This Independent Actuary's Report contains a Report dated 29 March 2021 and an Erratum dated 5 May 2021. Please refer to the last page of this Independent Actuary's Report for the Erratum. You should read the Report together with the Erratum as a whole.

MILLIMAN CLIENT REPORT

Report of the Independent Actuary on the Transfer of Business from the Hong Kong Branch of Zurich Life Insurance Company Ltd. to Zurich Life Insurance (Hong Kong) Ltd.

29 March 2021

PAUL SINNOTT, Principal & Consulting Actuary

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Independent Actuary's Statement of Opinion

I, Paul Sinnott, am associated with the firm of Milliman Limited ("Milliman"). I am a Fellow of the Institute and Faculty of Actuaries (United Kingdom), and a Fellow Member of the Actuarial Society of Hong Kong. I have been appointed to act as the Independent Actuary pursuant to Section 24 of the Hong Kong Insurance Ordinance Chapter 41 (the "Ordinance"), to provide an independent opinion on the terms and likely effects of the proposed scheme (the "Scheme") for the transfer of all long term insurance business carried on by Zurich Life Insurance Company Limited ("ZLIC") through its Hong Kong Branch ("ZLIC HK branch") (also hereinafter referred as "Transferring Business") to a new Hong Kong domiciled subsidiary of Zurich Insurance Holdings (HK) Limited ("ZIH"), which is wholly-owned by Zurich Insurance Company Ltd. ("ZIC"), namely Zurich Life Insurance (Hong Kong) Ltd. ("ZLIHK").

Throughout this report, ZLIC, ZLIC HK branch and ZLIHK are collectively referred to as the "Parties"; the Transferring Business policyholders are referred to as the "Transferring Policyholders", who hold policies which are underwritten by ZLIC HK Branch (the "Transferring Policies"); the policyholders remaining in ZLIC after the Scheme are referred to as the "Non-Transferring ZLIC Policyholders", who hold policies which are underwritten by ZLIC excluding those underwritten by ZLIC HK branch (the "Non-Transferring ZLIC Policies"); and the existing policyholders of ZLIHK before the Scheme are referred to as the "Existing ZLIHK Policyholders", who hold "Existing ZLIHK Policies".

The Scheme is an important component in the simplification of ZLIC's corporate structure, under which it is proposed that the Transferring Business, all employees and all other business undertakings of ZLIC HK branch should be transferred to ZLIHK.

In forming my opinion, I have been given free access to available information, reports and documents that I considered necessary and requested. In addition, I have also been given free access to the representatives of the Parties.

The scope of my review and opinions are confined to the effects of the Scheme on the policyholders of the Parties. There will be no remaining policyholders in the ZLIC HK branch once the Scheme is implemented. In particular, I have formed my view by considering:

- The likely effects of the Scheme on the reasonable expectations of the policyholders of ZLIC and ZLIHK respectively and, in particular, the Transferring Policyholders of ZLIC HK branch, with regards to benefits and levels of service;
- The effect of the Scheme on the financial security of the contractual benefits of the policyholders of ZLIC and ZLIHK respectively and, in particular, the Transferring Policyholders of ZLIC HK branch; and
- The adequacy of safeguards in the Scheme to ensure that the Scheme operates as presented.

The scope of my work does not include assessing the impact of the Scheme on the shareholders of the Parties. I have considered the Scheme as presented to me and have not considered any other alternative schemes of transfer.

In my opinion,

- The Scheme will not have a materially adverse effect on the reasonable expectations of the policyholders of ZLIC and ZLIHK, and in particular, the Transferring Policyholders of ZLIC HK branch, with regards to benefits and levels of service.
- The Scheme will not have a materially adverse effect on the financial security of the policyholders of ZLIC and ZLIHK, and in particular, the Transferring Policyholders of ZLIC HK branch.
- I am satisfied that the proposed Scheme provides sufficient safeguards to ensure that the Scheme operates as presented.

Paul Sinnott
Fellow of the Institute and Faculty of Actuaries (FIA)
Independent Actuary
29 March 2021

Section 1 Introduction

1.1. THE INDEPENDENT ACTUARY

1.1.1. When an application is made to the High Court of the Special Administrative Region of Hong Kong, Court of First Instance (the "Hong Kong Court") for an order to sanction the transfer of long term insurance from one insurer to another, it must be accompanied by a report on the terms of the scheme by an independent actuary in conformance to Section 24 of the Insurance Ordinance, Chapter 41 of the Laws of Hong Kong (CAP 41) (the "Ordinance").

1.1.2. I have been appointed by the ZLIC HK branch as the Independent Actuary in connection with the proposed scheme of transfer (the "Scheme") of the long term insurance business (also hereinafter referred as "Transferring Business" or "long term business") of ZLIC HK branch to ZLIHK, as a part of the restructuring of the Hong Kong operations of the Zurich Group.

1.1.3. My appointment as the Independent Actuary for the Scheme has been noted by the Hong Kong Insurance Authority ("IA").

1.2. SCOPE OF MY REPORT

1.2.1. This report considers the effects of the Scheme on the Transferring Policyholders, the Non-Transferring ZLIC Policyholders and the Existing ZLIHK Policyholders. It does not assess the impact of the Scheme on the shareholders of the Parties.

1.2.2. I have considered the Scheme as presented to me and have not considered other possible alternative schemes.

1.2.3. In reporting on the proposed Scheme I owe a duty to the Hong Kong Court to help it on matters within my expertise. This duty overrides any obligation to any person from whom I have received instructions or by whom I am paid.

1.2.4. In preparing the report, I consulted the IA on the required contents and incorporated suggestions from the IA as appropriate. The report is prepared in accordance with the approach and expectations in section 2 paragraphs 27 to 40 of the Prudential Regulation Authority ("PRA"), as set out in "The Prudential Regulation Authority's approach to insurance business transfers" dated April 2015 (the "PRA Statement of Policy"), this is enclosed as Appendix C to this report. I have also used Chapter 18 of the Supervision Manual ("SUP 18") contained in the Financial Conduct Authority ("FCA") Handbook as a reference document. Subsections SUP18.2.31G to SUP18.2.41G, which provide guidelines on the form of the independent expert scheme report, are enclosed as Appendix D to this report.

1.2.5. In May 2018, the FCA released further guidance with a document entitled "The FCA's approach to the review of Part VII insurance business transfer", where the FCA has set out expectations regarding the information to be included within the Independent Expert's report under Section 6 of this document. I have made reference to this guidance in the report and Section 6 of the document is enclosed as Appendix E.

1.2.6. I have been provided free access to the information that I requested as necessary to conduct my work. The key documents that have been made available to me include the Scheme document pursuant to Section 24 of the Ordinance, the Business Transfer Agreement, the Appointed Actuary Report for ZLIC as well as Appointed Actuary Report for ZLIC HK branch and ZLIHK, pricing approval policy, investment policy, statutory reserve and valuation reports, financial condition report (“FCR”), historical solvency positions for ZLIC under the Swiss Solvency Test (“SST”) basis and Hong Kong Insurance Ordinance basis (the “HKIO basis”) and the Dynamic Solvency Test (“DST”) for ZLIC HK branch before the Scheme implementation covering the recent 3 years, DST reports for ZLIHK with and without the Scheme implementation and information related to management of the Parties. Appendix B of this report shows the list of information and documents provided. In addition, I have also been given unrestricted access to and held discussions with various representatives of the Parties.

1.2.7. I have considered the following areas when forming my opinion in this report:

- the likely effects of the Scheme on the reasonable expectations of the policyholders of ZLIC and ZLIHK respectively and, in particular, the Transferring Policyholders of ZLIC HK branch, with regards to benefits and levels of service; and
- the effect of the Scheme on the financial security of the policyholders of ZLIC and ZLIHK respectively and, in particular, the Transferring Policyholders of ZLIC HK branch; and
- the adequacy of safeguards in the Scheme to ensure that the Scheme operates as presented.

1.2.8. The report should be read together with the full terms of the Scheme and the supporting information provided by the Parties as listed in Appendix B.

1.3. THE FRAMEWORK FOR THE INDEPENDENT ACTUARY’S CONSIDERATION OF THE SCHEME

1.3.1. As Independent Actuary, my assessment of the impact of the implementation of the Scheme on the various affected policies is ultimately a matter of expert judgement regarding the likelihood and impact of future possible events. Given the inherent uncertainty of the outcome of such future events and that the effects may differ across different groups of policies, it is not possible to be certain of the effect on the policies.

1.3.2. A Scheme may have both positive and negative effects on a group of policies and the existence of detrimental effects should not necessarily imply that the High Court should reject the Scheme as the positive effects may outweigh the negative effects or the negative effects may be very small.

1.3.3. In order to acknowledge this inherent uncertainty, the conclusions of the Independent Actuary in relation to transfers of long term insurance business are usually framed using a materiality threshold. If the potential impact under consideration is very unlikely to happen and does not have a significant impact, or is likely to happen but has a very small impact, then it is not considered to have a material effect on the policies.

1.3.4. The assessment of materiality will also take into account the nature of the potential impact so that, for example, the materiality threshold for a change that could have a direct financial impact on policyholders’ benefits is likely to be lower than the materiality threshold for a change that does not have a direct financial impact.

1.3.5. This is the framework in which I undertake my consideration of the Scheme.

1.4. QUALIFICATIONS AND DISCLOSURES

1.4.1. I am a Fellow Member of the Actuarial Society of Hong Kong and a Fellow of the Institute and Faculty of Actuaries (United Kingdom) (“UK”), having qualified in 1993.

1.4.2. I am Principal and Consulting Actuary of Milliman Limited, residing of 3901-2, AIA Tower, 183 Electric Road, North Point, Hong Kong (“Milliman”). I have been based in Hong Kong since 1993. I consider my knowledge and experience, which includes the familiarity with the role and responsibilities of an Appointed Actuary in Hong Kong and with the types of long term business written by the Parties involved, as well as my experience with previous Section 24 portfolio transfers, to be suitable and relevant in accepting the appointment as the Independent Actuary for the Scheme.

1.4.3. I am not a shareholder in Zurich Group or any of its subsidiaries. I have no other financial interest in the Zurich Group. Moreover, my compensation related to this appointment is independent of the outcome of the Scheme.

1.4.4. The terms of reference relevant to this report, including general requirements of the Independent Actuary, scope of the work of the Independent Actuary in relation to the Scheme and any prior Hong Kong assignments undertaken for the Parties, are set out in Appendix A.

1.4.5. In preparing the Report, I have taken into account professional guidance under the Institute and Faculty of Actuaries’ “APS X3: The Actuary as an Expert in Legal Proceedings” which sets out principles for actuaries to apply when instructed as an expert in relation to existing or contemplated legal proceedings (including those outside UK jurisdiction).

1.5. RELIANCES

1.5.1. In preparing my report, I have had access to documentary evidence provided by the Parties, the key elements of which are listed in Appendix B. I have also had access to, and discussions with staff and management of the Parties.

1.5.2. In coming to my conclusions, I have relied upon the accuracy of the information which has been provided to me in written or oral form, without independent verification. However, much of this information has been subject to audit or other external scrutiny, and I have had the opportunity to challenge any apparent inconsistencies in the information provided. I have considered, and am satisfied with, the reasonableness of this information based on my own experience of the insurance industry.

1.5.3. I have presented solvency positions of ZLIC under the Swiss Solvency Test basis (the “SST basis”) in Section 6. The results have been produced by the Parties. As the pre-Scheme results of ZLIC are publicly available and have been submitted to the relevant regulatory bodies, and the balance sheet underlying the SST results has been audited, I am satisfied, and have relied on the accuracy of the figures.

1.5.4. The Parties have reported the solvency positions of ZLIC HK branch under HKIO basis to the IA in the past. The Parties have also estimated the solvency positions of ZLIC under the HKIO basis. The results have been subject to internal review. The Parties have also reported the approximated year-end solvency positions of ZLIC under HKIO basis to the IA annually. In the context of my Independent Actuary opinion on the transfer of the Hong Kong portfolio of ZLIC to ZLIHK, I believe the Parties have taken a reasonable approach to estimating the HKIO basis results in order to compare the solvency ratios of ZLIC and ZLIHK.

1.5.5. The Parties have produced the projected solvency positions for ZLIHK after the Scheme is implemented, which have been used for ZLIHK's license application submission to the IA, but with first projection year being updated to reflect the delay of the Transfer Date to 1 September 2021. Details of the financial projections are set out in Section 6.5.11 and Appendix F.

1.5.6. I have not independently reviewed the calculations provided to me and I explicitly rely on the Parties and their Appointed Actuaries and Chief Actuaries that all the calculations used in relation to the Scheme are appropriate and accurate as presented. I have, however, reviewed the methodology and assumptions used in some of the calculations.

1.6. LIMITATIONS

1.6.1. This report has been prepared on the basis as set out in the report and its appendices. It has been written on the basis that it will be utilised by persons technically competent in the areas addressed and with knowledge of the business activities of the Parties and the nature of the risks and rewards inherent in the life insurance business in which they operate.

1.6.2. This report must be considered in its entirety as individual sections, if considered in isolation, may be misleading. Draft versions of this report should not be relied upon for any purpose. A summary of my report ("Summary Report"), approved by me, will be provided to:

- each Transferring Policyholder whose Transferring Policy(ies) is/are in force as at 28 February 2021;
- each Transferring Policyholder whose Transferring Policy(ies) has/have expired, terminated, matured or surrendered as at 28 February 2021 but who has claims or payments outstanding under such policy(ies) or from whom a notice of claim has been received by ZLIC;
- each Transferring Policyholder whose Transferring Policy(ies) has/have lapsed as at 28 February 2021, but such policy(ies) are still capable of being reinstated under a reinstatement option (if any) under the policy(ies) (such reinstatement period being 2 years from the lapse date);
- each Transferring Policyholder whose Transferring Policy(ies) has/have lapsed as at 28 February 2021 due to non-payment of premiums, but as at such date the policy(ies) is/are still providing a post-termination cover (which is the payment of a benefit if death of the insured occurs within 100 days after the lapse date); and
- each long term policyholder of ZLIHK ("ZLIHK Policyholders") whose policies is/are in force as at 28 February 2021 to be in line with Petition

Other than this, no summary of my report may be provided without my express consent.

1.6.3. This report has been prepared by Milliman on an agreed basis for the Parties in the context of the Scheme and must not be relied upon for any other purpose. No liability will be accepted by Milliman, or me, for any application of my report for a purpose for which it was not intended nor for the results of any misunderstanding by any user of any aspect of the report.

1.6.4. The estimated financial positions of the Parties under different solvency bases and as at different future valuation dates presented in this report are meant to be best estimates based on current information. The actual solvency level reported by the Parties on these valuation dates could vary from the estimates shown in this report due to various reasons, but I do not expect the deviations from the estimates shown would be material enough to affect my conclusions in this task.

1.6.5. When forming my conclusion in this report concerning the effect of the Scheme on the Transferring Policyholders and on the Parties, especially on the protection provided to the Transferring Policyholders and safeguards in place under the Scheme, I have considered the Scheme in isolation while there is a chance where the situation could be changed by the Parties as part of the normal management of the business according to the internal governance framework.

1.6.6. When forming my conclusions in this report concerning the effects of the Scheme on the Non-Transferring ZLIC Policyholders that are outside the legal jurisdiction of the Hong Kong SAR, I have explicitly relied upon the professional opinion of the Appointed Actuary and Chief Actuary of ZLIC on the effects of the Scheme on the respective policyholders. While I have relied on this opinion in forming my opinion of the effects of the Scheme on the Non-Transferring ZLIC Policyholders based on my knowledge of ZLIC, I confirm that I have reviewed the approach taken by the Appointed Actuary and Chief Actuary in forming his opinions and consider it reasonable.

1.6.7. Other than as set out below, the report is not meant for use by any third party to do or omit to do anything and no third party should place any reliance on the report for that reason. This report and the opinions and conclusions contained herein are for the internal use of the management of the Parties, their professional advisors, their shareholders, their policyholders, regulators, and in court. With the exception of the limited distribution and disclosure of the report specified in paragraph below, the report and any written or oral information or advice provided by me or Milliman must not be reproduced, distributed or communicated in whole or in part to any other person, or be relied upon by any other person except with the written consent of me and Milliman.

1.6.8. If the Parties wish to release a copy of the report to third parties or advisors, except as provided in the engagement letter dated 22 October 2018 (the “Engagement Letter”) and noted in paragraph 1.6.9 and Section 89, these parties must sign a disclaimer and release letter in the form approved by Milliman setting out the terms under which the information is provided and acknowledging that neither Milliman nor I assume any responsibility, liability or duty of care to them. If the Parties wish to disclose extracts from the report in documents, Milliman and I need to give prior written consent to the proposed wording.

1.6.9. In accordance with Section 24 of the Ordinance Chapter 41, in respect of a sanction for the transfer of Transferring Business, the exceptions referred to above include:

- a copy of the report will be provided to the IA;
- a copy of the report will be available for inspection at the premises in Hong Kong of the Parties concerned for a period of not less than 21 days subsequence publishing a notice in the Gazette and in an approved English language newspaper and an approved Chinese language newspaper in Hong Kong in connection with the Scheme; and
- a copy of the report will be made available to any person asking for one, provided that the request is made prior to an order for sanctioning the Scheme.

1.6.10. The use of Milliman's name, trademarks or service marks, or reference to Milliman directly or indirectly in any media release, public announcement or public disclosure, including in any promotional or marketing materials, websites or business presentations is not authorised without Milliman's prior written consent for each such use or release, which consent shall be given in Milliman's sole discretion.

1.6.11. This report was based on data as at 30 September 2020, which was made available to me and Milliman at, or prior to 29 March 2021, and takes no account of developments after that date. Neither I nor Milliman is under any obligation to update or correct inaccuracies which may become apparent in the report. This report does not provide financial or other advice to individual policyholders.

1.6.12. A supplementary report covering data as at 31 December 2020 will be prepared prior to the final hearings to update the findings and draw any significant developments or changes that may affect policyholders to the attention of the Hong Kong Court.

1.7. LIMITS OF LIABILITY AND LEGAL JURISDICTION

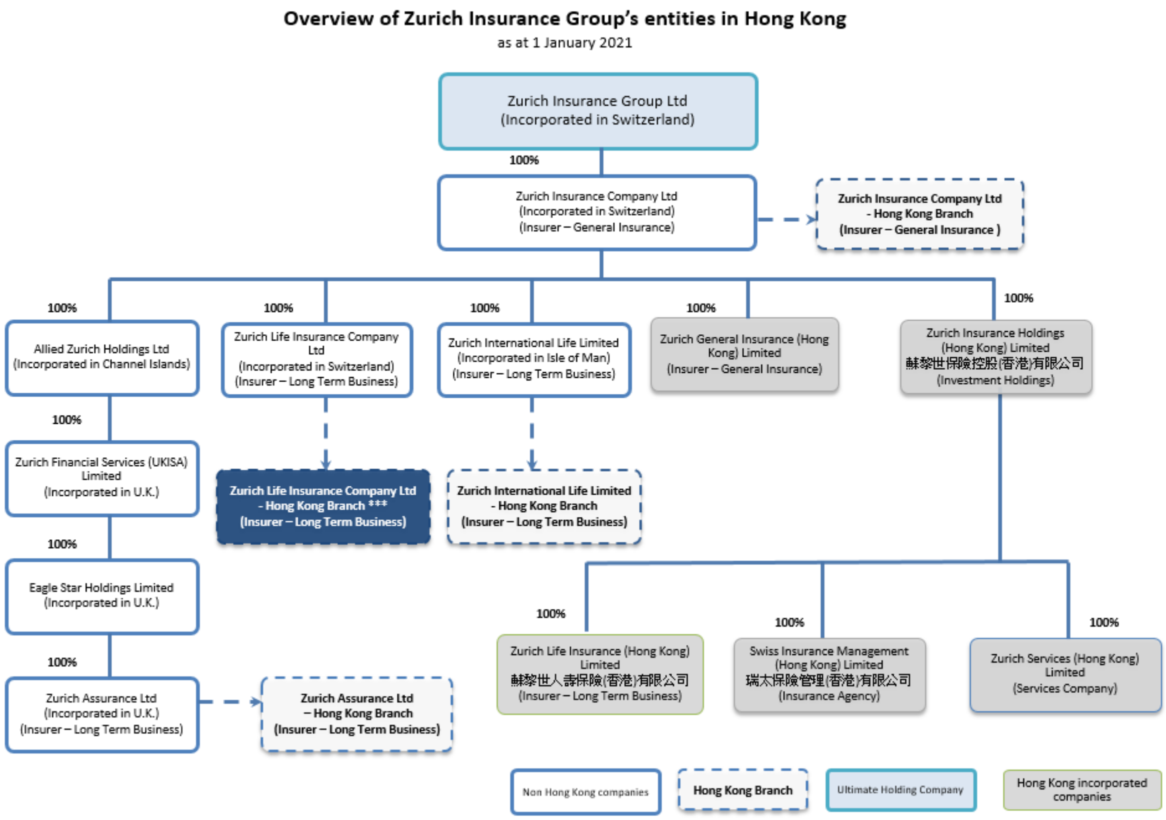
1.7.1. This report is subject to the terms and limitations, including limitation of liability and legal jurisdiction, set out in the Engagement Letter.

