PwC with-profits survey 2023

August 2023

Use of report

The report should be read in its entirety, reading individual sections in isolation may result in misinterpretation. The report contains information obtained from survey participants. We have not sought to establish the reliability of the information or otherwise verify the information so provided. Accordingly no representation or warranty of any kind (whether express or implied) is given by PwC to any person as to the accuracy or completeness of the report.

In some areas, not all 14 participants responded to the questions asked. This will have been for various reasons, e.g. where data was unavailable in the format requested. In these instances, the total number of responses is less than 14, however we have ensured that results disclosed in this report are always from a sufficiently credible set of responses. Where we have received an insufficient number of responses to meet this objective, we have refrained from disclosing quantitative results.

The Financial Reporting Council ('FRC') requires actuaries to comply with Technical Actuarial Standards ('TASs') for various types of actuarial work. We also believe that it is normally appropriate to apply the requirements of the TASs to other work conducted by actuaries. Given the nature of the work, however, we have not attempted to follow the requirements of the TASs on this assignment. You will need to consider the impact of this limitation on your interpretation of our work and results.

Participants

We would like to express our thanks to the following firms which took part in our 2023 survey

1. **Aegon UK**
2. **Aviva Plc**
3. **Countrywide Assured Plc**
4. **Forester Life Limited**
5. **Liverpool Victoria Financial Services Limited**
6. **Lloyds Banking Group Plc**
7. **M&G Prudential**
8. **The National Farmers' Union Mutual Insurance Society Limited**
9. **The Royal London Mutual Insurance Society Limited**
10. **Scottish Friendly Assurance Society Limited**
11. **Sun Life Assurance Company of Canada (U.K.) Limited**
12. **Utmost Life and Pensions Limited**
13. **Wesleyan Assurance Society**
14. **Zurich Assurance Limited**

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Introduction

Section one

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1. Introduction

1.1 Summary

Welcome to the 2023 PwC with-profits survey - we are delighted to be able to share with you our findings. Our previous 2021 survey focused on hot topics including macroeconomic factors (such as negative interest rates), investment strategy, mergers and sunset clauses.

We last performed our survey in 2021, and where relevant we have made observations on key changes.

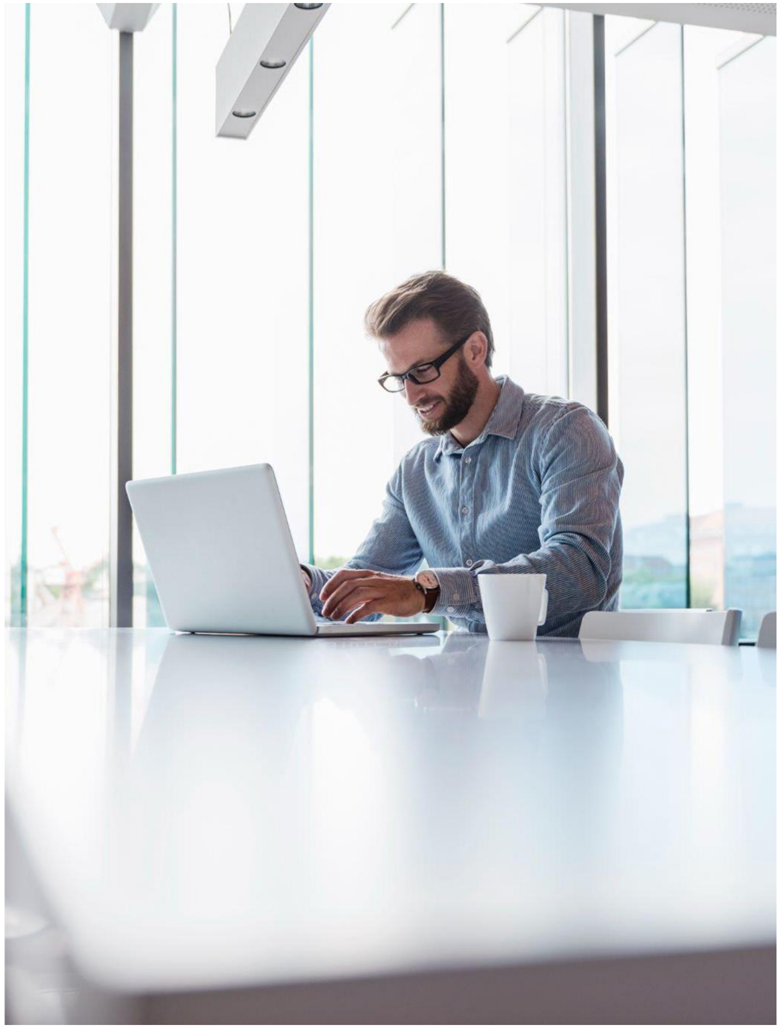
This year we have covered the following range of topics:

- Hot topics, including macroeconomic factors relating to the high interest and high inflation rate environment and investment strategy considerations.
- Consumer duty and fair value.
- Reserving for goneaways.
- Payouts and charges.

While the survey has been completed primarily by those responsible for day to day management of with-profits business, the output from the survey is relevant for everyone focused on the strategy and value of running with-profits business.

A common area of focus for with-profits business is the timing and approach for **winding up a with-profits fund** e.g. triggering of a sunset clause. When compared to the 2021 survey we have observed a reduction in the number of funds expected to merge and the timescales for winding up a with-profits fund are now longer.

We set out other key themes emerging from this year's survey on the following page.



1. Introduction

1.1 Summary (continued)

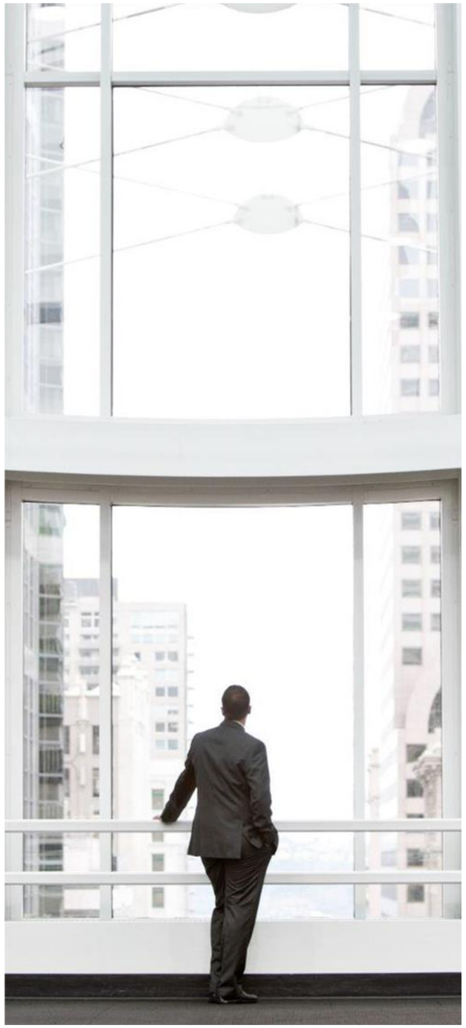
Reviewing and changing investment strategy continues to be the most common area of focus for with-profits business with the impact from the market environment being a key focus for funds, specifically in relation to the high interest rate and high inflation environment. As part of our findings around investment strategy, we have observed that:

- There has been a **move out of government bonds,** and **towards property and equity investments.** This is likely to be due to an appetite to protect real returns in times of high inflation.
- Where funds are invested in equities, there is a **wide range in the proportion invested in UK equities,** suggesting that some funds may benefit from further diversification.
- It is common for funds to use **hedging** as a tool in managing the risks within their fund(s). Whilst interest rate hedging is still commonly being used for GAOs, there has been a **reduction in interest rate hedging** when compared to the 2021 survey results - indicating that firms were hedging against lower interest rates where guarantees are more onerous. Further, the extent of **currency risk hedging has increased significantly** since the 2021 survey, which may be driven by an increase in exposure to overseas investments.

The FCA's Consumer Duty requires firms to take reasonable steps to achieve good outcomes for consumers. The requirements came into force on 31 July 2023 for new and existing products. Firms must comply with the requirements for closed books by 31 July 2024. It is clear this has been a focus for with-profits management and will continue to be as the 2024 deadline approaches for closed books. In fact, it seems the closed book deadline is potentially more impactful for many firms with with-profits funds than the deadline which has just passed.

As part of our findings, we have observed that:

- Firms are at varying stages of maturity with their approach to consumer duty. This is most likely because of the mix of open and closed products in with-profits books driving the timelines firms are working towards.
- There are a range of approaches across firms. This is to be expected but firms should consider whether there are aspects of their approach that need enhancing, taking into account FCA expectations and the market directions. For example, with respect to the metrics being considered for fair value or the approach to communications testing.
- With-profits does not operate in a vacuum to the rest of the business when it comes to consumer duty. It is right that a firm wide approach should be taken. However, where there are with-profits specific challenges or potential drivers of harm these need to be factored in. Some firms are considering this within fair value assessments and should consider whether there are also specific challenges with customer understanding or support.



1. Introduction

1.1 Summary (continued)

Finally, we have again sought to compare charges, expenses and payouts. The former being particularly relevant given that cost management continues to be a key focus for with-profits business, with streamlining existing processes and reducing costs of managing with-profits business being common areas of focus for with-profits business. Our key observations from this are:

- We have generally observed that charges and expenses have decreased, both on a monetary and percentage measure. The key exception being for UWP bonds where the average monetary charge has increased significantly.

- **A wide spread of both expenses and charges**, which shows that as per our 2021 survey that expenses/charges are on average larger for UWP products than CWP, both in monetary and percentage terms.

- We have not observed any patterns in the change in average payouts since 2021, albeit it should be noted that the data supporting this becomes more volatile over time as policies run off.

The issue of **goneaways** continues to be an area of focus for with-profits funds, with some firms making an allowance for goneaway policies who are not expected to claim from both a reserving and capital perspective. Of the funds that make an adjustment for this in Best Estimate Liabilities, the most common approach is to apply an experience analysis type methodology on expected claims, though making an adjustment based on a range of factors (age, policy type, premium status, maturity date) is also used. Interestingly we noted very few companies making an allowance for goneaway policies in capital calculations, suggesting this is not a material factor in capital management.

Having analysed the results of the survey, the top three questions we have are:

1. What is your approach for keeping your investment strategy relevant for your fund(s) given the macroeconomic environment, and in light of changing industry focus?

2. When implementing Consumer Duty what are your specific considerations for with-profits business e.g. customer understanding of with-profits products?

3. How do your measure the materiality of your goneaway policies, both now and how do you expect this to change over time?

Our thanks go to all 14 of the participants for kindly sharing their time and insights to help produce this survey.

In the coming months we are looking forward to hearing your views on other topics that would be useful to include in our next survey and to discuss how we can support your business.

We hope you find the report useful - our team looks forward to engaging in discussions with you about the themes emerging.

1. Introduction

1.1 Summary (continued)

If you have any questions regarding this survey please contact

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1. Introduction

1.2 Composition of with-profits funds surveyed

This survey covers 14 participants, across 43 funds and representing a total of c.£180bn Solvency II best estimate liabilities of UK with-profits funds - 7 funds are open to new business, of which 27 of the remaining 34 allow increments on existing policies.

This survey provides a high level of coverage across comparable UK with-profits funds, particularly closed funds. We estimate this covers c.80%, in monetary terms of with-profits funds in the UK market.

The with-profits funds that are not included within this survey include Phoenix funds excluding SLOC, and smaller funds specialising in providing Holloway-style income protection policies, where with-profits management considerations are likely to differ to the funds covered here.

Throughout this report, where we have made comparisons to prior surveys, we have considered the same set of participants across both surveys.

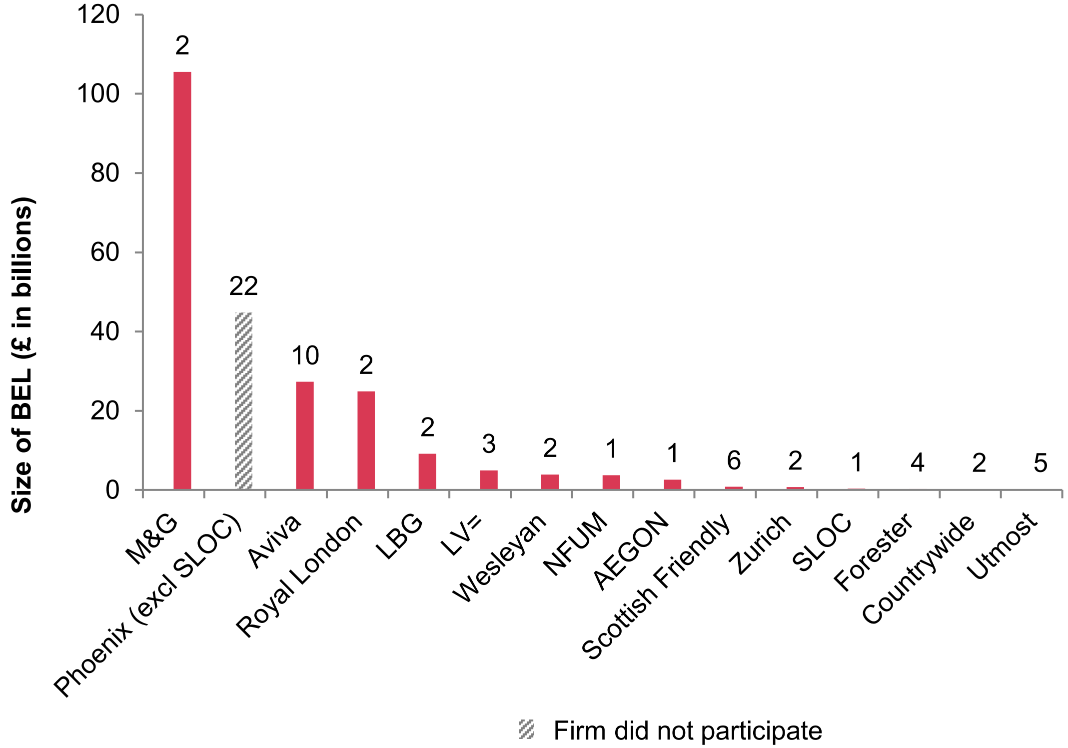
Throughout the survey, any reference to a “with-profits fund” is a reference to a ring-fenced fund (‘RFF’) as defined by Solvency II and all financial information has been captured as at 31 December 2022.

For the graphs within the survey we include a reference to the underlying question survey to help participants cross reference to their response.

Participants are required to publish with-profits BEL as part of their Solvency II disclosures. Figure 1.1 shows the distribution of BEL by firm, as taken from participants’ Solvency Financial Condition Report (‘SFCRs’).

In addition we show the number of with-profits funds each firm has (as denoted above the bar graphs).

