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Where an actuary makes a report to the PPB stating that in his view the benefit or benefits payable under a policy are excessive and recommends that such benefit should be treated as reduced or disregarded, the PPB may determine that the benefit be treated as reduced or disregarded for those purposes, and the benefit shall be cancelled (Section 12 and 17(5) of the PPA).

If the PPB is required to step in to protect policyholders, the funds required to meet the liabilities to policyholders will be raised through a levy on authorised insurance companies carrying on long term business.
The levy on a contributor is currently confined to 1% of its net premium income in the previous year (Section 21(4) PPA).

The PPB would take an assignment of the claims of the policyholder against the company in liquidation or insolvency and become a creditor in place of that policyholder.

1 Introduction

The purpose of this document is to:

- supplement the *Proposed Compromise* document;
- present the background to the issues faced by the Society in managing its liabilities under guaranteed annuity rate (GAR) policies and resolving potential claims arising out of the failure of the Society to anticipate the judgment of the House of Lords (see Section 1.2 below) and inform non-GAR policyholders of the cost of GARs;
- demonstrate the business case for the proposed solution (a compromise to be implemented through a Scheme of Arrangement under Section 425 of the Companies Act);
- outline the solution in the context of the legal opinions obtained by the Board from Gabriel Moss QC about the structure and content of the scheme and Nicholas Warren QC about possible claims by non-GAR policyholders against the Society;
- explain how the proposed solution will be implemented; and
- discuss the alternative options if there is no compromise.

The solution which the Society is proposing is essentially a compromise with three linked aspects, which are:

- compensation for loss of GAR rights;
- compensation for a waiver of potential claims by non-GAR policyholders who were not told of the cost of GAR policies;
- A waiver by GAR policyholders of potential claims for loss arising out of the claims of non-GAR policyholders.

Parts I and II discuss these aspects.

Part III discusses the implementation of the compromise and Part IV the options open to the Society if there is no compromise.

A list of statutory provisions and a glossary of terms referred to in this document is at Appendix A.

Appendix D – Note on the role of the Policyholders' Protection Board

The following is a summary of the main powers and duties of the PPB.

The Policyholders' Protection Board (PBB) is a statutory body set up under the Policyholders Protection Act 1975 (PPA) to protect policyholders in the event of the insolvency or liquidation of an insurance company.
In the case of any long term business, the PPB will secure 90% of the amount of any liability of a company in liquidation towards any policyholder under the terms of a long term policy which was a United Kingdom policy at the beginning of the liquidation as soon as reasonably practicable after the beginning of the liquidation (Section 10(2) of the PPA).

It is the duty of the PPB to make arrangements for securing continuity of insurance for policyholders.

There are a number of provisions in Section 11 of the PPA which allow the PPB to take appropriate measures for securing or facilitating the transfer of the long-term business to another authorised insurance company.

The PPB will also secure that policyholders will receive 90% of future benefits in relation to a long term policy, a future benefit being defined as one which has "not fallen due to be paid by the company before the beginning of the liquidation". A bonus provided for under a policy shall not be treated as a future benefit (as defined) unless it was declared before the beginning of the liquidation (Section 11(9) of the PPA).

If it is not reasonably practicable to secure continuity of insurance the PPB is under an obligation to pay 90% of the value attributed to a policy by the liquidators and admitted in the winding-up.

The PPB can also make payments to policyholders in the event of a provisional liquidation, where winding-up proceedings have been commenced on the basis of its inability to pay debts, or an application made to the court for the sanctioning of a scheme of arrangement under Section 425 or the Companies Act and the terms of the compromise or arrangement provided for reducing or deferring payment of the liabilities or the benefits provided for under any policies (Sections 15 and 16 of the PPA).

The PPB would also be allowed to take other measures for the purpose of safeguarding policyholders but this would involve the PPB imposing, as a prerequisite of their assistance, the reduction of all liabilities of the long-term business to 90% of the amount which would otherwise have been payable in accordance with the terms of the policies and also an equivalent reduction in the level of all premiums (Section 17(2) PPA).

Pre-1975 Retirement Annuity

Retirement Annuity policies issued before October 1975 are entitled to the 'flexible' form of GARs, but the GARs are 20% to 30% lower than the GARs for 'flexible' GAR policies issued subsequently depending on age and the form of the annuity. At 31 December 2000 there were 708 policies in force across a range of ages from 45 to 75. As this was too small a population of policies to provide a meaningful set of allocation results by age, the appropriate results have for pre-October 1975 Retirement Annuities been calculated by adjusting the results for 'flexible' GAR policies issued from October 1975 taking account of the extent to which the levels of GARs are different for these two groups of policies (as described at the beginning of this section).

Results

The results of the apportionment of the £1.06 billion GAR compensation were calculated for fixed GAR and flexible GAR policies separately (i.e. due to different legal entitlements at retirement) and, within those groups, by age. For each age within each type of GAR policy (i.e. 'fixed' or 'flexible') the amount apportioned to that group of policies was divided by the total of the post 16 July 2001 values for the same policies so as to express the amount apportioned as a percentage of Policy Values.

For fixed GAR policies the results varied very little with age (almost entirely within a range of 18.5% to 19.5%) and there was no significant trend. The average uplift was 19%. The Society therefore recommends a 19% uplift for fixed GAR policies before adjustments for non-GAR claims and the Halifax £250 million.

For flexible GAR policies there was a clear trend in the results which showed an increase in the potential future value of the GAR benefits up to ages 53 and 54 and a decline in value thereafter. The average modelled outcome was 23% before adjustments for non-GAR claims and the Halifax £250 million.

The progression of the results by age was not entirely smooth due to small differences in policyholder behaviour during 2000. The results were smoothed using statistical techniques.

PART I – THE GAR COMPROMISE

1.1 Background

Between 1957 and 1988 most of the Society's new pensions policies included the right to use the fund built up to buy a pension on guaranteed terms. Under these terms, when interest rates are high, policyholders can buy annuities on the open market or from the Society, and when interest rates are low they can buy annuities from the Society more advantageously using their GARs. The Society believed at that time that these policies provided a minimum guaranteed level of cash benefit and a minimum guaranteed level of annuity to protect policyholders against very low or very high interest rates. It believed that, in times of normal interest rates, bonus rates could be adjusted to avoid either of these guarantees causing significant cost to the with-profits fund.

The level of annuity that may be acquired by a policyholder on retirement is calculated by reference to interest rates and life expectancy derived from mortality tables. Open market annuity rates fall when interest rates fall. Similarly, open market annuity rates fall if life expectancy improves. The Society's guaranteed annuity rates were fixed by reference to assumptions as to both interest rates and life expectancy. Consequently, actual interest rate fluctuations affect the extent to which GARs are more or less valuable than current annuity rates. In addition, the mortality table used in the GAR policies has been superseded as people live longer and, therefore, receive the annuity for longer. Unlike the Society's GARs, current annuity rates offered by the Society and other annuity providers are calculated by reference to up- to-date mortality tables which assume that annuitants live for significantly longer than was assumed when the guaranteed annuity rates were calculated for the GAR policies.

GARs, in most cases, are now significantly more attractive than open market annuity rates. This has the effect that they are expensive for the Society to provide. However, some GARs, due to the restrictive nature of the benefits provided, may be unattractive to policyholders despite the high guaranteed annuity rate.

Most GAR policies also include the right to pay premiums of variable amount into the policies (subject to Inland Revenue limits) up to the point of retirement.

The last policy containing a GAR was sold in 1988.

In late 1993 annuity rates fell below those guaranteed in most GAR policies. The Society declared final bonuses so that the value of total benefits, including the value of the guaranteed annuity, was broadly equal to each policy's notional share of the with-profits fund, known as 'asset share'. With lower annuity rates, the option to take a pension at the guaranteed annuity rate had significant value. If a policyholder chose not to take the GAR option, preferring the flexibility of an alternative option, then the benefits were of lower value. The Society believed that asset share should be delivered whichever option was selected. This led to a lower rate of final bonus for policyholders taking the GAR option than for those not using the option. This was known as the differential final bonus policy.

In September 1998 a number of complaints surrounding the differential final bonus policy were made to the PIA Ombudsman. Some policyholders believed that the Society's stance was unlawful. An action group was formed to oppose the Society. The Society instigated a 'representative action' in the High Court to resolve the issue.

1.2 Impact of the House of Lords' decision

The representative action was designed to establish if it was lawful to pay different final bonuses to GAR policyholders depending on whether or not those policyholders exercised the right to take their benefits in annuity form at a rate guaranteed by the Society.

At first instance the High Court held that in applying the differential final bonus policy, the Society's Board had exercised its discretion as to final bonuses in a legally permissible manner. The representative policyholder appealed the decision to the Court of Appeal. The Court of Appeal determined by a majority that it was not lawful to differentiate in this way within the group of GAR policyholders. It decided that a GAR policyholder should receive the same proportionate final bonus irrespective of the form of benefits selected. The Court did not, however, decide that it was unacceptable for the Society to differentiate between GAR and non-GAR policyholders in this respect, so still allowing any cost of the GARs to be 'ring-fenced' to those policyholders with GAR policies. The Society appealed the decision to the House of Lords.

The House of Lords' decision took matters beyond this by saying that the Society could not apply a different bonus policy to GAR and non-GAR policyholders.

