

**LOTUS REINSURANCE COMPANY LTD.**

Financial Statements and  
Report of Independent Auditors

As of the period ended December 31, 2021, from September 29, 2021 (Commencement of Operations)

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## **Report of Independent Auditors**

To the Members of the Finance and Audit Committee of Lotus Reinsurance Company Ltd.

### ***Opinion***

We have audited the accompanying financial statements of Lotus Reinsurance Company Ltd. (the “Company”), which comprise the statement of financial position as of December 31, 2021, and the related statement of operations and comprehensive income, of equity and of cash flows for the period from September 29, 2021 to December 31, 2021, including the related notes (collectively referred to as the “financial statements”).

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021, and the result of its operations and its cash flows for the period from September 29, 2021 to December 31, 2021 in accordance with accounting principles generally accepted in the United States of America.

### ***Basis for Opinion***

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (US GAAS). Our responsibilities under those standards are further described in the Auditors’ Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Responsibilities of Management for the Financial Statements***

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company’s ability to continue as a going concern for one year after the date the financial statements are available to be issued.

### ***Auditors’ Responsibilities for the Audit of the Financial Statements***

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors’ report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with US GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material



if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with US GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

PricewaterhouseCoopers LLP

New York, New York  
April 22, 2022

**LOTUS REINSURANCE COMPANY LTD.**  
**Statement of Financial Position**  
**December 31, 2021 (in thousands, except share amounts)**

	<b>2021</b>
<b>ASSETS</b>	
Fixed maturities, available-for-sale, at fair value (allowance for credit losses: 2021 - \$0) (amortized cost: 2021 - \$98,295)	\$ 113,388
Total investments	113,388
Cash and cash equivalents	33,576
Accrued investment income	1,652
<b>TOTAL ASSETS</b>	<b>\$ 148,616</b>
<b>LIABILITIES AND EQUITY</b>	
<b>LIABILITIES</b>	
Future policy benefits, at fair value	\$ 24,095
Income taxes	29
Reinsurance payables	263
Other liabilities	260
Total liabilities	24,647
<b>EQUITY</b>	
Common stock (\$1 par value; 250,000 shares authorized, issued and outstanding)	250
Additional paid-in capital	111,117
Accumulated other comprehensive income (loss)	12,025
Retained earnings	577
Total equity	123,969
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 148,616</b>

See Notes to Financial Statements

**LOTUS REINSURANCE COMPANY LTD.**

**Statement of Operations and Comprehensive Income  
September 29, 2021 to December 31, 2021 (in thousands)**

	<b>2021</b>
<b>REVENUES</b>	
Net investment income	\$ 1,023
Total revenues	1,023
<b>BENEFITS AND EXPENSES</b>	
Changes in fair value of reinsurance balance	15
General, administrative and other expenses	278
Total benefits and expenses	293
<b>INCOME (LOSS) FROM OPERATIONS BEFORE INCOME TAXES</b>	730
Income tax expense (benefit)	153
<b>NET INCOME (LOSS)</b>	\$ 577
Other comprehensive income (loss):	
Net unrealized investment gains (losses)	15,093
Non-performance risk reserve	128
Less: Income tax expense (benefit) related to other comprehensive income (loss)	3,196
<b>COMPREHENSIVE INCOME (LOSS)</b>	\$ 12,602

See Notes to Financial Statements

**LOTUS REINSURANCE COMPANY LTD.**

**Statement of Equity  
September 29, 2021 to December 31, 2021 (in thousands)**

	<b>Common Stock</b>	<b>Additional Paid-in Capital</b>	<b>Retained Earnings</b>	<b>Accumulated Other Comprehensive Income (Loss)</b>	<b>Total Equity</b>
<b>BALANCE, SEPTEMBER 29, 2021</b>	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Capital contributions from parent	250	123,609			123,859
Contributed (distributed) capital - parent/ child asset transfers		(12,492)			(12,492)
Comprehensive income:					
Net income (loss)			577		577
Other comprehensive income (loss)				12,025	12,025
Total comprehensive income (loss)					12,602
<b>BALANCE, DECEMBER 31, 2021</b>	<u>\$ 250</u>	<u>\$ 111,117</u>	<u>\$ 577</u>	<u>\$ 12,025</u>	<u>\$ 123,969</u>

**See Notes to Financial Statements**

**LOTUS REINSURANCE COMPANY LTD.**

**Statement of Cash Flows**  
**September 29, 2021 to December 31, 2021 (in thousands)**

	<b>2021</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>	
Net income (loss)	\$ 577
Adjustments to reconcile net income (loss) to net cash provided by operating activities:	
Amortization	(4)
Change in:	
Future policy benefits, at fair value	24,223
Income taxes	153
Other, net	58
<b>Cash flows from (used in) operating activities</b>	<b>25,007</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>	
Proceeds from the sale/maturity/prepayment of:	
Fixed maturities, available-for-sale	69
<b>Cash flows from (used in) investing activities</b>	<b>69</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>	
Common stock issued	250
Capital contributions from parent	8,250
<b>Cash flows from (used in) financing activities</b>	<b>8,500</b>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>33,576</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<b>0</b>
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<b>\$ 33,576</b>

**Significant Non-Cash Transactions**

In October 2021, the Company received invested assets of \$98 million from Prudential Insurance Company of America. See Note 8 for additional information.

