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Value of with-profits for consumers Phase 1

Tim Bateman (Chair),
Jonathan Welsh (Deputy Chair), and
Rosalind Rossouw

03 May 2017

Working party members:

- **Chair:** Tim Bateman (Mazars)
- **Deputy Chair:** Jonathan Welsh (Wesleyan)
- **Secretary:** Ben Stroud (ReAssure)
- Andrew Fraser (Standard Life)
- Helen Jones (NFU Mutual)
- Rebecca MacDonald (PwC)
- Rosalind Rossouw (Sun Life Financial of Canada)
- Ross Thompson (Standard Life)

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Introduction

The Value of With-Profits for Consumers Working Party.

Scope: Do consumers understand the value of their with-profits policies?



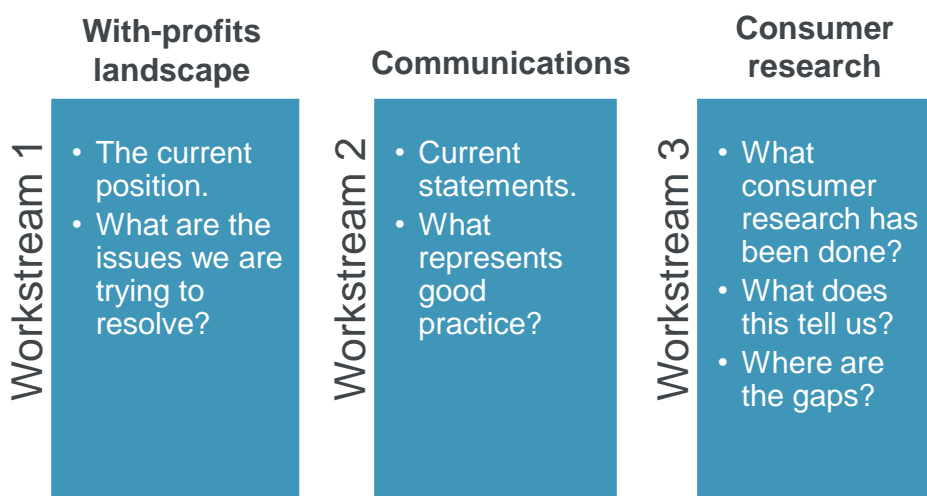
Purpose: To share findings to date and to request feedback on ideas and thoughts for further research

We have included contact details for anyone who would like to input

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Phase 1: Workstreams



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Workstream 1

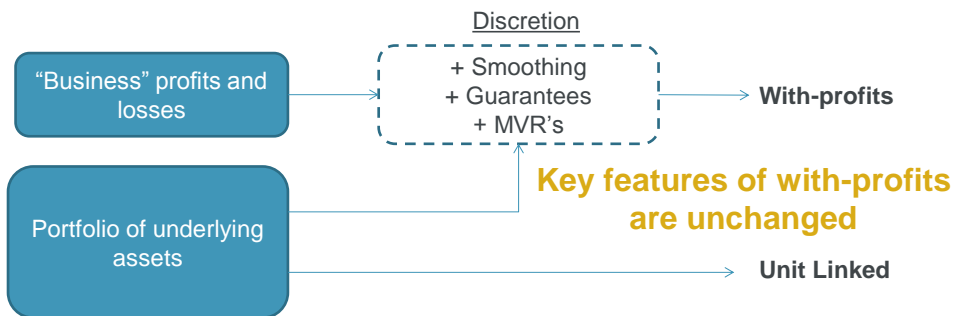
The with-profits landscape

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The with-profits landscape

Key features of with-profits business



“based on a diversified portfolio, a degree of smoothing to iron out peaks and troughs of asset performance, and increasing guarantees over a policy term is not seen in any other mass-marketed investment product...”¹