The with-profits fund is a single pot of money. The effect of the decision of the House of Lords was to reduce the share of the with-profits fund in respect of non-GAR policyholders and increase the share of GAR policyholders. The House of Lords' decision affects the way in which the assets in the with-profits fund are allocated between different categories of policyholder. Following the House of Lords' decision, the extra cost of providing for GARs was assessed on a realistic estimate basis at £1.3 billion for the future and £200 million for a rectification scheme for those policies that had matured since January 1994 (when the differential final bonus system was first introduced), making £1.5 billion in total. The realistic estimate was based on the Society's understanding of the types of annuity to which GARs apply, assumptions regarding future interest rates, mortality experience, take-up rates and the level of future contributions to GAR policies.

Results

The total likely future realistic estimate cost of honouring GAR benefits calculated on these assumptions for policies in force at 31 July 2001 was £1.06 billion.

Calculation of Apportionment

Although the total amount of compensation to all GAR policyholders has been estimated using actual experience (which, for example, has not been the same for Individual Pensions and Group Pensions even though both have the same GARs), the scheme allocates that compensation based on legal entitlement at retirement. The legal entitlement at retirement takes two main forms, being 'fixed' GARs which apply only to one specified form of annuity at retirement and 'flexible' GARs which are available for a wide range of non-profit annuities. In order to set an allocation basis which does not differentiate between policies with the same legal entitlements at retirement, the following changes were made to the costing basis:

Take up rate	100%
Transfers out	0%
Annuity escalation	
For pre 97 benefits and group Pensions AVC benefits	3%
(For post 97 benefits unchanged, as required by law	5%)
Spouse's annuity proportion	35%

The allocation of the scheme compensation takes account of the current age of beneficiaries of GAR policies and, as a result, the percentage allocation results vary by age for some types of GAR policy.

The allocation of the compensation at each age has been reduced by a risk margin of 1% per annum which has been taken in the form of a deduction from Policy Value growth. The longer the period until retirement the greater the risk that the benefits from the GAR rights at retirement will not be realised in full. Such potential risks include, for example, the risk that current annuity rates will increase (i.e. reducing the value of the GAR rights) and the risk of a significant reduction in future investment returns and with-profits bonuses as a result of a need, in response to external factors, to invest an increased proportion of the with-profits fund in fixed interest securities. Without such a risk margin policyholders with many years to retirement could crystallise their GAR benefits on the same basis as policyholders close to retirement, or those who could retire now, without any account taken of the inherent risks in being a with-profits policyholder and the uncertainty as to future benefits, as just described.

Type of Annuity Taken

For policies which have a choice of type of annuity:

a) the assumed rates of annual increase in income chosen are:

	Pre 97 Benefits	Post 97 Benefits
Individual Pensions/ Transfer Plans	1.5%	5.0%
Group Pensions Policies (non-AVC)	1.0%	5.0%
Group Pensions AVC	1.0%	1.0%

These increases are based on actual experience for policies maturing in 2000 except that in respect of premiums paid after 1997 (other than for Group Pensions AVCs) pensions are assumed to include 5% escalation. This reflects the requirement to take pensions increasing by at least Limited Price Inflation for such benefits.

b) In 2000, of those GAR policyholders who could take flexible benefits, 69% of Individual Pensions and Transfer Plan policyholders took spouse's pensions with the amount payable to the spouse averaging 60% of the main pension, i.e. representing an average spouse's pension proportion of 41%. For Group Pensions the equivalent figures were 49% and 55% representing an average spouse's pension proportion of 27%.

For calculating the cost of the guaranteed annuities it has been assumed that an 'average' spouse's pension is taken of 40% from Individual Pensions and Transfer Plans and 30% for Group Pensions schemes.

Age on Retirement

For Retirement Annuities, Individual Pensions and Transfer Plans, the Society's pre-House of Lords experience has been used. This seems more appropriate than using post-House of Lords data because there is more data and also post-House of Lords experience is distorted by some policyholders taking their pension early.

For Group Pensions each scheme's normal retirement date was used.

Annuity Expenses

0.2% of policy fund plus £40 p.a. per policy.

These represent the current expenses of the Society and are added to the total cost of the guaranteed annuity.

Policy Value Growth

A 6% p.a. gross investment return has been assumed, less the Society's normal deduction of 0.5% p.a. for expenses.

This rate is used to increase the Policy Values in the total cost calculation (including values secured by future premiums) up to the point of retirement.

Because assets attributable to GAR policies constituted around 25% of the with-profits fund as at 20 July 2000, the date of the House of Lords' judgment, and assets attributable to non-GAR policies constituted around 75% of the with-profits fund, the economic transfer from the non-GAR policyholders to the GAR policyholders was around 75% of £1.5 billion, approximately £1.1 billion.

On 27 July 2000 the Society announced that to cover the additional liability in relation to GARs, seven twelfths of the interim rate of return allocated for the year 2000 would be withheld.

Having assessed the consequences to the Society of the decision of the House of Lords, the Board decided that members' interests would be best served by relinquishing the Society's mutual status by way of a sale of the Society's business and sought a third party purchaser of the Society's business who could provide additional capital. Although there were a number of expressions of interest received, no binding contract was concluded.

On 8 December 2000 the Board announced that it was unable to sell the Society in its entirety as a going concern and closed the Society to new business.

1.3 The GAR Problem

As at 30 June 2001 there were approximately 70,000 individual with-profits policyholders with a GAR and 105,000 members of with-profits group pension schemes insured with the Society who were entitled to a GAR. There were approximately 415,000 individual with-profits policyholders and 510,000 members of group pension schemes without a GAR. There were about 485,000 individual policyholders in total and about 615,000 members of group pension schemes with interests in the Society's with-profits fund. These numbers do not include final salary schemes.

The cost of providing annuities on guaranteed terms falls on the with-profits fund. There is no external source of funding. In arriving at the amount available for inclusion in Policy Values the Society is obliged to calculate a realistic estimate of the cost of the aggregate GAR liability. This is notionally matched by longer dated cash flows from fixed income investments and therefore the impact of changing interest rates is reduced. However, the remaining variability of the realistic cost impacts on the amount of assets available to back Policy Values. The take-up rate of GARs at retirement, the ability to pay future premiums and variable retirement dates under these policies make it impossible to achieve a perfect match of assets to this liability.

An important feature of the GAR cost is its variability. The realistic estimate of the cost of meeting the future liabilities arising from the GAR options at 31 July 2001 (excluding the amount set aside for the Rectification Scheme) is £1.06 billion. However, if current annuity rates return to the levels of the 1980s and remain at those high levels, then that cost would reduce to zero. Conversely, if current annuity rates reduce and remain at low levels, then the cost would increase. This volatility has an impact on the Society's statutory capital requirements because the regulations require that tests are carried out to demonstrate that the reserving levels would remain sufficient to meet all guaranteed liabilities under a range of different economic circumstances. As noted, the change in the value of the liabilities is partially offset by the assets backing the GAR reserve. The cost of reserving for the GAR fluctuates with movements in interest rates, improvements in mortality, the payment of premiums and also with take-up rates of GARs and the timing of retirement of policyholders.

The Society has, therefore, since the decision of the House of Lords, been in a period of uncertainty and instability with the following damaging consequences for the Society and its with-profits policyholders:

- the prudent reserving requirements for life and pensions companies mean that, without further moves into fixed interest assets, meeting the statutory capital requirements could lead to restrictions on the Society's investment and bonus policy and hence lower long-term returns to policyholders;
- the Society is more vulnerable to declining values of stocks and shares;
- non-GAR policyholders, given the uncertainty and instability of the with-profits fund, are seeking to withdraw their funds and leave the Society in greater numbers;
- the prospect of further guaranteed bonuses being declared is remote;
- final bonus policy is more uncertain;
- the maintenance of the required minimum margin under Section 32 of the Insurance Companies Act has the potential to reduce investment returns through increasing transaction costs, arising from active asset management.

Therefore, the prospects for the Society and its policyholders are bleak unless a solution can be found to the GAR problem.

1.4 The Opportunity

On 5 February 2001 the Society entered into a number of agreements with Halifax plc and two of its subsidiary companies. The effect of the agreements was as follows:

- The Halifax group acquired the Society's infrastructure assets, such as its premises, the shares in Equitable Investment Fund Managers Limited and Equitable Services and Consultancy Limited, the Society's name

For premiums in subsequent years the following assumptions are made.

	Increases	Decreases	Premiums cease (net)	Transfers out to other providers
Retirement Annuities	16%	15%	9%	1%
Individual Pensions	15%	15%	7%	1%
Group Pensions	15%	15%	9%	4%

All above percentages are per annum changes from the previous year's premiums.

These rates are based on actual experience of both GAR and non-GAR policies prior to the House of Lords' judgment. This assumes that the very large reductions in premiums seen so far in 2001 would be unlikely to continue into 2002 and beyond, and that pre-House of Lords experience is a better measure for these purposes.

Mortality (life expectancy)

The mortality tables used in calculating the total cost of the guaranteed annuities assumed to be taken are the latest published tables from the Continuous Mortality Investigation Bureau which is an independent bureau that collects and analyses mortality data from most UK life offices.

For men, the mortality rates used are from Table PMA92 (U = 2001) assuming an age one year younger. For women, the equivalent table PFA92 (U = 2001) is used also assuming an age one year younger.

Prior to retirement those mortality rates are increased by 0.0004 per annum for men and 0.00045 per annum for women.

These assumptions have been chosen to be consistent with the Society's current experience and the tables allow for improvements in mortality continuing into the future.

Appendix C sets out the assumptions made in arriving at the realistic estimate of the total cost and apportionment of the GAR compromise sum.

It is primarily aimed at enabling actuarial consultants and financial advisers to assess the reasonableness of the basis of calculation.

