Appointed Actuary's Report on Foundation Life (NZ) Limited's Proposed Scheme of Arrangement

Paul Swinhoe

25 February 2025

Table of Contents

1 Overview 3

2 Proposal to restructure 8

3 New life insurance policy 12

4 Approach to allocation of assets 14

5 Policy valuation 17

6 Outcome of asset allocation 21

7 Illustration of results 24

8 Principles 32

9 Assessment overall 35

10 Assessment of Replacement Cover 38

11 Assessment against principles 46

12 Assessment at Effective Date 53

13 Reliances and limitations 54

Appendix A – Assumptions 55

Appendix B – Glossary 68

Appendix C - Data accuracy 71

1 Overview

1.1 Summary

I have been the Appointed Actuary to Foundation Life (NZ) Limited ("Foundation Life") since 2016. In this report I assess the impact on those participating policyholders ("Eligible Policyholders") subject to Foundation Life's proposal to restructure its policies by means of a scheme of arrangement ("Scheme") under Part 15 of the Companies Act 1993. I conclude that the restructure would be in Eligible Policyholders' individual and collective best interests, and I recommend to Eligible Policyholders that they vote in favour of the Scheme.

1.2 Introduction

The purpose of this report is to set out the Appointed Actuary's views of the Scheme. It explains how Foundation Life will calculate the value to be attributed to each policy ("Policy Value") and how the Policy Values will be applied to pay premiums for new life insurance policies and/or to provide cash to Eligible Policyholders. This is to assist the directors of Foundation Life, the Independent Actuary, the Reserve Bank of New Zealand ("RBNZ"), the High Court and Eligible Policyholders to form their own views on the Scheme. It sets out the results for Eligible Policyholders and the shareholder if the date the Scheme became effective ("Effective Date") had been 30 September 2023.

This report is presented in three parts which cover the following areas:

- Description of the restructuring proposal and the choices available to Eligible Policyholders if they vote in favour of the proposed restructure and the High Court approves it – Sections 2 and 3
- The process by which the assets of the Participating Fund would be allocated to Eligible Policyholders and an overview of the results based on assets and policies in force on 30 September 2023 – Sections 4 to 7
- Assessment of the impact on all policyholders of the proposed restructure by comparing the results with the status quo and against a number of principles – Sections 8 to 12.

1.3 Foundation Life's reasons for proposing to restructure its participating policies

Foundation Life's participating whole of life and endowment policies provide benefits on death, terminal illness, maturity (at age 95 in the case of Whole of Life) or earlier surrender. Foundation Life maintains a separate pool of assets to support its participating policies ("Participating Fund" or "Fund"). Premiums and investment earnings are paid into this Fund. Claims, expenses, tax and the shareholder's share of the profits are deducted. Eligible Policyholders receive their allocated share of the profits of the Participating Fund through Annual and Additional Bonuses.

There were approximately 28,000 policies in the Participating Fund at 30 September 2023. This number is reducing by around 5% p.a. through death, maturity and surrender. No new policies are being sold; the Fund has been closed to new business for over 20 years. Though declining, the Fund still has substantial assets. They were $484m at 30 September 2023. Eligible Policyholders currently pay premiums of $5.2m p.a. into the Fund; this is much less than payments out of the Fund to claimants, which were $29m in the year to 30 September 2023. These and other factors are increasing the expense burden on the remaining Eligible Policyholders.

On 30 September 2023, 232 policies for an extra premium had additional life insurance or the right to take out new insurance in the future without having to provide evidence of good health ("Rider Benefits").

Foundation Life on 30 September 2023 also had 22 non-participating policies.

Foundation Life has recognised that its Eligible Policyholders may be disadvantaged by a product that is inflexible by modern standards, historically low bonus rates that are likely to stay low, and Additional Bonuses on whole of life policies that are projected to reduce to zero over the next 12 years. This situation is driven by:

- The necessity to target a low investment-risk asset allocation (currently targeting 80% fixed interest and 20% growth assets) to help to ensure that Foundation Life can meet its guarantees to Eligible Policyholders
- Increasing expense rates per policy caused primarily by a declining number of policies.

This has led Foundation Life to propose the Scheme. Final approval of the Scheme is subject to a vote by Eligible Policyholders and approval by the High Court.

1.4 Scheme of arrangement

1.4.1 Overview of Scheme

The Scheme involves offering Eligible Policyholders, in exchange for the cancellation of their existing Foundation Life policies, the choice between:

- A replacement non-participating life insurance policy with Chubb Life Insurance New Zealand Limited ("Chubb Life") with no further premiums payable and, for some Eligible Policyholders, the payment of additional cash ("Replacement Cover")
- An all-cash pay-out ("Cash Payment")
- A mixture of the Replacement Cover and the Cash Payment.

All Eligible Policyholders with Rider Benefits will be offered a cash pay-out for their Rider Benefits. As an alternative, those Eligible Policyholders receiving the Replacement Cover in full or in part will be offered, by Chubb Life, similar insurance to their Rider Benefits.

Replacement Cover, including replacement insurance for Rider Benefits, is available to all Eligible Policyholders resident in New Zealand, regardless of the state of health of the life insured under the policy.

Eligible Policyholders will be asked to vote on the Scheme on the basis of documentation containing a description of the Scheme, an independent expert opinion, and indicative offers of the sum insured for Replacement Cover and Cash Payment alternatives for their policy. If Eligible Policyholders vote for the Scheme and the High Court approves it, Eligible Policyholders resident in New Zealand will then be invited to choose whether they wish to receive Replacement Cover, Cash Payment or a mixture. If the 'sufficient assets condition' (see next section) is met, Eligible Policyholders' chosen options will commence on the Effective Date. Existing policies will cease at that time and not before that time, ensuring there will be no gap in cover for Eligible Policyholders resident in New Zealand who want their life cover to continue.

1.4.2 Sufficient assets condition

The Scheme is conditional on the assets of the Participating Fund being sufficient to pay Chubb Life's premium, Eligible Policyholders' Cash Payments, the shareholder's entitlement and other liabilities of the Participating Fund. If this condition is not met, then the shareholder may decide to reduce the amount that it receives so that the condition can be met.

The Scheme will not go ahead if this condition is not met. A major matter affecting this condition is the percentage of Eligible Policyholders who would receive Replacement Cover ("Take-up Rate"). The Take-up Rate is calculated as the ratio of the sum insured provided by Chubb Life divided by the total sum insured offered. I estimate this condition would not have been met at 30 September 2023 at a 75% Take-up Rate or higher.

At a Take-up Rate of 80% at 30 September 2023, the sufficient assets condition would have been met by reducing the shareholder's share of the Participating Fund to $12.6m. I have shown the results in this report on the assumption that the shareholder's share of the Participating Fund would have been reduced to $12.6m.

1.4.3 Replacement Cover

As a result of going through a competitive process of tendering life insurance in the New Zealand life insurance market, Foundation Life selected Chubb Life as the preferred insurer to provide the required life insurance. The sum insured for each Eligible Policyholder's Replacement Cover will be at least 105% of the benefit they would have been paid under their existing policy on the death of the life insured on the Effective Date of the Scheme ("Existing Death Benefit"). It excludes any cover provided by a Rider Benefit. The sum insured will be payable on terminal illness (up to a limit of $500,000, with any remaining sum insured being paid on the death of the life insured), or on the death of the life insured. The sum insured will be guaranteed by Chubb Life and will remain unchanged until it is paid out.

The cash value of Eligible Policyholders' existing policies, as described below, will be used to buy Replacement Cover. Eligible Policyholders will not have to pay any further premiums. Any remaining cash value from a policy after buying life insurance will be paid to the Policyholder, unless the cash value is less than $1,000 and the Policyholder's option is wholly the Replacement Cover, in which case it will be used to buy additional life insurance.

Advantages of the Replacement Cover are that it locks in the current level of Additional Bonuses, it provides a guaranteed amount that is higher than the Existing Death Benefit, and no more premiums are payable. If the Scheme does not proceed, Foundation Life's expectation is for periods where some Eligible Policyholders' future death benefits will be lower than their current death benefit. This is because of the

projected reductions and expected elimination over time of Additional Bonuses, also known as terminal bonuses. If the Scheme proceeds, Eligible Policyholders will not receive new bonuses, which averaged 1.5% in 2023, but will have locked in the current level of their Additional Bonuses ($143m at 30 September 2023), meaning no reduction in their future life insurance cover.

1.4.4 Cash Payment

Eligible Policyholders can choose the Cash Payment. They will then have the freedom to make their own investment decisions to suit their tax situation and other circumstances rather than having the investments chosen by Foundation Life. They may choose, for example, a different investment profile from Foundation Life's and will be free to vary that profile in the future. Alternatively, they will be free to spend some or all of their pay-out. Eligible Policyholders taking cash will also be relieved from paying further premiums.

The existing policies have investment exposure to a portfolio presently targeted to hold 80% fixed interest and 20% equities and property, but with the fixed interest proportion expected to increase in the long term.

Eligible Policyholders with Foundation Life have no choice on the investment mix; all investments are pooled. Also, investment returns from Foundation Life's assets are delivered through bonuses rather than directly as they are earned. Delivering investment returns through bonuses typically delays Eligible Policyholders' receipt of investment returns. Hence the Scheme will give Eligible Policyholders much more flexibility in their investment choices.

In every case the Cash Payment will be at least 5% higher than the surrender value at the Effective Date, with a cap of the Existing Death Benefit.

1.5 Allocation of assets

1.5.1 Use of assets

All the assets of the Participating Fund will be used up, if the Scheme proceeds, in:

- Paying single premiums to Chubb Life for those receiving Replacement Cover, including paying $700,000 towards Chubb Life's set-up costs
- Paying cash to those who will receive a Cash Payment
- Meeting the Participating Fund's obligations to Foundation Life's shareholder in accordance with the shareholder's entitlement (see Section 1.5.3).
- Meeting the remaining liabilities of the Participating Fund, being:
    - Future costs of administering the Scheme including the paying out of Cash Payments
    - Paying a premium to Chubb Life for covering claims that occurred before the Effective Date (whether notified to Foundation Life or not)
    - Other liabilities, being outstanding bills, including tax.

1.5.2 Distribution to Eligible Policyholders

To determine each Policyholder's share of the assets of the Participating Fund, I valued each policy by modelling the future benefits that each policy would have delivered and the costs of administering it. Each policy's value was the present value of those future benefits and expenses less the present value of future premiums. Because the benefits delivered by a policy would vary with the future performance of the Participating Fund, I valued the policies in 10,000 randomly generated different scenarios of future investment returns and took the average. This approach was important to identify and value those scenarios in which, because of poor performance, the Participating Fund assets were insufficient to sustain bonuses and the guaranteed benefits had to be paid from Foundation Life's assets outside the Participating Fund. That the policies contain guarantees of the amounts payable on death and at maturity is a valuable policy feature. Therefore, it was important to use an approach that quantified the value of those guarantees.

The value of each policy will be set at a minimum of 5% above the surrender value at the Effective Date, but not exceeding the policy's death benefit on that date. This ensures there is an immediate benefit available for all Eligible Policyholders if the Scheme proceeds regardless of whether life cover is continued.

1.5.3 Distribution to the shareholder

Assuming the sufficient assets condition is met as per section 1.4.2, the expected shareholder's share of the assets of the Participating Fund has been set at $16.05m. At 30 September 2023 this represented 3.3% of the Participating Fund. See section 2.5 for further details.

1.5.4 Outcome

At 30 September 2023, the Participating Fund had net assets of $484m after providing for other liabilities. Because Eligible Policyholders' choices for the Replacement Cover or the Cash Payment, if the Scheme proceeds, will not be known until the Effective Date, the results shown below are for a range of Take-up Rates, being 20%, 35%, 50%, 65%, and 80%.

Table 1.1 Distribution of the Participating Fund at different Take-up Rates at 30 September 2023

		Insurance Take-up Rate				
		20%	35%	50%	65%	80%
		$m	$m	$m	$m	$m
Insurance recipients	Premium to Chubb Life	98.1	165.1	226.8	293.2	358.9
	Residual Cash	4.9	8.2	11.0	13.3	15.8
All Cash recipients		357.1	286.9	222.3	153.6	88.9
Total allocation to Eligible Policyholders		460.1	460.1	460.1	460.1	463.6
Allocation to the shareholder		16.1	16.1	16.1	16.1	12.6
Other liabilities of the Scheme from 30 September 2023		7.8	7.8	7.8	7.8	7.8
Net assets at 30 September 2023		484.0	484.0	484.0	484.0	484.0

Note: Totals may not exactly add due to rounding

1.6 Rider Benefits

The cost of providing cash or replacement insurance for the 232 policies with Rider Benefits will come from the non-Participating Fund as these benefits are not provided by the Participating Fund. The cash alternative for these benefits totalled $0.05m.

1.7 Surrender values

Surrender values are not guaranteed under the existing policies nor under the new Chubb Life policies. Chubb Life's surrender values will never exceed the single premium paid by Foundation Life for that policy. Eligible Policyholders who receive insurance and who some years later surrender their new policy are likely to receive a lower surrender value than they would have received from their existing policy. This is explained further in section 11.4.4.

1.8 Assessment of impact on Eligible Policyholders

I have considered the benefits to Eligible Policyholders from the Scheme by comparing their situation under their existing policies with their situation if the Scheme proceeds. I developed ten principles for the Scheme to satisfy, as described in section 8, to help me to assess both the Scheme overall and whether it is in the individual Eligible Policyholders' best interests. I confirm that the Scheme meets these principles overall and for each individual Policyholder.

I valued the benefits to Eligible Policyholders from their existing policy and from the Scheme. On my valuation, which treats each Policyholder as being in average health:

- The value of the benefits offered to each Policyholder at the Effective Date would not be less than the value of their existing benefits and in many cases more. Overall, if the Scheme had been implemented on 30 September 2023, then it would have increased the value for Eligible Policyholders by $23.9m at an 80% Take-up Rate of insurance and by $90m at a 20% Take-up Rate.

- No Policyholder will pay further premiums, including those who receive a new policy from Chubb Life. Eligible Policyholders receiving a new policy from Chubb Life will have a benefit on the death or terminal illness of the life insured on the Effective Date that is more than what they had, and the new benefits will be worth no less than the expected benefits from their existing policy.
- Every Policyholder receiving the Cash Payment will receive more under the Scheme than they could at that time surrender their policy for.

The principles described in Section 8 recognise that some lives insured will have below-average health.

1.9 Assessment of impact on non-participating policyholders

Non-participating policies will be transferred to Chubb Life on the Scheme's Effective Date.

The Scheme will change Foundation Life's capital position. This would not affect non-participating policyholders, provided their policies had been transferred to Chubb Life on the Scheme's Effective Date. There are no known reasons for the transfer not occurring. However, in the very unlikely event of the Scheme going ahead but the non-participating transfer failing, the impact on non-participating policyholders would be in how the Scheme would change the capital strength of Foundation Life. The table below illustrates what the capital position of the business would have been on 30 September 2023 immediately after the Scheme had been effected but with the non-participating transfer having failed. It shows the position before those Eligible Policyholders who will receive cash have been paid but after payment of the premium to Chubb Life for Eligible Policyholders who will receive Replacement Cover.

Table 1.2: Foundation Life's capital position immediately after 30 September 2023 if the Scheme had been effected on that date, with no transfer of non-participating policies

	$m
Prescribed Capital Requirement	5.0
Solvency margin	30.1

RBNZ has foreshadowed changes to its solvency requirements. Those changes would have reduced the Solvency Margin by $2.6m at 30 September 2023 to $27.5m.

Either way, this shows a very strong capital position. The security of the non-participating policies is well protected if their transfer to Chubb Life fails but the Scheme proceeds.

1.10 Alternatives considered

The directors of Foundation Life considered a number of alternative approaches for reconfiguring the participating policies, as well as continuing to run the business as is. These are described in the Explanatory Statement. I reviewed those approaches, and I am satisfied that the approach chosen was the best one. My reasons are the same reasons as the directors provide in the Explanatory Statement.

2 Proposal to restructure

2.1 Introduction

This section summarises Foundation Life's life insurance business and how it would be changed by the Scheme.

2.2 Existing policies

2.2.1 Foundation Life's participating products

Foundation Life has two types of participating policy in force. Both pay out on death or terminal illness, pay surrender values, and receive bonuses from the profits of the Participating Fund. Most Eligible Policyholders pay regular, level premiums throughout the policy term. Policies may, however, be made paid-up, meaning no more premiums are payable and the sum insured is reduced. The two policy types are:

- Whole of Life – these policies have a term to age 95. If a claim has not been made before age 95, the sum insured and bonuses are paid at age 95
- Endowment – these policies have a shorter term, typically to ages 60 to 70 of the life insured, as the Policyholder has chosen. They pay out the sum insured and bonuses at the end of the term if a claim has not been made before then.

These policies make up the Participating Fund, a segregated fund that receives the premiums and pays the claims and expenses of the policies. There are approximately 28,000 policies in the Participating Fund. This number is reducing by around 5% p.a. through deaths, maturities and surrenders. No new policies are being sold; the Fund has been closed to new business for over 20 years. Though declining, the Fund still has substantial assets. They were $484m at 30 September 2023. Eligible Policyholders currently pay premiums of $5.2m p.a. into the Fund; this is much less than payments to claimants out of the Fund, which were $29m in the year to 30 September 2023

On 30 September 2023, 232 of these policies had Rider Benefits – see the next section.

2.2.2 Rider Benefits

Additional benefits known as Rider Benefits are provided by some policies for additional premiums. These benefits will be one or more of the following:

- Guaranteed future insurability – this benefit allows the Policyholder, in certain circumstances, to increase the sum insured on their whole of life or endowment policy without having to produce evidence of the life insured's state of health. The increases may be taken once every four years up to age 44, or earlier on marriage or on the birth of a child;
- Level term insurance – increases the benefit on death or terminal illness up to a chosen age. No level term insurance rider goes past age 65. All but one rider have the option to convert into a policy with a longer term than the rider at any time up to the rider's expiry;
- Decreasing term insurance – also increases the benefit on death or terminal illness. The benefit reduces in regular annual steps, expiring at age 60 or 65. The rider has the option to convert into a policy with a longer term than the rider at any time, but not within ten years of the expiry of the rider;
- Total and Permanent Disablement – this benefit pays the sum insured and bonuses of the main policy on the life insured becoming totally and permanently disabled and unable to work again under age 60.

2.2.3 Policies excluded from the Scheme

There will be a cut-off date, the "Record Date", for identifying policies to be covered by the Scheme. The Record Date will be three business days before the meeting of Eligible Policyholders. The policies for lives insured who have died or had a terminal illness claim for their whole sum insured admitted before the Record Date will not be covered by the Scheme. Policies that mature before the Effective Date will also not participate in the Scheme.

2.2.4 Deaths between Record Date and Effective Date

The policies whose lives insured die on or after the Record Date and before the Effective Date will be covered by the Scheme if the Scheme is approved. Rather than being paid a claim based on their current

death benefit they will be paid the higher benefit that the Scheme would have paid under Replacement Cover. This higher benefit does not apply to policies that mature before the Effective Date as they are excluded from the Scheme.

Foundation Life will continue to process claims for terminal illness on or after the Record Date and before the Effective Date. If Foundation Life admits such claims and the Scheme is approved, they will be paid the higher benefit that the Scheme would have paid under Replacement Cover.

2.2.5 Other policy dealings

Foundation Life will cease to accept requests for policy alterations, making policies paid-up and surrenders from the date the Scheme is approved by the High Court.

2.2.6 Chubb Life transfer

Foundation Life will transfer any unsettled claims at the Effective Date to Chubb Life under the agreement with Chubb Life in accordance with the requirements of the Insurance (Prudential Supervision) Act 2010 ("IPSA"). This will include any claims incurred but not reported ("IBNR") at the Effective Date. Foundation Life will pay a premium to Chubb Life of $0.5m to cover these claims in addition to paying the amount of known unsettled claims at the Effective Date.

2.2.7 Non-participating policies

Foundation Life on 30 September 2023 had 22 non-participating policies. Non-participating policies still in force on the Effective Date will be transferred to Chubb Life on that date, not under the Scheme but under a separate contract with Chubb Life. The transfer has to be approved by RBNZ.

The terms of the transfer are that Chubb Life will provide the same insurance benefits as Foundation Life has provided and will require premiums to be paid only on the FuturePlan policy that insures investors with Fisher Funds.

Non-participating policies are discussed further in section 6.3.

2.3 Outline of offer to Eligible Policyholders

The proposal involves offering Eligible Policyholders, in exchange for the cancellation of their existing Foundation Life policies, the choice between:

- A replacement non-participating life insurance policy with Chubb Life ("Replacement Cover"), with a sum insured of 105% of the death benefit under the existing policy. No further premiums will be payable. Some Eligible Policyholders will be offered a further but relatively small amount of extra cover or be paid cash in addition
- An all-cash pay-out ("Cash Payment")
- A mixture of Replacement Cover and Cash Payment.

However, Eligible Policyholders who do not have a residential address in New Zealand will have only the Cash Payment available to them. This is because Chubb Life is able to issue policies only to those with a residential address in New Zealand. See section 2.4.

All Eligible Policyholders with Rider Benefits will be offered a cash pay-out for their Rider Benefits. Those Eligible Policyholders receiving Replacement Cover will also be offered by Chubb Life, as an alternative to a cash pay-out, similar insurance to their Rider Benefits.

Eligible Policyholders with loans (including premium debt) from Foundation Life who repay their loans before the Effective Date will receive their full benefits from the Scheme. Those who do not repay their loans will have the loan balance deducted from their allocation of cash. If necessary, their allocation to the Cash Payment will be increased to be sufficient to repay the loan. The allocation to Replacement Cover will be correspondingly reduced.

Final approval of the Scheme is subject to a vote by all Eligible Policyholders and approval by the High Court. On High Court approval, Eligible Policyholders with a New Zealand address will be asked to choose how they will take their benefits. There will be a default option for those Eligible Policyholders who do not respond of the:

- Replacement Cover for Eligible Policyholders of a whole of life policy
- Cash Payment for Eligible Policyholders of an endowment policy.

Eligible Policyholders who do not have a New Zealand address will not have a choice: they will automatically be given the Cash Payment.

The defaults for Rider Benefits for Eligible Policyholders will be:

- Replacement of Rider Benefits for those who receive Replacement Cover
- Cash for everyone else.

New covers will commence on the Effective Date, at the same time as life insurance cover ceases under the existing policies.

Once the Eligible Policyholders' choices are finalised, the next steps will be for Foundation Life to pay the required premium to Chubb Life, for Chubb Life to issue the new life insurance policies individually, and for Foundation Life to make the cash pay-outs where applicable. When these steps have been completed, the Participating Fund will be closed.

2.4 Overseas Eligible Policyholders

Overseas Eligible Policyholders who want to continue to have life cover may transfer the ownership of their existing policy to a person or entity with a New Zealand residential address ("Replacement Policyholder"). Doing so will not change the life insured covered by the policy. It will, however, mean that Replacement Cover becomes available. Any Policyholder who takes this course will need to be sure that their Replacement Policyholder will act in the Eligible Policyholder's interests. I understand that Foundation Life has provided and will continue to provide guidance and assistance on request to overseas Eligible Policyholders who want to continue to have life cover.

2.5 Distribution to the shareholder

Foundation Life's shareholder will receive $16.05m from the Participating Fund. This will, if required, be adjusted down for any increase in the budgeted net cost for administering the cash pay-out to Eligible Policyholders. The budget for the cash pay-out phase will be redetermined by Foundation Life at the Effective Date.

The shareholder may not receive more than is permitted under Insurance (Prudential Supervision) Regulations 2010. This limitation is unlikely to reduce the amount that the shareholder receives.

2.6 Sufficient assets condition

The Scheme is conditional on the net assets of the Participating Fund being sufficient to pay Chubb Life's premium, Eligible Policyholders' cash pay-outs and the shareholder's entitlement. If this condition is not met, then the shareholder may decide to reduce the amount it receives so the condition can be met.

If this condition is not met, then the Scheme will not go ahead. Whether this condition has been met will become known shortly after the Effective Date. At this time the amount of the assets of the Participating Fund for distribution will be known and Eligible Policyholders will have submitted their choices for the Replacement Cover and/or the Cash Payment. That enables the determination of the premium to pay to Chubb Life, the cash pay-outs and the shareholder's share.

A major matter affecting this condition is the proportion of Eligible Policyholders receiving the Replacement Cover. At 30 September 2023, I estimate this condition would have been met at a Take-up Rate under 75%. I have considered:

- There will be Eligible Policyholders who will prefer to receive the Cash Payment, possibly many
- There are 3% of Eligible Policyholders with Endowment policies whose default is the Cash Payment
- There are 7% of Eligible Policyholders living overseas who will receive the Cash Payment if their policy is still owned by an overseas resident Policyholder on the Effective Date.