Section 2 The Parties to the Scheme

2.1. OVERVIEW

2.1.1. This Scheme was initiated as part of the restructuring of the Hong Kong operations of the Zurich Insurance Group Ltd. ("Zurich Group") to enhance financial stability for policyholders and operating efficiency including facilitating more streamlined audit and regulatory compliance processes across the organisation. The current group structures is shown under Figure 2.1 below. Descriptions of the Parties to the Scheme and key entities involved are provided in this section.

Figure 2.1: Zurich Group before restructuring (simplified)



*** ZLIC HK branch will be removed from the group structure after Portfolio Transfer, upon deauthorisation with the Insurance Authority and deregistration with the Companies Registry.

2.2. ZURICH GROUP

2.2.1. Founded in 1872, the Zurich Group, which is headquartered in Zurich, Switzerland, is a multi-line insurer, providing a wide range of property and casualty, and life insurance products and services in more than 210 countries and territories.

2.2.2. Zurich Insurance Company Ltd. (referred to as "ZIC") is incorporated in Zurich, Switzerland. It is a wholly owned subsidiary of Zurich Insurance Group Ltd. and together with its subsidiaries forms part of the Zurich Group. ZIC and its subsidiaries mainly operate in Europe, North America, Latin America and Asia Pacific through subsidiaries, as well as branch and representative offices.

2.3. ZURICH LIFE INSURANCE COMPANY LTD.

2.3.1. Zurich Life Insurance Company Ltd. is a life insurance company domiciled in Zurich, Switzerland. It operates primarily in Switzerland and through its main branches in Hong Kong, Japan and United Arab Emirates ("UAE"). ZLIC is a wholly-owned subsidiary of ZIC. ZLIC is a life insurance company licensed and supervised by the Swiss Financial Market Supervisory Authority ("FINMA").

2.3.2. ZLIC is a major life insurer in the Swiss market, serving both retail and corporate life and pension (CLP) customers. Retail products include protection and savings products. The CLP business, a.k.a. group business, includes domestic protection and pension solutions.

2.3.3. As at 30 September 2020 the share capital of ZLIC amounted to CHF60 million. It is divided into 600,000 registered shares, each with a nominal value of CHF100. The shares were fully paid-in and held directly by Zurich Insurance Company Ltd.

2.3.4. ZLIC is registered as a non-Hong Kong company under the Companies Ordinance, Chapter 622 of the Laws of Hong Kong (CAP 622).

2.4. HONG KONG BRANCH OF ZURICH LIFE INSURANCE COMPANY LTD.

2.4.1. ZLIC is licensed to carry on life insurance business in Hong Kong through ZLIC HK branch. It was authorised to carry out long term insurance business of Class A (Life and annuity), Class C (Linked), and Class I (Retirement scheme management category III) under Part 2 of Schedule I to the Ordinance in 1984, 2004 and 1996 respectively.

2.4.2. At the end of 2013, ZLIC announced that ZLIC HK branch was closed to new business with immediate effect. After the branch stopped selling new business, the business was placed in run-off. The key in-force products include universal life, protection (such as death, critical illness and medical/hospital expenses), traditional participating and unit-linked. Since 1 December 2016, a note has been inserted in the Register of Authorised Insurers relating to ZLIC, stating that "Zurich Life Insurance Company Ltd. has ceased to effect any new contracts of insurance in or from Hong Kong".

2.4.3. ZLIC HK branch is the entity currently holding the long term insurance business that will be transferred in accordance with the proposed Scheme and the Section 24 of the Ordinance respectively.

2.4.4. Based on the unaudited accounts prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS"), ZLIC HK branch had assets of HKD 5,123 million and total net liabilities of HKD 4,616 million as at 30 September 2020. The net loss for the branch during the period from January 2020 to September 2020 was HKD (207) million, compared to a net loss of HKD (57) million during the full year of 2019.

2.4.5. For Hong Kong tax purposes, ZLIC HK branch has elected to be assessed on a premium tax basis for its Class A (Life and annuity) long term business and Class C (Linked) long term business, therefore the assessable profit is deemed to be 5% on the net premiums written for the year. For Class I (Retirement scheme management category III) long term business, tax is calculated at 16.5% on the assessable profit.

2.5. ZURICH INSURANCE HOLDINGS (HK) LIMITED

2.5.1. Zurich Insurance Holdings (Hong Kong) Limited (“ZIH”) operates as a holding company in Hong Kong and is a direct subsidiary of ZIC. It is proposed to be the parent corporation of the new company, Zurich Life Insurance (Hong Kong) Limited.

2.6. ZURICH LIFE INSURANCE (HONG KONG) LTD.

2.6.1. As part of the aforementioned Zurich Group restructuring of its Hong Kong operations to enhance financial stability for policyholders and operating efficiency including facilitating more streamlined audit and regulatory compliance processes across the organisation, a license application has been submitted on 2 January 2020 to the IA to establish a new subsidiary Hong Kong company called Zurich Life Insurance (Hong Kong) Ltd. ZLIHK became an authorised insurance company under the Insurance Ordinance on 23 March 2020. Following the restructuring, ZLIHK will be a Hong Kong domiciled wholly-owned subsidiary of Zurich Insurance Holdings (HK) Limited (“ZIH”), which in turn is wholly-owned by Zurich Insurance Company Ltd. (“ZIC”). ZIC is fully owned by Zurich Group.

2.6.2. The ZLIHK is the entity into which the long term insurance business of ZLIC HK branch will be transferred in accordance with the proposed Scheme and the Section 24 of the Ordinance.

2.6.3. ZLIHK’s license application and new business process uses a phased approach. During the initial phase, referred to as “First Phase”, ZLIHK has requested approval to underwrite Class A (Life and Annuity) and Class C (Linked) long term business. Under this phase, ZLIHK has started to underwrite Class A business and manage already in-force Class C (Linked) long term business now that it has received license approval. However no new linked business will be underwritten under this initial phase. In the following phase, referred to as the “Second Phase”, ZLIHK will start underwriting Class C business upon obtaining the necessary product approvals from the regulatory bodies. The First Phase has already been completed, while the product approvals for the Second Phase may occur either before or after the Transfer Date.

2.6.4. I have been informed that the ZLIHK will elect taxation on the same basis as elected by ZLIC HK branch, which means to be assessed on a premium tax basis for its Class A (Life and annuity) long term business and Class C (Linked) long term business.

2.6.5. According to the license application business plan submitted to the IA, ZLIHK will source all of its new business from independent financial advisors (“IFAs”).

2.6.6. I have been informed that in the first year of operation, the new business plan is to clone the major products that are being sold through another Hong Kong branch (“ZIL HK branch”) of Zurich International Life Ltd. (“ZIL”), a company incorporated in the Isle of Man.

Section 3 Existing Business and Fund Structures

3.1. ZLIC HK BRANCH

Overview

3.1.1. The ZLIC HK branch is authorised to carry out long term insurance business in Hong Kong.

3.1.2. The ZLIC HK branch is authorised to underwrite long term insurance business of Classes A (Life and annuity), C (Linked) and I (Retirement scheme management category III) under Part 2 of Schedule I to the Ordinance.

3.1.3. As at 30 September 2020, the long term insurance business of ZLIC HK branch consisted of Class A (Life and annuity) and C (Linked) only. The key products of the retail business cover universal life, protection (such as death, critical illness and medical/hospital expenses), traditional participating and unit-linked.

3.1.4. After the Scheme Transfer, ZLIC HK branch will be wound-up and the operating license surrendered. After the completion of the Scheme Transfer, ZLIC HK Branch is expected to withdraw its authorisation in accordance with Section 40 of Insurance Ordinance. There will therefore be no remaining policyholders within ZLIC HK branch once the Scheme is implemented.

Fund structure

3.1.5. The current fund structure used by the ZLIC HK branch to underwrite and administer its insurance business is summarised below:

- ZLIC HK branch long term business fund (pursuant to Section 22(1)(a) of the Ordinance):
  - ZLIC HK branch Life Insurance Fund (Class A);
  - ZLIC HK branch Linked Fund (Class C); and
  - ZLIC Swiss Individual Fund (Class A).

3.1.6. There is fund segregation of assets and liabilities between Class A and C business lines. Within Class A, the Swiss policies are separated from the rest of the Class A insurance fund given that these Swiss policies have a different dividend policy from the other Class A participating products. Similar segregation will be maintained in ZLIHK.

3.1.7. ZLIC HK branch does not have a shareholders' fund. The fund surplus after policy liabilities that are attributed to the shareholders of ZLIC is included in the ZLIC HK branch Life Insurance Fund (Class A) and ZLIC HK branch Linked Fund (Class C). As at 30 September 2020 the fund surplus amounted to around HKD 507 million.

Key statistics – long term business

3.1.8. As at 30 September 2020, there were 39,471 long term insurance policies in-force with the ZLIC HK branch accounting for HKD 4,540 million and HKD 4,246 million of total gross liabilities and total net liabilities respectively.

3.1.9. Liabilities are denominated in Hong Kong dollars (HKD), US dollars (USD), Sterling, Euro, Australia dollars (AUD) or Eagle Currency (minor with a few policies). Eagle Currency represents a basket of currencies consisting of 1 Sterling, 2 US dollars, 500 Japanese yen, and 2.04517 Euro.

3.1.10. The majority of ZLIC HK branch's long term business is non-participating, unit-linked and universal life business in nature, with a smaller proportion of participating business.

3.1.11. The details of the long term insurance business of ZLIC HK branch as at 30 September 2020, including the number of policies and net liabilities are summarised under the table below.

Table 3.1: Long term business of ZLIC HK branch as at 30 September 2020

Class	Number of policies	Amount of net liabilities In HKD million
A	25,725	2,707
C	13,746	1,539
Total	**39,471**	**4,246**

3.2. ZLIHK

Overview

3.2.1. As stated in paragraph 2.6.1, an application was submitted to the IA in 2018 for the authorisation of ZLIHK as a new subsidiary Hong Kong company to carry out the long term insurance business in Hong Kong. With effect from 23 March 2020, ZLIHK is an authorised insurer under the Insurance Ordinance. ZLIHK has started selling new business after receiving its license approval.

3.2.2. In common with the current ZLIC HK branch, the long term insurance business to be underwritten in the ZLIHK will consist of Class A (Life and annuity) and Class C (Linked) but no Class I (Retirement scheme management category III) business. During First Phase, ZLIHK has started to underwrite new Class A business and manage already in-force Class C (Linked) long term business now that it has received license approval. However no new linked business will be underwritten under this initial phase. In Second Phase, ZLIHK will start underwriting Class C business upon obtaining the necessary product approvals from the regulatory bodies.

Fund structure

3.2.3. To incorporate the Transferring Business, ZLIHK will maintain the following fund structure on and after the transfer of long term insurance business from ZLIC HK branch:

- ZLIHK Life Insurance Fund (Class A);
- ZLIHK Swiss Individual Fund (Class A);
- ZLIHK Linked Fund (Class C); and
- ZLIHK Shareholders' Fund.

The ZLIHK Life Insurance Fund (Class A) will combine the Transferring Class A policies (excluding Swiss policies) and new Class A policies of ZLIHK. The ZLIHK Linked Fund (Class C) will combine the Transferring Class C policies and new Class C policies of ZLIHK. I was informed that there is no plan to establish separate sub-funds for Transferring policies.

ZLIHK Life Insurance Fund (Class A)

3.2.4. The fund will consist of the existing ZLIC HK branch's non-linked business (except Swiss individual life portfolio), as well as new non-linked policies issued by ZLIHK.

3.2.5. This fund is intended to cover non-participating and universal life products, as well as some participating policies (other than the Swiss individual life portfolio) which are a relatively small proportion of the Transferring Business. The participating policies (other than the Swiss policies) in the Transferring business will remain in the ZLIHK Life Insurance Fund (Class A), similar to the situation in ZLIC HK pre-transfer. Once there are new Participating products launched in ZLIHK, or the size of liability is large enough to warrant a separate fund for investment management, a Participating business sub-fund will be established.

ZLIHK Swiss Individual Fund (Class A)

3.2.6. This is a closed block set up for the original ZLIC HK Swiss individual life portfolio. The small run-off portfolio of Swiss individual products is entitled to a share of surplus following the Swiss dividend methodology for participating business. These Swiss policies have a different dividend policy from other Hong Kong participating products. To avoid any conflict with dividend policies of other policies, these transferring participating policies will be managed separately from the Life Insurance fund of ZLIHK immediately after the Scheme Transfer.

3.2.7. This portfolio has been included in the ZLIC HK branch Life Insurance Fund (Class A) before the Transfer Date.

ZLIHK Linked Fund (Class C)

3.2.8. The fund will consist of the existing ZLIC HK branch's unit-linked business and new unit-linked policies issued by ZLIHK upon obtaining Class C product approvals from the regulatory bodies in Second Phase.

ZLIHK Shareholders' Fund

3.2.9. The fund will consist of the paid-in capital of ZLIHK, after considering the regulatory requirement of 1/6 solvency margin held in each class of businesses. The ZLIC HK branch fund surplus that is attributed to the shareholders of ZLIC will be apportioned and transferred to the ZLIHK Shareholder's Fund.

3.2.10. The net asset value (or amount of total assets after allowing for the policyholders' future insurance liabilities and other payables) is attributable to the shareholder. For ZLIC HK branch, after considering the regulatory requirement of 1/6 solvency margin held in each class of businesses, the pre-transfer surplus amounted to about HKD 487 million (representing the remaining 5/6 of the solvency capital) based on the unaudited financial account as at 30 September 2020. This amount will be transferred to the ZLIHK Shareholders' Fund after Scheme implementation.

Key statistics – long term business

Existing business of ZLIHK

3.2.11. ZLIHK's license application and new business issue process is a phased approach. During the initial phase, referred to as "First Phase", ZLIHK has requested approval to underwrite Class A (Life and Annuity) and Class C (Linked) long term business. Under this phase, ZLIHK has started to underwrite Class A business and manage already in-force Class C (Linked) long term business now that it has received license approval. However no new linked business will be underwritten under this initial phase. In the following phase, referred to as "Second Phase", ZLIHK will start underwriting Class C business upon obtaining necessary product approvals from the regulatory bodies. The First Phase has already been completed, while the product approvals for the Second Phase may occur either before or after the Transfer Date.

3.2.12. ZLIHK has started issuing new business after receiving its licencing approval from the IA on 23 March 2020. There were 13 in-force Class A term policies as of 30 September 2020. The total gross annualised premiums of these policies was HKD 103 thousand.

ZLIHK's business plan

3.2.13. The ZLIHK license application business plan submitted to the IA has been updated by the Parties to reflect the delay of the Transfer Date to 1 September 2021. The projected gross written premium and insurance liabilities of ZLIHK in 2020-2022 from the updated business plan are illustrated in Figures 3.4 and 3.5 below.

Figure 3.4: Projected gross written premium of ZLIHK (HKD million)

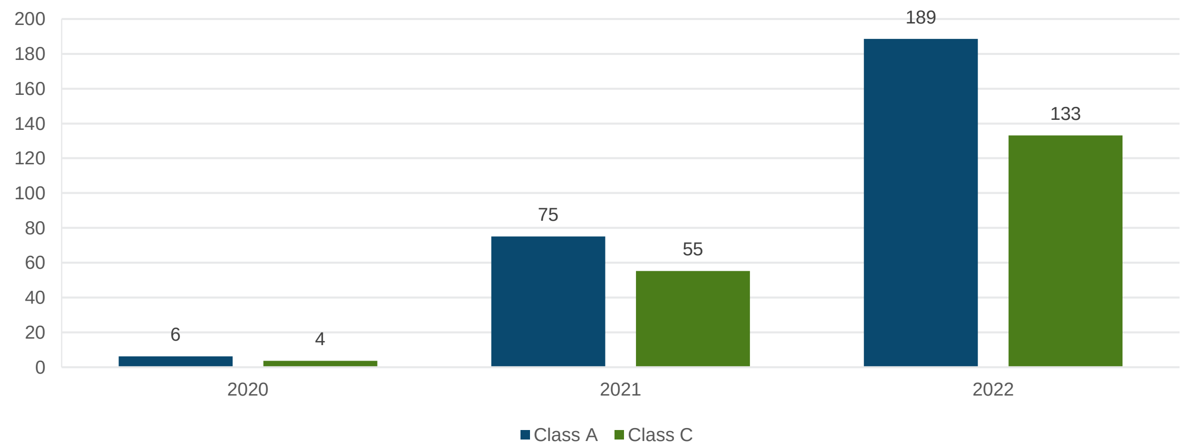
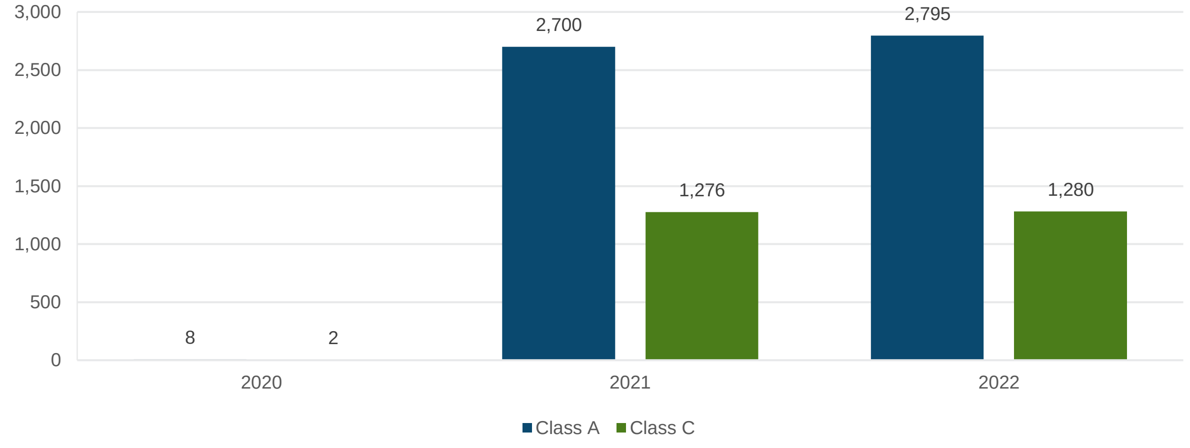


Figure 3.5: Projected insurance liabilities of ZLIHK (HKD million)



Section 4 The Proposed Scheme of Transfer

4.1. PURPOSE

4.1.1. The proposed Scheme is described in the documents produced by the Parties as presented to the Hong Kong Court.

4.1.2. The Parties wish to transfer all the long term business (under the Scheme) of the ZLIC HK branch to the ZLIHK, for the purposes of

- Simplification of ZLIC company structure;
- Consolidation of the Hong Kong life insurance business of ZIC;
- Discontinuance of the license of ZLIC HK branch; and
- Simplification of financial and statutory reporting.

4.1.3. The proposed Scheme involves the transfer of long term business from ZLIC HK branch to ZLIHK.

4.1.4. I have taken into account information provided to me by the Parties, as listed in Appendix B of this report, when considering the proposed Scheme.

4.2. EFFECTIVE DATE OF TRANSFER

4.2.1. Subject to the grants of the order of the Hong Kong Court for the transfer of long term business pursuant to Section 24 of the Ordinance, it is expected that the Scheme will take effect on 1 September 2021 (the "Transfer Date" or the "Effective Date"). The Scheme will take effect at 12:01 a.m. hours (Hong Kong time) on the Effective Date.

4.2.2. On the Effective Date, ZLIC HK branch will transfer all the Transferring Business, all its employees and all other business undertakings under this Scheme to ZLIHK.

4.2.3. ZLIHK will transfer an amount in cash equivalent to the acquisition price for the ZLIC HK branch in-force business (as defined in Section 4.3) to ZLIC as a consideration for the Transferring Business.

4.3. THE TRANSFERRING BUSINESS

Transferring Business

4.3.1. The Scheme defines the "Transferring Business" to be the ZLIC Business, the Transferring Assets and the Remaining Assets (if any), the Transferring Liabilities and the Remaining Liabilities (if any), and the Transferring Records.

4.3.2. The ZLIC Business is defined as the long term business of ZLIC HK branch.

4.3.3. Transferring Records refer to the books and records of ZLIC Business including any books and records relating to underwriting and outstanding claims in respect of the ZLIC Business, any accounting and financial records.

4.3.4. On the date of transfer, ZLIC HK branch will transfer all of its assets and liabilities to ZLIHK. In return, ZLIHK will pay an acquisition price for the ZLIC HK branch in-force business. The price will take reference to the embedded value (including net asset value of the transferring assets and liabilities) of the ZLIC Business as of the quarter end day prior to the Effective Date of transfer. The funding will be provided internally from within the Zurich Group, rather than paid out of ZLIHK's shareholder fund.

Transferring Assets

4.3.5. Transferring Assets refer to all property of ZLIC HK branch including the tax balances / tax recoverable (if any) as defined in Section 5.17. The Transferring Assets include the assets backing the fund withheld balance under the internal reinsurance arrangement (as part of the Transferring Reinsurance). Transferring Reinsurance is defined to be any reinsurance agreements or arrangements in respect of the ZLIC Business.

4.3.6. The Remaining Assets refer to any assets of ZLIC business, which are transferred at a later date than the Transfer Date, known as Subsequent Transfer Date or cannot be transferred to ZLIHK for any reason.