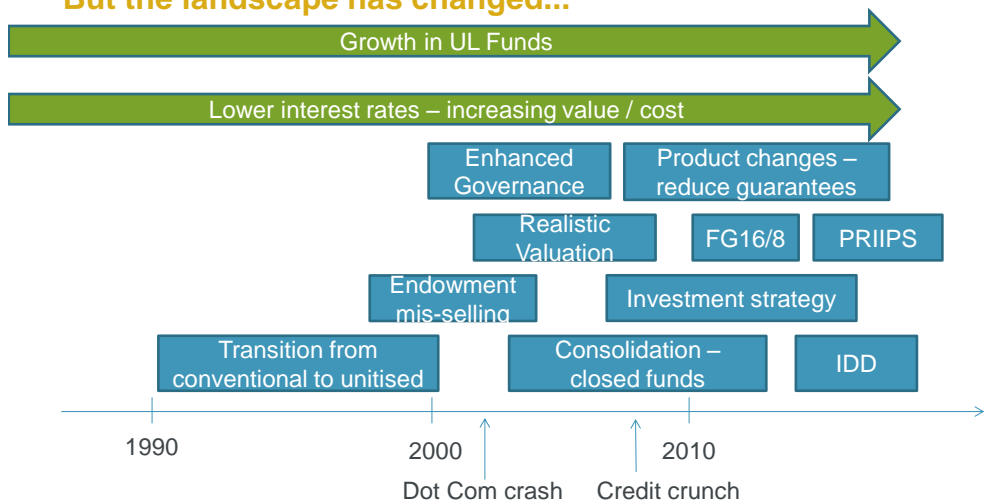
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1. With Profits without mystery; Ranson & Headdon; 1990 6

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The with-profits landscape

But the landscape has changed...

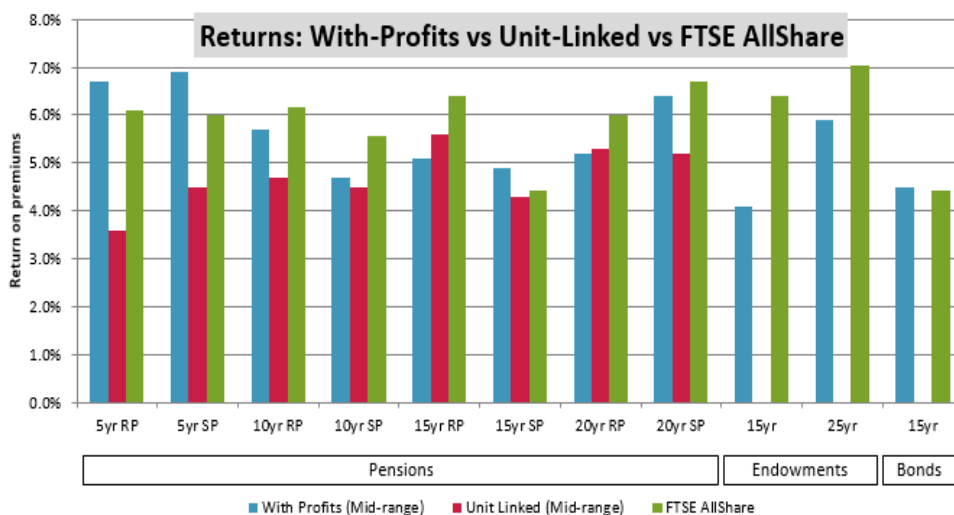


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Have with-profits policies performed?



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Source: Money Management surveys – values typically as at 1st Jan 2016, 1 March 2015 where PRA returns have been used. 8

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Have with-profits policies performed?

A selection of headlines ...

Savers should plot their escape from zombie funds

The Times – 9 July 2016

Help! Why has my 'with profits' pension fund shrunk 11% in two years as stocks hit record highs?

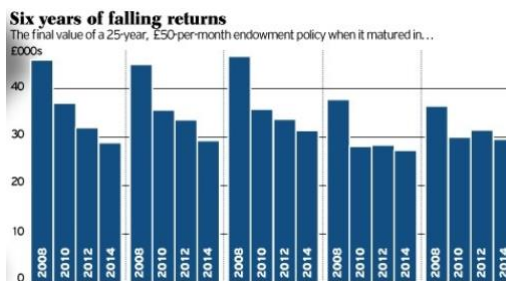
www.thisismoney.co.uk – 20 May 2015

Savers see with-profits pensions slashed by 87%: Thousands promised annual payments of £30,000 now set to receive just £3,700

www.thisismoney.co.uk – 12 July 2016

Deal or no deal? Why deciding when to take 'with profits' benefits can be like playing the popular game show

www.thisismoney.co.uk – 30 May 2015



The telegraph – March 2014

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Have with-profits policies performed?

