Institute and Faculty of Actuaries

Pre-paid funeral plans: call for evidence

IFoA response to HM Treasury

1 August 2018

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

We strive to act in the public interest by speaking out on issues where actuaries have the expertise to provide analysis and insight on public policy issues. To fulfil the requirements of our Charter, the IFoA maintains a Public Affairs function, which represents the views of the profession to Government, policymakers, regulators and other stakeholders, in order to shape public policy.

Actuarial science is founded on mathematical and statistical techniques used in insurance, pension fund management and investment. Actuaries provide commercial, financial and prudential advice on the management of assets and liabilities, particularly over the long term, and this long term view is reflected in our approach to analysing policy developments. A rigorous examination system, programme of continuous professional development and a professional code of conduct supports high standards and reflects the significant role of the profession in society.

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Submitted by email

1 August 2018

For the Attention of David Reeves, HM Treasury

Institute and Faculty of Actuaries response to HM Treasury call for evidence on pre-paid funeral plans

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to contribute to this call for evidence.
2. Actuaries have a statutory role in relation to pre-paid funeral plans where these are trust-based. As you will be aware, funeral plan contracts are a specified activity under article 59 of the Financial Services and Markets (Regulated Activities) Order 2001 (RAO). However, plans are excluded from article 59 if they are provided through a contract of whole life insurance effected by an authorised insurer; or through a trust which meets the requirements of article 60(1)(b) of the RAO.
3. One of the specified requirements is for a Fellow of the IFoA to determine, calculate and verify the assets and liabilities of such trusts every three years. Under the rules of the Funeral Planning Authority (FPA), actuaries' involvement is more frequent for the majority of providers who are registered with the FPA.
4. Given the nature of our experience and expertise in this field, this response focuses mostly on the questions about future regulation rather than those concerning consumer issues (questions 2-12).
5. We highlight in addition the special issues that apply for certain non-profit providers as discussed under Question 1.

Question 1: Are there any other common ways to structure funeral plans, not outlined in this call for evidence?

6. Yes, many religious organisations and some mutual associations provide funerals in a manner which is not outlined in the call for evidence. Crucially, they are not-for-profit arrangements.
7. Nationally and provincially, many different UK burial (funeral expenses) societies/schemes, representing different groups/denominations, offer burial arrangements for well over 150,000 members in total. This is virtually always the case for Jewish communities – and reflects a religious duty to bury the dead. They will typically be run for a community (or a set

of affiliated communities), in order to ensure religious burial on a standard basis, reflecting the specific religious requirements of the community involved.

8. Most members of each religious community join the relevant funeral expenses scheme – although this is not a compulsory requirement and funerals are carried out for non-members, subject to eligibility conditions and lump sum payments. Typically, the costs of the scheme are discharged by annual payments made simultaneously with other communal levies. The funds accrued are often not segregated from other community funds, not always set up as separate trusts and typically benefit from communal charitable status, with associated tax exemptions.
9. Although the benefits are akin to life assurance, there has historically been no statutory requirement for actuarial advice to such schemes as it has been recognised that these are essentially not-for-profit inherent provisions of a community. By contrast, if an actuary does advise on such a scheme, they are personally subject to IFoA and FRC requirements. The IFoA in particular has mandatory standards for Actuaries working for, advising or involved with UK Trust-Based Pre-Paid Funeral Plans to comply with[1], as well as non-mandatory guidance for actuaries and trustees.[2]
10. Discussions with the FCA in November 2016 indicated that the underlying assumption that these arrangements are not subject to regulation may now not be correct.
11. We would suggest that the position in relation to such arrangements should be clarified and that, if they are not to be subject to regulation, criteria should be laid down to make clear the extent of any exemption for qualifying community-based burial arrangements, consistent with safeguarding the public interest. We would be happy to assist in formulating such criteria, as appropriate.

Question 13: What types of investment strategies are being adopted by trustees who are managing trusts on behalf of funeral plan providers and what is your view on the effectiveness of these strategies in securing the short and long-term interests of plan holders?

12. Trustees are generally acting on the advice of the appointed investment manager or investment consultant, and allowance is made for the expected duration of the Trust's liability and the specific characteristics of the Trust, which are all being reflected in the Statement of Investment Principles (SIP). In most cases this is with the assistance of the appointed actuary. This is currently a voluntary system.
13. Furthermore, the actuary may comment on any unsuitable investment strategies at the actuarial reviews and bring this issue to the attention of the Trustees.
14. Ultimately, the actual strategy implemented will reflect the Trustees' appetite for risk and the need for growth type assets to outstrip future funeral price inflation.
15. Imposing a compulsory requirement for all Trusts to have a SIP which is reviewed every three years could improve the management of the Trusts. FPA providers are required to have a SIP that is reviewed annually and shared with the FPA.

Are trust returns withdrawn by providers for revenue raising/profit purposes and, if so, what proportion of these returns are withdrawn in this way?