**See Notes to Financial Statements**

**LOTUS REINSURANCE COMPANY LTD.**  
**Notes to Financial Statements**

**1. BUSINESS AND BASIS OF PRESENTATION**

Effective February 1, 2022, Lotus Reinsurance Company Ltd., ("Lotus Re" or the "Company") is a wholly-owned subsidiary of Prudential International Insurance Holdings, Ltd. ("PIIH"), which in turn is a direct wholly-owned subsidiary of Prudential Financial, Inc. ("PFI"), a United States of America ("U.S.") Corporation. Prior to February 1, 2022, Lotus Re was wholly-owned by The Prudential Insurance Company of America ("Prudential Insurance"), a direct wholly-owned subsidiary of PFI. See Note 10 for additional information regarding the transfer of ownership.

The Company was incorporated as a Bermuda exempted company on August 5, 2021 and licensed as a Class E insurer by the Bermuda Monetary Authority ("BMA"), under the Bermuda Insurance Act of 1978 (the "Act"), on September 29, 2021.

Effective October 1, 2021, the Company entered into a reinsurance agreement with Pruco Life Insurance Company ("Pruco Life"), a wholly-owned subsidiary of Prudential Insurance domiciled in the U.S., to reinsure, on a coinsurance basis, a closed block of variable life policies in the extended term status.

See Note 5 for additional information regarding the Company's reinsurance agreements.

***Basis of Presentation***

The Company's financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP").

The Company's financial statements have been prepared for the period September 29, 2021 to December 31, 2021.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant estimates include those used in determining the estimated fair value of future policy benefits and valuation of investments.

***COVID-19***

Since 2020, the novel coronavirus ("COVID-19") has resulted in extreme stress and disruption in the global economy and financial markets. While markets have rebounded, the pandemic may adversely impact the Company's results of operations, financial condition and cash flows. Due to the highly uncertain nature of these conditions, it is not possible to estimate the ultimate impacts at this time. The risks may manifest in the Company's financial statements in the areas of, among others, i) investments: increased risk of loss on the Company's investments due to default or deterioration in credit quality or value; and ii) assumed insurance liabilities and related balances: potential changes to assumptions regarding investment returns, mortality and policyholder behavior which are reflected in the Company's assumed insurance liabilities. The Company cannot predict what impact the COVID-19 pandemic will ultimately have on its business.

**2. SIGNIFICANT ACCOUNTING POLICIES AND PRONOUNCEMENTS**

**ASSETS**

***Fixed maturities, available-for-sale, at fair value*** ("AFS debt securities") are comprised of bonds and redeemable preferred stock that are carried at fair value. See Note 4 for additional information regarding the determination of fair value. The purchased cost of fixed maturities is adjusted for amortization of premiums and accretion of discounts to maturity or, if applicable, call date.

AFS debt securities, where fair value is below amortized cost, are reviewed quarterly to determine whether the amortized cost basis of the security is recoverable. For AFS debt securities, qualitative factors are first considered including, but not limited to, the extent of the decline and the reasons for the decline in value (e.g., credit events, currency or interest-rate related, including

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**Notes to Financial Statements**

general credit spread widening), and the financial condition of the issuer. If analysis of these qualitative factors results in the security needing to be impaired, the credit impairment will be measured as the extent to which the amortized cost exceeds the net present value. The net present value is calculated by discounting the Company's best estimate of projected future cash flows at the effective interest rate implicit in the AFS debt security at the date of acquisition.

Credit impairment is recognized as an allowance for credit losses and reported in "Realized investment gains (losses), net." Once the Company has deemed all or a portion of the amortized cost uncollectible, the allowance is removed from the balance sheet by writing down the amortized cost basis of the AFS debt security.

Interest income, including amortization of premium and accretion of discount, are included in "Net investment income" under the effective yield method. Prepayment premiums are also included in "Net investment income."

The Company may use the estimated fair value of collateral, if any, as a proxy for the net present value if it believes that the security is dependent on the liquidation of collateral for recovery of its investment. If the net present value is less than the amortized cost of the investment, an allowance for losses is recognized in earnings for the difference between amortized cost and the net present value and is limited to the difference between amortized cost and fair value of the AFS debt security. Any difference between the fair value and the net present value of the debt security at the impairment measurement date remains in "Other Comprehensive Income (Loss)" ("OCI"). Changes in the allowance for losses are reported in "Realized investment gains (losses), net."

When an AFS debt security's fair value is below amortized cost and (1) the Company has the intent to sell the AFS debt security, or (2) it is more likely than not the Company will be required to sell the AFS debt security before its anticipated recovery, the amortized cost basis of the AFS debt security is written down to fair value and any previously recognized allowance is reversed. The impairment is reported in "Realized investment gains (losses), net."

The associated unrealized gains and losses are included in "Accumulated other comprehensive income (loss)" ("AOCI").

**Cash and cash equivalents** include cash on hand, amounts due from banks, certain money market investments and funds managed similar to regulated money market funds. These assets are generally carried at fair value or amortized cost which approximates fair value.

**Accrued investment income** primarily includes accruals of interest income from investments that have been earned but not yet received.