Whether a fund has “delivered” is a combination of both:

- Performance
- Expectation – setting realistic expectations, managing these on a regular basis.

Some common themes:

- Pay outs trending downwards
- Projection rates
- Smoothing

“Criticism may not be agreeable, but it is necessary. It fulfils the same function as pain in the human body. It calls attention to an unhealthy state of things.” – Winston Churchill

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Workstream 1

“With-Profits” varies widely

Asset Mix

Average EBR = 35%¹

Varies from 0% - 60% (or 0%-70% incl. property).

Other features

- Estate distributions
- Exposure to business profits / losses
- Other strategic investments
- Expenses
- Smoothing
- Guarantees

These features vary between with-profits funds, but also vary over time within the same fund

Returns

Difference between best and worst:

Term	WP Pens ¹	UL Mixed ²
15 yr	+280%	+20%
20 yr	+330%	+40%

Pay outs on the best funds were around 4x the pay out on the worst

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1. Source: Money Management – as at 1 Jan 2016

2. Source: Money Management , mixed investment 40-85 shares – as at 1 Jan 2016

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Summary - The with-profits landscape

- On average, with-profits funds have performed reasonably when compared against Unit Linked.
- BUT there is a wide variation of payouts within the with-profits grouping.
- Given current market trends, this variation is likely to continue.
- Success will be measured by consumers against what they thought the product would deliver.
- This highlights the importance of clear communication.
- With-profits funds can change markedly over the consumers' investment lifetime, so ongoing communication is particularly important.

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Workstream 2

Review of with-profits communications

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Workstream 2

Review of with-profits communications

Communications are written to be understandable.

That doesn't mean they will be understood.

Review of existing with-profits communications

- Review approach
- Review output
- Proposals for further improvements with good practice highlighted

Workstream 2

Review of with-profits communications

Review approach

- 36 with-profits communications
- Identified comparable key aspects, including FG16/8 guidance
- Outcome 2: “It is for **firms to determine what information their customers need** on a regular basis, and an ad hoc basis, **so that they have a clear understanding of how their product is performing and of the benefits, risks and costs associated with their product.** The guidance states that firms may wish to make a record of the information that they consider relevant or appropriate to include in the annual statement or other regular communications for their range of products. The guidance also makes clear that **the list of items** that should be included in the communication **is not prescribed**, but **should be included where relevant or appropriate to customers’ information needs.**”
- Maintained a focus on **value**

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Workstream 2

Review of with-profits communications

Proposals for further improvement: Conventional With-Profits

Date of Statement	30 June 2017	
Policy Start Date	DD MMMM YYYY	
The date your policy is due to mature	DD MMMM YYYY	
Premiums paid over the last statement year	£420	
Basic guaranteed value (sum assured) [A]	£100,000	Your guaranteed benefits
Existing bonuses (the value of bonuses we've added to your policy in previous years) [B]	£20,000	
Annual bonus for 2017 [C]	£500	
Total guaranteed value [A + B + C]	£120,500	

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Review of with-profits communications

Proposals for further improvement: Conventional With-Profits

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Existing bonuses (the value of bonuses we've added to your policy in previous years) [B]	£20,000	
Annual bonus for 2017 [C]	£500	
Total guaranteed value [A + B + C]	£120,500	
Final bonus [D]	£6,500	Your benefits which are not guaranteed
Surrender value	£105,000	
Guaranteed minimum death benefit	£250,000	Other benefits