Meeting the sufficient assets condition will also depend on which Eligible Policyholders receive Replacement Cover (policy size, age and other factors all have an impact) and on the interest rates applying on the Effective Date, as these affect the premium payable to Chubb Life. Overall, I consider it likely that this condition will be met.

The sufficient assets condition would not have been met at 30 September 2023 at a Take-up Rate of 80% or higher. At 80%, it would have been met by reducing the shareholder's share of the Participating Fund to $12.6m. For this scenario, I have shown the results in this report on the assumption that this reduction would have occurred.

2.7 Scheme expenses

The expenses of the Scheme have been paid by the Participating Fund. The Scheme has been designed to be in the interests of Eligible Policyholders after considering the expenses of the Scheme. If the expenses had been so high as to remove the benefits of the Scheme to Eligible Policyholders, the Scheme could not have gone ahead or not in its current form. In view of the benefits to Eligible Policyholders, I consider it was fair for the Participating Fund to pay the expenses of the Scheme.

3 New life insurance policy

3.1 Replacement Cover

The Scheme provides that:

- Eligible Policyholders will be offered life insurance with a choice as to the level of Replacement Cover. (The trade-off is less cover for more cash.) The choices will be:
  - "Full Cover" - 105% of the Existing Death Benefit, which comprises their sum insured, their Annual Bonuses (also known as reversionary bonuses), and their current rate of Additional Bonus (also known as terminal bonus) on the Effective Date
  - 2/3^{rds} of Full Cover
  - 1/3rd of Full Cover
  - No cover.
- Replacement Cover will:
  - be payable on the death or terminal illness of the life insured whenever that may occur. The terminal illness benefit will be limited to $500,000, with any remaining sum insured being paid on the death of the life insured
  - not change over the lifetime of the life insured
  - be paid for by a single premium payable by Foundation Life on the Effective Date and not require the payment of any premiums from Foundation Life or the Eligible Policyholder in the future.

Eligible Policyholders receiving Full Cover may also receive some cash with their cover, referred to as 'Residual Cash'. However, it is preferable for Foundation Life to avoid paying low amounts of cash to Eligible Policyholders receiving Full Cover if there is a fair and practical way of doing this, due to the disproportionate administration and compliance costs associated with low cash payments and the inconvenience these requirements can cause Eligible Policyholders. Accordingly, Foundation Life will pay cash to Eligible Policyholders taking Full Cover only if the amount of Residual Cash is over $1,000. Otherwise, Foundation Life will use the Residual Cash to buy extra life insurance for the Policyholder.

Those Eligible Policyholders who choose 2/3^{rds} of Full Cover will receive Replacement Cover for 2/3^{rds} of Full Cover and 2/3^{rds} of the Residual Cash (if any) plus 1/3rd of the cash amount they would have received if they had chosen the Cash Payment. Those Eligible Policyholders who choose 1/3rd of Full Cover will receive Replacement Cover for 1/3rd of Full Cover and 1/3rd of the Residual Cash (if any) plus 2/3^{rds} of the cash amount they would have received if they had chosen the Cash Payment. Cash will be paid in full to Eligible Policyholders receiving 2/3^{rds} or 1/3rd of Full Cover even if the amount is under $1,000.

3.2 Premium for Replacement Cover

Foundation Life ran a tender for Replacement Cover, which was won by Chubb Life.

Chubb Life quoted single premiums only. It did not propose to collect annual premiums for three reasons:

- many policies would have had premiums below Chubb Life's minimum
- it was simpler not to
- it makes Replacement Cover more attractive to Eligible Policyholders.

Chubb Life's premium rates as offered to Foundation Life vary with both market interest rates and the Take-up Rate. The premium rates increase as the Take-up Rate reduces. The premium applicable to a policy at a 100% Take-up Rate is the "Base Premium". The increase to the Base Premium that occurs when using the actual Take-up Rate is the "Additional Take-up Premium".

The application of an Additional Take-up Premium is to be expected. This is because the Replacement Cover will, in general, be seen to be more valuable for Eligible Policyholders whose lives insured are in worse than average health and so they will be more likely to select Replacement Cover. Therefore, those receiving Replacement Cover are expected to have above average claim rates. Moreover, the lower the Take-up Rate the higher the claim rates of those receiving Replacement Cover are expected to be. By the same argument, those who receive the Cash Payment would be expected overall to have below average

claim rates. For these reasons, it is reasonable for Chubb Life to charge higher premiums when Take-up Rates are lower.

For each Replacement Cover, payment of the Base Premium will be funded from the Policy Value. Eligible Policyholders whose Policy Value exceeds their Base Premium will receive the balance of their Policy Value in cash or as extra cover (see section 3.1). Where a Policy Value is insufficient to cover the Base Premium, the Participating Fund will make up the difference by paying a "105% Uplift Premium". This will bring the premium up to the amount needed to buy Replacement Cover of 105% of the Existing Death Benefit. Eligible Policyholders who select 2/3^{rds} or 1/3rd of Full Cover will respectively have 2/3^{rds} or 1/3rd of their 105% Uplift Premium for Full Cover (if any) paid by the Participating Fund.

3.3 Chubb Life's premium rates and Pre-agreed Assets

Foundation Life's contract with Chubb Life contains 2 sets of premium rates:

- Pre-agreed premium rates – are premium rates that will be used for buying insurance up to a Take-up Rate of around 88%. They are based on interest rates at June 2018, when interest rates were lower than they were at 30 September 2023. Premiums at these rates will be met by transferring specified assets to Chubb Life ("Pre-agreed Assets") to pay the premium due.
- Effective Date premium rates – are premium rates that will be used only when no more insurance can be bought at the pre-agreed premium rates. They were lower than the pre-agreed premium rates by an average of 19.8% at 30 September 2023.

The Pre-agreed Assets are mostly long-term New Zealand government bonds; there is some cash also. These assets will accumulate coupons on the bonds up to the Effective Date.

If the full amount of the Pre-agreed Assets is not required for purchasing Replacement Covers from Chubb Life, then the balance will be sold and distributed to Eligible Policyholders as part of their Cash Payments.

On the other hand, if the Pre-agreed Assets are insufficient to meet the premium required for the Replacement Covers from Chubb Life, then the additional insurance needed will be bought at Chubb Life's Effective Date premium rates. In this case, the whole of the Pre-agreed Assets will be passed to Chubb Life along with cash to meet the additional premium. Chubb Life has supplied Foundation Life with Effective Date premium rates at 30 September 2023.

3.4 Chubb Life costs

In addition to premiums, Chubb Life will be paid $700,000 to cover part of its set-up costs regardless of the number of Eligible Policyholders receiving Replacement Cover.

3.5 Rider Benefits

Chubb Life will take over the Rider Benefits on similar terms if a Policyholder requests it and when it is the default for Eligible Policyholders who make no request. In these cases, the existing Foundation Life term insurance riders will become new standalone term insurance policies. Their convertibility options (if any) will continue under these new term insurance policies. The guaranteed future insurability benefits and the total and permanent disability rider will become riders to Replacement Cover with Chubb Life. Eligible Policyholders will pay no premiums to Chubb Life for these covers.

The terms of these new policies and riders will be at least as good for the Eligible Policyholders as Foundation Life's terms.

3.6 Underwriting loadings

Some policies pay higher premiums than the standard premium for their life insured's gender and age at entry because of their state of health, their hazardous pastimes or their occupation when the policy commenced. There were 346 such policies at 30 September 2023, paying additional premiums of $17,000 p.a. They have been treated in the same way as standard premium policies, meaning that their Policy Values have been calculated on standard mortality rates allowing for the standard premium being paid. Replacement Cover will be on the same terms as standard policies and at the same premium rates. I have taken the view that the additional premiums these Eligible Policyholders have paid more or less represents the extra risk that Foundation Life has insured and therefore that valuing them no differently from standard Eligible Policyholders leads to no material difference. It is to their advantage that Chubb Life will issue their Replacement Cover at normal premium rates and that no further loadings, or any premiums for that matter, will be required after the Effective Date.

4 Approach to allocation of assets

4.1 Introduction

The proposal is to distribute all of the assets of the Participating Fund by means of:

- Buying insurance for Eligible Policyholders
- Paying cash to Eligible Policyholders
- Allocation to the shareholder of its entitlement
- Meeting administration and wind-up costs.

This section describes the approach to allocating the assets of the Participating Fund. It also covers the value of the Rider Benefits that will come, not from the Participating Fund, but from other assets of Foundation Life.

4.2 Approach

The following steps are required to allocate the assets of the Participating Fund:

- Value Participating Fund assets at the Effective Date, the date for crystallising the premium to be paid to Chubb Life and the individual cash entitlements of Eligible Policyholders
- Deduct known costs of the Scheme and the estimated expenses that will occur on or after the Effective Date that will be met by the Participating Fund (see section 4.4)
- Deduct the cost of benefit enhancements for some Eligible Policyholders (see section 4.5)
- Deduct the shareholder's share of the Participating Fund

to obtain the assets distributable to Eligible Policyholders. Then:

- Use those assets to calculate the value for each policy as described in section 5.
- For those receiving Replacement Cover, deduct their share of the Base Premium from their Policy Value to obtain their cash component, if any
- For those wholly or partly receiving the Cash Payment, deduct their share of Additional Take-up Premiums from their Policy Value.

The following sections explain what each of these steps mean.

4.3 Value Participating Fund assets at the Effective Date

All Participating Fund assets will be valued at realisable value. A significant portion of the assets will be transferred to Chubb Life to pay the premium for Replacement Cover. The remainder, if not already cash, will be sold and held as cash. The assets include policy loans, premium debts and amounts owed to Foundation Life in the normal course of business. Amounts owed to Foundation Life's creditors will be deducted.

4.4 Participating Fund costs

The Participating Fund will meet expenses of $7.8m, made up of:

- Scheme expenses

  The remaining budget for completing the Scheme up to the Effective Date is $4.9m.

- Pay-out costs

  Although premiums for those receiving Replacement Cover will be paid to Chubb Life immediately, it will take some time for the cash distributions to be made. This is because Eligible Policyholders who are to receive cash will have to provide their bank details and return their forms to complete proof of ownership. Therefore, some assets will need to be held back at the Effective Date to meet the expenses of continuing to run the Participating Fund for several months.

  These costs have been estimated to be $7.9m. Some of these costs will be met from interest earnings on the remaining Participating Fund assets. After allowing for these interest earnings, the estimated amount to be set aside for pay-out costs is $2.0m. The actual amount to be set aside by

the Participating Fund for pay-out costs will be determined by Foundation Life on or just before the Effective Date, so giving the Participating Fund certainty as to what its share of this cost will be.

- IBNR claims

  Foundation Life will not have been notified by the Effective Date of all the deaths that occurred before the Effective Date (IBNR claims). Foundation Life will transfer these claims to Chubb Life for a premium of $0.5m payable on the Effective Date.

- Commission

  Foundation Life's designated financial advisers on policies on which they were receiving renewal commission will be paid the equivalent of three years' renewal commission. This is because, if the Scheme takes effect, they will no longer receive commission from these policies. It is anticipated that advisers will provide assistance to their Eligible Policyholders should the Scheme proceed to a vote; Foundation Life will refer Eligible Policyholders who ask for advice on the Scheme to their adviser. The compensation that would have been paid to Foundation Life's designated financial advisers at 30 September 2023, if the Scheme had been adopted then, would have been $0.4m.

4.5 Benefit enhancements paid by Participating Fund

The Participating Fund will also pay for the following:

- 105% Uplift premiums

  The Participating Fund will pay the 105% Uplift premiums for those Eligible Policyholders receiving insurance whose Policy Value is not sufficient to pay for the Base premium for their Replacement Cover, as stated in section 3.2

- Surrender Value minimum

  The cost of raising the Policy Values to 105% of Surrender Value (but to no more that the policy's Existing Death Benefit, as described in section 5.3) will be met by the Participating Fund

- Benefit minimum

  The cost of ensuring that the Scheme benefits have an equal or higher value at the Effective Date than the existing policy's benefits, as described in section 5.4, will be met by the Participating Fund

- Statistical Test

  The Participating Fund will pay for increasing Policy Values to satisfy the statistical test set out in section 5.5.

4.6 Premium Calculation

4.6.1 Chubb Life premiums

At the Effective Date, Foundation Life will know what each Policyholder will receive as their Replacement Cover. Hence the insurance premium to be paid to Chubb Life for each Policyholder can be calculated.

The Chubb Life set-up costs contribution of $700,000 will be allocated to policyholders in proportion to the Chubb Life premiums. In this report, from here onwards, references to Base Premium and to Additional Take-up Premium include the Chubb Life set-up costs.

At a 100% Take-up Rate, the Chubb Life set-up costs are 0.1% of the premium payable to Chubb Life. At very low Take-up Rates the Chubb Life set-up costs could be an unreasonable burden. To avoid this, the Chubb Life set-up costs charged to those taking Chubb Life policies will be no more than 1% of premium. This limit would be effective at Take-up Rates of around 15% or lower. In the unlikely scenario this limit is reached, then the excess Chubb Life set-up costs over 1% of premium will be met from the assets of the Participating Fund.

4.6.2 Effective Date premium rates

To be fair to Eligible Policyholders, the premium rates that they will pay have to be consistent with assets being valued at market value on the Effective Date. This consistency matters since Policy Values are based on the market value of assets. Therefore, Eligible Policyholders will be charged premiums using Effective Date premium rates.

However, the premium payable to Chubb Life will use Pre-agreed premium rates. The amount of the Chubb Life premium using Pre-agreed premium rates will differ from the market value of the assets payable to Chubb Life. At 30 September 2023, the market value was lower.

The premiums payable by Eligible Policyholders need to be equalised with the market value of the assets to be paid to Chubb Life. They will not be exactly equal because of variations in the sum insured, age and gender profile of those Eligible Policyholders receiving insurance from that of the whole portfolio. To resolve this difference, Effective Date premium rates will be scaled up or down so that the total of the Effective Date premiums for those receiving insurance equals the market value of the assets to be paid to Chubb Life on the Effective Date.

4.6.3 Additional Take-up Premium

The Additional Take-up Premiums will be at the Pre-agreed premium rates and, if necessary, at Chubb Life's Effective Date premium rates. The market value of the assets corresponding to the Additional Take-up Premiums is the amount to be deducted from Eligible Policyholders receiving cash in accordance with section 4.8.2.

4.7 105% Uplift Premiums

As stated in section 3.2, should a Policy Value be insufficient to pay the Base Premium for a Policyholder, the Participating Fund will make up the difference by paying a 105% Uplift Premium.

4.8 Policy Value of each policy

How this valuation is performed is described in section 5. It allocates the assets to be allocated to each Policyholder, as described in section 4.2.

The valuation process is an iterative one. This is because the 105% Uplift Premiums and other deductions depend on the Policy Values and vice versa.

4.8.1 Eligible Policyholders receiving Replacement Cover

For those receiving Replacement Cover, the Policy Value will be applied to pay the Base Premium. As stated above, there will be 105% Uplift Premiums for those receiving insurance whose Policy Values are insufficient to meet the whole Base premium. These will be paid from the Participating Fund.

Any remaining Policy Value for those receiving Replacement Cover will be paid in cash to the respective Eligible Policyholders, unless the amount is under $1,000 and the Policyholder is receiving Full Cover, in which case additional life insurance will be bought.

4.8.2 Eligible Policyholders receiving full or partial Cash Payment

The cash allocation to each Policyholder receiving the Cash Payment will be their Policy Value less a deduction for their contribution to the Additional Take-up Premiums.

Those Eligible Policyholders receiving a mixture of the Cash Payment and the Life insurance Option will make a proportional contribution to the Additional Take-up Premium.

4.9 Cash alternative to Rider Benefits

The value of Rider Benefits to Eligible Policyholders was determined by a model of the Rider Benefits. The valuation method and assumptions are specified in Appendix A, section A.9.

The cash value of each rider is a minimum amount of two times its annual rider premium. The results of the Rider Benefit valuation are shown in section 5.7.

5 Policy valuation

5.1 Purpose

The purpose of calculating the Policy Values is to allocate a share of the Participating Fund to each Eligible Policyholder, after allowing for the remaining costs that the Participating Fund must meet and the shareholder's share of the Fund. This allocation must use up all the assets of the Participating Fund.

5.2 Valuation method

5.2.1 Approach

A discounted cash flow approach is used. This approach recognises the cash flows expected for each policy as if Foundation Life continued to manage its policies until they had all been paid out. The Eligible Policyholders' cash flows are the premiums they will pay and the benefits they will receive. To deliver those benefits and to collect those premiums involves the investment of the assets of the Participating Fund and administration of the policies by Foundation Life. There are expenses and taxes incurred in doing so. These cash flows are all components of the valuation. The valuation takes the present value of these cash flows to obtain the value of each policy.

A discounted cash flow valuation recognises that the timing of cash flows is important: cash flows in the near future are worth more than the same cash flows in the more distant future. Cash flows are discounted to the date of the valuation to give their present value.

To value each policy involves the projection and discounting of the cash flows associated with that policy. However, that is not straightforward. It means using probabilities for when policies will claim or remain in force to pay premiums. Furthermore, future benefits will depend on the bonuses awarded to policies. These in turn will depend on the investment performance of the Participating Fund and its claims experience. Foundation Life makes an annual declaration of bonuses after considering the financial results for the year. Foundation Life also may change its mix of assets as it actively manages the assets. Foundation Life does so with the aim of investing to maximise Eligible Policyholders' bonuses while taking an acceptable (very low) level of risk with the security of guaranteed benefits. The bonus declaration and investment mix are two key decisions for Foundation Life that affect Eligible Policyholders' benefits. Those bonuses will vary with the Fund's performance and the decisions that Foundation Life makes in response to that performance and investment markets.

5.2.2 Multiple scenarios

To deal with the range of potential outcomes for Eligible Policyholders, the method chosen was to project the policies in a range of different scenarios. This approach is commonly taken for valuing life insurance business when it features complex relationships between investment performance and policyholder returns, as is the case with Foundation Life's Participating Fund.

A single scenario, that would have to be an 'average' scenario, would not sufficiently pick up that complexity. More particularly, a single scenario would not pick up those uncommon but important cases when the assets of the Participating Fund were insufficient to meet policy liabilities and the shareholder's capital held by Foundation Life was required to help to meet those liabilities. It is in these situations that Eligible Policyholders get value from having the shareholder's guarantee. The valuation method is needed to provide a value for this guarantee. Therefore, a range of scenarios was needed to value each policy.

Each scenario has different investment and inflation outcomes over the period of the projection. The policy benefits will differ as bonuses will differ according to investment conditions, and expenses will differ under different rates of inflation. The bonuses assumed to be declared in each year of each scenario depend on Foundation Life's approach to setting bonuses. Rules have been developed to apply Foundation Life's bonus philosophy to the projected financial situation of the Participating Fund. The projected financial situation also changes the asset mix in line with Foundation Life's investment approach to the Participating Fund. The rules for bonuses were designed to leave no assets remaining in the Participating Fund by the time the last claim is projected to settle in about 70 years' time.

The choice of the scenarios is an important one. They were created to produce 'market consistent' valuations. This means that the average values across all scenarios reproduce the values of financial assets for which reliable market values exist when used to discount the cash flows from those assets. I used 10,000 scenarios. The scenarios are described in Appendix A, section A.5.

5.2.3 Value of a policy

A policy's value in a particular scenario is the discounted value of the benefits paid and the expenses incurred in managing the policy less future premiums. Each policy's value for this report was the average value for that policy over all scenarios. The Policy Value was increased, if necessary, to cover the surrender value minimum (section 5.3) and for the scenario sample size (section 5.5). Pre-paid premiums were added to the Policy Value and policy debts were deducted.

I used the same approach for policies that were still paying premiums and those that were not. That was to be even-handed in the approach; I had no basis for differentiating them. Chubb Life did not seek future premiums whether or not the existing policy was paying premiums. The result was a higher proportion of premium paying policies than paid-up policies requiring the 105% Uplift premiums. However, those uplifts are necessary to make the Scheme in all Eligible Policyholders' interests. If they were not paid then no Eligible Policyholders, including no paid-up Eligible Policyholders, would benefit from the Scheme.

5.2.4 Assumptions

In addition to investment and inflation assumptions, I used other assumptions so I could project all of the cash flows. The assumptions were:

- Mortality and future mortality improvement

  The assumption was that Foundation Life's recent experience of mortality rates would continue, improving at 1% p.a. for ages 80 and under, with no improvement over age 80. Mortality improvement is assumed to cease in 2037.

- Surrender rates

  No surrenders were assumed. Though surrenders occur in practice, assuming no surrenders was reasonable as it reflected the same value for policies whether they surrender or not.

- Maintenance Expenses

  Total expenses for the Participating Fund were assumed to grow with inflation. This meant that unit costs would rise faster than inflation as the number of policies declined, currently at the rate of 5% p.a. The unit costs were capped at $164 per policy, inflation adjusted.

  Total expenses in a year were allocated to policies in proportion to the value of their new Annual Bonus for that year. This approach mirrors how profits are distributed through bonuses. If expenses were higher or lower then profits would be correspondingly lower or higher. Because profits would normally flow to policies through the bonus distribution method used by Foundation Life, it is consistent to allocate expenses in the same way.

- Commission

  Renewal commission is paid at 4% of annual premiums on those policies with a designated adviser. Advisers will be compensated for the loss of future commissions by the payment of a lump sum equivalent to three years' commission, i.e., 12% of one annual premium. The cost of doing this at 30 September 2023 would have been $0.4m.

- Investment management expenses

  Investment management expenses were applied to the projected assets at the rates in Foundation Life's investment management agreement. They were allocated to policies in proportion to each policy's value.

- Bonuses

  Future annual and Additional Bonuses depend on the financial position of the Participating Fund in each scenario. Rules were created, based on existing approaches, to set future bonus rates with the aim of running down all of the assets of the Participating Fund by the time the last policy left the Fund.

  Existing bonus relativities between bonus series were maintained.

- Investments

  The investment mix of the Participating Fund was modelled to change each year to reflect the outstanding term of the policy liabilities and the financial position of the Fund. Rules were created to achieve this, based on Foundation Life's existing investment approach.

The present target investment mix is 80% fixed interest and 20% equities and property. The projections use the target mix, which will change in the long term to have a higher fixed interest allocation. The Fund currently holds no equities or property assets. This was done to make the outcome of the Scheme more certain and for short term tactical reasons. This is not a factor in the assumptions chosen for the projections. Rather, the projected investment mix includes equities and property.

- Shareholder's share of profits

  The shareholder is entitled to 20% of profits under Foundation Life's constitution and under IPSA. I assumed this would continue.

- Tax

  Tax was assessed and charged on the current basis.

More details on these assumptions are set out in Appendix A. This appendix also describes how bonuses and the investment mix are set each year.

5.3 Surrender value minimum

To make sure that the Scheme was adding value for all Eligible Policyholders, the Policy Value is increased, if necessary, to 5% more than the policy's surrender value on the Effective Date, but not more than the death benefit on that date. The increase is to enhance the surrender value so that all Eligible Policyholders enjoy a benefit from the Scheme. The limit of the Existing Death Benefit is to reflect that the main benefit of the policies before maturity is the death benefit, and it would not be reasonable for an enhanced surrender value to exceed the death benefit.

Foundation Life changed its basis for determining surrender values in September 2023. It did this because of a significant fall in the market value of Foundation Life's long-term bonds when interest rates rose, making surrender values unfairly high overall. Surrender values were last reviewed in 2017. The new basis uses stochastic modelling to determine more suitable policy values. There is then a deduction, with the aim that Eligible Policyholders who decide to keep their policies will not face an unfair burden of future expenses.

The outcome was a fall in many surrender values but a rise for some as the new basis achieved greater fairness for Eligible Policyholders. The outcome of the new surrender value basis is that the surrender value minimum produces an increase in the Policy Value for some Eligible Policyholders.

Foundation Life now reviews surrender values three-monthly and will also do so on a significant and sustained change in interest rates. Surrender values can increase or decrease, depending primarily on the change in the value of the assets of the Participating Fund.

5.4 Benefit minimum

A small number of Eligible Policyholders will have their Cash Payment increased to make sure that the value of the benefits from the Scheme is no less than the value of the benefits from the existing policy at the Effective Date.

Furthermore, some Eligible Policyholders receiving Replacement Cover would have had some future years, but only some, when the Scheme's insurance benefit on death was lower than the expected death benefit from their existing policy. They will receive additional cash so that in no year up to the maturity of the existing policy (i.e. age 95 for whole of life policies) would the projected shortfall in the Scheme's insurance benefit be over 2%. The Scheme's insurance benefit for these purposes was the sum insured under Replacement Cover plus the accumulation of any premiums saved on the existing policy and any Residual Cash accumulated with interest.