## **LIABILITIES**

**Future policy benefits, at fair value** is primarily comprised of the present value of estimated future payments to or on behalf of policyholders, where the timing and amount of payment depends on policyholder mortality, less the present value of future net premiums. This liability includes reserves related to life policies. The Company has elected to use the Fair Value Option ("FVO") to measure these liabilities. For additional information see Note 4.

The impacts to the liability driven by changes in the Company's non-performance risk ("NPR") spread are included in AOCI.

The Company's liability for future policy benefits also includes a liability for unpaid claims. The Company does not establish claim liabilities until a loss has been incurred. However, unpaid claims include estimates of claims that the Company believes have been incurred but have not yet been reported as of the balance sheet date.

**Income taxes** primarily represents the Company's estimated taxes payable for the current period and net deferred tax asset.

The Company has filed an election to be treated as a US taxpayer for federal income tax purposes in accordance with IRC Section 953(d) and is a member of the federal income tax return of Prudential Financial. Pursuant to the tax allocation arrangement with Prudential Financial, total federal income tax expense is determined on a separate company basis. Members record tax benefits to the extent tax losses or tax credits are recognized in the consolidated federal tax provision.

Items required by tax regulations to be included in the tax return may differ from the items reflected in the financial statements. As a result, the effective tax rate reflected in the financial statements may be different than the actual rate applied on the tax return. Some of these differences are permanent such as expenses that are not deductible in the Company's tax return, and some differences are temporary, reversing over time, such as valuation of insurance reserves. Temporary differences create deferred

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### Notes to Financial Statements

tax assets and liabilities. Deferred tax assets generally represent items that can be used as a tax deduction or credit in future years for which the Company has already recorded the tax benefit in the Company's Statements of Operations. Deferred tax liabilities generally represent tax expense recognized in the Company's financial statements for which payment has been deferred, or expenditures for which the Company has already taken a deduction in the Company's tax return but have not yet been recognized in the Company's financial statements.

Deferred income taxes are recognized, based on enacted rates, when assets and liabilities have different values for financial statement and tax reporting purposes. The application of U.S. GAAP requires the Company to evaluate the recoverability of the Company's deferred tax assets and establish a valuation allowance if necessary to reduce the Company's deferred tax assets to an amount that is more likely than not expected to be realized. Considerable judgment is required in determining whether a valuation allowance is necessary, and if so, the amount of such valuation allowance. See Note 6 for a discussion of factors considered when evaluating the need for a valuation allowance.

U.S. GAAP prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that a company has taken or expects to take on tax returns. The application of this guidance is a two-step process. First, the Company determines whether it is more likely than not, based on the technical merits, that the tax position will be sustained upon examination. If a tax position does not meet the more likely than not recognition threshold, the benefit of that position is not recognized in the financial statements. The second step is measurement. The Company measures the tax position as the largest amount of benefit that is greater than 50 percent likely to be realized upon ultimate resolution with a taxing authority that has full knowledge of all relevant information. This measurement considers the amounts and probabilities of the outcomes that could be realized upon ultimate settlement using the facts, circumstances, and information available at the reporting date.

The Company's liability for income taxes includes a liability for unrecognized tax benefits, interest and penalties which relate to tax years still subject to review by the Internal Revenue Service ("IRS") or other taxing jurisdictions. Audit periods remain open for review until the statute of limitations has passed. Generally, for tax years which produce net operating losses, capital losses or tax credit carryforwards ("tax attributes"), the statute of limitations does not close, to the extent of these tax attributes, until the expiration of the statute of limitations for the tax year in which they are fully utilized. The completion of review or the expiration of the statute of limitations for a given audit period could result in an adjustment to the liability for income taxes. The Company classifies all interest and penalties related to tax uncertainties as income tax expense. See Note 6 for additional information regarding income taxes.

*Reinsurance payables* consist of payables associated with a reinsurance arrangement. For additional information about this arrangement see Note 5.

*Other liabilities* consist primarily of accrued expenses.

### REVENUES AND BENEFITS AND EXPENSES

*Changes in fair value of reinsurance balance* consists of (1) Premiums from reinsurance agreements and allowance for commissions and expenses recognized when due; and (2) Policyholders' benefits recognized when incurred. Changes in future policy benefits are recorded when premiums are recognized using a fair value methodology.

### OTHER ACCOUNTING POLICIES

#### *Reinsurance*

For each of its reinsurance contracts, the Company determines if the contract provides indemnification against loss or liability relating to insurance risk in accordance with applicable accounting standards. The Company reviews all contractual features, particularly those that may limit the amount of insurance risk to which the reinsurer is subject or features that delay the timely reimbursement of claims.

The Company has elected to use the FVO to value the insurance liabilities under reinsurance transactions. The fair value is reported in "Future policy benefits, at fair value." See Note 4 for additional information.

Reinsurance payables relating to the reinsurance agreement with Pruco Life are included in "Reinsurance payables" on a net basis on the balance sheet as a right of offset exists within the reinsurance agreement.

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See Note 5 for additional information about the Company's reinsurance agreement.

**RECENT ACCOUNTING PRONOUNCEMENTS**

Changes to U.S. GAAP are established by the Financial Accounting Standards Board ("FASB") in the form of Accounting Standards Updates ("ASUs") to the FASB Accounting Standards Codification. The Company considers the applicability and impact of all ASUs. There were no ASUs adopted during the current fiscal year. ASUs issued but not adopted as of December 31, 2021, and as of the date that these financial statements were available to be issued were assessed and determined to be either not applicable or not material.