4.3.7. On and with effect from the Transfer Date, the Transferring Assets shall, by virtue of the Hong Kong Order and without any further act or instrument and without investigation or requisition, be transferred by ZLIC HK branch to, and vested in, ZLIHK, subject to any encumbrances in respect thereof.

4.3.8. Under the proposed Scheme, the long term business funds of ZLIHK will be structured to incorporate the Transferring Business of ZLIC HK branch. The subdivision of the funds and allocation of assets and liabilities among the comprising funds are described in paragraphs 4.4.2 to 4.4.6 below.

Transferring Liabilities

4.3.9. Transferring Liabilities mean all liabilities of ZLIC HK branch as at the Transfer Date attributable to the Transferring Business including, without limitation, the liabilities and obligations (whether present, future or contingent) under the Transferring Policies and tax liabilities and tax obligations attributable to ZLIC HK branch.

4.3.10. The Remaining Liabilities refer to any liabilities of ZLIC business, which are transferred at a later date than the Transfer Date, known as Subsequent Transfer Date or cannot be transferred to ZLIHK for any reason.

4.3.11. On and with effect from the Transfer Date, all Transferring Liabilities shall, by virtue of the Hong Kong Order and without any further act or instrument and without investigation or requisition, be transferred by ZLIC HK branch to, and become a liability of ZLIHK, with the effect that ZLIC HK branch shall be entirely released from and ZLIHK shall assume all such Transferring Liabilities.

4.3.12. The following table show the details of the Transferring Business of ZLIC HK branch as at 30 September 2020.

Table 4.1: Long term business of ZLIC HK branch as at 30 September 2020

Class	Number of policies	Total gross sum assured HKD million	Total gross annualised premium HKD million	Amount of net liabilities HKD million
A - life assurance participating	4,431	1,483	50	862
A - life assurance non-participating	21,291	6,825	131	1,838
A – annuities	3	1	0	7
C - linked	13,746	4,552	111	1,539
Total	**39,471**	**12,860**	**292**	**4,246**

4.3.13. As at 30 September 2020, Class A life participating business comprised 4,367 whole of life policies, 46 endowment policies and 18 term policies. Non-participating Class A life assurance business comprised 8,097 endowment policies, 13,191 term policies and 3 refundable plans. Class C business comprised 12,746 whole of life policies and 1,000 endowment policies as at 30 September 2020.

4.3.14. Transferring Policies of ZLIC HK branch are denominated in Hong Kong dollars, US dollars, Sterling, Euro, Australia dollars or Eagle Currency (derived from a basket of major currencies).

4.4. FUND STRUCTURE UNDER THE SCHEME

4.4.1. The fund structure of ZLIHK will be designed to incorporate the Transferring Business of ZLIC HK branch under the proposed Scheme. The subdivision of the funds and the allocation of assets and liabilities among the comprising funds are described in paragraphs 4.4.2 to 4.4.5 below.

4.4.2. There will be three subdivision funds under the long term business fund maintained by ZLIHK and ZLIHK's Shareholders' Fund:

- ZLIHK Life Insurance Fund (Class A), which will consist of the existing ZLIC HK branch non-linked business as well as new non-linked policies issued by ZLIHK;
- ZLIHK Swiss Individual Fund (Class A), which will consist of the existing ZLIC HK branch Swiss individual products; and
- ZLIHK Linked Fund (Class C), which consist of the existing ZLIC HK branch unit-linked business and new unit-linked policies issued by ZLIHK.

4.4.3. The ZLIHK Life Insurance Fund (Class A) is intended to cover non-participating products as well as a small portfolio of participating policies within the Transferring Business. This fund excludes Swiss individual life portfolio. The participating policies (other than the Swiss policies) in the Transferring business will remain in the ZLIHK Life Insurance Fund (Class A), similar to the situation in ZLIC HK pre-transfer. Under the current investment mandate, the equities backing these existing participating policies are managed in a separate portfolio from those of other products, while the fixed income assets are managed with other Class A products of similar duration (to allow for better investment diversification given the small size of the transferring participating portfolio). If material amounts of new participating business is sold by ZLIHK in the future, a new participating business sub-fund will be established.

4.4.4. The small run-off portfolio of Swiss individual products is entitled to surplus shares following the Swiss dividend methodology for participating business. These Swiss policies have a different dividend policy from other Hong Kong participating products. To align the conflicting dividend policies for the transfer, these participating policies will be managed in a separate fund from the Life Insurance fund of ZLIHK immediately after the Scheme.

4.4.5. The current ZLIC HK branch Life Insurance Fund includes the fund surplus that is attributed to the shareholder of ZLIC, as well as the assets backing the insurance liabilities of Class A business. Separately, the current ZLIC HK branch Linked Fund includes the fund surplus that is attributed to the shareholder of ZLIC, as well as the assets backing the insurance liabilities of Class C business. The assets from both funds will be apportioned and transferred to ZLIHK Shareholders' Fund and ZLIHK Life Insurance Fund / ZLIHK Linked Fund, respectively after the Transfer.

4.4.6. The following diagram sets out the proposed change in fund structure under the proposed transfer:

ZLIC HK branch fund structure before transfer

ZLIC HK branch long term business

ZLIC HK branch Life Insurance fund (Class A)	ZLIC HK branch Linked fund (Class C)	ZLIC Swiss Individual fund (Class A)

ZLIHK fund structure before and after transfer

ZLIHK long term business

ZLIHK Life Insurance funds (Class A)	ZLIHK Swiss Individual fund (Class A)	Linked fund (Class C)	ZLIHK Shareholders' Fund

4.5. FUTURE OPERATION

4.5.1. ZLIHK has undertaken to fulfil all of the policy contract conditions once the Scheme is implemented. This will include the responsibility for paying all benefits of claims, maturities, policy dividends and other amounts arising from the Transferring Business including the cost of administration for all Transferring Policies.

4.5.2. The future earnings of the Transferring Business are projected to be positive after considering the cost of administration. The Parties have informed me that the ongoing cost of administration is likely lower than the pre-transfer, given there will be new business written but no major change in the functions and personnels in supporting the future operation of ZLIHK versus the status quo.

4.5.3. In terms of personnel, the Parties have confirmed that there will be no major change in the functions supporting the future operation of ZLIHK.

4.5.4. The Swiss Individual Life Policies, the so-called "Swiss Book", is a minor portfolio issued as early as from 1972 (some 12 years before the ZLIC HK Branch was established). The Swiss Book has been in run-off since 2004. During those early years, ZLIC Switzerland carried on international business by accepting business from local brokers in the Asian market, including Hong Kong. This is a portfolio of ZLIC Switzerland policies bought by expatriates in the Asian region who were expected to be moving back to their respective home countries some time in the future. After the Scheme Transfer, ZLIHK will retain the liabilities for these policies on its balance sheet and cede the risks to ZLIC by reinsurance arrangements, and will outsource to ZLIC such operational activities that ZLIC has been responsible for prior to the Scheme Transfer (including policy servicing, administration, payment of claims for such policies) to minimise potential immediate customer impact. ZLIHK may reassess the arrangement for optimising the longer term administration of the Swiss Book as part of its normal operational review of continuing with the reinsurance and outsourcing arrangement. As of 30 September 2020, there are 142 in-force policies, including 139 Class A life participating business and 3 Class A annuity business.

4.5.5. I have been informed by ZLIC Head Office that the Swiss Book is subject to FINMA regulations, in terms of regulatory reporting as the portfolio has also been included as part of the ZLIC Swiss business. In terms of portfolio transfer approval, I have been advised by the ZLIC Head Office that the Swiss Book is not interpreted as Swiss business subject to FINMA approval for any portfolio transfer, as required under Article 62 of the Swiss Insurance Supervision Act. This advice is based on the fact that the Swiss Book does not contain Swiss residents (determined at time of policy inception). Therefore, while the Swiss Book is subject to FINMA regulation for reporting purpose, I have been informed that its portfolio transfer is not subject to FINMA approval.

4.5.6. In relation to the ZLIC HK branch Swiss individual life portfolio of 142 policies as at 30 September 2020, the Parties have informed me that ZLIC will continue to perform administration, including paying claims and collecting premiums after the Transfer, similar to the current administration arrangement. I have been informed that this is because the portfolio is very small, making system transfer very expensive and non-value adding. Outsourcing and reinsurance arrangements will be put in place to transfer the operation and cash flows of the Swiss individual life portfolio from ZLIHK to ZLIC. In return ZLIHK will place an asset in ZLIC, which covers the liabilities of the reinsured portfolio.

4.5.7. ZLIHK will pay a single premium for this and there will be no further cash settlements after the initial setup of the reinsurance arrangement. It is expected that ZLIHK will pay a single premium of approximately CHF 7 million to fund reserves for this small portfolio of, which the Parties have estimated to be, around 135 as of year end 2020. After the initial establishment of the reinsurance, ZLIHK will only display a reinsurance asset with an equal offsetting direct liability. The intention of the reinsurance agreement is to transfer all the underlying insurance/investment risks, including the administration of the policies, back to ZLIC. Premiums and claims booked for these policies will also be ceded 100% back to ZLIC. The full contractual details of this reinsurance agreement will be agreed closer to the Transfer Date. In summary, the administration of the Swiss individual life portfolio remains the same and there will be no difference in policyholders' benefits before and after transfer. ZLIHK may reassess this arrangement as part of its normal operational review to safeguard the benefit of policyholders.

4.6. COST AND EXPENSES RELATED TO THE SCHEME

4.6.1. The costs associated with the Scheme are to be met by ZLIC shareholders, expensing through the ZLIC HK branch. The costs include those in relation to the preparation of the Scheme and obtaining the sanction of the Hong Kong Court, both incurred before, on and after the Transfer Date. The total costs and expenses incurred are estimated to be USD 1.6 million.

Section 5 Impact of the Proposed Transfer – Effect on the Benefit Expectations of Policyholders

5.1. INTRODUCTION

5.1.1. In this section I consider the major issues relating to the benefit expectations of the Transferring Policyholders. In forming my opinion on this aspect, I have considered the various matters addressed in the following paragraphs.

5.2. CONSIDERATIONS AFFECTING BENEFIT EXPECTATIONS OF POLICYHOLDERS

5.2.1. For non-participating business providing guaranteed benefits for guaranteed premiums, I need solely to consider the likely effects of the Scheme on the financial security of these contractual benefits. This is covered in Section 6 of this report.

5.2.2. For policies with discretionary components, I must also consider the likely effects of the Scheme on how such discretion will be exercised taking into account the current benefit expectations of policyholders. These policies include those with a combination of discretionary and guaranteed benefits such as participating policies. In this report discretionary benefits such as cash dividends, terminal dividends or other bonuses, are referred to as “dividends” or “bonuses”. I will elaborate further on the form of dividends and bonuses policyholders of ZLIC HK branch are paid in the later sections. I also consider policies with other discretionary elements such as unit-linked products with non-guaranteed fees and charges, or traditional products offering non-guaranteed premium structures and conversion rights.

5.3. CLASS A TRADITIONAL PARTICIPATING POLICIES AND UNIVERSAL LIFE POLICIES

5.3.1. In considering the likely effects of the Scheme on Transferring Policyholders’ dividend prospects, I have considered the following areas that could affect the future determination of dividends:

- The approach taken to determining the amounts of policyholder dividends subsequent to the Scheme implementation, and any differences compared with current practices.
- The future governance procedures and safeguards, provided by ZLIHK’s Articles of Association, the Scheme or other supporting documents, that prevent a change of approach that could have an adverse effect on participating policyholder dividends.
- The extent to which future investment strategy, and investment performance, of the assets backing the participating and universal life liabilities may be affected by the Scheme.
- The expenses and underwriting surplus/deficit from claims experience attributable to traditional participating policyholders as a result of the Scheme.

5.4. EXISTING BUSINESS OF ZLIHK BEFORE TRANSFER

5.4.1. ZLIHK has started to underwrite new long term insurance business after receiving its license approval on 23 March 2020. There were 13 in-force Class A term policies as of September 2020, and it is expected that the number of new policies will remain to be small at the time of Scheme implementation.

5.4.2. I have been informed that the plan is for ZLIHK to write non-participating protection products in the initial stage of operation. None of the proposed new products in the license application offer dividends to policyholders.

5.5. EXISTING PARTICIPATING BUSINESS AND UNIVERSAL LIFE BUSINESS OF ZLIC HK BRANCH

Participating business

5.5.1. ZLIC HK branch's participating portfolio was closed to new business in 2013. The participating policies are traditional whole life, endowment, critical illness and term assurance offering guaranteed surrender values, annual cash dividends and terminal dividends. The policies also typically offer a dividend on deposit ("DoD") feature.

5.5.2. The participating business of ZLIC HK branch consists of:

- HK Traditional Annual dividend products – Abundant Life, Simply Life and Leap Savings (all in-force policies were terminated at May 2018)
- HK Traditional Terminal dividend product – Super Protector
- Swiss Individual products – Endowment, Extended term insurance, Deferred annuity, Level term and decreasing term plans

HK Traditional Annual dividend products

5.5.3. This portfolio consists of traditional whole life and endowment policies that were sold between 2009 and 2013.

5.5.4. The policies offer annual cash dividends to policyholders, which can be placed with the ZLIC HK branch as dividend on deposit accumulating interest. There are no terminal dividends for these products.

HK Traditional Terminal dividend product

5.5.5. The product provides traditional whole life protection and accelerated critical illness benefits. It provides non-guaranteed terminal dividends which are payable upon policy termination starting from year 5 on deaths, surrender or maturity.

5.5.6. There is also a multiple-pay CI rider available to policyholders at an extra cost which covers critical illness payment up to three times (including one time from the basic plan).

Swiss Individual products

5.5.7. These are Swiss policies that were underwritten in Hong Kong, before the product line was closed to new business in 2001. The small run-off portfolio consists of endowment, extended term policy and deferred annuity, as well as level term and decreasing term policies. They are entitled to a share of surplus following the Swiss dividend methodology for participating business.

Universal life business

5.5.8. ZLIC HK branch's universal life contracts are referred to as Living products. Premiums are allocated to a notional investment account where interest is credited and mortality/policy charges are deducted.

5.5.9. The amount of interest credited is determined solely based on the investment performance of the underlying invested assets. Profits and losses arising from other sources of variation from expected experience, such as claims, persistency and expenses, are not shared with policyholders.

5.5.10. There is a career-average guarantee on the interest accumulation rate provided at policy maturity or for policies in-force for more than 15 years. The actual crediting rate is determined based on the performance of the underlying investment assets backing the liabilities, allowing for some smoothing mechanism. As the investment assets include some allocation to equity stocks and unit trusts, the actual return can be negative.

5.5.11. There are 3 generations of Living products:

- Old style – Target 21 converted to Single Premium Whole Life Plan
- "2003" series – Platinum Saver, Maxi Living, Smart Living, Golden Retirement, Smart Education Saver, Delight Living, Premier Saver, Prestige Living, Serene Living and Talent Education Saver
- New style – Juvenile 128 (5/10/15 Year), Education Saver and Senior Protector

Old style Living products

5.5.12. These are non-profit products with annual interest being credited at the end of each calendar year based on 90% of distributable investment earnings as prescribed in the policy provisions.

5.5.13. No maturity guarantee or guaranteed accumulation rate are provided under the Single Premium Whole Life Plan as all policies were converted from juvenile policies.

"2003" series Living products

5.5.14. These are non-profit products. Annual interest is credited at the end of each calendar year based on all distributable investment earnings.

5.5.15. There is a guarantee that the weighted average crediting rate over the term to date of withdrawal will be 2.0% per annum. This guarantee applies only if the policy has been in-force for more than 15 years or at policy maturity (when the policy term is less than 15 years). However, there is no interest guarantee over the policy term for juvenile policies upon conversion to the Single Premium Whole Life Plan.

New style Living products

5.5.16. Similarly, these are non-profit products. Annual interest is credited at the end of each calendar year and terminal interest is credited in event of claim or at maturity according to a pre-determined formulae.

5.5.17. The level of guarantee on the weighted average crediting rate over the term to maturity date is set at 2%, except for Juvenile 128 5 Year which has a 1% guarantee rate. However, there is no interest guarantee over the policy term for juvenile policies upon conversion to the Single Premium Whole Life Plan.

5.6. POLICYHOLDER DIVIDEND PHILOSOPHY FOR PARTICIPATING BUSINESS

5.6.1. The Parties have confirmed that, after transfer, ZLIHK will follow the current dividend policy adopted for the Transferring Business and that there will not be any significant change to the existing principles and methods with respect to the participating policies and universal life policies as a result of the Scheme. It is also important to recognise that the management of ZLIHK has the right to alter the principles and methods under the existing dividend or bonus policies in relation to the participating business and universal life business and this right will not change after the Scheme is implemented.

5.6.2. As mentioned in Section 5.5, the participating business of ZLIC HK branch consists of the following products:

- HK Traditional Annual dividend
- HK Traditional Terminal dividend
- Swiss Individual

5.6.3. For the Hong Kong traditional participating business, a comprehensive sharing methodology has been adopted to allocate profit between shareholders and policyholders. The mechanism assesses the sustainability ratio of the discretionary policyholder benefits and shareholder profits with reference to an underlying pool of assets (or asset share). At any time, asset shares are allocated into three components:

- assets required to meet future guaranteed benefits;
- assets required to meet future shareholder profits; and
- assets available to pay future discretionary policyholder benefits.

5.6.4. The sustainability ratio measures the ratio of the asset share to the assets required to meet the three components mentioned above. In the annual dividend review conducted by the Appointed Actuary, a dividend adjustment percentage is proposed to bring the sustainability ratio to 1, subject to further considerations of the management of policyholder's reasonable expectations, smoothing and solvency. A sustainability ratio higher than 1 means a dividend increase could be considered whereas a ratio lower than 1 means future guaranteed liability, dividend outgo and shareholder profit are not supportable. In addition, market performance and competitors' action are also taken into consideration. The profit sharing ratio to policyholders has been set to be at least 70%.

5.6.5. For Swiss individual products, the Swiss participating dividend methodology from FINMA is used. In general, the surplus sharing amounts are credited at each policy anniversary. The profit shares are financed by a surplus fund. The amount of surplus to be allocated to the surplus fund is decided by the management taking the overall result for the year into account. Due to the current low interest rate environment and the high guaranteed interest rates on the Hong Kong portfolio, similar to the previous years, no dividends are being paid out in 2020 and the Appointed Actuary believes this will likely remain in the case for the foreseeable future.

5.6.6. The DoD interest rate is set to be determined with reference to the portfolio earned rate of the participating business.

5.7. CREDITING RATE PHILOSOPHY FOR UNIVERSAL LIFE BUSINESS

5.7.1. The crediting rate strategy for the universal products reflects the effect of actual investment returns earned, with the consideration for the management of policyholder's reasonable expectations, smoothing and guarantees. Bond returns, calculated on an amortised book value basis, are used, while equities are marked-to-market. Other sources of experience variances, such as expenses and claims, are not shared with policyholders.

5.7.2. The investment strategy is 100% bond and cash assets for old style and "2003" series Living products. As a measure of maintaining policyholders' reasonable expectation, ZLIC HK branch aims to regulate any change of crediting rates from one year to the next by not more than 1.5% under normal circumstances. While ZLIC HK branch aims to ensure a smooth progression of annual crediting rates, material changes may apply in unusual or adverse economic environment to protect the financial resources of the life fund. In addition, the gross crediting rate is floored by the management charge so that the net crediting rate is non-negative.

5.7.3. The assets supporting the new style Living products are invested in a mixture of bonds and equity oriented mutual funds. The policy conditions for the new style Living products state that the terminal interest is credited with a rate of return equal to that actually achieved by ZLIC HK branch. The annual interest is regarded as the long term return expected over the term of the policy, such that the recommended annual rate can be higher or lower than the rate based on the actual performance. Any excess or shortfall in the interest credited over the actual return is reflected in the actual investment account via terminal interest.

5.8. HISTORICAL BONUS AND DIVIDEND CHANGES

5.8.1. An annual review of dividend rates for traditional participating products is performed by the Appointed Actuary and approved by the Board. As mentioned in the dividend methodology in Section 5.6, a dividend adjustment percent is proposed to bring the sustainability ratio to 1, subject to other considerations such as competitors' actions. ZLIC HK branch has not made any adjustments to the dividend scales of the participating policies up to the end of 2018. Both of the 2019 and 2020 dividend studies recommended a 40% dividend cut to be made in early 2020 or early 2021. These studies were performed in accordance with the existing principles and methodology set out in ZLIC HK branch's dividend policy of traditional participating products. They were conducted based solely on ZLIC HK branch as an on-going concern without taking into account of factors relating to the Transfer. Although the dividend cut recommendation is totally unaffected by the Transfer, after assessing the reasonable expectations of policyholders and competitors actions, I have been informed that ZLIC HK branch does not intend to make any adjustments to the dividend scales of the participating policies before the Transfer. ZLIHK will make future decisions in this area in the normal course of business during annual dividend investigations after the Transfer. I have been informed that the rationale for not adjusting the dividend scales before 2019 was as follows:

- given the projected small dividend pay-out in early years, the smoothed dividend adjustment of at most 40% cut derived from dividend policy may not bring material financial benefit to the branch, considering the operational cost of dividend adjustment procedure; and
- alignment with competitors' action to maintain the fulfilment ratio for their major products to be close to 100% within the first few policy years.

