

## **RUN-OFF PLANS FOR CLOSED WITH-PROFITS FUNDS INSTRUMENT 2005**

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### **Commencement**

- C. This instrument comes into force as follows:
- (1) SUP App 2.15.7G (7)(b), in Annex B to this instrument, comes into force on 31 December 2005;
  - (2) the remainder of this instrument comes into force on 30 June 2005.

### **Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with Annex A to this instrument.

### **Amendments to the Supervision manual**

- E. The Supervision manual is amended in accordance with Annex B to this instrument.

### **Citation**

- F. This instrument may be cited as the Run-Off Plans for Closed With-Profits Funds Instrument 2005.

By order of the Board  
16 June 2005

## Annex A

### Amendments to the Conduct of Business sourcebook

In this Annex, the text shown is that which results from the Treating With-Profits Policyholders Fairly Instrument 2005 (FSA 2005/4), underlining indicates new text and striking through indicates deleted text.

After COB 6.12.98R, insert the following:

6.12.98A G A firm should also include the information described in SUP App 2.15 in its run-off plan.

...

6.12.101 G ~~A run-off plan submitted to the FSA under COB 6.12.94R (2) should:~~

- ~~(1) identify, and explain, any material differences between the firm's run-off plan and the relevant parts of its PPFM;~~
- ~~(2) identify, and explain, any actual or potential changes in the firm's maturity or surrender payment target ranges and its smoothing policy;~~
- (3) explain how the fact of run-off affects the firm's investment strategy (if it does);
- (4) explain how the firm anticipates capital will become available for distribution to policyholders;
- (5) explain how the costs charged to the with-profits fund may change (if they will);
- (6) detail any new deductions to be made from surrender payments (if any) and explain how they are consistent with Principle 6 (Customers' interests) and COB 6.12.39R to COB 6.12.45R; and
- (7) explain how it plans to address any additional operational risks which might flow from closure. ~~[deleted]~~

6.12.102 G ~~The FSA has powers, for example, under section 165 of the Act (Authority's power to require information), to require a firm that has ceased to effect new contracts of insurance in a with-profits fund to provide information on how it will ensure a full and fair distribution of that fund and its inherited estate (if any). The FSA may use that power if a firm's run-off plan does not provide sufficient evidence of a full and fair distribution or appropriate arrangements for ensuring the protection of the interests and security of its with-profits policyholders. [deleted]~~

## Annex B

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

SUP Appendix 2 Insurers: Scheme of operations and run-off plans

- 2.1.1 R ~~This appendix applies~~ SUP App 2.2 to SUP App 2.14 apply to an *insurer*, unless it is:  
...
- 2.1.2 G This appendix applies to every *friendly society* ~~as a friendly society~~ that is an *insurer*.
- 2.1.3 G SUP App 2.15 applies to an insurer carrying on with-profits business, but only if COB 6.12.94R (Ceasing to effect new contracts of insurance in a with-profits fund) also applies.

After SUP App 2.14 insert the following new section, which is not underlined:

2.15 Run-off plans for closed with-profits funds

- 2.15.1 G The run-off plan required by COB 6.12.94R(2) should include the information described in SUP App 2.15.2G to SUP App 2.15.13G in respect of the relevant *with-profits fund*.

#### Funding

- 2.15.2 G A *firm's* run-off plan should describe how the *firm* proposes to manage the run-off of the *with-profits fund*. That description should include:
- (1) details of the expected duration and costs of fully running off the fund's liabilities;
  - (2) an explanation as to how a solvent run-off will be funded; and
  - (3) details of the *firm's* future strategy for managing the risks associated with the run-off of the fund.

#### Investment risk

- 2.15.3 G A *firm's* run-off plan should include an explanation of its future investment strategy, including:
- (1) its strategy for matching the *with-profits fund's* liabilities with appropriate

assets; and

- (2) any changes it expects to make to the *with-profits fund's* investment strategy as a result of the closure of the *with-profits fund*, including any changes to the proportions of different types of investments.

#### Credit risk

- 2.15.4 G A *firm's* run-off plan should include an explanation of its strategy for managing the *with-profits fund's* counterparty and *credit* risk, both within and external to the *firm's* group.