**3. INVESTMENTS**

*Fixed Maturity Securities*

The following table sets forth the composition of fixed maturity securities, as of the date indicated:

	December 31, 2021				Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Allowance for Credit Losses	
	(in thousands)				
<b>Fixed maturities, available-for-sale:</b>					
Obligations of U.S. states and their political subdivisions	\$ 40,178	\$ 7,248	\$ 0	\$ 0	\$ 47,426
Foreign government bonds	5,363	107	0	0	5,470
U.S. public corporate securities	32,422	6,479	0	0	38,901
Foreign public corporate securities	20,332	1,259	0	0	21,591
Total fixed maturities, available-for-sale	<u>\$ 98,295</u>	<u>\$ 15,093</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 113,388</u>

The following table sets forth the amortized cost and fair value of fixed maturities by contractual maturities, as of the date indicated:

	December 31, 2021	
	Amortized Cost	Fair Value
	(in thousands)	
<b>Fixed maturities, available-for-sale:</b>		
Due in one year or less	\$ 6,088	\$ 6,196
Due after one year through five years	38,844	42,093
Due after five years through ten years	13,850	18,717
Due after ten years	39,513	46,382
Total	<u>\$ 98,295</u>	<u>\$ 113,388</u>

Actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations.

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**Notes to Financial Statements**

The following table sets forth the sources of fixed maturity proceeds, as of the date indicated:

	<b>September 29, 2021 to December 31, 2021</b>
	<b>(in thousands)</b>
<b>Fixed maturities, available-for-sale:</b>	
Proceeds from sales	\$ 69

For the period September 29, 2021 to December 31, 2021, there was no activity in the allowance for credit losses for fixed maturity securities.

See Note 2 for additional information about the Company's methodology for developing our allowance and expected losses.

The Company did not have any fixed maturity securities purchased with credit deterioration as of December 31, 2021.

***Accrued Investment Income***

The following table sets forth the composition of "Accrued investment income" as of the date indicated:

	<b>December 31, 2021</b>
	<b>(in thousands)</b>
Fixed maturities	\$ 1,652
Cash and cash equivalents	0
Total accrued investment income	\$ 1,652

There were no write-downs on accrued investment income for the period September 29, 2021 to December 31, 2021.

***Net Investment Income***

The following table sets forth "Net investment income" by investment type, for the period indicated:

	<b>September 29, 2021 to December 31, 2021</b>
	<b>(in thousands)</b>
Fixed maturities, available-for-sale	\$ 1,038
Cash and cash equivalents	0
Gross investment income	1,038
Less: investment expenses	(15)
Net investment income	\$ 1,023

***Net Unrealized Gains (Losses) on Investments within AOCI***

The following table sets forth net unrealized gains (losses) on investments, as of the date indicated:

	<b>December 31, 2021</b>
	<b>(in thousands)</b>
Fixed maturity securities, available-for-sale	\$ 15,093
Net unrealized gains (losses) on investments	\$ 15,093

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**4. FAIR VALUE OF ASSETS AND LIABILITIES**

**Fair Value Measurement** – Fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The authoritative fair value guidance establishes a framework for measuring fair value that includes a hierarchy used to classify the inputs used in measuring fair value. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The levels of the fair value hierarchy are as follows:

Level 1 - Fair value is based on unadjusted quoted prices in active markets that are accessible to the Company for identical assets or liabilities.

Level 2 - Fair value is based on significant inputs, other than quoted prices included in Level 1, that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability through corroboration with observable market data. Level 2 inputs include quoted market prices in active markets for similar assets and liabilities, quoted market prices in markets that are not active for identical or similar assets or liabilities, and other market observable inputs. The Company's Level 2 assets and liabilities include: fixed maturities (corporate public bonds and government securities) and certain cash equivalents.

Level 3 - Fair value is based on at least one significant unobservable input for the asset or liability. The assets and liabilities in this category may require significant judgment or estimation in determining the fair value. The Company's Level 3 assets and liabilities primarily include future policy benefits.

**Assets and Liabilities by Hierarchy Level** - The tables below present the balances of assets and liabilities reported at fair value on a recurring basis, as of the date indicated.

	December 31, 2021				
	Level 1	Level 2	Level 3	Netting(1)	Total
	(in thousands)				
<b>Fixed maturities, available-for-sale:</b>					
Obligations of U.S. states and their political subdivisions	\$ 0	\$ 47,426	\$ 0	0	\$ 47,426
Foreign government bonds	0	5,470	0	0	5,470
U.S. corporate public securities	0	38,901	0	0	38,901
Foreign corporate public securities	0	21,591	0	0	21,591
Subtotal	0	113,388	0	0	113,388
Cash equivalents	0	30,638	0	0	30,638
Total assets	\$ 0	\$ 144,026	\$ 0	\$ 0	\$ 144,026
Future policy benefits	\$ 0	\$ 0	\$ 24,095	\$ 0	\$ 24,095
Total liabilities	\$ 0	\$ 0	\$ 24,095	\$ 0	\$ 24,095

(1) "Netting" amounts represent cash collateral of \$0 million as of December 31, 2021.