1.1 – Total with-profits best estimate liabilities (£ in billions)



1. Introduction

1.2 Composition of with-profits funds surveyed (continued)

The profile of total with-profits BEL has remained largely unchanged from our 2021 survey.

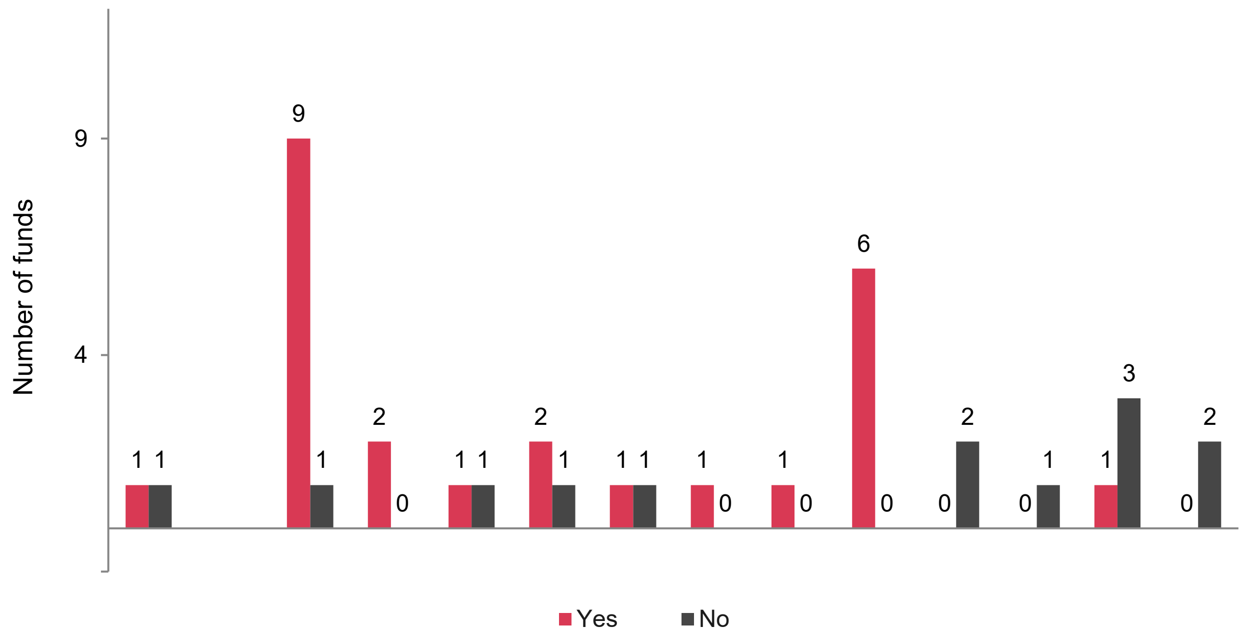
Most participants have one or two with-profits funds, with three participants having 3 to 5 funds, and two having 6 to 10 funds. On average, participants have a fewer number of with-profits funds when compared to the responses from the 2021 survey. This is consistent with the recent fund merger activity We have observed in the market, including:

The merging of Aviva's FLC Old and New With Profits Sub-Funds, which was put into effect from 1 July 2022, and **1**

The consolidation of a number of Royal London's closed Sub-Funds into the Royal London Open Fund during 2021 and 2022. **2**

Figure 1.2 shows roughly two thirds of with-profits funds also contain a non-trivial (i.e. more than 1%) proportion of non-profit business. This position is unchanged from our 2021 survey, demonstrating firms have generally not taken action during the previous two years to remove non-profit business from their with-profits funds. This could suggest that non-profit business is not a significant challenge to the management of the funds during run-off and/or a fair distribution, though we are aware of firms seeking to transfer (either directly or through reinsurance) longer duration business such as annuities.

1.2 - Does the with-profits fund contain a non-trivial (>1% gross liabilities) amount of non-profit business?



1. Introduction

1.2 Composition of with-profits funds surveyed (continued)

We asked participants about the future outlook of their funds. Figure 1.3 indicates that:

1. Over the medium to long term, approximately three quarters of the funds will convert to non-profit. This includes conversion to non-profit and then a plan to move to another fund or organisation.

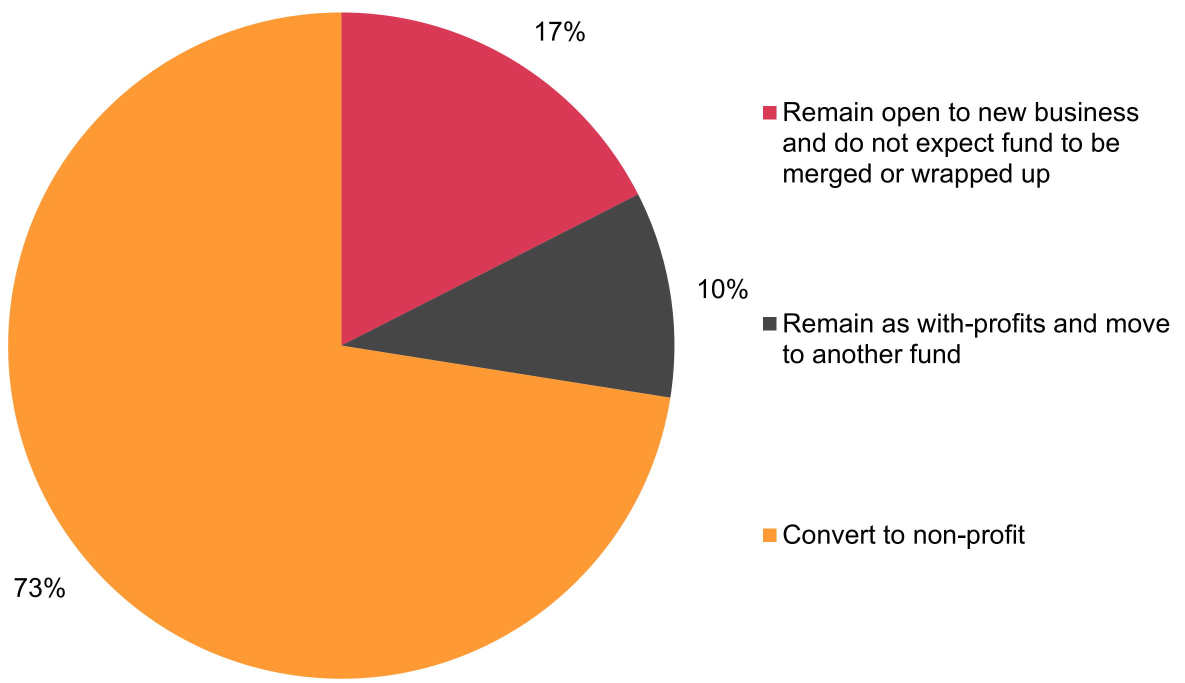
2. 10% will remain in the fund as with-profits business over the medium to long term before being moved to another fund.

3. 17% will remain unchanged over the long term.

The number of funds that plan to convert their with-profits business to non-profit business has increased when compared to the 2021 survey.

Further, the number of funds that are expected to merge has reduced when compared to the 2021 survey, where approximately half of participants indicated that they expected to merge, and half of those merging funds expected to convert to non-profit business.

1.3 - What is the best view of the future for this with-profits fund?

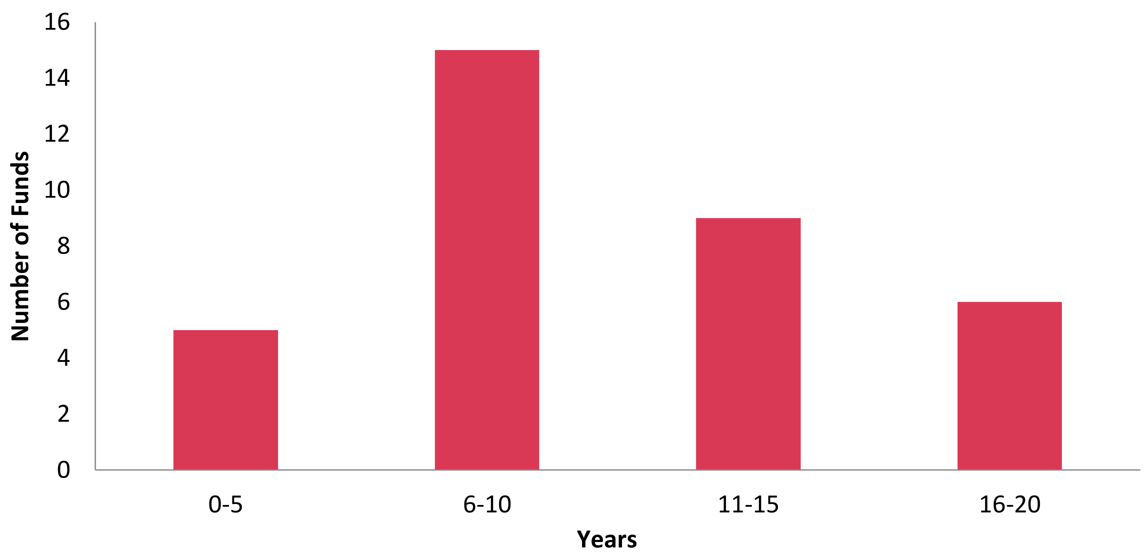


1. Introduction

1.2 Composition of with-profits funds surveyed (continued)

We asked participants the time frame over which they expect the funds to merge or be wrapped up. Figure 1.4 below shows that of the twenty eight funds for which we received responses, the majority of these are expected to change in structure over the next ten years, and the remaining are expected to change in structure between eleven to twenty years' time.

1.4 – Timescales for restructuring with-profits funds (years)



In comparison to the findings from our 2021 with-profits survey, we note that the timescales are now longer, suggesting that firms have now assessed that it would be more appropriate to change the structure of their funds at a later date.

There could be many reasons for this, including the consequence of the high interest rate environment which has reduced the pressure from onerous guarantees.

1.2 Composition of with-profits funds surveyed (continued)

We asked participants to provide their most recent national specific template NSR.02.01.01.01 relating to firms' with-profits liabilities and assets. This template requires firms to split with-profits best-estimate liabilities ('BEL') into those comprising the with-profits benefits reserve ('WPBR') and future policy-related liabilities ('FPRL').

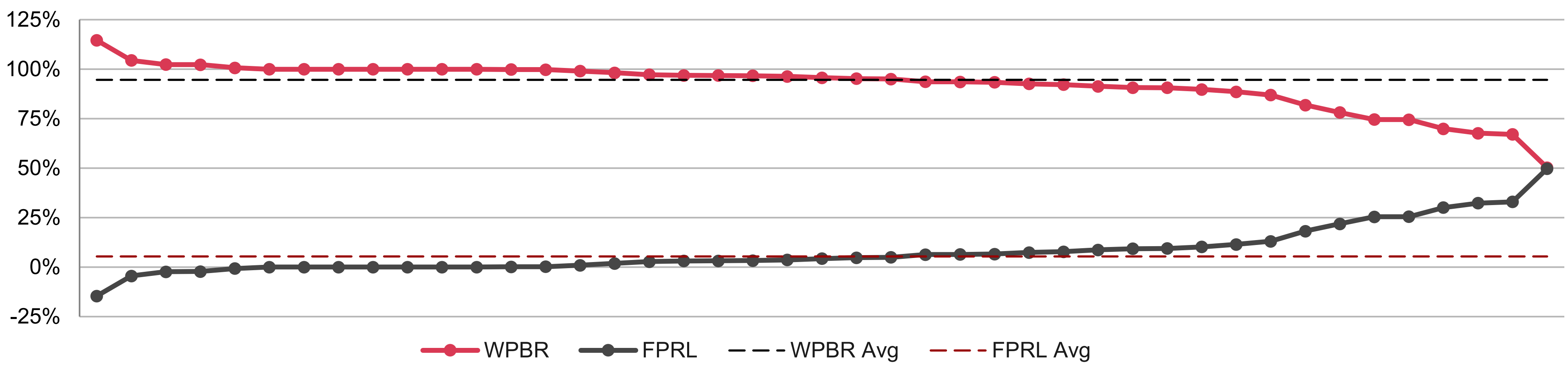
Funds with a higher proportion of FPRL denote those with larger proportions of guarantees that are heavily in the money. We have analysed the FPRL as a proportion of BEL by examining NSR.02.01.01.01 and compared our findings to what we observed as part of the 2021 survey.

Figure 1.5 below shows the results of our analysis.

- The weighted average FPRL as a % of BEL is 5%, which has reduced by c.10% since the 2021 survey.
- We also observe that the FPRL is substantially negative for one firm, and there are no cases where the FPRL exceeds the WPBR.
- This also supports the view that guarantee costs are lower relative to 2021.

The reduction in FPRL is likely to be attributable to an increase in interest rates leading to lower guarantees since the last survey two years ago.

1.5 - WPBR and FPRL as a proportion of BEL at fund level



1. Introduction

1.2 Composition of with-profits funds surveyed (continued)

Cost of smoothing

We have also included analysis of the cost of smoothing by fund using data from NSR.02.01.01.01.

Figure 1.6 shows the cost of smoothing as a proportion of the WPBR for each fund participating in this survey at both 31st December 2021; and 31st December 2022.

