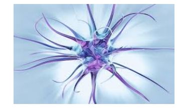

# Centriq Life

## REPORT OF THE HEAD OF ACTUARIAL FUNCTION

## on
## The effect of the proposed transfer of long-term insurance business
## from
## Shoprite Insurance Company Limited
## to
## Centriq Life Insurance Company Ltd

29 June 2021

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# 1 Introduction

## 1.1 Background

Shoprite Insurance Company Limited ("Shoprite Insurance") is a public company as defined in the Companies Act and a registered Short term insurance Company under the Short Term Insurance Act (of 1998). Shoprite Insurance is a wholly owned subsidiary of Shoprite Holdings. It writes inter alia Credit Life insurance policies to a niche market of customers of the Shoprite group inside South Africa, and also acts as a reinsurer to Credit Life policies underwritten in a number of African countries outside of South Africa.

As a result of the classification of the short-term and life insurance segments as specified under the Insurance Act of 2017 ("the Act"), some of the lines of business written by Shoprite Insurance, specifically the Credit Life and inwardly reinsured Credit Life business described above, needs to be transferred to a Life Insurance Company approved under the Act. The Life insurer deemed suitable for this transfer is Centriq Life Insurance Company (hereinafter referred to as "Centriq Life").

## 1.2 Purpose of this report

The purpose of this report is to outline the effect of the proposed transfer, in terms of Section 50 of the Insurance Act of 2017 ("the Act") of the long-term insurance business of Shoprite Insurance to Centriq Life.

This report documents my review of the proposed transfer, considering the likely effect on the policyholders of Centriq Life to which Life insurance policies will be transferred, as well as considering whether the transaction is actuarially sound for those policyholders that are transferring.

- This is done by considering the appropriateness of the liability calculation and the value of the transfer to be made, the capital requirement implications on Centriq Life, and the solvency coverage ratio for Centriq Life, before and after the proposed transfer; and

- Whether, or otherwise the extent to which, the reasonable benefit expectations of all policyholders currently within Centriq Life and those proposed to transfer into Centriq Life, are not adversely affected.

## 1.3 Intended Audience

This report is addressed to the Prudential Authority of South Africa. It is also understood that it will form part of the proposed Scheme of Transfer and may be considered by the affected policyholders, the Board of Directors and management of Centriq Life.

## 1.4 Qualifications

This report has been prepared by the HAF of Centriq Life (Alexander Roux). I am a Fellow of the Actuarial Society of South Africa with a Practising Certificate that qualifies me to undertake assignments within the Life insurance industry such as this.

## 1.5 Disclosure and Clarification

The business being transferred is a specified section of the policies underwritten within Shoprite Insurance Limited that writes inter alia Credit Life insurance policies, as well as inwardly reinsure Credit Life business from a number of African countries outside of South Africa. Not all the business is being transferred to Centriq Life, only the business that is deemed to be classified as Life insurance in terms of the segmentation of classes of insurance in the Act. It is however understood that the short-term insurance products written by Shoprite insurance will also be transferring and that Shoprite Insurance will cease to continue as a registered insurance company. While consideration should be given by the Prudential Authority to the affected short term insurance policyholders, this falls outside the scope of this report.

The business will be transferred to a new cell of Centriq Life that commenced on 1 July 2020. This cell is constituted as a preference share arrangement between Shoprite Checkers and Centriq Life. Shoprite Checkers, will remain responsible for the day-to-day operations of the business being transferred as well as the marketing and administration of the business being transferred, before and after the transfer.

While it is important to ensure the safeguard of policyholders' interest subsequent to the intended transfer, for all policyholders concerned, due to the fact that no benefits of either insurer is of a discretionary nature, none of these safeguards to any of the subsets of the policyholders, are achieved at the expense or detriment of the other.

