MILLIMAN REPORT

Summary of the Report of the Independent Expert to the High Court of Justice in England & Wales on the proposed transfer of business from FM Insurance Company Limited to the UK branch of FM Insurance Europe S.A.

29 July 2024

Derek Newton, FIA

1. About the Independent Expert's Report and this Summary

1.1 I, Derek Newton, am a principal of Milliman LLP and a Fellow of the Institute and Faculty of Actuaries. I have been appointed as the independent expert to provide, in accordance with Part VII of the Financial Services and Markets Act 2000, a report on the potential impact of the proposed transfer (the "**Scheme**") on the policyholders of FM Insurance Company Limited ("**FMI**") and of FM Insurance Europe S.A. ("**FMIE**") (the "**Scheme Report**"). FMI and FMIE are both members of the FM Global group ("**FM**"), which comprises those companies for which the ultimate parent is Factory Mutual Insurance Company. The Scheme Report is intended to assist the Court in assessing the effect of the proposed transfer on all affected policyholders, in particular commenting on possible material adverse effects in respect of the security of the benefits to which they are entitled under their policies and the levels of service that they could expect to receive post-Scheme.

1.2 In the Scheme Report, I comment only on the Scheme as presented and do not consider any possible alterations or alternative arrangements.

1.3 This is a summary (the "**Summary**") of the Scheme Report, dated 29 July 2024. The Summary is subject to the same limitations on its use as those set out in the Scheme Report. The Scheme Report contains the reasoning behind my conclusions, much of the detail of which I have omitted from this Summary. The Scheme Report also includes further information regarding FMI and FMIE (the "**Companies**"), which I have also not included within this Summary. While I am satisfied that this Summary provides an appropriate synopsis of the Scheme Report, reliance on this Summary alone could be misleading. Copies of the Scheme Report and any subsequent update can be obtained on the webpage dedicated to the Scheme that will be set up by FM on its UK website (the "**Transfer Website**").

1.4 I understand that this Summary will be accompanied by a separate summary that describes the proposed Scheme. Therefore, I have not included further description of the proposed Scheme or of the business to be transferred by the Scheme (the "**Transferring Business**") within this Summary. Furthermore, by way of background, the Scheme Report includes material regarding the insurance regulatory environment, both in the UK, where FMI and the **FMIE UK Branch** (which will receive the Transferring Business) are regulated, and in Luxembourg, where FMIE is regulated. Again, I have not included that material within this Summary.

2. Who will be affected by the Scheme?

2.1 I have determined that only the following policyholder groups might be affected by the proposed Scheme:

- those policyholders of FMI with policies that will be transferring to the FMIE UK Branch under the Scheme (the "**Transferring Policyholders**");
- the current policyholders of FMI whose policies will not be transferred under the Scheme (the "**FMI Non-Transferring Policyholders**") – it is intended that there will be no FMI Non-Transferring Policyholders but, nevertheless, I have considered the impact of FMI Non-Transferring Policyholders in case there are any; and
- the current policyholders of FMIE (the "**Current FMIE Policyholders**").

2.2 I have assessed the current circumstances, security and levels of service, separately for each of the groups of policyholders identified in paragraph 2.1, above, and have then similarly considered the changes that the Scheme is likely to cause to those circumstances, security and levels of service.

3. Will the Scheme affect the Transferring Policyholders?

SECURITY OF BENEFITS

3.1 The Scheme will result in no changes to the terms and conditions of any policy being transferred by the Scheme ("**Transferring Policies**"). The rights and obligations of FMI under the Transferring Policies will be transferred, without alteration, to FMIE.