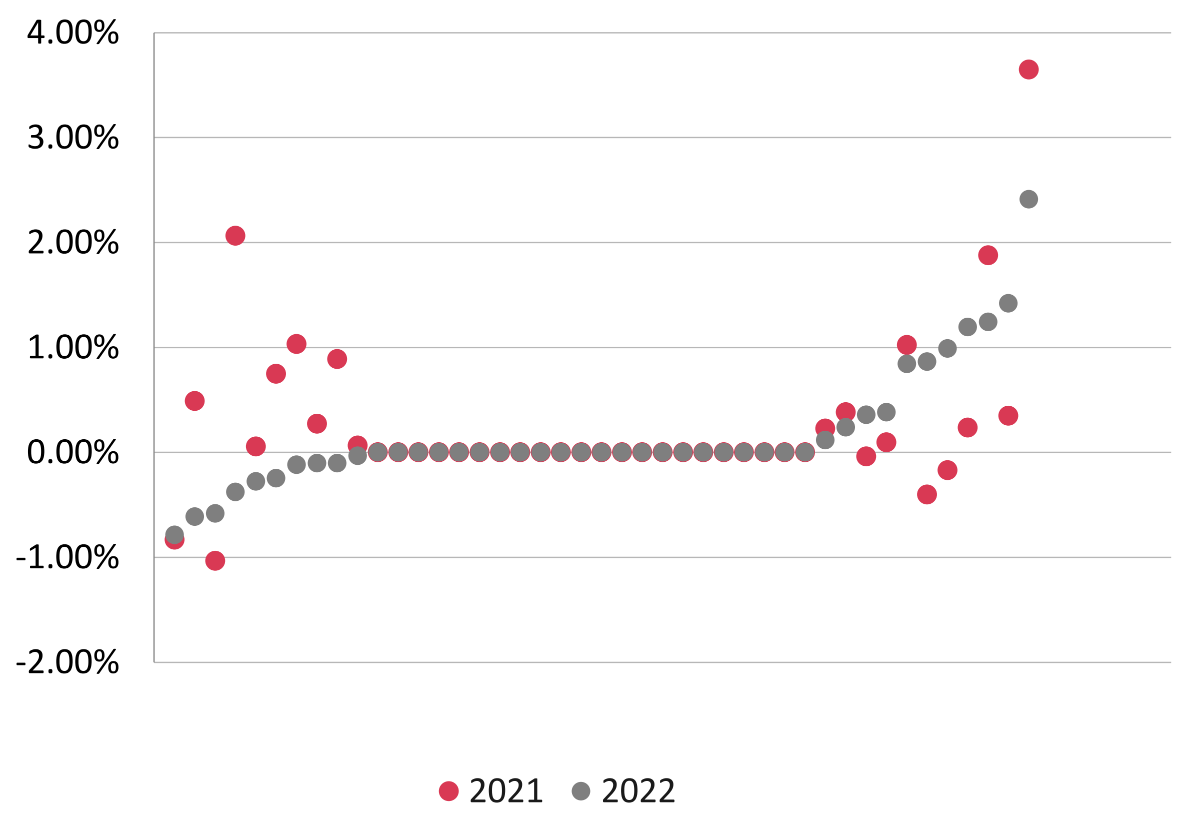
Whilst the median level of cost of smoothing remains at 0% of the WPBR in 2022, the weighted average for 2022 is 0.68%, compared to 0.65% for 2021.

This continues the trend we have observed in prior surveys where for the weighted average in 2020 was 0.26% and 2019 0.22%; noting the makeup of funds in these time periods are different due to fund mergers, sales and survey participants.

Regardless, this continues to suggest that the majority of with-profits funds expect to recycle both smoothing profits and losses directly back to policyholders.

Further, for funds where this proportion is higher, this suggests some of the losses will not be able to be directly passed back to policyholders. Figure 5.4 also illustrates that some funds are at different points in the smoothing cycle in 2022 when compared to 2021.

1.6 Cost of smoothing as a percentage of WPBR by fund



Hot topics

Section two

2

2. Hot topics

The current economic outlook is being defined by weak economic growth, rapid monetary tightening and moderating inflation. The rising cost of living continues to be a strain for many, with high interest rates further fuelling the crisis.

This will in turn impact on the management of with-profits funds with regards to investment strategy, investment performance and policyholder behaviour.

In this section we explore a number of topics, including:

- The effect of the high interest rate and high inflation environment
- Focus of the management of with-profits funds, asking firms about their top three areas.
- Investment Strategy of firms, covering asset holdings, UK equity holdings, approaches to fixed interest investments and hedging.

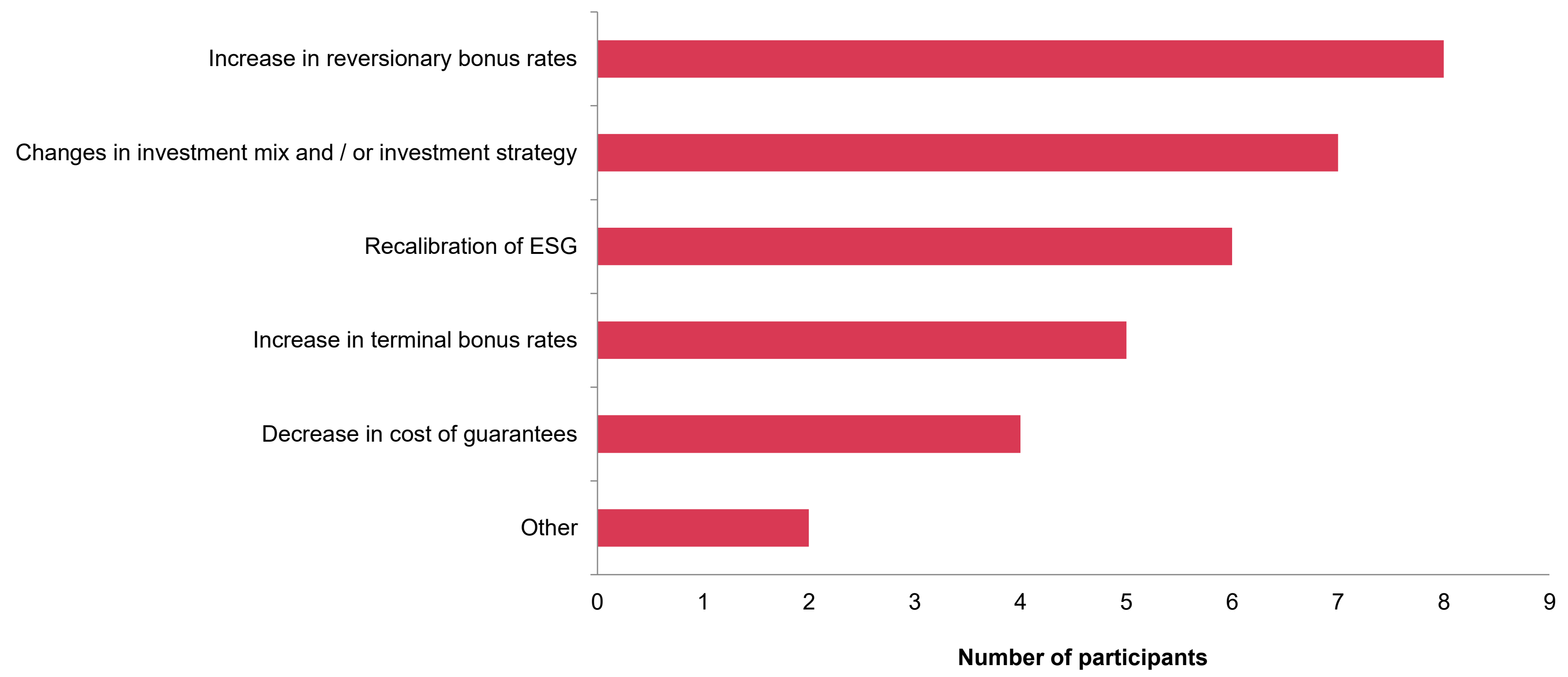
2. Hot topics

2.1 Effect of the high interest rate and high inflation environment

We asked participants to indicate the effects of the current high interest rate environment on their with-profits business.

Figure 2.1 below shows that half of the participants have already increased or plan to increase reversionary bonus rates in light of higher growth and investment returns in the medium to long term. Some of the remaining participants noted that they have not made any changes to reversionary bonus rates, but they will continue to be monitored. This suggests that there is some flexibility in terminal bonus headroom, and firms may instead choose to use this flexibility rather than immediately changing the reversionary bonus rates.

2.1 - Effect(s) of the current high interest rate environment on your with-profits business (A1)



2. Hot topics

2.1 Effect of the high interest rate and high inflation environment (continued)

The responses were more mixed in respect of terminal bonus rates, with four participants increasing or planning to increase terminal bonus rates, and three participants reducing terminal bonus rates due to falls in fixed interest asset valuations. Our observations are likely to be driven by two competing priorities:

- With higher interest rates, we are seeing greater investment returns and a fall in guarantee costs. This gives scope to increase reversionary bonus rates as guarantee costs are at lower levels than in previous years.
- However, higher interest rates will also cause a fall in fixed income asset values which may be backing asset shares. These fixed income assets may be used to determine terminal bonuses and therefore the total pay-outs on policies.

There may also be other factors such as differences in policy durations which are driving the decisions around bonus rates and some firms taking different views on the associated investment and tontine risks.

Related to the above, half of the participants have indicated changes in their investment mix and/or investment strategy, with one participant having updated their strategic asset allocation to reflect the higher interest rate environment.

Six participants have recalibrated their Economic Scenario Generator (‘ESG’), though three of these respondents noted that this was part of the regular recalibration cycle as opposed to being driven by interest rates.

Other comments noted in relation to effects on with-profits business relate to changes to the level of interest rate hedge and distribution of the estate.

Four participants noted that they observed a decrease in the cost of guarantees (‘CoG’), with two participants noting that this was due to lower values for guaranteed annuity options (‘GAOs’).

This is in line with our expectations, as typically in a high interest rate environment, GAOs are expected to become less attractive as annuity rates available in the open market become more attractive. Over the past couple of years, annuity rates have increased significantly, some by more than 50%.

For example, for a single life aged 60 with a £100k annuity and with level income would receive £4,308p.a. in 2021 and would now receive £6,548p.a. in 2023*.

This in turn will lead to a reduction in GAO take up rates and in the absolute cost of the guaranteed annuity business.

***Source: https://www.sharingpensions.co.uk/annuity-rates-chart-latest.htm**

2. Hot topics

2.1 Effect of the high interest rate and high inflation environment (continued)

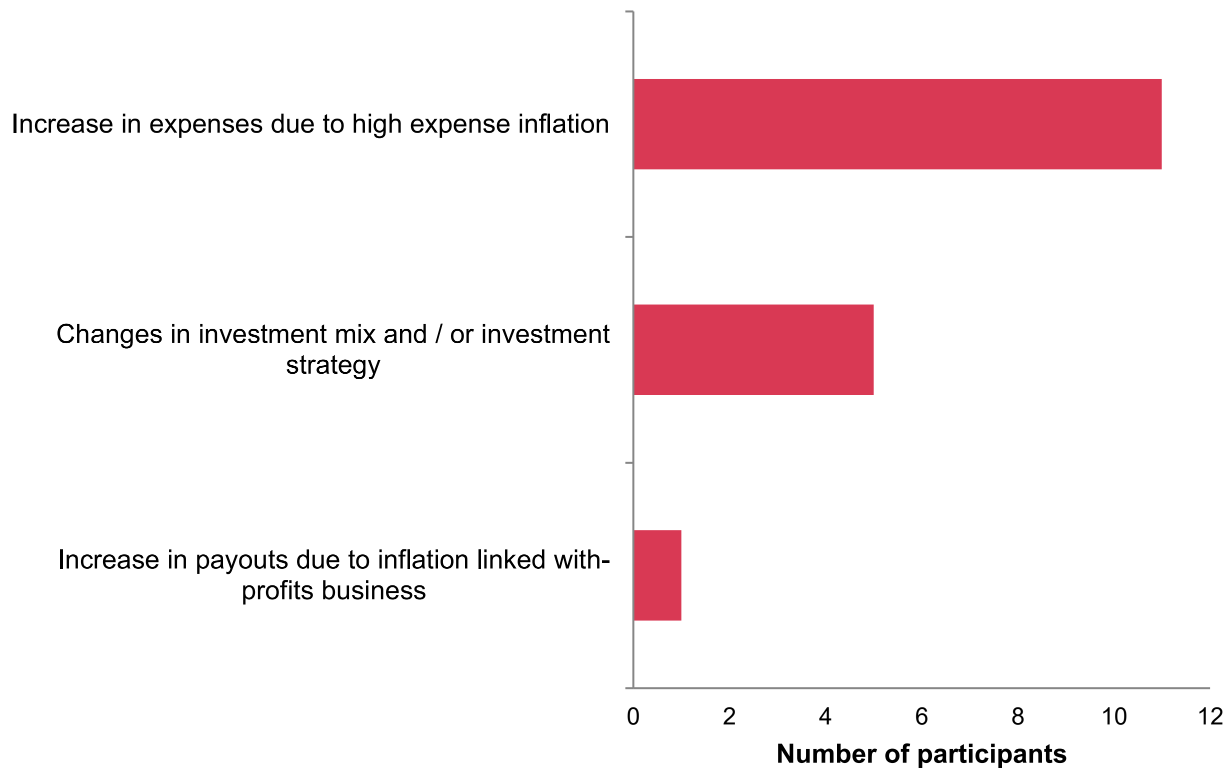
We also asked participants to indicate the effects of the current high inflation rate environment on their with-profits business. Figure 2.2 shows that the majority of participants have noted an increase in expenses due to high expense inflation. This has been largely driven by an increase in higher staff costs and higher contract costs where contractual cost increases are linked to inflation. Some participants have indicated that they have been able to absorb some of the expense increase due to existing service agreements in place, providing protection to the policyholders.

A number of participants indicated changes in investment mix and/or investment strategy in light of high inflation. Other participants indicated that a change in the asset mix was made to include real assets to counter the impact of inflation, while another noted that they are reconsidering holdings in cash in light of high inflation. However, we have observed that in general, holdings in liquid assets have reduced over time. This is likely to be driven by a desire to move to riskier, less liquid assets to protect funds against the eroding effects of high inflation.

Five participants noted that they had no or very little inflation linked with-profits business.

It was also noted that certain defined benefits that are inflation linked, such as GMP annuities, where the customer receives a greater benefit, may have reduced through a reduction in annuity purchase costs.

2.2 - Effect(s) of the current high inflation environment on your with-profits business (A2)



2. Hot topics

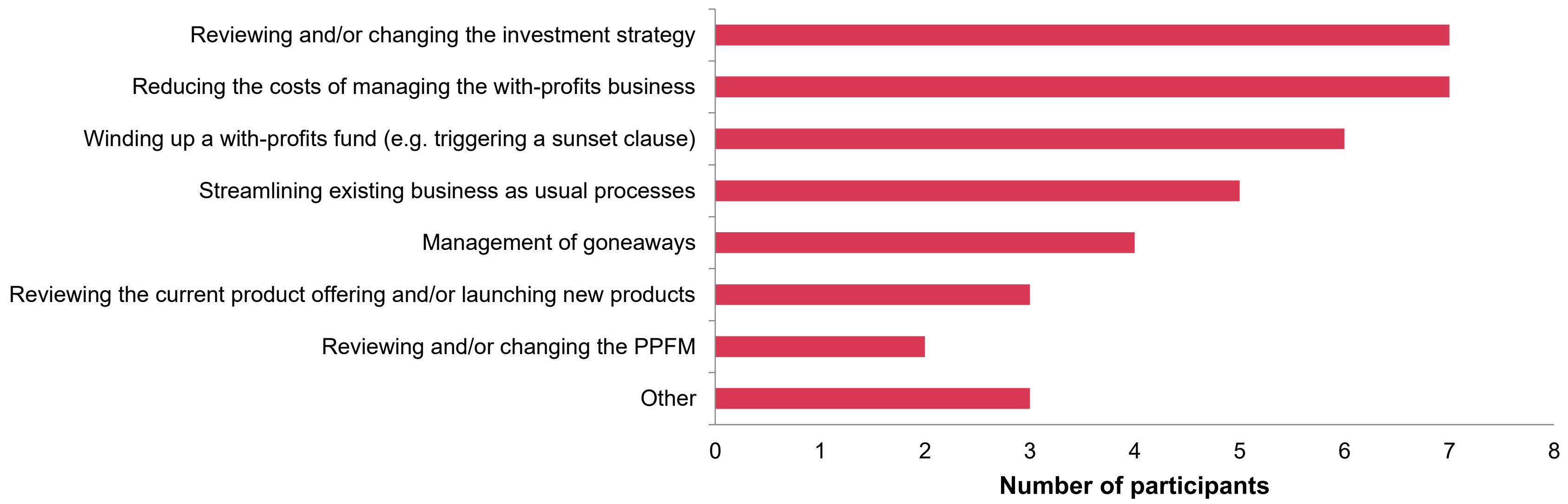
2.2 Current top three areas of focus of with-profits funds

The management of with-profits funds continues to present a number of challenges. These range from legacy issues such as the management of goneaways to the management of with-profits funds in run-off.

