

## **Annexe 5**

### **With profits governance – reporting to policyholders**

A report for the policyholder advocate in connection  
with the reattribution of the inherited estates  
of the CGNU Life and CULAC with-profits funds

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**Report by: KPMG LLP**

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## **Reporting to policyholders post reattribution of the CGNU Life and CULAC inherited estates**

### **1.00 Introduction**

Following the reattribution of the inherited estates of CGNU Life and CULAC, there will be two key areas where policyholders have a valid interest in the progress of the funds:

A: information applying to policyholders in both the Old WPSF and the New WPSF, in particular, the equity backing ratio for asset shares;

B: the development of and the change in the inherited estate of the Old WPSF.

### **2.00 Summary of Proposal**

In order to provide policyholders with the information which they might reasonably be interested in, the above two areas could be included either within the report of the Board or the report of the WPA to with-profits policyholders. This would enable the objective to be achieved within the existing governance framework. Currently these reports to policyholders from the Board/WPA are very short, but they could easily be expanded. A format of what the content of the relevant sections of the expanded reports might cover is set out below. Copies of the current reports are provided along with this note for ease of reference.

In addition the WPC should report separately to policyholders on the WPA report and to confirm it is accurate and fairly represented to policyholders. In addition, their voluntary reporting to policyholders should be made mandatory and annual, and should explicitly extend to covering their own work and deliberations, how these have affected policyholders, how the conflicts have been deliberated and the outcome.

#### **A: Information applying to policyholders in both the Old WPSF and the New WPSF**

A potential conflict of interest exists between the shareholders and policyholders due to the fact that a higher EBR in asset shares could increase the potential losses to shareholders in the New WPSF. There are detailed rules in the AFH report which set

out the criteria for determining the EBR, but these are not in policyholder friendly language.

How the EBR has been set will be of interest to policyholders of both the New and Old WPSFs. The report should summarise, in customer friendly language, any changes in the EBR over the year, including the rationale that the Board, WPC and WPA went through to agree any changes. If no changes were made then the rationale for this decision should be described.

In addition, any application of industry levies to asset share should be disclosed with a justification.

**B: Report on uses and the change in the Old WPSF inherited estate.**

Given that some policyholders will have gone into the Old WPSF under the expectation that they may do better in that fund than accepting the PIP, they will have a genuine interest in how the fund is run and, in particular, the uses to which the inherited estate is put. Given their decision in the re-attribution, this interest is greater than for a normal policyholder in a normal WP fund. Given this, there is a strong case to be made for providing Old WPSF policyholders with enhanced information in relation to the progress of the fund and the movement in the inherited estate over the year, as well as the uses to which the inherited estate has been put.

There is an analysis of change in the working capital in Appendix 9.4a of the FSA returns, and we assume that this analysis would going forwards be presented separately for the New and Old WPSFs. However, that analysis is not particularly policyholder friendly. The proposal set out below covers how this might be addressed within the existing governance framework (i.e, within the report of the Board and/or WPA to the Old WPSF policyholders).

**Analysis of change on the inherited estate over the year**

Item	£m
<i>Inherited estate at beginning of the year</i>	<i>X</i>

Investment return on the inherited estate	
Special distributions made to policyholders	
Impact of declaring new guaranteed benefits	
Impact of smoothing policy (if any)	
Impact on the inherited estate of selling new business: <ul style="list-style-type: none"> <li>• Permanent impact</li> <li>• Temporary impact</li> </ul>	
Payouts made where the guarantees are more than asset shares	
Movement in liabilities not matched by movement in assets: <ul style="list-style-type: none"> <li>• Assumption/methodology changes</li> <li>• Mismatching</li> <li>• Modelling changes</li> </ul>	
Other experience variances (e.g. expenses not charged to asset shares)	
Other permanent impact on the inherited estate (eg one-off costs)	
Other temporary impacts on the inherited estate (eg development costs (VIF not included in RBS))	
<b>Sub total</b>	<b>X-Y</b>
<b><i>Inherited estate at end of the year</i></b>	<b><i>Y</i></b>

Notes

1. Material items in the above should have a commentary attached to them, sufficient to enable a policyholder to understand the item in question.
2. A rationale should be provided for all assumption, methodology and modelling changes.
3. Particular reference should be made to those areas where the firm has taken advantage of discretion in accordance within the COBS rules to charge items to the Fund that would otherwise be borne by shareholders. Specific example of this may be shareholder tax, costs associated with mis-selling and charges for non-market risk on new business.

The report should also contain the following items:

## **General**

- an overview of WP and how the estate is permitted to be used extracted from PPFM, for example;
- description of how the interests of policyholders have been taken into account in the decisions made; and
- commentary of how the inherited estate has been used compared to the permitted uses.

## **Value of the estate and the strength of the fund**

- commentary on the strength of the fund compared to risk appetite and to last year;
- comment on any special distributions made during the year and the likelihood of special distributions going forwards; and
- commentary on any actions taken to move the inherited estate to within the risk appetite's preferred range and reasons for such actions.

## **New Business**

- commentary on the nature and amount of new with-profit new business sold; and
- the impact on the capital requirements and likelihood of special distributions of new with-profits business sold.

## **Use of the inherited estate to allow investment freedom/smoothing**

- commentary on how any mismatching of assets and liabilities has impacted the fund;
- commentary on the EBR backing the asset shares and the impact on the inherited estate; and
- commentary on the impact on the inherited estate of the smoothing rules.

### **Investment policy for the inherited estate**

- commentary on how the inherited estate is invested and rationale for this; and
- commentary on any strategic investments made or sold in the course of the year and returns earned.

### **Other uses of the inherited estate - particular commentary**

- shareholder tax paid by the fund but not borne by asset shares;
- mis-selling compensation paid by the fund;
- guarantee costs met by the fund; and
- costs met by the fund from restricting charges to asset shares for certain contracts (for example, the cost of shareholder transfers and any expenses not charged to asset shares).

### **For the first five years after the reattribution – particular commentary**

- a description of the difference in the main Aviva assumptions relating to investment returns, persistency rates and levels of new business between the actual position and that assumed by Aviva in the reattribution and the expected effect of those differences on potential special distributions.