3.2 I have reviewed the levels of eligible own funds ("**EOF**") held as at 31 December 2023 by both FMI and FMIE (pre-Scheme). I have also reviewed the levels of EOF that would have been held by both FMI and FMIE as at 31 December 2023 had the Scheme been implemented as at that date, and I have considered the projected levels for FMIE (post-Scheme) as at subsequent year-ends up to and including 2026. It is intended by FM that the Scheme, in combination with a separate intragroup agreement (the "**Intragroup Asset Transfer Agreement**"), which will be enacted on the date on which the Scheme is implemented (the "**Effective Date**"), will result in FMI becoming largely a shell company, retaining only sufficient assets to fulfil its regulatory requirements until such time as it can be wound up. Therefore, there are no post-Scheme projections relating to FMI for me to review.

3.3 For both companies, I have compared the EOF with the respective solvency capital requirements ("**SCR**") as at the same dates (actual or projected, as appropriate), the ratio of which I refer to as the **Capital Cover Ratio**. Based on data as at 31 December 2023, the pre-Scheme Capital Cover Ratio of FMI was 231% and the post-Scheme Capital Cover Ratio of FMIE would have been 188%, had the Scheme been implemented as at that date. I note that:

- for an insurer to meet its ongoing regulatory solvency requirements, its Capital Cover Ratio must be above 100%;
- for an insurer to be able to meet all of its insurance liabilities in full, its Capital Cover Ratio must be above 0%; and
- for FMI and FMIE to satisfy their own risk appetites, their respective Capital Cover Ratios must be above 125%.

3.4 I do not consider that a diminution of the Capital Cover Ratio from 231% to 188% would mark a material decline in the security of the financial benefits of policyholders so affected as the likelihood of an insurer with either those Capital Cover Ratios becoming insolvent would be very small.

3.5 I note that the SCRs for FMI and for FMIE have been prepared under different regulations: for FMIE, the SCR has been prepared in accordance with the Solvency II regime that applies throughout the EU; for FMI it has been prepared in accordance with the Solvency UK regime, which is largely the same as Solvency II but which diverged slightly from Solvency II with effect from the 2023 year-end. For the purposes of the Scheme Report, I have considered the SCRs produced under the two regimes to be comparable.

3.6 I further note that the SCRs (actual and projected) in respect of both FMI and FMIE have been prepared in accordance with the standard formula, which was calibrated with reference to the experience across all insurers within the EU (which then included the UK). As such, the SCRs do not necessarily fully reflect the risks faced by FMI or FMIE. Therefore, I have also tested the robustness of FMIE's post-Scheme balance sheet vis à vis the pre-Scheme balance sheet of FMI using four stress tests. In the conditions set by each of these tests, which are based on stresses that I regard as extreme and hence very unlikely, FMIE would remain not only solvent and hence able to meet in full its insurance obligations but also with a Capital Cover Ratio in excess of 125%. I have also tested what combination of stresses applied to FMIE's post-Scheme balance sheet would result in FMIE being unable to meet in full its insurance obligations, including those to the Transferring Policyholders. In my view, the likelihood of all of these stresses (each of which is extreme in isolation) occurring simultaneously is extremely remote.

3.7 Taking all of these aspects into account, I have concluded that the security of the Transferring Policyholders will not be adversely affected to a material extent on implementation of the Scheme by differences in the financial strength between FMI on the one hand and FMIE on the other.

RISK PROFILE

3.8 FMI (pre-Scheme) and FMIE (both pre-Scheme and post-Scheme) are exposed to broadly similar types of risk, due to significant overlap in their respective governance processes and practices, in the types of business that they write and in the investment of their assets. However, there are differences in their profile:

- FMI (pre-Scheme) is smaller than FMIE (both pre-Scheme and post-Scheme).
- The risks of FMI (pre-Scheme), as measured by its pre-diversification SCR, are dominated by market risk, which reflects the high level of excess surplus within FMI, most of which is invested in equities. In FMIE (both pre-Scheme and post-Scheme), market risk is the pre-eminent risk, but other risk types (insurance risk, credit risk and operational risk) are more significant than they are in FMI (pre-Scheme).
- FMIE (both pre-Scheme and post-Scheme) is exposed to a wider geographical range of risk spread than is FMI (pre-Scheme). This provides greater diversification of risk.

