

# Report of the Management Committee to With-Profits Policyholders for the year 2016

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## Contents

A	Introduction .....	2
B	Governance Arrangements .....	3
B1	With-Profits Advisory Arrangement .....	3
B2	With-Profits Actuary .....	3
C	Compliance with the PPFM and Exercise of Discretion .....	4
C1	Communications with policyholders.....	4
C2	Bonus policy and declarations .....	4
C3	Payouts on maturity.....	4
C4	Payouts on surrender.....	5
C5	Investment Strategy.....	5
C6	Business risk and new business .....	5
C7	Charges and expenses.....	6
C8	Management of inherited estate.....	6
D	Conclusion.....	7
E	Appendix 1 Report of the With-Profits Actuary to with-profits policyholders of Railway Enginemmen's Assurance Society on the application of discretion during 2016.....	8

## **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. You can obtain a copy 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 from the office.

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 2016 to 31 December 2016.

The Society became a directive society on 1 January 2016, so produced its first PPFM in December 2015. No changes to the PPFM were made in 2016. This is therefore the first report to with-profits policyholders in line with the new requirements.

## **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**

During 2015, it was agreed that a WPAA would be set up. The Management Committee agreed the terms of reference of the WPAA on 23 February 2016 and the WPAA's inaugural meeting was held on 6 December 2016. 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 taken into account.

The WPAA consists of three non-executive members of the Management Committee. The Chair 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 raised no material concerns regarding the administration of the With-Profits Fund during 2016 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 2016 was Alison Carr, who is a Fellow of the Institute and Faculty of Actuaries.

A report from Alison Carr to the with-profits policyholders can be found at Appendix 1.

## **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.

### **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 2016.

All of the Society's policies are conventional with-profit policies, with maturity payouts based on guaranteed sums assured plus bonuses. During 2016, the With-Profits Actuary recommended the following regular bonuses in respect of 2015 as a percentage of sum assured:

Policies issued on or before 13 March 1984	2.50%
Policies issued after 13 March 1984	1.25%

The rates were proposed after considering the experience of the Society in 2015 and the effect on the Society's surplus of such a declaration. These rates were accepted by the Management Committee and declared by the Society.

### **C3 Payouts on maturity**

The PPFM practices state that the Society aims to limit the differences between maturity payouts on similar policies to a maximum of 10% pa. In setting bonus rates for 2015, sample policies were shown to have changes in maturity payouts between 2015 and 2016 of less than 5%.

The PPFM practices also 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. The PPFM also states 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. Three policies (0.3% of maturities) had payouts above 120%, due to the high level of guarantees on those policies. The Society's plans to introduce a terminal bonus series during 2018, alongside new premium rates, will lead to average maturity payouts in the long term of 100% of asset shares.

#### **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 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 2016.

The PPFM also states that the surrender payout for an individual policy should fall in the range of 80% to 120% of the average asset shares for the group. During 2016, some policies fell outside of this range. This generally reflected the need to ensure fairness and protect the interests of remaining policyholders by limiting payouts to no more than the equivalent maturity payouts. This area of non-compliance with the PPFM will be addressed through a review of surrender factors and the introduction of a terminal bonus series.

#### **C5 Investment strategy**

The PPFM principles state that the investment strategy of the Society is to maximise the overall return of the investments of the Society subject to ensuring that the guarantees are met through maintaining adequate 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. A review took place during 2016 and led to changes in investment strategy.

#### **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. It is believed that the risk management system has been effective during 2016. The Society intends to introduce new rates for its regular savings product in 2018.

## **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 2016 the management of free assets was in accordance with the PPFM and Risk Appetite Statement.

## D Conclusion

Considering compliance with the PPFM in 2016, the Management Committee confirms:

- In setting its payouts, including the setting of bonus rates, the Society complied with the relevant principles and practices in the PPFM except that payouts on maturity and surrender were not line with the asset share ranges as specified in the PPFM.
- 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 2016 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 2016 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 2016. The Management Committee has also received advice from the Society's With-Profits Advisory Arrangement.

J W Goolamier, Chairman

20 June 2017

M A Bicknell, Chief Executive

20 June 2017

## **Appendix 1 Report of the With-Profits Actuary to with-profits policyholders of Railway Enginemen's Assurance Society Limited on the application of discretion during 2016**

### **Introduction**

I was appointed as With-Profits Actuary ("WPA") of Railway Enginemen's Assurance Society Limited ("the Society") on 12 June 2014 and held this appointment throughout 2016. I am a Fellow of the Institute and Faculty of Actuaries. I am not a policyholder of the Society.

I have been provided with a copy of the *Report of the Management Committee to With-Profits Policyholders for the year 2016* from the Committee of Management of the Society to with-profits policyholders dated 20 June 2017 for which the Society remains responsible. I have also requested from the Society such information and explanations as I consider reasonably necessary to enable me to perform my duties as WPA. In providing this report, I have relied on the accuracy and completeness of the Committee of Management report and of the information and explanations provided to me by the Society.

### **Purpose**

This report has been prepared for the purpose of compliance with section 4.3.16 of the Supervision Handbook of the Financial Conduct Authority ("FCA"). This requires me to report annually to with-profits policyholders on whether the Society has exercised discretion in a reasonable and proportionate manner, having regard to the rules and guidance laid down in section 20.2 of the Conduct of Business Sourcebook of the FCA.

As the Society became directive on 1 January 2016, this is the first such report I have made for the Society's policyholders.

### **Actuarial guidance**

The report accords with the following guidance from the Financial Reporting Council:

- TAS R on "Reporting Actuarial Information"
- TAS D on "Data"
- TAS M on "Modelling"
- Insurance TAS

However, it should be noted that I have not considered it necessary or desirable to repeat or elaborate on material that is covered by the Committee of Management report to which my report is annexed.

## Conclusion

In my opinion, based on the information and explanations provided to me by the firm, and taking into account the rules and guidance in COBS 20:

- With-profits policyholders have been treated fairly in material respects in relation to the exercise of discretion during 2016.
- The discretion exercised by the firm during 2016 took the interests of each class of the firm's with-profits policyholders into account in a reasonable and proportionate manner.

Alison Carr, With-Profits Actuary

29 June 2017