GAR Cost and Apportionment

Assumed Annuity Interest Rate 5.5% p.a.

This is based on a AAA long term bond yield with allowance for default.

Take-up Rate for GARs

Not all GAR policyholders take up their full entitlement to take annuities at guaranteed rates. Most policyholders in particular take their tax free cash lump sum and some prefer to take alternative pensions products with other providers. The percentage of the possible maximum entitlement taken ('take-up rate') has been monitored for policies maturing over the period following the House of Lords' ruling (September 2000 to June 2001).

The following percentage take-up rates reflect that experience (with some slight rounding up) and are assumed to continue unchanged in the future.

For estimating the cost the assumptions are:

Retirement Annuities	60%
Individual Pensions/Transfer Plans	65%
Group Pensions	40%

Future Premiums

The cost of the GAR benefits includes guaranteed annuities secured with funds purchased by future premiums paid to GAR policies.

To calculate this cost the assumptions for premiums in 2001 are:

Retirement Annuities	55% of premiums received in 2000
Individual Pensions	65% of premiums received in 2000
Group Pensions	45% of premiums received in 2000

These percentages reflect the experience of the first half of 2001 compared with first half of 2000 and give a starting point for premiums on policies on the books at 31 July 2001.

and brand, its workforce, its administration and investment management activities and (through a reinsurance arrangement) an interest in some of the Society's non-profit business, including its unit-linked business.

- The Society agreed to prepare and put before its policyholders a scheme of arrangement under Section 425 of the Companies Act with the purpose of compromising the GAR liabilities of the Society.
- The Society received payments amounting to £500 million on 1 March 2001.

If the compromise scheme becomes effective before 1 March 2002, then the Society would benefit to the extent of a further £250 million (the Halifax £250 million) being made available from Halifax immediately and would have the possibility of benefiting from up to a further £250 million being made available on the achievement by the business acquired by Halifax of certain business sales and profitability targets. If both an effective scheme and the targets could be achieved, it would bring the total paid by Halifax for the acquisition of that part of the Society's business to £1 billion. However, the structure of the agreement means Halifax has no exposure to the Society's with-profits fund, so the GAR problem has to be solved by the Society.

As part of the agreement, the Society agreed with Halifax that any scheme proposed by the Society should meet six basic objectives (the Scheme Objectives). These are:

- the compromise of the rights to GARs enjoyed by certain policyholders;
- the compensation to be provided under the scheme in respect of compromised guaranteed annuity rates being fair and reasonable as between the various classes of creditors entitled to vote thereon (including its effect on the solvency of the with-profits fund and taking into account the amounts paid or payable by Halifax pursuant to the agreement);
- all creditors of the with-profits fund entitled to vote on the scheme being bound by the scheme;
- the classes of creditors of the with-profits fund, whose approval of the scheme is required in accordance with Section 425(2) of the Companies Act being no greater than the minimum practicable in the circumstances;
- the operative provisions of the scheme, being as simple as reasonably possible (in order to assist in effective communication to policyholders and other interested parties); and
- the Society being in a position to implement the scheme in accordance with its terms.

At the point when the agreement with Halifax was concluded, issues concerning the non-disclosure of the GAR costs to the non-GAR policyholders were not considered or discussed by the parties as the Society had not yet been advised of the issue.

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2. Options available to the Society to solve the GAR problem through a scheme

2.1 Summary

The Society has agreed with Halifax to prepare a scheme in accordance with the Scheme Objectives and place that scheme before the Society's with-profits policyholders.

The new Board nevertheless considered it was under a duty to investigate whether there were any other potential solutions to the GAR problem (other than a scheme) available to the Society. Having given careful consideration to the matter, the Board has concluded that a compromise implemented through a scheme is the only viable solution. Details of other options considered and rejected by the Board are at Part IV.

This section of the document assesses the options open to the Society to propose a scheme which complies with the Scheme Objectives.

A scheme which meets the Scheme Objectives could be structured in one of two ways:

A 'Ring-Fenced Fund Scheme'

A structure whereby the GAR liability is capped or limited by recourse to a limited ring-fenced top-up fund which 'tops-up' the asset share of a GAR policyholder on retirement to bring it up to the amount required to purchase an annuity reflecting the GAR at current annuity rates. Through such a scheme GAR policyholders would agree that they would have no right to the with-profits fund assets beyond those which would enable them to buy an annuity at the current rate. Future premiums would not attract GARs. The ring-fenced fund would be limited, thus sealing off the GAR liability from the general with-profits fund.

A 'GAR Buy-Out Scheme'

A structure whereby the Society's GAR liability is crystallised by the GAR policyholders having their GAR rights bought out for an immediate uplift on their Policy Values.

A scheme which meets the Scheme Objectives (in the sense that it compromises the GAR rights before 1 March 2002 through a crystallisation or capping mechanism) would have a number of benefits for the Society (referred to as 'the capping and crystallisation benefits'):

- uncertainty about future interest rate movements, improved mortality and the spread between GAR and current annuity rates would be removed;
- statutory reserving requirements for GARs would be capped making the fund more stable and would allow a more flexible investment policy with the aim of achieving higher returns;
- non-GAR policyholders would be less likely to leave the Society thereby increasing stability;
- premium paying may recommence in greater quantities leading to increased stability;

Appendix B – Table of GAR Policy Value increases

Age on 31.12.2001	Retirement Annuity policies issued before October 1975 ('Flexible' form of GARs)	Retirement Annuity policies issued after September 1976 ('Fixed' form of GARs)	All other policies (with the 'Flexible' form of GARs)
30 or less		16.3%	16.5%
31		16.3%	16.5%
32		16.3%	16.5%
33		16.3%	16.5%
34		16.3%	16.5%
35		16.3%	16.6%
36		16.3%	16.8%
37		16.3%	17.0%
38		16.3%	17.2%
39		16.3%	17.4%
40		16.3%	17.7%
41		16.3%	18.0%
42		16.3%	18.3%
43		16.3%	18.5%
44		16.3%	18.8%
45	3.5%	16.3%	19.1%
46	3.5%	16.3%	19.3%
47	3.5%	16.3%	19.6%
48	3.6%	16.3%	19.8%
49	3.6%	16.3%	19.9%
50	3.6%	16.3%	20.1%
51	3.7%	16.3%	20.2%
52	3.8%	16.3%	20.3%
53	3.8%	16.3%	20.4%
54	3.9%	16.3%	20.4%
55	4.0%	16.3%	20.3%
56	4.1%	16.3%	20.3%
57	4.1%	16.3%	20.2%
58	4.2%	16.3%	20.1%
59	4.3%	16.3%	19.9%
60	4.5%	16.3%	19.7%
61	4.8%	16.3%	19.5%
62	5.0%	16.3%	19.3%
63	5.1%	16.3%	19.1%
64	5.3%	16.3%	18.9%
65	5.5%	16.3%	18.7%
66	5.9%	16.3%	18.5%
67	6.0%	16.3%	18.3%
68	6.2%	16.3%	18.1%
69	6.4%	16.3%	17.8%
70	6.6%	16.3%	17.6%
71	6.8%	16.3%	17.4%
72	6.9%	16.3%	17.3%
73	7.0%	16.3%	17.1%
74	7.1%	16.3%	17.0%
75	7.2%	16.3%	16.9%

PART 1 – STATUTES AND STATUTORY INSTRUMENTS

'Companies Act' means the Companies Act 1985

'Financial Services Act' means the Financial Services Act 1986

'Financial Services and Markets Act' means the Financial Services and Markets Act 2000

'Insolvency Act' means the Insolvency Act 1986

'Insurance Companies Act' means the Insurance Companies Act 1982

'Insurance Companies (Winding-Up) Rules' means the Insurance Companies (Winding-Up) Rules 1985

'PPA' means Policyholders Protection Act 1975

PART 2 – GLOSSARY OF TERMS

final bonus means the indicative amount which is added by the Society to a with-profits policy from time to time which the Society is not contractually bound to pay until it is finally determined by the Society on contractual terminations. Final bonus can be increased or reduced by the Directors at any time.

guaranteed bonus means the bonus added from time to time to the guaranteed element of with-profits policies by the Society. Once added it is guaranteed to be payable on contractual events.

Policy Value means the fund value attributed by the Society to a with-profits policy, including both guaranteed and non-guaranteed elements.

realistic estimate means an estimate which is neither cautious nor optimistic

- the remote risk of the Society defaulting on its obligations by reason of the GAR problem would be removed; and
- the Halifax £250 million would be made available.

Each of the two scheme structures was considered by the Society and appraised against the following criteria:

- the likelihood of success of the structure proposed (the scheme being approved by the relevant classes of policyholders in their statutory majorities and sanctioned by the High Court);
- the value to policyholders (both GAR and non-GAR);
- the advantages and disadvantages as well as intangible benefits to policyholders;
- the tax implications to the Society and policyholders;
- the cost of implementing the structure; and
- whether the option would enable the Halifax £250 million to be realised.

2.2 A Ring-Fenced Fund Scheme

A ring-fenced fund structure has a number of advantages:

- it minimises the cross-subsidy from those GAR policyholders who intend to exercise their GARs to a higher than average extent, or in full, to those GAR policyholders who intend to exercise them to a lower than average extent, or not at all;
- GAR rights could continue to be exercised in the ordinary course (as long as future experience was in line with the assumptions used to calculate the amount deposited in the ring-fenced fund);
- there are unlikely to be any adverse tax implications; and
- if the scheme met the relevant criteria the Halifax £250 million would become available.