We asked participants to select their current top three areas of focus for their organisation's with-profits business. Figure 2.3 below indicates that the key areas of focus across the participants include reviewing and/or changing the investment strategy, reducing the costs of managing the with-profits business and streamlining of existing business as usual processes. These areas of focus are largely consistent with the results of our 2021 with-profits survey. We note that more participants are now focusing on the winding up of with-profits funds.

Other areas of focus include the management of goneaways and reviewing and/or changing the PPFM (including the run-off plan). The 'Other' category captures responses covering: consumer duty, updating pay-out methodology, modelling improvements and investment in new platforms.

2.3 - Top three areas of focus for your organisation's with-profits business (A4)



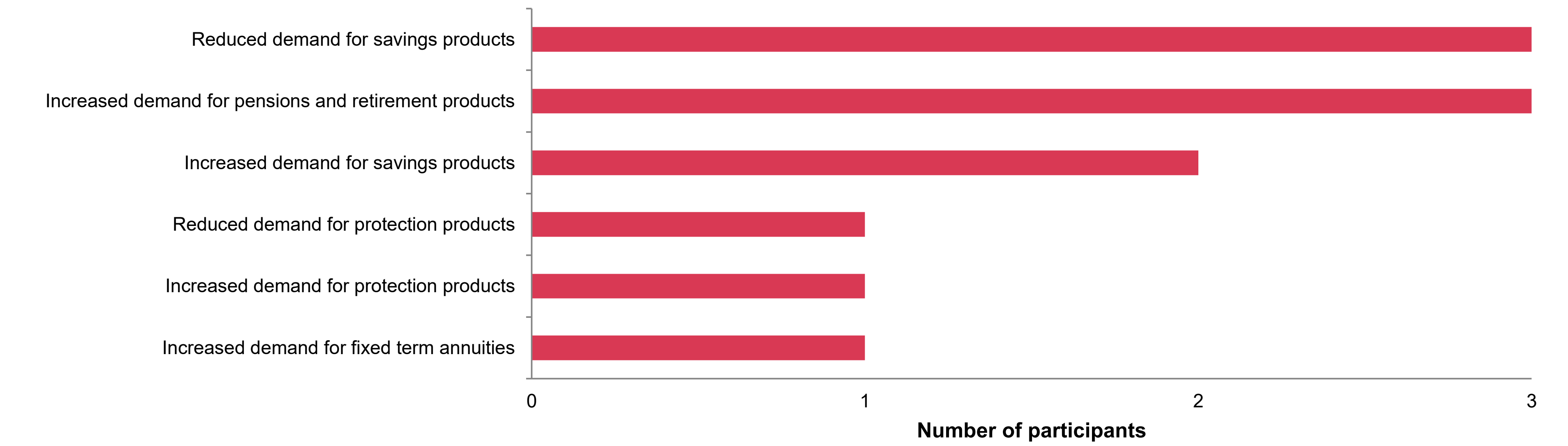
2. Hot topics

2.2 Current top three areas of focus of with-profits funds (continued)

The with-profits funds that continue to remain open to new business are looking to launch new products or amend current offerings. Figure 2.4 below shows that participants have seen increased demand for pensions and retirement products, but the levels of demand have been more mixed across the market for savings and protection products.

The increase in demand for pensions and retirement products is likely to be a result of the high inflation environment, where policyholders may look for products whose benefits will protect them against high inflation.

2.4 - Demand of with-profit business under current macroeconomic environment (A3)



2. Hot topics

2.3 Investments

One of the key topics that we covered in our 2021 with-profits survey was on investment strategy. We covered different aspects on this topic such as analysing the asset allocations, equity backing ratios ('EBR') and the investment management of funds.

Given that this continues to be an area of focus, we have considered some additional topics on investments as part of this year's survey.

Figure 2.5 shows the comparison of asset mix over time for the with-profits funds that are included in this survey - there has generally been a move out of government bonds, and increased investment in property and equity.

2.5 - Comparison of asset mix over time

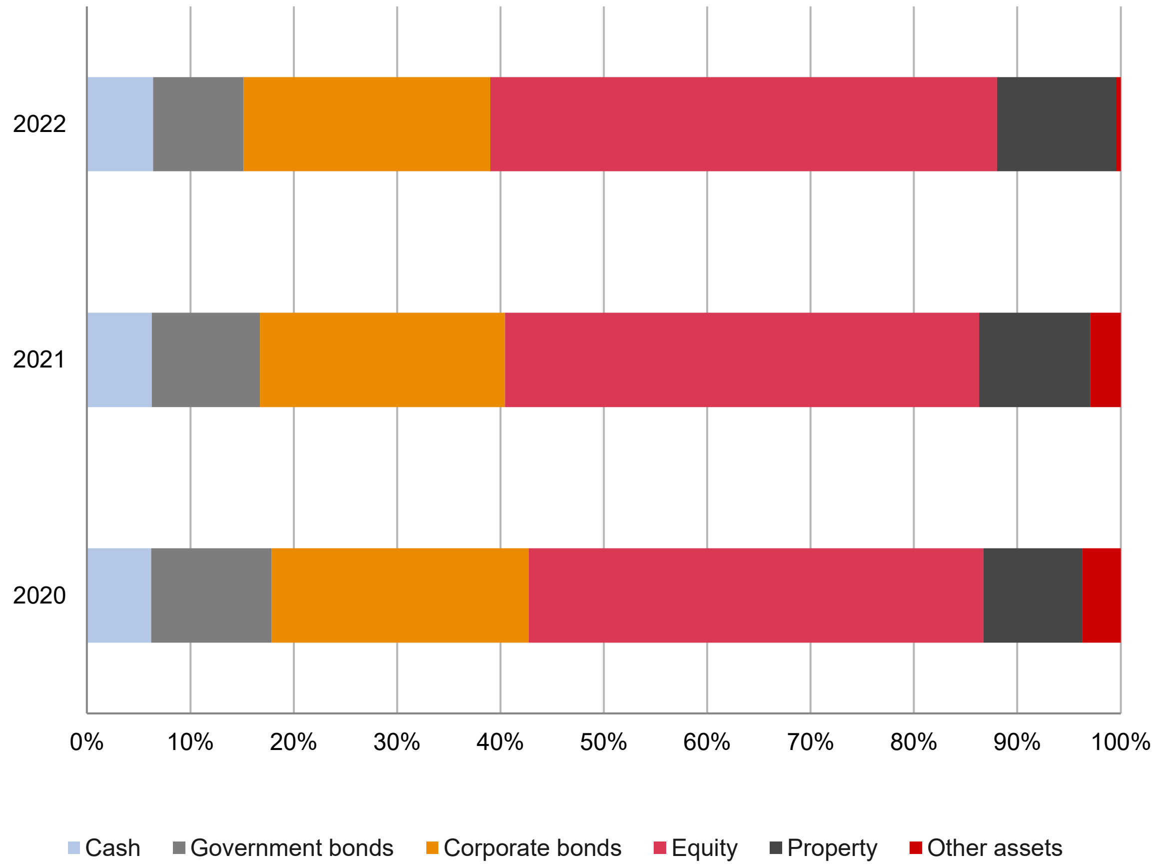
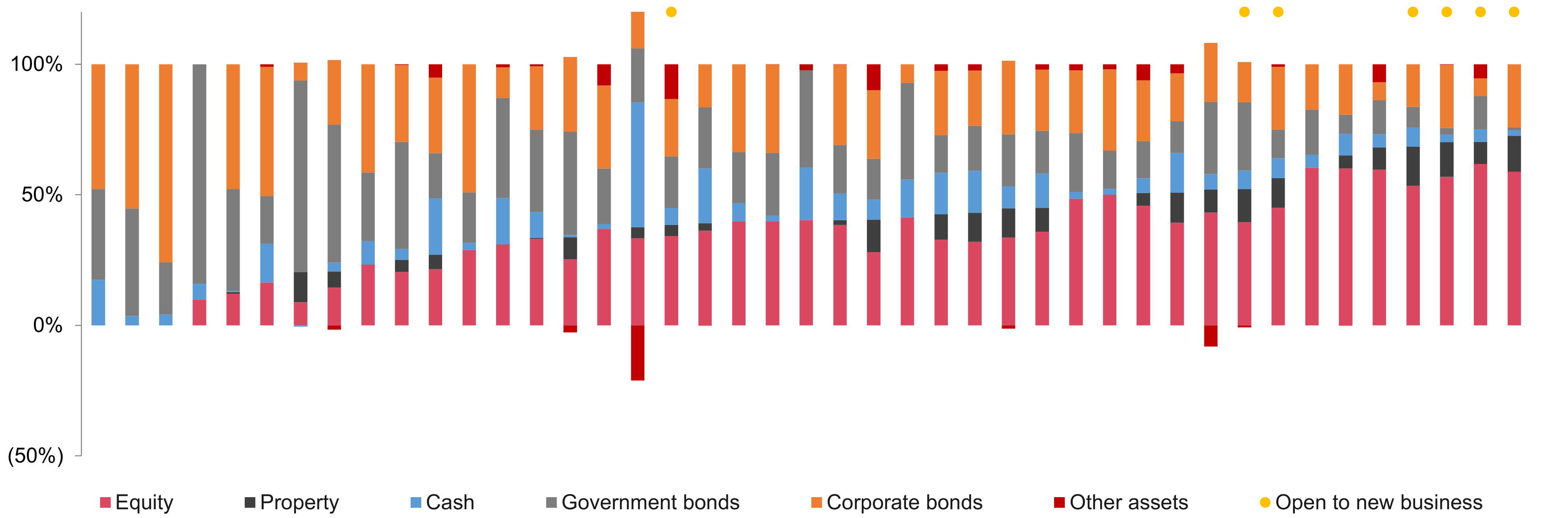


Figure 2.6 below shows a breakdown of the asset mix by fund as at December 2022 for each with-profits fund that is included in this survey. They are ordered by equity and property holdings.

The funds that have negative asset holdings are on account of the derivatives held. Overall, the combined asset mix sums up to 100%.

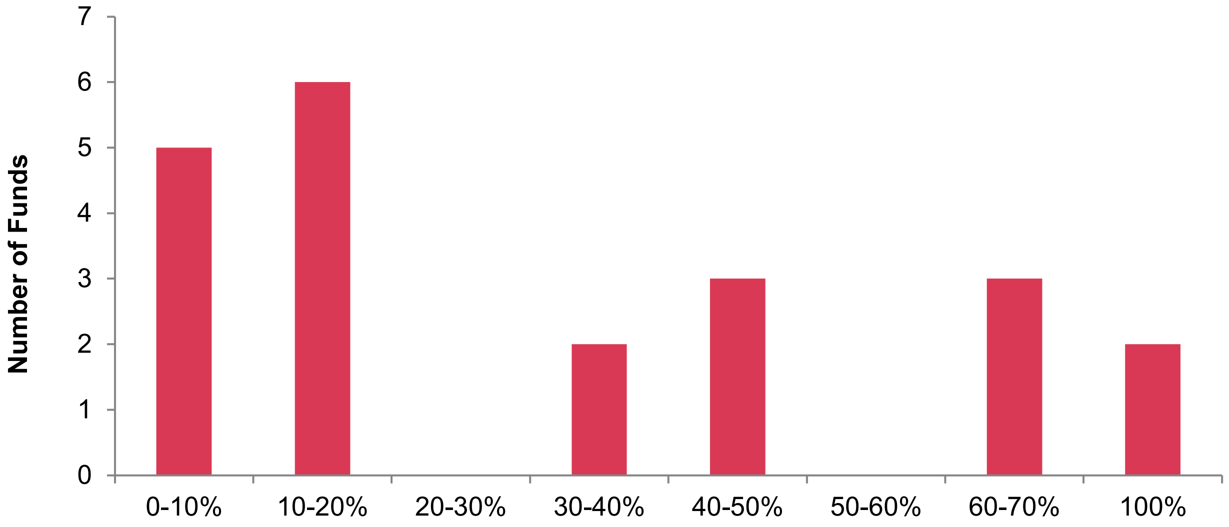
2.6 - Assets mix



Following discussions with participants of the 2021 with-profits survey, we noted that a number of funds were heavily invested in UK equities only, with little diversification away from UK equities. We therefore asked participants of this year's survey to provide, for each fund for which they were responding, the percentage of their equity investments that is invested in UK based equities. Figure 2.7 shows a distribution of these percentages across all participants and funds for which we received responses.

Over half of with-profits funds that are invested in equities hold a percentage of equity investments in UK based equities of between 0-20%. However, a number of funds have much larger percentages of their equity investments in UK based equities: five funds fall between 30-50%, a further three funds fall between 60-70% and a further two funds whose entire equity investments are invested in UK based equities.

2.7 - Percentage of your equity investment invested in UK based equities (A6)



We also asked participants to indicate the proportion and type of investments they hold in non-traditional fixed interest investments. Only a few funds invest in non-traditional fixed assets and where they do this accounts for up to 30% fixed interest holdings. We also saw that they invested across a range including: private equities, commercial mortgages, emerging market debt, infrastructure loans, venture capital and ship leases. No funds were invested in buy to let or equity release mortgages.

2. Hot topics

2.3 Investments (continued)

Hedging

Hedging risks in a with-profits fund is a key tool in managing long term returns to policyholders. Our experience suggested that the practice is quite varied.

Similarly to our 2021 with-profits survey, we asked participants how with-profits risks are managed, with the results of how risks are hedged across funds shown in figure 2.10 on the next page. We have also included the results from the 2021 with-profits survey for comparative purposes in figure 2.11. The x axis in the figures reflects the percentage of funds who responded.

