Transfer of business from Centriq to OMART

Report by the Old Mutual Alternative Risk Transfer Limited Head of Actuarial Function on the impact of the proposed transfer of the insurance business ring-fenced within the Selonako cell of Centriq Life Insurance Company Limited to OMART in terms of Section 50 of the Insurance Act, 2017

Author: Nicolette Patchett, OMART Head of Actuarial Function

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1. INTRODUCTION

1.1. BACKGROUND

Old Mutual Alternative Risk Transfer Limited ("OMART") is a licensed life insurer, within the Old Mutual Group.

The Centriq Life Insurance Company Limited ("Centriq") is a licensed life insurer, within the Sanlam Group.

Selonako Limited ("Selonako") is a cell owner with Centriq, with all administration and operations of the cell outsourced to AllLife (Pty) Ltd ("AllLife").

AllLife was established in 2004 with the aim of serving a then-seemingly "uninsurable" market segment consisting of people living with HIV. AllLife has successfully achieved "profit with a purpose" by delivering sustainable, high growth, good margin business that positively impacts the lives of its clients, their beneficiaries, and the broader society. The operations of the business have a materially positive impact on the health and longevity of its clients by walking a life-long journey with their clients and providing them assistance with their health management.

In 2018, the AllLife board made significant changes to their executive team. The new executive team reviewed the current business model and structure, engaged OMART to provide them with a third-party cell captive structure, and requested Centriq to transfer the existing life insurance business ring-fenced within the Selonako cell of Centriq to OMART.

As such, Centriq wishes to transfer the existing life insurance business ring-fenced within the Selonako cell, in accordance with Section 50 of the Insurance Act, 2017, to a cell captive structure with OMART. A third-party cell, owned by Selonako, has already been opened with OMART.

As at 31 December 2021, the Centriq financial year-end, Centriq collected approximately R 93m in annual premium in respect of the insurance business ring-fenced within the Selonako cell.

1.2. PURPOSE

One of the requirements of the Prudential Authority for a proposed transfer of insurance business is that the Head of Actuarial Function of the transferee, in this instance OMART, prepares a report regarding the soundness of the proposed transfer.

The purpose of this report is to document my review of the proposed transfer and to record my opinion on:

- The soundness of the transfer;
- The likely effects of the transfer on the security of current and future policyholders; and
- Any potential adverse impacts on the reasonable benefit expectations of policyholders.

This report is produced for the Prudential Authority and looks at the impact of the transfer on OMART as well as the impact on the current OMART policyholders.

1.3. GUIDANCE

In preparing this report I have been guided by Section 50 of the Insurance Act, 2017, as issued in the Republic of South Africa, as well as by the Prudential Standard GOI6, issued by the Prudential Authority which deals with the "Transfers of Business and Other Significant Transactions by Insurers". The insurance standard requires that "the head of the insurer's actuarial function is responsible for expressing an opinion to the board of directors about the soundness of the proposed action as far as the action relates to his or her functions as set out in GOI 3 (Risk Management and Internal Controls for Insurers)".

I have also taken account of the professional guidance set out in Advisory Practice Note 106 ("APN106") and Advisory Practice Note 108 ("APN108") issued by the Actuarial Society of South Africa ("ASSA"). APN106 provides guidance on the statutory duties and professional responsibilities of the head of the actuarial function for South African insurers. APN108 provides guidance on the issues to be considered by an Independent Actuary appointed to assess the desirability of the transfer of life insurance business.

2. INFORMATION AND DATA

In performing the analysis of the impact the transfer will have on OMART, I relied on the following information, amongst others, provided by Selonako, Centriq and OMART.

- Audited financial statements as at 31 December 2021 for OMART;
- The relevant regulatory returns for OMART as at 31 December 2021;
- Email communication confirming the Solvency and Financial position as at 31 December 2021 prepared by Centriq in respect of the business being transferred;
- The transfer agreement between Centriq and OMART;
- The terms and conditions of the OMART policies which will replace the Centriq policies following the transfer;
- The communication plan; and
- The transfer process and timetable.

In addition to this, discussions were conducted regarding the transfer between Centriq and OMART Heads of Actuarial Function.

The data for this transfer, upon which the calculations were based, was provided by AllLife. This included a full extract of the policies in-force as at 31 December 2021. Reasonability checks, which regards to quality and completeness, were performed on the data prior to use.

I am satisfied that the information provided is relevant, reliable and free from bias.

