

Current Issues in Life Assurance Seminar 3 May 2006

Current Topics in With Profits

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Current Topics in With Profits

Topics to be covered

- Rules & Governance
- Payouts
- Investments
- Risk
- The estate
- The future

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Rules & Governance

- The PPFM & CFPPFM
- PPFM has unquestionably resulted in improved with profits management, but too detailed for most readers
- A number of PPFM changes required since 30 April 2004
- CFPPFM arguably too detailed as well for target audience; changes to coincide with ABI's "Customer Impact" initiative ?
- Significant costs

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Rules & Governance

- The With Profits Actuary
- Concept successful; has a substantial stick to wave at Boards
- How quickly would practical changes have been effected in the Appointed Actuary regime ?
- First public reports to policyholders loom : what should be in them?

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Rules & Governance

- The With Profits Actuary
- Significant back-up required
- Ultimate responsibility with the Board
- Whistleblowing requirements

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Rules & Governance

- Independent Judgement
- With Profits Committees in the majority
- WPCs have to deal with some highly technical issues : do they have the right expertise ?
- Important to have a good dialogue between the WPA & WPC

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Payouts

- PS 05/01
- Explicit target ranges
- 90% within range
- How do you demonstrate this and at what level ?
- Individual asset shares or specimen policies ?

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Payouts

- Customer Care if payout < lower target
- Why does this happen ?
- Can you prevent it automatically ?
- If it does happen, should you reopen claims ?

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Payouts

- Frequency of Bonus declarations
- ½ yearly current norm
- In future ¼ ly to ensure remain within target range?
- Even more frequently?
- MVR changes and imposed restrictions
- System functionality
- Operational difficulties

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Payouts

- Payout analysis
- Year on year comparisons - are they fully understood?
- Return compared to other investments
- Same product – different company – different return
- Are they value for money?

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Payouts

- Broad Equity or Individual Unit Linked
- Do we still have with profits business ?
- End of surrender profit
- Conflict with expectations
- Charges for guarantees

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Investments

- Are policyholders' expectations being met ?
- What was said at point-of-sale ?
- Many different levels of guarantee on offer; understood ?
- Still a huge demand for equities – providing they never fall !
- Reduced EBRs mean that impact of market upturn is diminished
- Closed fund considerations – EBRs must fall over time

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Investments

- ALM changes
- Firms now have a much better understanding of the risks run by their with profits funds
- Substantial de-risking of funds has taken place, particularly those that are closed to new business
- Is there any scope for future EBR increases ? Size of the estate and its use is key (see later)

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Investments

- Derivatives
- Significant increase in the use of derivatives
- Traditionally dominated by put options & interest rate swaptions (for GAOs)
- With Profit Bonds have much to answer for ! Substantial short-term guarantees backed by equities across the industry

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Current Topics in With Profits

Investments

- Derivatives
- Credit derivatives : the next area of significant activity ?
- Corporate bonds do not necessarily represent a "free lunch" relative to gilts
- Will gilts come back into favour ?

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Current Topics in With Profits

Risk

- RBS / ICA / ICG
- Requirement
- Alignment with PPFM
- Has it helped with running of the business?
- Do we agree with ICG ?

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Risk

- Increased Customer awareness
- Do they understand with profits ?
- Desire for a simpler world
- Enhanced service level expectations
- Expense control v increased costs to provide above
- Clarification of other uses to which the fund may be put

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Risk

- Misselling / Compensation issues
- Compensation culture
- Absolute need for clarity in all documentation
- Risk explanation
- Where does the liability lie – WP fund or shareholders?

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Management of the Estate

- What is it for ?
- The same use in any two companies ?
- Different potential uses within open & closed funds and within 90:10 & 100:0 funds (e.g. reattribution, distribution, support for poorly performing policies)
- More & more with profits funds are closing to new business : equitable distribution to policyholders the key
- Likely to attract close FSA attention, particularly run-off plans

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Management of the Estate

- Closed fund issues
- Estate needs to be sufficient (but no more) to meet regulatory capital requirements
- Look to distribute the estate in as smooth a way as possible consistent with this
- But regulatory capital requirements (both Pillar 1 Peak 2 & Pillar 2) are market consistent, hence volatility exists
- Smooth distribution aided by de-risking the estate

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Management of the Estate

- Closed fund presentational issues
- In Form 19 of FSA Returns, working capital & realistic excess capital will be zero
- Gives no indication of the true risks to which a closed fund is exposed
- Change would be welcomed

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Management of the Estate

- Investment Issues
- Is there a case for equities ? Yes in open funds; debatable in closed funds
- If purpose of estate is to "cushion blows", little case for equities
- But what about policyholders' expectations ? And what does the PPFM say ?

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Management of the Estate

- Investment Issues
- Do policyholders care whether non-equity investments are in gilts or corporate bonds ?
- May be a strong case for using derivatives

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The Future

- New Business Plans
- Is there still an appetite ?
- Contract design – guarantees, flexibility and special features
- Financing
- Securitisation

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The Future

- Closed funds
- Run off plan
- Closed fund specialists
- Does the customer get treated fairly ?
- Do some open funds have similar issues ?

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The Future

- Overseas
- The new growth market
- Exciting opportunities or disaster waiting to happen

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The Future

- Overall – YES there is life
- Has to be greater transparency than in the past

But

- Has the FSA strangled with profits business?
- Should we anticipate yet more regulation?
- Has the regulation achieved its desired purpose?
- At what cost?

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The end

More questions ?

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