

BRETT & WATSON PTY. LTD.

A.B.N. 65 060 568 676

CONSULTING ACTUARIES

19 December 2022

Mr D Silvy
Company Secretary and Chief Investment Officer
KeyInvest Ltd
PO Box 3340
Rundle Mall SA 5000

Dear Dion,

Proposed Benefit Fund Restructure – Actuarial Opinion

Introduction

Thank you for your request to prepare the actuarial opinion regarding the proposed restructure of the AFS Funeral Benefit Fund Taxable Fund and AFS Funeral Benefit Fund Non-Assessable Fund (AFS Funds) into the KeyInvest Funeral Bond Fund (Capital Guaranteed Benefit Fund under Division 6 of the KeyInvest Benefit Fund Rules).

This actuarial opinion has been prepared under APRA Prudential Standard LPS700 – Friendly Society Benefit Funds. Under the proposed restructure, all the assets and liabilities of the AFS Funds are to be transferred to the KeyInvest Funeral Bond Fund. Therefore, the actuarial opinion is required to certify that:

- The effect of the restructure does not result in any unfairness to members of and owners of policies referable to the AFS Funds and the KeyInvest Funeral Bond Fund, and
- After the restructure, the KeyInvest Funeral Bond Fund will comply with the APRA Prudential Standards LPS110 – Capital Adequacy and LPS112 – Capital Adequacy: Measurement of Capital.

The following items are considered in this opinion:

- Proposed rules
- Capital guarantee
- Fees
- Investments
- Financial position
- Other terms and conditions.

Deborah Jones FIAA - **Geoff Keen** FIAA - **Victor Tien** FIAA, CERA - **Bruce Watson** FIAA

Level 1, 26 Flinders Street, Adelaide SA 5000

Telephone: (08) 8232 1333

Email: contact@brettandwatson.com.au

Website: www.brettandwatson.com.au

Rules

Following the merger between KeyInvest Ltd and Australian Friendly Society Ltd, the AFS Funds are closed to new members from 31 October 2022 and new members who select a capital guaranteed funeral bond will join the KeyInvest Funeral Bond Fund. The effect of the proposed restructure will be that the terms and conditions in the KeyInvest Funeral Bond Fund Rules will be adopted for the AFS Funds' members and policies. Some changes are being made to the KeyInvest Funeral Bond Fund Rules that preserve terms conditions that existed in the Rules of the AFS Funds.

Capital Guarantee

All Benefit Funds involved in the restructure are capital guaranteed Funeral Benefit Funds whereby members' benefits are based on their accumulated account balances. As all Benefit Funds involved in the restructure include this capital guarantee, the restructure does not result in any unfairness to members.

Fees

The maximum fee in the Rules of the AFS Funds is 3% of the average of the Fund's assets per annum, inclusive of investment management costs.

Prior to the restructure, the maximum management fee rate in the KeyInvest Funeral Bond Fund Rules is 2.5% of the average of the Fund's assets per annum. Investment expenses are an additional expense. The sum of the maximum management fees and the current rate of investment fees in the KeyInvest Funeral Bond is less than the AFS Funds' maximum fee rate of 3%.

The actual fee rates currently being charged for KeyInvest Funeral Bond Fund policies are 1.795% for members who joined prior to 1 June 2013 and 1.495% for members who joined from 1 June 2013.

Under the Merger Scheme, the fee rate for the AFS Funds is 1.45% from 31 October 2022 to 31 October 2025 and thereafter no more than 1.6% or the rate charged to post June 2013 members (currently 1.495%), whichever is lower. These fee rates for the former AFS Funds' members are reflected in the Rules of the restructured Fund. There is no unfairness to members of the AFS Funds upon the transfer to the restructured Fund.

There is no change to fee rates applicable to the KeyInvest Funeral Bond Fund members as at the restructure date or for new members who join the Fund after the restructure date. There is no unfairness to these members as a result of the restructure.

Investments

There are significant differences between the Rules of the AFS Funds and the KeyInvest Funeral Bond relating to investments, as shown in Appendix A. The existing actual asset allocation is also shown in Appendix A. The revised Rules reduce the minimum allocation to “Cash” from 20% to 0% in the KeyInvest Funeral Bond Fund.

The impact of the change in Rules on investments for AFS Funds’ members are:

- Large reduction in allocation to term deposits.
- Increase in allocation to other asset sectors with a higher risk profile and, in practice, this is predominantly to mortgages and investment grade corporate debt.
- Introduction of the use derivatives for non speculative investment.

The Rules of all Funds do not specify limits on duration to maturity or the overall level of credit quality. These metrics are controlled in the KeyInvest Funeral Bond Fund via the selection process and credit assessment for direct mortgages and the investment mandate with Janus Henderson for the remaining assets.

Modelling that we have undertaken indicate that future bonus rates for the AFS Funds’ policies would increase by of the order of 0.5% to 1.0% per annum on average by adoption of an investment profile similar to the asset allocation for the KeyInvest Funeral Bond Fund with exclusion of short term money market assets due to the reduction in the minimum “Cash” allocation to nil. The modelling also demonstrates the capacity of the Management Fund to support the risk associated with the investment profile for the restructured Fund. The modelling is contained in a separate report dated 22 November 2022.

The change in investments is expected to enhance returns to AFS Funds’ members, with an increase in the expected volatility of returns as there is greater exposure to market movements. Given the long term nature of the liabilities, I consider that the restructured Fund and the Society is able to withstand the increased volatility of investment returns and that the proposed change to investments for AFS Funds’ members does not result in unfairness to those members.

