


Institute
and Faculty
of Actuaries

Managing the Fund: De-risking and the path to run off


Tim Stedman & Tricia Ross



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Disclaimer


- The views in this presentation are those of the presenters and do not necessarily reflect the views of our employer.
- The opinions are generally given from the viewpoint of a proprietary company, although many of the issues will also be relevant to Mutuals.



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Agenda

- Background
- Strategy & Issues
- Specific Challenges



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Background

- Majority of WP Funds now in decline
- RDR has proved detrimental to new business volumes
- Many funds closed to new business or considering closure
 - For the 10 largest funds new business APE in 2012 was only 0.2% of the assets
- Need for a distribution or run-off plan, even if fund remains open



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Strategy - The First Step

- Need Board Engagement
- Closure:
 - Stay Open, "soft" close or "hard" close
- Alternative sources of Capital
- From our PPFM:
 - The most important Overriding principle is that the With profits Sub-Fund will be managed with the objective of ensuring that its assets are sufficient to meet its liabilities without the need for additional capital from outside the With Profits Sub Fund. This overriding Principle has supremacy over the other Overriding Principles.
- De-risking in preparation for run-off
- Run-off Plan



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Policyholder Issues

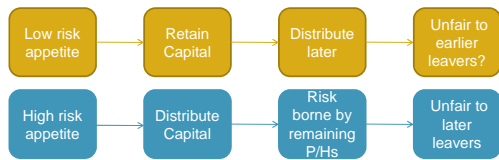
- In any de-risking or run-off plan you must work out how to balance
 - Fairness to Policyholders
 - Fairness between generations and classes of Policyholders
 - Risk & Capital Management
 - Expectations of Shareholders (if any)
- Have your final solution in mind



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Risk Appetite

- This will usually need to be revised as you go from open to closed
- There is a tension between this and fairness to policyholders



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Specific Challenges

- In preparation for creating a run-off plan, these are some of the issues we have encountered:
 - Non-profit Business within the Fund
 - Pension Schemes
 - Expenses
 - Investment Strategy
 - Incremental New Business
- In addressing these Governance is key

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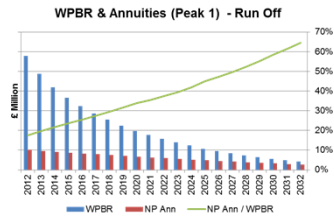
Non-Profit Business in the Fund

- The challenge:
 - If unhedged the VIF asset tends to be volatile
 - Ties up capital
 - Profits may emerge too late for a fair distribution of the estate

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For L&G the run-off profile is key:



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NP Business - Possible Solutions

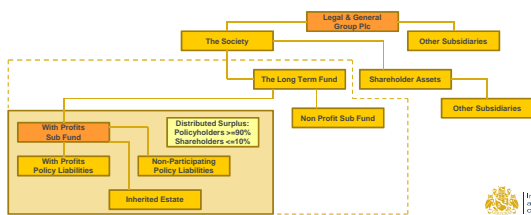
	Is there a market?	Residual Risk?	Cashflow Timing Resolved?	Inform policy-holders?	Part VII required?
De-risk longevity	Yes	Yes	Partially	No	No
De-risk Investments	Yes	Yes	Partially	No	No
Reinsure	Yes	Yes	?	No	No
Sell externally	Yes	No	Yes	Yes	Yes
Sell internally	Maybe	No	Yes	Maybe	Maybe

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Our Fund Structure

The diagram below shows how the With Profits Sub Fund fits into the broader structure of the Society and the Legal & General Group



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Our Principles for an Internal Deal

- With profits is a willing seller and the shareholders are a willing buyer... but neither at any price
- The final price needs to be demonstrably fair to both sides given their objectives
- The shareholders will be taking risk and it's appropriate for them to receive a fair return for the risks that they will be running
- The shareholder should not charge for items where they are taking no risk, nor should they charge for uncertainty where none exists
- The Directors have obligations to both the with profits policyholders and shareholders and the resulting price should be shown to strike a fair balance between both parties.
- Both parties should share openly information including pricing assumptions, methodologies and results.



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Pension Schemes

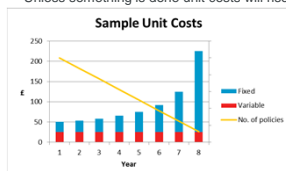
- The Challenge:
 - Many defined benefit schemes have historic deficits
 - A significant proportion may relate to the WP Fund
 - WP may not be the sponsoring employer
 - How to manage impact on WP customers.....and shareholders
- Possible Solutions
 - Do a deal with the shareholder
 - Constrain the pension fund to manage the risk



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Expenses

- The Challenge:
 - Unless something is done unit costs will rise:



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Expenses - Possible Solutions

	Helpful?	Sufficient?	Residual Risk?	Inform policy-holders?
Cost Control	Yes	No	Yes	No
Outsource	Partly	No	Yes	Yes
Deal with Shareholder	Yes	Yes	No	No
Charge excess to Estate	Possibly	No	Yes	No



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Investment Strategy

- The Challenge:
 - Ensure liquidity to meet policyholder payments
 - Continue to meet policyholder expectations
- Possible Solutions
 - Simplify asset classes
 - Manage sales carefully, especially illiquid classes
 - Pooled investments



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Incremental New Business

- The Challenge:
 - If the fund is closed to all except incremental business how long can you go on accepting this?
 - Will there be consequences for Group policies if you stop accepting increments
- Possible Solutions
 - Offer Non-Profit Increments
 - Accept the Risk



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Summary

- Issues with declining funds:
 - Reducing economies of scale
 - Durational mismatches
 - Intergenerational fairness
 - Fairness to Shareholder

Development of solutions and run off plans
is an interesting actuarial challenge...
but a potentially thankless task!



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Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

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