The results from the 2023 survey responses indicate that hedging for interest rate risk is most significant, followed by hedging for currency and equity risks. We have also observed:

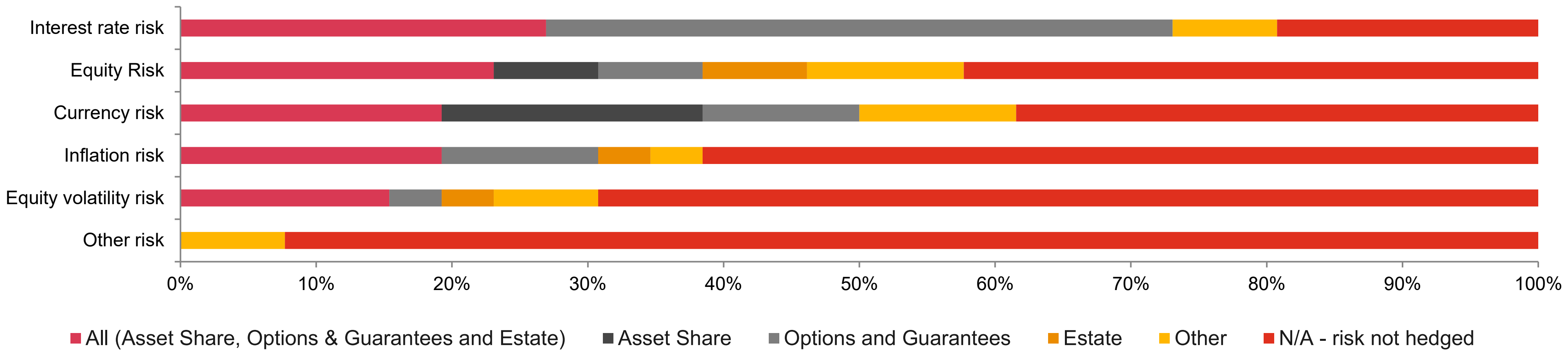
- That interest rate hedging has reduced slightly when compared to the 2021 survey results. This may indicate that firms were hedging against lower interest rates, as guarantees on products become more expensive in a low interest rate environment. Despite this, interest rate hedging is still commonly being used for GAOs.
- Equity risk hedging has reduced significantly since the 2021 survey, this is not overly surprising, and may reflect the fact that participants are trying to be more explicit about the risks they run and recognising that hedging equities reduces the upside risk.
- Interest rate risk is most commonly hedged across options and guarantees and the estate, whilst equity risk is most commonly hedged across either asset shares or the estate.
- Currency risk is hedged in just under half of funds (broadly consistent with 2021), primarily through asset shares, with inflation, equity volatility and other risks being less commonly hedged.

The responses included in the ‘Other’ category include longevity risk.

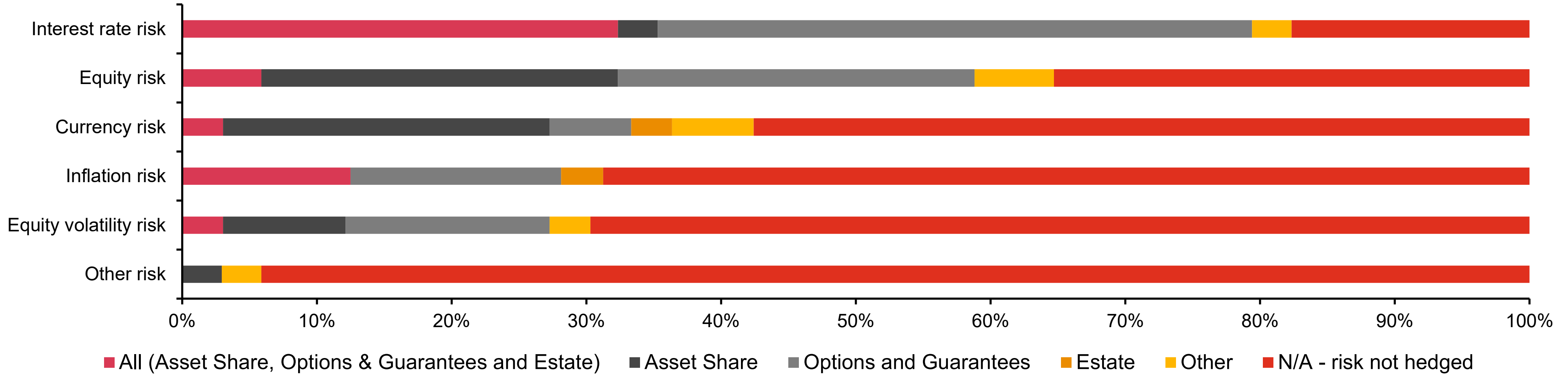
2. Hot topics

2.3 Investments (continued)

2.10 - How are each of the below risks used in risk management (A8)?

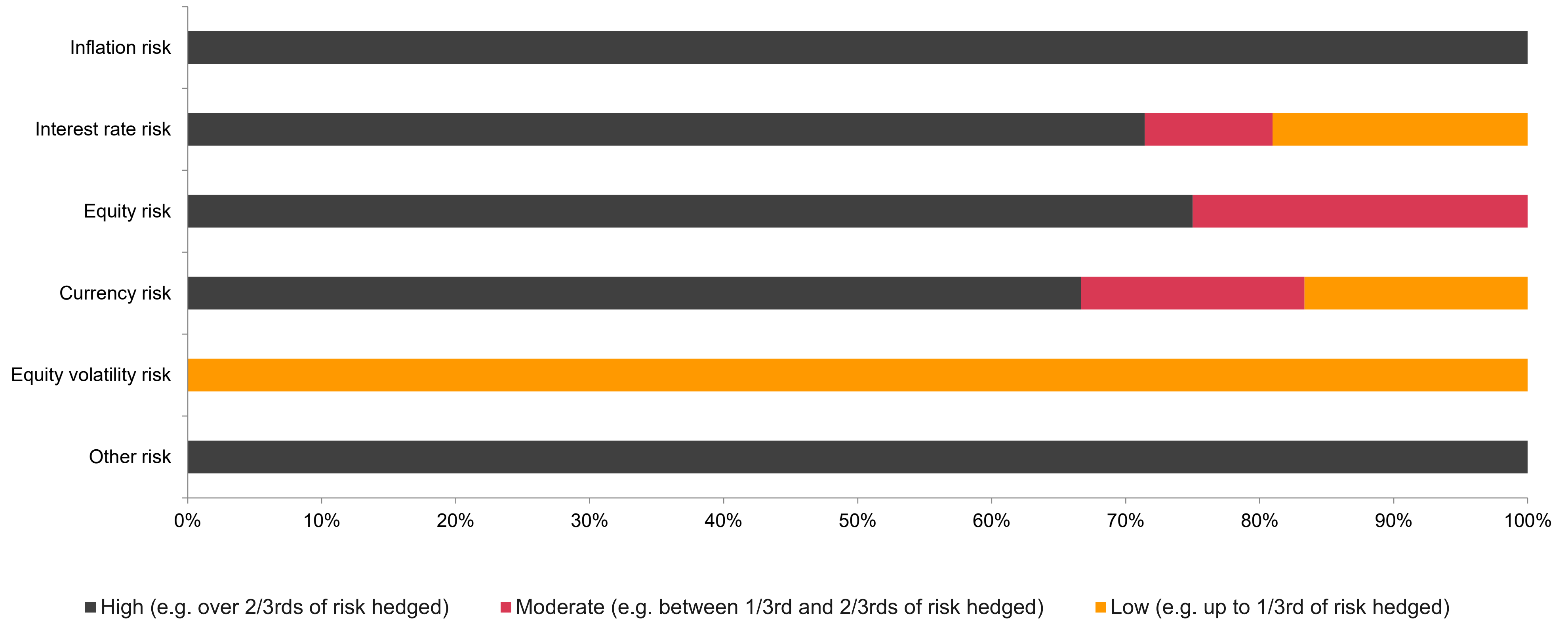


2.11 - How are each of the below risks used in risk management? (2021 survey results)



We asked participants the extent to which each of their risks is hedged, with responses shown in figure 2.12 below. This shows that, where hedging has been used, the extent of hedging in respect of inflation is most significant, followed by hedging for equity risks. The widest range of approaches exists for interest rate and currency risks, with some participants noting significant equity hedging, some noting lower amounts of equity hedging and others with no equity hedging.

2.12 - Extent of hedging, where it is used, by risk in with-profits funds (A8)



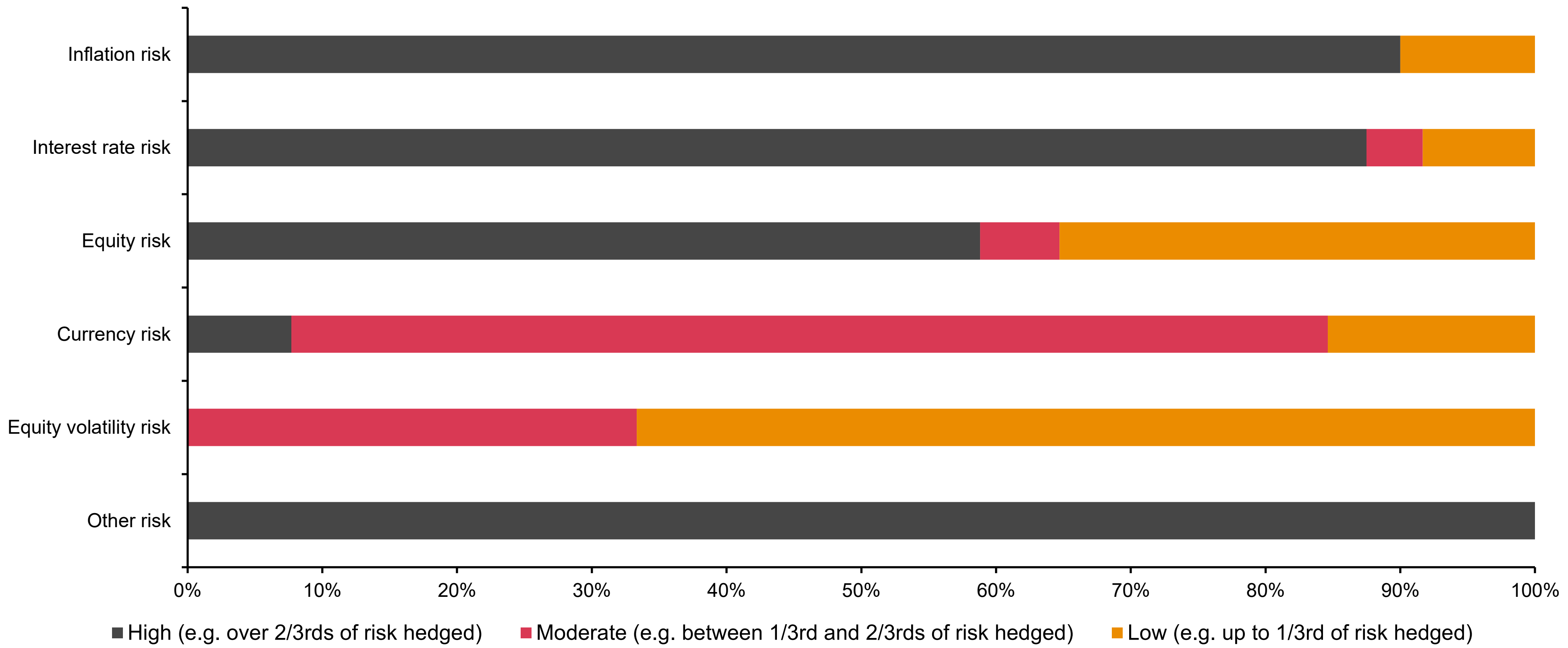
2. Hot topics

2.3 Investments (continued)

We have also included the results from the 2021 with-profits survey for comparative purposes in figure 2.13 below.

This shows that Where hedging has been used, the extent of currency risk hedging has increased significantly since the 2021 survey, which may be driven by an increase in exposure to overseas investments.

2.13 - Extent of hedging, where it is used, by risk in with-profits funds (2021 survey results)



Consumer Duty and Fair Value

Section three

3

3. Consumer Duty and Fair Value

The FCA's Consumer Duty represents what the regulator terms a "paradigm shift" in its expectations of firms. The Consumer Duty introduces a new Consumer Principle, which requires firms "to act to deliver good outcomes for retail customers". In recognition of the barriers many consumers face to pursuing their financial objectives, the FCA wants to see firms deliver a higher standard of customer care and protection, and to go further to equip consumers to make effective decisions in their interests. The FCA has recently conducted research to assess the preparedness of firms for the implementation of Consumer Duty: Consumer Duty: firm preparedness

As part of the new Consumer Duty Structure, a suite of rules and guidance setting more detailed expectations for firm conduct have been developed for four specific outcomes that define the key elements of the firm-consumer relationship. These are: products and services, price and value, consumer understanding and customer support.

Consumer duty is now in force for new and existing products or services (as of 31 July 2023). Firms need to comply by 31 July 2024 for closed book products or services. The rules do not apply retrospectively.

This section considers how firms are approaching Consumer Duty through a with-profits lens, with reference to the four specific outcomes.

3. Consumer Duty and Fair Value

3.1 Products and Services and Price and value

We asked participants a number of questions to explore how they assess fair value. This included the quantitative and qualitative factors they use to assess fair value.

All firms had some method in place to assess fair value, although some with closed books acknowledged they needed to look at this as part of their consumer duty implementation for 2024. However, within that there was no consistent approach to assessing fair value amongst firms.

The more consistent features were quantitative. Using investment performance, charges and bonus/surrender rates were fairly consistent metrics across firms. The update of GARs was also raised as a factor in the fair value assessment by a number of firms. Only around half of respondents said they currently used benchmarking as part of their fair value assessment.

There was more variety in qualitative metrics and those metrics which considered non-financial information. Complaints were considered by most firms and was the only real consistency in approach. Some firms considered qualitative customer feedback such as NPS (Net Promoter Scores - loyalty of customer), testing outputs and customer feedback scores. SLAs (Service Level Agreements) and service performance were also considered by some firms. Risk events and channels of service were considered by one firm. Another firm considered distribution channels.

It is not surprising that there are variations in approach and metrics across firms. Previous requirements to assess value for money have not specified the approach to take. Whilst the consumer duty guidance does set out the areas firms should consider it does not mandate metrics. However, consumer duty does not sit in a vacuum and firms should consider regulatory feedback in other, linked, areas and upcoming regulatory change when evolving their approach. For example:

- The FCA has, in the unit-linked space, been critical of a lack of benchmarking and requires IGCs to consider this in their assessment of value. Current TPR approaches to value for money in pensions also requires benchmarking (for small schemes) and the recent joint FCA/TPR/DWP consultation on value for money in pensions also proposed a mandatory benchmarking requirement. This could suggest that benchmarking should be an important feature of fair value assessments.