## 1.6 Legislation and Guidance

In preparing this report I have been guided by the following:

- the terms of reference outlined in the Insurance Act (of 2017), and specifically Section 50, as issued in the Republic of South Africa;

- the Prudential Standards ("GOI 6") issued by the Prudential Authority of the South African Reserve Bank, which provides a framework for the governance and operational standards for Insurers. Specifically, GOI6 covers the Transfers of Business by insurers;

- the Actuarial Practice Note 108 ("APN108") on the Transfer of Long-term Business of a registered insurer; and,

- the Actuarial Practice Note 106 ("APN106"), which provides general guidance to the Head of Actuarial Function for South African Insurers.

# 2 Overview of the Transfer

## 2.1 Motivation for the transfer

As a result of the new Insurance Act of 2017 ("the Act") becoming effective in 2018, certain classes of insurance that were historically written on short term insurance licences have to be transferred to long term insurance licences. Since this transfer is a requirement given the definition of segmentation of classes in the Act, the motivation for this decision is not within the scope of this report. The transferee company had been identified as Centriq Life Insurance Limited (hereinafter referred to as Centriq Life). The purpose of this report is to consider and present the views of the Head of Actuarial Control on the soundness of the proposed transfer of business to Centriq Life.

## 2.2 Business affected by the transfer

Shoprite Insurance currently underwrites the business while the retail business, Shoprite Checkers, intermediates the Credit life insurance policies on behalf of Shoprite Insurance. The risks underwritten include:

- Natural death cover;
- Permanent Total disability cover;
- Temporary total disability cover; and,
- Retrenchment Cover.

The above risks all form part of the class Credit Life as defined in the Act and the description of the risks covered under each is therefore not repeated here.

The Credit Life insurance products to be transferred are written in South Africa. In addition, Shoprite Insurance also currently acts as a reinsurer on credit life insurance business that are distributed through Shoprite Checkers branches in the following countries: Eswatini, Botswana, Lesotho, Mozambique and Zambia. It is the intention of Shoprite Insurance that these lines of business will be inwardly reinsured by Centriq Life from the same effective date as the transfer of the South Africa Credit Life business.

All the Credit Life policies, both the directly insured originating from South Africa, and the inwardly reinsured business from outside South Africa, comprises of the four insured events listed above. The contracts with the policyholders will remain unchanged as a result of the intended transfer.

Shoprite Insurance also intends to transfer its Short-term insurance business to Centriq Insurance Company and consequently cease to operate as a registered insurer, which is beyond the scope of this report.

As at 30 June 2020 the number of South African credit life policies contemplated for the transfer is approximately 104,741. The death, disability and temporary disability benefits are lumpsum amounts equal to the amount payable to settle the remaining outstanding debt at the time of the claim event. For the retrenchment cover the credit instalments are waived up to a maximum of 12 months unless the claimant is reemployed prior to that.

The average lumpsum benefits payable is R7,800, while the average cost of the retrenchment cover for all payments waived while not being employed is approximately R3,000.

As is shown in Section 3 below, the new cell within Centriq Life, through a preference share arrangement between Shoprite Checkers and Centriq Life, is expected to be viable and a self-sustaining business venture, given the volume of business transferring as well as the future growth expected in this cell. More generally, the Transferee company will remain a sufficiently solvent going concern as a whole, in order to support the benefits and security of its entire portfolio subsequent to the transfer.

## 2.3 Mechanics of the transfer

### 2.3.1 Effective Dates

The actual transfer, pending approval, is intended to take place prior to the financial year-end of Centriq Life, which is 31 December 2021. Shoprite Insurance will remain responsible for the policies until approval in terms of the transfer agreement.

Centriq Life will become responsible for all valid claims from this date onwards. This includes claims with event dates prior to the date of transfer. Therefore, if a claim arises before the closing date, and is only notified after the closing date, such a claim will become the liability of Centriq Life.

### 2.3.2 Administration

All policyholders will continue to be serviced by Shoprite Checkers who will act as the binder holder and intermediary of Centriq Life.

Shoprite Checkers will continue to collect premiums on behalf of Centriq Life in respect of the life insurance contracts that will be transferred and will continue to be administered by the same system and same owners of that system. There will therefore be no administrative disruption to the business as a result of this intended transfer.

