

Conduct of Business Sourcebook

Chapter 20

With-profits

20.5 With-profits governance

Requirement to appoint a with-profits committee or advisory arrangement

20.5.1

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A *firm* must, in relation to each *with-profits fund* it operates:

- (1) appoint:
 - (a) a *with-profits committee*; or
 - (b) a *with-profits advisory arrangement* (referred to in this section as an 'advisory arrangement'), but only if appropriate, in the opinion of the *firm's governing body*, having regard to the size, nature and complexity of the fund in question;
- (2) ensure that the *with-profits committee* or advisory arrangement operates in accordance with its *terms of reference*; and
- (3) make available a copy of any *terms of reference* on the *firm's* website, or if the *firm* does not have a website, at the request of *policyholders*.

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- (1) Ultimate responsibility for managing a *with-profits fund* rests with the *firm* through its *governing body*. The role of the *with-profits committee* or advisory arrangement is, in part, to act in an advisory capacity to inform the decision-making of a *firm's governing body*. The *with-profits committee* or advisory arrangement also acts as a means by which the interests of *with-profits policyholders* are appropriately considered within a *firm's* governance structures. The *with-profits committee* or advisory arrangement should address issues affecting *policyholders* as a whole or as separately identifiable groups of *policyholders* generally rather than dealing with individual *policyholder* complaints or taking management decisions with respect to a *with-profits fund*.
- (2) If a *firm* considers that it is appropriate to appoint an advisory arrangement, a *firm's governing body* will need to decide whether it is appropriate to appoint an independent person or one or more *non-executive directors* to carry out the role. The *FCA* expects *firms* to make this determination according to the nature, size and complexity of the fund in question. So the larger or more complex the fund is, the more likely it would be that it would be appropriate to appoint an independent person.
- (3) Where a *firm* has appointed a *with-profits committee* to one of its *with-profits funds* it may also decide to appoint that *with-profits*

committee to some or all of its other *with-profits funds*, even if the *firm* would not have determined it appropriate to appoint a *with-profits committee* to those other funds when considered individually having regard to their size, nature or complexity.

Terms of reference of with-profits committee or advisory arrangement

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A *firm* must ensure that the *terms of reference* contain, as a minimum, terms having the following effect:

- (1) the role of the *with-profits committee* or advisory arrangement is, as relevant, to assess, report on, and provide clear advice and, where appropriate, recommendations to the *firm's governing body* on:
 - (a) the way in which each *with-profits fund* is managed by the *firm* and, if a *PPFM* is required, whether this is properly reflected in the *PPFM*;
 - (b) if applicable, whether the *firm* is complying with the principles and practices set out in the *PPFM*;
 - (c) whether the *firm* has addressed effectively the conflicting rights and interests of *with-profits policyholders* and other *policyholders* or stakeholders including, if applicable, shareholders, in a way that is consistent with *Principle 6* (treating customers fairly); and
 - (d) any other issues with which the *firm's governing body*, *with-profits committee* or advisory arrangement considers *with-profits policyholders* might reasonably expect the *with-profits committee* or advisory arrangements to be involved;
- (2) that the *with-profits committee* or advisory arrangement must:
 - (a) decide on the specific matters it will consider in order to enable it to carry out its role described in (1)(a) to (d) as appropriate to the particular circumstances of the *with-profits fund(s)*; and
 - (b) in any event give appropriate consideration to the following non-exhaustive list of specific matters:
 - (i) the identification of surplus and *excess surplus*, the merits of its distribution or retention and the proposed distribution policy;
 - (ii) how bonus rates, smoothing and, if relevant, market value reductions have been calculated and applied;
 - (iii) if relevant, the relative interests of *policyholders* with and without valuable guarantees;
 - (iv) the *firm's* with-profits customer communications such as annual policyholder statements and product literature and whether the *with-profits committee* or advisory arrangement wishes to make a statement or report to *with-profits policyholders* in addition to the annual report made by a *firm*;
 - (v) any significant changes to the risk or investment profile of the *with-profits fund* including the management of material illiquid investments and the *firm's* obligations in relation to *strategic investments*;

- (vi) the *firm's* strategy for future sales supported by the assets of the *with-profits fund* and its impact on surplus;
- (vii) the impact of any management actions planned or implemented;
- (viii) relevant management information such as customer complaints data (but not necessarily information relating to individual customer complaints);
- (ix) the drafting, review, updating of and compliance with run-off plans, court schemes and similar matters;
- (x) the costs incurred in operating the *with-profits fund*;
- (xi) the identification and extent of the *firm's with-profits funds*, with particular regard to the considerations as to whether a part of the *with-profits fund* constitutes a separate *with-profits fund* in accordance with ■ COBS 20.1A.2 R (Sub-funds); and
- (xii) the use and purpose of, and terms under which, support assets are available to the *with-profits fund*, having regard to the considerations in ■ COBS 20.2.33 G to ■ COBS 20.2.34 G and ■ COBS 20.2.34A R.

(3) that any person appointed as a member of the *with-profits committee* or as a person carrying out the advisory arrangement must have the appropriate skills, knowledge and experience to perform, or contribute to, as appropriate, the role set out in (1) and (2);

(4) if the firm appoints a *with-profits committee*:

- (a) that there must be three or more members;
- (b) that the quorum for any meeting (or decision by written procedure) must be at least half of the number of, and no less than two, members; and

(5) that the *with-profits committee* or advisory arrangement must:

- (a) advise the *governing body* on the suitability of candidates proposed for appointment as the *with-profits actuary*; and
- (b) assess the performance of the *with-profits actuary* at least annually, and report its view to the *governing body* of the *firm*.