5.5 Accuracy of the average values

I applied statistical tests to the average value for each policy over the 10,000 scenarios used. A small number of the average values were then increased so that I could have 95% confidence or higher that no policy's average value was more than 1% understated by using a sample size of 10,000 scenarios rather than one million (say) scenarios. Although I could have used a sample size of more than 10,000 scenarios to obtain a more accurate average, it was not cost effective to do so.

5.6 Starting assets

The valuation approach results in the distribution of all of the assets of the Participating Fund with which the projection starts. For the allocation of the Participating Fund to each Policyholder, those starting assets were the market value of assets less the shareholder's share of the Fund, provisions for future costs of the

Scheme, as set out in section 4.4, and payments by the Participating Fund for benefit enhancements as set out in section 4.5.

Because this report is based on an Effective Date of 30 September 2023, the Deferred Tax Asset at 30 September 2023 has no value under the Scheme.

5.7 Rider Benefit valuation

Eligible Policyholders taking Replacement Cover who have Rider Benefits with Foundation Life may continue with cover provided by Chubb Life that would be similar to that provided by their Foundation Life Rider Benefits at no cost to themselves. The cash alternatives at 30 September 2023 totalled $52,957 as shown in the table below.

Table 5.1 Cash value of Rider Benefits at 30 September 2023

Rider Benefits	Number of riders	Offer to Eligible Policyholders
Level term insurance	6	$4,851
Total and Permanent Disablement	1	$335
Decreasing Term insurance	18	$4,622
Guaranteed future insurability	207	$43,149
Total	232	$52,957

6 Outcome of asset allocation

6.1 Introduction

This section shows the overall distribution of the Participating Fund assets of $484m had the Scheme taken effect on 30 September 2023. Examples of results for a sample of Eligible Policyholders are shown in section 7.

6.2 Overall outcomes

The results of the Scheme are summarised below at a range of Take-up Rates.

Table 6.1 Overall results at 30 September 2023

		Insurance Take-up Rate				
		20%	35%	50%	65%	80%
		$m	$m	$m	$m	$m
Insurance recipients	Base premium (excl. 105% Uplift Premium)	101.1	175.0	246.3	311.8	369.9
	105% Uplift Premium	6.8	13.1	22.0	36.6	58.5
	Additional Take-up Premium	9.9	10.0	4.1	3.7	2.6
	Capital loss on Pre-agreed Assets	(19.6)	(33.1)	(45.5)	(58.9)	(72.1)
	Total premium	98.1	165.1	226.8	293.2	358.9
	Residual Cash	4.9	8.2	11.0	13.3	15.8
Cash recipients		357.1	286.9	222.3	153.6	88.9
Total allocation to Eligible Policyholders		460.1	460.1	460.1	460.1	463.6
Allocation to the shareholder		16.1	16.1	16.1	16.1	12.6
Other liabilities of the Scheme from 30 September 2023		7.8	7.8	7.8	7.8	7.8
Net assets at 30 September 2023		484.0	484.0	484.0	484.0	484.0

Note: Totals may not add exactly due to rounding

At 30 September 2023, $15.5m of policy loans and premium debt were outstanding. Eligible Policyholders with loans and premium debt will be allocated sufficient cash to repay them in full, with a corresponding reduction in their allocation to Replacement Cover. These amounts are included in the allocations to Cash recipients.

There were three Eligible Policyholders whose Cash Benefit was no more than enough to repay their policy loans and premium debt. They receive no benefit from the Scheme beyond full repayment of their debt.

The net assets above are at market value. Chubb Life has locked-in its premium rates for the majority, if not all, of the Replacement Cover it will issue. Those premium rates were higher than premium rates would have been at 30 September 2023. In exchange, Foundation Life has locked-in the Pre-Agreed Assets, as described in section 3.3 for paying the Chubb Life premium. Those assets had a lower market value than their locked-in value at 30 September 2023. This is shown as ‘Capital loss on Pre-agreed Assets’ in Table

6.1 for the proportion of the Pre-Agreed Assets that will be paid to Chubb Life. The capital loss on the whole of the Pre-Agreed Assets as at 30 September 2023 was $80.0m.

6.3 Solvency after Effective Date

6.3.1 Introduction

Eligible Policyholders receiving Replacement Cover will be insured by Chubb Life from the Effective Date. Foundation Life will still have to pay cash to those Eligible Policyholders receiving the Cash Payment. Foundation Life's non-participating business will be transferred to Chubb Life on the Effective Date. However, to be prudent, I have assessed solvency on the basis that the transfer of non-participating business fails.

The Scheme does not change the contractual terms of the remaining 22 non-participating policies. The Scheme's impact on non-participating business, should the transfer fail, is solely on the security of those policies.

6.3.2 Foundation Life solvency as at 30 September 2023 post-Scheme

The estimated solvency position for the remaining business post-Scheme is shown in table 6.2 at a Take-up Rate of 65%.

Table 6.2 Foundation Life solvency as at 30 September 2023 post-Scheme

	$m
Total Equity	36.5
Shareholder's Release from Participating Fund	**16.1**
Expense reserve	**(17.4)**
Solvency Capital	**35.1**
Prescribed Capital Requirement	**(5.0)**
Solvency Margin	**30.1**
Solvency Ratio	**703%**

Note totals may not add due to rounding.

This shows a solvency margin of $30.1m. Thus, Foundation Life would have been highly secure as at 30 September 2023 if the Scheme had been effected on 30 September 2023.

RBNZ has foreshadowed changes to its solvency requirements. Those changes would have reduced the Solvency Margin by $2.6m at 30 September 2023 to $27.5m, still highly secure.

At Take-up Rates of over 75%, the release to the shareholder may have been reduced. A reduction would have required further shareholder approval of the Scheme going ahead. Even if the shareholder had received nothing from the Participating Fund, the solvency margin at 30 September 2023 would have been $14.0m and Foundation Life would still have been highly secure.

Take-up Rates under 65% do not have a material effect on the solvency margin. For example, at a 20% Take-up Rate, the solvency margin would have been $1m lower.

6.3.3 Assumptions

The major effect of the Scheme being executed would have been a need for an expense reserve. This is to cover $5.9m of the budgeted expenses of the Cash Payment phase of $7.9m (see section 4.4). The $5.9m is assumed to be covered by interest earnings on the cash held by Foundation Life until it is paid out to Eligible Policyholders. However, it is prudent to reserve that amount until the interest has actually been earned.

Secondly, the expense reserve is to cover the expenses of administering the remaining non-participating business, which, after the Scheme had been executed would greatly exceed the expense loadings in the few remaining policies. It has been estimated to be $14.5m above the prescribed risk charge of $2.0m on the basis of:

- Foundation Life's analyses in determining its annual management expenses and variable per policy costs for its existing business. It identified fixed expenses of approximately $0.8m p.a.
- The annual expenses are discounted by a real gross of tax interest rate of 2.5% p.a. over a period of 18 years, by when no policies will remain in force. This will involve paying out the sum insured of $46,000 on the last remaining policy in 2041, being better for the policyholder and cheaper for Foundation Life than remaining in business with a single policyholder.
- Allowance for wind-up costs of $2.3m as per the 30 September 2023 Financial Statements.

I have assumed that assets will be invested in index linked bonds with a real yield of 2.5% to back the expense reserve thereby matching the interest rate / inflation exposure. The remaining assets will be held in cash, as at present. The yield on inflation linked bonds as reported by RBNZ as at 30 September 2023 ranged from 2.3% to 3% at longer (2040) dated maturities. Taking a mix of maturities into account a real yield of 2.5% is assumed.

Other assumptions were the same as Foundation Life's existing assumptions.

6.3.4 Results

RBNZ has imposed a licence requirement on Foundation Life to hold a minimum solvency margin of $3.0m in the statutory fund. The solvency margin at 30 September 2023 if the Scheme had taken effect then would have been $27.1m above the minimum solvency margin. That shows that Foundation Life would remain in a strong solvency position for the protection of both non-participating business and during the cash pay-out phase.

If the Take-up Rate were 20%, the capital charges would be $1m higher for the cash Pay-out phase, making just a small difference to Foundation Life's solvency position.

7 Illustration of results

7.1 Introduction

This section gives examples of the cash and life insurance options from the Scheme for a range of ages, periods in force, male and female, whole of life and endowment, and paid-up/premium-paying.

These examples compare the projected average death benefit from typical Foundation Life policies with the proposed Scheme benefits. The actual death benefits from the Foundation Life policies would vary with bonuses and could be above or below the average, depending particularly on investment conditions.

The projected Scheme options are presented for two levels of take up of replacement insurance (Take-Up Rate) to demonstrate that the Take-Up Rate influences the value of final Scheme options.

None of these examples is of an actual policy, for reasons of privacy, but they are representative.

7.2 Case 1

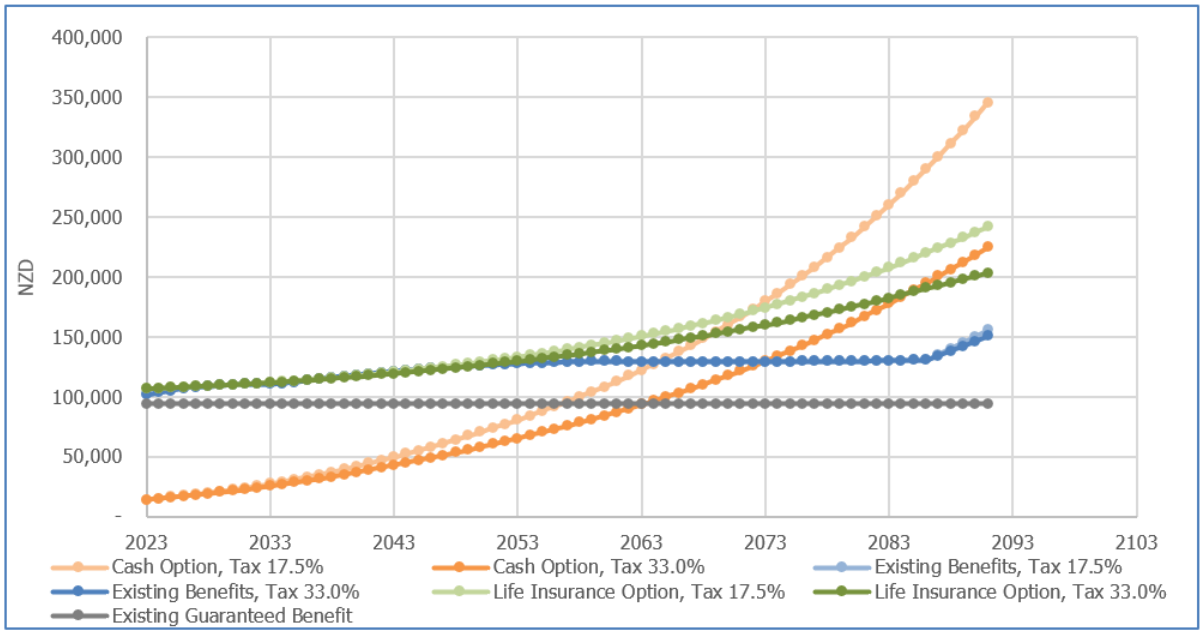
Existing Policy Characteristics			
Age	32	**Current Death Benefit**	$101,883
Gender	Female	**Surrender Value**	$13,788
Product Type	Whole of life	**Annual Premium**	$427.21
Risk Commencement Date	1 Aug 1991		

		Scheme Options			
80% Take-Up Rate	**Existing Policy**	**Full Cover**	**Two Thirds Full Cover**	**One Third Full Cover**	**All Cash**
Death Benefit	$101,883	$106,976	$71,318	$35,658	-
Cash Payment	-	-	$4,826	$9,652	$14,477

		Scheme Options			
50% Take-Up Rate	**Existing Policy**	**Full Cover**	**Two Thirds Full Cover**	**One Third Full Cover**	**All Cash**
Death Benefit	$101,883	$106,976	$71,318	$35,658	-
Cash Payment	-	$1,206	$5,868	$10,532	$15,194

Case 1 receives the surrender value minimum benefit of 105% of surrender value at an 80% Take-up Rate and a higher benefit at a 50% Take-up Rate.

Chart 7.1 – Projections of Case 1's Existing Death Benefit (blue lines) compared with projected Scheme benefits at a 65% Take-up Rate. Projections for the Replacement Cover are in green, and the projections for the Cash Payment are in orange.



Case 1's projected death benefits are the blue lines in the chart and comprise the initial sum insured plus projected Annual Bonuses and Additional Bonuses up to age 95. The blue lines rise more sharply from age 95 as the chart includes the interest expected to be earned on the pay-out at age 95.

The line shown in grey is the amount of the death benefit that was guaranteed at 30 September 2023. Benefits above the grey line depend on future Annual and Additional Bonuses that in turn will depend, amongst other things, on the investment performance of the Participating Fund.

Projections for the Replacement Cover for two tax rates, dark green for a Policyholder subject to a 33% marginal tax rate and a light green line for a 17.5% marginal tax rate, comprise:

- Replacement Cover, being 105% of the Existing Death Benefit
- Savings which come from not paying any more premiums, accumulated with interest
- Any Residual Cash payable to the Policyholder, accumulated with interest.

Projections for the Cash Payment for two tax rates, dark orange for a Policyholder subject to a 33% marginal tax rate and a light orange line for a 17.5% marginal tax rate, comprise:

- The cash balance paid to the Policyholder, accumulated with interest
- Savings which come from not paying any more premiums, accumulated with interest.

On 30 September 2023 the maximum personal tax rate was 39%. This was for incomes over $180,000 p.a. The tax rate was 33% for incomes from $70,001 up to $180,000. The 33% marginal tax rate was used to be conservative for most Foundation Life Eligible Policyholders. Foundation Life expects very few Eligible Policyholders to be paying tax on their investment income at 39% for the rest of their life. 17.5% was the marginal tax rate on incomes between $14,001 and $48,000 on 30 September 2023.

Interest has been accumulated at the risk-free interest rate, which was used to ensure consistency with the modelling used to derive existing policies' expected death benefits. All other examples in this section are on the same basis.

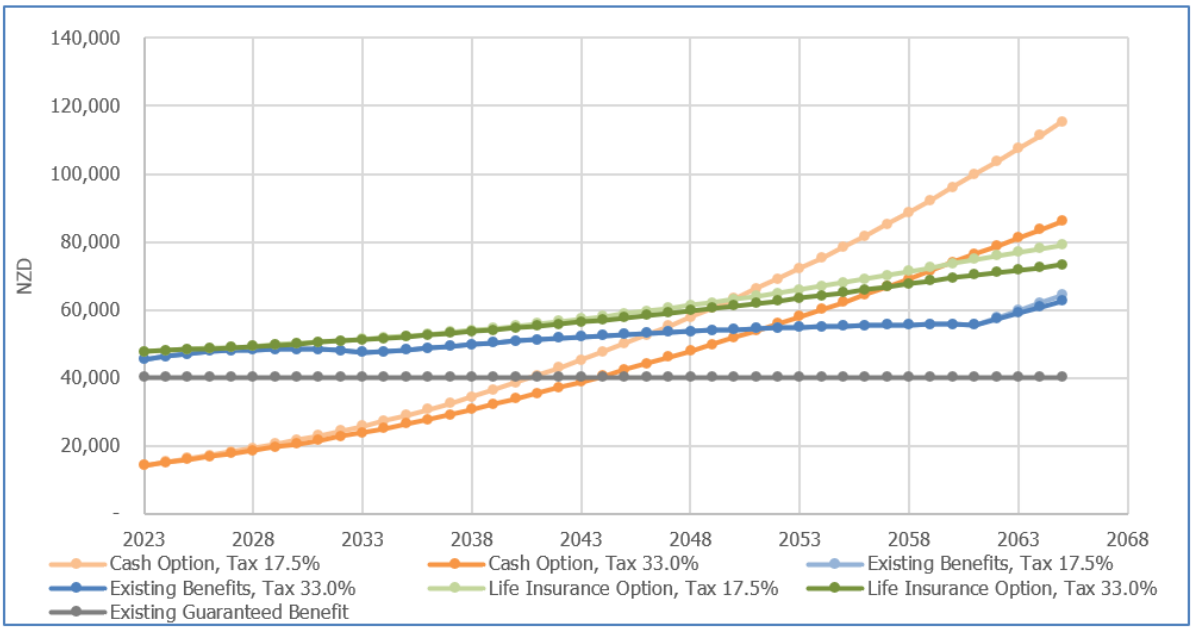
7.3 Case 2

Existing Policy Characteristics			
Age	58	**Death Benefit**	$45,531
Gender	Male	**Surrender Value**	$11,668
Product Type	Whole of life	**Annual Premium**	$290.85
Risk Commencement Date	1 November 1982		

80% Take-Up Rate	Existing Policy	Scheme Options: Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$45,531	$47,808	$31,872	$15,936	-
Cash Payment	-	-	$4,084	$8,167	$12,251

50% Take-Up Rate	Existing Policy	Scheme Options: Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$45,531	$47,808	$31,872	$15,936	-
Cash Payment	-	-	$5,170	$10,338	$15,508

Chart 7.2 – Projections of Case 2's Existing Death Benefit compared with projected Scheme benefits.



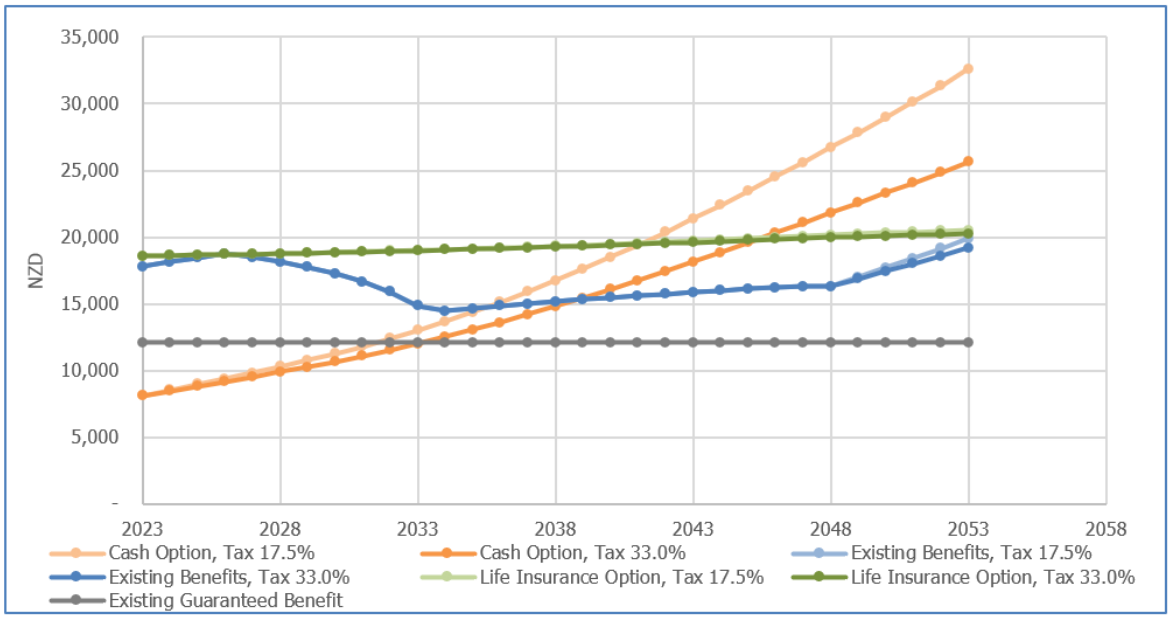
7.4 Case 3

Existing Policy Characteristics			
Age	70	**Death Benefit**	$17,714
Gender	Male	**Surrender Value**	$7,275
Product Type	Whole of life	**Annual Premium**	$34.15
Risk Commencement Date	1 April 1964		

80% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$17,714	$18,600	$12,400	$6,200	-
Cash Payment	-	-	$2,547	$5,093	$7,639

50% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$17,714	$18,600	$12,400	$6,200	-
Cash Payment	-	-	$2,833	$5,666	$8,499

Chart 7.3 – Projections of Case 3's Existing Death Benefit compared with projected Scheme benefits.



This case shows (blue lines) how the expected reduction in Additional Bonuses starting in 2026 reduces the existing expected death benefit.

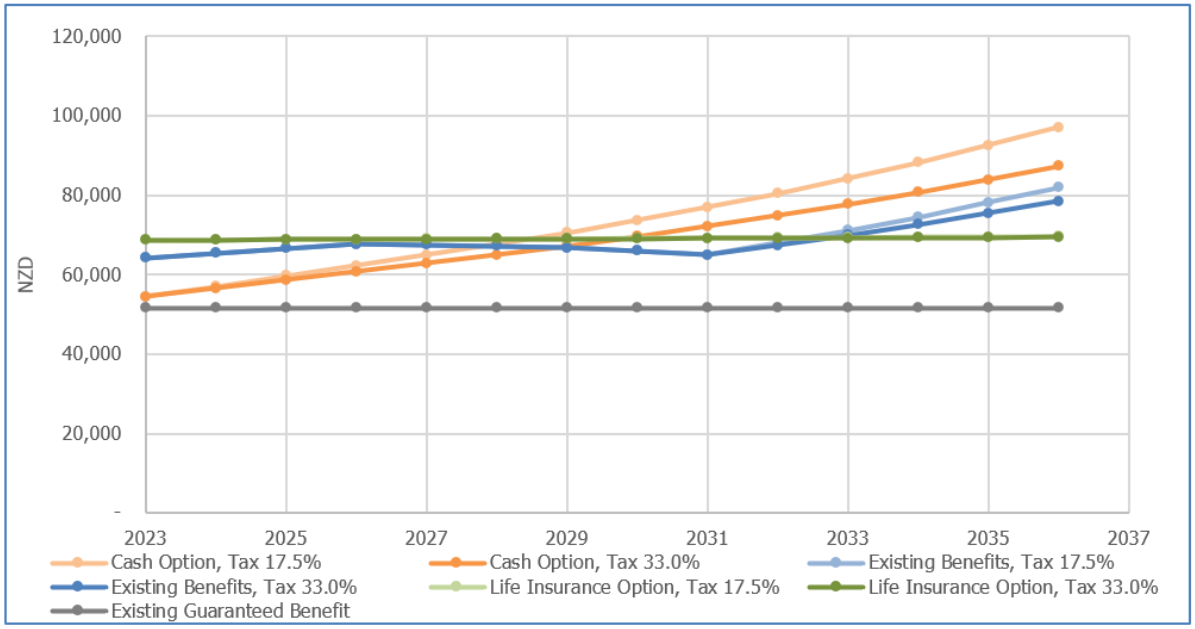
7.5 Case 4

Existing Policy Characteristics			
Age	87	**Death Benefit**	$64,347
Gender	Male	**Surrender Value**	$51,858
Product Type	Whole of life	**Annual Premium**	-
Risk Commencement Date	1 June 1974		

80% Take-up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$64,347	$67,564	$45,043	$22,521	-
Cash Payment	-	$1,161	$18,151	$36,301	$54,451

50% Take-up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$64,347	$67,564	$45,043	$22,521	-
Cash Payment	-	$1,161	$18,151	$36,301	$54,451

Chart 7.4 – Projections of Case 4's Existing Death Benefit compared with projected Scheme benefits.



This is another case that illustrates the expected reduction in Additional Bonuses starting in 2026.