The figures presented in this report are based on the current Prudential Supervisory Reporting basis, Solvency Assessment and Management ("SAM"), of OMART as at 31 December 2021 (the intended effective date of the transaction). Where numbers are shown for the Selonako cell pre-transfer, these have been provided by Centriq and no attempt has been made to verify their accuracy and completeness.

Full audited SAM QRT returns as at 31 December 2021 were available and reviewed for OMART.

A comprehensive review of the impact on OMART's assets, liabilities, and solvency capital requirement ("SCR") have been considered pre and post the transfer and the impacts have been outlined in this report. Furthermore, the adequacy of this review will be included in the external audit review of the transfer of business transaction.

3. OVERVIEW OF THE TRANSFER

3.1. BUSINESS BEING TRANSFERRED

The following categories of products will be transferred from the Selonako cell of Centriq to a third-party cell captive with OMART:

- Risk Individual

The table below contains a summary of the products that will be transferred from Centriq to OMART, with the in-force policy count as at 31 December 2021:

Product	In Force Policy Count	Open to New Business
Advantage Life	2037	Closed
Advantage Life 2.0	9744	Closed
New Advantage Life / Kalibre	55	Closed
Advantage Life for Diabetics	28	Closed
Optimum Life	2395	Closed
Essential Life	27	Closed
Standard Life	736	Closed
Total policies in force	**15,022**	

3.2. HOW THE TRANSFER WILL WORK

The effective date of the transfer will be 31 December 2021, but the actual transfer of policies will take place on or around 1 July 2023, conditional on approval being obtained from the Prudential Authority. Centriq will remain responsible for the policies from the effective date until (and including) 1 July 2023, or until approval has been obtained.

The book to be transferred is closed to new business. A third-party cell, owned by Selonako, has already been opened with OMART through which new business is being sold. OMART already has a binder agreement in place with AllLife, therefore, there will be no change in administration and operational processes that would have an impact on policyholders. The branding of the policies will remain the same after the transfer, however the underwriter will be changed in all client material, e.g. policy documents and terms and conditions, to refer to OMART.

At the same time, premium collections will be moved into a bank account in the name of OMART which has been set up for the Selonako cell. Overall, there should be no impact on either the service or benefits provided to the policyholders.

An additional consideration is the reinsurance treaties currently in place between Centriq and the relevant reinsurers. The intention is for these reinsurance treaties to be transferred to OMART, without any changes to the material and commercial terms, to ensure that no material risks are introduced to the book of business upon transfer.

Only policyholder assets and liabilities will be transferred from Centriq to OMART as part of the Section 50 Transfer. However, as discussed below, given that the liabilities are fully reinsured, the actual amount transferred is R 0.

3.3. REINSURANCE ARRANGEMENTS

As mentioned above, Centriq currently has reinsurance in place in respect of all the insurance business ring-fenced within the Selonako cell. As part of the transfer of business to OMART, Centriq have engaged with the reinsurer to also transfer the reinsurance treaties, on a like-for-like basis, to OMART.

The reinsurance arrangements currently in place are as follows:

Product	Reinsurer	Basic Terms
All	General Reinsurance Africa Limited	• Quota share and reviewable risk premium • No retention

In addition to the above, Centriq also has financial reinsurance in place in respect of a proportion of the insurance business ring-fenced within the Selonako cell. As part of the transfer of the business to OMART, Centriq have engaged with the reinsurer, General Reinsurance Africa Limited, to also transfer this arrangement to OMART.

4. SOUNDNESS OF THE TRANSFER

For the purposes of providing an opinion on the soundness of the transfer, "soundness" may be defined as the ability to maintain post-transfer a financially sound condition as measured on the prudential supervisory basis. The financial soundness on this basis can be evaluated by comparing the excess of assets over liabilities ("Own Funds") with the SCR.

Policyholder liabilities

The policyholder assets transferring will be determined based on a published reporting (IFRS) actuarial valuation of the risk policies being transferred. The basis used has been agreed between OMART and Centriq and is consistent with the Financial Soundness Valuation principles laid out in ASSA's guidance note, Statement of Actuarial Practice 104 ("SAP104").

On an IFRS basis, OMART's liability valuation methodology is to zeroise any negative policyholder liabilities on a component level. In other words, a negative prospective reserve is zeroised, however positive reserves are maintained in respect of any positive IBNR, claims-in-payment and/or discretionary reserves. The negative prospective reserve is determined as the discounted value of projected future cash flows over the policy term, projected separately for gross and reinsurance cash flows. Reinsurance cash flows include premiums related to financing arrangements.