5.8.2. ZLIHK has undertaken to carry out annual dividend reviews according to the same dividend methodology used by ZLIC HK branch, whereby dividends may need to be adjusted based on the actual surplus or deficit position of the participating portfolio at the time of future review, as well as after taking into other consideration including the materiality of the financial benefits, competitors' actions and other factors not associated with the Transfer. As such, the Transfer is not a factor which will be taken into account in the dividend determination in the future review. I have been informed that, given the internal governance systems in place within ZLIHK and the same management team of Zurich, the dividend mechanism/principles communicated to policyholders will be applied consistently in the future time as prior to the Scheme transfer.

5.8.3. Participating policy dividends (except terminal dividends) are credited annually on policy anniversaries. Policyholders can choose to withdraw the dividends or allow dividends to be left to accumulate with the ZLIC HK branch at non-guaranteed deposit interest rates. Given the small DoD asset size, the deposit interest has been remained the same as per the original product pricing.

5.8.4. For the Swiss individual products, which are managed separately in Switzerland, no dividends are being paid out and the Appointed Actuary believes this will likely remain in the case for the foreseeable future. I have been informed that no dividends have been paid out for these products in the current low interest rate environment as the interest rate guarantees on those products are already high.

5.9. HISTORICAL CREDITING RATES

5.9.1. Universal life crediting rates are reviewed annually. The crediting rates are generally defined in relation to current year investment returns. The historical changes in crediting rates in general reflected the downward movement in the portfolio earned rates, mainly as a result of the low reinvestment yields of bond assets in recent years.

5.9.2. The historical changes in the crediting rate for universal life policies are summarised in the table below.

Table 5.1: Historical crediting rate changes

Year	Education Saver / Senior Protector	Juvenile 128 – 5/10/15	Old Style products	Other Living products
2006	No change	No change	Eagle: increase 35bps Sterling: increase 35bps USD and HKD: reduce 70bps	Sterling: increase 125bps USD and HKD: reduce 45bps AUD: reduce 65bps EUR: increase 110bps
2007	No change	No change	Eagle: reduce 10bps Sterling: reduce 55bps USD and HKD: reduce 50bps	Sterling: reduce 60bps USD and HKD: reduce 55bps AUD: reduce 50bps EUR: reduce 60bps
2008	No change	No change	Eagle: increase 20bps Sterling: increase 150bps USD and HKD: reduce 50bps	Sterling: increase 165bps USD and HKD: reduce 50bps AUD: reduce 55bps EUR: increase 5bps
2009	No change	No change	Eagle: reduce 68bps Sterling: reduce 186bps USD and HKD: reduce 24bps	Sterling: reduce 208bps USD and HKD: reduce 29bps AUD: increase 5bps EUR: reduce 99bps

Year	Education Saver / Senior Protector	Juvenile 128 – 5/10/15	Old Style products	Other Living products
2010	Reduce 25bps prevailing crediting rates	No change	Eagle: reduce 84bps Sterling: reduce 147bps USD and HKD: reduce 4bps	Sterling: reduce 150bps USD and HKD: reduce 4bps AUD: increase 60bps EUR: reduce 150bps
2011	Reduce 25bps prevailing crediting rates	No change	Eagle: reduce 58bps Sterling: reduce 33bps USD and HKD: reduce 65bps	Sterling: reduce 50bps USD and HKD: reduce 73bps AUD: reduce 25bps EUR: reduce 150bps
2012	Reduce 25bps prevailing crediting rates	No change	Eagle: reduce 38bps Sterling: reduce 122bps USD and HKD: reduce 51bps	Sterling: reduce 135bps USD and HKD: reduce 57bps AUD: reduce 45bps EUR: reduce 75bps
2013	No change	No change	Eagle: reduce 61bps Sterling: reduce 109bps USD and HKD: reduce 56bps	Sterling: reduce 122bps USD and HKD: reduce 62bps AUD: reduce 122bps EUR: reduce 150bps
2014	Reduce 25bps prevailing crediting rates	No change	Eagle: reduce 4bps Sterling: increase 14bps USD and HKD: increase 25bps	Sterling: increase 16bps USD and HKD: increase 27bps AUD: reduce 90bps EUR: reduce 121bps
2015	Reduce 25bps prevailing crediting rates	No change	Eagle: reduce 4bps Sterling: increase 3bps USD and HKD: increase 29bps	Sterling: increase 4bps USD and HKD: increase 33bps AUD: reduce 2bps EUR: no change
2016	No change	No change	Eagle: no change Sterling: reduce 4bps USD and HKD: increase 27bps	Sterling: reduce 5bps USD and HKD: increase 30bps AUD: reduce 6bps EUR: no change
2017	No change	No change	Eagle: reduce 1bps Sterling: reduce 1bps USD and HKD: increase 18bps	Sterling: reduce 1bps USD and HKD: increase 20bps AUD: reduce 8bps EUR: no change
2018	No change	No change	Eagle: increase 3bps Sterling: no change USD and HKD: increase 14bps	Sterling: no change USD and HKD: increase 15bps AUD: reduce 6bps EUR: no change
2019	No change	No change	Eagle: increase 5bps Sterling: reduce 8 bps USD and HKD: increase 9bps	Sterling: reduce 9bps USD and HKD: increase 10bps AUD: reduce 15bps EUR: no change

5.10. ASSET ALLOCATION

5.10.1. The table below summarises the target asset allocation stated in the latest Investment Management policy of the ZLIC HK branch.

Table 5.2: Target asset allocation of ZLIC HK branch

		Strategic Asset Allocation (SAA)		
Asset Class	**Asset Type**	**Lower**	**Target**	**Upper**
Cash	Cash	0%	4%	9%
Equities	Shareholder	0%	2%	4%
	Policyholder	0%	1%	5%
Fixed income	Government	30%	35%	55%
	Credit	48%	57%	67%
Policyholders' loan		0%	1%	2%
Total			**100%**	

5.10.2. The majority of the asset portfolio is invested in USD and HKD denominated securities or cash, while less than 4% of the holdings are in AUD/EUR/GBP to support the corresponding liabilities. The Parties have confirmed that there is no significant change of SAA in related to the legacy liabilities of ZLIC HK branch after the Scheme is implemented if there is no significant change in ZLIHK's product mix.

5.11. INVESTMENT POLICY

5.11.1. The ZLIC HK branch has established formal investment policies as below.

Statutory Fund	Business lines	Investment Policies / Mandate applicable
Life Insurance fund	Traditional Participating policies, Universal Life policies, Other Protection products	Zurich Life Insurance Company Ltd., HK branch – Credit Mandate Zurich Life Insurance Company Ltd., HK branch – Government Mandate

5.11.2. Investment activities within the ZLIC HK branch are governed by investment mandates, which are approved by the Asset Liability Management Investment Committee ("ALMIC"). The extract of the "Market Risk Report, Investment Management" and the ALMIC charter set out the ZLIC HK branch's SAA, investment constraints and approval processes of each investment policy.

5.11.3. The majority of fixed income portfolios are managed by external asset managers, whose services are bounded by Investment Management Agreement. Equity investments and cash are managed internally by Investment Management Hong Kong.

5.11.4. Where assets underlying ZLIC HK branch's business are currently under the management of external financial institutions or external investment managers, such investment agreements will be transferred from ZLIC HK branch to ZLIHK under the same terms after the proposed transfer. While the financial institutions will retain the rights to review the respective asset allocation and investment decisions within the context of the investment policies, which were set by ZLIC HK branch before the Transfer Date and will be adopted by ZLIHK thereafter, such rights exist whether or not the Scheme proceeds, and will not be affected by the Scheme.

5.11.5. The Investment Risk Policy Manual also contains the control requirement related to investment overall as well as reporting requirements.

5.11.6. The Parties have confirmed that there is no intention to make significant change to the existing investment strategies and internal governance currently adopted by ZLIC HK branch for the assets supporting the Transferring Policies after the Scheme is implemented.

5.12. OVERALL COMMENTS

5.12.1. In light of my review, it is my opinion that current participating business dividend setting and universal life crediting rate principles and methodologies, and the governance for any changes to the existing approach, which are intended to be used by ZLIHK after the transfer, provide sufficient safeguard that policyholders should expect to be treated in a similar manner before and after the Scheme is implemented.

5.13. CHARGES AND INVESTMENTS OF UNIT-LINKED POLICIES

5.13.1. For the existing unit-linked products, while ZLIC HK branch has not made adjustments on the policy charges in the past, ZLIC HK branch has broad rights to vary policy charges, as well as the right to impose any other charges for administering the policies.

5.13.2. The charging structure of ZLIC HK branch's unit-linked products include monthly charges such as annual management charges, policy administration charges, allocation/setup charges, bid offer spreads, surrender charges, and benefit charges. Policyholders will be given written notice in advance according to policy provisions before any changes come into effect. These rights will continue with ZLIHK and exist whether or not the Scheme proceeds.

5.13.3. I have been informed that the process and principles involved in determining the level of non-guaranteed charges following Scheme implementation will not change as a result of the transfer.

5.14. CONTRACTUAL BENEFITS PROVISIONS

5.14.1. According to the Scheme, ZLIHK shall be bound by, observe and perform all terms, conditions and covenants of the Transferring Policies, assume all liabilities and satisfy all claims and demands arising out of or in respect of the Transferring Policies in every way as if ZLIHK has issued the policies. Therefore, ZLIHK will commit to continue paying the contractual benefits of the Transferring Policyholders of the ZLIC HK branch.

5.14.2. I am aware that the contractual benefits (options and guarantees) embedded in the Transferring Policies, in addition to the guaranteed cash value include:

- Guaranteed accumulation rate for Living products
- Guaranteed insurability option (cash and cover option) for Living products where the clients can take up a new non-profit whole of life policy without cash value, without evidence of insurability, with death benefit sum assured equal to the Guaranteed Sum Insured immediately prior to substitution
- Capital guarantee for eligible unit-linked policies, where the capital in the specific US dollar funds under the investment choices, after all related fees and charges are deducted, is guaranteed.
- Various guaranteed specific bonus for products including Talent Education Saver/Smart Education Saver, Delight Living, Brilliant Link, Deluxe Link, Deluxe Link Junior, Royal Link, Maxi Link, Treasure Link.
- Guaranteed insurability option (convertible option) for Term Plan and Life Insurance to Age 86 where the clients can take up a new policy, without evidence of insurability, with sum assured does not exceed the original amount immediately prior to substitution.
- Guaranteed coupon for Abundant Life at the fifth policy anniversary and every five years thereafter.
- Guaranteed survival benefits for Age 86 term plan, Extra Care 100 plan L, Supreme Care and Whole Life Hospital Cash.

5.14.3. I have been informed that these guaranteed benefits will not be altered after the transfer. The rights of policyholders, as defined under their existing policy documents, will be the same before and after the Scheme is implemented.

5.15. OTHER POLICIES SUBJECT TO COMPANY DISCRETION

5.15.1. For some of the packaged plans and many of the rider policies, including renewable term, accident and health benefits, dread disease benefits, ZLIC HK branch has broad rights to adjust premium rates either at each renewal, at each policy anniversary, at every 5 years or at any of the policy anniversary, as set out in the policy provisions. According to the Scheme, in accepting the Transferring Business, ZLIHK will retain the same rights with respect to these policies. However, these rights exist whether or not the Scheme proceeds and I have no reason to believe the Scheme will lead to a materially adverse exercise of discretion in relation to the Transferring Policyholders of the ZLIC HK branch.

5.16. COSTS AND EXPENSES IN RELATION TO THE SCHEME

5.16.1. The total cost incurred as a result of the Scheme is estimated to be USD 1.6 million. The costs are planned to be covered by ZLIC shareholders, expensing through the ZLIC HK branch. The Parties have confirmed that the costs and expenses incurred in relation to the Scheme are not expected to lead to an increase in the unit costs charged to policyholders or a decrease in the policyholder dividend levels paid.

5.16.2. Therefore, I have no reason to believe there will be a materially adverse impact on the Transferring Policyholders of ZLIC HK branch in this regard.

5.17. TAX IMPLICATIONS

5.17.1. ZLIC HK branch has been calculating its tax liability based on its total assessable profits, at the prescribed tax rate for Hong Kong profit tax of 16.5%. Assessable profit of the Class A (Life and annuity) long term business and Class C (Linked) long term business is assumed to be 5% of the net premiums written for the year. For Class I (Retirement scheme management category III) long term business, tax is calculated at 16.5% on the assessable profit. Based on the draft profit tax computations for year of assessment 2019/20 and provisional tax for 2020/21 submitted to the Hong Kong Inland Revenue Department, the total payable tax for ZLIC HK branch is estimated to be HKD 1,327,000.

5.17.2. The Parties have advised me that there is no requirement in HK Inland Revenue Ordinance that prohibits the transfer of tax asset or tax liabilities on the books of a company. However, the Inland Revenue Department would still request the settlement of tax liabilities from or issue tax refund to ZLIC after a transfer of tax assets or liabilities to ZLIHK and hence there will be implications on the accounts of ZLIC and ZLIHK.

5.17.3. The tax regime applied to the Transferring Business will remain unchanged after the Scheme is implemented. Therefore, I have no reason to believe there will be a materially adverse impact on the Transferring Policyholders of ZLIC HK branch in this regard.

5.18. POLICY TERMS AND CONDITIONS

5.18.1. I am informed that, other than the replacement of references to ZLIC HK branch to ZLIHK, there will be no change to the policy terms and conditions of in-force insurance policies as a result of the Scheme. The provision of policy loan being part of the policy terms and conditions will remain unchanged after the transfer. I have no reason to believe there will be a materially adverse impact on the policy terms and conditions of Transferring Policyholders due to the Scheme itself in this regard.

5.19. CONCLUSION

5.19.1. In summary of my assessments above, I consider that the Scheme will not have a materially adverse effect on the reasonable benefit expectations of the Transferring Policyholders of ZLIC HK branch, which include the policyholders of Swiss individual products.

Section 6 Impact of The Proposed Transfer – Effect on the Financial Security of Policyholders

6.1. INTRODUCTION

6.1.1. In this section I consider the main issues relating to the financial security of the Transferring Policyholders of the ZLIC HK branch, and whether there might be any detrimental impact to the security of ZLIHK's new policyholders after Scheme implementation. In arriving at my opinion, I have considered the issues covered in the paragraphs below.

6.2. CONSIDERATIONS AFFECTING FINANCIAL SECURITY OF POLICYHOLDERS

6.2.1. The security of the contractual benefits of policyholders can be measured by the excess assets in the long term insurance business fund plus the net shareholder assets. It is affected by the conservatism of the reserving bases used and the capital and free reserves, together with additional security provided by the entity as a whole, and any potential support available from its shareholders.

6.2.2. I also need to consider the expected overall solvency position of ZLIHK following implementation of the proposed Scheme and its possible future development.

6.2.3. Any additional policyholder protection rules offered by regulations before and after the Transfer also need to be considered.

6.3. THE PROVISION OF FINANCIAL SECURITY

6.3.1. To protect the security of policyholders, insurance companies maintain three asset layers namely policy reserves, minimum solvency margin and excess assets, with the first two layers required by legislation.

- Policy reserves: Assets supporting the policy liabilities calculated according to the underlying contractual obligations using valuation standards prescribed by statutory rules.
- Minimum solvency margin: Assets required to fulfil the minimum statutory solvency requirements, serving as a margin relating to the risks of liabilities underwritten by insurers.
- Excess assets: Assets that are over and above the statutory minimum solvency margin, which can be expressed as a percentage of the required minimum solvency margin.

6.4. POLICY RESERVES

6.4.1. ZLIC HK branch has been reporting under the Hong Kong regulatory regime, with the Appointed Actuary and the auditor certifying compliance with the Hong Kong Insurance Ordinance (CAP 41).

6.4.2. In accordance with the required valuation standards, ZLIC HK branch has previously set up reserves for the Transferring Business using established methods and valuation bases that satisfy the Hong Kong regulatory standards (with reference to the Ordinance and Actuarial Guidance Notes issued by the Actuarial Society of Hong Kong, "Actuarial Guidance Notes").

6.4.3. I have not independently reviewed the reserve calculations of the Parties. I explicitly rely on the Appointed Actuary and management of both Parties that the reserves are appropriate with respect to regulatory compliance and accurate as presented. The Appointed Actuary and the auditor of the Parties, PricewaterhouseCoopers ("PWC") have both certified compliance with Hong Kong Insurance Ordinance (CAP 41E-Insurance (Determination of Long Term Liabilities) Rules).

6.4.4. In the statutory valuation reporting process, the current procedure is that each year, the Appointed Actuary of ZLIC HK branch, as the advisor to the ZLIC's Board of Directors, proposes the valuation methods and a set of valuation assumptions.

6.4.5. After the Scheme is implemented, the procedures will remain the same such that each year the Appointed Actuary of ZLIHK will advise on the reserving methods and valuation bases of the Transferring Business, as well as the new policies of ZLIHK's business, to the ZLIHK Board of Directors. As no changes in procedure in determining the valuation methodology and assumptions have been proposed if the Scheme is implemented, I do not believe there will be an adverse impact on the financial security of the Transferring Policyholders in this regard.

6.5. SOLVENCY POSITIONS

6.5.1. Solvency margins are currently maintained by ZLIC HK branch, in addition to the policy reserves in respect of the in-force business. The table below displays the historical solvency positions based on the audited accounts. Net assets are defined as the amount of total assets in excess of total liabilities. Solvency margin refers to the Hong Kong statutory minimum solvency requirement and solvency ratio measures the shareholder assets as a proportion of the minimum solvency requirement.

6.5.2. The outstanding letter of credit, which was supplied by UBS, has been cancelled effective 27 June 2018 and the Parties have confirmed that there is no replacement letter of credit and other sort of financing in place or planned for ZLIC HK branch. Capital repatriations of HKD 100 million and 70 million have been made from ZLIC HK branch to its parent company in November 2018 and November 2019 respectively.

Table 6.1: ZLIC HK branch's solvency ratios (on HKIO basis)

HKD million	Dec 2017	Dec 2018	Dec 2019	Sep 2020
Solvency margin	103	102	106	121
Net assets	945	498	556	507
Letter of Credit (LoC)	40	0	0	0
Solvency ratio (Including LoC)*	**956%**	**489%**	**523%**	**420%**

* Figures derived from this table may not be the same due to rounding.

6.5.3. There is a significant drop in the actual solvency ratio in 2018 to the level of 489% as shown in Table 6.1. The Parties have explained that this is due to “Ischia Project”, involving the moving of all the business in Swiss Group block to another business unit in Isle of Man in 2017, i.e. ZIL HK branch. The group business was renewed in the Isle of Man's balance sheet rather than renewing in the ZLIC HK branch. The reduction in the solvency ratio was caused by the Transfer of around HKD 500 million of surplus allocated to this block of group business to ZIL HK branch. The available capital held for this group business was not transferred out until 2018, resulting in a high solvency ratio in 2017 and a subsequent decrease in total available capital and solvency ratio in 2018.

6.5.4. ZLIC, the parent company of ZLIC HK branch, is incorporated in Switzerland in which the solvency is subject to Swiss Solvency Test (SST) framework for determining the risk based capital. The historical solvency position of ZLIC on the SST basis is shown in below.

Table 6.2: ZLIC’s solvency ratios (on SST basis)

CHF millions	Dec 2017	Dec 2018	Dec 2019	Sep 2020**
Target capital	2,858	3,286	4,524	4,601
Risk-bearing capital	5,989	7,002	7,635	7,749
Market value margin	778	820	1,409	1,453
Solvency ratio*	**251%**	**251%**	**200%**	**200%**

* Figures derived from this table may not be the same due to rounding.

** The number is not required by FINMA. It has not been reviewed by FINMA and is an estimate by ZLIC. Currently only the SST as at 1 Jan 2020 or Dec 2019 is relevant for FINMA.

Source: ZLIC internal non-public information for the estimated SST figures as at September 2020.

6.5.5. ZLIC HK branch has estimated the solvency position of the entire ZLIC legal entity under HKIO basis for the purpose of this transfer. As the HKIO reserving is very similar to the old Swiss Solvency 1 reserving, the Swiss Solvency 1 reserve was used as an approximation of the HKIO reserve in the application of the Insurance (Margin of Solvency) Rules. The calculations have been carried out using public information including local statutory reserves, sum assured and premium of ZLIC. The historical approximated solvency position of ZLIC on the HKIO basis is shown in below.

Table 6.3: ZLIC’s solvency ratios (on HKIO basis)

CHF million	Dec 2017	Dec 2018	Dec 2019	Sep 2020**
Solvency margin	960	990	1,019	1,011
Net assets	3,505	3,122	3,609	3,436
Solvency ratio*	**365%**	**315%**	**354%**	**340%**

* Figures derived from this table may not be the same due to rounding.

** Derived based on ZLIC internal non-public information.

6.5.6. ZIC the ultimate parent of ZLIHK, the holding company for is also the parent of ZLIC. ZIC, similar to ZLIC is incorporated in Switzerland in which the solvency is subject to SST framework for determining the risk based capital. The historical solvency position of ZLIC on the SST basis is shown in below.

Table 6.4: ZIC's solvency ratios (on SST basis)

CHF millions	Dec 2017	Dec 2018	Dec 2019**
Target capital	24,573	22,280	24,687
Risk-bearing capital	43,181	41,628	45,961
Solvency ratio*	**212%**	**225%**	**241%**

* Figures derived from this table may not be the same due to rounding.