Financial Position

There are significant differences in the financial position of each of the following groups of members (based on data as at 31 October 2022):

- members of AFS Funeral Benefit Fund Taxable.
- members of AFS Funeral Benefit Fund Non-Assessable.
- members of the KeyInvest Funeral Bond.

These differences are too large to achieve equity by way of a benefit equalisation on the restructure date. In order to maintain equity between each of these groups of members, the Rules of the restructured Fund provide a mechanism such that KeyInvest maintains separate revenue accounts for each of these groups of members. As a result, there is no unfairness to members of any of the Funds involved in the restructure.

Appendix B sets out the financial position for each Fund as at 31 October 2022 and for the combined Fund post restructure (had the restructure occurred on 31 October 2022). Appendix B shows that the restructured Fund is in a strong capital position. The net assets of the Fund less the non-discretionary policy liabilities and capital adjustments equal \$46.5 million. This is equal to 195% of the prescribed risk charges of \$23.9 million. The capital position is expected to be similar as at the actual restructure date of 31 March 2023 or the date that the restructure is approved by APRA (whichever is later). Therefore, the restructured Fund will comply with APRA Prudential Standards LPS110 – Capital Adequacy and LPS112 – Measurement of Capital.

Other Terms and Conditions

There are some other changes to the Rules relating to applications made by a trustee for a nominated life assured that preserve existing provisions that existed in the AFS Funds prior to the restructure. These Rule changes exist in the General Rules, so apply to either all KeyInvest Benefit Funds or to all KeyInvest Funeral Benefit Funds. These changes do not adversely affect the existing KeyInvest Benefit Fund members or new members. Therefore, there is no unfairness to existing or prospective members as a result of the proposed restructure.

The cooling off period has been increased to 30 days, which does not result in unfairness to existing or prospective members of the KeyInvest Funeral Bond Fund.

Actuarial Opinion

I consider that:

- The effect of the restructure does not result in any unfairness to members of and owners of policies referable to the AFS Funds and the KeyInvest Funeral Bond Fund, and
- After the restructure, the KeyInvest Funeral Bond Fund will comply with the APRA Prudential Standards LPS110 – Capital Adequacy and LPS112 – Capital Adequacy: Measurement of Capital.

Please let me know if you require any further information.

Yours sincerely,



B A Watson
Fellow of the Institute of Actuaries of Australia

APPENDIX A : EXISTING ASSET ALLOCATIONS

A.1 AFS FUNDS RULES

The permissible range for each of the major investment categories for the Fund are as follows:

Investment Category	Allowable Range
Cash and equivalent, bank bills, term deposits, negotiable certificates of deposit and government securities	70% - 100%
Equities	0% - 10%
Other investments similar in nature to those specified	0% - 20%

A.2 KEYINVEST FUNERAL BOND RULES

Investments of the Fund will fall within the following minimum and maximum percentages for each Asset Class below:

<u>Asset Class</u>	<u>Minimum</u>	<u>Maximum</u>
Cash	20%	100%
Australian Fixed Interest	0%	80%
Australian Shares	0%	40%
Australian Listed Mortgage Trusts	0%	25%
Australian Registered 1st	0%	25%

Note that Cash includes short term money market and term deposits.

A.3 CURRENT ASSET ALLOCATIONS

<u>Fund</u>	<u>KeyInvest Funeral Bond</u>	<u>AFS Funeral Taxable</u>	<u>AFS Funeral Untaxed</u>
Cash	4%	4%	1%
Term Deposits	0%	74%	78%
Fixed Interest Bonds	51%	1%	0%
Floating Rate Notes #	14%	20%	20%
Discount Securities	16%	0%	0%
Property	0%	0%	0%
Listed Equities #	0%	1%	1%
Unlisted Equities	0%	0%	0%
Mortgages	14%	0%	0%

APPENDIX B : VALUATION RESULTS

Fund	Valuation Results				Regulatory Capital							
	Assumed Future Fee Rate	Net Assets	Non- Discretionary Liabilities	Discretionary Component Liabilities	Capital Adjustments	Surplus After Capital Adjustments	Asset Risk Charge	Insurance Risk Charge	Aggregation Benefit	Prescribed Risk Charges	Regulatory Capital Surplus	Regulatory Capital Surplus (%)
	A	B	C	D = B + C	E	F = D + E	G	H	I	J	K = F - J	L = K / J
		\$000s	\$000s	\$000s	\$000s	\$000s	\$000s	\$000s	\$000s	\$000s	\$000s	%
KIFB	1.60%	117,217	(98,532)	18,685	(1,743)	16,942	9,603	2,151	(1,502)	10,252	6,690	65%
AFS Taxed	1.45%	142,558	(117,932)	24,626	(598)	24,028	10,888	2,442	(1,704)	11,625	12,403	107%
AFS Untaxed	1.45%	17,227	(13,732)	3,495	-	3,495	1,239	357	(240)	1,356	2,139	158%
Restructured	1.50%	277,002	(228,135)	48,867	(2,341)	46,526	22,348	5,046	(3,519)	23,874	22,652	95%

Notes

- A The Assumed Future Fee Rate is the rate assumed to apply in the valuation of the non-discretionary component of liabilities under the stressed scenario in the capital standards.
- B Net Assets is equal to Gross Assets less Non-Policy Liabilities.
- E Capital Adjustments consist of Deferred Tax Assets in excess of Deferred Tax Liabilities.