#### Operational risk

- 2.15.5 G A *firm's* run-off plan should show how it will address any additional operational risks that may flow from the closure of the *with-profits fund*, including:
- (1) any changes that it proposes to make to staffing arrangements for the run-off;
  - (2) an estimate of the cost of proposed operational changes, including redundancy costs; and
  - (3) any *material outsourcing* arrangements it proposes to enter into, explaining how the *firm* will address any specific operational risks created by those arrangements.

#### Reinsurance

- 2.15.6 G A *firm's* run-off plan should explain how it will use and manage *reinsurance* (if it will), including:
- (1) any new inwards or outwards *reinsurance* it proposes to enter into as a result of the closure of the *with-profits fund* identifying, in each case, the proposed counterparty and the counterparty's relationship to the *firm's* group (if any); and
  - (2) how it will manage the risk that the *reinsurance* in (1) will not perform as expected.

#### Governance and impact on policyholders

- 2.15.7 G A *firm's* run-off plan should include:
- (1) details of any changes that will be made to the *firm's* corporate governance arrangements as a consequence of closure;

- (2) an explanation of how costs charged to the *with-profits fund* may change in the light of closure;
- (3) an explanation of any changes it will make, as a consequence of closure, to any charges for guarantees, including:
  - (a) the circumstances in which those charges may be varied in the future; or
  - (b) the manner by which the level of any appropriate variation to those charges may be determined;
- (4) an explanation of any actual or potential changes in the maturity payment or surrender payment target ranges that the *firm* will apply to determine benefits under its *with-profits policies*;
- (5) an explanation of any actual or potential changes in the *firm's* smoothing policy as a consequence of closure;
- (6) an explanation of any changes to the *firm's projection* rates as a consequence of closure;
- (7) details of any new deductions to be made from the *firm's* surrender payments, together with an explanation as to how those deductions are consistent with:
  - (a) *Principle 6* (Customers' interests); and
  - (b) *COB 6.12.39R* to *COB 6.12.45R* (Amounts payable under with-profits policies: Surrender payments);
- (8) if there are groups of unitised *with-profits policies* in the *with-profits fund* with similar market value reduction free dates, an explanation as to whether:
  - (a) the *firm* expects surrenders to peak around any of those dates; and
  - (b) if it does, how it proposes to deal with those peaks;
- (9) details of the information that the *firm* gives to its *with-profits policyholders* about their *open market options* when its *pension policies* vest and any changes that will be made to that information as a result of the closure;
- (10) details of how the *firm* will deal with any potential mis-selling costs that may arise in the future in respect of *contracts of insurance* effected in the *with-profits fund*;
- (11) an explanation of how the *firm*:
  - (a) anticipates capital will become available for distribution to *policyholders* (and shareholders where appropriate); and
  - (b) will ensure a full and fair distribution of the closed *with-profits fund*, including any *inherited estate*;

including details of:

- (c) how the *firm* plans to provide in the long term for *annuity* payments on any *with-profits* and non-profits *policies* under which benefits have vested;
  - (d) how the *firm* will address future adverse circumstances in relation to these (e.g. increased annuitant longevity); and
  - (e) details of the *firm's* plans for distributing the embedded value in any major *subsidiaries* held in or by the closed *with-profits fund*;
- (12) an explanation of any material differences between the *firm's* run-off plan and relevant parts of its *PPFM*, together with details of any changes that will be made to the *PPFM* as a consequence of closure (The *firm* should provide the *FSA* with a copy of the revised sections of its *PPFM* when it submits its run-off plan.);
- (13) an explanation of whether the *firm* will be seeking to expand any other business following closure of the *with-profits fund*. (This explanation should include whether the *firm* will effect any new *with-profits policies* in a different *with-profits fund* and whether it will seek to expand its unit-linked or *non-profit insurance business*. It should also include an explanation of how such plans will impact on the closed *with-profits fund*. For example, will the *firm* offer *policyholders* in the closed *with-profits fund* the opportunity to switch into another *with-profits fund* or into unit-linked business?)

#### Financial projections

2.15.8 G A *firm's* run-off plan should include:

- (1) a forecast summary revenue account for the *with-profits fund*, in the form of *SUP* App 2.15.9G Table 1;
- (2) a forecast summary balance sheet and statement of solvency for the *with-profits fund*, which has been prepared in the form of *SUP* App 2.15.9G Table 2 and on a regulatory basis; and
- (3) a forecast summary balance sheet and statement of solvency for the entire *firm*, which has been prepared in the form of *SUP* App 2.15.9G Table 3 and on a regulatory basis;

in each case, for at least a three year period, beginning on the date of closure; and

- (4) a description of the assumptions underlying the forecasts at (1) to (3) and the reasons for adopting those assumptions.