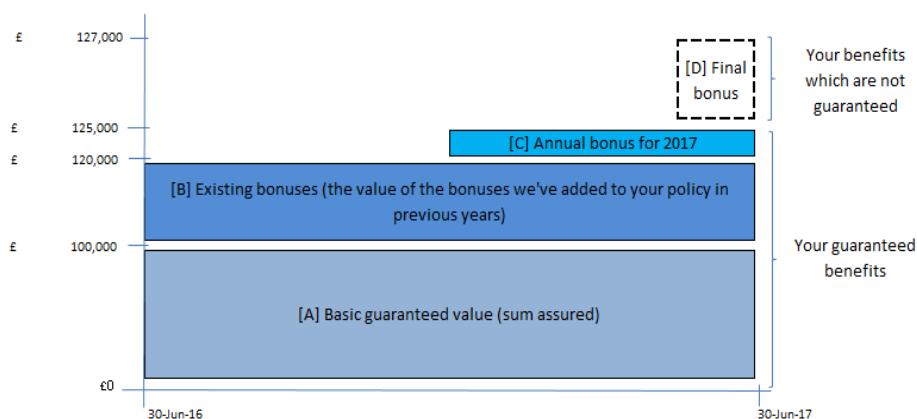
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Review of with-profits communications

Proposals for further improvement: Conventional with-profits



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Workstream 2

Review of with-profits communications

Proposals for further improvement: Pensions and Investments

Date of Statement	30 June 2017
Policy Start Date	DD MMMM YYYY
Premiums paid over the last statement year	£3,000
Fund based charges over the last statement year	£69

	Fund Name	Number of Units held [A]	Unit Price (£) [B]	Fund Value [A x B]	% of Plan
	Global Property	100,000	1.1	£110,000	63%
+	With-Profits	50,000	1.2	£60,000	34%
+	Growth Bonus	5,000	1.2	£6,000	3%
=	Total Fund Value			£176,000	100%

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Review of with-profits communications

Proposals for further improvement: Pensions and Investments

Date of Statement	30 June 2017
Total Fund Value	£176,000
+ Interim Bonus	£250
+ Final Bonus	£30,000
- Market Value Reduction	£0
= Plan Value as at 30 June 2017	£206,250
Transfer Value as at 30 June 2017	£205,500
Plan Value as at 30 June 2016	£195,000
Guaranteed Minimum Death Benefit	£250,000

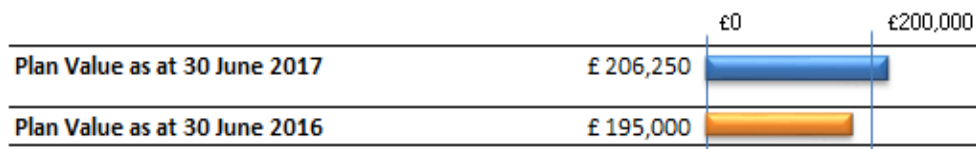
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Workstream 2

Review of with-profits communications

Proposals for further improvement: Pensions and Investments



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Workstream 3

Review of with-profits consumer research



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Workstream 3

Review of with-profits consumer research

Desk-based research of material available to cover:

- A. Existing with-profits consumer research
- B. Wider consumer research of relevance

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Workstream 3

Review of with-profits consumer research

A. Existing with-profits consumer research

- A range of **research was reviewed** from the profession, insurance providers and industry bodies going back nearly a decade.
- Whilst there is much research around with-profits very little has been undertaken **from the perspective of the consumer**.

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Workstream 3

Review of with-profits consumer research

A. Providers' with-profits consumer research

Value of received information:

- Consumers placed the greatest value on their benefit statement, followed by the covering letter
- Less value is placed on Q&As or booklets, which are perceived to be sales pitches
- Document margins are seen as a good place to fit additional information

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Workstream 3

Review of with-profits consumer research

A. Providers' with-profits consumer research

Reason for receiving information:

- It is not always clear to consumers why they have been contacted
- Consumers like to see a company logo on a plain envelope to identify its importance
- Glossy envelopes were seen to contain promotional / sales material and often binned whilst plain envelopes were overlooked!