The methods and assumptions the Company uses to estimate the fair value of assets and liabilities measured at fair value on a recurring basis are summarized below.

**Fixed Maturity Securities** - The fair values of the Company's public fixed maturity securities are generally based on prices obtained from independent pricing services. Prices for each security are generally sourced from multiple pricing vendors, and a vendor hierarchy is maintained by asset type based on historical pricing experience and vendor expertise. The Company ultimately uses the price from the pricing service highest in the vendor hierarchy based on the respective asset type. The pricing hierarchy is updated for new financial products and recent pricing experience with various vendors. Consistent with the fair value hierarchy described above, securities with validated quotes from pricing services are generally reflected within Level 2, as they are primarily based on observable pricing for similar assets and/or other market observable inputs. Typical inputs used by these pricing services include but are not limited to, reported trades, benchmark yields, issuer spreads, bids, offers, and/or estimated cash flow, prepayment speeds, and default rates. If the pricing service updates the price to be more consistent with the presented market observations, the security remains within Level 2.

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The Company conducts several specific price monitoring activities. Daily analysis identifies price changes over predetermined thresholds defined at the financial instrument level. Various pricing integrity reports are reviewed on a daily and monthly basis to determine if pricing is reflective of market activity or if it would warrant any adjustments. Other procedures performed include, but are not limited to, reviews of third-party pricing services methodologies, reviews of pricing trends and back testing.

**Cash Equivalents** - Cash equivalents include money market instruments and other highly liquid debt instruments. The Company believes that due to the short-term nature of these instruments, the carrying value approximates fair value.

**Future Policy Benefits** - The FVO is elected by the Company for future policy benefits. As a result, the liabilities are measured at fair value at each financial reporting date reported in Future policy benefits.

The Company calculates the fair value of future policy benefits using discounted cashflow models. The fair values of these liabilities are calculated as the present value of future expected benefit payments to customers and the future expected expense allowances, minus the present value of projected future premiums. The fair value is based on the in force business and calculated using actuarial and capital market assumptions.

Actuarial assumptions, including contractholder behavior and mortality, are reviewed at least annually, and updated based upon emerging experience, future expectations and other data, including any observable market data. These assumptions are generally updated annually unless a material change that the Company feels is indicative of a long-term trend is observed in an interim period. As these significant inputs are not observable, the valuation is accordingly considered as Level 3 in the fair value hierarchy.

Observable capital market inputs are used for the risk-free rates used in the discounting of future cashflows. The discounting for the liabilities also includes an adjustment for NPR. The NPR adjustment is calculated using publicly available information related to credit spreads on corporate bonds.

The valuation of the liabilities also includes risk margins that are established to represent the additional compensation a market participant would require to assume the liabilities. The risk margins are calculated using a discounted cost of capital approach. The establishment of the risk margins requires the use of management judgement, including assumptions of the target capital ratios and cost of capital for a market participant.

**Quantitative Information Regarding Internally-Priced Level 3 Assets and Liabilities** - The tables below present quantitative information on significant internally-priced Level 3 assets and liabilities.

December 31, 2021						
Fair Value	Valuation Techniques	Unobservable Inputs	Minimum	Maximum	Impact of Increase in Input on Fair Value(1)	
(in thousands)						
<b>Liabilities:</b>						
Future policy benefits(2)	\$ 24,095	Discounted cash flow	Lapse rate(3)	2 %	47 %	Increase
			Mortality rate(4)	0 %	100 %	Increase
			Target capital level	200 %	200 %	Increase
			Cost of capital	6.5 %	6.5 %	Increase

- (1) Conversely, the impact of a decrease in input would have the opposite impact on fair value as that presented in the table.
- (2) Since the valuation methodology for the Future policy benefits uses a range of inputs that vary at the product level over the cash flow projection period, presenting a range, rather than weighted average, is a more meaningful representation of the unobservable inputs used in the valuation.
- (3) For any given contract, lapse rates vary throughout the period over which cash flows are projected for the purposes of valuing the liability. Lapse rates are also generally assumed to be lower for the period where surrender charges apply.
- (4) Mortality rates may vary by product, age and duration. A mortality improvement assumption is also incorporated into the overall mortality table.

**Changes in Level 3 Liabilities** – The change in fair value of Level 3 liabilities relating to issuances of future policy benefits were \$24 million for the period September 29, 2021 to December 31, 2021.

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**Transfers** – All transfers are based on changes in the observability of the valuation inputs, including the availability of pricing service information that the Company can validate. Transfers into Level 3 are generally the result of unobservable inputs utilized within valuation methodologies and the use of indicative broker quotes for assets that were previously valued using observable inputs. Transfers out of Level 3 are generally due to the use of observable inputs in valuation methodologies as well as the availability of pricing service information for certain assets that the Company can validate.

There have been no transfers into or out of Level 3 for the period September 29, 2021 to December 31, 2021.

**Fair Value of Financial Instruments**

The table below presents the carrying amount and fair value by fair value hierarchy level of certain financial instruments that are not reported at fair value. The financial instruments presented below are reported at carrying value on the Company's Statement of Financial Position. In some cases, as described below, the carrying amount equals or approximates fair value.