3.9 Different risk profiles, insofar as they might affect the future financial security of policyholders, are reflected in the capital requirements of FMI and FMIE. As indicated by the Capital Cover Ratios and verified through stress tests, the likelihood of either FMI, pre-Scheme, or FMIE, post-Scheme, becoming insolvent is negligible. Therefore, I am satisfied that, even though the Scheme will lead to some change to the risk exposures of the Transferring Policyholders, the capital protection available to them post-Scheme will not be materially different to that which they enjoyed pre-Scheme and, therefore, there will be no materially adverse impact on the security of the Transferring Policyholders from a change in the risk profile.

POLICY SERVICING

3.10 There are no material differences between FMI and FMIE in respect of their respective conduct standards and rules or of their respective policy servicing processes and practices. Moreover, with effect from the Effective Date, all members bar one[1] of FMI staff will be transferred to the FMIE UK Branch and will continue to service the Transferring Business in accordance with the current FMI Individual Conduct Rules. Therefore, I am satisfied that the Scheme will result in no change to the management and administration of the Transferring Business.

CHANGE IN REGULATORY ENVIRONMENT

3.11 FMI is regulated by the PRA and the FCA. The FMIE UK Branch is also regulated by the PRA and the FCA, albeit as a Non-Solvency UK firm (as such, it is not required to maintain a solvency margin (as per Solvency UK) but is required to maintain the value of its admissible assets at not less than the value of its liabilities). Otherwise, as a branch operation, the FMIE UK Branch looks to FMIE for its financial strength. FMIE is regulated in Luxembourg by the Commissariat aux Assurances ("**CAA**"). I have noted in the Scheme Report that, although some of the detail of the governance and conduct requirements applying in the UK appear different from those applying in Luxembourg, their effect is very similar.

[1] The member of FMI staff who will not be transferred to the FMIE UK Branch is an engineer who it is intended will instead be transferring to an engineering company that FM is in the process of establishing.

3.12 In the event that FMIE became insolvent post-Scheme, Transferring Policyholders who are not reinsureds would rank alongside Transferring Policyholders who are reinsureds (as well as alongside the Current FMIE Policyholders), whereas, in the event of the pre-Scheme insolvency of FMI, they would have ranked ahead of those Transferring Policyholders. Therefore, in the event of FMIE became insolvent post-Scheme, Transferring Policyholders who are not reinsureds would be worse-off post-Scheme than they would have been pre-Scheme. However, I consider the likelihood of FMIE becoming insolvent post-Scheme to be remote. Therefore, I am satisfied that the Transferring Policyholders will not be materially adversely affected by the implementation of the Scheme in respect of local insolvency rules.

3.13 FMI believes that none of its policyholders are currently eligible to access the Financial Ombudsman Service ("**FOS**"). I note that, were any Transferring Policyholders eligible, pre-Scheme, to access the FOS, post-Scheme they would remain eligible to access the FOS.

3.14 Similarly, FMI believes that none of its policyholders would be eligible for compensation under the Financial Services Compensation Scheme ("**FSCS**"). I further note that, were any Transferring Policyholders eligible, pre-Scheme, to seek compensation from the FSCS, post-Scheme they would remain eligible to seek compensation from the FSCS.

3.15 Therefore, I conclude that, in respect of access to compensation schemes and ombudsman services, the Transferring Policyholders will not be adversely affected by the Scheme.

CONCLUSION

3.16 I am satisfied that the proposed Scheme will not adversely affect, to a material extent:

- The security of benefits under the Transferring Policies;
- The benefits that the Transferring Policyholders could reasonably expect to receive; or
- The standards of administration, service, management and governance that apply to the Transferring Policies.