**No updated information available after December 2019 as ZIC's solvency ratio is only calculated annually.

Source: ZIC's 2018 and 2019 Financial Condition Report.

6.5.7. The Parties have also assessed projected solvency position of ZLIHK before and after the Transfer Date which have been considered to assess the impact of the Scheme.

Table 6.5: ZLIHK's solvency position (on HKIO basis) as at 1 September 2021

HKD million	Pre-transfer	Transfer	Post-transfer
Solvency margin	4	111	115
Net assets	152	582	734
Solvency ratio *	**3779%**	**523%**	**637%**

* Figures derived from this table may not be the same due to rounding.

Table 6.6: ZLIHK's projected solvency ratios (on HKIO basis)

HKD million	1 Jan 2021(*)	1 Jan 2022	1 Jan 2023
Solvency margin	2	119	127
Net assets	204	721	675
Solvency ratio**	**9438%**	**604%**	**533%**

* Solvency ratio at 1 Jan 2021 is the solvency position before the Transfer Date.

** Figures derived from this table may not be the same due to rounding.

6.5.8. The Parties have confirmed that ZLIHK's paid-in capital has been invested in short term fixed deposits which have been unaffected by the capital market volatility resulting from the COVID-19 pandemic.

6.5.9. I have been informed by the Parties that if ZLIHK's solvency ratio is below 200%, or if it is anticipated that ZLIHK's solvency ratio will likely fall below 200% measured on the local statutory basis, it will seek assistance from Zurich Group to raise solvency capital or for a capital injection from ZIC via ZIH, the shareholders of ZLIHK, to meet the target solvency ratio.

6.5.10. I have compared the historical solvency position of the ZLIC being parent of ZLIC HK against the historical solvency position of the ultimate parent of ZLIHK, which is ZIC. As observed from Table 6.2 and Table 6.4, the solvency positions of both of the entities are similar, which are in the range of 200% to 250% for the 2017 to September 2020, implying the financial strength of both entities have been comparable.

6.5.11. I have also focused on the comparison of the projected solvency position of the ZLIHK after the Scheme is implemented against the current solvency position of ZLIC under HKIO basis, since the results under SST basis are not available for ZLIHK. As observed from Table 6.3 and Table 6.6, the estimated solvency ratio of ZLIHK post-Scheme is higher than the current solvency ratio of ZLIC under HKIO basis, which is positive for the financial security of the Transferring Policyholders.

6.6. DYNAMIC SOLVENCY TESTING

6.6.1. In addition, there have been projections which examine the solvency positions of ZLIC HK branch before the proposed transfer and ZLIHK after the proposed transfer under a number of possible adverse scenarios. These are Dynamic Solvency Testing ("DST") calculations conducted as prescribed under the Guidance Note issued by the Actuarial Society of Hong Kong and required by the IA, with the aim to project the likely solvency of the company under a range of adverse scenarios in the near future.

6.6.2. I have been provided with these DST results for ZLIC HK branch as standalone entity and ZLIHK post-Scheme implementation. A summary of the DST results is shown in Appendix E. I have considered these results to assess the impact of the Scheme and the highlights include.

6.6.3. The results of these projections for ZLIC HK branch standalone before the Transfer and ZLIHK after the Transfer show that the solvency of ZLIHK to be comfortably above acceptable solvency requirements being 200% of the Hong Kong statutory minimum solvency requirement. While the actual solvency ratios are likely to vary over time as actual operating experience reveals, in any event the ZLIHK Appointed Actuary has the responsibility under prescribed regulations to ensure that the statutory minimum capital requirements are fulfilled.

6.7. OVERALL FINANCIAL POSITION AND SHAREHOLDERS' CAPITAL

6.7.1. The overall financial security of the Transferring Policyholders of ZLIC HK branch does not only depend on the amount of statutory reserves and minimum solvency requirements, but also on the level of free assets and any additional shareholder support. As mentioned earlier, the letter of credit that was in place with UBS has been cancelled effective 27 June 2018 and no other financing support has been put in place to replace it. Capital repatriations of HKD 100 million and 70 million have been made from ZLIC HK branch to ZLIC in November 2018 and November 2019, respectively.

6.8. CAPITALISATION POLICY

6.8.1. The Parties have stated that ZLIC HK branch has established an internal target solvency ratio range of 200% - 250% over many years and shareholder dividends are considered when free assets exceed this level to a material degree. The IA has required ZLIC HK branch to monitor its solvency position on a weekly basis and to retain the solvency capital in excess of the 200% of minimum solvency requirement, however the IA approval is not required in the capital repatriation for the branch. To ensure a buffer is retained, ZLIC HK will retain local capital between 200% and 250% of the minimum solvency requirement. In addition, since the capital requirement of ZLIC is also subject to the supervision of FINMA, the upper range is reinforced as the target solvency level.

6.8.2. If ZLIC HK's solvency ratio is below 200%, the branch will seek assistance from Zurich Group to raise solvency capital or a capital injection from ZLIC.

6.8.3. I have been informed that following the transfer, the intention is to manage ZLIHK's solvency ratio at the internal target of 225% using a similar approach. This is in line with the Zurich Group risk policy that it holds capital equivalent to the statutory minimum in the local regulated entity plus an adequate agreed buffer to allow for short-term volatility Zurich Group endeavours to manage its internal physical capital such that all its regulated entities are adequately capitalised in compliance with the relevant regulatory capital adequacy requirements.

6.8.4. If ZLIHK's solvency ratio is below 200%, or if it is anticipated that ZLIHK's solvency ratio will likely fall below 200% measured on the local statutory basis, it will seek assistance from Zurich Group to raise solvency capital or for a capital injection from ZIC via ZIH, the shareholders of ZLIHK, to meet the target solvency ratio.

6.9. RISK EXPOSURES

6.9.1. In accordance with the ZLIHK's plan, a new term product was launched in Q3 2020 after receiving license approval from the IA on 23 March 2020. ZLIHK plans to continue writing non-participating protection business in the initial stage of operation towards early 2021. In terms of insurance risks, ZLIC HK branch currently has more lines of business than the ZLIHK before the Scheme Transfer. The various classes of business are considered as listed below.

6.9.2. Both Parties write individual life businesses belonging to Class A under the Ordinance classification. ZLIC HK branch has underwritten participating business and universal life products offering minimum guarantees which pose greater investment risks than the non-participating protection products, due to higher asset allocation in equity stocks and unit trusts. Interest rate risk is of particular relevance to ZLIC HK branch, due to the characteristics of life insurance liabilities made up of limited-pay policies which results in asset liability mismatching. The interest rate sensitivity of the asset instruments is regularly reviewed as part of Asset Liability Management ("ALM") analysis in the local ALMIC. After the transfer, ZLIHK will follow the established formal investment policies of ZLIC HK, while the investment activities are governed by the similar investment mandates. This covers other categories of risks including credit risk, liquidity risk and currency mismatch risk.

6.9.3. ZLIHK has started selling business after receiving its license approval on 23 March 2020. Only 13 new policies have been underwritten so far, and it is expected that the number of new policies will remain to be small at the time of Scheme implementation, and therefore the risk profile of ZLIHK is expected to be similar to the risk profile of ZLIC HK branch.

6.9.4. Class C, unit-linked funds are currently offered by ZLIC HK branch and are planned to be offered by ZLIHK as well. As majority of the investment risks are passed to the policyholder in the underlying investment funds for these products, the risk profile is expected to be similar with or without the transfer.

6.9.5. ZLIC HK branch had no Class I group insurance policies in-force since the end of 2017.

6.9.6. ZLIC HK branch has had reinsurance arrangements in place for its Class A business and Class C business and such arrangements will continue after the transfer. This provides an additional security.

6.9.7. Both ZLIC HK branch and ZLIHK are required to meet the Zurich Risk Policy.

6.9.8. Based on the above considerations, I have not identified any areas where additional risk exposure resulting from the Scheme implementation is likely to prejudice the contractual entitlements of any group of policyholders.

6.10. INVESTMENT POLICY

6.10.1. Investment activities within ZLIC HK branch are governed by investment mandates, which are approved by the ALMIC. The mandate set out the strategic asset allocation, investment constraints and approval processes. The same investment team of ZLIC HK branch will support ZLIHK.

6.10.2. The Parties have confirmed that there is no intention to make significant change to the existing investment strategies currently adopted by ZLIC HK branch for the assets supporting the Transferring Policies after the proposed transfer.

6.11. CURRENCY RISK HEDGING

6.11.1. Since early 2018, ZLIC HK branch has used currency forward exclusively for the currency risk hedging purpose.

6.11.2. Short-term HKD USD currency forwards, with maturity of 3 months are used. These are employed to mitigate the minimal exchange rate variances arising from the USD bond assets that are invested for backing the HKD denominated liabilities, due to the lack of liquid fixed income securities with maturities sufficient to match the HKD insurance liabilities.

6.11.3. As at 30 September 2020, the hedged notional amount was HKD 286.4 million.

6.12. SHAREHOLDERS' FUND AND POLICY ON SHAREHOLDER DIVIDENDS

6.12.1. Hong Kong regulation requires insurance companies to have adequate capital resources to meet local statutory solvency requirement. The IA asks that all life insurers operating in Hong Kong maintain a solvency ratio of at least 150% on a Hong Kong basis to fulfil local regulatory requirement.

6.12.2. Hong Kong regulatory requirements have restricted that the transfer of surplus capital is allowed only if the net asset value after remittance is still in excess of the minimum required solvency margin, without jeopardising the capital adequacy position in near future.

6.12.3. ZLIC HK branch's individual business has established a target range of solvency ratio of 200% - 250%. Repatriation will be proposed with the solvency ratio in excess of this target solvency ratio without adversely affected the future branch's capital adequacy position. ZLIHK will adopt the similar approach at the internal target solvency ratio of 225%. This is in line with the principle of Zurich Group risk policy that it holds capital equivalent to the statutory minimum in the local regulated entity plus an adequate agreed buffer with the excess capital held at the group level to satisfy Zurich Group capital requirement.

6.12.4. I have been informed by the Parties that if ZLIC HK branch's solvency ratio is below 200%, the branch will seek assistance from Zurich Group to raise solvency capital or for a capital injection from ZLIC, the parent corporation. Similarly, if ZLIHK's solvency ratio is below 200%, or if it is anticipated that the solvency ratio will likely fall below 200% measured on the local statutory basis, it will seek assistance from Zurich Group to raise solvency capital or for a capital injection from ZIC via ZIH, the shareholders of ZLIHK. In addition, I have been informed by the Parties that there was a letter of undertaking from ZLIHK to the IA when the license was issued, which specifies a parental commitment to maintain ZLIHK's solvency ratio of at least 150% of the statutory minimum solvency margin.

6.12.5. In monitoring the capital adequacy of ZLIC HK branch and ZLIHK, the management takes appropriate steps to comply with the Hong Kong regulatory capital requirements, including:

- filing annual statements with the IA that are required to confirm the ZLIC HK branch and ZLIHK's solvency position; and
- preparing a DST result based on annual business plan, which is a projection of ZLIC HK branch and ZLIHK's balance sheet covering at least three years into the future under plausible scenarios, to address any actions that may be required in order to maintain the regulatory capital requirements over the projection horizon.

6.12.6. Distribution of shareholder dividends is subject to approval of the Board of Directors following the recommendation of the Chief Financial Officer and the Appointed Actuary. ZLIHK will seek the IA's approval prior to any payment of shareholder dividend.

6.13. RISK POLICY / RISK MANAGEMENT FRAMEWORK

6.13.1. ZLIC has a strong corporate governance framework that is implemented in its daily business, which provides the basis for ZLIC to create sustainable value for all of its stakeholders. The principles of corporate governance are incorporated and reflected in a number of corporate documents, in particular the Articles of Incorporation, the Organizational Rules, the charter of the Audit Risk Committee of the Board and the ZLIC Governance Framework.

Board of Directors

6.13.2. The Board, under the leadership of the Chairman, is responsible for determining the overall strategy of ZLIC and the supervision of management. It holds the ultimate decision-making authority for ZLIC, except for decisions on matters reserved for the shareholders' general meetings. The Board prepares the Annual General Meeting and implements its resolutions.

Audit & Risk Committee

6.13.3. Management is responsible for preparing ZLIC's financial statements, managing risk, developing and maintaining internal controls and ensuring appropriate governance processes, the Audit & Risk Committee serves as a focal point for discussion and for the communication of matters related to financial reporting oversight, internal controls, compliance and risk management, and reports on these matters to the full Board.

Risk Policies

6.13.4. ZIC and ZLIC are regulated and supervised by FINMA in Switzerland, which has its prescriptive requirements in relation to risk management. The risk management of ZIC and ZLIC is in line with these controls and is documented within the Zurich Risk Policy ("ZRP"), which is approved by the Zurich Group CEO. The ZRP sets the standard for effective risk management across all of its subsidiaries. ZRP is comprised of a main document as well as the accompanying detailed risk policy manuals, which cover underwriting, claims handling, reserving, reinsurance, investment management, investment operations, outsourcing, business continuity etc. These will be applied to the relevant companies, along with the adoption of the companies' specific local policies / standards. Any material deviations from the ZRP required by local laws and regulations must be reported to and approved by the Zurich Group.

6.13.5. The table below provides an overview of the policies and procedures being applied generally across the Zurich Group.

Policies applicable across Zurich Group	**Description**
Zurich Risk Policy	The Zurich Risk Policy ("ZRP") articulates the Zurich Group's approach to risks, and sets standards for effective risk management throughout the Zurich Group. The ZRP: ▪ Describes the Zurich Group's risk management framework ▪ Identifies Zurich Group's principal risk types ▪ Defines the Zurich Group's appetite for risks at group level.
Risk Appetite and Tolerance Framework Policy Manual (Local Level)	The purpose of this document is to assist local legal entities and management units to create a local risk appetite that helps to cascade the Zurich Group risk appetite to make it more usable and relevant at a local level and to foster targeted and strategic risk-taking by local management.
Operational Risk Policy Manual	This document outlines the key elements of the Operational Risk Framework which establishes the general requirements for the effective management of OR at Zurich Group and applies to all business units (BUs), legal entities and group functions across the Zurich Group including shared service centers. The scope also includes processes executed by second line functions to support business activities
Capital Management Risk Policy Manual	This manual defines the Zurich Group's approach to managing its internal and external capital, taking into consideration economic risks inherent in Zurich Group's businesses, regulatory requirements and constraints, ratings criteria and other relevant considerations.

6.13.6. Both ZLIC HK branch and ZLIHK develop their risk policies with reference to the Zurich Group's policies. Their policies have to comply with both the Zurich Group requirement and statutory requirements. As a result, there should not be any obvious deviation in the risk management framework.

6.13.7. In particular, the Risk Appetite Statement ("RAS") of ZLIC HK branch follows Zurich Group governance and local statutory requirements. The same approach is currently being followed by ZLIHK. The key requirements set up by RAS are related to risk taking approach and risk appetite for every risk category (where risk appetite is expressed as Low Appetite/ Moderate Appetite/ High Appetite), incorporating defined quantitative key performance indicators and tolerance levels.

6.13.8. Overall, the risk appetite statements are similar for both ZLIC HK branch and ZLIHK, there are no material differences in the target levels of risk measures applicable for both ZLIC HK branch and ZLIHK and the Parties have confirmed that risk appetite is materially unchanged in the new entity.

6.14. REGULATORY OVERLAY

6.14.1. The financial security of the policyholders needs to be further considered from a legal perspective, especially when the Scheme involves moving from Hong Kong branch with a Swiss parent to a Hong Kong subsidiary. Therefore, I have considered the regulatory overlay from two perspectives, including regulatory framework and solvency regime, as well as policyholder protection.

Regulatory framework and solvency practice

6.14.2. I have considered the possible impacts on the financial security of Transferring Policyholders from the perspective of regulatory framework and solvency regime. Given this broad topic covers a number of important aspects which are difficult to be compared with a bottom-up approach, I have made reference to the reports of "Detailed Assessment of Observance – Insurance Core Principles" produced by the International Monetary Fund ("IMF") on both the Hong Kong and Switzerland regulatory frameworks in drawing my conclusion.

6.14.3. In these reports, the IMF compared the Hong Kong and Swiss regulatory frameworks and solvency practice against the 26 Insurance Core Principles ("ICPs") set out by the International Association of Insurance Supervisors that are regarded as the role model of regulatory framework. Each of these 26 ICPs serves as the guideline on important regulatory aspects including but not limited to corporate governance, risk management and internal controls, supervisory review and reporting, capital adequacy, conduct of business, public disclosure etc. The local regulatory frameworks are compared to the ICPs and a score ranging from "observed", "largely observed", "partly observed" to "not observed" will be given by the IMF on each ICP.

6.14.4. Based on the IMF reports, the regulatory framework in Hong Kong has 9"observed" items and 12 "largely observed" items and 5 "partly observed", while the regulatory framework in Switzerland has 16 "observed" items, 7 "largely observed" items and 3 "partly observed" items. These scores show that both regimes were held in high regard by the IMF.

6.14.5. Most importantly, in terms of day to day regulatory supervision, the IA maintains regulatory and supervisory authority of the operations in Hong Kong at all times that apply to both ZLIC HK branch and ZLIHK.

Policyholder protection

6.14.6. I have considered the policyholder protection under both Swiss and Hong Kong regulatory environment in the case of insolvency, from the perspectives of both available policyholder protection scheme and the creditor ranking of the policyholders in the case of insurance company wind-up.

6.14.7. There is no policyholder protection scheme in Switzerland and Hong Kong that provides protection should an insolvency happen, despite there having been consultation paper issued on the topic previously in Hong Kong.

6.14.8. In the event of the insolvency of ZLIC HK branch (before the Scheme is implemented) or ZLIHK (after the Scheme is implemented), the ranking of policyholders would be governed by Hong Kong law and follow a pre-determined ranking waterfall set out by statute. The Scheme has no impact on this pre-determined ranking.

6.14.9. In the event of the insolvency of parent company, before the Scheme is implemented, ZLIC HK branch, as the Hong Kong operation (i.e. the ZLIC HK branch before the Scheme) is set up as a branch of ZLIC, the wind-up of the parent company would automatically trigger the wind-up of the branch itself given it is part of the same company. Whereas, after the Scheme is implemented, ZLIHK, being a subsidiary, the wind-up of ZLIC will not impact ZLIHK in the same way.

6.15. CONCLUSION

6.15.1. The estimated HKIO basis solvency ratio of ZLIHK post-Scheme is higher than the 30 September 2020's solvency ratio of ZLIC, which is positive for the financial security of the Transferring Policyholders.

6.15.2. Based on the policies provided, I recognise that the Transferring Policyholders will continue to be protected by the financial strength of ZIC after the Scheme is implemented through support from the capitalisation policies in the extreme event where ZLIHK faces financial difficulties. I consider this to be an important factor in maintaining the financial security of the Transferring Policyholders post-Scheme.

6.15.3. In view of my assessment above, I believe the Scheme is unlikely to expose the Transferring Policyholders of the ZLIC HK branch to new risks of significance. I conclude there will be no materially adverse impact on the Transferring Policyholders' financial security after the Scheme.

Section 7 Other Considerations for Transferring Policyholders

7.1. INTRODUCTION

7.1.1. In this section, I have considered other operational areas that may impact the Transferring Policyholders if the Scheme proceeds.

7.2. GROUP STRUCTURE

7.2.1. The Zurich Group structure before the Transfer is shown under Figure 2.1.

7.2.2. As a result of the restructuring, the ZLIHK will replace the ZLIC HK branch. The Zurich Group also planned to transfer the business of Hong Kong branch of Zurich Assurance Ltd. ("ZAL") into ZLIHK by 2024.

7.2.3. As Zurich Insurance Group Ltd. remains as the ultimate parent of the Zurich Group after the restructuring and all the Zurich Group policies continue to apply, I do not expect any materially adverse impact to the Transferring Business as a result of the change in group structure.

7.3. REINSURANCE ARRANGEMENTS

7.3.1. The current reinsurance arrangements include the treaties between ZLIC HK branch and Swiss Re, Munich Re, RGA and affiliated reinsurer, Zurich Insurance Company Ltd.. The Parties have stated that all the existing reinsurance arrangements of these branches are to be retained and remained in force under ZLIHK in accordance with the transfer clause of the treaty.

7.4. DISTRIBUTION ARRANGEMENTS

7.4.1. ZLIC HK branch was closed to the new Hong Kong retail business on 31 December 2013, but continued to renew the CLP business up to 31 December 2017. The core distribution channels used by ZLIC HK branch, before it stopped selling new business, were tied agency and broker.

7.4.2. There is also a policy servicing agreement with a medical administrator, Global Health company and its sub-contractor, April Singapore Assistance PTE. LTD. This agreement covers the administrative service for the annual renewal of individual health policies under the Global Health product. There will also be a service level agreement or similar to service the Swiss policies.

7.4.3. For ZLIHK, new products are expected to be distributed through IFA/brokers following the existing strategy of the ZIL HK branch, while direct/digital distribution capability may be developed in the future.

7.5. RECENT INCIDENTS OF ZLIC HK BRANCH

7.5.1. I have been informed of two recent regulatory breaches by ZLIC HK branch. The incidents are related to (i) annual management charge calculation in the universal life products and (ii) unit dealing for unit-linked policies.