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- (1) The *FCA* expects that a *with-profits committee* will meet at least quarterly and ad hoc if required.
- (2) The *FCA* expects that, in general, a *with-profits committee* or advisory arrangement will work closely with the *with-profits actuary*, and obtain his opinion and input as appropriate.

Role of with-profits committee or advisory arrangement in the firm's governance

20.5.5

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A *firm* must:

- (1) ensure that its *governing body*, in the context of its consideration of issues referred to in ■ COBS 20.5.3R (1)(a) to ■ (d) and ■ (2)(b)(i) to ■ (x):

- (a) obtains, as relevant, assessments, reports, advice and/or recommendations of the *with-profits committee* or advisory arrangement, if the *governing body*, the *with-profits committee* or advisory arrangement considers that significant issues concerning the interests of *with-profits policyholders* need to be considered by the *firm*;
 - (b) allows the *with-profits committee* or advisory arrangement sufficient time to enable it to provide fully considered input on the issues to be considered;
 - (c) considers fully and gives due regard to the input of the *with-profits committee* or advisory arrangement when determining issues concerning the management of the *with-profits funds* and the interests of *with-profits policyholders*;
 - (d) if the *governing body* decides to depart in any material way from the advice or recommendations of the *with-profits committee* or advisory arrangement, sets out fully its reasons and allows the *with-profits committee* or advisory arrangement a reasonable period to consider them and respond; and
 - (e) considers any further representations from the *with-profits committee* or advisory arrangement and, if appropriate, sets out fully any additional reasons if it continues to depart from the *with-profits committee* or advisory arrangement's advice or recommendation;
- (2) provide a *with-profits committee* or advisory arrangement with sufficient resources as it may reasonably require to enable it to perform its role effectively;
 - (3) notify the *FCA* of the decision of the *governing body* to depart from the advice or recommendation of the *with-profits committee* or advisory arrangement if the *with-profits committee* or advisory arrangement considers that the issue is sufficiently significant and requests of the *governing body* that the *FCA* be informed; and
 - (4) consult the *with-profits actuary* on the appointment of a new member of the *with-profits committee* or of the person or persons carrying out the advisory arrangement.

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- (1) ■ COBS 20.5.5R (2) requires that a *firm* provides a *with-profits committee* or advisory arrangement with sufficient resources. A *with-profits committee* or advisory arrangement should be able to obtain external professional, including actuarial, advice, at the expense of the *firm*, if the *with-profits committee* or advisory arrangement considers the advice to be necessary to perform its role effectively. In a proprietary *firm* the *with-profits committee* or advisory arrangement should be able to request that the cost of the external professional advice either is not chargeable to the *with-profits fund* in question, or is shared with the *with-profits fund*, according to whether the issue under consideration is wholly or partly to the benefit of the *firm* rather than *policyholders*. A *with-profits committee* or advisory arrangement should also be adequately supported by the *firm's* own internal resources and support functions. This may include the *firm* ensuring that relevant employees, including the *with-profits actuary*, are made sufficiently available, and provide

relevant information and input, to assist the *with-profits committee* in its role, as required.

- (2) If the *with-profits committee* or advisory arrangement wishes to make a statement or report to *with-profits policyholders* in addition to the annual report made by a *firm*, the effect of ■ COBS 20.5.5R (2) is that a *firm* will need to facilitate this.
- (3) In order to comply with ■ SYSC 3.2.20 R the *FCA* expects *firms* to keep full records of all requests of, and material produced by, the *with-profits committee* or advisory arrangement, and of all decisions and reasons of the *governing body* as described in ■ COBS 20.5.5R (1)(d) and ■ (e).
- (4) For the purposes of ■ COBS 20.5.5R (3), the *FCA* expects that it will only be in exceptional circumstances that a *with-profits committee* or alternative arrangement will consider a departure from a recommendation or advice to be sufficiently significant to warrant its making a request of the *governing body* that the *FCA* be informed.

Assessment of independence by governing body

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- (1) The *FCA* expects the *governing body* of the *firm* to decide whether a member of the *with-profits committee* or a person (other than a *non-executive director*) carrying out the advisory arrangement is independent. The *FCA* expects a *firm's governing body* to adopt the following approach and have regard to the following factors when making this assessment:
 - (a) the *governing body* should determine whether the person is independent in character and judgment and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the person's judgment; and
 - (b) the *governing body* should state its reasons if it determines that a person is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination, including if the person:
 - (i) has been an employee of the *firm* or group within the last five years; or
 - (ii) has, or has had within the last three years, a material business relationship with the *firm* either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the *firm*; or
 - (iii) has received or receives additional remuneration from the *firm*, participates in the *firm's* share option or a performance-related pay scheme, or is a member of the *firm's* pension scheme; or
 - (iv) has close family ties with any of the *firm's* advisers, directors or senior employees; or
 - (v) has significant links with the *firm's* directors through involvement in other companies or bodies; or
 - (vi) represents a significant shareholder; or
 - (vii) has served on the *governing body* for more than nine years from the date of their first election.

- (2) If a *firm* appoints one or more *non-executive directors* to carry out the advisory arrangement, the *FCA* expects the *governing body* of the *firm* to be satisfied that that person or persons is or are adequately able to provide independent judgment.

Governance arrangements in relation to the PPFM

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In complying with the *rule* on systems and controls in relation to compliance, financial crime and money laundering (■ SYSC 3.2.6 R), a *firm* should maintain governance arrangements designed to ensure that it complies with, maintains and records, any applicable *PPFM*. These arrangements should:

- (1) be appropriate to the scale, nature and complexity of the *firm's with-profits business*; and
- (2) include the approval of the *firm's PPFM* by its *governing body*.