	December 31, 2021				Carrying Amount
	Fair Value			Total	
	Level 1	Level 2	Level 3		(in thousands)
<b>Assets:</b>					
Cash and cash equivalents	\$ 2,938	\$ 0	\$ 0	\$ 2,938	\$ 2,938
Accrued investment income	0	1,652	0	1,652	1,652
<b>Total assets</b>	<b>\$ 2,938</b>	<b>\$ 1,652</b>	<b>\$ 0</b>	<b>\$ 4,590</b>	<b>\$ 4,590</b>
<b>Liabilities:</b>					
Other liabilities	\$ 0	\$ 260	\$ 0	\$ 260	\$ 260
<b>Total liabilities</b>	<b>\$ 0</b>	<b>\$ 260</b>	<b>\$ 0</b>	<b>\$ 260</b>	<b>\$ 260</b>

The fair values presented above have been determined by using available market information and by applying market valuation methodologies, as described in more detail below.

***Cash and Cash Equivalents and Accrued Investment Income***

The Company believes that due to the short-term nature of certain assets, the carrying value approximates fair value. These assets include cash and cash equivalent instruments and accrued investment income that meet the definition of financial instruments.

***Other Liabilities***

Other liabilities are primarily payables, such as accrued expense payables. Due to the short-term until settlement of most of these liabilities, the Company believes that carrying value approximates fair value.

**5. REINSURANCE**

The Company participates in reinsurance with its affiliate Pruco Life as described below:

**Pruco Life**

Effective October 1, 2021, the Company entered into an automatic coinsurance agreement with Pruco Life to reinsure a closed block of variable life policies in the extended term policy status.

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Significant effects of reinsurance amounts included in the Company's Statement of Financial Position as of December 31, were as follows:

	2021
	(in thousands)
Future policy benefits, at fair value	\$ 24,095
Reinsurance payables	\$ 263

Significant effects of reinsurance amounts included in the Company's Statement of Operations and Comprehensive Income were as follows:

	September 29, 2021 to December 31, 2021
	(in thousands)
Changes in fair value of reinsurance balance	
Reinsurance assumed	\$ 15
Net changes in fair value of reinsurance balance	\$ 15

The gross amounts of life insurance face amount in force as of December 31, were as follows:

	2021
	(in thousands)
Assumed gross life insurance face amount in force	\$ 294,132

## 6. INCOME TAXES

The following schedule discloses significant components of income tax expense (benefit) for the period presented:

	September 29, 2021 to December 31, 2021
	(in thousands)
Current tax expense (benefit):	
U.S. federal	\$ 514
Total current tax expense (benefit)	514
Deferred tax expense (benefit):	
U.S. federal	(361)
Total deferred tax expense (benefit)	(361)
Total income tax expense (benefit)	\$ 153

### *Reconciliation of Expected Tax at Statutory Rates to Reported Income Tax Expense (Benefit)*

For the period September 29, 2021 to December 31, 2021, the Company did not have any differences between the Company's statutory U.S. federal income tax rate of 21% applicable for 2021, and the Company's effective tax rate. The effective tax rate is the ratio of "Income tax expense (benefit)" divided by "Income (loss) from operations before income taxes."

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*Schedule of Deferred Tax Assets and Deferred Tax Liabilities*

	<u>As of December 31, 2021</u>
Deferred tax assets:	
Insurance reserves	\$ 1,725
Deferred policy acquisition costs	439
Other	1,615
Deferred tax assets	<u>3,779</u>
Deferred tax liabilities:	
Net unrealized gain on securities	<u>3,170</u>
Investments	124
Deferred tax liabilities	<u>3,294</u>
Net deferred tax asset/(liability)	<u>\$ 485</u>

The application of U.S. GAAP requires the Company to evaluate the recoverability of deferred tax assets and establish a valuation allowance if necessary to reduce the deferred tax asset to an amount that is more likely than not expected to be realized. Considerable judgment is required in determining whether a valuation allowance is necessary, and if so, the amount of such valuation allowance. In evaluating the need for a valuation allowance, the Company considers many factors, including: (1) the nature of the deferred tax assets and liabilities; (2) whether they are ordinary or capital; (3) in which tax jurisdictions they were generated and the timing of their reversal; (4) taxable income in prior carryback years as well as projected taxable earnings exclusive of reversing temporary differences and carryforwards; (5) the length of time that carryovers can be utilized in the various taxing jurisdictions; (6) any unique tax rules that would impact the utilization of the deferred tax assets; and (7) any tax planning strategies that the Company would employ to avoid a tax benefit from expiring unused. Although realization is not assured, management believes it is more likely than not that the deferred tax assets, net of valuation allowances, will be realized.

The Company had no valuation allowance as of December 31, 2021. Adjustments to the valuation allowance will be made if there is a change in management's assessment of the amount of deferred tax asset that is realizable.

***Tax Audit and Unrecognized Tax Benefits***

The Company's liability for income taxes includes the liability for unrecognized tax benefits and interest that relate to tax years still subject to review by the IRS or other taxing authorities. The completion of review or the expiration of the Federal statute of limitations for a given audit period could result in an adjustment to the liability for income taxes.

The Company had no unrecognized tax benefits as of December 31, 2021. The Company does not anticipate any significant changes within the next twelve months to its total unrecognized tax benefits related to tax years for which the statute of limitations has not expired.