As per Section 6.3 of the Transfer agreement, upon implementation of the Transactions, the instalment amount collected monthly will remain unchanged notwithstanding the reduction of the premiums in terms of the Life Policies in respect of the VAT charge. The component of the VAT charge previously paid in terms of the Life Policies will be treated as an early payment of the debt due in terms of the credit agreement, as contemplated in section 126 of the National Credit Act, 34 of 2005.

### 2.3.3 Branding

The branding (white labelling) of policies will remain the same after the transfer. However, as required by legislation, the communication to policyholders will make it clear that there is a change in underwriter of the policies transferring.

## 2.4 Tax and transfer costs

### 2.4.1 Tax

There will be no loss of value to policyholders resulting from the transfer or as a result of associated expenses, undervaluation of assets and/or the fairness of the split of assets between policyholders' funds and shareholders' funds. There will also be no additional capital gains tax emanating from the transfer of assets or liabilities.

### 2.4.2 Transfer Costs

Based on the transfer agreement between the parties, all costs incurred in support of the intended transfer will be treated as stipulated in that agreement and are therefore not repeated here. However, no fees will be charged to the policyholders as a consequence of the transfer.

# 3 Policyholder Security

## 3.1 Financial strength of Centriq Life Pre- and Post-transfer

As required by the Actuarial Practice Note 106 (APN106) as issued by the Actuarial Society of South Africa, I have considered the impact of the proposed transfer on Centriq Life, on the Prudential Supervision Reporting basis as well as the impact on the Published basis.

This report specifically considers the financial results of the Transferee Company (Centriq Life) Pre- and Post- the transfer. The protection of the policies not transferring is considered in a separate report for submission to the Prudential Authority.

A cell have been created through a preference share arrangement between Shoprite Checkers and Centriq Life. The impact of the transfer on the results of the assessment of the new Centriq Life Shoprite cell as at the effective date of the transfer, 30 June 2020, is shown in the table below.

| **Centriq Life Shoprite Cell** | **Prudential Supervisory Reporting Basis ('000)** | |
|---|---|---|
| | **Pre-Transfer** | **Post-Transfer** |
| Best Estimate Liabilities | 0 | 37,651 |
| Risk Margin | 0 | 341 |
| Other Liabilities | 0 | 2,752 |
| Total Assets | 0 | 44,628 |
| **Basic Own Funds** | **0** | **3,884** |
| Own Funds available to Cover SCR | 0 | 3,884 |
| Solvency Capital Requirement | 0 | 6,026 |
| **SCR Cover Ratio** | **0.00 X** | **0.64 X** |

For the newly formed Shoprite cell, as at the effective date of 30 June 2020, the coverage ratio subsequent to the transfer as is 0.64. Where the solvency coverage ratio for a particular cell is less than one, the difference between the available own funds and the solvency capital requirement is supported by the Promoter cell. This reduces the eligible own funds when considering the SCR coverage ratio of the statutory entity, which is shown in the table below).

In addition, as stipulated in the preference share arrangement with Shoprite Checkers, the latter will be required to further capitalise the business if so required, which will depend on the coverage ratio as at the actual date of transfer, once approved by the PA. Between the effective date of 30 June 2021 and the actual date of transfer, it is expected that the profits retained in the cell, driven in part by the new business that is being written into the cell since 1 July 2020, will be more than sufficient to address the coverage ratio requirements as set by the board for cells.

The impact of the transfer on the results of the assessment of Centriq Life statutory entity (with all cells combined including the Promoter cell), as at the effective date of the transfer, 30 June 2020, are shown in the table below.

| Centriq Life Statutory Entity impact | Prudential Supervisory Reporting Basis ('000) | |
|---|---|---|
| | Pre-Transfer | Post-Transfer |
| **Assets** | **317,840** | **362,467** |
| Best Estimate Liabilities | (1,513,386) | (1,475,736) |
| Risk Margin | 71,031 | 71,372 |
| Other Liabilities | 549,718 | 552,471 |
| **Total Liabilities (TPs & Other)** | **(892,637)** | **(851,893)** |
| | | |
| **Own Funds** | **1,210,477** | **1,214,361** |
| **Own Funds Eligible to meet the SCR** | **464,886** | **468,770** |
| Solvency Capital Requirement | 440,530 | 446,206 |
| Minimum Capital Requirement | 148,569 | 151,239 |
| **SCR Cover Ratio** | **1.06 X** | **1.05 X** |
| **MCR Cover Ratio** | **3.13 X** | **3.10 X** |