4. Will the Scheme affect the FMI Non-Transferring Policyholders?

4.1 It is intended that the Scheme will transfer all business from FMI to the FMIE UK Branch and, therefore, the FMI Non-Transferring Policyholders will comprise only those holders of policies that, for any reason, are not transferred by order of the Court on the Effective Date ("**Excluded Policies**"). It is expected that there will be no Excluded Policies. If there were any Excluded Policies then FM would work towards subsequently transferring each and every such Excluded Policy to FMIE, by novation or other means. The Scheme provides that FMIE will meet FMI's obligations in respect of any and all Excluded Policies until such time as those Excluded Policies have been transferred to the FMIE UK Branch.

SECURITY OF BENEFITS AND RISK PROFILE

4.2 Post-Scheme, the Capital Cover Ratio within FMI is projected to be virtually unchanged, although that assessment is based on there being no Excluded Policies post-Scheme and on cash-equivalent assets worth £5 million remaining within FMI, pending the eventual winding-up of FMI. Should the liabilities in respect of Excluded Policies be material then it is possible that the Capital Cover Ratio would be reduced, due to counterparty default risk arising from FMIE's indemnification of FMI in respect of those Excluded Policies, but I consider it highly unlikely that any such reduction in the Capital Cover Ratio would be material.

4.3 I have concluded that the FMI Non-Transferring Policyholders will not be adversely affected by the Scheme in terms of the financial security afforded to their benefits from FMI.

POLICY SERVICING

4.4 The holders of any Excluded Policies would be treated the same as they had been pre-Scheme, with the same standards applied as before. As explained above in paragraph 3.10, all members bar one of FMI staff will be transferred to the FMIE UK Branch, but it is intended that, should there be any Excluded Policies, former FMI employees would be seconded from the FMIE UK Branch to FMI, as necessary, to provide the services required by FMI.

CONCLUSION

4.5 I am satisfied that the proposed Scheme will not affect:

- The security of benefits of the FMI Non-Transferring Policyholders;
- The benefits that the FMI Non-Transferring Policyholders could reasonably expect to receive; or
- The standards of administration, service, management and governance that apply to the policies of FMI that are not being transferred under the Scheme.

5. Will the Scheme affect the Current FMIE Policyholders?

SECURITY OF BENEFITS AND RISK PROFILE

5.1 The Current FMIE Policyholders will see an increase in the financial strength afforded to them, post Scheme, as measured by the Capital Cover Ratio, which (based on the economic balance sheet as at 31 December 2023) would have increased to 188% from its pre-Scheme level of 155%, had the Scheme been effective as at 31 December 2023. Projected balance sheets for year-ends 2024-2026 indicate that the (post-Scheme) Capital Cover Ratio is expected to remain at a level around 180% throughout that period.

5.2 As noted above in paragraph 3.6, I have tested the robustness of FMIE's post-Scheme balance sheet, using a series of stresses that I regard as extreme and as representing the consequences of scenarios that are very unlikely. I have performed, for comparison purposes, similar stress tests on FMIE's pre-Scheme balance sheet. These show that FMIE’s balance sheet would be better able, post-Scheme, to ride out the consequences of the various stresses than it would be pre-Scheme.

5.3 In my view, the financial strength afforded to the Current FMIE Policyholders will, if anything, be enhanced if the Scheme is implemented.

5.4 The risk profile within FMIE will change as a result of the Scheme but not to a material extent, and not so as to be materially adverse for the Current FMIE Policyholders.

5.5 I have therefore concluded that the Current FMIE Policyholders will not be adversely affected by the Scheme in terms of the financial security afforded to their benefits.

POLICY SERVICING

5.6 The existing arrangements for the servicing of the policies of the Current FMIE Policyholders will remain unchanged post-Scheme. Likewise, the terms and conditions of those policies will remain unaltered post-Scheme. Therefore, the Current FMIE Policyholders should experience no change in the servicing of their business.

IN THE EVENT OF FMIE’S INSOLVENCY

5.7 I have concluded that the Scheme does not affect to a material degree the prospects of the Current FMIE Policyholders in the event of the insolvency of FMIE.

CONCLUSION

5.8 I am satisfied that the proposed Scheme will not adversely affect, to a material extent:

- The security of benefits of the Current FMIE Policyholders;
- The benefits that the Current FMIE Policyholders could reasonably expect to receive; or
- The standards of administration, service, management and governance that apply to the policies of Current FMIE Policyholders.