However, weighed against those advantages there are a number of disadvantages:

- GAR policyholders further from retirement would be uncertain of the sufficiency of the fund being set aside in a climate of low and falling interest rates and may insist on a higher amount being placed within the ring-fenced fund than the non-GAR policyholders are prepared to pay;
- a change in legislation, for example the abolition of the 'tax-free cash' allowance or other material change such as a material drop in current annuity rates, could significantly increase the take-up rate of GAR rights causing a higher attrition rate on the ring-fenced fund, possibly causing that fund to become insolvent in the long term to the prejudice of younger policyholders;
- conversely, a change such as the abolition of the requirement to convert the fund (after taking tax-free cash) into an annuity before the age of 75 or a material rise in current annuity rates could decrease the take-up rate of GAR rights causing a significantly lower attrition rate on the fund giving rise to a surplus;
- the allocation of any surplus in the ring-fenced fund

could be difficult and would have to be resolved at the time of the scheme;
- the determination of the available surplus could be conducted only once all policyholders had taken their benefits or are otherwise not entitled to their GARs;
- the ring-fenced fund could not be used to determine bonus policy or to effect any form of smoothing;
- the creation of a ring-fenced fund could be said to contravene the spirit of the House of Lords' ruling of July 2000;
- additional management and administration costs would accrue;
- in addition to scheme meetings, a vote of the Society's members in General Meeting would be required to establish the ring-fenced fund (Regulation 57 of the Articles of Association); and
- the scheme structure may be more difficult to explain to policyholders.

2.3 A GAR Buy-Out Scheme

A GAR Buy-Out Scheme has a number of specific advantages:

- a fixed cost is placed on the GAR thereby providing the Society with the 'capping and crystallisation benefits' set out above;
- all with-profits policyholders are placed on the same footing going forward;
- the methodology of the uplift is easily understood by both GAR and non-GAR policyholders and is transparent; it does not have the uncertainty that the ring-fenced fund scheme involves for the individual GAR policyholder and it is clear what each policyholder is receiving;
- a significant part of the uplift can be given in guaranteed form;
- GAR policyholders would be able to use their uplifted Policy Values to purchase products from providers other than the Society if they offered better current annuity rates or more flexibility than the Society;
- GAR policyholders would be able to transfer out of the Society taking their uplifted amount with them (subject to any financial adjustment imposed by the Society);
- there are unlikely to be adverse tax implications for the individual policyholders;
- if the scheme met the relevant criteria the Halifax £250 million would become available; and
- uplifted benefits would be available on death before retirement, compared to their GARs which will die with them.

There are, however, a number of disadvantages:

- some GAR policyholders nearing retirement who wish and are entitled to exercise their GAR rights to the maximum may feel they are not receiving like for like financial compensation from the Society. The Society has looked at this issue very closely. The proposed scheme takes the overall actual experience into account whereas these policyholders may feel that they can do

- there would probably be severe adverse tax consequences for policyholders.

8.7 Conclusion on liquidation options

There are no advantages and many serious disadvantages to the Society and its with-profits policyholders by liquidating the Society. In particular, it is likely that all non-guaranteed bonuses would be lost, benefits could be scaled back still further than that, competing legal claims would be likely to delay payments for years and annuity payments would be suspended. The costs of liquidation could be well over £100 million which would be paid for as a first charge on policyholders' funds.

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its powers to assist policyholders, there could well be a delay of years before it made any payment. As the position would be unprecedented, the PPB would be required to satisfy itself that it was under a statutory obligation to exercise its powers in the Society's case and, if so, to what extent. It may decide to test a number of legal issues arising out of the PPA, the untested Insurance Companies (Winding-Up) Rules (insofar as they apply to life assurance companies) which might result in a number of test cases and appeals through the courts, all of which will take time. It is possible that the PPB might be lobbied by other life assurance companies (who are liable to fund the PPB through a levy) to test all legal points which could be reasonably taken. Policyholders should therefore not rely on immediate assistance from the PPB in the event of a liquidation of the Society. In the best case scenario the PPB would only secure a maximum of 90% of the minimum guaranteed value of a policy and could scale back benefits further. It is possible that no payments would be made for several years including the payment of annuities;
- the liquidators would be under a statutory obligation to continue the long-term business with a view to it being transferred to another insurance company and the emphasis of the liquidation would be on achieving such a transfer, but in view of the Society's lack of success in seeking a purchaser of its with-profits business, it is questionable whether a liquidator would have any greater success;
- the investment policy of the liquidators would be extremely conservative;
- as a company in liquidation cannot assume additional liabilities, the Society will not declare any further bonus, either contractual or final, in favour of policyholders;
- the court may order a reduction of Policy Values including guaranteed values in order to make the business more attractive to a buyer;
- professional costs would be substantial and would be the first charge on policyholders' funds;
- the Halifax £250 million would be lost.

8.6.3 A formal liquidation of the Society with a Stop Order made

A Stop Order would be made by the Court if the liquidators had failed to find a purchaser. Policyholders should remember that the Society failed in its own attempt to find a purchaser. The Court can reduce Policy Values including guaranteed values, potentially causing substantial losses for policyholders. In addition to the consequences set out above:

- the process could take many years given the untested nature of the statutory framework;
- the liquidators would be obliged to place the entire liquid assets of the Society in the Insolvency Services Account where it would be held in gilts or cash attracting a very low rate of interest and substantial fees would be payable, over the life of the liquidation; and

better than the average experience. However, by making this choice they accept a different set of risks. For example, taking maximum GAR rights under a single life non-guaranteed annuity would give much poorer value to a policyholder who died shortly after retirement than exercising minimum GAR rights in order to take maximum cash and maximum spouse's pension. These are issues of individual choice. Any policyholder who wishes to and can exercise maximum GAR rights may do so before the compromise scheme takes effect.
- the scheme would necessarily involve an element of cross-subsidy from those GAR policyholders who would have exercised their GAR rights to a higher than average extent, or in full, to those GAR policyholders who would have exercised them to a lower than average extent, or not at all.

2.4 Conclusion

Although both structures have advantages and disadvantages, the Board has concluded that a GAR Buy-Out scheme has clear advantages over a Ring-Fenced Fund Scheme.

The key advantages are:

- it provides fair value to GAR policyholders irrespective of their distance to retirement;
- it is easier to understand and implement;
- the benefits offered are immediate and more certain;
- there is no opportunity for future disputes over the compensation given to GAR policyholders;
- there is no risk of compensation being denied to younger policyholders.

The Board has therefore decided a proposal for a GAR Buy-Out Scheme should be put to policyholders for consultation.

3 The proposed solution for GAR policyholders

3.1 Summary

The proposed solution is a GAR Buy-Out Scheme, the terms of which would remove the GAR rights from the GAR policies (by endorsement to those policies). The consideration for consenting to this removal would be an uplift of the values attaching to those GAR rights according to a pre-determined methodology.

3.2 Basic principles underpinning the solution

There are four basic principles underpinning the solution proposed by the Society. The solution must:

- be fair to all with-profits policyholder groups;
- be easy to understand;
- mean all with-profits policyholders share the pain and the benefit of the compromise;
- be able to be implemented.

3.3 GAR compromise principles

These basic principles are reflected in the following GAR compromise principles:

- fair value compensation given to the GAR policyholders as a group should reflect a realistic estimate of the additional cost to the Society of providing GAR benefits in the future; the realistic estimate should be neither cautious nor optimistic;
- the realistic estimate of the additional cost to the Society of providing GAR benefits in the future should form the financial basis of the compromise between GAR policyholders and the Society; it should be affected only by the need to compensate non-GAR policyholders for giving up their possible claims;
- the compensation should be distributed among GAR policyholders in proportion to the value of the legal rights which they are being asked to give up; and
- the compensation should take the form of a proportionate increase in GAR policyholders' relevant Policy Values in both guaranteed and non-guaranteed form.

3.4 Stages of the solution proposed by the Society

The solution will have two key stages:

- the calculation of the amount to be taken from the with-profits fund to be applied exclusively to the GAR policyholders in consideration for the buy-out of their GAR rights, referred to below as the 'calculation of the amount of compensation' or alternatively 'the cost'; and
- the apportionment of the resulting amount between GAR policyholders in accordance with their rights and certain characteristics, referred to below as the 'apportionment of the compensation'.

3.5 Methodology

3.5.1 Calculation of the amount of compensation

The starting premise for determining the level of compensation that will be applied to buy out the GAR rights should be based on the actual cost to the Society of those GAR rights. In practice, the actual cost of the GAR rights will only be known when all the benefits have been taken over the next 40 years and will reflect conditions over those 40 years including economic and demographic factors and the retirement benefits chosen by policyholders.

At present it is not known what the actual cost will be over the next 40 years and therefore the Society must estimate this cost to determine the amount of compensation. So that the scheme is a fair compromise between the GAR and non-GAR policyholders, the estimate of the cost has been calculated by making the best possible estimates of future experience.

policyholders and members. All the non cash assets would be sold in order to raise cash for distribution. The valuation methodology would have the effect of crystallising the aggregate cost of GAR policyholders' GAR rights (as well as the rights of non-GAR policyholders) as at the effective date of the scheme (or such later date as the scheme provides) and distributing the assets in accordance with those crystallised rights. Such a scheme is unprecedented. The tax consequences are unknown and could be severe. At the scheme's conclusion the Society would cease to have any assets or liabilities and would be wound up.

