Agenda

- With Profit landscape
- Latest regulatory requirements
- Process for completing a WP ROP
- Working with the FSA
- Summary

The with-profits landscape

- In the UK there are in the region of 100 WP funds, with total peak 1 reserves of £230bn
- Approximately half of these are closed to new business with the majority of these having closed prior to 2005

Fig 1 – UK WP funds that are open/closed to new business

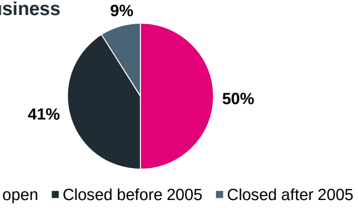
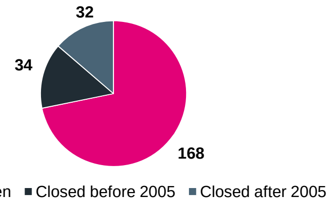


Fig 2 – UK WP Funds – total peak 1 reserves £bn



Latest regulatory requirements PS12/04

Requirements pre PS12/04

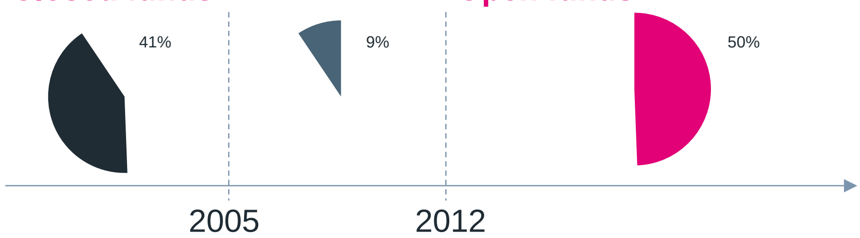
- Rules introduced in 2005
- Submit run off plan within 3 months of closure
- Closed < 2005 – no requirement to do a ROP.

Requirements post PS12/04

- Funds closed < 2005 now need to do a ROP
- This needs to be submitted by 31/12/2012
- Requirement for firms to submit a run off plan within 3 months of closure remains.
- Open funds
  - ⬇ new business? Discuss adequacy of planning with the regulator
  - The ORSA is key.

Latest regulatory requirements PS12/04 (cont.)

Closed funds | **Open funds**



Produce run off plan by end of 2012

✓

ORSA

Submit run off plan within 3 months of closure

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Latest regulatory requirements Link to the ORSA

- For firms with dwindling new business the ORSA will be a key element of communication with the regulator and will drive dialogue on the development of a run off plan
- For with-profits funds the ORSA needs to consider both the shareholder risks AND the policyholder risks
- Run off risks are a key consideration for any closed fund and should be included within the ORSA
- Going forward, fair distribution, management and run off plans for WP funds may align under the banner of the ORSA.

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Latest regulatory requirements
What should a run off plan include

- SUP App2.15
- The key elements are
  1. Funding → What are the costs of running the fund off and how will these be met?
  2. Risk management → What is the strategy for managing risks
  3. Governance → How the fund will be managed in run off including estate distribution?
  4. Financial projections → The numbers!
- Guidance intended for firms recently closed to new business
- Care and interpretation needed for firms that closed < 2005.

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Latest regulatory requirements
What should a run off plan include (Example)

Table 1 - forecast summary revenue account for the relevant with-profits fund	
(1)	Premiums and claims (gross and net of reinsurance) analysed by major class of insurance business
(2)	Investment return
(3)	Expenses
(4)	Other charges and income
(5)	Taxation
(6)	Increase (decrease) in fund in financial year
(7)	Fund brought forward
(8)	Fund carried forward

Table 2 - forecast summary balance sheet and statement of solvency for the relevant with-profits fund	
	Assets analysed by type (excluding implicit items):
(1)	Equities
(2)	Land and buildings
(3)	Fixed interest investments
(4)	All other assets
(5)	Total assets (excluding implicit items)
(6)	Policyholder liabilities
(7)	Other liabilities
(8)	Total liabilities
(9)	Excess/(deficiency) of assets over liabilities before implicit items
(10)	Implicit items allocated to the with-profits fund
(11)	Long-term insurance capital requirement for the with-profits fund
(12)	Resilience capital requirement for the with-profits fund
(13)	With-profits insurance capital component (for realistic basis life firms only)
(14)	Net excess/(deficiency) of assets in the with-profits fund

…………Projected for 3 years?.............