The Company classifies all interest and penalties related to tax uncertainties as income tax expense (benefit). In 2021, the Company recognized \$0 for tax related interest and penalties.

The tax years that remain subject to examination by the U.S. tax authorities at December 31, 2021 is 2021.

The Company participates in the IRS's Compliance Assurance Program. Under this program, the IRS assigns an examination team to review completed transactions as they occur in order to reach agreement with the Company on how they should be reported in the relevant tax returns. If disagreements arise, accelerated resolutions programs are available to resolve the disagreements in a timely manner.

**7. EQUITY**

The Bermuda capital and solvency return is an annual return relating to an insurer's risk management practices and information used by an insurer to calculate its Enhanced Capital Requirement ("ECR") and Target Capital Level ("TCL") as prescribed by Prudential Standard Rules made under section 6A of the Act. Every Class E insurer shall submit to the BMA a completed

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capital and solvency return on or before its filing date of April 29th. The most recent version of the capital and solvency return is available on the BMA website.

The capital and solvency model is used to calculate an insurer's ECR, a capital and surplus requirement imposed by Rules made under section 6A of the Act. The ECR of an insurer shall be calculated at the end of its relevant year by the higher of the Bermuda Solvency Capital Requirement ("BSCR") model and an approved internal model, if applicable, provided that the ECR amount is equal to or exceeds the Minimum Margin of Solvency. The TCL of an insurer is calculated as 120% of the ECR and although not a capital requirement per se, insurers are expected to hold eligible capital resources to cover it; failure to do so will result in additional reporting requirements and enhanced monitoring, and in the submission of a remediation plan to restore capital above the TCL.

The BSCR model calculates a risk-based capital measure by applying capital factors to capital and solvency return elements, including investments and other assets, operational risk, and Long-Term insurance risks, in order to establish an overall measure of capital and surplus for statutory solvency purposes. The capital factor established for each risk element, when applied to that element, produces a required capital and surplus amount. The individual capital amounts generated for each risk element (excluding operational risk) are then summed. Covariance adjustments are made to arrive at the BSCR (after covariance adjustment), which may be further adjusted to include insurer-specific operational risk and capital add-ons, as assessed by the BMA, to finally produce the BSCR of an insurer.

An insurer's available statutory capital and surplus divided by the BSCR gives the BSCR ratio. An insurer's available statutory capital and surplus divided by the ECR gives the ECR ratio. The BSCR and ECR ratios will assist the BMA to evaluate the financial strength of an insurer.

The BSCR, ECR and TCL establish solvency capital levels that are used by the BMA to monitor the capital adequacy of the Company as a Class E insurer.

***Return of Capital***

Through December 31, 2021, the Company had no returns of capital.

***Return of Capital Restrictions***

Any return of contributed capital that would reduce the Company's total statutory capital (share capital and contributed surplus) by 15% or more must be approved by the BMA.

***Dividends***

Through December 31, 2021, the Company did not pay any dividends.

***Dividend Restrictions***

The Company may not pay dividends during any financial period if such payment would cause the Company to fail to meet its minimum solvency margin as defined in the Act. Further, the Company may not distribute a dividend to any person other than a policyholder unless the value of the assets of its long-term business fund, as certified by the Company's approved actuary, exceeds its insurance and other liabilities.

The Company may not pay a dividend or a distribution out of contributed surplus unless there are reasonable grounds for believing the Company will be remain able, and after the payment of the dividend or distribution, to meet its liabilities when they become due and that the realizable value of the Company's assets will, after the payment of the dividend or distribution, be greater than value of its liabilities.

Furthermore, dividends up to 25% of total statutory capital and surplus require Board approval. Dividends above 25% of total statutory Capital and Surplus require Board approval and an affidavit, signed by at least two Directors and the Company's Principal Representative, filed with the BMA at least seven days prior to payment of the dividend.

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***Common Stock***

As of December 31, 2021, Lotus Re had 250,000 shares of common stock authorized, issued and outstanding. The total shares of common stock outstanding were 100% owned by Prudential Insurance. See Note 10 for more information regarding Prudential Insurance's transfer of ownership to PIIH as of February 1, 2022.

***Accumulated Other Comprehensive Income (Loss)***

AOCI represents the cumulative OCI items that are reported separate from net income and detailed on the Statements of Operations and Comprehensive Income. The balance of and changes in each component of AOCI as of and for the period September 29, 2021 to December 31, 2021 are as follows:

	<b>Accumulated Other Comprehensive Income (Loss)</b>		
	<b>NPR adjustment to Future Policy Benefits</b>	<b>Net Unrealized Investment Gains (Losses)</b>	<b>Total Accumulated Other Comprehensive Income (Loss)</b>
	(in thousands)		
Balance, September 29, 2021	\$ 0	\$ 0	\$ 0
Change in OCI before reclassifications	128	15,093	15,221
Income tax benefit (expense)	(27)	(3,169)	(3,196)
Balance, December 31, 2021	<u>\$ 101</u>	<u>\$ 11,924</u>	<u>\$ 12,025</u>

***Reclassification out of Accumulated Other Comprehensive Income (Loss)***

For the period September 29, 2021 to December 31, 2021, the Company had zero net unrealized investment gains (losses) reclassified from AOCI.