This is in contrast to Centriq's methodology which zeroises the total negative liability net of any positive components. However, a financing repayment liability is calculated in respect of all the financed policies. A corresponding asset of the same amount is raised. Overall, however, the net position is zero as assets and liabilities of the same magnitude are raised.

Upon transfer of the policies to OMART, a positive IBNR and gross pending claims liability - for all claims that have been reported but not yet paid - should be raised to be consistent with and calculated in accordance with the OMART methodology. However, given the quota share reinsurance treaty in place with no retention, a corresponding reinsurance IBNR and pending claims recoverable should also be raised. No financing repayment liability should be raised as this is offset by the negative prospective reserves, which are zeriosed. Overall, the net position is zero as assets and liabilities of the same magnitude are raised.

IFRS Valuation	
Gross IBNR	R 5,850,500
Reinsurance IBNR	R 5,850,500
Net IBNR	**R -**
Gross Pending Claims Liability	R 18,500,000
Reinsurance Pending Claims Recoverables	R 18,500,000
Net Pending Claims Liability	**R -**
Assets to be transferred	**R -**

Financial Soundness Standards

According to OMART's valuation methodology as per the Financial Soundness Standards, referred to as the SAM basis for the purposes of this report, a long-contract boundary, consistent with the underlying policy term is applied. As per the terms and conditions of the underlying policies, premiums are guaranteed for the first 12 months, after which the Insurer may review the premiums at any time to determine whether the premiums then payable are sufficient to continue providing cover. Cover will only be maintained if the policyholder accepts and pays the revised premium.

However, based on the premium escalation patterns (approximately 39% of the book have level premiums, whilst the remaining have low annual escalation rates), it is evident that material pre-funding exists and thus a long-contract boundary is applied.

Solvency Capital Requirement

The capital requirement of the transferred book will be driven by the Life Underwriting Risk component and will increase OMART's SCR by R52.5m, as at 31 December 2021.

The financial positions of the Selonako cell of OMART before and after the transfer on the SAM basis as at 31 December 2021 is summarised as follows:

In R'000	**Selonako**	
	Before transfer	**After transfer**
Solvency Cover		
SCR	**1.09**	**1.21**
Summary of Solvency Position		
Total Assets	-113 844	-220 566
Total Liabilities	-280 345	-468 517
Basic Own Funds / Excess Assets	**166 501**	**247 951**
Own funds eligible to meet SCR	166 501	247 951
Summary of Liabilities		
BEL	-431 847	-672 693
Risk Margin	60 940	81 940
Other liabilities	90 561	122 236
Summary of Capital Requirements		
SCR	**152 660**	**205 266**

The financial positions of OMART before and after the transfer on the SAM basis as at 31 December 2021 is summarized in the table on the following page:

In R'000	OMART	
	Before transfer	After transfer
Solvency Cover		
MCR	4.136	4.129
SCR	**1.037**	**1.035**
Summary of Solvency Position		
Total Assets	5 956 794	5 850 073
Total Liabilities	4 454 272	4 266 100
Basic Own Funds / Excess Assets	**1 502 522**	**1 583 972**
Own funds eligible to meet MCR	874 439	927 046
Own funds eligible to meet SCR	876 863	929 470
Summary of Liabilities		
BEL	3 329 545	3 088 699
Risk Margin	371 950	392 949
Other liabilities	752 777	784 452
Summary of Capital Requirements		
MCR	211 409	224 542
SCR	**845 636**	**898 170**

There will therefore be:

- An increase in OMART's IFRS assets and liabilities as the business will be transferred at a value equal to the IBNR and gross pending claims liability as calculated by OMART. As a result of the 100% reinsurance arrangement the net increase in excess IFRS assets is 0.
- A decrease in the overall OMART SAM liabilities and an increase in the OMART Own Funds as shown in the table above.

Due to the ring-fencing of each cell's assets and liabilities the total OMART Basic Own Funds are only increased by the amount of the SCR in respect of the business being transferred as any excess funds that sit within a cell are excluded from the total calculation as per the Prudential Standard. The SCR will increase as a result of transferring the insurance business ring-fenced within the Selonako cell of Centriq onto the OMART license, and this will result in a slight reduction in the OMART SCR and MCR cover ratios as expected. However, the OMART promoter cell is in a strong financial position with sufficient excess assets, which increase from R 31,228 to R 31,300 post-transfer due to the slight reduction in the SCR of the promoter. In addition, this transfer has no impact on the financial soundness and solvency position of any of OMART's other cells which are individually protected through ring-fencing of their assets and liabilities.