The impact of the transfer on the results of the assessment of Centriq Life as reported on the Published Reporting basis, and therefore as it appears in the annual financial statements, as at the effective date of the transfer, 30 June 2020, is shown in the table below:

| Centriq Life Statutory Entity impact | Published Reporting Basis ('000) | |
|---|---|---|
| | Pre-Transfer | Post-Transfer |
| **Total Assets** | **1,049,045** | **1,115,945** |
| Technical Provisions | 112,162 | 176,309 |
| Reinsurance Contract Liability | 20,119 | 20,119 |
| Cell Owners Interest | 534,469 | 534,469 |
| Other Liabilities | 355,954 | 358,706 |
| **Total Liabilities** | **1,022,704** | **1,089,603** |
| | | |
| **Net Asset Value** | **26,341** | **26,341** |

### 3.1.1 Solvency of the Transferee Company – Centriq Life

As can be seen from the above tables, the SCR and MCR cover of Centriq Life (the Transferee company) post-transfer is financially sound at a ratio of 3.10 and 1.05, respectively.

When the business is transferred in, the resulting solvency coverage ratio of the newly formed cell is 0.64, as shown in the first table above. Since the cell is in a shortfall, Centriq Life as cell captive provider has to provide for this from the excess own funds in the Promoter cell. This has a marginal impact on the solvency coverage ratio of the statutory entity as shown in the second table above from 3.13 to 3.10. However, if the cell had excess own funds over and above the amount required to cover the SCR in the cell, this would not have been taken into consideration when considering the solvency of the statutory entity. For this reason, the SCR ratio appear low at statutory entity level. However, considering the solvency levels of each individual cell, this remains a solvent entity operating well within the risk appetite framework as set by the board.

The assets contemplated in the transfer is R 66,900,000 (as reflected in the change in the total assets on the Published Reporting basis from 1,049,045,000 to 1,115,945,000). This is inclusive of deferred acquisition costs of R 22,272,000. On the Prudential Supervisory reporting basis, the increase in assets as a result of the transfer is R 44,628,000 (from 317,840,000 to 362,467,000), which is net of the deferred acquisition costs. The difference in the impact of the liabilities on the two bases is reflective of the deferred acquisition costs, as well as the difference in the valuation margins required for published reporting purposes.

The business being transferred is for contract terms equivalent to the underlying credit agreements, which is up to a maximum of 60 months. The business is written on profitable terms, and given the pricing basis is expected to remain profitable, even under strained risk claims scenarios given the Covid19 pandemic.

The actuarial and claims liabilities considered and determined for this transfer are as follows:

For the South Africa and Foreign business:

- the 'Incurred-But-Not-Reported' claims reserves (IBNR claims);
- the Outstanding claims reported (OCR claims) (for the South Africa and Foreign business);

For the South African business:

- the Discounted Cashflow reserves for the remaining term of policies;

For the Foreign business:

- the Unexpired Risk component since the foreign business is written as single premium credit life policies.

The transferee company will become responsible for all claims intimated as from the date of transfer, as well as prior to the date of transfer. The claims intimated prior to the date of transfer is represented by the IBNR and OCR claims. The claims intimated subsequent to the date of transfer for the foreign business is represented by the unexpired risk reserves. For the South African business this is represented by the premiums being charged which are sufficient to cover the costs of claims and expenses to be incurred from the date of transfer.

For the South African business, claims intimated subsequent to the date of transfer is therefore not reserved for. I.e., it excludes the discounted cashflow reserves. The reason for this is because these reserves will result in a negative liability, due to the profits expected to emanate from the future premiums, less claims and expenses. It is prudent that this negative liability is not considered as part of the transfer, as it would imply that the future profits expected to emanate from the business is funded for by the transferee company. It is therefore more appropriate for the profits to materialise over time within the cell into which these future profits will be generated.