- The recent consultation also proposes a series of service and qualitative assessments. This suggests this should feature as part of assessments but also the consultation makes specific proposals on what should be considered. This includes things like communications testing outputs which do not appear to feature in many firms considerations of fair value at present.

- No firms stated that they considered the profit they make as part of their assessment. This is an area the FCA has, in some sectors, criticised. It is likely therefore to be prudent to consider how this feeds into fair value assessments.

3. Consumer Duty and Fair Value

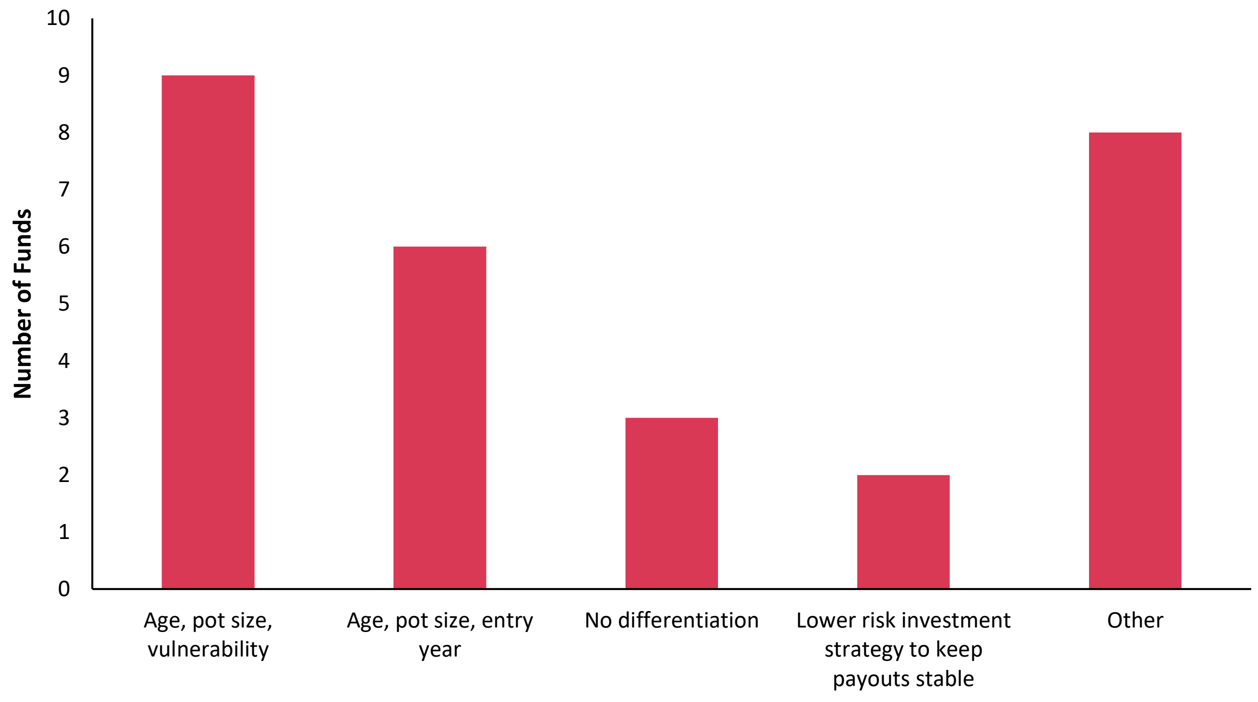
3.1 Products and Services and Price and value (continued)

We explored with firms whether they considered any sub-groups of policyholders within their fair value assessments.

- Age and pot size were considered by almost all firms.
- Vulnerable customers were also considered by around half of firms.
- Other groupings included duration to retirement/exit, target market and sales channel.

The responses from three firms suggested there were no groupings considered beyond the product or investment strategy.

3.1 - Groupings of policyholders when assessing fair value (B6)



3. Consumer Duty and Fair Value

3.1 Products and Services and Price and value (continued)

As the FCA is concerned that some groups of customers may not get a good outcome it is important to consider whether fair value needs to be considered specifically for some groups.

In particular, firms need to be able to demonstrate that vulnerable customers are getting as good an outcome as other customers (FG21/1). Firms will also recognise that charges can impact some groups differently, for example those with smaller pot sizes or nearing retirement may be impacted differently by certain charge structures. As such, it is important firms consider how to think about this within fair value assessments under consumer duty.

Most firms also did not consider the fair value separately for small blocks of business. Two firms considered these in groupings and one explained that actions may need expediting for these books. Given the impact expenses could have on fair value in smaller books of business or funds, it will be important that firms have some way to identify this through their assessments, even if not through a separate assessment for small books.

We also asked firms whether they took a different approach to assessing fair value for with-profits to other products. Generally firms did not. Where there was differentiation it was less in the methodology and more in the data points considered. For example, some firms considered GAR take-ups, the values of guarantees and bonus rates. These are more specific to with-profits products. This approach seems sensible as a completely different methodology could cause a disparity in assessment between unit-linked and with-profits products. We would, however, expect more difference with pure protection (with no investment element) products given they fall under the PROD 4 rules.

Linked to product management, we asked participants how Consumer Duty is impacting on their future plans for the run-off of the business. Although some firms were still assessing the impact, most of the respondents noted that there would be no impact, with further detail supporting this limited impact being:

- The discretionary decisions and the governance in the management of the fund (e.g. payouts).
- Prior activity on customer strategy initiatives and interactions.

There is a recognition that increased customer communications could impact on the engagement and therefore the run-off profile for with-profits funds.

3. Consumer Duty and Fair Value

3.2 Consumer understanding

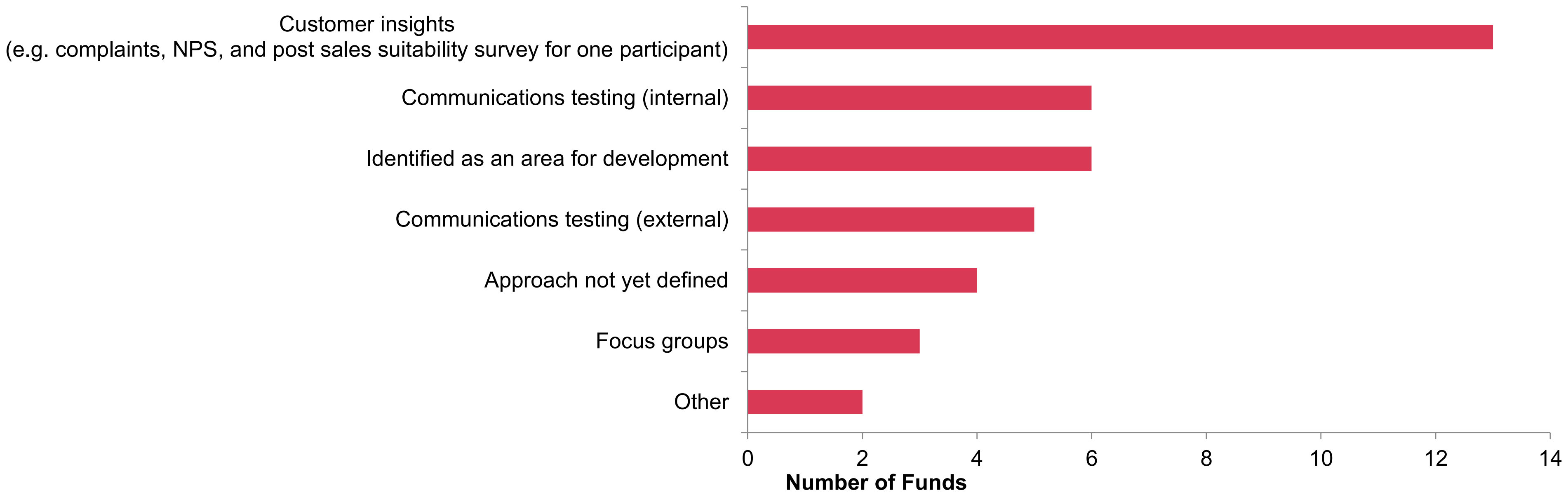
Given the complexity of the with-profits products, consumer understanding is an important area from a Consumer Duty perspective. We asked participants about how they assess customer understanding for with-profits products.

The responses indicate that the majority of respondents either hold customer focus groups or obtain customer insights from Net Promoter Scores ('NPS'), complaints or post sales suitability surveys. Approximately half of respondents carry out communications testing either internally or externally.

Other methods include data on the number of external hits to with-profits material on their public website, and comparison against internally developed communications guidance. Some participants have indicated that assessing customer understanding for with-profits products is an area for further development.

It is important that firms have methods of assessing and achieving consumer understanding. It is expected that some testing will be undertaken. MI will also play an important role.

3.2 - Testing of customer understanding (B10)



3. Consumer Duty and Fair Value

3.2 Consumer understanding (continued)

We also asked participants questions regarding their approach to customer testing. One firm has no plans to do any new testing. As would be expected no firms are testing all communications, and this is not required under consumer duty.

Firms generally appear to be testing all key communications and where possible testing master documents/templates to get greater coverage. The communications being tested include:

- Key new business communications;
- Annual statements; and
- Calls to action.

Some firms have tested all letters including change of address confirmations.

Testing key documents that drive customer outcomes is key when devising an approach to customer testing. It is also important to ensure that the focus is not just on sales documentation. The FCA has indicated that it expects the servicing part of customer journeys to get as much focus as sales focused documents. Firms should consider this in its approach to the closed book deadline.

3. Consumer Duty and Fair Value

3.2 Consumer understanding (continued)

We also asked participants on the type of testing they are undertaking for customer understanding. As seen in Figure 3.3, the majority of participants use customer focus groups, with digital testing tools and online testing directly with customers also being common practices.

In respect of using digital testing tools, one participant cited the use of an AI tool in particular, whilst for online testing directly with customers, another cited emailing surveys to customers for new business.

Firms can also use Flesch reading age scores to assist their assessment of the accessibility of documents to the average person. Considering it is widely accepted that the average reading age in the UK is between ages 9 and 11 this can be a useful assessment when direct customer testing is not being undertaken.

Reviewing product Terms and Conditions remain factually correct can also be undertaken when considering whether a product continues to deliver good customer outcomes.

3.3 - Types of testing of customer understanding (B11)

3. Consumer Duty and Fair Value

3.3 Consumer support

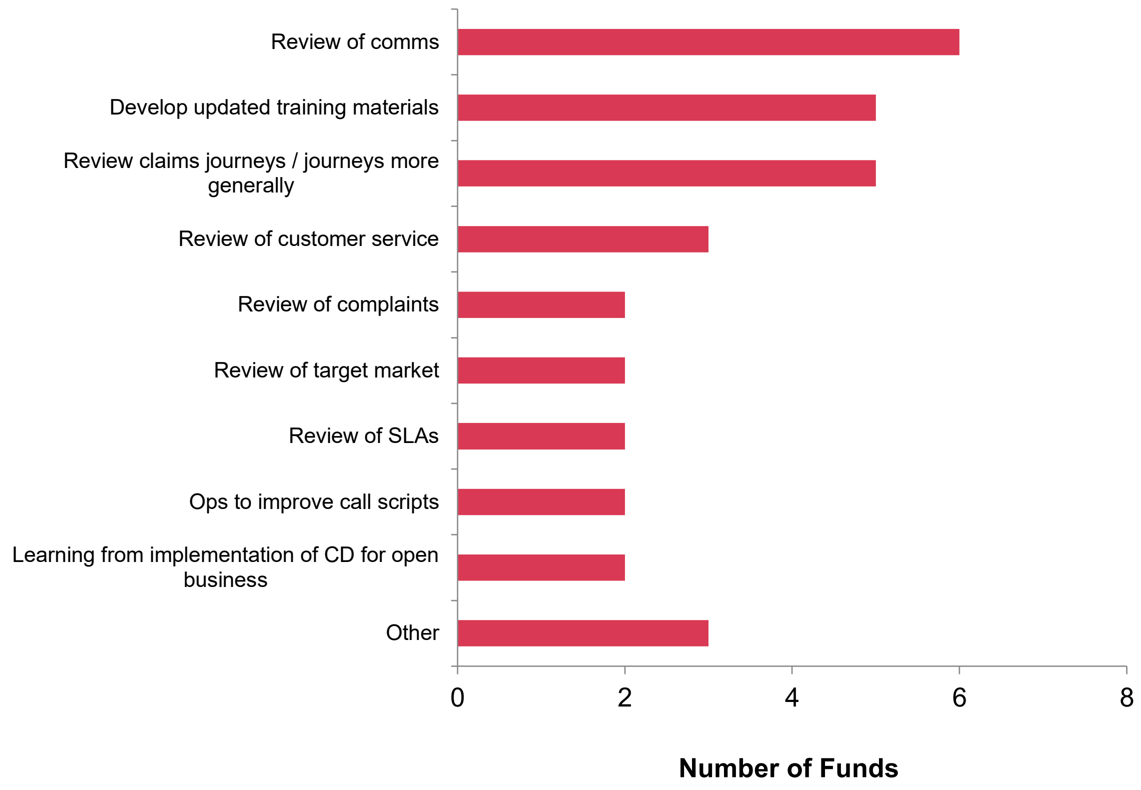
We asked participants if they have considered whether the support provided to with-profits policyholders remains appropriate under Consumer Duty. A number of participants indicated that this requires further consideration. Some of the areas considered - communications, target market seemed more aligned to other consumer duty outcomes. Specific service areas that were identified in responses included:

- Quality assurance;
- Complaints;
- NPS scores;
- SLAs;
- Customer journey reviews;
- Additional training for team members; and
- Improving call centre scripts.

There is a danger that firms can underestimate the importance and difficulty of addressing the consumer support outcome under consumer duty. Some areas firms may want to consider include:

- Vulnerable customers and how well supported they are;
- Whether they have the right channels available for their target market;
- Whether closed customers have the same level of support to open product customers;
- If SLAs across the business provide the right level of support. Where these is variation whether this still results in good outcomes for customers; and
- If there are long call centre waiting times how this is being addressed. This is an area the FCA is expected to focus on in coming months.