7.5.2. I have reviewed all the incident reports of the aforementioned breaches, as well as the remediation proposals. I have been informed that the incidents have involved compensation payments amounting to HKD 317,313.65 and USD 246,964.68 respectively for incident (i) and (ii) and the payments have been made to the adversely affected policyholders on 14 July 2020 for incident (i) and 18 December 2020 for incident (ii). I have been informed that the ZLIC HK branch has also implemented various changes to the company's internal control framework and has taken various actions to prevent reoccurrence of similar incidents in the future. The amount of compensation is not material to the financial position of ZLIC HK branch, and the payments have been settled before the Transfer Date.

7.5.3. The Parties have confirmed that, other than the regulatory incidents on annual management charge calculation and unit dealing, it is not aware of any other local regulatory non-compliance incidents with material outstanding remedial measures to the effect that policyholders may be adversely affected by the Scheme. The Parties have also confirmed that it has not received any complaints or objections from any policyholders affected by any other local regulatory non-compliance incidents. If any policyholders (including those with unpaid compensation) raise any queries after the Proposed Transfer, ZLIHK undertakes to address such queries in a professional and responsible manner.

7.5.4. In addition, various rectification actions have been put in place to prevent reoccurrence of similar incidents in the future, therefore, I do not expect these incidents and the remediation will have any impact on the Transfer, from either a financial or non-financial perspective.

7.6. UNSETTLED CLAIMS

7.6.1. All unsettled claims under the Transferring Policies shall be transferred to ZLIHK on and with effect from the Effective Date. Existing policy terms and conditions will continue to govern the assessment of the claim. ZLIHK will take over the processing of the claims from ZLIC HK branch and be responsible for any subsequent payment to policyholders. Overall, I do not expect this will have any materially adverse impact on the Transferring Policyholders as a result of the Scheme.

7.7. CONTINUITY OF LEGAL PROCEEDINGS

7.7.1. On and with effect from the Transfer Date, by virtue of the Hong Kong Order, any judicial, quasi-judicial, disciplinary, administrative, arbitration or legal proceedings pending by or against ZLIC HK branch in relation to the Transferring Policies, Transferring Assets and Transferring Liabilities shall be continued by or against ZLIHK, in substitution for ZLIC HK branch and ZLIHK shall be entitled to the same defences, claims, counterclaims and rights of set-off as ZLIC HK branch in respect thereof. I am satisfied that, in itself, this will not have a materially adverse impact on the Transferring Policyholders as a result of the Scheme.

7.8. PREMIUMS, MANDATES, SERVICES AND OTHER INSTRUCTIONS

7.8.1. All premiums attributable or referable to the Transferring Policies shall, on and after the Effective Date, be payable to ZLIHK.

7.8.2. Any mandate or other instruction in force on the Effective Date (including, without limitation, any instruction given to a bank by its customer in the form of a direct debit or standing order) and providing for the payment by a banker or other intermediary of premiums payable under or in respect of any Transferring Policy to ZLIC HK branch shall, on and from the Effective Date, take effect as if it had provided for and authorised such payment to ZLIHK.

7.8.3. Any mandate or other instruction in force on the Effective Date related to customer services and as to the manner of payment of any sum payable by ZLIC HK branch under any of the Transferring Policies and the Transferring Reinsurances shall, on and from the Effective Date, continue in force as an effective authority to ZLIHK.

7.9. VARIATIONS TO THE SCHEME

7.9.1. The Scheme provides that ZLIC HK branch and ZLIHK may apply to the Hong Kong Court for consent to modify, vary or amend the terms of the Scheme, provided that:

- the proposed modification, variation or amendment has been approved by the respective Appointed Actuaries and Board of Directors of ZLIC HK branch and ZLIHK;
- the IA shall be notified of, and has the right to be heard at any hearing of the Court at which such application is considered; and
- such application shall be accompanied by a certificate from an independent actuary to the effect that in his opinion, the proposed modification, variation or amendment will not materially and adversely affect the reasonable benefit expectations or the financial security of the holders of Transferring Policies.

7.10. LEVEL OF SERVICE

7.10.1. The Parties have informed me that the target service levels of ZLIHK after the Transfer will be on the same level as that of ZLIC HK branch before the Transfer for all key areas. In particular, it is targeted to take up to 5 business days to process the benefit claims and up to 2 business days for claim finalisation and payment. Complaints from the customers are targeted to be acknowledged within 1 business day, whereas resolution or progress updates are targeted within 5 to 15 business days depending on the complexity. In addition, new business cases are targeted to be attended by ZLIHK within 5 business days.

7.10.2. The Parties have confirmed that the same teams of operational and administrative staff (including life policy administration, customer care and life claims) will continue to service transferring, non-transferring and existing policyholders. Administrative rules applied to transferring policies before the Transfer would continue to be applied after the transfer. The Parties have committed to maintaining and improving customer serviced levels in all material aspects. Operations will review the administrative rules and service offering from time to time to ensure that customers' rights are being fulfilled and that there is full compliance with the various regulatory requirements. Overall, the Parties have committed that level of service to policyholders will not be negatively impacted by the transfer.

7.11. POLICYHOLDER SERVICES

7.11.1. For unit-linked Transferring Policyholders, the existing range of fund choices currently available to the long term Transferring Policyholders of ZLIC HK branch will not be affected as a result of the Scheme implementation.

7.12. CONCLUSION

7.12.1. I consider the above various operational areas, including the level of service provided, will not have a material negative impact on the Transferring Policyholders and the Scheme should provide sufficient safeguards to ensure that the Scheme operates as presented.

7.12.2. While I do not expect my conclusions to change, I will prepare a Supplementary Report to the Hong Kong Court prior to the final hearings to update the findings and draw any significant developments or changes that may affect policyholders to the attention of the Hong Kong Court. I would expect the Supplementary Report to include consideration of the following, if relevant:

- updated commentary on the solvency position of the ZLIC HK branch based on financial data as at 31 December 2020, updated commentary on the Phase 2 product approvals status of ZLIHK and any new business written by ZLIHK prior to the Transfer Date;
- any material changes to the risk profile of ZLIC and its branches including ZLIC HK branch;
- policyholder responses regarding the Scheme; and
- any other material developments that have occurred since the date of this report, including the effects of the COVID-19 pandemic.

Section 8 Impact of the Proposed Transfer on the Non-Transferring Policyholders

8.1. INTRODUCTION

8.1.1. While I have considered the effects of the Scheme on the Transferring Policyholders extensively in this report given they are under the jurisdiction of the Hong Kong Court, I also consider the effects of the Scheme on the Non-Transferring ZLIC Policyholders to ensure the Scheme does not bring materially adverse impact to policyholders of both Parties.

8.1.2. My considerations on the Non-Transferring ZLIC Policyholders are discussed in this section. When forming my opinion in this section, I have relied upon the professional opinions of the Appointed Actuary and the Chief Actuary of ZLIC.

8.2. NON-TRANSFERRING BUSINESS

8.2.1. ZLIC is a life insurance provider serving both retail and corporate customers, primarily in Switzerland as well as through branches in Japan, Hong Kong and Dubai.

8.2.2. The tables below summarise the gross written premium and policy fee of ZLIC breakdown by type of business and by country respectively.

Table 8.1: Gross written premiums and policy fee by type of business

CHF millions	2017	2018	2019
Group insurance Switzerland	812	777	884
Group insurance abroad	-	-	-
Individual insurance Switzerland	632	635	660
Individual insurance abroad	46	43	41
Health insurance abroad (Japan)	242	320	403
Reinsurance assumed	144	5	5
Gross written premiums and policy fee	**1,876**	**1,780**	**1,994**

Source: ZLIC's 2018 and 2019 Financial Condition Report.

Table 8.2: Gross written premiums and policy fee by country

CHF millions	2017	2018	2019
Switzerland	1,587	1,418	1,549
Hong Kong	47	43	41
Japan	242	320	403
Dubai	(1)	-	-
Gross written premiums and policy fee	**1,875**	**1,780**	**1,994**

Source: ZLIC's 2018 and 2019 Financial Condition Report.

Materiality of the Non-Transferring Business

8.2.3. The comparison of the in-force portfolios of ZLIC and the Hong Kong branch as at 30 September 2020, set out in the table below, show that the ZLIC HK branch represents a very small proportion of its parent's overall business.

Table 8.3: In-force portfolio of ZLIC as at 30 September 2020

Statistical data	ZLIC Total	HK branch	Percentage
Number of policies (number of insured for corporate life and pension business) at 30 September 2020 (in million)	1.84	0.039	2.2%
Gross written premiums (GWP) and policy fees (in CHF million)	1,381	27	2.0%
Insurance reserves, gross and provisions for unit-linked contracts (in CHF million)	19,166	498	2.6%

Source: ZLIC internal non-public information

The Portfolio of the Non-Transferring Business

8.2.4. Most business of ZLIC is participating in nature. This covers both the individual life business and the corporate life and pension businesses. An overview of the products is provided below:

Individual Life

8.2.5. Main products include the following participating products:

- Endowment and Pure endowments;
- Annuities and deferred Annuities;
- Term and other protection products; and
- Unit-linked and hybrid products.

Corporate Life and Pension

8.2.6. Corporate Life and Pension business covers a wide range of products designed for companies and pension funds, providing a variety of mortality and morbidity type benefits. There is also a portfolio of legacy savings and annuity business.

8.2.7. Currently sold business can be split into two main categories: legal quote business and the non-legal quote business. The difference between the two is that the former has a fixed level of profit sharing set out in regulation, while the non-legal quote does not have such a fixed level and it is typically negotiated with clients individually.

8.3. BENEFIT EXPECTATION

8.3.1. Same as the comment I have made for the Transferring Policyholders, when considering the effects of the Scheme on the benefit expectations of the Non-Transferring ZLIC Policyholders, I have mainly considered factors related to the fulfilment of contractual terms and provisions.

8.3.2. The likely effects of the Scheme on the current benefit expectations for various products are also considered. It includes the policies with discretionary components such as those participating products with a combination of discretionary and guaranteed benefits, and policies with other discretionary elements such as unit-linked products with non-guaranteed fees and charges, or traditional products offering non-guaranteed premium structures and conversion rights.

Contractual benefit provisions

8.3.3. When forming my opinion on contractual benefits provision, I have not attempted to look at the contractual benefits provided by ZLIC. However, given the ZLIC HK branch is only a small part of ZLIC's entire business, I agree with the Appointed Actuary and Chief Actuary's opinions that the benefit expectations of the Non-Transferring ZLIC Policyholders in terms of ZLIC's ability to pay valid claims, as well as to act appropriately in other contractual matters, should be unchanged.

Bonus policy

8.3.4. The way the policyholder participation works for Swiss business is in two steps. On an annual basis as part of the result steering credits are set by management to a bonus fund which covers a large collective of policyholders. There are currently 3 main bonus funds used in Switzerland:

- Individual Life;
- Corporate Life and Pensions – legal quote; and
- Corporate Life and Pensions – non-legal quote.

8.3.5. Once the profit sharing has been credited to the bonus funds, these amounts have to be paid out to policyholders over a certain period. The term over which the bonus fund has to be paid out is regulated in law and differs slightly between the different businesses but typically is in the range of 5 years. There are also some scenarios under which the bonus fund can be used to cover losses, which means under some scenarios the bonus fund is not paid out to policyholders.

8.3.6. The bonus funds are paid out to policyholders in various forms. The most common ones are the following:

- Increasing policyholder benefit;
- Reducing the premium paid by the policyholder;
- Bonus in a separate account or unit-linked policy; or
- Cash bonus.

8.3.7. Similar policyholders have to be treated in the same way which means similar policies are credited with similar bonuses. Some more details on this are given in the next section.

8.3.8. The two-step method adopted by ZLIC results in a smooth and stable pay-out of bonuses to policyholders.

8.3.9. The Parties have confirmed that there will be no changes to the bonus philosophy and crediting rate philosophy as a result of the Scheme.

Other policies subject to company discretion

8.3.10. The charging structure of ZLIC's Non-Transferring unit-linked products include monthly charges such as annual management charges, policy administration charges, allocation/setup charges, bid offer spreads, surrender charges, and benefit charges. Policyholders will be given written notice in advance according to policy provisions before any changes come into effect. These rights will continue with ZLIC and exist whether or not the Scheme proceeds.

8.3.11. There are ZLIC's products which allow the conversion of the savings capital into a series of annuity payments. For these products, the applicable conversion rates used to convert a savings capital into an annuity at the time of conversion would not be impacted by the transfer.

8.3.12. Therefore, in conclusion, apart from the fact that these rights exist whether or not the Scheme proceeds and I have no reason to believe the Scheme will lead to a materially adverse exercise of discretion in relation to the Non-Transferring ZLIC Policyholders.

Policy terms and conditions

8.3.13. Both of the Appointed Actuary and Chief Actuary of ZLIC have confirmed that there will be no change to the policy terms and conditions of the in-force Non-Transferring ZLIC Policies as a result of the Scheme.

8.4. FINANCIAL SECURITY

8.4.1. The security of the contractual benefits of policyholders can be measured by the excess assets in the long term insurance business fund plus the net shareholder assets.

8.4.2. Same as the comment I have made for the Transferring Policyholders, when considering the effects of the Scheme on the benefit expectations of the Non-Transferring ZLIC Policyholders, I have mainly considered the conservatism of the reserving bases used and the capital and free reserves, together with additional security provided by the entity as a whole, and any potential support available from its shareholders.

FINMA supervision

8.4.3. ZLIC is subject to insurance supervision by FINMA. The Swiss Insurance Supervision Law (ISL) requires Swiss insurance companies to establish and maintain corporate governance including an effective risk management and internal control system that is appropriate to their business activities. In addition to the supervision exercised by FINMA, ZLIC and its branches are supervised according to the requirements of relevant local supervisory authorities.

8.4.4. ZLIC assesses its solvency under the Swiss Solvency Test (SST). In performing the SST, ZLIC assesses its solvency and financial condition, expressed as the SST ratio which must be submitted to FINMA annually.

The provision of financial security

8.4.5. To protect the security of policyholders, insurance companies maintain sufficient policy reserves and sufficient solvency margin under the Swiss Solvency Test required by legislation.

- Policy reserves: Assets supporting the policy liabilities calculated according to the underlying contractual obligations using valuation standards prescribed by statutory rules with prudent assumptions. Assets are held in accounts explicitly dedicated to the policyholders (tied assets).
- Solvency margin: prescribed by statutory regulation, this is the capital required according to the risks the insurance company is exposed (target capital) and its own eligible capital (risk-bearing capital).

Policy reserves

8.4.6. ZLIC has been reporting under the Switzerland regulatory regime to FINMA, with the Appointed Actuary and the auditor certifying compliance with the Swiss Insurance Supervision Ordinance ("AVO") and the actuarial requirements specified in ZLIC's business plan. In the statutory valuation reporting process, the Appointed Actuary is responsible for the valuation methodology and the setting of adequate actuarial assumptions. After the transfer, the procedures and responsibilities will remain the same. There is no change in procedure in determining the valuation methodology and assumptions before and after the transfer.

Overall financial position and shareholders' capital

8.4.7. The overall financial security of the long term Non-Transferring Policyholders of ZLIC does not only depend on the amount of statutory reserves and solvency requirements, but also on the level of free assets.

8.4.8. The historical solvency ratios of ZLIC for 2017-September 2020 on both SST basis and HKIO basis are shown in Table 6.2 to Table 6.4.

8.4.9. ZLIC is part of the Zurich Insurance Group which maintains a strong capital position. The Insurer Financial Strength Rating (IFSR) of ZIC is currently rated 'AA/Stable' by Standard and Poor's, 'Aa3/ Stable' by Moody's and 'A+/Stable by A.M. Best. This reflects an insurance company that offers good financial security and has superior financial strength with respect to ability to pay policies and contracts. In particular, A+ companies rated by A.M. Best have a very strong ability to meet ongoing obligations to policyholders.

8.4.10. The projected solvency ratio ZLIC has been assessed to show the immediate impact before and after transfer as at the Transfer Date. In addition, as demonstrated by the solvency position of the ZLIC under the plan projection (as shown in below table), ZLIC is adequately capitalised and is projected to have stable solvency ratio as at the Transfer Date, and the company expects the same after the transfer.

Table 8.4: ZLIC's solvency position on HKIO basis as at 30 September 2020

CHF million	Including HK branch business	HK branch business	Excluding HK branch business
Solvency margin	1,011	14.8	997
Net assets	3,436	62.0	3,374
Solvency ratio [1)]	340%	420%	339%

1) Approximated Hong Kong IO basis derived by Hong Kong team from public figures

8.4.11. Given the size of the Transferring Business is relatively immaterial to ZLIC and from the projected solvency position of ZLIC shown above, I agree with the Appointed Actuary and Chief Actuary that the Transfer is not expected to materially adversely affect the financial security of the Non-Transferring ZLIC Policyholders.

Risk exposure

8.4.12. Due to the relatively small size of the Transferring Business compared to the Non-Transferring Business as shown in paragraph 8.2.3, the risk exposure of the Non-Transferring Business does not change materially as a result of Scheme implementation.

Capitalisation policy

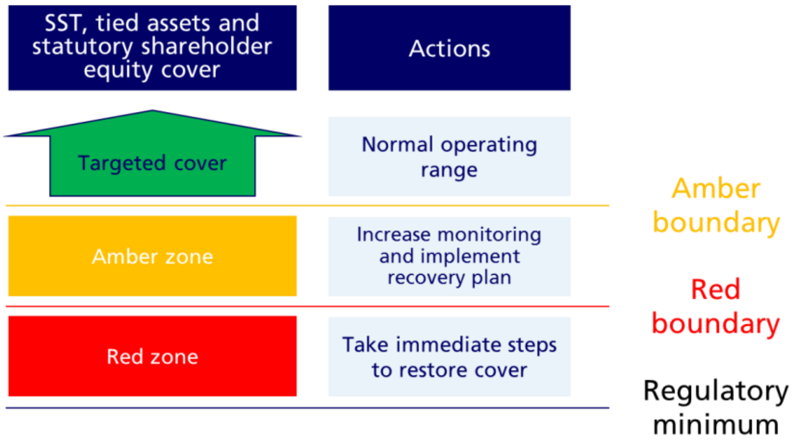
8.4.13. ZLIC maintains a Risk Appetite Statement which includes a framework of coverage boundaries in excess of the minimum level required by Swiss law and regulation for the following:

- Tied assets,
- Statutory shareholder equity, and
- Swiss Solvency Test (SST) solvency.

8.4.14. For each of these three measures, there is a red boundary, requiring urgent response, and an amber boundary informing the target coverage level, as explained in the diagram below. The different measures can move independently from one another, so all three are monitored on a regular basis. Appropriate actions are taken in response to changes in coverage under each individual measure.

8.4.15. The risk appetite amber boundary is set so that the probability of observing a drop in the SST ratio to 100% is no more than 1 in 4 annually, without allowing for any possible recovery actions. For tied assets and shareholder equity, the amber boundary is set based on a 1 in 200 confidence level over a two-month time horizon. This reflects both the respectively shorter response time needed to implement recovery actions for tied assets and shareholder equity than SST, and the relatively more severe consequences of a breach than for SST.

8.4.16. ZLIC pays shareholder dividends annually only if shareholder equity and Swiss Solvency Test are both above respective amber boundaries. Cash is remitted to the Zurich Group only if tied assets coverage is in excess of the targeted level above the amber boundary for tied assets.



8.4.17. Besides management of its solvency position, ZLIC has a corresponding framework for its liquidity requirements, to ensure both expected and unexpected claims can be paid as they fall due.

8.4.18. The Risk Appetite Statement will continue to apply after the Transfer so the capitalisation policy will not be changed as a result of the Scheme.

Risk policy and risk management framework

8.4.19. I have been informed that risk policy and risk management framework will not be changed as a result of the Scheme.

8.4.20. With the risk policies and risk management frameworks expected to be maintained in the same way, the Scheme is expected to have no impact on how risks are managed within ZLIC. Details of the risk policies and risk management frameworks have been provided under Section 6.13.

Investment policy and currency risk hedging

8.4.21. Since the Transferring Business is ring-fenced from ZLIC parent company and the Non-Transferring Business, there is no change in the investment policy/investment strategy and currency hedging tool and strategy after the transfer.

Shareholders' Fund and policy on shareholder dividends

8.4.22. ZLIC have an overall framework of making dividends to its owner ZIC. The amount of dividend is restricted by the capital ZLIC holds in relation to its risk appetite statements and other legal requirements. When making dividends the level of shareholders fund, solvency ratio and other metrics are considered.

8.4.23. The proposed transfer will have no material impact on the ZLIC shareholders' fund or on ZLIC's dividend policy.

8.5. OTHER CONSIDERATIONS

Policyholder services

8.5.1. For unit-linked Non-Transferring Policyholders, the existing range of fund choices currently available to the long term Non-Transferring Policyholders of ZLIC will not be affected as a result of the Scheme implementation.

Reinsurance arrangements

8.5.2. The current reinsurance arrangements include a set of relatively minor risk reinsurance treaties outside of Hong Kong and a set of reinsurance treaties covering the Transferring Business. As the Hong Kong reinsurance treaties will be transferred along with the business. The other non-Hong Kong treaties are not impacted.