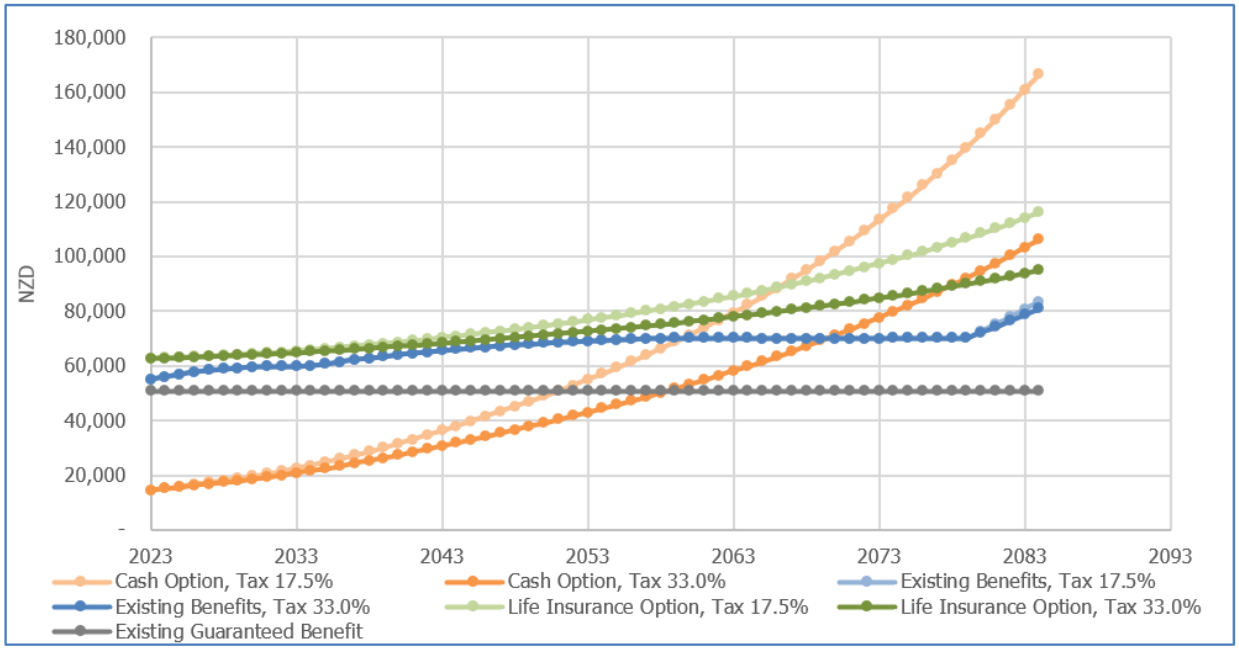
7.6 Case 5

Existing Policy Characteristics			
Age	39	**Death Benefit**	$54,804
Gender	Female	**Surrender Value**	$10,083
Product Type	Whole of life	**Annual Premium**	-
Risk Commencement Date	1 February 1997		

80% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$54,804	$57,544	$38,362	$19,182	-
Cash Payment	-	$3,779	$6,339	$8,900	$11,462

50% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$54,804	$57,544	$38,362	$19,182	-
Cash Payment	-	$6,036	$9,257	$12,480	$15,701

Chart 7.5 – Projections of Case 5's Existing Death Benefit compared with projected Scheme benefits.



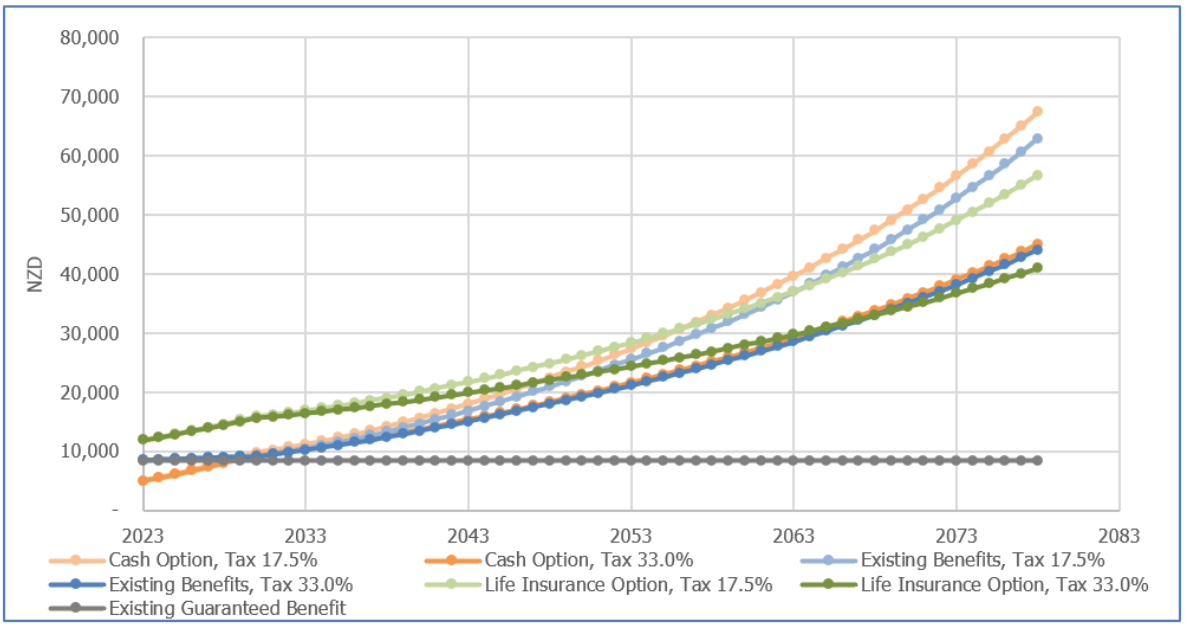
7.7 Case 6

Existing Policy Characteristics			
Age	45	**Death Benefit**	$8,609
Gender	Male	**Surrender Value**	$4,807
Product Type	Endowment	**Annual Premium**	$372.56
Risk Commencement Date	1 December 2009	**Maturity Date**	1 December 2029

80% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$8,609	$9,038	$6,026	$3,013	-
Cash Payment	-	$2,900	$3,616	$4,332	$5,048

50% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$8,609	$9,038	$6,026	$3,013	-
Cash Payment	-	$3,002	$3,704	$4,407	$5,110

Chart 7.6 – Projections of Case 6's Existing Death Benefit compared with projected Scheme benefits.



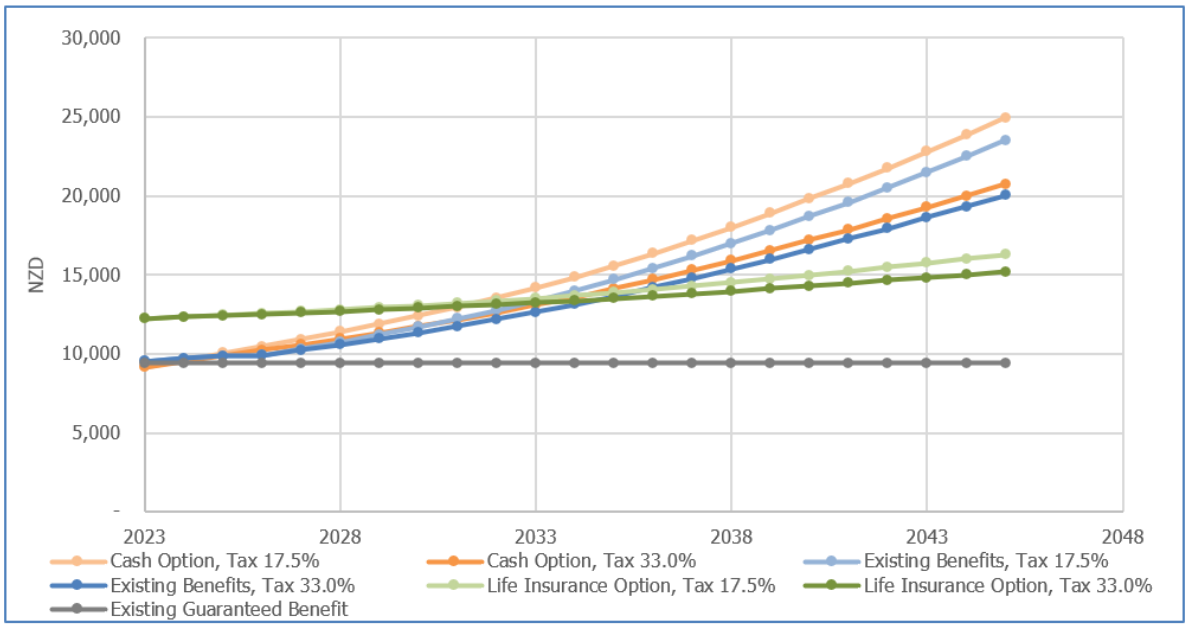
7.8 Case 7

Existing Policy Characteristics			
Age	78	**Death Benefit**	$9,399
Gender	Male	**Surrender Value**	$8,727
Product Type	Endowment	**Annual Premium**	-
Risk Commencement Date	1 December 1945	**Maturity Date**	1 December 2025

80% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$9,399	$9,869	$6,580	$3,290	-
Cash Payment	-	$2,363	$4,629	$6,896	$9,163

50% Take-Up Rate	Existing Policy	Scheme Options			
		Full Cover	Two Thirds Full Cover	One Third Full Cover	All Cash
Death Benefit	$9,399	$9,869	$6,580	$3,290	-
Cash Payment	-	$2,363	$4,629	$6,896	$9,163

Chart 7.7 – Projections of Case 7's Existing Death Benefit compared with projected Scheme benefits.



8 Principles

8.1 Introduction

To assess whether the Scheme is in Eligible Policyholders' best interests I have identified ten principles that the Scheme must meet.

The principles recognise the individual circumstances of Eligible Policyholders that matter in deciding whether the Scheme is in their individual best interests. It is usual in life insurance to assess policies on assumptions that are appropriate to the business as a whole. For example, the mortality assumption used in valuing policy liabilities will normally be an average assumption reflecting the expected mortality rates of the pool of lives insured. It would not reflect the circumstances of any particular Policyholder. Pertinent to the Scheme and the existing life insurance benefits that Foundation Life provides, Eligible Policyholders will be in a range of states of health. Some will be terminally ill; at the other end of the scale some will be on track to live past age 100. The principles for assessing the Scheme need to allow for the wide range of Eligible Policyholders' individual circumstances.

These circumstances will include a range of personal goals and financial situations, all of which can change over time. They include Eligible Policyholders' desires to hold life cover and the amount of cover. They also include their appetite for investing in growth assets and the returns they expect from their investments, after tax. For these reasons, Eligible Policyholders will assess the Scheme differently from one another; hence the need for a set of principles for determining whether the Scheme is in all Eligible Policyholders' best interests.

I have taken note of RBNZ's guidance on transfers of life insurance business under section 44 of IPSA. Even though it does not apply to the Scheme, there is sufficient commonality for parts of the guidance to be relevant. For a transfer of life insurance business under section 44 of IPSA, section 48 of IPSA says that RBNZ must consider:

- The ability of the transferee to comply with solvency requirements
- The interests of the policyholders of the insurers that are parties to the proposed transfer or amalgamation
- Any other matter RBNZ considers relevant.

Taking the above together with the guidelines, I consider the important matters to be the contractual rights of Eligible Policyholders, their benefit expectations in addition to those contractual rights, and the security for the policyholders of Foundation Life of their benefits post-Scheme. These are reflected in the ten principles stated in section 8.3.

8.2 Non-financial considerations

The purpose of the Scheme is to give financial advantage to Eligible Policyholders by addressing the financial disadvantages that the existing business faces. Eligible Policyholders may, however, have non-financial reasons either for supporting the Scheme or for preferring no change to their existing policies. Non-financial reasons for a Policyholder are totally valid and will be able to be expressed in the vote on the Scheme. They do not, however, form a part of my assessment of the Scheme. My assessment is from a financial viewpoint. Even though there will be some Eligible Policyholders who are happy with the status quo, the Scheme should not be prevented from proceeding so long as those Eligible Policyholders are no worse off.

8.3 Ten principles

The principles so determined are:

	Principle	Comment on Principle
1	The tests are on Eligible Policyholders with a New Zealand residential address.	Foundation Life has sold policies only in New Zealand. Some Eligible Policyholders have subsequently left the country. The different treatment of existing policy benefits and Scheme benefits for tax or other purposes is just one of many consequences for a Policyholder of choosing to live in a different country. New Zealand based Eligible Policyholders should not be disadvantaged because of the requirements of non-New Zealand based Eligible Policyholders.
2	Life cover in place must be honoured.	Any Eligible Policyholder who wants to keep their guaranteed death benefit (sum insured plus existing bonuses) must as a minimum be able to do so. Eligible Policyholders should not be forced to take cash instead.
3	No Eligible Policyholder overall should be worse off when compared with the Eligible Policyholder's reasonable expectations for their existing benefits.	This principle applies to all Eligible Policyholders, but particularly to Foundation Life's most vulnerable Eligible Policyholders. These include the sick, the elderly, and those on a low income. The matters to consider include: a) Life cover where life cover is continued b) Any benefit payable on terminal illness c) Surrender values d) Future premiums not to increase e) The security of future benefits. Irrespective of the 'value for money' that a premium increase might provide, it was considered that many Eligible Policyholders would consider a premium increase unacceptable.
4	The design in the opinion of the shareholder must not be disadvantageous to the shareholder.	The shareholder will not agree to a design they do not see as being in their interests. Being a major transaction, the Scheme cannot proceed without being approved by the shareholder.
5	Allocation of Scheme costs between Eligible Policyholders and the shareholder to be fair and seen to be fair.	The test for this is subjective, but it is a principle, nevertheless. It requires an acknowledgement of the benefit to the shareholder from being released from the cost of the shareholder's guarantee.
6	The design must ensure the whole of the 'distributable fund' is distributed to Eligible Policyholders.	The 'distributable fund' is the Eligible Policyholders' share of the Participating Fund after allowing for the shareholder's entitlement, the Participating Fund wind up expenses, and the Participating Fund's share of the Scheme expenses. The principle is necessary because: • It is a shareholder requirement for the Scheme to proceed that the Participating Fund will be wound up, and • The shareholder is entitled to 20% of profits from the Participating Fund and no more. So, there could be a problem if there were significant unclaimed money left in the Participating Fund following the Scheme's implementation.

	Principle	Comment on Principle
7	The allocation of the 'distributable fund' between Eligible Policyholders to be fair and seen to be fair.	The test for this is subjective, but it is a principle, nevertheless.
8	In assessing overall benefit to a Policyholder, a greater weight is given to benefits that might be payable in the short term (less than ten years) than to those that might be payable in the long term (more than ten years).	People plan and focus on the near term much more than on events many years away. In part this is because people's needs in the next five years are much more predictable than, for example, their needs in 25 years' time. Similarly, the benefit Foundation Life could deliver in 25 years' time, which is only relevant if the life insured is still alive, is less predictable.
9	If an Eligible Policyholder can be advantaged without disadvantaging other Eligible Policyholders, then do it.	The purpose of the Scheme is to advantage Eligible Policyholders as much as possible. So, it is desirable to give Eligible Policyholders choices over the form in which they will take their benefits if it can be done without disadvantaging other Eligible Policyholders.
10	It should be simple in design and the options for Eligible Policyholders easy to explain.	Eligible Policyholders will be asked to vote on the Scheme and to decide what form of benefit to take. Eligible Policyholders, many of whom are elderly, need to understand the choices. With a complex design, there would be a greater risk of Eligible Policyholders making poor choices through misunderstanding. A complex design is also likely to be more expensive to execute.

9 Assessment overall

9.1 Introduction

This section shows how the Scheme adds value for Eligible Policyholders as a whole. This provides context for the assessments that follows. Section 10 covers the life insurance aspects of the Scheme. Section 11 contains the assessment of the Scheme against the ten principles set out in section 8.

This section also shows my assessment of Eligible Policyholders' voting rights. It comments on the security for those Eligible Policyholders who will be taking Replacement Cover with Chubb Life. It also covers the security of Foundation Life's non-participating policies immediately after the Scheme is effected in the unlikely event that their transfer to Chubb Life fails.

9.2 Value of existing policies

The Scheme will be subject to an approval process involving a vote of Eligible Policyholders and High Court approval. I have compared the value for Eligible Policyholders at the point the result of the approval process is known. Then, either the existing policies will continue or the Scheme benefits will be given to Eligible Policyholders.

For this report, this is as at 30 September 2023, when the net assets of the Participating Fund were $484m. Provision has been made for the Scheme expenses that would have continued to be incurred up to the date of the High Court hearing.

If the Scheme was rejected by Eligible Policyholders, the existing policies would continue unchanged. This would mean that benefit payments would continue to be made to Eligible Policyholders, who would continue to pay premiums. There would also be payments from the Fund for the costs of administering these policies, commission to advisers, investment management of the assets, tax and for transfers to the shareholder. The present values of these amounts are set out in the table below. It shows that Eligible Policyholders, on a net present value basis, would have received 69% of the net assets at 30 September 2023.

Table 9.1 Projection of how the Participating Fund would have been used assuming no Scheme

Present value of payments for:	Value $m	Value as % of assets
Death and Maturity Benefits	387.9	
Premiums payable to Foundation Life	(52.1)	
Net Eligible Policyholder insurance benefits	335.8	69%
Administration expenses	56.0	12%
Renewal commission to advisors	1.3	<1%
Investment Management Expenses	14.7	3%
Tax	48.3	10%
Value of future Shareholder Transfers	24.5	5%
Scheme expenses up to High Court hearing	3.4	1%
Net Assets at 30 September 2023	484.0	100%

At 30 September 2023, the Participating Fund had a Deferred Tax Asset of $17.2m on its balance sheet as an ongoing business. That asset would reduce future tax payable by Foundation Life. Its value is reflected in higher death and maturity benefits above than if there had been no such asset. Correspondingly, the value of future tax payments above is lower than it otherwise would have been.

9.3 Value of Scheme benefits

Table 9.2 below shows the values for Eligible Policyholders if the Scheme had become effective on 30 September 2023. It shows that Eligible Policyholders would have received insurance and cash benefits that would have been worth more than their existing benefits (valued at $335.8m in table 9.1) by $23.9m at an 80% Take-up rate to $90m at a 20% Take-up Rate. The value of benefits to Eligible Policyholders would have increased from 69% to between 74% and 88% of the net assets of the Participating Fund. The increase mainly arises from Eligible Policyholders paying less for future administration expenses and tax if the Scheme is implemented.

Table 9.2 Projection of the value from the Participating Fund if the Scheme had become effective on 30 September 2023

	Insurance Take-up Rate				
	20% $m	**35% $m**	**50% $m**	**65% $m**	**80% $m**
Eligible Policyholder insurance benefits	63.7	111.5	159.3	207.2	255.0
Additional cash for insurance receivers	4.9	8.2	11.0	13.3	15.8
Cash for Cash Payment recipients	357.1	286.9	222.3	153.6	88.9
Net Eligible Policyholder benefits	425.8	406.6	392.6	374.1	359.7
Allocation to the shareholder	16.1	16.1	16.1	16.1	12.6
Value of Eligible Policyholder benefits as % assets	88%	84%	81%	77%	74%
Value of the shareholder's allocation as % of assets	3.3%	3.3%	3.3%	3.3%	2.6%

Note: Totals may not exactly add due to rounding

9.4 Voting rights

The Scheme is subject to a vote by Eligible Policyholders. To succeed, Eligible Policyholders who vote "for" the Scheme must do so:

- by more than 50% in number (i.e. one vote per policy) of the policies held by Eligible Policyholders who vote, and
- representing not less than 75% in attributed value of the policies held by Eligible Policyholders who vote. For this purpose, each Eligible Policyholder will have a value attributed equivalent to the Surrender Value of their policy as at the Record Date.

9.4.1 Voting proportions

The proportions of 50% and 75% are the prescribed statutory thresholds of parts 14 and 15A of the Companies Act 1993. Though not applicable to this Scheme, it provides a benchmark. I have considered the specific details as follows:

- 50% by number is appropriate because it is a straight majority as used in many voting systems and gives equal weight to each policy
- 75% by value is appropriate because it makes it harder for large policies voting for the scheme to dominate small policies than the use of a 50% threshold

- Using a proportion of those who vote is appropriate because it is used in the Companies Act 1993. It would also be detrimental to Eligible Policyholders if a low voting turn-out led to a Scheme voted as being in Eligible Policyholders best interests not proceeding.

9.4.2 Surrender value

I consider surrender values to be an appropriate measure of value for voting purposes. They are a reasonable proxy for the relativities between the Policies' current values and are readily obtainable. They are preferred to Policy Values for the purposes of the Scheme because, at the Record Date, only estimates of the Policy Values are available because Policy Values will depend on the choices Eligible Policyholders make for Replacement Cover and the Cash Payment.

Surrender values have the desirable features that they:

- Are designed to give Eligible Policyholders a reasonable value for their policy on the basis of the value accumulated in the policy
- Like Policy Values, are expected to increase over time with payment of premiums and the accretion of investment earnings
- Use the important parameters of the policy, being age of the life insured, gender of the life insured, duration of policy, sum insured, accumulated bonuses and annual premium, as do Policy Values.
- For altered policies, surrender values and Policy Values reflect the terms of the alteration.

Therefore, surrender values provide a reasonable way of reflecting the different values of policies for voting purposes.

9.4.3 Voting class

Eligible Policyholders will form a single class for voting purposes. I have considered whether a group of Eligible Policyholders could be disadvantaged by being a minority in the single class. Since the Scheme distributions are based on the value of the existing policies, no disadvantaged minorities are created in the distribution process. Rather, Eligible Policyholders, where necessary, are given a value uplift or a 105% Uplift Premium to make sure they are advantaged by the Scheme.

Endowment Eligible Policyholders are a minority. They are being offered the same choices in the Scheme as Whole of Life Eligible Policyholders. They have different defaults. The remedy for a Policyholder who does not like their default is to make a different choice rather than to vote against the Scheme.

Accordingly, I support the use of a single class for voting on the Scheme.

9.5 Security after Effective Date

On the basis of the Scheme becoming effective on 30 September 2023, Foundation Life's only business remaining would have been to pay cash to those Eligible Policyholders who would receive the Cash Payment from the Scheme. In the unlikely event of the transfer of the non-participating business failing, Foundation Life would also have its 22 non-participating policies to administer. Section 6.3 showed that Foundation Life would then have had capital in excess of its solvency requirements of $30.1m and a solvency ratio of 703%, assuming a Take-up Rate for insurance of 65%. This is a substantial level of capital support, and the non-participating business would have been well-protected.

9.6 Security for participating policies transferring their cover to Chubb Life

For those Eligible Policyholders transferring their cover to Chubb Life, their insurer will move from having an AM Best rating of A minus to an AM Best rating of A.

9.7 Conclusion

The Scheme adds value to Eligible Policyholders as a whole and so is in the best interests of Eligible Policyholders as a whole. The next sections look at the value added for individual Eligible Policyholders.

10 Assessment of Replacement Cover

10.1 Introduction

This section contains my assessment of the Replacement Cover against the principles in section 8. The rest of the assessment of the Scheme against the principles is in section 11.

10.2 Comparison with existing life cover

10.2.1 Guaranteed cover

The whole of the Replacement Cover will be guaranteed. By contrast, only the sum insured and declared bonuses are guaranteed under Foundation Life's existing policies. This is because Additional Bonuses are not guaranteed and, until declared by Foundation Life, neither are future Annual Bonuses.

Additional Bonuses for endowment policies have been nil since 2021, and for whole of life policies are projected to fall to nil by 2036 but, in the event of Foundation Life making sustained losses on its investments, they could fall more quickly than this. The purpose of Additional Bonuses is to pay a share of undistributed profits to Eligible Policyholders who die or whose policies mature. Undistributed profits eventually go to Eligible Policyholders whose policies remain in force through their Annual Bonuses.

The Annual Bonuses for the financial year ended September 2023 were declared at the rates of 1.4% of sum insured plus 1.7% of existing bonus for Foundation Life's main class of whole of life policy. (Other policies' rates were set with established relativities to these rates.) Though these rates are not guaranteed into the future, they were intended to be sustainable in a stable investment environment, which did not occur during 2022/23 as interest rates rose substantially over that period. Lower interest rates will lead to lower bonuses, while higher interest rates lead to higher bonuses.

The maximum Replacement Cover is not less than 105% of the Existing Death Benefit. Thus the maximum Replacement Cover provides an immediate increase in cover. Whether the maximum Replacement Cover will continue to be higher than the cover that would have been provided by Foundation Life's existing policies cannot be known as the level of future bonuses on Foundation Life's existing policies is not certain. The Existing Death Benefits at 30 September 2023 for all policies in total was made up as:

Table 10.1 – Existing Death Benefits at 30 September 2023

	$m
Sum Insured	363
Annual Bonuses Awarded	384
Potential Additional Bonus	143
Total	890

The Additional Bonuses comprise 16% of the Existing Death Benefits in total and are projected to reduce to zero. This means that, for some Foundation Life policies, the projected future death benefits at some points in the future are lower than their Existing Death Benefit. This is analysed and explained further below.

In summary, there is a trade-off. The Replacement Cover will not reduce and will initially be higher than the existing cover. On the other hand, some Eligible Policyholders might at some durations have received higher amounts of cover under their existing policies through future bonuses. However, these Eligible Policyholders at no time will have a shortfall of more than 2% of the projected sum insured from their existing policies because of the Benefit Minimum described in section 5.4.

10.2.2 No future premiums

Eligible Policyholders paying premiums will have the advantage of paying no more premiums after the Effective Date of the Scheme, even if they continue with life cover.

10.3 Basis for assessing Replacement Cover offered

I compared the projected average Death Benefit from the existing policy with the Replacement Cover for every policy from the Effective Date up to age 100. The actual death benefit will vary with bonuses and

could be above or below the average, depending particularly on investment conditions. The results for a range of policies are shown in Section 7.