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Workstream 3

Review of with-profits consumer research

A. Providers' with-profits consumer research

Consumer understanding:

- The most common reason for choosing a with-profits policy was as a result of receiving independent financial advice
- The **majority** of consumers were unable to articulate the features, benefits or drawbacks of a with-profits policy
- Financially sophisticated consumers were often less happy with the information provided, possibly suggesting greater expectations.

Despite the lack of understanding or appreciation of the inner workings of their policy, the majority of consumers intend to hold onto their policy until maturity / retirement

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Workstream 3

Review of with-profits consumer research

B. Wider consumer research of relevance

The Money Advice Service (MAS) performed research of retirement language by a combination of focus groups and in-depth interviews

- Different **terminology used** for the options available to consumers at retirement was considered
- Recommendations included the use of accessible language including terms such as “pension pot”, “lump sums” and “lifelong, regular income” (see appendix)
- The research was **not with-profits specific**.

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Conclusion

Concluding thoughts and next steps

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 Sponsorship
 Thought leadership
 Progress
 Community
 Sessional Meetings
 Education
 Working parties
 Volunteering
 Research
 Shaping the future
 Networking
 Professional support
 Enterprise and risk
 Learned society
 Opportunity
 International profile
 Journals
 Support

Conclusion

- The performance of with-profits has been comparable to UL or FTSE, but provided the additional security offered by guarantees
- With-profits funds can change markedly over the consumers' investment lifetime, so ongoing communication is particularly important
- Providers should ensure benefit statements continue to meet the needs of consumers
- We should focus on encouraging better, more helpful communication with consumers
- There is not much existing consumer-specific with-profits research

Next steps

This concludes the first phase of the working party's research.
Phase 2 will comprise of a consumer survey.

Please contact us if you would like to get involved.

Survey to be performed in coming months and results shared later in the year.

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Contributors

Our special thanks go out to the following contributors to the working party:

- Mazars
- Wesleyan
- ReAssure
- Standard Life
- NFU Mutual
- Sun Life Financial of Canada
- Aviva
- LV=
- Equitable Life
- KPMG
- Healthy Investment
- Kingston Unity
- Royal London
- AEGON
- Phoenix Life
- Legal & General
- Scottish Widows
- ABI
- MAS

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Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

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Should you require any further information, please do not hesitate to contact:

- **Chair:** Tim Bateman (Mazars) Tim.Bateman@mazars.co.uk
- **Deputy Chair:** Jonathan Welsh (Wesleyan) Jonathan.Welsh@wesleyan.co.uk
- **Secretary:** Ben Stroud (ReAssure) Ben.Stroud@reassure.co.uk
- Andrew Fraser (Standard Life) Andrew_M_Fraser@standardlife.com
- Rebecca MacDonald (PwC) Rebecca.Macdonald@pwc.com
- Rosalind Rossouw (Sun Life Financial of Canada) Rosalind.Rossouw@sloc.co.uk
- Ross Thompson (Standard Life) Ross_Thompson@standardlife.com

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Pic 5

Appendices

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Product	Freq	Term (years)	WP Return	FTSE AllShare	Avg UL Pens	Comments
Pension	RP	10	5.7%	2.5%	5.9%	Slightly lower than UL, beats FTSE
Pension	RP	20	5.2%	2.5%	5.6%	Slightly lower than UL, beats FTSE
Pension	RP	30	8.4%	4.1%		Beats FTSE
Pension	SP	10	4.7%	1.9%	4.8%	In line with UL, beats FTSE
Pension	SP	20	6.4%	3.3%	5.0%	Beats UL, beats FTSE
Pension	SP	30	8.9%	5.5%		Beats FTSE
Endowment	SP	10	4.1%	2.5%		Beats FTSE
Endowment	SP	25	5.9%	3.3%		Beats FTSE
Bond	SP	15	4.5%	2.8%		Beats FTSE