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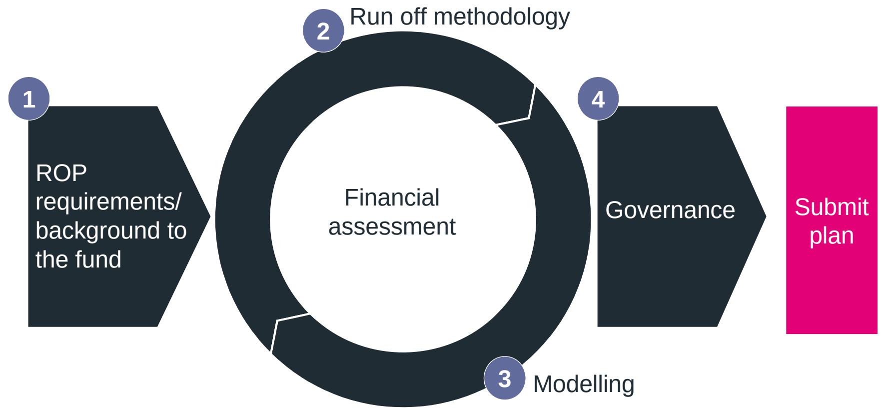
Process for completing a run off plan



1) Run off plan requirements and fund background

What business is there in the fund?

What previous scheme requirements are there?

Is the bonus distribution method appropriate?

Does this easily facilitate estate distribution?

- Management actions
- Expense deal that will run out in future
- Admin external/internal
- Segregated support funds
- Facility to convert the fund to NP

How do these impact the run off?

2) Develop methodology – Estate distribution

Key requirements

1. Surplus = zero in the end
2. Distribution should be equitable (avoiding a tontine)
3. Capital requirements and CoG and additional solvency margins must be met.

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2) Develop methodology – Estate distribution (cont.)

1. ⬆ Claims only
2. ⬆ Asset share
3. ⬆ Asset share investment return

Distributable surplus = Free estate > Cap Rqmt + COG + Solvency Margin

Calculate % such that surplus at end is zero

4. ⬇ Guarantee charges
5. ⬆ EBR

Reduces the estate

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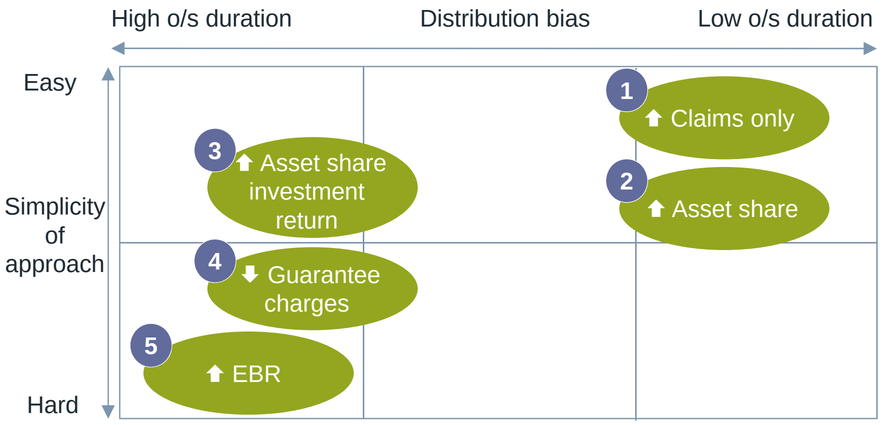
2) Develop methodology – Estate distribution (cont.)



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3) Modelling

2 Approaches:

1. Full balance sheet projection from modelling software
2. Construct balance sheet from best estimate cash flows

	Advantages	Disadvantages
Approach 1	• Greater degree of sophistication.	• Less transparent • Harder to adjust for mgmt actions etc. • Dependency on modelling capabilities.
Approach 2	• Greater degree of flexibility.	• High level of manual process.