2.15.9 G These tables belong to *SUP* App 2.15.8G

Table 1 – forecast summary revenue account for the relevant with-profits fund	
(1)	<i>Premiums and claims</i> (gross and net of <i>reinsurance</i> ) analysed by major <i>class</i> of <i>insurance business</i>
(2)	Investment return
(3)	Expenses
(4)	Other charges and income
(5)	Taxation
(6)	Increase (decrease) in fund in financial year
(7)	Fund brought forward
(8)	Fund carried forward

Table 2 – forecast summary balance sheet and statement of solvency for the relevant with-profits fund	
	Assets analysed by type (excluding <i>implicit items</i> ):
(1)	Equities
(2)	Land and buildings
(3)	Fixed interest investments
(4)	All other assets
(5)	Total assets (excluding <i>implicit items</i> )
(6)	<i>Policyholder</i> liabilities
(7)	Other liabilities
(8)	Total liabilities
(9)	Excess/(deficiency) of assets over liabilities before <i>implicit items</i>
(10)	<i>Implicit items</i> allocated to the <i>with-profits fund</i>
(11)	<i>Long-term insurance capital requirement</i> for the <i>with-profits fund</i>
(12)	<i>Resilience capital requirement</i> for the <i>with-profits fund</i>
(13)	<i>With-profits insurance capital component</i> (for <i>realistic basis life firms</i> only)

(14)	Net excess/(deficiency) of assets in the <i>with-profits fund</i>
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Table 3 – forecast summary balance sheet and statement of solvency for the firm		
L1	Surplus <i>long-term insurance assets, with-profit fund(s)</i>	
L2	Surplus <i>long-term insurance assets, non-profit fund(s)</i>	
L3	Total <i>long-term insurance assets</i>	L1+L2
L4	Total <i>long-term insurance liabilities (excluding resilience capital requirement)</i>	
L5	Total <i>long-term insurance fund surplus</i>	L3-L4
L6	Shareholder fund assets	
L7	<i>Implicit items</i>	
L8	<i>Long-term insurance capital requirement</i>	
L9	Excess of regulatory assets over <i>long-term insurance capital requirement</i>	L5+L6+L7-L8
L10	<i>With-profits insurance capital component</i>	For realistic basis life firms only.
L11	<i>Resilience capital requirement</i>	
L12	Net excess assets	L9-L10-L11
L13	FTSE level at which the <i>long-term insurance capital requirement would be breached</i>	

- 2.15.10 G If a *firm* is a *realistic basis life firm*, its run-off plan should include:
- (1) a realistic balance sheet and statement of solvency position in the form of *SUP App 2.15.9G Table 2*, if the financial position of the relevant *with-profits fund* would, when stated in that form, be materially different from the *firm's* most recent realistic solvency submission for that fund; or
  - (2) a statement that the *firm* is satisfied that the closure of the *with-profits fund* will not materially affect the realistic solvency position of that fund, as reflected in the *firm's* most recent realistic solvency submission for that fund.
- 2.15.11 G A *firm's* run-off plan should include:
- (1) a revised individual capital assessment for the *firm* (see *PRU 2.3*), which reflects the impact of the closure of the relevant *with-profits fund*; or
  - (2) a statement that the *firm* is satisfied that the closure will not materially affect the *firm's* most recent assessment.
- 2.15.12 G A *firm's* run-off plan should include details of any:
- (1) *intra-group* balances held by the *with-profits fund*;
  - (2) *group company* investments held by the *with-profits fund*; and
  - (3) guarantees given by the *firm*;
- which, in each case, have a value in excess of 5% of the *firm's* gross technical provisions.
- 2.15.13 G A *firm's* run-off plan should include any other information that the *firm* considers relevant to the run-off of the closed *with-profits fund*.
- 2.15.14 G The *FSA* may request additional information and explanations from the *firm*. (See section 165 (Authority's power to require information) of the *Act*.)
- 2.15.15 G Significant changes to, or departures from, a *firm's* run-off plan are likely to trigger one or more of the *firm's* obligations to notify the *FSA*. (See, for example, *Principle 11* (Relations with regulators). The guidance in *SUP 15.3* (General notification requirements) may also be relevant.)