In summary, allowing for premiums saved and Residual Cash paid (if any), the Replacement Cover that would have been offered at 30 September 2023 was higher than the existing policy's projected death benefit for:

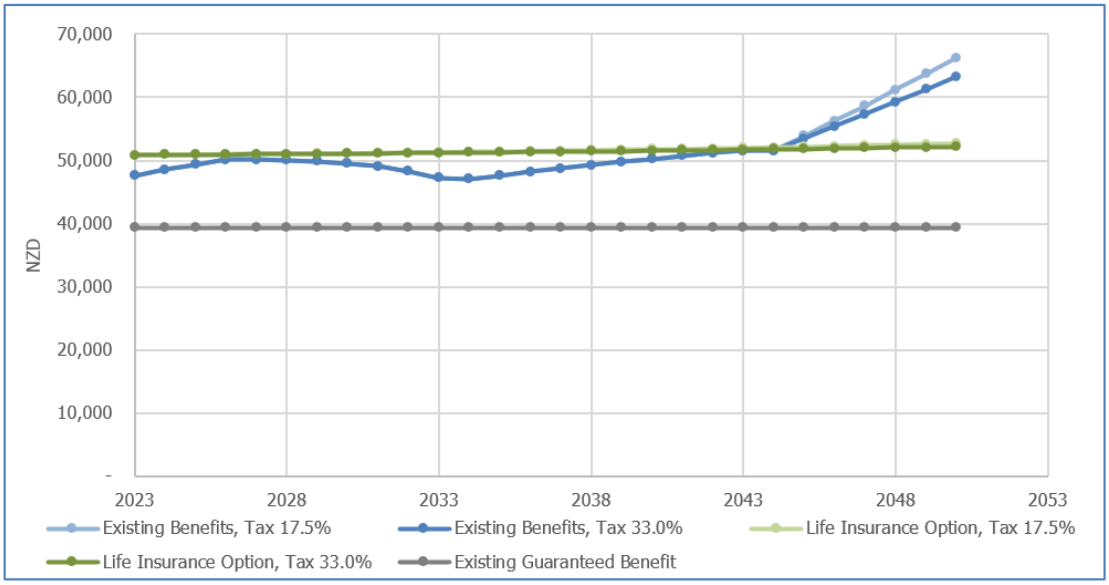
- All 845 Eligible Policyholders of an endowment policy up to their maturity age
- 14,039 (51.27%) out of the 27,381 Eligible Policyholders of a whole of life policy at any age.

Three Eligible Policyholders would have had their loans and premium debt repaid in full but no other benefit from the Scheme. I have examined the Scheme benefits of the remaining 13,339 Eligible Policyholders of a whole of life policy whose Scheme benefit was at some stage below the existing policy's projected death benefit. Further examination of this group highlighted three categories:

- *Category* 1 - 6,652 whole of life Eligible Policyholders had a Scheme benefit that fell below the existing projected benefit only after the maturity of their existing policy. These situations occurred because the maturity proceeds of the existing policy are assumed to be reinvested at age 95 whereas Replacement Cover lasts for life. The largest shortfall was 17.6% which occurred at age 100 for a life insured aged 73. This is illustrated below.

  I consider that the expected improvement in the death benefit up to around 2044 outweighs the disbenefit over age 95, applying Principle 8 that puts more emphasis on shorter term benefits. I note that most lives insured will likely die under age 95 and so will receive higher benefits on death from the Scheme on average.

  Chart 10.1 - Projections of a representative policy (Male, age 73) with a maximum insurance shortfall at age 100



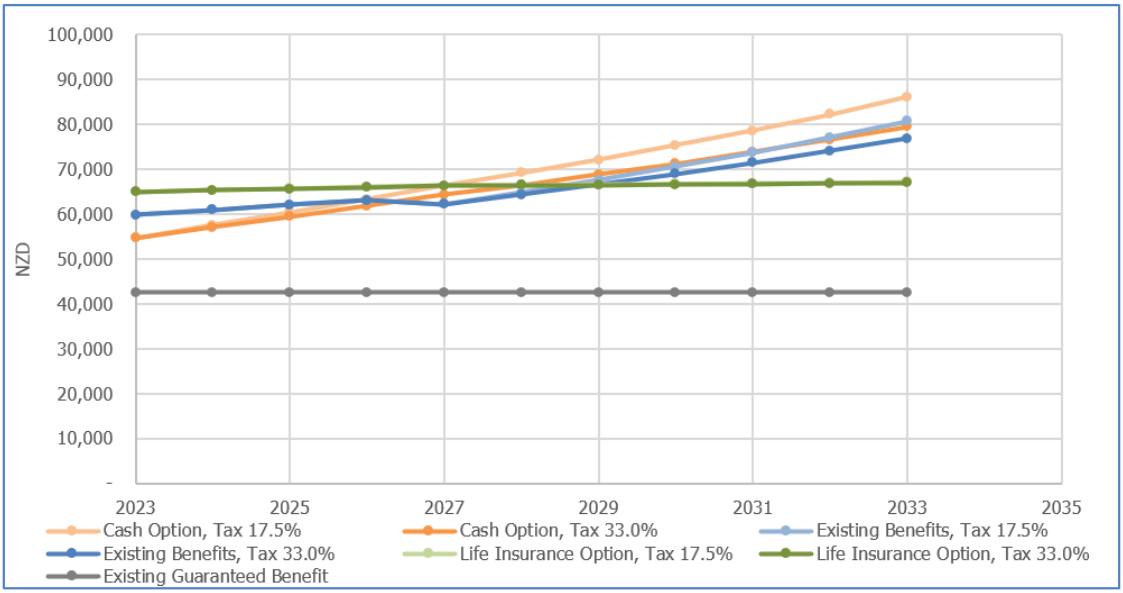
  On my mortality assumptions, 85% of 73 year-old males are expected to die before reaching age 95.

  Note that the above policyholder did not receive Residual Cash and was not paying premiums. That meant that there was no interest earned in the projections until age 95. So, the Scheme benefits were the same for tax at 17.5% and at 33% to age 95 and the two blue lines up until age 95 in the above graph sit on top of one another.

Principle 8 is less relevant to older lives insured for obvious reasons. The policy with a life insured aged 90 or over with the largest shortfall had a shortfall of 13.0%. This was at age 100. This policy is illustrated below. Also shown is the Scheme benefit if the Policyholder received the Cash Payment.

The graph shows the Insurance Option provides a death benefit that is initially higher than the existing projected death benefit for 6 years and ultimately is lower. Alternatively, the Cash Payment starts below the existing projected death benefit and is higher than it after 3 to 4 years. For a 90-year-old male in average health, the probability of living for another four years is 39%, and for another six years (i.e., to age 96) it is 24%. Since the Policyholder has the choice between the Insurance Option and the Cash Payment, and considering the number of years for which each option is of greater benefit, I believe the Scheme is in the interests of Eligible Policyholders like this one.

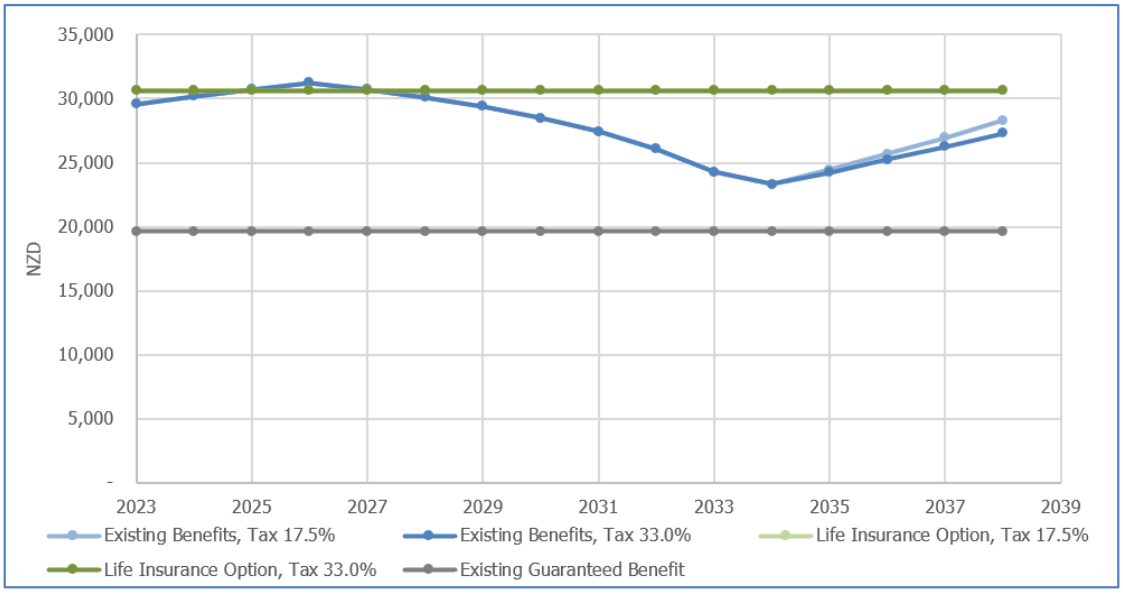
Chart 10.2 - Projections of a representative policy (Male, age 90) with a maximum insurance shortfall at age 100



- *Category 2* - On 30 September 2023, 6,319 whole of life Eligible Policyholders had a Scheme benefit that fell below the existing projected benefit in the period 2025 to 2027, and then by not more than 2%, in the period up to the maturity of their existing policy at age 95. An example is below (Life insured aged 85).

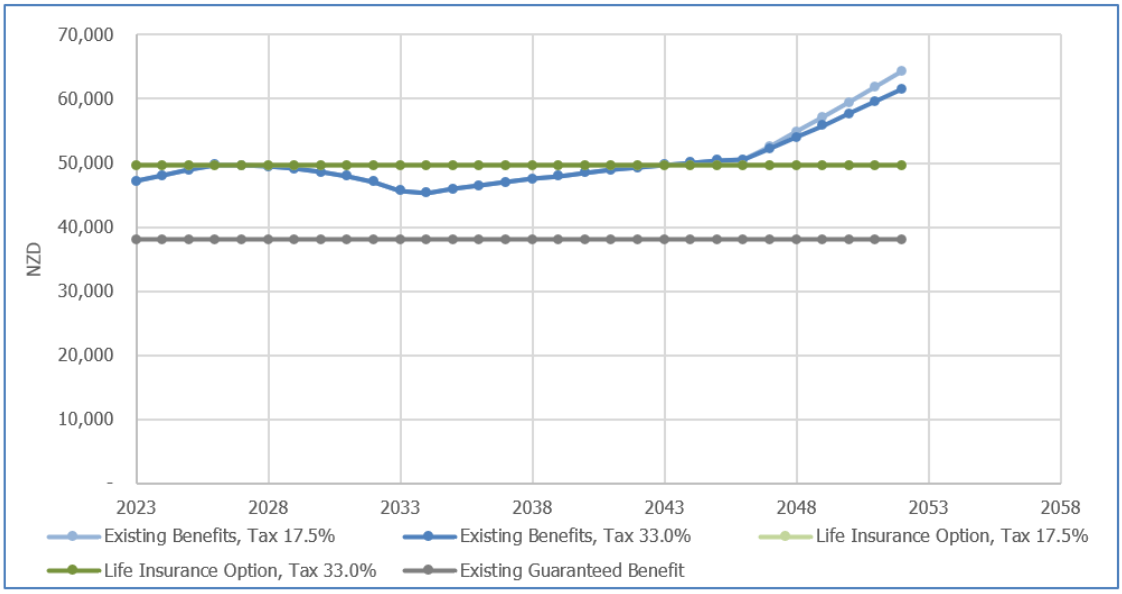
I consider that the benefit shortfall is immaterial, albeit at short durations. The benefit gain at later durations can be seen in the graph to be much greater and so Principle 3, that no Policyholder overall should be worse off, is met.

Chart 10.3 - Projections of a representative policy (Male age 85) with an insurance shortfall in 2025 to 2027



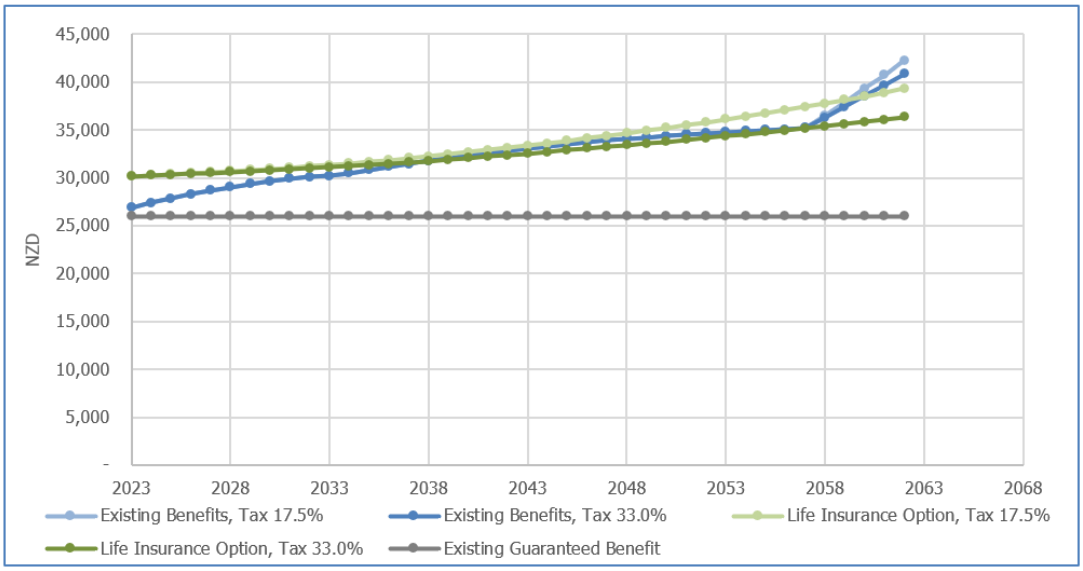
Some Eligible Policyholders in this category also had a shortfall after the maturity of their existing policy. These were similar to category 1 above and the same reasons for acceptability apply. An example is below.

Chart 10.4 - Projections of a representative policy (Male age 71) with an insurance shortfall in 2026 to 2027 and a maximum shortfall of 19.4% at age 100 after maturity



- *Category 3* – On 30 September 2023, 368 whole of life Eligible Policyholders had a Scheme benefit that fell below the existing projected benefit after 2027, but by no more than 2% up to the date of the maturity of the existing policy. Of these Eligible Policyholders, 262 had a shortfall for 10 years or longer. The most years with a shortfall was 25. An example of this is below, where there is a shortfall in years 15-39. The life insured is age 61.

Chart 10.5 - Projections of a representative policy (age 61) with an insurance shortfall later than 2027

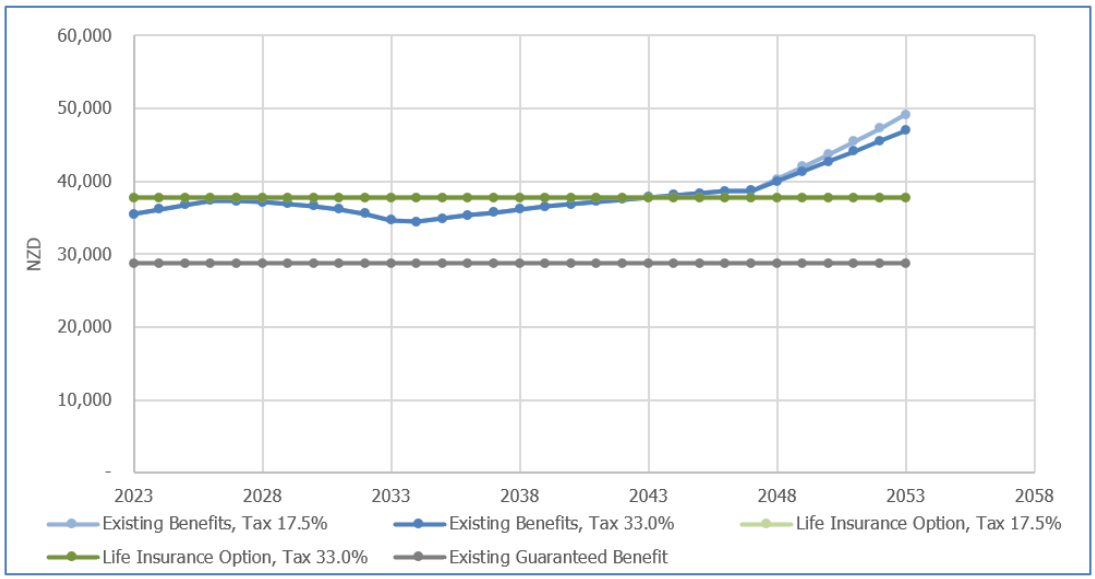


The shortfalls of up to 2% are at the 33% tax rate. The comparison between Full Cover and Pre-Scheme benefits at 33% tax are shown by the dark green and dark blue lines. It is apparent from the chart that the greater Scheme benefits in the first 15 years, when the dark green line is above the dark blue line, are more significant that the subsequent shortfall.

The pale green line shows Full Cover at 17.5% tax. There is no shortfall in years 15-39 at that tax rate.

Some Eligible Policyholders in this category, including the above example, also had a shortfall greater than 2% after the maturity of their existing policy. These were similar to category 1 above and the same reasons for acceptability apply. Another example is below.

Chart 10.6 - Projections of a representative policy (Male age 70) with an insurance shortfall later than 2027 and a maximum shortfall of 19.7% at age 100 after maturity



10.4 Eligible Policyholders with a short life expectancy

Replacement Cover starts at a higher level than the Existing Death Benefit. This is to the advantage of those who have a short life expectancy, meaning under five years. Replacement Cover provides greater benefits than those expected under the existing policies for all who die or become terminally ill within two years after the Effective Date. After two years, Replacement Cover in all cases will be no worse than 2% lower than the expected benefit under the existing policy, a shortfall I regard as immaterial.

10.5 Chubb Life contract terms for benefit payment

I have compared the conditions for benefit payment on death or terminal illness in the Chubb Life policy with those on Foundation Life's policies. The Chubb Life policy is the same or better for Eligible Policyholders than the Foundation Life policy.

The Chubb Life policy also offers an advanced funeral benefit (an advancement of part of the sum insured) which is an additional benefit for Eligible Policyholders.

The new policy has a surrender value, but the basis and level of the values will be different from those of the existing Foundation Life policy. Surrender values are discussed in section 11.4.4.

10.6 Rider benefits

I have compared the terms for the new rider benefits with those on Foundation Life's policies. The Chubb Life rider policy terms are the same or better for Eligible Policyholders than those of the Foundation Life policy.

The payment terms upon death, diagnosis of a terminal illness or total and permanent disablement are at least as favourable as the existing policies' terms. The reducing sum insured schedule on the reducing term insurance is also at least as favourable.

The terms for exercising the convertibility and guaranteed future insurability options are equivalent to the existing policy in that Eligible Policyholders can buy new life insurance. The type of product will be different, however.

When Eligible Policyholders exercise their convertibility and guaranteed future insurability options they will be offered a Chubb Life Assurance Extra Life Cover policy, or any other standard life insurance policy available at the time of exercising the option. Chubb Life Assurance Extra Life Cover is a term insurance policy that can last for the life insured's whole life. Its terms are market standard for a modern insurance policy. Premiums will be payable. They may either be fixed up to a chosen age (65, 70, 80 or 100) or they may increase every year with age. This product does not have an investment component and therefore does not have a surrender value.

10.7 Alternatives considered

While there are many life insurance designs which could potentially be used, as part of my final assessment I looked at five alternatives. I limited it to five as the tenders received in relation to the Replacement Cover had no future premiums payable and were for a flat cover for the lifetimes of the lives insured. This meant that the only life insurance designs available required a flat level of cover, so there were only two logical design approaches:

- Tailored level of flat cover for each Policyholder with the same present value of future benefits as the cover provided by their existing policy using standard mortality and interest rate assumptions
- Flat cover that was the same percentage of their Existing Death Benefit for all Eligible Policyholders with any excess value in their policies returned as cash to the Policyholder.

In assessing which approach was appropriate I looked at the following designs:

- Flat 100% of Current Death Benefit for all Eligible Policyholders ("100% Alternative")
- Flat 103% of Existing Death Benefit for all Eligible Policyholders ("103% Alternative")
- Flat 105% of Existing Death Benefit for all (Full Cover)
- Flat 110% of Existing Death Benefit for all ("110% Alternative")
- Tailored life cover, which provided an equivalent level of life cover to the existing life insurance benefits with a minimum of 105% of Existing Death Benefit ("Tailored Alternative").

The 100% Alternative was not suitable as it did not give an immediate benefit to Eligible Policyholders.

After extensive analysis I discarded the Tailored Alternative because it achieved a similar result to the Replacement Cover at a higher cost and was much more complicated to explain and implement.

The 103% and 110% Alternatives are simply variations of the Full Cover which use a higher (10%) and lower (3%) adjustment factor against the Existing Death Benefit. These options were rejected for different reasons. The 103% Alternative was rejected as some Eligible Policyholders failed the various tests and principles adopted to assess suitability. The 110% Alternative was rejected as the equivalent of the 105% Uplift Premiums under this option over-penalized those Eligible Policyholders taking cash.

I decided that 105% of Existing Death Benefit was the appropriate level of life cover for Full Cover as it satisfied the various principles which I used to assess appropriateness at the lowest possible cost. I believe this ensures that the best interests of Eligible Policyholders are being satisfied from a variety of perspectives without placing the cost of unreasonably high 105% Uplift Premiums on those Eligible Policyholders with no 105% Uplift Premium.

10.8 About Chubb Life

10.8.1 Background

Chubb Life is a specialist insurance provider. It has been operating in New Zealand for over 100 years and protects around 300,000 New Zealanders with its insurance policies. Chubb Life's products and services include life, funeral, income protection, trauma and accidental death insurance.

Chubb Life is part of Chubb Limited, a global insurance and reinsurance company. Chubb Limited operates in 54 countries and had assets of approximately US$229 billion on 31 December 2023. Chubb Limited's financial strength rating by A.M. Best is A++ (Superior).

Chubb Life is considerably larger than Foundation Life and, unlike Foundation Life, is actively selling policies and growing. In 2023, Chubb Life had a premium income of $341m, which is over sixty times that of Foundation Life.

Chubb Life has an A (Excellent) financial strength rating from A.M. Best. Chubb Life advised that it had no reason to believe that this rating would go down if the Scheme was successful. Chubb Life's rating from A.M. Best at A is higher than Foundation Life's rating of A minus.

A.M. Best's scale of ratings is shown in table 10.2.

Table 10.2 A.M. Best's Financial Strength Rating Scale

Rating Category	
Superior	A++, A+
Excellent	A, A-
Good	B++, B+
Fair	B, B-
Marginal	C++, C+
Weak	C, C-
Poor	D

10.8.2 Solvency

All life insurers in New Zealand are under the prudential regulation of RBNZ, which is responsible for overseeing the security and solvency of these life insurers. RBNZ introduced new solvency requirements in 2023. The figures for both Chubb Life and Foundation Life are shown below on the new requirements.

As at 30 September 2023, the minimum solvency capital required to be held by Chubb Life, referred to as its Prudential Capital Requirement, was $1,220m. The actual solvency capital was $1,349m, giving Chubb Life a solvency margin of $129m, as shown in table 10.3.

Chubb Life has a single statutory fund for all of its life insurance business. The assets of the statutory fund are specifically for paying life insurance claims and expenses. Most of Chubb Life's assets are in its statutory fund. Policies for Replacement Cover will be a part of Chubb Life's statutory fund.

Table 10.3 Chubb Life solvency at 30 September 2023

	Statutory Fund $m	Shareholder's Fund $m	Aggregate $m
Solvency capital	**1,336**	**13**	**1,349**
Prescribed Capital Requirement	**1,211**	**9**	**1,220**
Solvency margin	**125**	**4**	**129**
Solvency ratio	**110%**	**149%**	**111%**

Source: Chubb Life

Foundation Life too has a single statutory fund. The solvency figures for Foundation Life at 30 September 2023 (Scheme not effected) are shown in table 10.4.

Table 10.4 Foundation Life solvency at 30 September 2023

	Statutory Fund $m	Shareholder's Fund $m	Aggregate $m
Solvency capital	**66**	**0.055**	**66**
Prescribed Capital Requirement	**14**	**-**	**14**
Solvency margin	**52**	**0.055**	**52**
Solvency ratio	**483%**	**20,000%**	**483%**

The Prescribed Solvency Requirement comprises the capital requirement set out in RNBZ's solvency standard. In addition, Foundation Life must maintain a solvency margin of a minimum of $3m.

RBNZ has foreshadowed changes to its solvency requirements. Those changes would have reduced the Solvency Margin by $1.3m at 30 September 2023 to $51m, with the Solvency ratio reducing to 444%.