3.4 - Support provided to WP policyholder and consumer duty (B13)



3. Consumer Duty and Fair Value

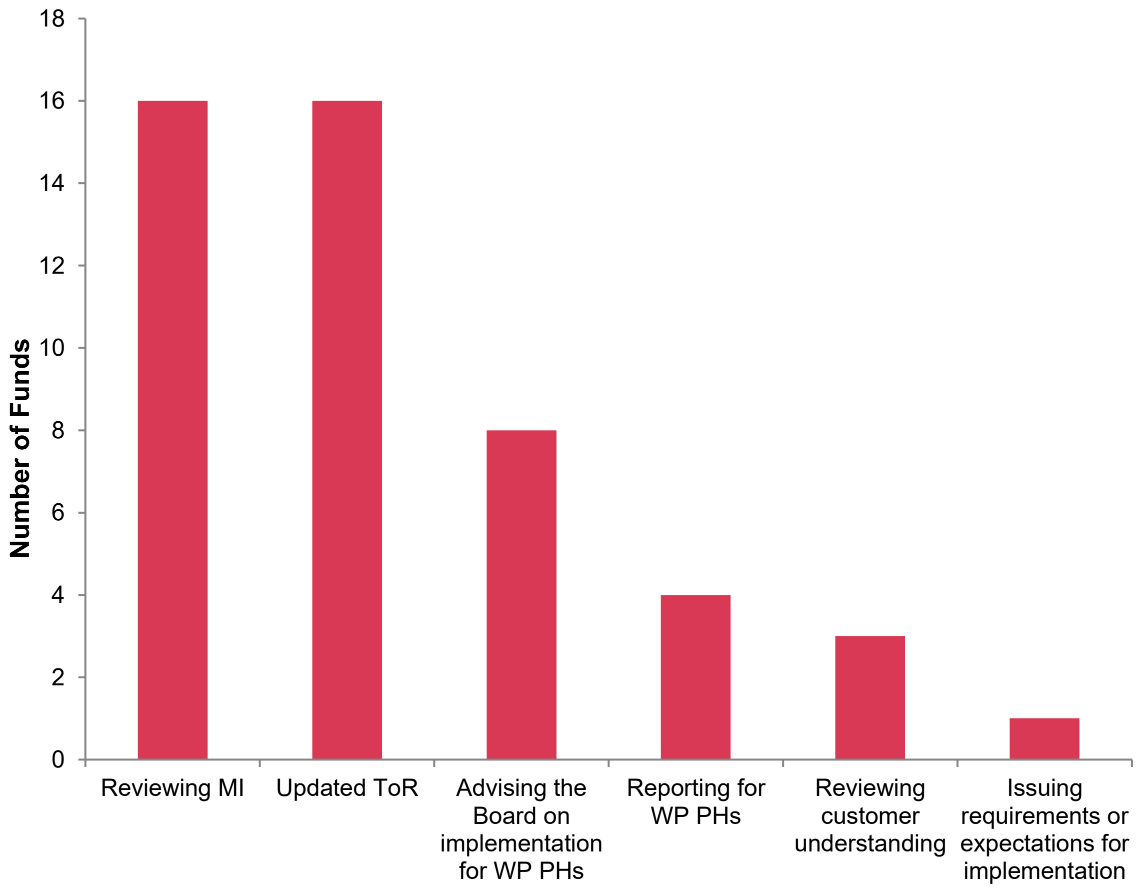
3.4 Role of WPC

We also sought response from participants regarding the role of the With-Profit Committees in the context of Consumer Duty. We have displayed the responses to this question in figure 3.9.

Reviewing MI and updated terms of reference are the most popular answers, advising the Board on the implementation of Consumer Duty for with-profit policyholders also features more commonly.

One of the key roles of a With-Profits Committee is to ensure the interests of with-profits policyholders are appropriately considered within a firm's governance structure, and therefore it’s clear that they have a role to play in Consumer Duty - what this is precisely is still evolving.

3.5 - What role is your WPC taking in the context of Consumer Duty? (B9)



Goneaways

Section four

4

4. Goneaways

The issue of goneaways, where there is a lack of contact between policyholders and the life office over a period of time, continues to be significant for many insurers. Holding reserves for policies where there is unlikely to be a claim, risks delaying the distribution of surplus which may lead to tontine, but on the other hand, releasing reserves for such policies exposes the fund to unexpected claims and an adverse experience.

We last performed a deep dive into goneaways as part of our 2020 with-profits survey. The results of our deep dive showed that:

Common tools were adopted for tracing customers, including the use of external parties and national databases, with over 50% of participants using these.

The continued challenge for the industry was the cost benefit from performing these activities, where only a proportion of customers were re-engaged and ultimately reconnected with their money.

4. Goneaways (continued)

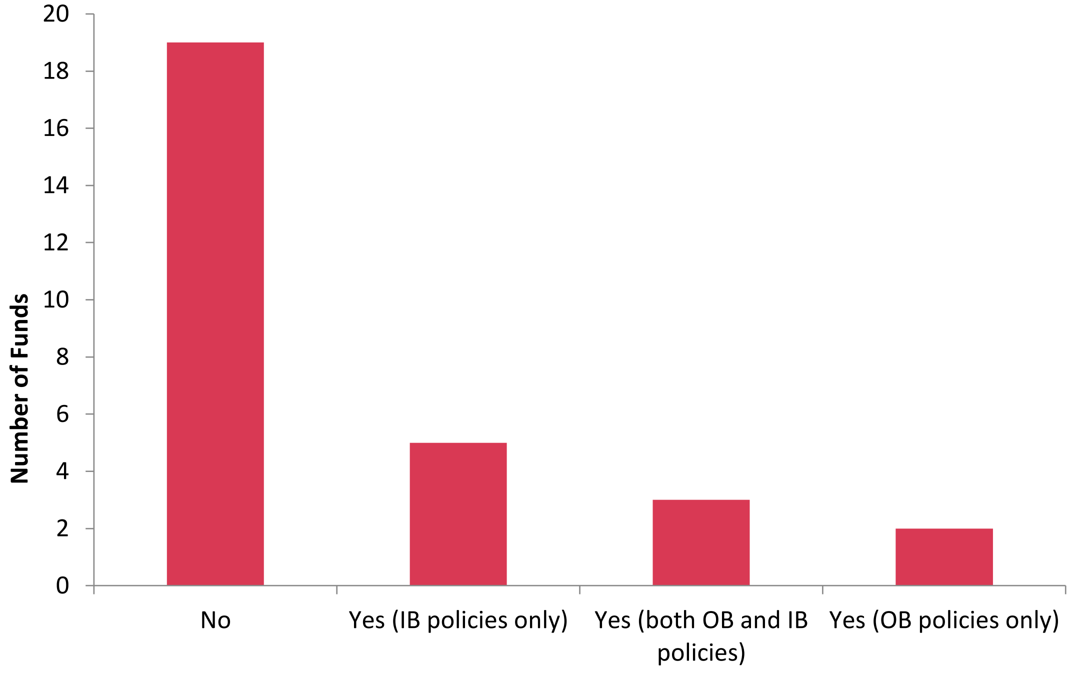
In this year's survey, this section considers how firms are making an allowance for goneaway policies who are not expected to claim from both a reserving and capital perspective. The graphs in this section represent responses from fourteen participants across twenty nine with-profits funds.

We asked participants if they make adjustments to the BEL for goneaway policies.

Figure 4.1 indicates that the majority of participants do not make adjustments.

Out of the funds that do apply adjustments, half of these make adjustments for IB policies only, three funds make adjustments for both IB and OB policies, and two funds make adjustments for OB policies only - though we understand these funds do not have any IB policies.

4.1 - Do you make an adjustment to best-estimate liabilities (BEL) for goneaway policies? (C2)



4. Goneaways (continued)

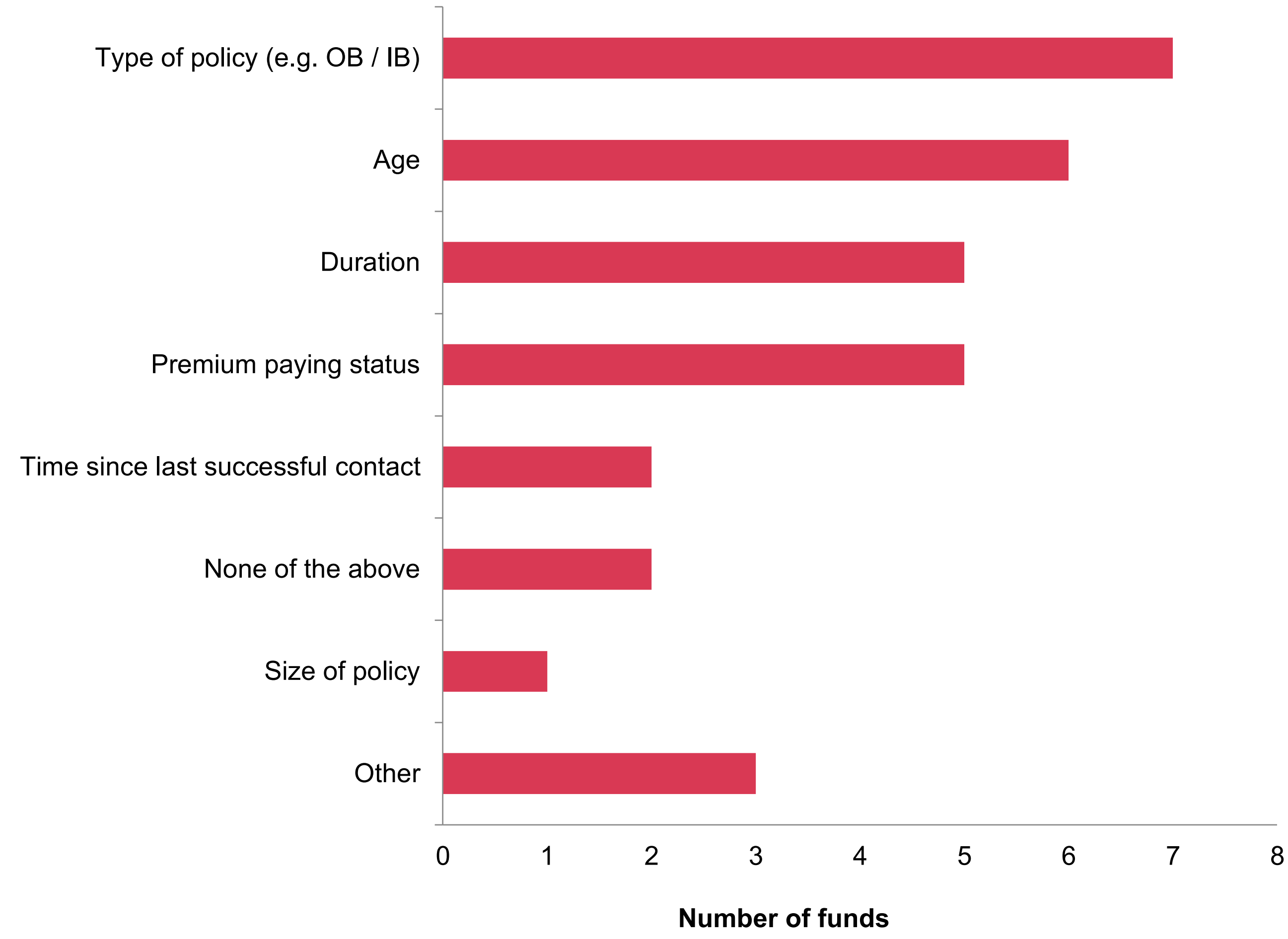
Related to the above, we asked participants to indicate what factors they make an allowance for in their reserving methodology for goneaways, where applicable.

Figure 4.2 shows that the most common factors are:

- Type of policy;
- Age;
- Duration; and
- Premium paying status.

The ‘Other’ category captures tax status and adjustments made for reconnection at a later date.

4.2 - What factors do you make an allowance for in your reserving methodology for goneaways? (C5)



4. Goneaways (continued)

We also asked participants to explain the methodology that they use to calculate any adjustments applied to the calculation of the BEL, and if this was not relevant, to confirm the rationale for not applying an adjustment.

Of the funds that apply adjustments we observe there are two key methodologies being employed.

An experience analysis approach comparing:

(i) the claims on policies which are goneaway; and

(ii) claims on policies where customer contact remains.

1

Applying an adjustment based on the age and/or time elapsed since maturity

2

Considering these two methods further we note:

When looking at the experience analysis approach, making an adjustment based on the age of the policyholder and the premium paying status of the policy was the most common approach.

Typically the experience analysis considers mortality rates between paid up and premium paying policies, which captures differences by age and gender. This brings in standard considerations of experience analysis, such as the weighting and number of historical years of data to include.

In relation to the adjustment based approach, some companies used an approach of bringing a range of information (e.g. duration, age, policy type) together to bucket policies into a chance of future claim e.g. low, medium or high, with the reduction in reserve varying between the buckets.

An alternative mechanism to applying an adjustment based on age, is to remove policies past a certain age/maturity and hold a separate reserve which is run-off over time

In addition to the two methods referenced we note:

When considering the reduction in payouts, companies consider whether a larger proportion of the expense reserve should be retained.

When writing down payouts companies commented on the recycling of profits back via asset share enhancements, this can be directly or via a smoothing account.

Conversely some companies hold policies past maturity as an accounting liability.

4. Goneaways (continued)

Unsurprisingly the key driver of not making an allowance for goneaways is materiality. Though we note a number of funds that are not currently making adjustments for goneaways, are considering bringing this in over time, with the key driver being the impact on estate distribution.

There are also a number of firms developing the way they process and account for goneways, which might trigger a change in views of the reserving methodology.

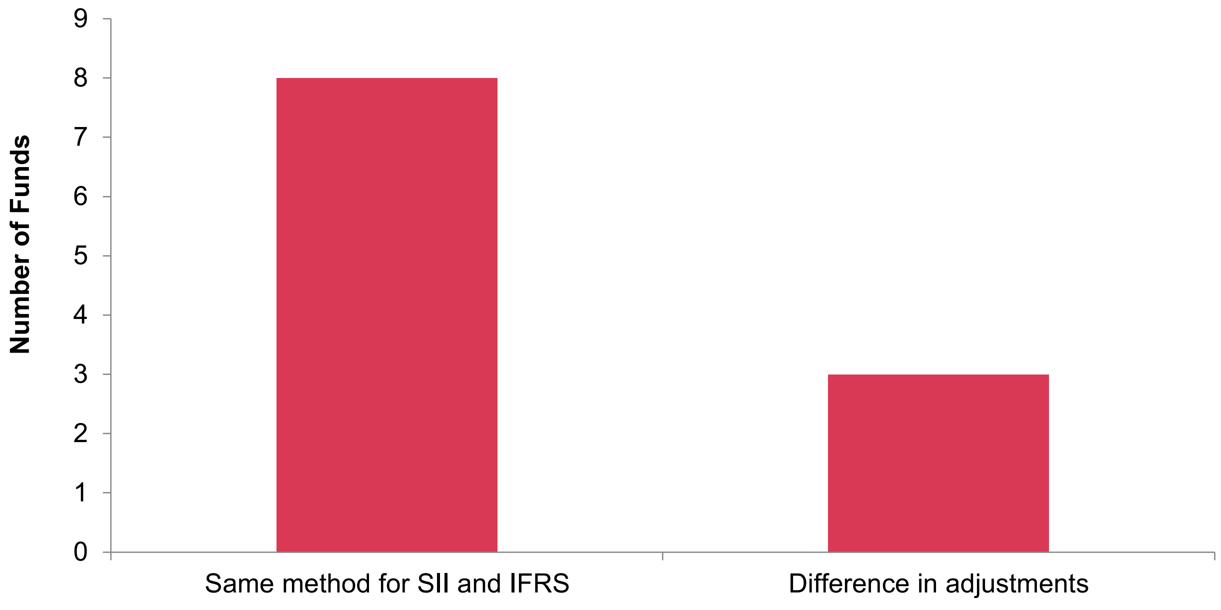
We also note some companies, who currently reserve for goneaways, are intending to extend their methodology to other lines of profits business.