The Society would only propose such a scheme if ending its existence earlier than if the Society was left to run-off its business would benefit policyholders. This seems highly unlikely. In addition this approach provides no solution to the GAR problem. To achieve a solution to the GAR problem, provisions would need to be built into the scheme to cap or crystallise the GAR policyholders' rights according to an agreed methodology. Non-GAR policyholders would need to have their claims valued. Both GAR and non-GAR policyholders are also likely to insist that under a scheme they are not treated worse than they would have been had a formal liquidation taken place. Unless it incorporates a compromise solution to the GAR problem, an informal liquidation through a scheme does not take the Society or its policyholders any further forward and would be likely to substantially reduce policyholder value.

Policyholders could not be prevented from leaving the Society while the Scheme was in preparation, increasing its instability, unless an order was made appointing provisional liquidators (which would freeze the Society's funds, preventing any payments being made at all, including those to annuitants).
Such a scheme would also be complex and very costly and the Halifax £250 million would be lost.
There would therefore appear to be no advantages and very significant disadvantages over the compromise set out in the *Proposed Compromise* document.

8.6.2 A formal liquidation of the Society where its long-term business is carried on by the liquidators and no Stop Order is made by the court

The following are likely to be the consequences of a liquidation of this type to the Society:

- a winding-up order could be preceded by a substantial period of provisional liquidation where the provisional liquidators will make an assessment of the options during which period all the assets of the Society would be frozen (unless a court order to the contrary was obtained) and all payments to policyholders, including annuitants, would be suspended;
- the Policyholders' Protection Board (PPB) (which will be replaced on 30 November 2001 by the Financial Services Compensation Scheme) would be asked to exercise its powers. If the PPB were requested to exercise

applies on winding-up. There are a number of variations built into the statutory scheme. In particular the way a liquidation proceeds will depend on whether a transfer of the with-profits business to a third party is feasible and whether a Stop Order is made. A Stop Order is an order of the court made under Section 56 (2) of the Insurance Companies Act ordering a liquidator of a life insurance company to stop carrying on the long term business of the company. It is likely to be made if no transfer of the with-profits business to a third party proves possible. The strategy adopted by a liquidator would also be difficult to predict. He may decide to wait and see how the matters develop before deciding on a course of conduct.

A full liquidation is likely to be preceded by a period of provisional liquidation where the provisional liquidators will make an assessment of the options. If no transfer of the business proves possible, the provisional liquidator might consider that it was more beneficial to distribute the assets of the Society through a scheme and avoid a full liquidation altogether. Much of the legislation in this area is untried and untested. Since the passing of the Insurance Companies (Winding-Up) Rules in 1985 there has been one liquidation of an insurance company writing long term business, which was not of the magnitude of the Society.

The costs of any liquidation option are likely to be very substantial (possibly over £100 million) and will rank as a first charge on the with-profits fund.

The Society may only be wound up compulsorily by the court. Members of the Society may not, by extraordinary or special resolution, place the Society into voluntary liquidation.

A court may order the winding-up of the Society under the Insolvency Act as modified by the Insurance Companies Act. If it can be demonstrated that the Society is insolvent, a petition may be presented by the Society, its directors or its creditors. A petition could be presented by a member on the ground that it is 'just and equitable' to wind-up the Society.

A petition may also be presented by the FSA on a number of grounds, including that the Society is unable to pay its debts.

In summary, there are three types of liquidation:

- an informal liquidation through a scheme;
- a liquidation without a Stop Order; and
- a liquidation with a Stop Order.

8.6.1 A liquidation through a scheme

The Society could be liquidated through a scheme of arrangement under Section 425 of the Companies Act without the need formally to commence liquidation proceedings. The scheme would replicate a liquidation by importing a valuation methodology for the Society's liabilities and a distribution of its assets to its

The cost of the GAR rights will depend on:

- current and future interest rates;
- likelihood of survival to retirement; and
- life expectancy past retirement.

The actual cost to the Society of the GAR rights may be reduced by reason of the selection of non-GAR related options under the policy. These include:

- the taking of some or all of the retirement fund in the form of a tax free lump sum. The Society's experience is that almost all policyholders choose to take the maximum allowable tax free lump sum and so choose to give up the higher GAR value on this portion;
- investing in other ways during retirement through income drawdown, or with-profits and unit-linked annuities;
- the taking of a flexible non-GAR option because some GAR policies only permit a restricted form of GAR annuity to be taken, which precludes any provision for a spouse or any increases to the annuity; and
- transferring to another annuity provider should they wish.

The Society, since the House of Lords' decision, has reviewed the take-up rate of the GAR rights of GAR policyholders at retirement. This is the Society's best (and least arbitrary) estimate for the future value and future cost of GARs. The Society considers this approach to be fair to both GAR and non-GAR policyholder groups.

The valuation methodology and the assumptions used to calculate the GAR cost are based on the following key factors:

- the level of current and future interest rates;
- the proportion of benefits taken in GAR form (the take-up rate);
- the level of future contributions attracting GAR rights;
- future mortality; and
- future transfers out of the fund.

The assumptions are based on relevant experience since the decision of the House of Lords or where appropriate, before that time (see Appendix C). The assumptions will be reviewed just prior to finalising the scheme.

3.5.2 Apportionment of the compensation

3.5.2.1 Introduction

Once the total amount of compensation has been calculated in accordance with the above principles, it will be necessary for the Society to apportion the compensation among GAR policyholders.

3.5.2.2 Method of apportionment

Two methods of apportionment have been considered:

(a) An apportionment between groups with broadly similar policies.

There are four broad groups of generic policy types:

- Retirement annuities
- Individual pensions
- Group pensions
- Transfer plans

While it is reasonable to assume that as the various policy types were designed to meet the specific needs of groups of policyholders these policyholders would act in a similar way, it is impossible to predict with any certainty how an individual would act. Different generic policy types offer identical GAR options. Therefore, apportioning the compensation between the above broad groups on the basis of that group's behaviour could result in two individuals in different groups with exactly the same GAR option receiving differing amounts of compensation simply because the behaviour of their respective groups as a whole differed. The view of the Board is that the relative compensation for each policyholder should be dependent on the relative rights of the GAR policyholders.

As the above method of apportionment does not achieve this result it has been discarded.

(b) An apportionment based on groups of policyholders with the same identifiable GAR rights at retirement regardless of the generic policy type.

Such groups have been identified as those with:

- GARs calculated on a similar interest rate basis;
- the ability to choose a flexible form of GAR annuity.

This method of apportionment is based on the full GAR rights of all those within the same 'group' even if experience from some or most other policyholders of the same type of generic policy is that they do not take their GAR rights in full. This ensures that the apportionment is based on legal rights, not on take-up rates of GAR options.

This basis has been adopted.

3.5.2.3 Other potentially significant attributes

Notwithstanding the above principles of apportionment, the following attributes could have an effect on the value of the legal rights of an individual policyholder and must also be considered:

- current age (distance from retirement);
- sex;
- marital status;
- size of premium relative to existing policy funds.

Act. Paragraph 5(1) of Schedule 2C to the Insurance Companies Act provides that:

"Where the Court makes an order under this Part of the Schedule sanctioning a scheme [i.e. a Schedule 2C scheme] the Court may, either by that order or by any subsequent order, make provision for all or any of the following matters….

(e) such incidental, consequential and supplementary matters as are necessary to secure that the scheme shall be fully and effectively carried out."

Consideration was given to whether, in the context of a portfolio transfer either to a third party purchaser or a special purpose vehicle, the removal of the GAR rights during the course of a Schedule 2C scheme would fall within the definition of "such incidental, consequential and supplementary matters as are necessary to secure that the Scheme shall be fully and effectively carried out".

The Society has been advised that, while there is no absolute certainty on the point, a court would not have jurisdiction under Schedule 2C to the Insurance Companies Act, to amend the GAR policies in order to implement the GAR compromise which the Society is seeking.

Accordingly, amending the GAR policies pursuant to a Schedule 2C to the Insurance Companies Act transfer does not appear to be an option available to the Society.

It should be noted that on 30 November 2001 Section 112(8) of the Financial Services and Markets Act comes into force. Section 112(8) would enable the court to implement a compromise of GAR rights through a "Section 112 scheme" which would be broadly similar to a Schedule 2C scheme, but where the power of the court to make amendments to policies is more extensive. Nonetheless, the court retains a discretion as to whether or not to approve a particular scheme. Meetings of policyholders would still have to be held so that it could be demonstrated to the court that there was widespread policyholder support. Policyholder reaction to a proposed scheme would impact a court's view on the exercise of its discretion to approve a particular scheme. The position might therefore not be very different from a scheme under Section 425 of the Companies Act. However, neither a Schedule 2C scheme nor a Section 112 scheme could affect the claims of non-GAR policyholders.

8.6 Liquidation options

A liquidation could be achieved either informally through a scheme of arrangement or formally through the implementation of the statutory scheme which

- a number of policyholders may seek to negotiate individual terms for themselves;
- a number of policyholders would decline the offer;
- a number of policyholders would not accept the offer until they were sure that a sufficient number of their peers had accepted;
- policyholders may not accept the offer in the belief that if they declined an improved offer would be made;
- those GAR policyholders likely to accept the offer may be those who would not have exercised the GAR option in any event. This would lead to the requirement of a high acceptance threshold before the agreements became effective;
- those GAR policyholders who intended to exercise higher than average GAR rights or their full rights would be reluctant to accept the offer;
- the Halifax £250 million would not accrue;
- it is almost certain that an extraordinary General Meeting of Members would have to approve the Society's offer and methodology but under the Society's present constitution, this could be attended by both GAR and non-GAR policyholders who would have different interests and thus a structure would need to be developed to enable the GAR and non-GAR policyholders to vote on the offer in isolation which, while not impossible, might prove difficult; and
- there may be adverse tax consequences for policyholders (particularly holders of retirement annuity policies) if consensual amendments are made to their policies. In the circumstances, it would be necessary to approach the Inland Revenue to see whether they would agree a concessionary treatment so that no adverse tax consequences arose.