Based on the above, I am satisfied that the solvency of Centriq Life on the Prudential Supervision Reporting basis post-transfer will not adversely affect the financial security of the policyholders transferring into this licence nor those that had been policyholders of the transferee company prior to the proposed transfer.

### 3.1.2 Capital Requirements in the Transferee Company

As stated above, the cell that the business will be transferred into is a new cell that will be owned by Shoprite Checkers through a preference share arrangement. The Solvency Capital Requirements in this cell is based on all the business underwritten, including the business being transferred. As stated earlier in this report, the business as managed in the transferor has historically been profitable. The capital that is required for the new cell to be solvent is included in the asset side of the new cell as shown in the first table as shown in Section 3.1 above.

### 3.1.3 Liquidity of the Transferring and Transferee Companies

The historic profitability of the business being transferred have consistently shown a strong positive cashflow. Given the positive cashflow expected, under a reasonable range of scenarios, it is not expected that the cell will need additional cash to be able to meet the commitments under the business being transferred in addition to the assets contemplated of the transfer.

It is also my opinion that any stretched scenario of experience that may result in negative cashflows at any point in time within the business being transferred can be adequately compensated for by the Transferee company subsequent to the transfer. There is therefore no concern over the liquidity requirements, either within the new cell being constituted, nor for the remaining policyholders in the transferring company.

#### 3.1.4 Asset management

The management of the assets backing the transferring policies will change subsequent to the transfer, and will be performed by the asset management function of the Transferee company. The principle being followed is to retain sufficient liquidity of the retained profits for either dividend payments or other liquidity management needs within the cell. This is consistent with the manner in which assets had been managed thus far in the Transferring company.

#### 3.1.5 The ORSA

The given that the nature of the transfer and the impact it will have on the financial soundness of Centriq Life, it is not expected to be material. Therefore, it is the view of the HAF that no out-of-cycle ORSA process will be required as a result of the intended transfer.

# 4 Policyholder Reasonable Expectations and Principles of Financial Management Post-transfer

## 4.1 Transferring Policyholders

Actuarial Guidance requires the HAF to specifically consider the following items with respect to the transferring policyholders:

### 4.1.1 Terms and Conditions

The management of both the transferor and transferee has confirmed that the only terms and conditions of the policies in question that will change are those required to ensure they are compliant to the Policyholder Protection Rules within the Long-Term Insurance Act of 1998 (as amended). Since these changes were compulsory, to comply with the policyholder protection rules, no comment is provided on the fairness of these changes.

### 4.1.2 Policy Servicing and Maintenance

As discussed, in Section 2.3.2 of this report, the policies affected by the transfer are currently serviced by Shoprite Checkers who will continue to act as the binder holder and intermediary of Centriq Life. Shoprite Checkers will also continue to collect premiums on behalf of Centriq Life in respect of the life insurance contracts that will be transferred. There will however be a reduction in the amount collected from policyholders as VAT is not chargeable on the premiums payable for the life benefit.

### 4.1.3 Correspondence

The communication responsibilities towards policyholders had historically been serviced by Shoprite Checkers. This will remain their responsibility. Therefore, the manner of correspondence with policyholders will remain the same after the transfer.

### 4.1.4 Premiums and Benefits

Since the policies will transfer on their same terms and conditions, there will be no change to benefits provided or fees charged.

### 4.1.5 Investment policy and Asset-Liability matching

To the extent that cash will be retained within the cell in the transferee company, Centriq Life, these funds will be invested in a pool of liquid money market instruments managed by Centriq Life. Since the policies overall generate negative liabilities, the cash held in the cell will be generated from the expected positive cashflows in the business and will be retained to the extent necessary for liquidity purposes. Therefore, the investment requirements will remain to be liquid assets.

### 4.1.6 Minimum Solvency Requirements

As demonstrated in Section 3, the post-transfer solvency position of Centriq Life, on the Prudential Supervision Reporting basis, is strong both before and after the intended scheme of transfer. Therefore, the proposed transfer will not have an adverse impact on the security of the transferring policyholders. The Solvency position of the transferor company after this intended transfer will become irrelevant as the licence will be deregistered and no policies will remain.