Chubb Life showed a higher solvency margin and a much lower solvency ratio than Foundation Life. Chubb Life's solvency ratio appears low. Further examination showed that it is heavily influenced by policies that are treated as assets when determining the Actual Solvency Capital and given no value for solvency purposes. These policies contribute $1,018m to both the Actual Solvency Capital and to the Prescribed Capital Requirement. I consider it more helpful to remove the $1,018m from both numbers to show a more realistic solvency ratio. This would not change the Solvency Margin; it would remain at $129m. The solvency ratio would go up to 164%.

What matters more than the comparison, however, is whether Chubb Life is strongly capitalised. I regard a solvency ratio, as modified above, of 164% as indicative of Chubb Life being in a suitably strong position for its capital.

Chubb Life has advised that issuing the Replacement Cover policies will increase its solvency margin. Chubb Life expects its participation in the Scheme will increase Chubb Life's ability to generate retained earnings that could provide capital support.

In view of the above, I am satisfied that Eligible Policyholders who take the Replacement Cover with Chubb Life will enjoy suitably high security for their insurance benefits.

10.9 Conclusion

Having performed this analysis and for the reasons outlined above I have found that:

- Replacement Cover provides a suitable level of cover for replacing the existing policies
- Chubb Life's policy conditions are equivalent to or better than Foundation Life's
- Chubb Life provides security for Eligible Policyholders' life insurance benefits that is suitably high.

11 Assessment against principles

11.1 Comparison of Outcomes against Principles

Section 9 showed that the Scheme was value-adding for Eligible Policyholders in aggregate. This section considers the needs of Eligible Policyholders on an individual basis by comparing the Scheme against the ten principles in section 8.3.

11.2 Principle 1 - The tests are on Eligible Policyholders with New Zealand residential addresses

All my assessments have been performed on the basis that the Policyholder has a New Zealand residential address and is resident in New Zealand for tax purposes. This was particularly relevant to the assessment of the level of Replacement Cover in sections 7.2 to 7.8 and section 10.3, which used New Zealand tax rates.

11.3 Principle 2 - Life cover in place must be honoured

The Life Cover offered is greater than the Existing Death Benefit at the Effective Date.

Notwithstanding principle 1, I was concerned that any Policyholder with an overseas residential address should be able to obtain Replacement Cover if they wanted it. Because of regulatory restrictions, Chubb Life is not able to issue a life insurance policy to someone with an overseas residential address. Foundation Life has endeavoured to tell all affected Eligible Policyholders how to assign their Foundation Life policy to a person or entity with a New Zealand residential address so that Replacement Cover can be issued. It is not a straight-forward process and Foundation Life is offering support by telephone and on its website. Foundation Life is making reasonable efforts, in my view, to inform Eligible Policyholders with overseas residential addresses about what they need to do if they want to continue to have life insurance.

11.4 Principle 3 - No Eligible Policyholder overall should be worse off when compared with the Eligible Policyholder's reasonable expectations for their existing benefits

11.4.1 Overall

It is important to note that some Eligible Policyholders in some circumstances may not be better off under the Scheme. For example, at some durations they may have slightly less life cover than otherwise they might have had (see sections 7.2 to 7.8 and section 10.3) and at longer durations their new policies are likely to have lower surrender values than they might otherwise have had (see section 11.4.4). In making my assessment of the Scheme it has been necessary for me to balance the positives and negatives of the Scheme for these Eligible Policyholders.

Each Policyholder under the Scheme will receive benefits in one or more of:

- Replacement Cover
- Cash Payment
- Premiums saved.

In section 9, I showed that the Scheme was value enhancing for Eligible Policyholders as a whole. I have carried out the same analysis for each Policyholder. I found that every Policyholder had both a life insurance option and a cash option that were worth more than the benefits, less premiums, under their existing policy. This was on the basis of average claims rates for each Policyholder and before deducting Additional Take-up Premiums from cash recipients. See section 11.8.4 for the treatment of Additional Take-up Premiums.

Furthermore, the Scheme must satisfy the sufficient assets condition (section 2.6). The Scheme would not be in Eligible Policyholders' interests if it did not satisfy the sufficient assets condition, which is why the Scheme would then be prevented from proceeding.

11.4.2 Replacement Cover

Replacement Cover was assessed in section 10.

11.4.3 Minimum Policy Value

The Policy Value is set so that it is at least 105% of the policy's surrender value, capped at the Existing Death Benefit. This ensures that no Eligible Policyholder at the Effective Date would be better off by surrendering their existing policy than by participating in the Scheme.

11.4.4 Surrender value of Chubb Life's replacement insurance policy

Foundation Life has historically paid a surrender value if a Policyholder wanted to terminate their Whole of Life or Endowment policy. Surrender values are not guaranteed. Generally, they increase as time passes (they can fall in adverse circumstances) as premiums are paid and interest is earned.

Chubb Life's policy also has a surrender value. It too is not guaranteed. It will never exceed the single premium paid by Foundation Life for that policy.

This is different from Foundation Life's policies. The surrender values of Foundation Life's policies normally increase with time with changes up or down to reflect changes in the market value of Foundation Life's investments in the Participating Fund and further premium payments. However, the surrender value of a Chubb Life policy could increase only up to the premium for that policy. Eligible Policyholders who receive insurance and a few years later decide they want to surrender their Chubb Life policy are likely to receive a lower surrender value than their existing policy would have delivered. This disadvantage is offset by the advantage of lower Chubb Life single premium rates. Chubb Life is able to charge lower premium rates than it would charge for the same policy with surrender values in the future greater than the premium. This in part is because Chubb Life would pay higher taxes on such a policy. I have taken the following points into account:

- The low rate of surrender of existing policies of around 3% pa
- Some Foundation Life surrenders occur on policies with loans when the loan plus accumulated interest exceeds the surrender value. Chubb Life will have no policy loans so there will be no more surrenders from this cause
- Eligible Policyholders could choose to cash in or partly cash in their policy now, meaning that those who receive insurance will be less likely to surrender
- Having no future premiums will also tend to reduce surrender rates
- Eligible Policyholders may still have the option to sell their new policy on the secondary market for more than its surrender value or to secure a bank loan using their new policy as collateral.

As a result, I consider many more Eligible Policyholders will benefit from the lower premium rates than will be disadvantaged by the lower surrender values. Therefore, I consider this aspect of the Scheme to be acceptable.

Nevertheless, it is important that Eligible Policyholders have this feature fully explained to them so that they can make their choices for insurance and cash in an informed way. Eligible Policyholders who think they may want to surrender their Chubb Life policy in years to come may seek advice on whether choosing the Cash Payment or a partial cash option and making alternative arrangements for insurance would suit them better.

11.4.5 Endowments

Endowment Eligible Policyholders will receive the Cash Payment by default. If they choose the Replacement Cover, then the Replacement Cover will last for longer than their insurance under their existing endowment; it will last for life and not just to their existing policy's maturity date. However, Replacement Cover will not provide a maturity benefit.

- Endowments receiving cash

  The amount of cash under the Cash Payment is at least as great as the value of expected benefits under the existing policy. The value increase ranges from very little for policies close to maturity up to 20% or more for policies with a longer time to maturity.

- Endowments receiving insurance

  I have compared average death benefits from existing endowment policies with the sums insured under Replacement Cover together will the accumulation of the cash payments and the premium savings. The existing policy's death benefit ceases at maturity. I found that all endowment Eligible Policyholders who chose the Replacement Cover were projected to receive more on death under the Scheme than from their existing policies up to maturity.

  It is on surrenders a few or more years in the future that endowment Eligible Policyholders who choose insurance will be affected by the limit of the Chubb Life surrender value to be no more than the premium paid by Foundation Life for that policy. Because of this limit they may not be able to match their expected maturity value from their existing policy by choosing insurance and surrendering it at the maturity date of their existing policy. This means that endowment Eligible

Policyholders are being offered insurance and cash that does not replicate both their existing insurance and maturity benefits.

I consider this is acceptable because:

- The Scheme is providing benefits worth more than the benefits from the existing policy at the Effective Date.
- Eligible Policyholders of an endowment policy taking insurance will have done so in the knowledge that they could have accepted the Cash Payment or a partial cash option
- Eligible Policyholders may still have the option to sell their new policy on the secondary market for more than its surrender value or to secure a bank loan using their new policy as collateral
- Replacement Cover lasts for life, providing insurance for longer than the existing policy
- Those receiving cash can make alternative arrangements for their insurance needs. If they are in poor health and unable to obtain alternative insurance, then they can choose the Replacement Cover.

11.4.6 Deaths between Record Date and Effective Date

If the life insured dies between the Record Date and Effective Date, the Eligible Policyholder will be entitled to the benefits they would have received under the Scheme. That would be Replacement Cover for NZ residents. The benefit will be payable by Foundation Life and if not paid by the Effective Date, it will be transferred to Chubb Life for payment. That benefit would be more than they would have received with no Scheme because the benefit will be 105% of the Existing Death Benefit. It may be more.

Non-NZ resident Eligible Policyholders will be entitled to request the benefit be changed to the death benefit under their existing policy at the date of death. I understand that both Foundation Life and Chubb Life will deem that request to have been made when it would result in a higher payment than the Cash Payout.

Therefore, the Scheme does not disadvantage those Eligible Policyholders whose life insured dies between the Record Date and the Effective Date.

11.5 Principle 4 - The design in the opinion of the shareholder must not be disadvantageous to the shareholder

The Scheme could not proceed without shareholder approval. The shareholder supports the Scheme proceeding.

11.6 Principle 5 - Allocation of Scheme costs between Eligible Policyholders and shareholder to be fair and seen to be fair

There are various costs of developing and finalising the Scheme. Up to 30 September 2023 the expenses of developing the Scheme had been $12.1m. Another $4.0m had been spent investigating alternative potential schemes before settling on the Scheme being put to Eligible Policyholders. These costs covered legal, actuarial and other professional advice and project costs incurred in assessing the alternatives.

There are costs after 30 September 2023. They were set out in section 4.4. The benefit enhancements described in section 4.5 are also costs to be met.

Thus, the costs of the Scheme comprise the expenses incurred to date, expenses to be incurred in the future and the cost of benefit enhancements. Since all of these costs are incurred to advantage the stakeholders in the Participating Fund, being Eligible Policyholders and the shareholder, they are charged to the Participating Fund. It is then a question of how those costs are shared between Eligible Policyholders and the shareholder.

IPSA and Foundation Life's constitution provide for Participating Fund profits to be shared between Eligible Policyholders and the shareholder in the ratio of 80% or more to Eligible Policyholders and 20% or less to the shareholder. When it comes to expenses, that would mean Eligible Policyholders pay no more than 80% of them, with the shareholder paying 20% or more.

The sharing of profits in the 80/20 ratio is Foundation Life's well-established practice. It gives an appropriate basis for sharing the costs of the Scheme.

I have assessed below the outcome of the Scheme, combining the past and future Scheme costs allocated in the 80/20 ratio and the amount of the $16.05m to be allocated to shareholder, as described in section 2.5.

When it comes to dividing the assets of the Participating Fund, I have regarded assets up to the value of the guaranteed policy liabilities as wholly for Eligible Policyholders with the remaining assets to be split in the 80/20 ratio. Table 11.1 shows how those remaining assets would be allocated.

Table 11.1 Analysis of the shareholder's share of the Participating Fund at 30 September 2023

	35% Take-up	50% Take-up	65% Take-up	80% Take-up
	$m	$m	$m	$m
Assets in excess of guaranteed policy liabilities	114.0	114.0	114.0	114.0
Scheme expenses and benefit enhancements	(20.2)	(28.2)	(41.9)	(66.2)
Sub-total	93.8	85.8	72.1	47.8
Amount for the shareholder at 20%	18.8	17.2	14.4	9.6
Cost of guarantee	(0.7)	(0.7)	(0.7)	(0.7)
Share of FY23 bonuses	2.3	2.3	2.3	2.3
Amount for the shareholder on 80/20 split	20.4	18.8	16.0	11.2
Actual shareholder's share	16.05	16.05	16.05	12.6

Notes: Totals may not exactly add due to rounding
See explanation below for the 80% take-up actual shareholder's share exceeding the amount on the 80/20 split

The assets are after the costs of the Scheme up to 30 September 2023 had been paid.

The Shareholder covers the guarantee that the Eligible Policyholders' benefits will be paid even if the assets of the Participating Fund are insufficient. The value of that guarantee was $0.7m and so is deducted above from the amount for the shareholder.

The Shareholder is entitled to 25% of the cost of bonuses allocated to Eligible Policyholders for FY23. That amount had not been credited to the shareholder at 30 September 2023.. It was excluded from the assets of $114.0m so it is included explicitly above.

The row 'Amount for the shareholder on 80/20 split' shows the potential result for the shareholder after providing the benefit enhancements to make the Scheme in the interests of Eligible Policyholders.

The amount that the shareholder could receive varies with the Take-up Rate. However, the shareholder offered to receive a fixed amount of $16.05m instead of an amount that would depend on the Take-up Rate. This would mean that the shareholder would also not be affected by changes in interest rates or the Scheme costs. Interest rates affect the premium payable to Chubb Life, the value of the assets, the value of the guaranteed liabilities of the Participating Fund, and the cost of the shareholder's guarantee. As assets and liabilities are closely matched, the impact of changing interest rates is expected to be small and could be positive or negative for Eligible Policyholders. At Take-up Rates of 35% and 50%, the fixing of the shareholder share benefited Eligible Policyholders by $4.3m and $2.7m respectively. There was no loss or benefit at a 65% Take-up Rate. At an 80% Take-up Rate, the benefit to the shareholder was $1.4m, noting that the sufficient assets condition brought down the shareholder's share from $16.05m to $12.6m. Considering a reasonable proportion of Eligible Policyholders are likely to receive cash, I assessed that accepting the fixed amount of $16.05m was more likely to benefit Eligible Policyholders than to disadvantage them. I also noted at the time that the budget for the Scheme expenses included a contingency margin that would have benefited Eligible Policyholders if it were not spent.

The above shows that the shareholder is likely paying more than 20% of the scheme expenses and benefit enhancements. Therefore, I am satisfied that the Scheme costs have been appropriately allocated between Eligible Policyholders and the shareholder.

The shareholder may not receive more than is permitted under Insurance (Prudential Supervision) Regulations 2010. This limitation is unlikely to reduce the amount that the shareholder receives. The

limitation is in the agreement with the shareholder to make sure that the legal requirements are met in all eventualities.

11.7 Principle 6 - The design must ensure the whole of the 'distributable fund' is distributed to Eligible Policyholders

It will be done this way, with the amounts for Eligible Policyholders being crystallised on the Effective Date. Eligible Policyholders' benefits will not be affected by any events after that date. As already noted, the shareholder will cover any unbudgeted Scheme and pay-out phase costs after the Effective Date. On the other hand, the shareholder will benefit if the expenses after the Effective Date turn out to be lower than the budgeted expenses. Accurately budgeting the expenses after the Effective Date will be important. Also, Chubb Life will take on responsibility for settling claims incurred but not paid, whether reported or not, as at the Effective Date. This means that claims experience emerging after the Effective Date will not impact the distributable fund.

11.8 Principle 7 - The allocation of the 'distributable fund' between Eligible Policyholders to be fair and seen to be fair

11.8.1 Introduction

There is a number of aspects to the fairness of the distribution between Eligible Policyholders. These are discussed below.

11.8.2 Modelling approach

There is a strong argument that the stochastic modelling being used is as fair as it is possible to be. The modelling picks up the way Eligible Policyholders and the shareholder will be paid out of the Participating Fund in a wide range of scenarios (10,000 of them) for the existing business. Those scenarios were chosen so that the average result would be a fair value for all Eligible Policyholders, meaning that the valuation was consistent with market interest rates and other conditions.

The model distributes all the assets of the Participating Fund after allowing for Scheme expenses. Adjusting the value of the assets to allow for Scheme expenses has the effect of lowering projected bonuses in the model. This is fair because it is through bonuses that profits of the Participating Fund are distributed to Eligible Policyholders.

11.8.3 105% Uplift Premiums

105% Uplift Premiums are the amounts required to top-up the Policy Value to ensure that each Policyholder has sufficient value to purchase the full amount of Replacement Cover, as described in section 4.7. If this were not done, there would be Eligible Policyholders who would be better off keeping their existing policy. In this case, the Scheme would not be approved as it would not be in the best interests of all Eligible Policyholders. Paying 105% Uplift premiums from the Participating Fund reduces the assets available to others. It is, however, in Eligible Policyholders' interests for the Scheme to be approved, and so it is in their interests where applicable to contribute to the 105% Uplift premiums.

This is an example of the mutuality of the Eligible Policyholders' interests in the Participating Fund. Mutual interests are the basis of a participating fund and of insurance in general. It leads to value transfer between policyholders in a number of ways:

- Insurance works on the basis that the premiums of those who do not claim help to pay for the claims of those who do claim
- As have many participating funds in the past, Foundation Life has a uniform bonus system. This means that all policies of the same type receive the same bonus rates paid from the profits of the Participating Fund. This occurs regardless of how the profitability of policies may vary by the age or gender of the policyholders. Bonuses depend on the performance of the portfolio; they do not reflect the changing profitability of individual policies as investment markets change, varying claim rates by age or gender nor, also, any difference in how expenses may be attributed to policies since they were issued. Profitability may also vary by the length of time the policies have been in force, which will affect the amount of accumulated bonus. However, traditionally policies of the same type have received the same rate of Annual Bonus on that accumulated bonus
- Additional Bonuses are used to pay undistributed profits to policyholders on death and maturity. This is a final adjustment to policyholder benefits to catch up with the distribution of profits attributable to the exiting policies. Foundation Life's Additional Bonuses vary with the year that the policy was issued and whether the policy was a whole of life or an endowment policy.

Eligible Policyholders have pooled their interests in taking out policies in the Participating Fund with its broad-brush bonus system. In effect, simplicity in the bonus system has been chosen over precision in the allocation of profits. It is consistent with this approach that the value attributed to some Eligible Policyholders would be used for the benefit of others so that all Eligible Policyholders could benefit from the Scheme.

105% Uplift premiums are needed whenever the Policy Value is lower than the cost of Replacement Cover and this can occur for a range of reasons. One reason is that Eligible Policyholders will not pay any more premiums for insurance. Some Eligible Policyholders will gain more than others from not paying future premiums, either because they are paying large premiums or because they expect to have many years' premiums to pay. This could be considered unfair. However, the tender for the Replacement Cover received no responses requiring payment of future premiums so this is a design element of the Replacement Cover which cannot be changed. Consequently, my assessment is that this perceived unfairness is acceptable as to remove it by eliminating 105% Uplift Premiums would mean the Scheme was not in the interests of all Eligible Policyholders, in breach of Principle 3. That would mean the Scheme would not proceed, an outcome very much not in the interests of Eligible Policyholders. Hence, it is in the interests of Eligible Policyholders where required to do so to cover the costs of 105% Uplift Premiums so that the Scheme can proceed.

11.8.4 Additional Take-up Premium

The single premiums paid to Chubb Life will have two components. These are the Base Premium and the Additional Take-up Premium, as explained in section 3.2. The Eligible Policyholders receiving Replacement Cover will use their Policy Value to pay the Base Premium. Additional Take-up Premiums will be paid by Eligible Policyholders receiving the Cash Payment, in full or part. These positions are discussed below.

- Replacement Cover

  Eligible Policyholders generally have policies whose premiums were at Foundation Life's standard premium rates at the time they commenced their policy. Regardless of their current state of health, they would continue to pay standard premiums for their existing policy. The Replacement Cover with Chubb Life will have two components to its premium, being the Base Premium and the Additional Take-up Premium. The Base Premium corresponds to the standard Foundation Life premium. The Additional Take-up Premium is for the additional claims expected from those who take Replacement Cover, as explained in section 3.2. Because Eligible Policyholders are paying standard premium rates for their existing policies, I regard it as fair that they should continue to have policies based on standard premium rates and that it would not be reasonable to charge the Additional Take-up Premium to Eligible Policyholders receiving Replacement Cover. This is why only the Base Premium for each Policyholder is to be paid from their Policy Value.

- Cash Payment

  At 100% Take-up for Replacement Cover, there would be no Additional Take-up premium. At lower Take-up Rates, the higher expected claim rates of those receiving insurance are balanced by the lower expected claim rates of those receiving all cash. The higher the expected claim rates are, the higher the value of insurance. Thus, the existing insurance benefit is worth more to those receiving insurance and is worth less to those receiving all cash. In aggregate, the value increases and reductions offset one another. As explained above, it would not be reasonable for those taking the Replacement Cover to pay their own Additional Take-up Premium. With those taking the Cash Payment giving up a less valuable insurance benefit, it is reasonable for the Eligible Policyholders receiving the Cash Payment collectively to pay the Additional Take-up Premiums of those receiving insurance.

11.8.5 Chubb Life costs

As stated in section 4.6.1, the proportion of the Chubb Life set-up costs contribution of $700,000 will be capped for the new Chubb Life policyholders at 1% of the premium paid to Chubb Life. This would have taken effect on 30 September 2023 at (an unlikely) Take-up Rate of 15% or lower, and it would have required the other Eligible Policyholders to have met the balance of this cost. Since this would have reduced their benefits by a maximum of 0.15%, an immaterial amount, I consider the 1% cap to be a reasonable way of ensuring the contribution to the Chubb Life set up cost was not a burden on a minority of Eligible Policyholders.

11.9 Principle 8 - In assessing overall benefit to a Policyholder, a greater weight is given to benefits that might be payable in the short term (less than ten years) than to those that might be payable in the long term (more than ten years).

It would be easy if the Scheme produced insurance benefits that were greater than currently provided in all circumstances and at all points of time, but this is not the case. That is because the existing policies could produce higher benefits, through higher bonuses, in the circumstances, for example, of particularly favourable investment returns or low claims rates. To buy more insurance than the most favourable of all future scenarios for the existing policies, the insurance premiums charged by Chubb Life would have to be much higher. The assets of the Participating Fund would most likely be insufficient to afford those premiums and it would reduce the amounts payable to those Eligible Policyholders who chose the Cash Payment.

Given this, the question arises as to how to judge the balance between the 'overs' and 'unders'. As part of this assessment, it is necessary to acknowledge that the existing policies' total death benefits are not guaranteed while Replacement Cover will be and that it is necessary to allow for the different levels of certainty associated. My assessment is that the 'overs' will outweigh the 'unders' when Replacement Cover, plus accumulated premium savings and any cash pay-out is:

- higher than the existing policy's death benefit for at least the first two years
- never lower than the existing policy's expected death benefit by 5%.

I chose 5% here because it is the bottom of a range of 5% to 10% commonly used for assessing materiality in accounting, actuarial and other financial assessments. The Scheme has been designed so that 2% was the largest shortfall of Replacement Cover below any existing policy's expected death benefit. That was at 33% tax. The shortfall was lower or eliminated at lower tax rates. Section 10.3 provided examples of this.

11.10 Principle 9 - If an Eligible Policyholder can be advantaged without disadvantaging other Eligible Policyholders, then do it

All Eligible Policyholders are advantaged by the Scheme in that they are being offered options at the Effective Date that are currently not available to them. These include a cash value that is higher than their existing policy's surrender value, a chance to have a partial surrender on more favourable terms than otherwise would have applied, and certainty as to the death benefit payable.

The Scheme also addresses two matters that will become issues in the future: the rising per policy expense costs as the number of policies being administered by Foundation Life falls, and the reduced ability of the Fund to invest in growth assets as the relative size of the buffer assets shrinks.

Of note is that Eligible Policyholders who continue with life cover will not be penalised by any underwriting loadings or equivalent because the Chubb Life single premium rates that will apply will be the rates for 100% Take-up.

11.11 Principle 10 - It should be simple in design and the options for Eligible Policyholders easy to explain

It is my assessment that providing all Eligible Policyholders with four choices between cash and insurance for a level amount that lasts for life, with no premiums payable for life, meets this Principle.

11.12 Alternatives considered

The Scheme as proposed is not the only potential scheme that Foundation Life considered. Alternatives considered are discussed in section 4.4 of the Explanatory Statement. I have reviewed those alternatives and concur with the directors' assessment that they were inferior to the Scheme.

11.13 Conclusion

I consider the Scheme meets the principles established.

12 Assessment at Effective Date

12.1 Introduction

This report has shown the results of the Scheme if 30 September 2023 had been the Scheme's Effective Date and has shown that the Scheme would have been in Eligible Policyholders' individual and collective best interests. At the Scheme's actual Effective Date, there will be fewer policies in force, different values of assets and different interest rates, some of the assumptions may also change. This section shows that the Scheme would still be in the individual and collective best interests of Eligible Policyholders at the Effective Date.