Distribution arrangements

8.5.3. Given that ZLIC Hong Kong branch is closed to new business, there are no active distribution agreements relating to the Transferring Business that needs to be considered. For Non-Transferring Business, there are multiple distribution agreements, but these will not be impacted by the Transfer and hence there is no change to these.

Level of services

8.5.4. As the ZLIC HK Branch portfolio is such a small portion of the overall ZLIC business, I have been informed that the transfer of these policies will have a negligible impact on the level of services provided to the Non-Transferring Policyholders.

8.6. CONCLUSION

8.6.1. Taking account of the above considerations, I am satisfied that the Scheme will not materially adversely affect either the reasonable expectations or the financial security of the Non-Transferring ZLIC Policyholders.

Section 9 Impact of the Proposed Transfer on the Existing ZLIHK Policyholders

9.1. INTRODUCTION

9.1.1. In this section I consider the effects of the Scheme on the Existing ZLIHK Policyholders, given that ZLIHK started issuing policies in July 2020. When forming my opinion, I have relied upon the professional opinion of the Appointed Actuary of ZLIHK.

9.2. EXISTING BUSINESS OF ZLIHK

9.2.1. The following table shows the number of policies, total gross sum assured, total gross annualised premium and amount of net liabilities of ZLIHK's Existing Business as at 30 September 2020

Table 9.1: Long term business of ZLIHK as at 30 September 2020

Class	Number of policies	Total gross sum assured HKD million	Total gross annualised premium HKD million	Amount of net liabilities HKD million
A - life assurance participating	-	-	-	-
A - life assurance non-participating	13	63	0.103	0.103
A – annuities	-	-	-	-
C - linked	-	-	-	-
Total (as at 30 September 2020)	13	63	0.103	0.103

9.3. BENEFIT EXPECTATIONS

9.3.1. When considering the effects of the Scheme on the benefit expectations of the Existing ZLIHK Policyholders, I have mainly considered factors related to the fulfilment of contractual terms and provisions.

Contractual benefit provisions

9.3.2. Although the contractual benefits that will provided by ZLIHK have not been finalised, I have been informed by the Appointed Actuary of ZLIHK that there will be no change to the contractual benefits provided to the Existing ZLIHK Policyholders following the implementation of the Scheme, and that valid claims will continue to be paid when due in the same manner as before the Scheme.

Other policies subject to company discretion

9.3.3. ZLIHK has started to issue individual non-linked policies (Class A) after receiving its license approval on 23 March 2020. Unit-linked policies will be issued upon ZLIHK obtaining its necessary Class C product approvals from the regulatory bodies in Second Phase.

9.3.4. The Parties have informed me that for Class A business, in accordance with the ZLIHK's current 2020 plan, a new term product was launched in Q3 2020. ZLIHK will launch a new critical illness protection product by Q3 2021 and will continue monitoring Qualifying Deferred Annuity Policy ("QDAP") market developments assessing the possibility of launching such a retirement solution in the future. However, any annuity product will offer guaranteed cash values during the fixed annuity period and no discretionary component to align with ZLIHK's strategy of only offering non-participating Class A products. As the move into the QDAP sector is not decided and, even if it were to happen, sales volumes are expected to be small and therefore will not be included in the 2021 ZLIHK business plan which is currently in production. The Parties have also informed me that, due to recent COVID-19 pandemic, there will be a slight delay in launching various products, although the overall roadmap remains the same.

9.3.5. For Class C business with non-guaranteed fees and charges, ZLIHK will have the broad rights to vary policy charges, as well as the right to impose any other charges for administering the policy, provided that the policyholders will be given advance written notice before changes.

9.3.6. In conclusion, apart from the fact that these rights to vary unit-linked charges exist whether or not the Scheme proceeds and I have no reason to believe the Scheme will lead to a materially adverse exercise of discretion in relation to the Existing Policyholders of ZLIHK.

Policy terms and conditions

9.3.7. The Appointed Actuary of ZLIHK has confirmed that there will be no change to the policy terms and conditions of the Existing ZLIHK Policies as a result of the Scheme.

9.4. FINANCIAL SECUIRTY

9.4.1. Same as the comment I have made for the Transferring Policyholders, when considering the effects of the Scheme on the financial security of the Existing ZLIHK Policyholders, I have mainly considered the conservatism of the reserving bases that are planned to be used and the capital and free reserves, together with additional security provided by the entity as a whole, and any potential support available from its shareholders.

Policy reserves

9.4.2. ZLIHK is reporting under the Hong Kong regulatory regime, with the Appointed Actuary and the auditor certifying compliance with the Hong Kong Insurance Ordinance (CAP 41).

9.4.3. After the Scheme is implemented, the procedures will remain the same such that each year the Appointed Actuary of ZLIHK will advise on the reserving methods and valuation bases to the ZLIHK Board of Directors. As no changes in procedure in determining the valuation methodology and assumptions have been proposed if the Scheme is implemented, I do not believe there will be an adverse impact on the financial security of the Existing ZLIHK Policyholders in this regard.

Overall financial position and shareholders' capital

9.4.4. The overall financial security of the long term Existing ZLIHK Policyholders does not only depend on the amount of statutory reserves and solvency requirements, but also on the level of free assets.

9.4.5. The projected pre- and post-transfer solvency ratio of ZLIHK under HKIO basis, as shown in Table 6.5 as at the Transfer Date is respectively 3779% and 637%. The significant reduction in solvency ratio can be explained by the statutory solvency margin in Hong Kong is calculated according to a formula using the sum assured and sum-at-risk of the underlying in-force portfolio subject to a minimum of HKD2 million. Pre-transfer, while there is little or no in-force business, the solvency margin is equal to this minimum amount of HKD2 million but after transfer it will be determined by the formula. This is the main reason for the artificially high solvency ratio shown before transfer. After Scheme implementation the solvency ratio is still at a very high level, well above both the statutory minimum requirement and the level most insurance businesses are managed to.

9.4.6. Based on the projected post-transfer solvency ratio of ZLIHK under HKIO basis as at the Transfer Date and projection years thereafter as shown in Table 6.6, I have no reason to believe there will be any materially adverse impact on the financial security of the Existing ZLIHK Policyholders caused by the Scheme from a solvency perspective.

9.5. OTHER CONSIDERATIONS

Group structure

9.5.1. Same as the comments I have made under Section 7.2, given the ultimate parent remains the same after the implementation of the Scheme and all the group policies will continue to apply, I do not expect there to be any materially adverse impact to the Existing ZLIHK Policyholders as a result of the change in group structure.

9.6. CONCLUSION

9.6.1. Taking account of the above considerations in respect of the benefit expectations of the Existing ZLIHK Policyholders, financial security of ZLIHK before and after the Transfer and various operational areas, I am satisfied that the Scheme will not materially adversely affect both the reasonable expectation with regard to benefits and levels of service, as well as the financial security of the Existing ZLIHK Policyholders if new business in written in ZLIHK between operating licence approvals and Scheme implementation.

Section 10 Policyholder Communications

10.1. INTRODUCTION

10.1.1. In this section I summarise the notifications that ZLIC HK branch and ZLIHK will send out to the Transferring Policyholders and my view on whether these communications are appropriate in respect of the benefits to the Transferring Policyholders.

10.2. NOTIFICATIONS TO ALL POLICYHOLDERS OF ZLIC HK BRANCH AND EXISTING ZLIHK POLICYHOLDERS

10.2.1. All ZLIC HK branch's policyholders and existing ZLIHK policyholders, whose details are known, will receive copies of a letter, enclosed with "Summary of the Terms and Effects of the Proposed Transfer", which includes a summary statement of the proposed transfer and a summary of the Independent Actuary Report. Legal Notice will be published in newspapers and Gazette.

10.2.2. All ZLIC HK branch's policyholders and existing ZLIHK policyholders will be able to access on the corporate website information about the Scheme, including Notification with Summary of Scheme of Transfer, a full version of this Report, copy of the Court Petition (with copy of the Scheme annexed thereto) and Legal Notice. Alternatively, policyholders will be able to call a helpline with any enquiries about the Scheme.

10.2.3. Key documents, including both this report and the Summary Report, will be available in English and Chinese.

10.2.4. I am satisfied that the proposed approach to communicating with Transferring Policyholders is reasonable. I have also reviewed the English version of the proposed communication documents and am satisfied that these documents should help explain the material effects of the transfer.

10.3. NOTIFICATIONS TO NON-TRANSFERRING POLICYHOLDERS OF ZLIC

10.3.1. I have been informed by the Parties that they have applied for a waiver in respect of the notifications to the Non-Transferring ZLIC Policyholders, whereby 99% of the latter policyholders are located outside Hong Kong . I am satisfied that this is an appropriate approach as I agree with the reasons suggested by the Parties, including the fact that there will be no materially adverse impact caused by the Scheme to those policyholders, the immaterially of the Transferring Business and for the sake of avoiding unnecessary confusion to Non-Transferring Policyholders of ZLIC.

10.4. OBJECTIONS AND QUERIES

10.4.1. The ZLIC HK branch's Transferring Policyholders and Existing ZLIHK Policyholders as well as others, such as any employee from the Parties, who feel they will be negatively affected by the Scheme may put their objections to the Court either in writing or by attending the hearing. In dealing whether to sanction the Scheme, the Court will consider these objections. I will also consider them in coming to my view on the appropriateness of the Scheme.

Appendix A Terms of Reference

General requirements

A1. The Independent Actuary shall have a duty to act independently and this duty is paramount and overrides any obligation to the person from whom he has received instructions or by whom he is paid.

A2. Evidence presented to the Hong Kong Court should be, and should be seen to be, the independent product of the Independent Actuary uninfluenced by the exigencies of the instruction or court proceedings.

A3. The Independent Actuary should provide independent assistance to the Hong Kong Court where appropriate, by way of objective unbiased opinion in relation to matters within his expertise. He should never assume the role of an advocate.

A4. The Independent Actuary should not omit to consider material facts within his knowledge which could detract from his concluded opinion.

A5. The Independent Actuary should make it clear when a particular question or issue falls outside his expertise.

A6. If the Independent Actuary's opinion is not properly researched because he considers that insufficient data is available, then this must be stated with an indication that the opinion is no more than a provisional one.

A7. In a case where the Independent Actuary who has prepared a report could not assert that the report contained the truth, the whole truth and nothing but the truth without some qualification, that qualification should be stated in the report.

A8. If the Independent Actuary changes his view on a material matter having read another expert's report or for any other reason, such change of view should be communicated in writing (through legal representatives) without delay to the company, and where appropriate to the Hong Kong Court.

A9. The Independent Actuary may communicate with the IA as he considers appropriate in connection with the services and the Scheme Report provided in connection with the appointment as Independent Actuary.

Scope of the work of the Independent Actuary in relation to the Scheme

My report is to consider the terms of the Scheme generally and the effect which the Scheme will have on the policyholders of the Parties.

In particular my report will consider the following specific matters:

- The impact of the Scheme on the financial security of the different groups and generations of policyholders of the Parties involved in the Scheme;
- The impact of the Scheme on the benefit expectation of the different groups and generations of policyholders of the Parties involved in the Scheme;
- A review of, and opinion on the fairness of, the operational continuity resulted by the change in operational plans following implementation of the Scheme, which will include types of new business to be written after the Scheme and its potential impact to the existing rights of the current policyholders of the Parties, as well as the cost implications;
- A review of, and opinion on the fairness of, proposals to combine any funds to the extent that any such combinations are included in the Scheme (either as at the effective date or subsequently), and consideration of any further covenants or undertakings that may be required to ensure that each category of policyholders is treated fairly;
- A review of, and opinion on the fairness of, any mechanisms to be implemented at the same time as the Scheme, but not included in the Scheme, to provide financial support to any of the funds involved in the Scheme;
- An assessment, and opinion on the fairness of, the potential change in capital position and review of the capital management policy to be adopted by the Parties following implementation of the Scheme to the policyholders of the Parties involved in the Scheme;
- A review, and opinion on the fairness of, the current risk exposure and potential change in risk exposure to the various groups of policyholders of the Parties involved in the Scheme. An assessment of any potential increase in concentration risks to the Parties after the transfer;
- An assessment of the nature of business written by the Parties before the transfer. A review of the guarantees offered by the Parties, and assessment of whether the existing guarantees will be matched after the transfer. An opinion on the fairness based on the assessment and review to the policyholders of the Parties involved in the Scheme;
- An assessment, and opinion on the fairness of, the potential change in the investment policies adopted by the Parties following implementation of the Scheme to the policyholders of the Parties involved in the Scheme; and
- An assessment, and opinion on the fairness of, the differences in the regulatory overlay between Switzerland and Hong Kong, e.g. how will the Scheme affect policyholder compensation schemes and priority on wind-up in case of financial instability following implementation of the Scheme to the policyholders of the Parties involved in the Scheme.

My review and report will address generally the way in which the Parties have conducted their insurance business but taking into account the particular circumstances of each class of business to be transferred. It will deal inter alia with the following aspects:

- Memorandum, and the Articles of Association, at least insofar as these affect the rights, expectations and interests of policyholders;
- The terms of the policies issued by each of the Parties;
- The existing and proposed internal working arrangements relating to the financial management of the long term business fund, including the operational and administrative arrangements which will apply to the policies to be transferred under the terms of the Scheme; and
- The terms and conditions expected to be imposed by the Scheme to be presented to the Court, including the views expressed by the governing body or management of the Parties.

The above list is not intended to be exclusive to any other aspects which may be identified during the completion of the project and which are considered to be relevant.

I shall not be directly involved in the formulation of the proposed transfer although I should expect to give guidance during the evolution of the detailed proposals on those issues which concern me, or which I consider unsatisfactory.

I will not provide any advice with respect to the merits of the transfer.

Disclosure of prior Hong Kong assignments undertaken for the Parties

The Hong Kong projects undertaken by Milliman Limited for the Parties and its related companies over the last 5 years are as follows:

- Preparation of a report presenting the embedded value of ZAL HK branch as at 31 December 2015;
- Preparation of a report presenting the embedded value of ZLIC HK branch as at 31 December 2015; and
- Preparation of a report presenting the embedded value of ZLIC HK branch as at 31 December 2018.

Appendix B Key Sources of Data

Documents related to the Scheme

B1. The Scheme pursuant to section 24 of the Ordinance (CAP 41) for the transfer of the long term insurance business from ZLIC HK branch to ZLIHK, as filed with the Hong Kong Court.

B2. The report on the proposed Scheme by the Key Person of the Actuarial Function of ZLIC and ZLIC HK branch.

B3. Organisation chart showing proposed organisation structure of the insurance operations of Zurich Group in Hong Kong.

B4. Policyholder communication pack issued by both ZLIC Hong Kong branch and the ZLIHK to Transferring Policyholders.

ZLIC

B5. Articles of Incorporation of ZLIC

B6. Solvency positions of ZLIC under SST basis as at 31 December 2016, 31 December 2017, 31 December 2018, 31 December 2019 and 30 September 2020

B7. Methodology and calculation of solvency positions of ZLIC under approximated HKIO basis

B8. Financial condition report of ZLIC for the years ended 2016, 2017, 2018 and 2019

B9. Risk management policy including, investment risk policy manual, foreign exchange risk policy manual, capital management risk policy manual, product development and pricing risk policy manual

B10. 2018 ZLIC reinsurance strategy

B11. Product development and pricing guidelines

ZLIC HK branch

B12. Certificate from the IA evidencing the classes of insurance business for which ZLIC is authorised to carry on in its Hong Kong branch

B13. Audited accounts and financial statements of ZLIC HK branch, for the years ended 2015, 2016, 2017, 2018 and 2019, and unaudited accounts of ZLIC HK branch as at 30 September 2020

B14. Appointed actuarial valuation reports of ZLIC HK branch for the years ended 2015, 2016, 2017, 2018 and 2019

B15. Fund structure of ZLIC HK branch before transfer

B16. Policyholder dividend policy of ZLIC HK branch

B17. Product specifications for major products of ZLIC HK branch

B18. Description of discretionary charges of unit-linked business of ZLIC HK branch

B19. Fund list for unit-linked business of ZLIC HK branch

B20. Particulars of options and guarantees

B21. Dynamic solvency testing report of ZLIC HK branch for the years ended 2015, 2016, 2017, 2018 and 2019

B22. History of dividend reduction to the original scales of product launch for traditional participating business of ZLIC HK branch

B23. History of crediting rate for universal life business

B24. Summary of cash surrender value basis

B25. Summary of reinsurance arrangements

B26. Details of tax computation of ZLIC HK branch for the years of assessment 2018/19

ZLIHK

B27. The latest application document to the IA for the authorisation for ZLIHK to carry out insurance business, including proposed organization chart showing the management and reporting lines of ZLIHK, financial projections and governance/management arrangements.

B28. Fund structure of ZLIHK after transfer

B29. Dynamic solvency testing report of ZLIHK, showing projected solvency positions during 2020 – 2022, with and without transfer

B30. Estimated solvency positions of ZLIHK as at 1 September 2021 before and after transfer

Others

B31. Solvency positions of ZIC under SST basis as at 31 December 2016, 31 December 2017, 31 December 2018 and 31 December 2019

B32. Other information and clarifications obtained through various email and telecommunication during the period of our assignment.

Appendix C Prudential Regulation Authority Handbook Section 2.27 to 2.40

C.1 INTRODUCTION

C.1.1. In this appendix I set out the guidance in PRA's Handbook Section 2 (The Prudential Regulation Authority's approach to insurance business transfers) on the form of a report on an insurance business prepared by an independent expert.

C.2 SCHEME REPORT

Section 2.27

C.2.1. Under section 109 of FSMA, a Scheme report must accompany an application to the court to approve an insurance business transfer scheme. This report must be made in a form approved by the PRA (following consultation with the FCA). The PRA would generally expect a Scheme report to contain at least the information specified in 2.30 below before giving its approval.

Section 2.28

C.2.2. When the PRA has approved the form of a Scheme report, the Scheme promoter may expect to receive written confirmation to that effect.

Section 2.29

C.2.3. There may be matters relating to the Scheme or the parties to the transfer that the regulators wish to draw to the attention of the independent expert. The regulators may also wish the report to address particular issues. The independent expert would therefore be expected to contact the regulators at an early stage to establish whether there are such matters or issues. The independent expert should form his own opinion on such issues, which may differ from the opinion of the regulators.

Section 2.30

C.2.4. The Scheme report should comply with the applicable rules on expert evidence and contain the following information:

- who appointed the independent expert and who is bearing the costs of that appointment;
- confirmation that the independent expert has been approved or nominated by the PRA;
- a statement of the independent expert's professional qualifications and (where appropriate) descriptions of the experience that makes them appropriate for the role;
- whether the independent expert, or his employer, has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest;
- the scope of the report;
- the purpose of the Scheme;
- a summary of the terms of the Scheme in so far as they are relevant to the report;
- what documents, reports and other material information the independent expert has considered in preparing the report and whether any information that they requested has not been provided;

- the extent to which the independent expert has relied on:
  a) information provided by others; and
  b) the judgment of others;
- the people on whom the independent expert has relied and why, in his opinion, such reliance is reasonable;
- their opinion of the likely effects of the Scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between:
  a) Transferring Policyholders;
  b) policyholders of the transferor whose contracts will not be transferred; and
  c) policyholders of the transferee;
- their opinion on the likely effects of the Scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the Scheme;
- what matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in their opinion, be relevant to policyholders' consideration of the Scheme; and
- for each opinion that the independent expert expresses in the report, an outline of their reasons.

Section 2.31

C.2.5. The purpose of the scheme report is to inform the court and the independent expert, therefore, has a duty to the court. However reliance will also be placed on it by policyholders, reinsurers, and others affected by the scheme and by the regulators. The amount of detail that it is appropriate to include will depend on the complexity of the scheme, the materiality of the details themselves and the circumstances.

Section 2.32

C.2.6. The summary of the terms of the Scheme should include:

- a description of any reinsurance arrangements that it is proposed should pass to the transferee under the Scheme; and
- a description of any guarantees or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred.

Section 2.33

C.2.7. The independent expert's opinion of the likely effects of the Scheme on policyholders should:

- include a comparison of the likely effects if it is or is not implemented;
- state whether they considered alternative arrangements and, if so, what;
- where different groups of policyholders are likely to be affected differently by the scheme, include comment on those differences they consider may be material to the policyholders; and
- include their views on:
  a) the effect of the Scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;

b) the likely effects of the Scheme on matters such as investment management, new business strategy, administration, claims handling, expense levels and valuation bases in relation to how they may affect:

   i. the security of policyholders' contractual rights;

   ii. levels of service provided to policyholders; or

   iii. for long term insurance business, the reasonable expectations of policyholders; and

c) the cost and tax effects of the Scheme, in relation to how they may affect the security of policyholders' contractual rights, or for long term insurance business, their reasonable expectations.

Section 2.34

C.2.8. The independent expert is not expected to comment on the likely effects on new policyholders, that is, (those whose contracts are entered into after the effective date of the transfer).

Section 2.35

C.2.9. For any mutual company involved in the Scheme, the report should:

- describe the effect of the scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders;
- state whether, and to what extent, members will receive compensation under the scheme for any diminution of proprietary rights; and
- comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between members with voting rights and those without.