[1] Actuarial Profession Standard (APS) Z1: Duties and Responsibilities for Actuaries Working for UK Trust-Based Pre-Paid Funeral Plans
[2] https://www.actuaries.org.uk/upholding-standards/standards-and-guidance/non-mandatory-guidance

16. Some providers withdraw for profit reasons. Trusts will be bound by their own governance provisions in relation to surplus withdrawal. Many withdrawals (including, we understand, all from FPA registered trusts) are subject to actuarial certification, in which case the actuary will determine the amount available for withdrawal. It will be assessed after allowing for the need to have sufficient assets to meet the Trust's future liabilities. In addition it is customary to allow an additional prudent margin over and above the liability required to remain in the Trust.

Question 14: What are your views on the government's proposal for FCA regulation of all funeral plan contracts and whether such a proposal will meet the government's stated objectives (as set out above)? Do you consider that an alternative proposal could better meet these objectives?

17. The IFoA notes that the stated objectives include seeking to ensure that all pre-paid funeral plan providers are subject to robust and enforceable conduct standards, that there is enhanced oversight of providers' prudential soundness and that consumers have access to dispute resolution mechanisms.
18. The IFoA previously raised with Government in 2014 the fact that there is no legislative requirement to ensure that the assets of a trust are managed well enough to be sufficient to meet the cost of the plan provider's contractual agreement with the consumer. This poses a risk for consumers as trust-based funeral plans are not regulated by the FCA or a compensation scheme such as the Financial Services Compensation Scheme (FSCS).
19. Therefore, there is arguably a regulatory gap which could increase the risk that planholders do not gain their promised peace of mind. Instead, planholders are unknowingly facing higher investment risks without any regulatory or legislative protection if the trust mismanages its funds and cannot meet the plan provider's contractual agreement. The requirement for an actuarial valuation cannot of itself adequately address this risk. Given the nature of the customer base, if a plan becomes insolvent it may create a considerable degree of unhappiness and hardship for the bereaved. There is the possibility additionally that too much reliance is placed under the current arrangements on the ability of the actuary to safeguard consumer interests, recognising that the ability of the actuary to influence the funding/ investment strategy of the trust is limited.
20. The IFoA would welcome regulatory protection to consumers if the trust mismanages its funds, to address the risks described above. Regulation could focus on the plan providers having to meet a minimum capital adequacy requirement (similar to the recent approach for the Sipp provider industry). Alternatively, there could be a minimum solvency measure for the funeral plan trust. Regulations designed to ensure the financial solvency of the plan providers would be appropriate in our view. Clearly, actuarial input would be likely to continue to be important in reinforcing the effectiveness of such a regime. The IFoA, through its Regulation Board, will continue to ensure that appropriate standards are in place to support the public interest role of its members under any such regime.
21. The IFoA would suggest bringing customers within the scope of the FSCS protection, as at present the FSCS does not provide protection for those who have a funeral plan with a provider that fails.
22. Naturally it may be appropriate to undertake a suitable impact assessment to assess the potential impact any regulation will have on the industry.

23. In principle, however, the IFoA is of the view that there is a strong case for more robust regulation of trust based funeral plans. We will be happy to assist in supporting the development of such proposals.

Question 15: How should the regulatory framework apply in relation to funeral plans that consumers have already entered into?

24. The regulatory framework – whatever shape it takes - could apply to all plans in force from day one rather than just those plans sold in the future, save for any religious/communal /private not-for- profit schemes, for which exemption criteria are established.
25. In order to provide customers with reasonable choice and to enable local schemes servicing a particular geographic region to continue, it may be appropriate to allow suitable transition provisions for existing providers. They should clearly be given adequate time to implement any new obligations placed on them.

Question 16: Should regulation extend beyond funeral plan providers, and apply to intermediaries engaged within the sector? Should such intermediaries become regulated entities, or should they be overseen by funeral plan providers as appointed representatives?

26. The new regulation should we believe appropriately extend to anyone associated with the selling or managing of pre-paid funeral plans.

Question 17: What would be the overall impact on the market/your firm if all funeral plan contracts were subject to FCA regulation? Are there specific activities or businesses, such as SMEs, within the sector that would be particularly affected by strengthened regulation? What is your view of the potential costs and benefits of the government's proposal?

27. While there is inevitably some risk of increased cost to consumers if plan providers seek to pass on the cost of regulation, this risk is we believe capable of being appropriately mitigated by proportionality in the regulatory approach and is in any event outweighed in this case by the important need for heightened consumer protection, recognising that the relevant customer base will include significantly the vulnerable and elderly.

Question 18: How long would the sector need to adapt to any new regulatory framework the government may seek to put in place?

28. We suggest that a timescale of around two years would be appropriate for the implementation of the transition into the new regulated environment.

Yours sincerely,

Jules Constantinou
President, Institute and Faculty of Actuaries