6. Other matters

REINSURANCE

6.1 I have considered the likely effects of the Scheme on the reinsurers whose reinsurance contracts cover the Transferring Business. All reinsurance contracts relating to the Transferring Business will remain in place, albeit with FMI replaced as cedant by FMIE. The amount of the liabilities of each external reinsurer of the Transferring Business will not change as a result of the Scheme. Similarly, due to the transfer to the FMIE UK Branch of the FMI employees, the Scheme will result in no change to the way in which recoveries are managed in respect of the reinsurance protecting the Transferring Business.

WHAT WOULD HAPPEN WERE THE SCHEME NOT TO PROCEED?

6.2 Were the Scheme not to proceed, then

- the Transferring Business would remain with FMI;
- all renewals of that business would be into the FMIE UK Branch, and FMI would be closed to new and renewal business;
- all FMI employees would transfer to the FMIE UK Branch, once it became operational;
- FMIE would second former FMI employees from the FMIE UK Branch to FMI, as necessary, to provide all administrative services required by FMI;
- to the extent possible, the existing business within FMI would be transferred to FMIE, by novation or other means, but otherwise it would simply be run-off. Once the run-off were completed, FM would seek the PRA’s agreement for the cancellation of FMI’s permissions and for FMI to be wound-up.

GEOPOLITICAL ISSUES

6.3 The Companies have negligible and only indirect involvement with the countries affected by the ongoing conflicts in Ukraine and Gaza. Were these conflicts to escalate or to spread then both Companies might be more affected. However, I do not consider that the Scheme increases materially the exposure of any of the groups of policyholders identified in paragraph 2.1, above, to the risks arising from these conflicts.

7. Conclusions

7.1 I confirm that I have been provided with access to all material facts of which I am aware and that I consider relevant in order to assess the proposals under the proposed Scheme, and I further confirm that all information that I have requested in relation to my review has been provided. In performing my review and in producing the Scheme Report, I have relied, without detailed verification, upon the accuracy and completeness of the data and information provided to me by the Companies. My conclusions depend on the substantial accuracy of this data, information and the underlying calculations. At the time of preparing the Scheme Report, I was unaware of any issue that might cause me to doubt the accuracy of the data and other information provided to me by the Companies. As far as I am aware, there are no matters that I have not taken into account in undertaking my assessment of the proposed Scheme and in preparing the Scheme Report, but that nonetheless should be drawn to the attention of policyholders in their consideration of the proposed Scheme.

7.2 In summary, in my opinion, provided the proposed Scheme operates as intended, and I have no grounds for believing that it will not do so, I am satisfied that the implementation of the proposed Scheme would not have a material adverse effect on:

- The Transferring Policyholders;
    - Their benefit expectations;
    - The security of their benefits;
    - The level and standards of administration and service that would apply to their policies;
- The FMI Non-Transferring Policyholders;
    - Their benefit expectations;
    - The security of their benefits;
    - The level and standards of administration and service that would apply to their policies;
- The Current FMIE Policyholders;
    - Their benefit expectations;
    - The security of their benefits;
    - The level and standards of administration and service that would apply to their policies.

8. Supplemental Report

8.1 My analysis has been based upon the material supplied to me, including balance sheets and other information, which themselves are based on accounting positions as at 31 December 2023. I have made allowance for developments that have occurred since those dates, insofar as I have been notified of them.

8.2 Shortly before the date of the Court hearing at which an order sanctioning the Scheme will be sought, I will prepare a supplementary report (the "**Supplemental Report**"), covering any relevant matters that might have arisen since the date of the Scheme Report. This will include consideration of updates to the accounting positions. It is intended that the Supplementary Report will be published on the Transfer Website at least one week before the date of the final Court hearing.

Derek Newton / 29 July 2024

Fellow of the Institute and Faculty of Actuaries