8.4 Section 58 Insurance Companies Act

Section 58 Insurance Companies Act provides:

"Reduction of contracts as alternative to winding up
In the case of an insurance company which has been proved to be unable to pay its debts, the court may, if it thinks fit, reduce the amount of the contracts of the company on such terms and subject to such conditions as the court thinks just, in place of making a winding-up order."

Unless the Society were "unable to pay its debts" the court would have no jurisdiction to "reduce the amount of the contracts" of the Society. The Society would also not want to discriminate against GAR policyholders by reducing their contracts only and leaving those of non-GAR policyholders unaltered. An order under section 58 of the Insurance Companies Act could also not affect the claims of non-GAR policyholders.

8.5 Schedule 2C to the Insurance Companies Act

A transfer of the with-profits business (i.e. the assets and liabilities of that business) of the Society to a third party (which could be a specially formed company) could be effected under Schedule 2C to the Insurance Companies

Current age has the potential to be a significant attribute. There are three main considerations:

- how close the policyholder is to retirement, which will determine the interest of the policyholder in the future performance of the with-profits fund;
- the time remaining for him or her to continue (potentially) to pay premiums to which guaranteed benefits would attach over time; and
- improvements in mortality which make the GAR option more valuable.

The first issue impacts on the likely approval of the scheme by older policyholders or those close to retirement; the second and third raise a significant loss of potentially valuable benefits affecting the youngest policyholders the most. A table demonstrating the impact of age on the uplifts proposed for GAR policyholders is at Appendix B. For fixed GAR policies there was very little variation in value with age and a fixed value is proposed.

A unisex approach is proposed for reasons of equal treatment between the sexes. For fixed GAR policies separately calculated increases for females would be smaller because the improvement in life expectancy for women has been less marked than for men. As women form a small proportion of the total, the effect of averaging is small. For other business the effect is negligible as flexible GARs allow joint-life GAR annuities.

Current marital status could in theory be ascertained, although the data is not held on our records. The effect of marital status is small and as that status could be different at retirement it is not an appropriate attribute on which to vary the apportionment.

The size of premiums relative to existing policy funds is not fixed. The stream of future premiums is not contractual and has no certainty (it could be halved or doubled tomorrow). Therefore this attribute cannot be quantified and so cannot be taken into account for individuals.

3.6 Waiver of GAR policyholders' potential claims for damages

One of the consequences of the legal advice from Nicholas Warren QC and Thomas Lowe is that it is possible that GAR policyholders may have potential claims against the Society arising out of the potential damage caused to the Society by the non-GAR policyholders not being told of the GAR costs and the damages the Society might, as a result, be required to pay. As part of the compromise, it is proposed that the GAR policyholders waive these potential claims so as to end the legal uncertainty. This will resolve the GAR issue to the benefit of all policyholders.

PART II – THE NON-GAR COMPROMISE

4.1 Background

The Society has received legal advice from Nicholas Warren QC and Thomas Lowe, in the form of a joint opinion (the joint opinion) that policyholders who do not have GARs have potential claims against the Society because they were not made aware of the existence and potential impact of GAR rights in policies previously issued by the Society.

The potential claims identified by Nicholas Warren could be brought not only through the courts but also to the PIA Ombudsman. Alternatively, the Financial Services Authority (FSA) could compel the Society to put in place a scheme for compensating non-GAR policyholders under the rules of the Personal Investment Authority (PIA Rules).

An estimate of the cost of defending any action and of meeting any successful claims would have to be made. A suitable sum would have to be set aside from the with-profits fund before any profits were made available to allocate bonuses to policies.

4.1.1 Potential heads of liability

The joint opinion identifies a number of potential heads of liability under which a non-GAR policyholder might be able to make out a claim against the Society for a failure to disclose the existence of the GAR liability, namely:

- a breach of the regulatory rules, giving rise to a breach of statutory duty under section 62 of the Financial Services Act;
- statutory or common law misrepresentation or negligent misstatement or advice under the rule in the legal case of *Hedley Byrne v Heller;*
- implied warranty/collateral promise;
- estoppel by convention; and
- unfair prejudice under section 459 of the Companies Act.

The joint opinion does not consider the availability of any particular remedy on a policy by policy basis but instead examines the heads of liability by reference to the general facts in existence at any relevant time. The joint opinion also examines the extent to which such claims might be statute barred or otherwise limited by law.

The Society notes that the description in the joint opinion of the prospects of success of each of the potential claims varies from "substantial case", "may well be established but … not uncontroversial", "may … on a case by case basis … be able to establish", "may be possible" and "reasonably arguable case". The Society also notes that overall, the joint opinion concludes that there is a likelihood that some claims exist against the Society for some non-GAR policyholders and, potentially, for substantial amounts, and that it also acknowledges that there will be difficulties evaluating the claims on an individual basis, taking into

- there would be no adverse tax implications for the Society or its policyholders; and
- non-GAR policyholders would have their claims dealt with on an individual basis.

However the disadvantages of maintaining the current position are considerable:

- a reserve would have to be set aside to meet the potential claims of non-GAR policyholders;
- the prudent reserving requirements for life assurance companies mean that, without further moves into fixed interest assets, meeting the statutory capital requirement could lead to restrictions on the Society's investment and bonus policy and hence lower long-term returns to policyholders;
- the Society would be more vulnerable to declining values of stocks and shares;
- non-GAR policyholders, given the uncertainty and instability of the with-profits fund, may seek to leave the Society in greater numbers;
- the prospects of further guaranteed bonuses being declared would be remote;
- final bonus declaration policy would be more uncertain;
- the maintenance of the required margin under section 32 Insurance Companies Act would require active management with potentially damaging implications for investment returns;
- GAR policyholders would be able to increase their GAR rights by paying additional GAR attracting premiums, increasing the uncertainty for the Society;
- hedging instruments are likely to be costly;
- the cost of dealing with non-GAR policyholders' claims would be substantial; and
- the Halifax £250 million would not accrue.

8.3 Bilateral agreements

The Society could enter into bilateral agreements with each of its 70,000 GAR policyholders and 415,000 non-GAR policyholders. The agreements would buy out GAR rights and non-GAR policyholders' claims for a consideration pre-determined by an approved methodology. Under this option:

- GAR and non-GAR policyholders would be free to accept or decline the offer (which would be open for acceptance only up to a given date) depending on their particular situation; and
- provided the acceptance rate of the offer was sufficient, the capping and crystallisation benefits (with the exception of the Halifax £250 million) would accrue.

There are, however, overwhelming doubts as to whether a solution to the GAR problem and the potential claims of the non-GAR policyholders through bilateral contracts could, in practice, be achieved:

- a number of policyholders would do nothing and their silence could not constitute acceptance of the offer in law;

PART IV - OPTIONS OPEN TO THE SOCIETY IF THERE IS NO SCHEME

8.1 Background

This section considers the options in the event that the scheme was not approved by the statutory majorities (a majority in number representing three quarters in value of those voting) or by the High Court, or, it was decided (with the consent of the Halifax) not to proceed with a scheme following the outcome of consultation with policyholders.

These options were considered by the new Board when it conducted a full review of the options open to the Society. Each of these options is, in the view of the Board, far less favourable to the Society and its policyholders than any form of compromise scheme. **No option can currently be recommended by the Society as a fallback in the event there is no scheme. Indeed, the Board regards the scheme as the only viable solution to the problems confronting the Society. If no scheme becomes effective, the Society will have to continue in its uncertain and unstable condition managing its liabilities as best it can. The extent of the fundamental uncertainties referred to in the 31 December 2000 financial statements would not abate. The management and quantification of competing claims from non-GAR and GAR policy holders would create substantial challenges for the financial management of the Society.**

The options considered were as follows:

- maintain the current position attempting to match GAR liabilities with hedging instruments;
- enter into bilateral agreements with policyholders;
- apply to the court for a "reduction of contracts" under Section 58 Insurance Companies Act;
- make amendments to GAR policies during the course of a Schedule 2C Insurance Companies Act transfer or, when in force, a section 112 Financial Services and Markets Act transfer;
- liquidate the Society.

Each of these options is now explained in detail.

8.2. Maintain the current position matching the GAR liabilities with hedging instruments

The Society could maintain the current position and not take any action to solve the problem of the GAR rights or the claims of non-GAR policyholders. There are a number of advantages and disadvantages to this approach.

The advantages:

- the problem might resolve itself if current annuity rates rose and stayed at a level equalling or exceeding GARs (following a significant rise in long term interest rates or increase in mortality rates);

account the existence of any defence of limitation open to the Society (actions becoming time-barred), the need to demonstrate factual reliance on the Society's alleged misrepresentation and the assessment of the quantum of loss any one policyholder has suffered.

Indeed, it is the Society's view, having taken further legal advice from Gabriel Moss QC that, despite the substantial arguments that there are potentially significant claims against the Society, it is not possible to be sure that any particular non-GAR policyholder has a definite claim against the Society for any particular sum.

