Railway Enginemen's Assurance Society Limited: Report of the Management Committee to With-Profits Policyholders for the year 2019

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A Introduction

The Society's Principles and Practices of Financial Management (PPFM) document describes how the Society manages its With-Profits business. The PPFM is available to all members from our website or by contacting the office. We also publish a summary of the PPFM entitled the Customer Friendly Principles and Practices of Financial Management (CFPPFM), which is also available from our website or by contacting the office. No changes were made to the PPFM during 2019.

The Society is required by the Financial Conduct Authority to produce an annual report to its With-Profits policyholders setting out whether it believes it has complied with its obligations in relation to its PPFM including the exercise of discretion and the way that the Society has addressed any competing or conflicting rights, interests or expectations of its policyholders. This report covers the financial year 1 January 2019 to 31 December 2019.

B Governance Arrangements

The Management Committee is responsible for the governance of the Society's With-Profits Fund, including compliance with the regulatory requirements contained in the Financial Conduct Authority's Conduct of Business sourcebook. In discharging its duties the Management Committee receives advice and guidance from the With-Profits Actuary (WPA) and the With-Profits Advisory Arrangement (WPAA).

B1 With-Profits Advisory Arrangement

A WPAA was in place throughout 2019. The role of the WPAA is to exercise independent judgement in assessing compliance with the Society's PPFM and in addressing conflicting rights and interests of With-Profits policyholders within the Society. The WPAA reviews the exercise of discretion by the Management Committee and provides advice to it if it feels that policyholders' interests are not being fully and properly taken into account.

As at 31 December 2019 there were 4 members of the WPAA. One of the members of the WPAA is a qualified actuary with substantial life office experience. The Terms of Reference for the WPAA are available on the Society's website or by contacting the office. The WPAA's Terms of Reference state that it should meet at least twice per year. Three meetings of the WPAA took place during 2019.

The WPAA raised no material concerns regarding the administration of the With-Profits Fund during 2019 and, therefore, the WPAA does not wish to make a separate report to policyholders for this period.

B2 With-Profits Actuary

The role of the With-Profits Actuary (WPA) includes consideration of compliance with the PPFM, and the exercise of discretion in relation to With-Profits business and the interests of With-Profits policyholders. The Society's WPA during 2019 was Mrs. Alison Carr of SDA LLP, who is a Fellow of the Institute and Faculty of Actuaries.

C Compliance with the PPFM and Exercise of Discretion

This report comments on specific areas, in particular where discretion was used and where the fair treatment of policyholders was relevant.

C1 Communications with policyholders

The Management Committee has responsibility for approving communications with policyholders by reviewing and signing off documents. The Society's PPFM and CFPPFM have been approved by the Management Committee and With-Profits Actuary, as have the bonus notices.

Since 1 January 2018, insurers have been required to provide Key Information Documents (KIDSs) to new policyholders. These documents are updated annually and both provided to policyholders during the application process and shown on the Society's website for selected terms. Revised figures were calculated by the With-Profits Actuary in January 2019 and were issued in respect of all policy sales. However, the documents on the website were not updated. This was an oversight and the Society will ensure that in future it updates the KIDs on its website promptly once the new figures have been provided.

C2 Bonus policy and declarations

The PPFM principles state that when setting regular bonus rates, the Society aims to:

- distribute a proportion of the investment income earned by the assets backing the liabilities in a smoothed manner
- reflect the surplus generated by policies
- have regard to long-term expected rates of return on fixed interest securities
- distribute surplus in a manner that is fair to all policyholders and does not jeopardise the Society's solvency.

The PPFM principles also state that maturity and death payouts will be smoothed from one period to the next by avoiding major changes in regular bonuses.

The PPFM principles were all complied with when setting bonus rates during the year.

All of the Society's policies are conventional With-Profit policies, with maturity payouts based on guaranteed sums assured plus bonuses. During 2019, the Management Committee approved the following regular bonuses in respect of 2018 as a percentage of sum assured:

Policies issued on or before 13 March 1984	1.0%
Policies issued after 13 March 1984 to 31 December 2017	0.50%
Policies issued after 31 December 2017	0.75%

The rates were set by reference to a sustainable level based on asset share and expected investment income according to the investment strategy. The rates were smoothed to avoid a large change in regular bonus rates.

Final bonuses were also paid on maturities. The final bonus rates varied according to the year of policy inception.

C3 Payouts on maturity

The PPFM practices state that the aim in the long term, in determining payouts for maturing With-Profits policies, is to return as a group, on average, 100% of asset shares. On average during 2019, the maturity payouts were 105% of asset shares. This was based on a deliberate decision to pay final bonuses to bring payouts in line with asset shares for each group of policies by term. On average in the period 2011-19, maturity payouts were 96% of asset shares.

The implementation of final bonuses from 1 May 2018 has enabled the Society to vary its surplus payouts by commencement date. It is anticipated that this, together with the new premium rates introduced from 1 January 2018, will lead to average maturity payouts in the long-term of 100% of asset shares.

The PPFM practices also state that, subject to meeting any guaranteed benefits, the maturity payout should fall in the range of 80% to 120% of the average asset share for the group. The aim is for all maturity payouts to fall within this range, although where this is not possible for all policies, at least 90% of payouts should fall within the range. During 2019, there were 1,059 maturing policies. All maturing policies had payouts in the range of 90% to 118% of asset shares. Therefore, this practice was met during 2019.