12.2 Assessment

The Scheme's benefits for every Eligible Policyholder will be calculated at the Effective Date using policy data, asset data and assumptions that will then be up to date. The result for Eligible Policyholders will be different from the result at 30 September 2023. However, the Scheme has a number of features to prevent an advantage at 30 September 2023 becoming a disadvantage at Effective Date. These are:

- 105% Uplift premiums – These are paid by the Participating Fund so that all Eligible Policyholders may have access to Replacement Cover.
- Replacement Cover is never more than 2% below the expected death benefit from the existing policy over the life of the policy – The expected death benefit from the existing policies will be projected at the Effective Date to reflect future bonuses that the business could pay on the interest rates, asset values and other economic circumstances at the time. This means that, if expected bonuses had increased, the Scheme will deliver Replacement Cover that is an appropriate alternative to the existing policy.
- Benefit minimum – The Scheme provides benefits whose present value is no lower than the present value of the existing benefits. Even if the present value of the existing benefits has risen to the Effective Date, the Scheme will deliver benefits with a present value at least as high.
- Surrender value minimum – This ensures that Eligible Policyholders who receive cash are advantaged relative to surrendering their policy at the Effective Date.
- Statistical test – This makes sure to a high level of confidence that no Eligible Policyholder has been disadvantaged by statistical error in the modelling of their policy.
- IPSA compliance – IPSA says how policyholders are to be protected. It limits the shareholder's share of profits to 20% of the profits with policyholders to receive at least 80% of the profits. The shareholder's share of the Participating Fund will be reduced if necessary to meet this requirement.
- Sufficient assets condition – This condition prevents the Scheme from going ahead to the detriment of Eligible Policyholders.

These aspects of the Scheme mean that it will continue to be in the individual and collective best interests of Eligible Policyholders on the Effective Date and that it will not go ahead if it is not in their individual and collective best interests.

13 Reliances and limitations

I have relied on the accuracy and completeness of all data and other information (qualitative, quantitative, written and verbal) provided to me for the purpose of this report. I have not independently verified or audited the data, but I have reviewed it for general reasonableness and consistency. I am well qualified to do this having written the Financial Condition Reports for Foundation Life since 2016. It should be noted that if any data or other information is materially inaccurate or incomplete, the advice in this report may need to be revised.

This report has been prepared to assist Eligible Policyholders, the directors of Foundation Life, the Independent Actuary, the Reserve Bank of New Zealand, and the High Court to make their determinations about the Scheme. No other use of this report should be made without prior written consent from me and Foundation Life.

The report should be considered as a whole. All questions in the first instance should be addressed to the Chief Executive of Foundation Life. Contact details for Foundation Life are available on www.foundationlife.co.nz.

Appendix A – Assumptions

A.1 Introduction

This appendix outlines the assumptions used in the valuation model described in section 5.2.4, with reasons for having chosen them. These are:

- Mortality and future mortality improvement
- Surrender rates
- Maintenance expenses, commission and investment management expenses
- Bonuses
- Investments and multiple scenarios
- Tax

This appendix also shows the assumptions used for the valuation of rider benefits.

A.2 Mortality and Future Mortality Improvement

A.2.1 Introduction

The purpose of this section is to set out the justification for, and the detail of, the mortality assumptions for use in the Scheme. It includes future mortality improvements as they are material to the value determined for individual policies in the Scheme. The following paragraphs separately discuss the base-line mortality assumptions and the future mortality improvement assumption.

A.2.2 Base-line mortality assumptions

The mortality experience for participating products has been measured over the 7½ years up to March 2020. This was a detailed investigation of the experience over 4 years 10 months up to 31 July 2017, and a high-level investigation after that. The mortality assumptions were set on the results of the detailed investigation as a percentage of the standard NZ97 mortality table. For a good fit to the experience, the percentage varied with age and gender. The mortality experience for the 6 years to September 2022 showed claim payments were within 10% of the amounts expected on the assumptions set. This result confirmed that the assumptions were reasonable.

The following table and charts show the main analysis of the 2013 - 2017 claims experience against claims expected on the assumptions adopted for the Scheme.

Table A.1 Whole of Life mortality by age group and gender on mortality rates adopted

	Male			Female			Combined
Age	**Exposure (Lives)**	**Actual Deaths (A)**	**Expected Deaths (E)**	**Exposure (Lives)**	**Actual Deaths (A)**	**Expected Deaths (E)**	**A / E**
<=30	0	0	0	0	0	0	0%
31-40	8,062	6	3	5,981	0	2	140%
41-45	8,113	1	4	5,565	3	3	54%
46-50	9,369	8	9	5,537	3	5	81%
51-55	13,590	24	23	6,622	11	9	109%
56-60	17,071	49	50	7,060	22	17	106%
61-65	17,765	98	92	6,132	30	24	111%
66-70	19,522	165	174	5,051	29	33	94%
71-75	15,553	263	272	3,584	38	41	96%
76-80	11,409	343	345	2,658	62	63	99%
81-85	8,770	506	501	1,769	65	73	100%
86-90	5,224	621	617	958	75	77	100%
91+	1,730	329	325	293	38	38	101%
Total	**136,180**	**2,413**	**2,415**	**51,212**	**376**	**384**	
A / E			**99.9%**			**98.0%**	**99.7%**

Chart A.1 Whole of Life Male Mortality Rates for ages 31-70

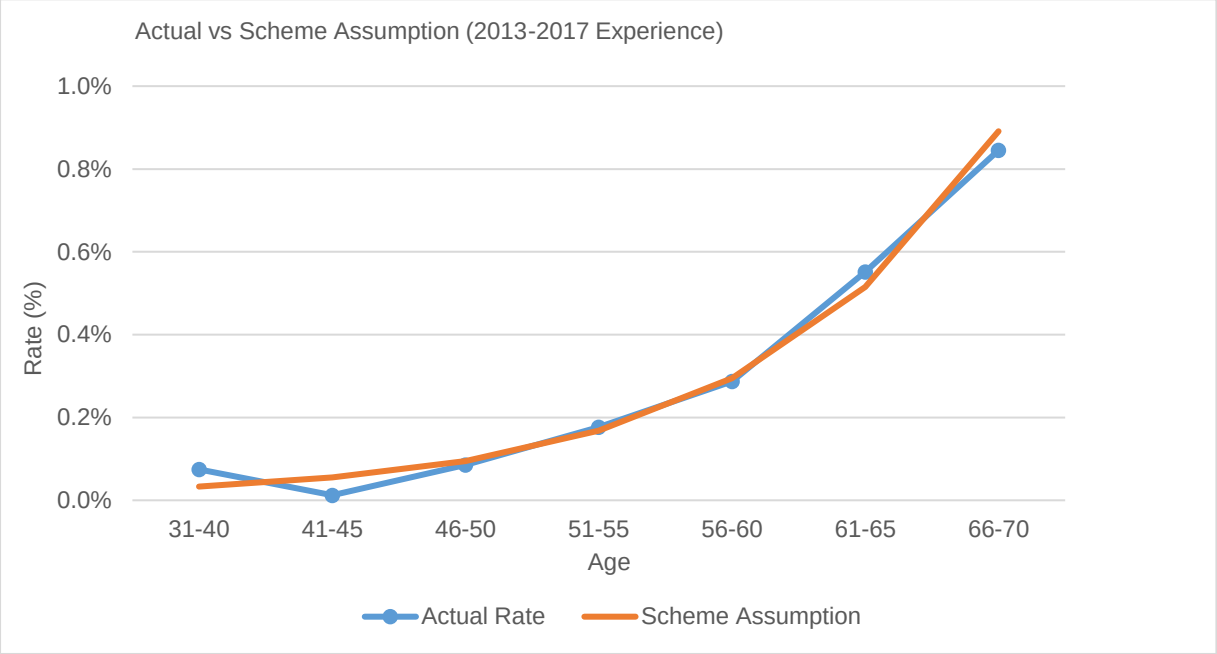


Chart A.2 Whole of Life Male Mortality Rates for ages 71 and over

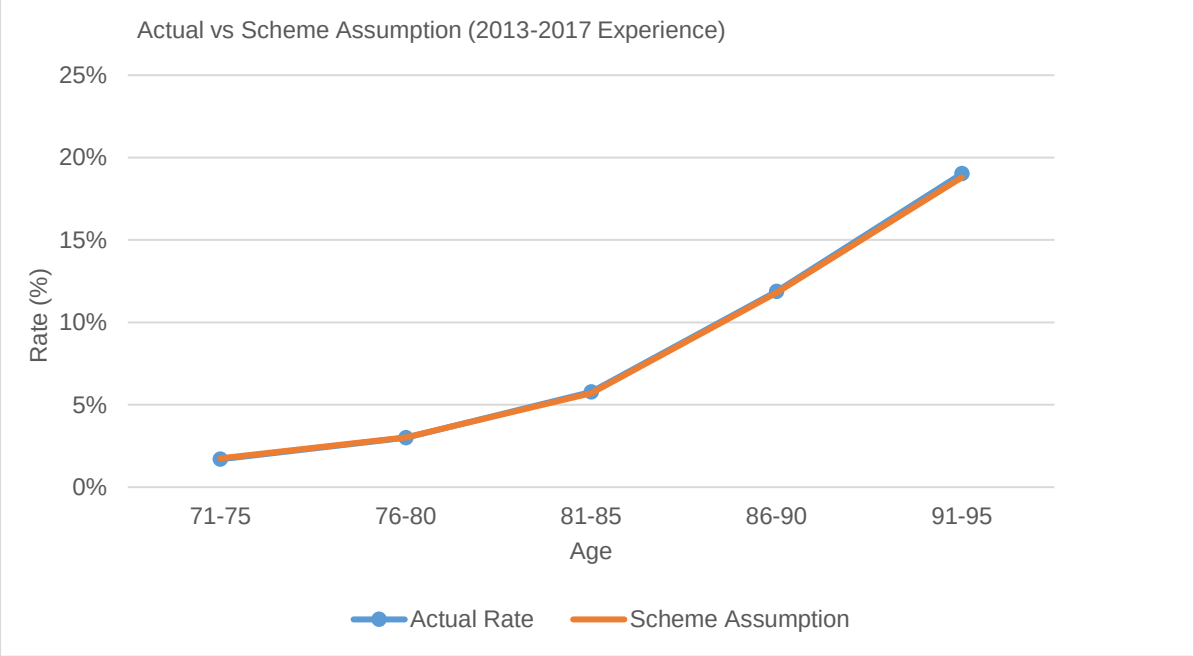


Chart A.3 Whole of Life Female Mortality Rates for ages 31-70

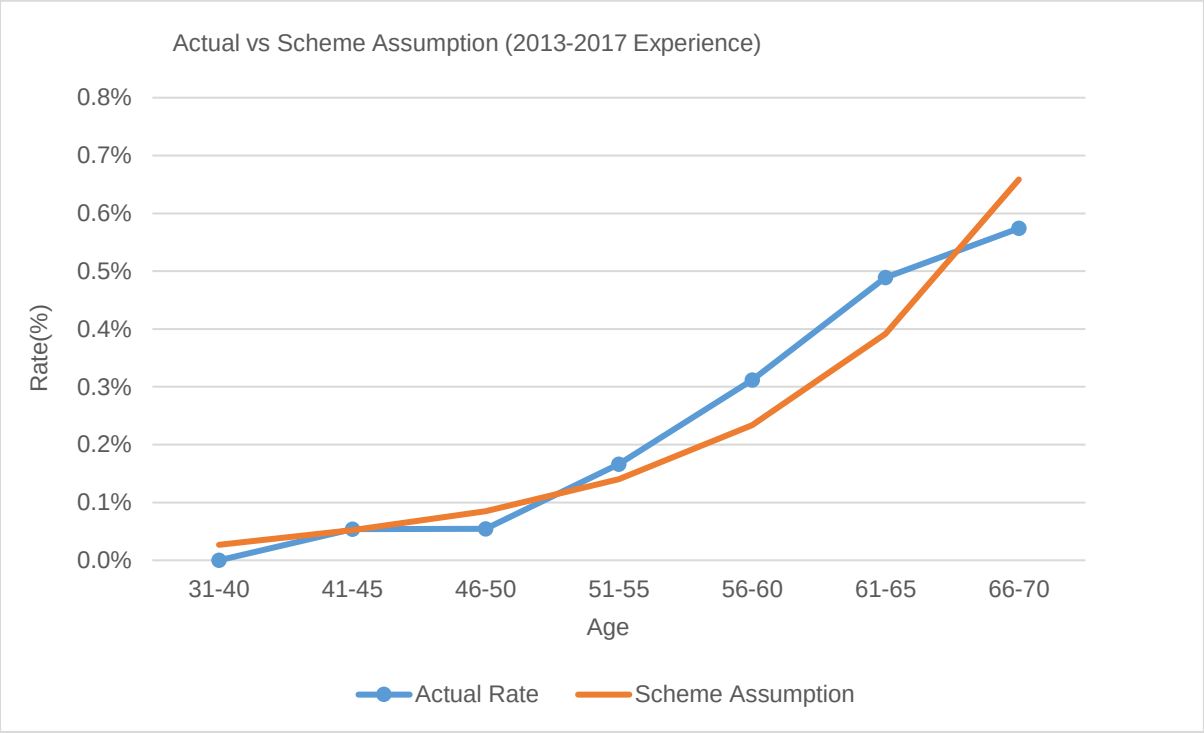
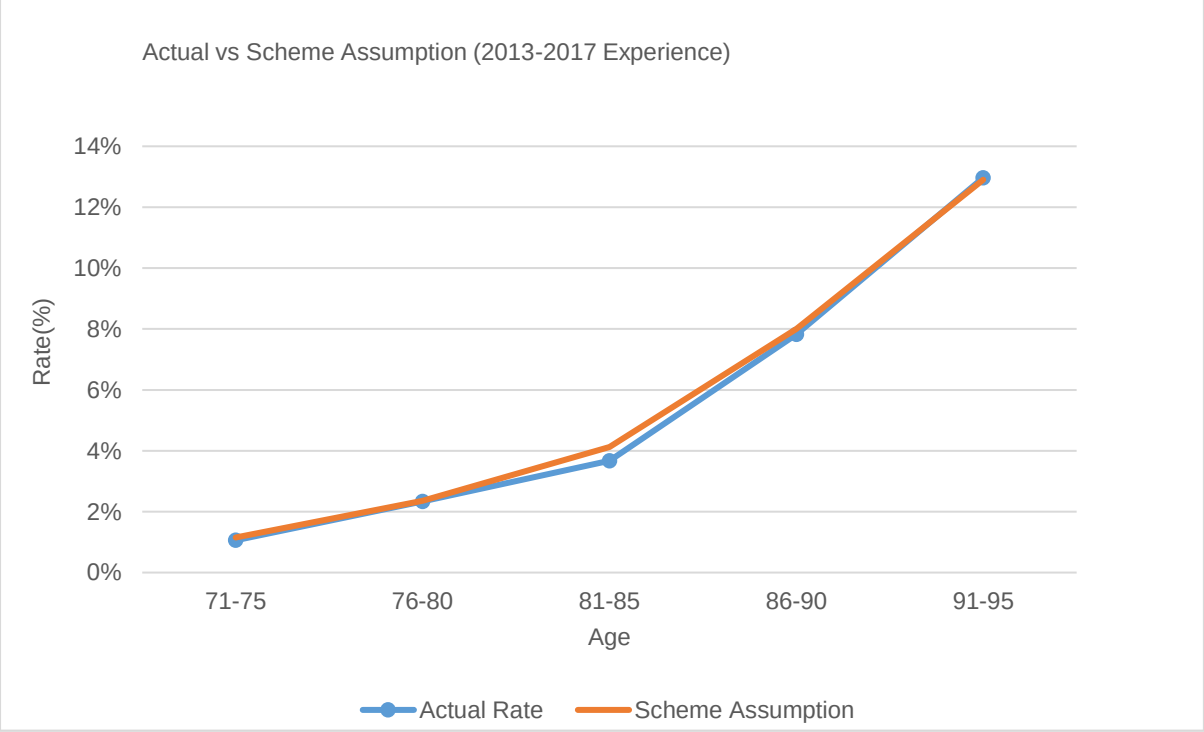


Chart A.4 Whole of Life Female Mortality Rates for ages 71 and over



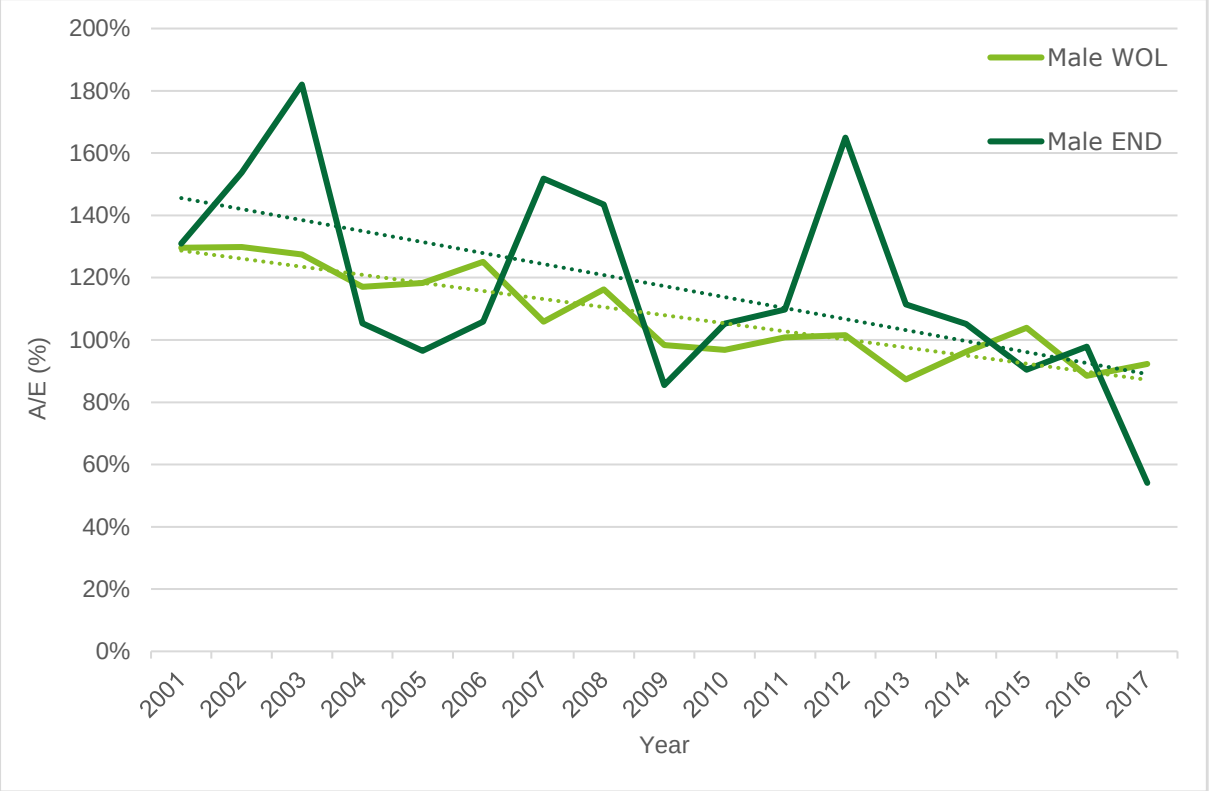
The volume of Endowment business is much lower than it is for Whole of Life. The mortality investigation used Foundation Life's existing assumptions for the investigation. For Endowment mortality, male experience (98 deaths) was in line with expected (103 deaths) over 2013 to 2017. Low numbers of female endowment policies made the analysis of low statistical significance, with only 10 deaths in the prior 5 years. However, this was in line with 11 expected deaths. The existing assumptions were, therefore, adopted for the Scheme.

A.2.3 Future mortality improvement

The mortality of male lives insured has shown general improvements since 2001. The chart below (against a consistent base of 2016 assumptions) is indicative of an overall male Whole of Life mortality improvement of some 2% per annum.

Male Endowment policies have also shown a very similar trend, albeit with a much lower policy count.

Chart A.5 Aggregate Male Mortality Experience 2001-2017, Actual/Expected



The mortality of female lives insured has shown a general improvement since 2001 of some 4% pa. Female Endowment policies have not been analysed due to the low number of policies and deaths.

The annual mortality improvement seen over 15 years to 2018 in the official NZ population Mortality Tables was around 1.7% for both males and females aged 40-80 and was 1.2% over age 80. The corresponding figures over the last 5 years to 2018 were around 1.1% and 0.4% respectively.

The slowing of mortality improvements is a common trend in countries with a similar standard of living to New Zealand and has been taken into account when setting the improvement assumption – it may mean that mortality reaches the point at which it ceases to improve. In recognition of this, it is reasonable to assume that mortality continues to improve for 20 years and that mortality remains level thereafter.

A.2.4 Mortality improvement assumption

Using the NZ population mortality improvements as a guide alongside recent declines in the rate of population mortality improvements, the mortality improvement assumptions are;

- males and females aged 80 and under - the mortality improvement to be 1.0% pa from 2017 to 2037 and no improvement thereafter
- males and females aged over 80 - no mortality improvement.

A.3 Surrender Rates

A.3.1 Introduction

This section sets out the rationale for the assumptions for surrenders. There are different assumptions for the main projection and for other purposes in the model.

A.3.1 Main projection

Surrenders are not assumed at all in the cash flows of the main stochastic projection.

Assuming no surrender rates aligns the value allocated to those Eligible Policyholders who would surrender with those who would not. Effectively, it gives value to each policy on the basis that it runs for its full term and so is an appropriate approach to take in modelling the Participating Fund for its allocation to Policyholder level.

A.3.2 Other purposes

Surrender rate assumptions are used, however, to support the modelling - for example, in bonus determinations where Foundation Life's existing practices are followed and these include valuing policies with a surrender assumption.

The analysis carried out for October 2013 to July 2017 showed that the surrender rates were in line with Foundation Life's existing surrender assumptions and so those rates were appropriate. A high-level analysis of surrenders from 2017 to 2020 indicated no changes were needed.

A.4 Maintenance expenses, commission and investment management expenses

A.4.1 Introduction

The Scheme requires an allocation of expenses to policy level and, in the case of investment management expenses, to both shareholder and Eligible Policyholders. This Section considers the amount and allocation of the maintenance expenses, commission and investment management expenses.

A cap on the maintenance expense is an important part of the assumption setting. Set out below is the rationale for the adopted assumption.

A.4.2 Maintenance and Commission Expense assumptions

The starting per policy expense figure is the FY24 Budget expense of $3.7m spread over the average number of policies over FY24 (strictly speaking, full policy equivalents after allowing for the 1/3rd weight given to paid-up policies). The Scheme costs are not included in the expenses for determining the per policy expense assumption.

Within the projections, the aggregate maintenance expenses are increased each year with inflation and checked against the cap which is also inflated.

The Paid-up Policy (PUP) expense assumption is a long-standing assumption.

Commission of 4% is generally paid on premium paying policies. However, not every policy has a designated adviser and associated commission payment. The commission rate assumption used at the Effective Date will be the average commission rate allowing for the adviser data at the time. This rate will be applied to all policies.

Designated advisers will be paid the equivalent of three years' renewal commission if the Scheme goes ahead. This amount is appropriate given the termination of the commission stream and the anticipated assistance advisers will be giving Eligible Policyholders should the Scheme proceed to a vote. Foundation Life will refer Eligible Policyholders who ask for advice on the Scheme to their adviser. Foundation Life will continue to provide information on the Scheme to advisers as required and on its website. The amount payable will be allowed for in the financials of the Scheme; it was estimated to be $0.4m at 30 September 2023.

Expense inflation assumptions, including those for the expense cap, are generated from the Economic Scenario Generator (See A.5.2) and are not within the remit of this section.

Table A.2 Expense assumptions

Expense Type	Assumption
Per policy expense	$140.59 pa
Per policy expense cap before future inflation adjustments	$164 pa
Proportion of per policy expense allocated in respect of PUPs	33%
Average renewal commission	2.50% Annual Premium
Commission to Close	3 x 12 months' commission

A.4.3 Maintenance Expense Cap Assumption

In respect of maintenance expenses, it is reasonable for the Participating Fund to meet expenses at the market level. However, Foundation Life would continue to lose policy count at around 5% p.a., and it is not reasonable, in my view, to assume the Participating Fund will meet ever-increasing per policy expense rates. Therefore, it is appropriate for the projections to introduce a per policy expense cap on the expenses charged to the Participating Fund by assuming Foundation Life will find a way to cap them in the future.

I assessed that market expense levels in 2017 would likely lie in the range $100 to $140 per policy, based on limited information. Foundation Life was at the bottom of this range. The assumption for the cap of $130 in 2017 is above the middle of the range to avoid disadvantaging Eligible Policyholders through the use of a low cap (because the calculation of Policy Values includes future expenses). With six years' inflation to bring it up to 2023 from 2017, the cap was $164 per policy at September 2023.

A.4.4 Investment Management Expense Assumptions

Assumptions are based on the investment management charges from the Fisher Funds Investment Management Contract as amended in March 2023 and allow for asset allocation costs, expense recoveries, GST where appropriate, custodial charges and Foundation Life expenses.