4.1.2 Quantum of damage

Nicholas Warren QC has addressed the issue in his opinion of whether the damages suffered by a non-GAR policyholder should also include the consequences of similar claims that might arise from other non-GAR policyholders leading to lower bonuses in the future. The effect on damages would in such circumstances be significant in terms of the quantum of the claims. For example, if all non-GAR policyholders could frame their claims as negligent advice and if Mr. Warren is correct in his view of the law, then the cost of the claims would fall largely on GAR policyholders and would include the costs of consequential loss arising from the claims of other non-GAR policyholders. Mr. Warren accepts that this is a difficult question that depends on the nature of the cause of action. The issues presented in Mr. Warren's opinion are complex.

The Board has considered Mr. Warren's opinion on the matter very carefully. It has also reflected on the views of other leading Counsel Gabriel Moss QC who does not agree that a non-GAR policyholder could recover this type of consequential loss.

The Board has concluded that the cost of compensation to non-GAR policyholders for potential claims is more appropriately treated as a cost for all policyholders to bear. This is analogous to the treatment of the cost of GARs subsequent to the House of Lords' judgment.

4.2 Impact of the non-GAR policyholders' claims

4.2.1 Types of claim and compromise

The existence of the different heads of liability will be affected by the application of any relevant limitation periods and, therefore, the timing of the relevant key events which gave rise to any potential liability.
The analysis of the factual matrix and the different heads of liability will therefore give rise to a different range of claims for each non-GAR policyholder.

4.3 Options to address potential non-GAR claims

The main options which have been considered by the Society include:

4.3.1 Continue with the scheme without reference to non-GAR policyholders' claims

This option would involve taking no action within the scheme to address the possible non-GAR rights. Individual cases may be resolved through the courts, the Pensions Ombudsman or an FSA ordered scheme under PIA Rules. This would make the compromise less attractive as the with-profits fund would still be exposed to non-GAR policyholders' claims arising through the existence of the GAR liability. Furthermore, a scheme which left the claims unresolved while providing tangible benefit to GAR policyholders would be unattractive to non-GAR policyholders and unlikely to be approved. Such a scheme would not, therefore, achieve finality in resolving the GAR issue and the Society would be forced to adopt a more restrictive investment strategy and make substantial reserves to cover potential claims. The incidence of costly claims handling would depress future bonuses, to the detriment of all with-profits policyholders. For the above reasons, the possibility of leaving resolution of the non-GAR policyholders' claims to a second scheme was also considered impractical.

4.3.2 Establish an individual review process for non-GAR policyholders' claims alongside the scheme

This option would be a slow, cumbersome approach where cases are assessed individually. The number of potential claims that would have to be processed could be substantial and would impose a heavy administrative burden on the Society. Legal costs would be high. For these reasons and the reasons at 4.3.1 above, such a scheme would be less attractive as uncertainties would remain after the GAR scheme was implemented.

4.3.3 Incorporate a generic compromise of the non-GAR policyholders' claims into the solution proposed in the scheme

This option is technically challenging, but offers the prospect that a single scheme will resolve all the fundamental uncertainties arising out of the GAR problem. This is likely to be attractive to policyholders as it provides the greatest degree of finality of all the options.

7.14 Other parties who have an interest in the scheme

There are a number of other parties who have an interest in the scheme. They are:

- The Financial Services Authority (as the Society's regulator);
- The Independent Actuary (in support of fairness and actuarial accuracy);
- The Inland Revenue (with regard to the fiscal effects of the scheme); and
- Halifax (as party to a dependent contractual obligation).

Their approval (or non-objection) will be required before the scheme documents are sent to policyholders.

7.15 The Independent Actuary

There is no legal requirement in a Section 425 scheme to have a report from an Independent Actuary. However, the Society considers that it is of great assistance to the court and policyholders for the Independent Actuary, who is Michael Arnold, a partner in the firm of actuarial consultants, Hymans Robertson, to be involved in the scheme. His role is principally to report on the actuarial work performed by the Society in relation to the compromises with GAR and non-GAR policyholders and to give his assessment on whether the compromise is fair and reasonable to each class of with-profits policyholder.

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The position in relation to joint policyholders and trustees of occupational pension schemes will be set out in the scheme documents.

7.9 The court's sanction

Provided that requisite majorities are obtained, the chairman of the meeting will prepare a detailed report to the court stating the result of the meetings, any difficulties concerning the voting and any issues raised about the statement of Policy Values. An application will then be made to the court to sanction the scheme.

7.10 Issues the court will take into account at the sanction hearing

The matters that will be taken into consideration are:

- whether all statutory conditions have been satisfied under Section 425 Companies Act;
- whether the classes summoned to the meeting were fairly represented by those who attended and whether the majority voting at the meetings acted in good faith; and
- generally whether the compromise or arrangement was such that an intelligent and honest man, acting in his own interest, would reasonably approve.

The court will be concerned to establish that the scheme does constitute a genuine compromise or arrangement between policyholders and the Society, there being some element of accommodation on each side and not the mere expropriation of rights of policyholders without compensation.

7.11 Filing the scheme with the Registrar of Companies

In order for a scheme to become effective, an office copy of the court order sanctioning the scheme must be filed with the Registrar of Companies for registration.

7.12 Rights against third parties

These will remain unaffected by the scheme.

7.13 What policyholders will receive

After the consultation process, a scheme will be finalised and the formal scheme documents will be produced. These will include:

- a letter from the chairman;
- proxy forms and an explanation of how to vote;
- the scheme document and Explanatory Statement;
- details of policyholders' policies with an indicative voting value. Overseas policyholders will be notified of their Policy Value in sterling at a conversion rate set shortly before the scheme is finalised. The voting value in sterling will be based on the currency conversion rate as specified in the scheme documents; and
- a Question and Answer Booklet.

5 The proposed solution for non-GAR policyholders

5.1 Summary

The same four basic principles (set out in section 3.2) should underpin the proposed solution for non-GAR policyholders. These basic principles are reflected in the following non-GAR compromise principles:

- The non-GAR compromise should recognise the financial interests (including claims arising from the cost of GARs) of all non-GAR policyholders in a limited with-profits fund;
- The starting point for fair value compensation for non-GAR policyholders as a group is a comparison with industry pay-outs. There are practical difficulties with this approach, as discussed below;
- Fair value compensation for non-GAR policyholders should require that account is taken of:
  - The uncertain prospects of their claims;
  - The argument that non-GAR policyholders as owners of approximately three quarters of the with-profits fund would be responsible for three quarters of their own compensation, whilst acknowledging that there are differing legal opinions on this point.
- The compensation to non-GAR policyholders should be allocated to give a proportionate increase in Policy Values and an addition to guaranteed benefits to compensate for the guaranteed bonuses that would reasonably have been expected in the absence of the House of Lords' judgment; and
- The compensation to non-GAR policyholders should be paid for by proportionate reduction in the increases to GAR policyholders.

5.2 Valuing the compensation for non-GAR policyholders

In order to determine an appropriate value for compensation for non-GAR policyholders, three approaches were examined:

- Considering what might have been achieved with an alternative provider's product, by comparing the underlying performance of the Society's with-profits fund with the industry;
- Restoring the bonus reduction directly incurred as a result of the House of Lords' judgment;
- Considering the value of an alternative provider's policy by comparing the Society's payouts with industry payouts.

5.2.1 Comparison of investment performance

The first approach compares the investment performance of the Society with its competitors. The accumulated value of any given level of premium payments depends principally on the investment return achieved and the charges taken. For both elements we can obtain comparative data from independent industry surveys.

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Using this data, we found that the Society's investment performance is very close to the industry average, while its charges are considerably lower. The combined effect is that the with-profits policyholders' funds should have accumulated (to date) to a level that is typically equal to or higher than the industry average. This is broadly true whether we go right back to 1988, the start of non-GAR policies, or look at shorter terms.

5.2.2 Restoring the bonus reduction

The second approach calculates the amount required to restore non-GAR policyholders to the position they would have enjoyed had the House of Lords not decided as it did.

The effect of this is:

- to add the seven twelfths of the interim rate of return that was deducted in July 2000 to Policy Values; and
- to add to guaranteed benefits an amount to compensate for the guaranteed bonus that would reasonably have been expected to be declared for the year 2000 in the absence of the House of Lords' decision. This is assumed to be 4% for UK pensions policies that are entitled to declared bonus. Such with-profits policies which have already received a guaranteed 3.5% increase would receive an extra 0.5%. (For UK life assurance and international business, equivalent rates apply).

This gives a compensation value of around 5% of Policy Values.

5.2.3 Comparison to industry average payouts

The third approach seeks to compare actual payouts for the Society's policies with the industry average payout.

This comparison (after allowing for the 16 July 2001 Policy Value reductions) shows the Society's payouts to be below industry average payouts. For regular premium policies, this would lead to a level of compensation of 4% - 8% for terms up to ten years. Single premium policy comparisons at five and 10 years lead to appreciably higher levels of compensation.

These simple comparisons represent a snapshot on standard bases and are difficult to interpret for the following reasons:

- The gap between the Society's payouts and the industry average is likely to narrow considerably in the future as other companies reflect reduced investment returns in lower bonuses and policy values over a reasonably short period of time;
- The flexibility of the Society's policies tends to mean that the payouts shown in surveys may be flattering to competitors' results, since the flexibility of maturity of the Society's policies allows benefits to be taken as maturity values, whereas competitors' true comparative values ought sometimes to be on a surrender basis;

This current lack of guidance on the constitution of classes prior to the convening hearing, meetings and sanction hearing has recently been recognised by the Court of Appeal.

The Society has been advised to seek as much guidance as practicable in the circumstances from the court on the issue of classes at the convening hearing.