The Centriq book would represent approximately 0.1% of the total OMART gross policyholder liabilities, on an IFRS basis as at 31 December 2021. On the basis that the products being transferred are risk products with similar features to products currently on the OMART license as well as the materiality of the acquisition relative to the existing OMART book, an out-of-cycle Own Risk and Solvency Assessment ("ORSA") was not performed. However, OMART's most recent ORSA, which was approved by its Board in November 2022, includes the impact of transferring the insurance business ring-fenced within the Selonako cell of Centriq onto the OMART license.

In my opinion, based on the above information and the expected impact on the solvency position, OMART will be financially sound on a SAM basis following the transfer.

5. EFFECT OF THE TRANSFER ON POLICYHOLDERS

5.1. SECURITY AND REASONABLE BENEFIT EXPECTATIONS OF POLICYHOLDERS

On a cell captive insurance license, the interests of an individual cell are ring-fenced and OMART requires each cell to be fully capitalized (i.e. maintain eligible Own Funds equal to at least 1x SCR for the cell). As such both the transferring policyholders from Centriq to the Selonako cell of OMART and the existing OMART policyholders (across other cells including the promoter cell) should not be affected adversely by a change in the mix of business on the OMART license. The transfer will improve the security of the existing policyholders of the Selonako cell of OMART given the increase in the cell's solvency cover from 1.09x to 1.21x SCR.

The security of both existing OMART policyholders and transferring policyholders from Centriq is dependent on the financial position of the company. As illustrated in section 3, OMART will be financially sound on a prudential supervisory basis as at the transfer date. In addition, the solvency of each individual cell is unaffected by the transfer because of the ring-fencing requirements of the cell captive license. In addition, no dividends will be paid out of the Selonako cell if the SCR cover ratio is below the multiple prescribed by the OMART Board (currently 1.3x SCR).

Reliance is placed on the work of the HAF for Centriq Life Ltd in determining the pre-transfer SCR cover of the Selonako cell. With reference to the document titled 202203 SCR Report – 10003 Selonako.pdf and subsequent email updates provided by Centriq Life, this has been determined as 1.19x as at 31 December 2021. The SCR cover ratio of the Selonako cell of OMART, which includes existing business written on the OMART license, improves after the transfer to 1.21x. Substantially, there is no change in the security of the policyholders in the Selonako cell following the transfer.

	Centriq **Before transfer**	**OMART** **After transfer**
SCR Solvency Cover	**1.19**	**1.21**

Therefore, the reasonable benefit expectations of policyholders should remain unchanged. The policies will be transferred on the same terms as the original policies and the administration and operational processes will remain with AllLife who currently perform these functions.

5.2. POSSIBLE LOSS OF VALUE TO TRANSFERRING POLICYHOLDERS

The transfer will not result in any loss of value to policyholders as policy terms, conditions and benefits will remain unchanged.

In addition, no fees will be charged to the policyholders as a consequence of the transfer.

As per the opinion of Old Mutual Group Tax, there will be no tax impact for policyholders, due to the following:

- Centriq will transfer risk business from its risk policy fund into a cell in OMART (also a risk policy fund);
- The transaction will not be done in terms of any roll-over provisions as the entities are not part of the same group. The assets will be transferred at market value and Centriq will account for any tax on the transfer of asset; and
- Assets, e.g. reinsurance recoverables, equal to liabilities will be transferred to OMART.

In my opinion, based on the above information, the transfer will not result in any loss of value to the policyholders.

The transfer in no way affects the terms and conditions or reasonable expectations of policyholders in any of OMART's other cells which are individually protected through ring-fencing of their assets and liabilities.

6. PROCESS OF COMMUNICATION WITH THE POLICYHOLDERS

A comprehensive communications plan has been developed that will ensure that all Centriq policyholders are provided with the necessary information relating to the transfer of their policies to OMART. This includes direct communication (in the form of email or posted letters) as well as general communication (in the form of newspaper and Government Gazette advertisements). Additionally, since the administrators do not change, policyholders will continue to contact the same administration staff for information on their policies.

I am satisfied that the process of communication with policyholders (details of which form part of the transfer application) meets guidance provided in the Governance and Operational Standards (GOI6) and maximises the likelihood of reaching all affected policyholders with all the necessary information.

7. CONCLUSION

In conclusion, it is my opinion that:

- the proposed transfer is financially sound and that OMART will be financially sound on a SAM basis following the transfer;
- the security of OMART policyholders is adequately safeguarded; and
- the reasonable benefit expectations of OMART policyholders are not adversely affected by the transfer.