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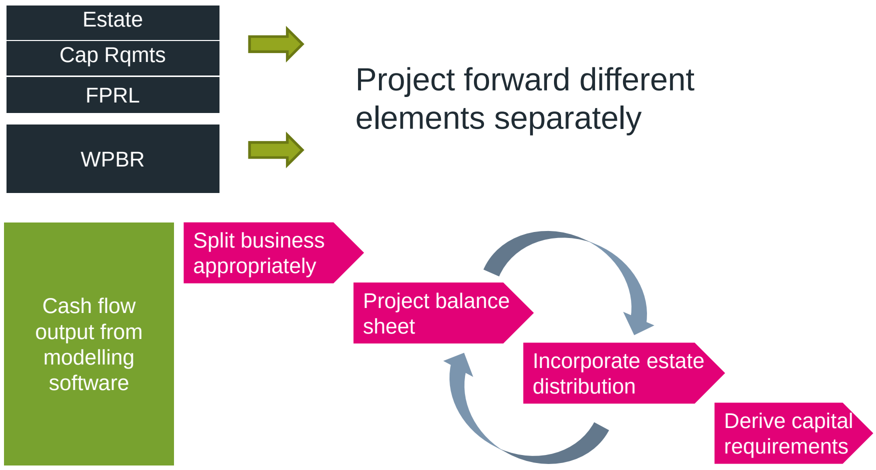
3) Modelling (cont.)

Common approach



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3) Modelling (cont.)

Modelling considerations:

- Opening position – RBS, ICA, Solvency position
- Any adjustments necessary?
- Some products more difficult to model due to nature of product and guarantees
- Intrinsic and time value of guarantees may run off differently to each other and asset shares.

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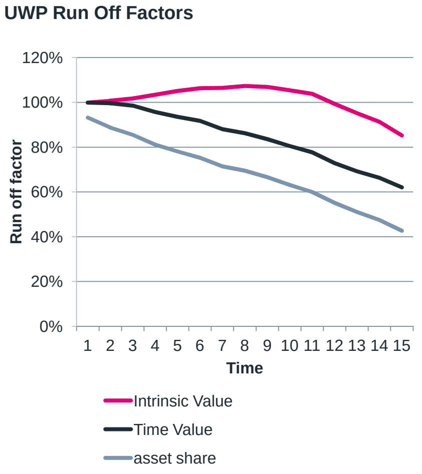
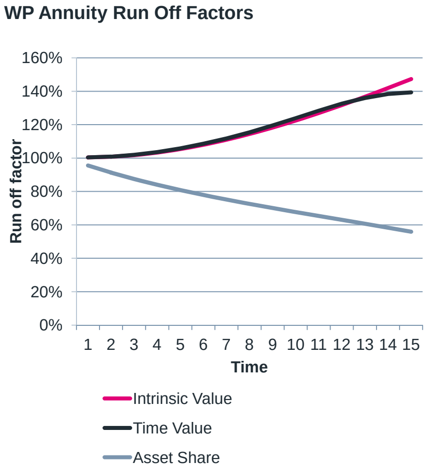
3) Modelling (cont.)





4) Governance and impact on policyholder

- Revise corporate governance arrangements in light of revised operating model
- Changes to costs and charges
- Changes to payouts and smoothing
- Assess changes required to PPFM
- Policyholder communication

Challenges and pitfalls

Challenges 	Pitfalls 	Top tips 
• Sophistication of run off methodology vs. simplicity and transparency of approach • Dealing with structural issues.	• Treating it like an exam question or tick box exercise • Too many words • Not enough effort on the projections.	• Identifying the structural issues and addressing them is key • Getting the right methodology is important • Don't cut corners on the projections • May need to have a bit of a tontine to protect the fund and ensure an orderly run off of the estate.

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Working with the FSA

- Be open about conflicts of interest
- It's ok to expect the run off plan to be self supporting
- Address conflicts between capital requirements and PRE
- All transactions to be at market rates
- Costs after closedown will need to be discussed clearly

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Summary

Key messages

- A large number of funds caught be PS12/04
- The ORSA will be a big focus for open WP funds
- Planning and tidying up bonus philosophy is key
- Most focus is needed on the projections
- May need to have a bit of a tontine to protect the fund and ensure an orderly run off of the estate
- **WPA needs to get on and do it!**

Questions

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