Section 2.36

C.2.10. For a Scheme involving long term insurance business, the report should:

- describe the effect of the Scheme on the nature and value of any rights of policyholders to participate in profits;
- if any such rights will be diluted by the Scheme, describe how any compensation offered to policyholders as a group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders;
- describe the likely effect of the Scheme on the approach used to determine:

  a) the amount of any non-guaranteed benefits such as bonuses and surrender values; and

  b) the levels of any discretionary charges;
- describe what safeguards are provided by the Scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm;
- include the independent expert's overall assessment of the likely effects of the Scheme on the reasonable expectations of long term insurance business policyholders;

- state whether the independent expert is satisfied that for each firm, the Scheme is equitable to all classes and generations of its policyholders; and
- state whether, in the independent expert's opinion, for each relevant firm the Scheme has sufficient safeguards (such as principles of financial management or certification by the a with-profits actuary or actuarial function holder) to ensure that the Scheme operates as presented.

Section 2.37

C.2.11. Where the transfer forms part of a wider chain of events or corporate restructuring, it may not be appropriate to consider the transfer in isolation and the independent expert should seek sufficient explanations on corporate plans to enable them to understand the wider picture. Likewise, the independent expert will also need information on the operational plans of the transferee and, if only part of the business of the transferor is transferred, of the transferor. These will need to have sufficient detail to allow them to understand in broad terms how the business will be run.

Section 2.38

C.2.12. A transfer may provide for benefits to be reduced for some or all of the policies being transferred. This might happen if the transferor is in financial difficulties. If there is such a proposal, the independent expert should report on what reductions they consider ought to be made, unless:

- the information required is not available and will not become available in time for his report, for instance it might depend on future events; or
- he is unable to report on this aspect in the time available.

Under such circumstances, the transfer might be urgent and it might be appropriate for the reduction in benefits to take place after the event, by means of an order under section 112 of FSMA. The PRA considers any such reductions against its statutory objectives. Section 113 of FSMA allows the court, on the application of the PRA, to appoint an independent actuary to report on any such post-transfer reduction in benefits.

Section 2.39

C.2.13. The PRA expects the independent expert to provide a supplementary report for the final court hearing. Any supplementary reports will form part of the scheme report required to be produced under section 109 of FSMA and must also comply with 2.30–2.37.

Section 2.40

C.2.14. The purpose of the supplementary report is for the independent expert to provide an update on any relevant new information or events that have occurred since the date of the scheme report and to provide an opinion on whether they have affected the transfer. Matters that should be considered include, but are not limited to:

- the latest available financial information in respect of the transferor and transferee;
- any recent economic, financial or regulatory developments; and
- any representations made by policyholders or affected persons that raise issues not previously considered in the scheme report.

Appendix D Financial Conduct Authority Handbook SUP18.2.31G to 18.2.41G

D.1 INTRODUCTION

D.1.1. In this appendix I set out the guidance in FCA's Supervision Handbook section 2 of SUP 18 (Transfers of Business) on the form of a report on an insurance business prepared by an independent expert.

D.2 FORM OF SCHEME REPORT

SUP 18.2.31G

D.2.1. Under section 109 of the Act, a Scheme report must accompany an application to the court to approve an insurance business transfer Scheme. This report must be made in a form approved by the appropriate regulator. The appropriate regulator would generally expect a Scheme report to contain at least the information specified in SUP18.2.33G before giving its approval.

SUP 18.2.31AG

D.2.2. When the appropriate regulator has approved the form of a Scheme report, the Scheme promoter may expect to receive written confirmation to that effect from that regulator.

SUP 18.2.32G

D.2.3. There may be matters relating to the Scheme or the parties to the transfer that the regulators wish to draw to the attention of the independent expert. The regulators may also wish the report to address particular issues. The independent expert should therefore contact the regulators at an early stage to establish whether there are such matters or issues. The independent expert should form his own opinion on such issues, which may differ from the opinion of the regulators.

SUP 18.2.33G

D.2.4. The Scheme report should comply with the applicable rules on expert evidence and contain the following information:

- who appointed the independent expert and who is bearing the costs of that appointment;
- confirmation that the independent expert has been approved or nominated by the appropriate regulator;
- a statement of independent expert's professional qualifications and (where appropriate) descriptions of the experience that fits him for the role;
- whether the independent expert has, or has had, direct or indirect interest in any of the parties which might be thought to influence his independence, and details of any such interest;
- the scope of the report;
- the purpose of the Scheme;
- a summary of the terms of the Scheme in so far as they are relevant to the report;
- what documents, reports and other material information the independent expert has considered in preparing his report and whether any information that he requested has not been provided;

- the extent to which the independent expert has relied on:
  a) information provided by others; and
  b) the judgment of others;
- the people on whom the independent expert has relied and why, in his opinion, such reliance is reasonable;
- his opinion of the likely effects of the Scheme on policyholders (this term is defined to include persons with certain rights and contingent rights under the policies), distinguishing between:
  a) Transferring Policyholders;
  b) policyholders of the transferor whose contracts will not be transferred; and
  c) policyholders of the transferee;
- his opinion on the likely effects of the Scheme on any reinsurer of a transferor, any of whose contracts of reinsurance are to be transferred by the Scheme;
- what matters (if any) that the independent expert has not taken into account or evaluated in the report that might, in his opinion, be relevant to policyholders' consideration of the Scheme; and
- for each opinion that the independent expert expresses in the report, an outline of his reasons.

SUP 18.2.34G

D.2.5. The purpose of the Scheme report is to inform the court and the independent expert, therefore, has a duty to the court. However reliance will also be placed on it by policyholders, by reinsurers, by others affected by the Scheme and by the regulators. The amount of details that it is appropriate to include will depend on the complexity of the Scheme, the materiality of the details themselves and the circumstances.

SUP 18.2.35G

D.2.6. The summary of the terms of the Scheme should include:

- a description of any reinsurance arrangements that it is proposed should pass to the transferee under the Scheme; and
- a description of any guarantee or additional reinsurance that will cover the transferred business or the business of the transferor that will not be transferred.

SUP 18.2.36G

D.2.7. The independent expert's opinion of the likely effects of the Scheme on policyholders should:

- include a comparison of the likely effects if it is or is not implemented;
- state whether he considered alternative arrangements and, if so, what;
- where different groups of policyholders are likely to be affected differently by the Scheme, include comment on those differences he considers may be material to the policyholders; and
- include his views on:
  a) the effect of the Scheme on the security of policyholders' contractual rights, including the likelihood and potential effects of the insolvency of the insurer;

b) the likely effects of the Scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases in so far as they may affect:

   i. the security of policyholders' contractual rights;

   ii. levels of service provided to policyholders; or

   iii. for long term insurance business, the reasonable expectations of policyholders; and

c) the cost and tax effects of the Scheme, in so far as they may affect the security of policyholders' contractual rights, or for long term insurance business, their reasonable expectations.

SUP 18.2.37G

D.2.8. The independent expert is not expected to comment on the likely effects on new policyholders, that is, those whose contracts are entered into after the effective date of the transfer.

SUP 18.2.38G

D.2.9. For any mutual company involved in the Scheme, the report should:

- describe the effect of the Scheme on the proprietary rights of members of the company, including the significance of any loss or dilution of the rights of those members to secure or prevent further changes which could affect their entitlements as policyholders;
- state whether, and to what extent, members will receive compensation under the Scheme for any diminution or proprietary rights; and
- comment on the appropriateness of any compensation, paying particular attention to any differences in treatment between with voting rights and those without.

SUP 18.2.39G

D.2.10. For a Scheme involving long term insurance business, the report should:

- describe the effect for the Scheme on the nature and value of any rights of policyholders to participate in profits;
- if any such rights will be diluted by the Scheme, how any compensation offered to policyholders as group (such as the injection of funds, allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders.
- describe the likely effect of the Scheme on the approach used to determine:

  a) the amount of any non-guaranteed benefits such as bonuses and surrender values; and

  b) the levels of any discretionary charges;

- describe what safeguards are provided by the Scheme against a subsequent change of approach to these matters that could act to the detriment of existing policyholders of either firm;
- include the independent expert's overall assessment of the likely effects of the Scheme on the reasonable expectations of long term insurance business policyholders;

- state whether the independent expert is satisfied that for each firm the Scheme is equitable to all classes and generations of its policyholders; and
- state whether, in the independent expert's opinion, for each relevant firm the Scheme has sufficient safeguards (such as principles of financial management or certification by the a with-profits actuary or actuarial function holder) to ensure that the Scheme operates as presented.

SUP 18.2.40G

D.2.11. Where the transfer forms part of a wider chain of events or corporate restructuring, it may not be appropriate to consider the transfer in isolation and the independent expert should seek sufficient explanations on corporate plans to enable him to understand the wider picture. Likewise he will need information on the operational plans of the transferee and, if only part of the business of the transferor is transferred, of the transferor. These will need to have sufficient details to allow him to understand in broad terms how the business will be run.

SUP 18.2.41G

D.2.12. A transfer may provide for benefits to be reduced for some or all of the policies being transferred. This might happen if the transferor is in financial difficulties. If there is such a proposal, the independent expert should report on what reductions he considers ought to be made, unless either:

- the information required is not available and will not become available in time for his report, for instance it might depend on future events; or
- otherwise, he is unable to report on this aspect in the time available.

Under such circumstances, the transfer might be urgent and it might be appropriate for the reduction in benefits to take place after the event, by the means of an order under section 112 of the Act. Each regulator would wish to consider the fairness of any such reduction against its objectives and section 113 of the Act allows the court, on the application of either regulator, to appoint an independent actuary to report on any such post-transfer reduction in benefits.

Appendix E Dynamic Solvency Testing ("DST") Results and Assumptions

E.1 INTRODUCTION

E.1.1. In this appendix I present the DST results of ZLIC HK branch as well as the solvency position of ZLIHK under different scenarios.

E.2 SOLVENCY POSITION

Table E.1: Solvency position of ZLIC HK branch as at 31 December 2019

	2020 YE	2021 YE	2022 YE
Base Scenario	**579%**	**654%**	**727%**
Prescribed scenario 1	561%	638%	697%
Prescribed scenario 2	530%	559%	575%
Prescribed scenario 3	509%	521%	553%
Prescribed scenario 4	617%	804%	899%
Compound scenario 1 (More adverse scenario after termination of agency and threat of flu pandemic)	537%	607%	663%
Compound scenario 2 (Monetary tightening)	580%	717%	774%
Compound scenario 3 (Interest down and foreign exchange rates deteriorate)	454%	442%	471%
Additional plausible adverse scenario 1 (operational risk)	566%	744%	793%
Additional plausible adverse scenario 2 (counter-party risk)	532%	608%	670%
Additional plausible adverse scenario 3 (credit spread risk)	457%	541%	613%
Additional plausible adverse scenario 4 (COVID-19 scenario)	345%	315%	338%
Change from base scenario			
Prescribed scenario 1	-18%	-16%	-30%
Prescribed scenario 2	-49%	-95%	-152%
Prescribed scenario 3	-70%	-133%	-174%
Prescribed scenario 4	38%	150%	172%
Compound scenario 1 (More adverse scenario after termination of agency and threat of flu pandemic)	-42%	-47%	-64%
Compound scenario 2 (Monetary tightening)	1%	63%	47%
Compound scenario 3 (Interest down and foreign exchange rates deteriorate)	-125%	-212%	-256%
Additional plausible adverse scenario 1 (operational risk)	-13%	90%	66%
Additional plausible adverse scenario 2 (counter-party risk)	-47%	-46%	-57%
Additional plausible adverse scenario 3 (credit spread risk)	-122%	-113%	-114%
Additional plausible adverse scenario 4 (COVID-19 scenario)	-234%	-339%	-389%

Table E.2: Solvency position of ZLIHK

	1 Jan 2021	1 Jan 2022	1 Jan 2023
Base Scenario	9438%	**604%**	**532%**
Prescribed scenario 1	8320%	571%	476%
Prescribed scenario 2	8911%	516%	411%
Prescribed scenario 3	8714%	477%	388%
Prescribed scenario 4	8757%	709%	636%
Prescribed scenario 5	7154%	564%	467%
Prescribed scenario 6	10258%	623%	579%
Compound scenario 1 (Pandemic)	9629%	548%	462%
Compound scenario 2 (Monetary tightening)	5491%	590%	507%
Compound scenario 3 (Interest down and foreign exchange rates deteriorate)	8379%	368%	296%
Additional plausible adverse scenario 1 (operational risk)	8584%	647%	517%
Additional plausible adverse scenario 2 (counter-party risk)	9311%	561%	487%
Additional plausible adverse scenario 3 (credit spread risk)	9150%	500%	439%
Additional plausible adverse scenario 4 (COVID-19 scenario)	9792%	295%	218%
Change from base scenario *			
Prescribed scenario 1	-1119%	-33%	-56%
Prescribed scenario 2	-528%	-88%	-121%
Prescribed scenario 3	-725%	-127%	-144%
Prescribed scenario 4	-681%	105%	104%
Prescribed scenario 5	-2284%	-40%	-65%
Prescribed scenario 6	819%	19%	47%
Compound scenario 1 (Pandemic)	191%	-56%	-70%
Compound scenario 2 (Monetary tightening)	-3948%	-14%	-25%
Compound scenario 3 (Interest down and foreign exchange rates deteriorate)	-1059%	-236%	-236%
Additional plausible adverse scenario 1 (operational risk)	-855%	43%	-15%
Additional plausible adverse scenario 2 (counter-party risk)	-127%	-43%	-45%
Additional plausible adverse scenario 3 (credit spread risk)	-289%	-104%	-93%
Additional plausible adverse scenario 4 (COVID-19 scenario)	354%	-309%	-314%

* Change to base scenario as at 1 January 2021 is very sensitive as the denominator of solvency ratio calulation is very small, which is close to the minium solvency margin of HKD 2 million.

E.3 SUMMARY OF CRITICAL ASSUMPTIONS IN DST

E.3.1. The base scenario is based on a realistic set of assumptions for investment return, management expenses and new business sales used to project the financial position over the forecast period between 2020 and 2022 for ZLIC HK branch and ZLIHK.

E.3.2. For ZLIC HK branch, the starting point of the projection is 31 December 2019 and the opening assets, liabilities, net assets and solvency ratio are the actual 2019-year end statistics as at 31 December 2019.

E.3.3. For ZLIHK, the starting point of the projection is 1 January 2021 and the opening assets, liabilities, net assets and solvency ratio are in line with the business plan submitted to the IA for the ZLIHK license application in 2 January 2020, except for first projection year due to the update to reflect the delay of the Transfer Date to 1 September 2021.

E.4 SUMMARY OF SCENARIOS

E.4.1. The scenarios conducted under the DST results are as prescribed under the Guidance Note issued by the Actuarial Society of Hong Kong, with the aim to investigate the likely solvency of the companies under a range of adverse scenarios in the near future. Three compound scenarios and two additional plausible adverse scenarios are performed to identify the possible critical scenarios to the financial position.

E.5 DETAILED DESCRIPTIONS OF SCENARIOS

Prescribed scenario 1: deterioration in claims experience

- 15% deterioration in mortality and morbidity rates

Prescribed scenario 2: deterioration in persistency experience

- 5% change in lapse rates in whichever direction produces deteriorating results (a 5% subtraction from the original lapse rates).

Prescribed scenario 3: drop in interest rates, combined with a market crash

- 30% reduction in bond yields in all three projection years
- 25% reduction in equity values at first year with same growth rate as base scenario in the following 2 years

Prescribed scenario 4: rise in interest rates, combined with a market crash

- 30% rise in bond yields with plus 2% floor in all three projection years
- 25% reduction in equity values at first year with same growth rate as base scenario in the following 2 years

Prescribed scenario 5: high new business growth rates

- High growth throughout the forecast period, with growth rate being 30%, or 150% of plan growth rate if higher, and with a reasonable corresponding increase in expenses.

Prescribed scenario 6: low new business growth rates

- The sales growth rate is -20% in every projected year, while the expense will not change.

Compound scenario 1: pandemic

- 10% increase of expenses;
- First year mortality added by 0.15%
- 20% decrease in first year sales

Compound scenario 2: monetary tightening

- 300bps increase in interest yield curve;
- 50% increase in expenses in the first projection year;
- 30% drop in equity values in the first year.

Compound scenario 3: interest down and foreign exchange rates deteriorate

- 50% reduction in bond yields in all 3 projection years;
- 25% reduction in equity values at first year;
- 10% increase in sales of non-saving protection products;
- 10% deterioration in foreign exchange rates in year 1, and then the foreign exchange rates remain unchanged in the later years.

Additional plausible adverse scenario (operational incidents)

- HKD 5 million of fine at time 0;
- 10% addition in lapse rate in the first and second year for existing business and 30% drop in sales in first and second year for new business;
- Aggregate loss equal to 2.5% of unit-linked fund under management and 1% of non -linked fund under management;
- 20% increase of expense.

Additional plausible adverse scenario (counterparty default)

- Bond: Default on the corporate bond portfolio equivalent to 0.5% of the market value with 35% recovery rate, and a widening of 50bps for government bond spread with credit rating below AA- and all corporate bond spread;
- Reinsurance: Default of the most significant reinsurer in terms of business ceded

Additional plausible adverse scenario (credit spreak risk)

- Widening of 150bps for bonds of investment grade, and 250 bps for bonds of non-investment grade. Shock only applied on all corporate bonds and government bonds with credit rating below AA-

Additional plausible adverse scenario (COVID-19 scenario)

- 1.5% decrease in interest rate, 25% reduction in equity values in the first year with same growth rate as base scenario in the following 2 years,0.15% addition in the first year mortality and 20% reduction in first year sales.

Appendix F Description of Swiss Solvency Test ("SST")

Description of Swiss Solvency Test ("SST")

F1. SST is a comprehensive, economic and risk based solvency regime. The SST ratio is calculated as:

$$SST\ Ratio = \frac{Risk\ Bearing\ Capital - Market\ Value\ Margin}{Target\ Capital - Market\ Value\ Margin}$$

The entity is regarded as solvency when the SST Ratio is greater than 100% and insolvent if otherwise.

F2. Risk Bearing Capital minus Market Value Margin is similar to the concept of available capital in other solvency regimes. The Risk Bearing Capital represents the total economic capital available to cover unexpected extreme event before affecting policyholders. It is calculated as the market consistent value of assets minus best estimate value of liabilities plus other risk bearing items.

F3. Target Capital refers to the capital required to cover an unexpected extreme event over 1 year horizon, as calculated by the 99% expected shortfall. To calculate capital requirements, SST Opt-In standard model or approved internal models can be used to assess the corresponding risks. In 2017, ZLIC implements the SST Opt-In standard model, following the design principles and requirements described by FINMA.

F4. Market Value Margin represents the cost of holding required capital for insurance risk in run-off as prescribed in SST, calculated by multiplying the capital requirement by the cost of capital rate (prescribed 6%), discounted to valuation date and aggregated.

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ERRATUM

5 May 2021

From: Paul Sinnott

To: Zurich Life Insurance Company Ltd. and Zurich Life Insurance (Hong Kong) Limited

Report of the Independent Actuary on the Transfer of Business from the Hong Kong Branch of Zurich Life Insurance Company Ltd. to Zurich Life Insurance (Hong Kong) Ltd. (Full Report) and Summary of Independent Actuary's Report (Summary Report)

I have been appointed to act as the Independent Actuary pursuant to Section 24 of the Hong Kong Insurance Ordinance Chapter 41 (the "Ordinance"), to prepare aforementioned reports to provide an independent opinion on the terms and likely effects of the proposed scheme (the "Scheme") for the transfer of all long term insurance business carried on by Zurich Life Insurance Company Ltd. ("ZLIC") through its Hong Kong Branch ("ZLIC HK branch") (also hereinafter referred as "Transferring Business") to a new Hong Kong domiciled subsidiary of Zurich Insurance Holdings (HK) Limited ("ZIH"), which is wholly-owned by Zurich Insurance Company Ltd. ("ZIC"), namely Zurich Life Insurance (Hong Kong) Limited. ("ZLIHK").

This Erratum covers corrections to Table 6.4 on Page 36 of the Full Report and Table 3 on Page 7 of the Summary Report.

The revised Table 6.4 in Full Report and the revised Table 3 in the Summary Report are shown below. Only one change on the heading has been made in both tables, which has been highlighted.

This change does not change my opinion with regards to the effect on the Scheme/policyholders mentioned in the reports.

The reliances and limitations covering this Erratum are those set out in the reports.

Milliman

Table 6.4 in Full Report

Table 6.4: ZIC’s solvency ratios (on SST basis)

USD millions	Dec 2017	Dec 2018	Dec 2019**
Target capital	24,573	22,280	24,687
Risk-bearing capital	43,181	41,628	45,961
Solvency ratio*	**212%**	**225%**	**241%**

* Figures derived from this table may not be the same due to rounding.

**No updated information available after December 2019 as ZIC’s solvency ratio is only calculated annually.

Source: ZIC’s 2018 and 2019 Financial Condition Report.

Table 3 in Summary Report

Table 3: ZIC’s solvency ratios (on SST basis)

USD millions	Dec 2017	Dec 2018	Dec 2019**
Target capital	24,573	22,280	24,687
Risk-bearing capital	43,181	41,628	45,961
Solvency ratio*	**212%**	**225%**	**241%**

* Figures derived from this table may not be the same due to rounding.

**No updated information available after December 2019 as ZIC’s solvency ratio is only calculated annually.

Source: ZIC’s 2018 and 2019 Financial Condition Report.