C4 Payouts on surrender

Surrender values, where applicable, are the amounts payable on cancellation of a policy before it would otherwise be payable on death, disablement or maturity.

The PPFM practices state that the amounts payable on surrender are calculated by reference to the premiums paid and that asset share is used as a guide in determining the bonuses and surrender factors to calculate the amounts payable. This was complied with during 2019.

The PPFM practices state that the aim in the long term, in determining payouts for surrendering With-Profits policies, is to return as a group, on average 100% of asset shares, subject to smoothing and any deductions necessary to protect the interests of remaining policyholders. On average, the surrender payouts during 2019 were 97% of asset shares. On average in the period 2011-19, surrender payouts were 92% of asset shares. However, the average payout for 2017-19 was 99%. It is anticipated that payouts in the long term should be closer to 100% than they have been over the past nine years.

The PPFM states that at least 90% of the surrender payouts for individual policies will fall in the range of 80% to 120% of the average asset shares for the group. During 2019, 89% of surrendering policies had payouts in the range of 80% to 120% of their asset share (with 11% paid between 71% and 80% and none above 120%). Therefore, this practice was not met during 2019. However, all these policies were in force for one to two years. During 2020, the Society will assess the feasibility of updating its surrender factors for policies that have been in force for a short period more frequently than annually.

C5 Investment strategy

The PPFM principles state that the investment strategy of the Society is to maximise the overall return of the investments subject to ensuring that the guarantees are met through maintaining adequate levels of solvency and liquidity. This was put into practice by holding a diversified portfolio of assets and measuring the performance for each asset class against a specified set of benchmarks. The Chief Actuary reviews the Society's investment strategy annually in light of the Society's capital requirement and solvency position, taking into account the statements in the PPFM on investment strategy and makes proposals to the Management Committee. During 2019, the Society invested in bonds, equities, properties, deposits, mortgages and policy loans. The Society retains LGT Vestra as its investment managers and Walker Singleton as its property advisers.

C6 Business risk and new business

The Society manages its risks within a defined framework which comprises the Risk Appetite Statement, the Capital Assessment of Risks and the Risk Register. Ultimate responsibility for risk management rests with the Management Committee whilst the Audit and Risk Management sub-Committee has responsibility for the detailed scrutiny of risk management issues. The Society's Own Risk and Solvency Assessment is a rolling process that provides a detailed analysis of the Society's capital adequacy, risk management and forward-looking perspective. This is achieved using a combination of internal, actuarial and regulatory documents and information to report appropriately on the Society's financial position.

In controlling its business risk and new business, the Society complied with the relevant principles and practices in the PPFM. However, the PPFM states that new business will only be accepted if, in the reasonable opinion of the Management Committee, the terms upon which such plans are accepted are unlikely to have a materially adverse effect on the interests of existing policyholders of the Society at that time. The current investment returns and expenses mean that the new business (on rates introduced in January 2018) is not breaking even on a standalone basis. However, the Management Committee is comfortable that it is not likely to have a materially adverse effect on the interests of the existing policyholders due to the fixed nature of most of the Society's expenses; the new business contributes towards those expenses, thereby reducing those allocated to existing policyholders.

C7 Charges and expenses

The charges applied to policies for the purpose of determining asset shares are the charges deemed appropriate by the Management Committee taking into account the charges included within the premium rates, the level of charges disclosed in product literature and initial costs relating to the acquisition of policies. The total expenses charged to asset shares are the actual expenses incurred by the Society. This is deemed fair and appropriate given the mutual nature of the Society. The asset shares charge expenses to each policy in proportion to the premiums paid which is also deemed to be a fair allocation.

C8 Management of inherited estate

The Society maintains a level of free assets which enables it to invest in a range of investments and to fund the writing of new business. Within the Risk Appetite Statement, a target range for free assets is set and if the free assets were to fall below that range then remedial action would be taken. It is confirmed that through 2019 the management of free assets was in accordance with the PPFM and Risk Appetite Statement.

D Conclusion

Considering compliance with the PPFM in 2020, the Management Committee confirms:

- In setting its payouts for maturities, disablements and deaths, including the setting of bonus rates, the Society complied with the relevant principles and practices in the PPFM.
- In setting its payouts for surrenders, the Society complied with the relevant principles and practices in the PPFM, except:
    - The PPFM states that at least 90% of the surrender payouts for individual policies will fall in the range of 80% to 120% of asset shares. During 2019, 89% of surrendering policies had payouts in the range 80% to 120% of their asset share.
- In setting and complying with its investment strategy, the Society complied with the relevant principles and practices in the PPFM.
- In controlling its business risk and new business, the Society complied with the relevant principles and practices in the PPFM.
- In managing its inherited estate, the Society complied with the relevant principles and practices in the PPFM.

Considering the treatment of With-Profits policyholders and the exercise of discretion in 2019 the Management Committee confirms:

- With-Profits policyholders have been treated fairly in material respects in relation to the exercise of discretion.
- The discretion exercised by the Society during 2019 took the interests of each class of the Society's With-Profits policyholders into account in a reasonable and proportionate manner.

In making this declaration the Management Committee has taken into account advice provide by the With-Profits Actuary on compliance with the PPFM and exercise of discretion during 2019. The Management Committee has also received advice from the Society's With-Profits Advisory Arrangement.

J W Goolamier, Chair	M A Bicknell, Chief Executive
16 June 2020	16 June 2020