A.4.5 Expense Allocation Assumption

Maintenance expenses, once determined, are allocated to individual policies in proportion to the value of new Annual Bonuses in the same year (effectively the surrender value of the new Annual Bonus in the year). This approach matches the allocation of expenses to the allocation of bonuses in the same year. It is appropriate because marginal changes in expenses would lead to marginal changes in bonuses.

The allocation of commission to individual policies is handled by applying the assumption as a proportion of premiums.

The investment management expense needs further allocation between the shareholder and Eligible Policyholders.

Investment income and investment management expenses are generated by the Participating Fund assets. Therefore, the allocation of the investment management expenses to each policy and to the shareholder ought to be in proportion to each party's stake in the assets of the Fund. This will change in each future time period as some policies exit, to reflect cash flows and changing interest rates. Projected policy liabilities in each future time period have been used for this purpose. The component of the policy liabilities that is the value of future shareholder transfers has been used for the shareholder. The balance of the policy liability has been used for each policy, with a part period allocation to policies that matured in the period.

A.5 Investments and multiple scenarios

A.5.1 Introduction

This section explains the approach taken to asset modelling and the multiple scenarios used, each with different asset returns. Foundation Life's investment strategy has been applied every year in each scenario, to set the mix of assets for the year ahead. The scenarios were obtained from Towers Watson Australia Pty

Ltd trading as Willis Towers Watson ("WTW") to produce an appropriate model as at 30 September 2023. New scenarios will be obtained for the implementation of the Scheme to reflect the then current investment conditions, interest rates in particular.

A.5.2 Multiple scenarios

WTW used its own Economic Scenario Generator ("ESG") to create multiple scenarios. Each scenario was different, containing, for every year of the projection:

- NZ$ risk free yield curve
- Equity returns, NZ and international
- Property returns
- Credit spreads
- Credit losses
- Inflation.

The ESG was calibrated to market conditions at 30 September 2023 and signed off by WTW. I was satisfied with the documentation provided by WTW to demonstrate the calibration of the ESG.

A.5.3 Foundation Life investment strategy

The modelled investment strategy has been aligned with Foundation Life's approach to managing the assets of the Participating Fund as if there were no Scheme.

Foundation Life has summarised its obligations to Eligible Policyholders, in the absence of the Scheme, as follows:

- To meet Eligible Policyholders' claims in full in all but extreme circumstances
- To ensure that Eligible Policyholders' interests are prioritised relative to the interests of the shareholder. Subject to the point above, this will involve seeking to maximise Policyholder outcomes
- To treat Eligible Policyholders fairly. This is not only relative to the shareholder, but also between Eligible Policyholders.

The approach that Foundation Life has taken to meet the above obligations is to view the investment assets as comprising two separate portfolios and to manage them accordingly. The two portfolios are:

- Liability matching portfolio ("LMP") – this is the fixed income portfolio comprised of high rated bonds, being a mixture of NZ Government bonds and corporate bonds rated AA- or higher. The assets are invested in such a way that the guaranteed policy liability ("GPL") is covered or "matched" in a wide range of circumstances. Duration mismatch is an issue for a long duration fund backed by shorter duration available assets. This mismatch is managed by holding fixed interest assets greater in value than the GPL and/or by using swaps to increase the duration of the asset portfolio. A small amount of mismatch may be taken to reflect the investment manager's views of future interest rates. For modelling purposes, this has been taken as, if interest rates go below a view of a long-term neutral position, then assets shorter than liabilities will be held. Similarly, if interest rates go higher than a view of a long-term neutral position, then assets longer than liabilities will be held.
- Future return portfolio ("FRP") – this is the portfolio of residual investment assets that will be an additional source of the future bonuses payable to Eligible Policyholders. Given the remaining term of the Participating Fund, this portfolio could be considered a long duration portfolio which will liquidate over the next 40+ years.

The FRP target asset mix is:

Table A.3 FRP target asset mix

	Mix
New Zealand Equities	23.4%
Australian Equities	10.0%
International Equities – currency hedged	33.3%
Property	33.3%
Total	**100%**

I agree with Foundation Life's adoption of this approach to managing the assets of the Participating Fund as it appropriately seeks to maximise returns to Eligible Policyholders while taking a very low risk of the fund becoming unable to meet its liabilities. This is a sound approach to Eligible Policyholders' interests that is consistent with Foundation Life's constitution. I believe that the company's demutualisation in 1999 placed no constraints on the management of the assets of the Participating Fund.

Foundation Life's investment approach leads to the LMP being around 80% of the assets of the Participating Fund, with the remaining 20% of the assets in the FRP. While 20% may seem a low proportion to be invested in growth assets, protecting the Fund's solvency requires a high allocation to the LMP. In preparation for the Scheme vote, however, Foundation Life has taken a short-term tactical decision to sell its growth assets. This is not relevant to a long-term projection of Foundation Life's business. A long-term projection needs to forecast those situations in which the guarantees that Eligible Policyholders receive under their policies must be met by the shareholder. To do this, it needs to reflect the risks that may be taken rather than the present de-risked portfolio.

At the beginning of each year of the projection under stochastic modelling, the then policy data is used to determine a portfolio duration and the allocation of assets between the two portfolios. Policy data remains relevant throughout a projection and asset allocations are developed according to projected policy cash flows and the stochastically varying investment return.

A.5.4 Best Estimate Investment Return for year

A Best Estimate investment return is needed for projecting each year's valuation of the policy liabilities. This is used in the determination of each year's bonus rates. Once the portfolio for a year is determined, a base return rate of the 10-year Government Bond yield is taken from the ESG. Asset class specific returns are built up from the following spread assumptions for how much the earnings for each asset class are expected to exceed the 10-year Government Bond yield:

Table A.4 Spread on base return by asset class

Asset Class	Spread	Notional Assets Applicable
Fixed Interest	0%	LMP
Trans-Tasman Equities	5%	FRP (1/3rd)
International Equities	4%	FRP (1/3rd)
Property	2.25%	FRP (1/3rd)

Previous analysis undertaken by Foundation Life has determined that the spreads detailed above are appropriate for these asset classes. These risk premium spreads are used in the current Foundation Life valuation basis and have been held constant since 2004.

A.6 Bonuses

A.6.1 Introduction

This section sets out the approach to modelling future bonuses for each year of each scenario in the model, based on Foundation Life's bonus philosophy.

A.6.2 Existing bonuses

Currently Foundation Life uses:

- An Additional Bonus scale to distribute past profits
- An Annual Bonus to distribute the remainder of the Participating Fund assets based on best estimate assumptions.

If the best estimate assumptions were borne out then the Additional Bonus would run off as described in section 10.2.1 and the Annual Bonus would be stable. The stochastic model, however, will incorporate different scenarios which will generate additional profits and losses above/below those generated using the best estimate assumptions. Those future gains or losses will come from the performance of the Future Return Portfolio ("FRP") in the main and also, to some extent, from the tactical mismatching in the Liability Matching Portfolio ("LMP").

These additional profits and losses will be reflected in changes to future bonuses, in line with Foundation Life's bonus philosophy.

A.6.3 Future bonuses

Foundation Life declares bonuses annually. Each year's bonuses are decided by the directors on the advice of the appointed actuary. The model emulates this approach.

Foundation Life's philosophy for the Participating Fund calls for the assets of the Participating Fund to be wholly distributed over the life of the Fund and for fair treatment of all Eligible Policyholders. Eligible Policyholders who exit the Fund in the near future must be treated equitably compared with those who will remain in the fund for many years.

The model uses a sustainable Annual Bonus in line with this philosophy. The Annual Bonus is determined in the model each year in each simulation based on economic conditions at the time. It is the Annual Bonus that would endure if conditions did not change.

Any additional profits and losses result are reflected in the modelled rate of Additional Bonus.

A.6.4 Bonus Rates

A.6.4.1 Annual Bonus rates

Annual Bonus rates differ by product. The tables below show the 2023 Annual Bonus rates for all products. They were the same bonus rates as those for the 2022 financial year.

Table A.5 2023 Annual Bonus Rates per $1,000 by Product

Table Name	Annual Bonus on sum insured	Annual Bonus on bonus
Asp, Bsp	15.0	17.0
2L	**25.0**	**17.0**
A, B	14.0	16.0
CD	**12.5**	**15.0**
CN	11.0	15.0
AN, BN	**14.0**	**17.0**

Table A.6 2023 High Annual Premium (>$1800pa) Rates Declared Per $1,000

Table Name	Annual Bonus on sum insured	Annual Bonus on bonus
CN	**14.0**	**21.5**
AN, BN	17.0	24.0

A.6.5.2 Future Annual Bonus rates

In line with Foundation Life's past practice, the relativities between the Annual Bonus rates above is maintained in the model for future Annual Bonuses. This means that the ratios between different products' Annual Bonus rates do not change in the modelling, whatever the level of bonus. Similarly, the ratio of each product's Annual Bonus on bonus to its bonus on sum insured does not change.

A.6.5.3 2023 Additional Bonus rates

Foundation Life's Additional Bonus rates depend on the issue date of a policy. They are currently for whole of life policies only. Additional Bonuses for endowment policies ceased in 2020, following a 5-year phasing down period. The Additional Bonus rates for 2023 are shown in the table below for a sample of policy terms, the term being the number of years the policy has been in force.

Table A.7 2023 Additional Bonus rates as a % of Annual Bonuses

Term in years	Whole Life Additional Bonus Rates (as a % of added Annual Bonuses)
0 - 10	10.0
15	11.5
20	14.0
40	24.0
45	26.5
50	37.25
57+	60

In the absence of the Scheme proceeding, Foundation Life's intention is that these rates of Additional Bonus will be retained until 30 September 2026 and that they will then reduce to nil over the next 10 years in even steps.

A.8 Tax

A.8.1 Basis

Tax is assumed to be payable on the September 2023 New Zealand taxation basis.

A.8.2 Tax payable

The projections will reflect whether or not tax is payable in a year. Tax losses are to be carried forward. In some scenarios, there may be tax losses that are not recovered by the end of the projection. In those cases, the tax benefit will be lost. The deferred tax asset ("DTA") is an input at the projection start date (being $28.6m as at 30 September 2023). If the tax for any given period is positive the DTA is reduced until it is eliminated and any tax remaining is payable in cash. Negative tax for a period is added to the DTA.

A.8.3 Allocation of tax between policyholders and the shareholder

The tax expense is allocated between shareholder and policyholders.

The tax deductions for maintenance expenses and renewal commission are allocated to each policy in proportion to its allocation of maintenance expenses and renewal commission.

Investment income and investment management expenses are generated by the Participating Fund assets. Therefore, the allocation of the tax / tax relief on them to each policy and to the shareholder ought to be in proportion to each party's stake in the assets in each time period. Policy liabilities as used in the projections have been used for this purpose. The component of the policy liabilities that is the value of future shareholder transfers has been used for the shareholder. The balance of the policy liability has been used for each policy, with a part period allocation to policies that matured in the period.

A.9 Valuation of Rider Benefits and assumptions

A.9.1 Introduction

This section sets out the methodology and assumptions for valuing the Rider Benefits, which on 30 September 2023 were attached to 232 policies within the Scheme.

A.9.2 Level and decreasing term riders

A.9.2.1 Rider death and disability benefits

The cash value of the death benefit has been calculated as the present value of benefits less the present value of premiums, but subject to the minimum value stated in section A.9.2.3.

A.9.2.2 Rider convertibility option

The conversion option allows the Policyholder to take out a new whole of life policy at ordinary rates without further evidence of health. The option is assumed to be exercised at the latest possible date. For level term riders this at the expiry of the rider. For reducing term riders, that is 10 years before expiry of the rider in line with the policy conditions.

The option has value to those Eligible Policyholders whose health was sufficiently poor at the time of exercising the option that they could not buy a new whole of life policy at ordinary rates. The option has value because of the premium saving it generates. Thus, the value of the option is the discounted value of the extra premium that the Policyholder would have to pay in the absence of the option. The option has no value to a Policyholder who was in sufficiently good health that they could obtain insurance at ordinary rates.

The extra premium was based on the average level of loading that applied at policy inception for all Foundation Life Eligible Policyholders (see section A.9.4.5 for further details).

For all the riders it is assumed that all of the available benefit is converted into a whole of life benefit to age 95.

The value for the convertibility option has been calculated as the present value of premiums saved across the new policy term multiplied by the probability of a premium loading being applied (see section A.9.4.6 for further details), but subject to the minimum value stated in section A.9.2.3.

A.9.2.3 Total rider value

The total value of the rider is then calculated by adding together the value of the death benefit above and the value of the attaching convertibility option (calculated below) where applicable. A minimum of two times the annual rider premium is then applied to that result to produce the final rider valuation. The minimum is to make sure that there is some value for Eligible Policyholders.

A.9.3 Guaranteed Insurability Option

Eligible Policyholders with this rider ("GIO") are entitled to take out a new whole of life policy for the given sum insured on ordinary rates on attaining each of a series of specific ages, namely ages 24, 28, 32, 36, 40 and 44.

It is assumed that Eligible Policyholders exercise all future options that they are entitled to take.

The method for valuing each of the future options is the same as the method for the convertibility option on the term death benefit riders including the application of a minimum of two times the annual GIO premium.

A.9.4 Rider valuation assumptions

A.9.4.1 Investments

A curve of risk-free rates from the Economic Scenario Generator has been used for discounting. The tax rate has been set at 28% and investment management expenses have been set at 0.20%, the cost for fixed interest investments.

A.9.4.2 Mortality and disability

The mortality methodology follows that used in the model for valuing the participating policies. The assumed disability rates were the same as the mortality rates.

A.9.4.3 Expenses

Expenses have not been allowed for in any of the rider valuations as these are all borne by the main policy in the Scheme.

A.9.4.4 Surrenders

In line with the model for valuing the participating policies, no withdrawals have been assumed.

A.9.4.5 Average premium loading

The average premium loading of the book was investigated based on all policies with a premium loading. The data was analysed by age at inception and sum insured. The resulting averages are shown in the table below. The overall average loading is 21.8%. There is no strong trend in the level of premium loading by age or sum insured band. Given that the data excludes people who have declined loadings or are uninsurable a single average loading percentage of 30% has been assumed.

Table A.8 Average premium loading by age and sum insured bands

	Sum Insured Band				
Age band	$0-5,000	$5,001-10,000	$10,001-15,000	$15,001-20,000	$20,001+
0-20	16.63%	20.16%	20.56%	21.71%	25.13%
21-40	28.94%	20.52%	17.64%	20.61%	19.09%
41-60	22.86%	31.37%	18.31%	26.67%	22.47%
61+	35.71%	22.55%	22.88%	20.88%	19.85%

A.9.4.6 Probability of a policy being loaded

The probability that a new underwritten policy will be loaded is assumed to be 5%. This value has been set based on the proportion of policyholders with a loading in a presentation about substandard lives given by Leonie Tickle in 2005 at the Australian Institute of Actuaries Convention in 2005 entitled "Are substandard lives charged appropriate loadings?". The presentation identified that 3% of the exposure of a large block of whole of life, endowment and renewable temporary policies studied between 1995-2000 related to substandard lives. Even recognising that the data is out-of-date, the assumption of 5% is conservative given that no options have been exercised in the past 5 years.

Appendix B – Glossary

Item	Definition	Defined in section
Additional Take-up Premium	The increase to the premium payable to Chubb Life that occurs when using the actual Take-up Rate	3.2
AIA	Foundation Life's main computer system that holds the data on participating policies	12.1
Base Premiums	The premiums calculated for each policy at 100% Take-up Rate	3.2
Cash Payment	The option to take the Scheme benefits wholly in cash	1.4.1
Chubb Life	Chubb Life Insurance New Zealand Limited	1.4.1
Economic Scenario Generator	The system that produced the 10,000 scenarios used for the calculation of Policy Values	A.5.2
Eligible Policyholder	The owner of a policy to which the Scheme applies	1.1
Effective Date	The date on which the Foundation Life policies cease, the Chubb Life policies commence, and any cash benefits become payable	1.2
Existing Death Benefit	The total of the sum insured, annual bonuses and additional bonus on the Effective Date. It excludes any cover provided by a Rider Benefit.	1.4.3
Full Cover	105% of Existing Death Benefit	3.1
Fund	Participating Fund	
High Court	The High Court of New Zealand	
IBNR	Claims that were incurred but not reported before the Effective Date	2.2.6
IPSA	Insurance (Prudential Supervision) Act 2010	2.2.6

Item	Definition	Defined in section
Participating Fund	The segregated pool of assets formed from the accumulation of premiums on participating policies less the claims and expenses of those policies. Investment earnings on the assets after tax are added to the Fund, and the shareholder's entitlements are deducted.	1.3
Policy Value	The share of the Participating Fund to be attributed to each policy on the Effective Date as determined through Stochastic Modelling	1.2
Pre-agreed Assets	The specified assets at a pre-agreed value that will be used in whole or in part to meet the premium payable to Chubb Life	3.3
RBNZ	The Reserve Bank of New Zealand	1.2
Record Date	The cut-off date for identifying policies covered by the Scheme. It will be three days before the Scheme Meeting.	2.2.3
Replacement Cover	Life insurance provided by Chubb Life to replace existing life insurance	1.4.1
Replacement Policyholder	The person or entity with a New Zealand residential address to whom a Policyholder with an overseas residential address may transfer their policy in order to have Replacement Cover available under the Scheme	2.4
Residual Cash	Any cash payable to an Eligible Policyholder receiving Full Cover	3.1
Rider Benefits	Extra benefits that some policies have for additional life insurance benefits or the right to take out new insurance in the future without having to provide evidence of good health	1.3
Scheme	The scheme of arrangement that will define the benefits to Eligible Policyholders and to the shareholder to replace their existing entitlements	1.1

Item	Definition	Defined in section
Tailored Alternative	A possible Scheme in which Full Cover was an equivalent level of life cover to the existing life benefits, with a minimum of 105% of Existing Death Benefit	10.7
Take-up Rate	The Take-up Rate for Replacement Cover by Eligible Policyholders, which is determined by dividing the total sum insured under Replacement Cover by the total sum insured that would have arisen if all Eligible Policyholders had received Replacement Cover. Any insurance bought with Residual Cash is not included in this calculation.	1.4.2
103% Alternative	A possible Scheme in which Full Cover was 103% of Existing Death Benefit instead of 105%	10.7
105% Uplift Premium	The excess, if any, of the Base Premium for a Policyholder over their Policy Value	3.2
110% Alternative	A possible Scheme in which Full Cover was 110% of Existing Death Benefit instead of 105%	10.7

Appendix C - Data accuracy

C.1 Introduction

Accurate data is needed if Foundation Life is to provide the correct benefits to its Eligible Policyholders. This section describes the steps that Foundation Life took to maximise the accuracy of its data. It then describes the steps I took to check I had used all of that data correctly.

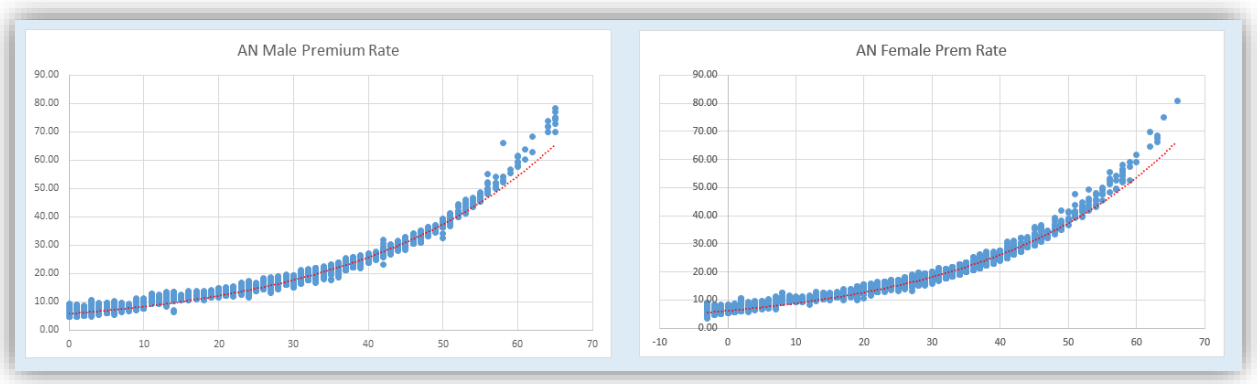
The data used for the Scheme is the policy data held on Foundation Life's main computer system ("AIA"). This includes data on policy loans, premium debt, and on premiums paid in advance of the date they were due. AIA has been used by Foundation Life for policy administration since 2001.

C.2 Premium rate check

Foundation Life checked the premium rates on its whole of life policies. It did this by dividing the standard premium for each premium paying policy by the sum insured. The standard premium is the total premium less any extra premium payable for reasons of poor health, pastimes or occupation. By product, most premium rates sat on a curve by age at policy start date, one curve for each gender. This was to be expected as, at any time, premium rates varied by age and gender. It was apparent that premium rates had not changed very much over time. Foundation Life examined all outliers from the curves. It corrected all errors that it found.

After correcting the data, Foundation Life reperformed its tests. The charts below show the premium rates for every policy in the main whole of life product group. They demonstrate the closeness of the premium rates to the fitted curve shown in red below.

Chart C.1 Premium rates for the main policy type (AN) in the whole of life product group



C.3 Missing addresses

Foundation Life has run a project to trace Eligible Policyholders whose mail had been returned to Foundation Life as the address was no longer the Policyholder's address. As a result, it found some death claims that had not previously been notified to Foundation Life that have now been paid or are in the process of being paid. It also was able to correct the addresses for many Eligible Policyholders to where they are now living. Foundation Life continues to work on tracing Eligible Policyholders for whom a valid address is not held.

Eligible Policyholders not responding to the Scheme will be awarded their default benefits. If Eligible Policyholders entitled to a cash pay-out do not claim it, the money will be passed to the Inland Revenue under the Unclaimed Monies Act 1971. This will be not less than 6 months after the Effective Date. Eligible Policyholders can then claim their pay-out from the Inland Revenue. Eligible Policyholders who have been issued a life insurance policy with Chubb Life can claim the sum insured from Chubb Life upon the death of the life insured.

It appears to me that Foundation Life has been as diligent as it can be in locating Eligible Policyholders with an out-of-date address. If Eligible Policyholders who could not be traced eventually come forward, then they will find they have been given an acceptable replacement for their policy with Foundation Life even if it may not have been the choice that they would have made had they responded to the Scheme documentation. In the circumstances, I consider these Eligible Policyholders will have been handled appropriately.

C.4 Letters to Eligible Policyholders

When Foundation Life has written to Eligible Policyholders to inform them of the Scheme, it has asked them to confirm key policy data. With better address data, more Eligible Policyholders had the opportunity to advise Foundation Life if their data was incorrect. The response rate to the letters was low, which suggests good data accuracy.

C.5 Audit

PwC carried out a data audit in 2017. This identified some inaccurate data and this audit was one of the sources used by Foundation Life to correct its policy data.

C.6 Data used in the Scheme

Policy data was extracted from AIA and converted into a format for use in the models used for calculating Policy Values and Eligible Policyholders' insurance and cash benefits from the Scheme. I received all of the data that I needed.

Foundation Life developed procedures and controls to manage the collection and transfer of data through the model run process. Reconciliations were established to AIA source data and then at every data transfer point, ensuring completeness and accuracy of data inputs and outputs. I reviewed the reconciliations, following sign off by Foundation Life, and found them to be accurate. There were no security breaches to my knowledge.

Table C.1 Data reconciliation at 30 September 2023

	AIA System	Model Inputs	Variance	Model Outputs	Variance
Policy Count	28,226	28,233	7	28,226	-
Sum Insured	363,335,582	363,439,280	103,699	363,355,582	-
Reversionary Bonus	383,345,845	383,401,891	56,046	383,345,845	-
Annual Premium	5,095,073	5,095,073	-	5,095,073	-

Foundation Life investigated and explained all variances, as follows:

- Model Inputs Variance

  7 policies had a maturity date of 30 September 2023. These policies were not in-force on 1 October 2023 and therefore would not have been included in the Scheme. They have therefore been excluded from this report. However, for system processing purposes they needed to be included in the model input files. This is a matter of cut off, and I was happy with the explanation provided and action taken.

- Model Outputs Variance

  The model outputs were satisfactorily reconciled to AIA, which demonstrated that all eligible policies at 30 September 2023 had been accurately included in the data forming the basis of my report.

C.7 Conclusion

I have reviewed the controls performed to ensure the data was accurately extracted from AIA for use in my work for the Scheme. I was satisfied that Foundation Life had taken reasonable steps to identify and correct errors in its data, including giving Eligible Policyholders the opportunity to review their own data. I consider the data provided by Foundation Life to be suitable for the calculations required to implement the Scheme.