## 4.2 Communication plan

A comprehensive communications plan has been developed that will ensure that policyholders are provided with the necessary information relating to the transfer of their policies to Centriq Life as well as those not transferring. Additionally, since the entity responsible for the administration of the policies, the Shoprite Checkers does not change, policyholders will continue to contact the same people for information on their policies. Shoprite Checkers will continue to act as binder holder and intermediary, but as a binder holder to Centriq Life, while Shoprite Insurance will be deregistered.

As part of the review by the HAF in preparing this report, the communication plan was provided. The communication plan consists of the following:

1. A formal notice in the national newspapers;

2. The websites of the Parties will be used to display information about the Transfer as well as a complaints and information request email address which will respond to all queries;

3. The call centre of Shoprite Checkers will be made available with effect from the first date of publication of the Formal Notice to answer queries of Affected Policyholders in accordance with a prescribed script that is detailed in the Communication Plan.

   All enquiries and complaints submitted to the call centres will be submitted to the Head of the Internal Audit Control Function of Shoprite Insurance in the case of the Shoprite Insurance call centre and to the Head of the Internal Audit Control Function of Centriq Life. All calls will also be recorded. The telephone details of both Shoprite Insurance and Centriq Life will be included should a policyholder wish to contract Centriq directly.

Each of these methods of communication is described in detail in the Communication Plan.

For the reasons mentioned in the Communication Plan, Shoprite Insurance does not intend publishing the Formal Notice in the Government Gazette.

Shoprite Checkers will implement the communication plan, and will be overseen by both Shoprite Insurance and Centriq Life. The Shoprite Checkers call centre and contact details used, will be for both the Short-term insurance business intended to be transferred into Centriq Insurance, and the Centriq Life policies intermediated by Shoprite Checkers. However, policyholders will also be able to contact Centriq Life directly at its head office telephone number.

# 5 Alternatives to the proposed Scheme of Transfer

This transfer of the specified business was compelled due to the fact the Act does not permit the Life insurance to be written on a Non-life (short term) insurance licence. This was permitted under the previous regulatory framework. Given the size of the Shoprite Insurance business, it would not be commercially viable or practical for it to be written on to a new Life insurance licence. There is therefore no alternative to the transfer being performed other than the closure of the future new business from the sources that generate the business, which is required to be transferred. Therefore, no alternative is being contemplated in this report.

# 6 Conclusions

I am satisfied that the information provided in the process of completing this report was relevant, reliable, complete and of sufficient detail in order to make the assessment and draw the conclusions required for this report.

Based on the review performed as detailed in this report, it is my opinion as the Head of the Actuarial Function of Centriq Life (the Transferee company) that:

- the proposed transaction is actuarially sound;
- the security of policyholders transferring to Centriq Life as well as the existing policyholders of Centriq Life is adequately safeguarded;
- the reasonable benefit expectations of policyholders are not adversely affected; and,
- the nature of the transfer and the impact it will have on the financial soundness of Centriq Life will not be material and therefore no out-of-cycle ORSA should be required as a result of the intended transfer.

I would like to express our gratitude to the staff and management of both Shoprite Insurance (the Transferring company) and that of Centriq Life (The Transferee company) for their assistance and support during the preparation of this report.

Alexander Roux
FASSA
Head of Actuarial Function
Centriq Life Insurance Limited

29 June 2021

# Appendix A: Data sources

In addition to the model results and detailed policy data and analyses, the following data sources were used:

- Audited annual QRTs as at 31 Dec 2020 for Shoprite Insurance and Centriq Life;
- Annual qualitative return template for both the Shoprite Insurance and Centriq Life;
- Shoprite Insurance and Centriq Life pro-forma QRT in respect of Statements OF1 and OF2 as presented in this report;
- Shoprite Insurance and Centriq Life Audited Annual Financial Statements as at 30 June 2020, i.e., on the effective date and not on the closing date.