7.6 Class meetings and voting

Section 425 requires that the scheme be approved by each class of policyholder by a majority in number representing three fourths in value of the policyholders present and voting at the meeting. Policyholders may vote in person or by proxy.

If a policyholder votes by proxy, then the proxy form will be in the special form previously settled with the court at the convening hearing. The proxy forms will contain an indicative statement of the Policy Value that will be very close to the value used for voting purposes. It is not possible to give the actual value as that can only be calculated on the day of the meeting. Policyholders are requested to indicate on the proxy form whether they will vote for or against the scheme.

7.7 Valuation for voting

The value for voting for policyholders will be the relevant Policy Value as at the date of the meeting, or the guaranteed value if higher. The importance of determining the valuation of the policies cannot be overestimated as the policyholders' votes must be valued to determine whether the requisite majority in value has voted in favour of a scheme and a failure to apply an appropriate value or indeed the inability to value a claim may be fatal to the scheme.

7.8 The voting process

The voting process will be undertaken on an independent basis by Computershare, specialists in conducting corporate ballots. The vote will be independently scrutinised by KPMG. A policyholder may cast his vote either in favour of the scheme or against the scheme. As set out above, a policyholder may appoint a proxy to attend the meeting on his/her behalf.

There are a number of issues which relate to particular types of policyholders who have specific positions:

Policyholders who hold both GAR policies and non-GAR policies will be entitled to vote in both classes. Their vote in the GAR class will be equal to the total Policy Value of all their GAR policies at the date of the class meeting. The vote in the non-GAR class will be the total Policy Value of all their non-GAR policies at the date of the class meeting.

To the extent that GAR policies also have non-GAR benefits under the policy, the policyholder will be able to vote in the GAR and non-GAR classes with the relevant GAR and non-GAR value.

7.3 The scheme document

Although there are no statutory provisions covering the content of the scheme itself, the document will almost certainly contain the following:

- a Definitions and Interpretation section;
- a description of the Society and a summary of its objects;
- a clause setting out the purpose of the scheme;
- a clause setting out whom the scheme will bind;
- the mechanism for the removal of the GAR rights of GAR policyholders;
- the formula and mechanism by which the increases to GAR policyholders' Policy Values are applied;
- the mechanism for the waiver and releases of the relevant rights of GAR and non-GAR policyholders to make claims against the Society;
- the formula and mechanism by which the increase to non-GAR policyholders' Policy Values is applied;
- a description of the effective date and other key timing provisions of the scheme; and
- a provision reflecting the right of the Society to consent to modifications to the scheme ordered by the court at the sanction stage.

7.4 The explanatory statement

There is a statutory requirement that there be a document sent with the scheme explaining the effect of the scheme known as 'the explanatory statement'. Section 426 of the Companies Act, together with case law, requires that the following information should be set out in the Explanatory Statement:

- an explanation of the effect of the compromise or arrangement in language that enables the ordinary lay person to understand it;
- a statement of any material interest of a director in the scheme; and
- any other information known to the directors which is material to the making of a decision by a policyholder on whether or not to agree to the compromise or arrangement.

The Court may reject the scheme if the Explanatory Statement is found to be inadequate.

7.5 The application to the court to convene the meetings of policyholders

Section 425 of the Companies Act requires an application be made to the court for permission to convene the meetings of policyholders (or classes of them) to consider and, if thought fit, to approve the scheme. Historically the court took little interest in whether the classes had been correctly determined at this stage. On occasion that has meant that a court has made an order to convene the policyholders' meetings for voting, the scheme has received the requisite votes in favour and the court has decided at the final sanction hearing (where it considers fairness) that the classes were not correctly identified so the court has no jurisdiction to sanction the scheme.

- It is difficult, if not impossible, to find competitive products which offer the range of features of the Society's product. It is therefore questionable whether truly comparable figures can be produced;
- There are serious practical difficulties in relation to the valuation of the more flexible benefits in the Society's policies and the unreliability of comparison of policy values at a time when the Society has adjusted to reflect falls in asset values and other companies are phasing adjustments to bring policy values into line with underlying asset values.

5.3 Conclusion

Different approaches are more appropriate for different types of legal claim. The third approach, based on industry comparisons, produces results very close to the House of Lords' impact as set out in 5.2.2. As this is readily calculable, the Board has therefore decided to adopt the compensation basis set out in 5.2.2.

The basis of the non-GAR compensation therefore has two elements:

- an addition to Policy Values to compensate for giving up potential claims and in respect of the Halifax £250 million;
- an addition to guaranteed benefits to restore guaranteed bonus for the year 2000.

6 Calculation of the compensation

6.1 How the 2.5% increase is calculated

The increase of 2.5% for non-GAR policyholders has been calculated as follows:

The theoretical aggregate sum of all these potential claims of current non-GAR policyholders (following the approach described above) has been estimated to be £850 million (approximately 5% of their share of the with-profits fund). However, not all these claims are likely to be successful. The range of probability of success of these potential claims, when taken as a whole, was estimated by the Society's legal advisers to vary widely from perhaps 20% to 70%.

Around 75% by value of the Society's with-profits fund is made up of non-GAR policies. Any successful claims would have to be met out of the with-profits fund largely owned by non-GAR policyholders. Therefore around 75% of non-GAR policyholders' claims could end up being paid for by non-GAR policyholders themselves. As a result compensation would have to be reduced by 75%. The Society has received differing legal advice on whether, if a claim was framed in a certain way, this would still be the case, or whether the cost would be borne by the GAR policyholders. The range of discount on account of this would therefore be up to 75% depending on which legal opinions were followed. The lawyers, however, all agree that there is doubt and that a contrary view to that which they have expressed is arguable. There is insufficient time to bring a test case to resolve the issue if the compromise is to be in place before 1 March 2002 which is the deadline for receipt of the Halifax £250 million.

In summary, the total estimated value of potential claims of £850 million needs to be discounted with regard to the probability of success (between 20% and 70%) and with regard to non-GAR policyholders paying for non-GAR claims themselves (between 0% and 75% but expected to be between 25% and 65%). Having carefully examined the range of legal advice the new Board has taken the view that the likely value for potential claims lies in the range of £100 million to £300 million and has decided to propose a scheme using a value of £220 million.

This sum of £220 million equates to an uplift of 1.4% across all non-GAR Policy Values. This together with the non-GAR proportion of the Halifax £250 million brings the uplift to 2.5% in total for non-GAR policies.

6.2 Overall uplift

Once the uplifts for the GAR compromise as detailed in section 3 are adjusted to reflect the potential non-GAR liabilities, and the Halifax £250 million is taken into account, the overall scheme uplifts would be as follows:

- **GAR policyholders receive on average an uplift of 17.5% on their GAR Policy Values in exchange for giving up their GAR rights.** This includes an average 16.2% increase on their guaranteed fund because the average uplift of 1.3% in respect of Halifax money is not added to the guaranteed fund.
- **non GAR policyholders without GARs receive an uplift of 2.5% on their Policy Value in settlement of any claims against the Society related to the existence of the GARs.** The Halifax £250 million, which is part of the 2.5%, increases non-guaranteed Policy Values by 1.1%. For policies entitled to declared bonus, guaranteed benefits will also be uplifted by an amount to compensate for the guaranteed bonuses that would reasonably have been expected to be declared for the year 2000 in the absence of the House of Lords' judgment.

Examples showing the application of the guaranteed and final bonus elements of the GAR and non-GAR Policy Values can be found on pages 14 to 18 of the *Proposed Compromise* document.

PART III - IMPLEMENTATION OF THE SCHEME

7.1 Introduction

The legal procedure required to implement the scheme involves the following steps:

- the legal design of the scheme;
- the preparation of the scheme document;
- the preparation of the explanatory statement;
- the application to the court to convene the separate meetings for the GAR and non-GAR policyholders;
- the holding of meetings of policyholders to obtain approval of the scheme by the specified majorities;
- the court hearing for sanction of the scheme; and
- the filing of a copy of the scheme and an office copy of the order of the court sanctioning the scheme with the Registrar of Companies at Companies House.

7.2 Legal design of the scheme and classes

The 'compromise' or 'arrangement' between the Society and its GAR and non-GAR policyholders is required to be clearly identified. In the case of GAR policyholders the nature of the compromise or arrangement is that amendments will be made to their policies removing the GAR benefit in consideration for an uplift of Policy Values and they will waive their rights as described in section 3.6. In the case of non-GAR policyholders the nature of the compromise is that they will give up certain rights to make claims against the Society in relation to the existence of the GAR liability in consideration for an uplift of their Policy Values. Each class is agreeing to the crystallisation of the value of the other's rights, thereby giving up the possibility that those rights might become more or less valuable in the future.

The correct identification of classes for voting is one of the pillars of fairness in relation to the scheme. If the Society were to identify the classes incorrectly in relation to the proposed scheme, the court could hold that it had no jurisdiction to sanction the scheme. It would not be possible to cure the defect by amendment to the scheme. A redraft and revote would be necessary and the timing implications of this would mean that it would be certain that the Halifax £250 million would not accrue. It is the responsibility of the Society and not the court to ensure that the classes are correctly constituted. Classes are essentially determined by an analysis of the relevant legal rights of the policyholders against the Society. Policyholders can be in the same class for voting if their rights are not so dissimilar that it is impossible for them to consult together with regard to their common interests. Their legal rights do not therefore need to be identical.

Leading Counsel, Gabriel Moss QC and David Richards QC, have considered that the proposed scheme should consist of two classes, GAR policyholders and non-GAR policyholders.