	377.8	113.6	-	380.4
Value of subsidiaries	3.9	-	135.4	3.9	-	130.0
Reinsurance assets	6.1	-	665.3	5.9	-	665.5
Other assets	4.3	-	203.1	4.2	-	203.1
Total Assets	**134.3**	**3.9**	**1,436.4**	**131.4**	**-**	**1,437.9**
Liabilities:						
Insurance liabilities	55.8	-	963.0	54.4	-	964.5
Other liabilities	3.4	-	121.0	3.4	-	121.0
Total Liabilities	**59.2**	**-**	**1,084.0**	**57.8**	**-**	**1,085.5**
Equity	**75.1**	**3.9**	**352.4**	**73.6**	**-**	**352.4**

The Transfers are not dependent therefore one group of policyholders could transfer while the other group remains as AMIL or PLI policyholders.

- For the balance sheet of AEL following only the successful transfer of AMIL's UK policyholders, see Table 8.1.
- For the balance sheet of AEL following only the successful transfer of PLI policyholders, see Table 8.1 in the report titled "Report on the transfer of business from Pedigree Livestock Insurance Ltd to AmTrust Europe Ltd".