***Net Unrealized Investment Gains (Losses)***

Net unrealized investment gains (losses) on available-for-sale fixed maturity securities are included in the Company's Statement of Financial Position as a component of AOCI. Changes in these amounts include reclassification adjustments to exclude from OCI those items that are included as part of "Net income (loss)" for a period that had been part of OCI in earlier periods. There are no amounts related to available-for-sale fixed maturity securities on which an allowance for credit losses has been recognized as of December 31, 2021. The amounts for the periods indicated below, are as follows:

	<b>Net Unrealized Investment Gains (Losses) on Available-for-Sale Fixed Maturity Securities</b>	<b>Income Tax Benefit (Expense)</b>	<b>Accumulated Other Comprehensive Income (Loss) Related to Net Unrealized Investment Gains (Losses)</b>
	(in thousands)		
Balance, September 29, 2021	\$ 0	\$ 0	\$ 0
Net unrealized investment gains (losses) on investments arising during the period	15,093	(3,169)	11,924
Balance, December 31, 2021	<u>\$ 15,093</u>	<u>\$ (3,169)</u>	<u>\$ 11,924</u>

**8. RELATED PARTY TRANSACTIONS**

The Company has extensive transactions and relationships with Prudential Insurance, Prudential International Insurance Service Company, LLC ("PIISC") and other affiliates.

***Expense Charges and Allocations***

The majority of the Company's expenses are allocations and charges from Prudential Insurance and PIISC. These affiliates and the Company operate under service agreements whereby certain general and administrative support services are provided to the

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Company by Prudential Insurance and PIISC. The Company periodically reviews its methods for determining the level of administrative expenses charged to the Company. These agreements obligate the Company to compensate Prudential Insurance and PIISC for the appropriate cost of providing such services. General and administrative support expenses related to these agreements were \$236 thousand for the period September 29, 2021 to December 31, 2021. These expenses are recorded as "General, administrative and other expenses" in the Statement of Operations and Comprehensive Income.

***Affiliated Investment Management Expenses***

The Company entered into an investment advisory agreement with PGIM, Inc. ("PGIM"), a PFI affiliated company, whereby PGIM provides discretionary investment advisory services to the Company, as directed by the Company's Investment Committee. Investment expenses paid to PGIM related to this agreement were \$15 thousand for the period September 29, 2021 to December 31, 2021. These expenses are recorded as "Net investment income" in the Statement of Operations and Comprehensive Income.

***Affiliated Asset Transfers***

The table below shows affiliated asset trades for the period September 29, 2021 to December 31, 2021:

Affiliate	Date	Transaction	Security Type	Fair Value	Book Value	APIC, Net of Tax Increase/ (Decrease)
					(in thousands)	
Prudential Insurance	October 2021	Transfer In	Fixed Maturities	\$ 114,173	98,360	\$ (12,492)

***Capital Contributions from Parent and Dividends***

The Company received capital contributions of \$123.9 million from Prudential Insurance during the period September 29, 2021 to December 31, 2021. The capital contributions included \$98.4 million of invested assets.

Through December 31, 2021, the Company did not pay any dividends.

***Reinsurance with Affiliates***

As discussed in Note 5, the Company participates in a reinsurance transaction with Pruco Life.

**9. LITIGATION**

The Company is subject to legal and regulatory actions in the ordinary course of its business. The Company may also be subject to litigation that could arise out of its general business activities, such as its investments and third party contracts. Should such litigation arise, the plaintiffs may seek large and/or indeterminate amounts, including punitive or exemplary damages. The outcome of litigation or a regulatory matter, and the amount or range of potential loss at any particular time, is often inherently uncertain. It is possible that the results of operations or the cash flow of the Company in a particular quarterly or annual period could be materially affected by any ultimate unfavorable resolution of litigation and regulatory matters depending, in part, upon the results of operations or cash flow for such period.

There are no pending legal or regulatory actions that are specific to the Company.

**10. SUBSEQUENT EVENTS**

The Company has evaluated subsequent events through April 22, 2022, the date these audited financial statements were issued.

Effective January 1, 2022, Pruco Life recaptured the risks related to a closed block of variable life policies in the extended term status, that had previously been reinsured to the Company, on a coinsurance basis, from October 1, 2021 to December 31, 2021. The Company held a Future policy benefits liability, at fair value of \$24 million at December 31, 2021 for the block. The Company then entered into reinsurance agreements with Prudential Insurance and Pruco Life to assume a closed block of their variable life business under a coinsurance and modified coinsurance basis including policies in the extended term policy status, which resulted in a Reinsurance recoverable, at fair value of approximately \$620 million. In order to satisfy collateral support

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obligations stated in the reinsurance agreements, on March 31, 2022, the Company executed letters of credit with an external counterparty in the amounts of \$125 million and \$50 million for Prudential Insurance and Pruco Life, respectively.

Effective February 1, 2022, Prudential Insurance, a direct wholly-owned subsidiary of PFI, transferred 100% of its ownership to PIIH, also a wholly-owned subsidiary of PFI.

Effective March 29, 2022, PIIH contributed \$827 million to the Company to fund a ceding commission and tax payment resulting from the execution of the reinsurance agreements, mentioned above.