Willis Towers Watson survey

With-Profits Expense and Pay-out Benchmarking Survey - 14 November 2016

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Freq	Term (years)	WP Payout	WP Return	UL Payout	UL Return	Comments
RP	5	14,221	6.7%	13,734	5.1%	WP win
RP	10	32,329	5.8%	32,992	5.9%	UL narrow win
RP	15	53,731	5.1%	58,193	5.8%	UL win
RP	20	81,494	5.0%	82,979	5.6%	UL win
SP	5	13,964	6.9%	12,745	4.7%	WP win
SP	10	16,679	5.2%	16,543	4.8%	WP win
SP	15	20,614	4.9%	19,402	4.3%	WP win
SP	20	35,579	6.6%	28,655	5.0%	WP win

Money Management Survey

Money Management Personal Pensions survey – March 2016

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Workstream 2

Review of with-profits communications

Review output

	The Current Value of the Policy ¹	Surrender Value of the Policy	The Value of the Policy at the previous communication	Premiums paid in the last year	Informing customer benefit is not guaranteed	Indicative level of charges (in £ terms) applicable to the policy	Where a policy has a guarantee	Where a policy has (additional) life cover
Conventional	100%	8%	Not directly applicable	25% showed monthly premium	58%	33% made mention of charges	100%	67%
Pensions	100%	77%	31%	38%	77%	33% made mention of charges	62%	38%
Investment / Savings	100%	100%	88%	38%	50%	50%	63%	88%
Total	100%	58%	52%	24%	64%	30%	76%	61%

¹ Taken to be guaranteed minimum policy benefit for Conventional with-profits plans

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Workstream 2

Review of with-profits communications

Review output

	Sum Assured	Regular Bonus	Final Bonus	Market Value Reduction	Details of a customer's options are provided	Contact details
Conventional	92%	92%	25% stated one might be payable but didn't specify the value	8%	Not directly applicable	100%
Pensions	15%	54%	54%	54%	46%	100%
Investment / Savings	n/a	63%	88%	63%	50%	100%
Total	39%	70%	42%	39%	48%	100%

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Workstream 2

Review of with-profits communications

Proposals for further improvement: Conventional with-profits

- **Premiums paid over the last year:** This is the total payment you've made in the past year. It's important to pay your premiums. The guaranteed benefit amounts quoted below are only payable if we have received all of your premiums due.
- **Basic guaranteed value (sum assured) [A]:** This is the minimum amount that we guarantee to pay at the maturity date or when a life assured dies (if this is earlier), before we add bonuses.
- **Regular bonus [B + C]:** Regular annual bonuses increase the minimum amount that we guarantee to pay at the maturity date or when a life assured dies (if this is earlier).
- **Total guaranteed value [A + B + C]:** This is the total amount that we guarantee to pay at the maturity date or when a life assured dies (if this is earlier).

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Short descriptor	Descriptive sentence	Additional Detail
Take your pension pot in one go	You can take the whole amount as a lump sum in one go if you wish, subject to tax and fees.	Explicitly refer to tax implications and fees. Avoid references to cash – seen to invite short-termism
Take your pension pot as a number of lump sums	You leave your money in your current pension pot and take lump sums from it when you need it.	Explicitly refer to tax implications, fees and rules regarding frequency of withdrawals. Avoid references to cash.
Get a flexible retirement income	You convert all or some of your pension pot into an investment specifically designed to provide an income.	Differentiate from annuities. Emphasise tax implications and that income is not guaranteed. Outline advantage – flexibility.
Get a lifelong, regular income	A lifetime annuity provides you with a regular retirement income for life – with the guarantee that the money won't run out before you die.	Differentiate from drawdown. Clarify guaranteed / low-risk nature. Address concerns regarding early death and the effect of inflation.
You don't have to choose one option – you can mix them over time or over your total pot	You don't have to choose one option – you can choose from a variety of options as you like, and take income or lump sums at different times to suit your needs.	Relate explicitly to all the other options. Clarify the advantages of using this option to create a balanced portfolio and mix of flexible and steady income. Encourage use of financial advice.
Keep your retirement savings where they are	You can delay accessing your pension pot beyond your selected retirement date, or your scheme's normal retirement date.	Address reasons for doing so – advantages of leaving pension untouched. Clarify for how long this can be left and what would happen to the fund in the event of death.

Money Advice Service – Retirement Language

Retirement Language – 4th February 2016

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