We also consider whether the goneaway adjustments are the same under IFRS/GAAP and SII reporting, as shown in figure 4.3.

Of the funds that apply adjustments:

- Seven funds apply the same goneaway adjustments under SII and IFRS/GAAP; and
- Three funds allow for a smaller goneaway adjustment under IFRS/GAAP than SII due to the use of IFRS/GAAP margins.

4.3 - Differences in goneaways adjustment between IFRS/GAAP and SII reporting? (C4)



4. Goneaways (continued)

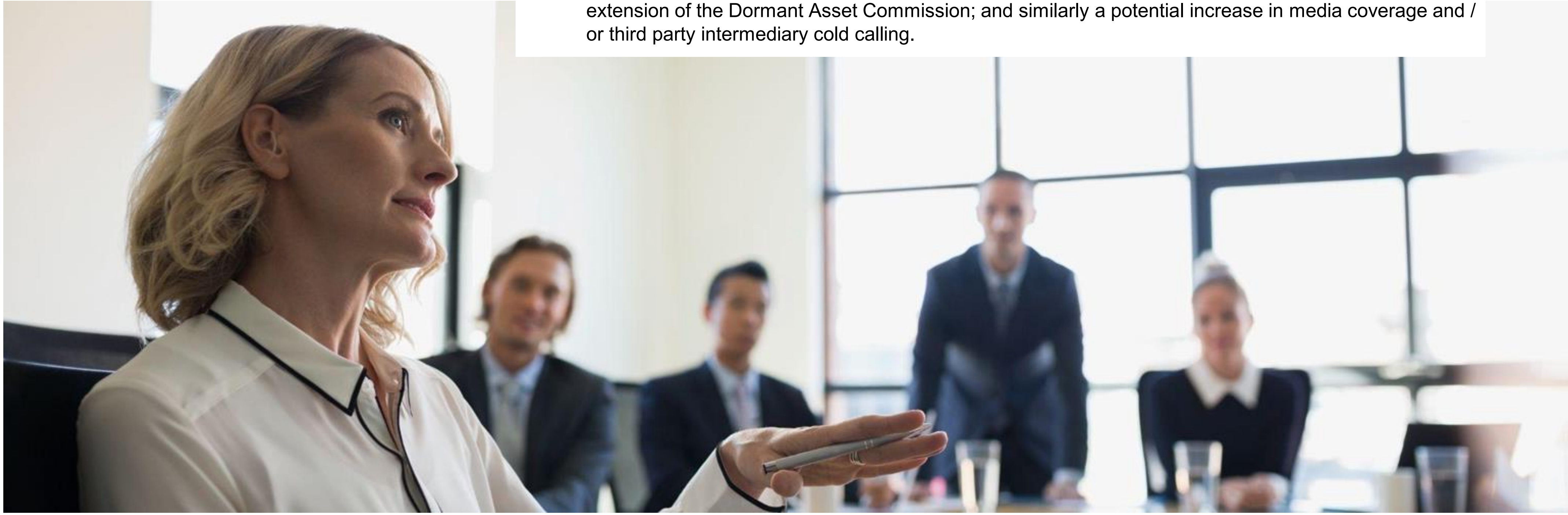
Capital Adjustment:

In addition to the reserving adjustments discussed above, we also considered whether funds make any adjustments to the solvency capital requirements ('SCR') for goneaway policies within an internal model, a partial internal model or the Own Risk Solvency Assessment ('ORSA').

For example, the adjustments may be driven by allowing for a higher amount of claims (as more people come forward) when compared to the base position, or through some other lever. We also asked, for those funds that were making adjustments through their capital position, to confirm the drivers of this and the financial impact that this would have on their balance sheet.

The responses indicated that the majority of funds make no adjustment to the solvency capital requirements for goneaways policies within an internal model, a partial internal model or the ORSA - the limited number of adjustments suggest the capital impact is deemed immaterial.

Where an adjustment has been made we note the driver of applying the adjustment was due to a potential increase in policyholder awareness caused by a national government campaign or scheme e.g. extension of the Dormant Asset Commission; and similarly a potential increase in media coverage and / or third party intermediary cold calling.



We asked participants to confirm who bears the cost of any tracing activities. The responses from this question are displayed in figure 4.4.

The responses indicate that the cost of tracing activities is most commonly borne by the shareholder fund, which is the case for ten funds.

Other common methods include spreading the cost across the asset shares of all the policies in the fund, and charging the costs to the estate.

4.4 – Who bears the cost of tracing activities? (C9)

4. Goneaways (continued)

We asked participants to describe how they allow for interest on late claims payments.

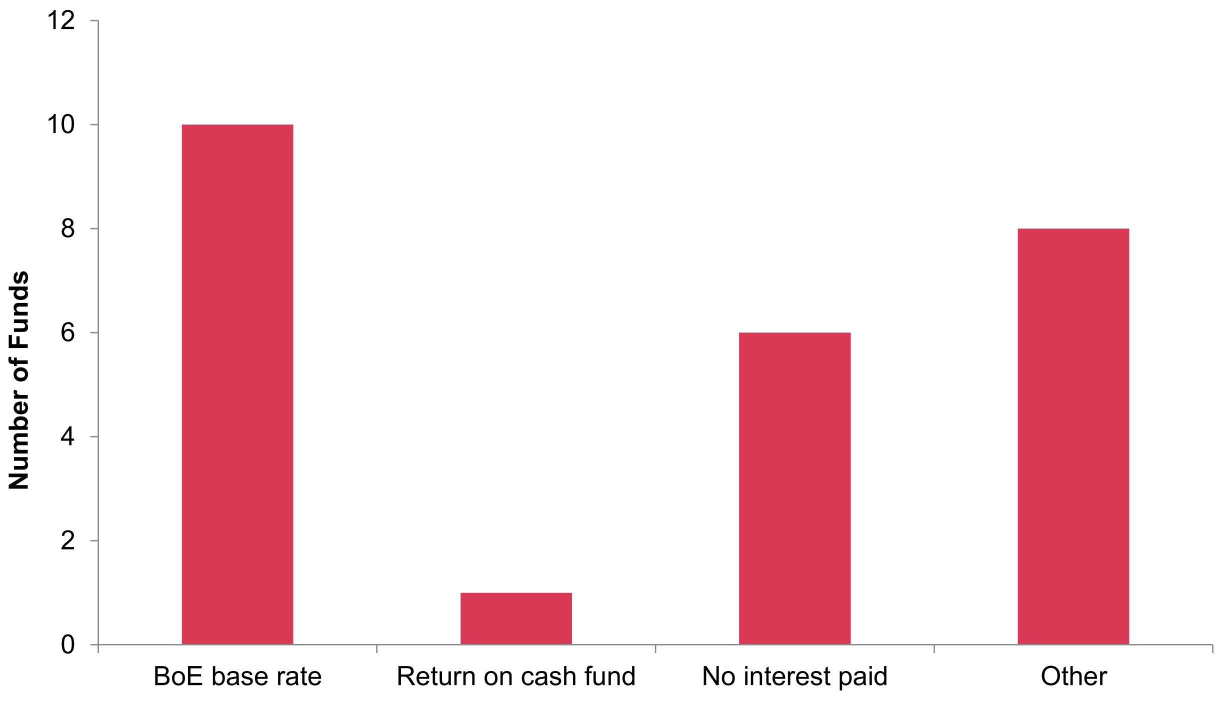
Figure 4.5 shows that the most common method of allowing for interest on late claims payments, used by ten funds, is by paying interest at the Bank of England base rate, whilst four funds pay interest based on return on cash fund. 'Other' responses included:

Bank of England base rate adjusted by a fixed amount. **1**

Variation dependent on whether it is a contractual or discretionary late payment interest, and **2**

Linked to bonus rates over the relevant period. **3**

4.5 - How do you allow for interest on late claims payments? (C11)



Comparison of payouts, expenses and charges

Section five

5

5. Comparison of payouts, expenses and charges

Feedback from our 2021 with-profits survey suggested participants found the comparison of payouts, charges and expenses valuable. This is while recognising it is complex to compare with-profits policies due to various approaches taken by different organisations. We have therefore focused the section on these two areas, plus some additional information relating to the topical subject of internal pricing of GAOs.

Historically, benchmarking of annual payouts has been used to compare performance of with-profits policies, however since PRA returns were replaced by Solvency II reporting this information is no longer available in the public domain.

We asked participants to provide payouts for a number of notional policies, using defined premiums and in force durations.

We acknowledge that comparisons of this nature are complicated by the maturity of the fund, the size of the inherited estate and the speed at which it can and is being distributed. Nevertheless, it can provide another useful measure of the relative value different groups of policyholders will receive.

In this section of the survey, the responses received from participants were more scarce due to policies having run off.

On the following page we have included box and whisker diagrams to illustrate the distribution of payouts on policy types where we obtained at least seven responses.
For those policy types where we received fewer than seven responses, we have included a table illustrating the average payouts.

5. Comparison of payouts, expenses and charges

5.1 Payouts

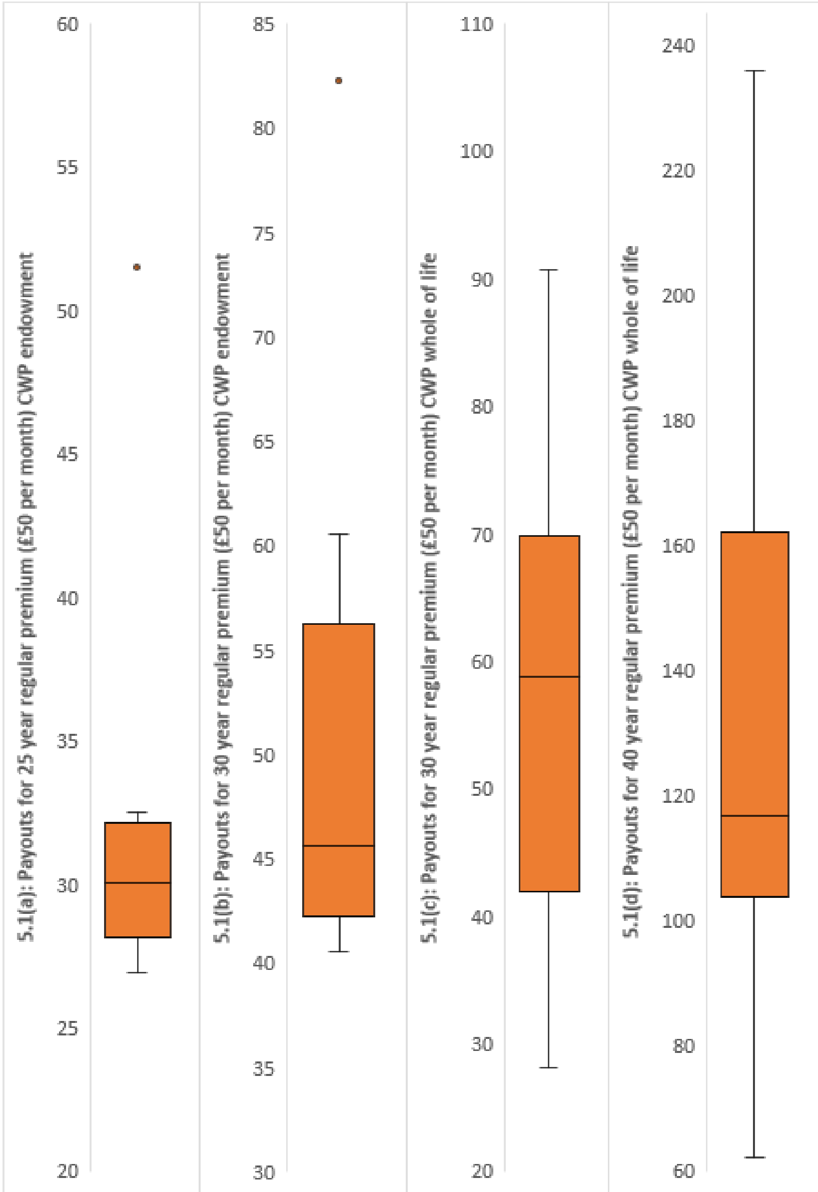
Figures 5.1(a)-(f) show comparisons of payouts for various policy types, split by conventional with profits (‘CWP’) in figures 5.1(a)-(d) and unitised with profits (‘UWP’) in figures 5.1(e)-(f).

There are a number of factors that can drive differences in payouts, including:

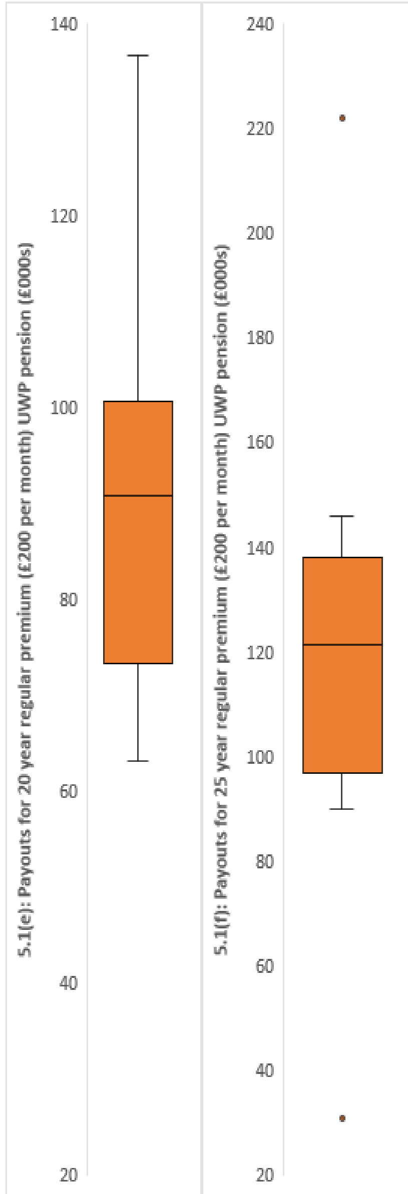
- The relative timing for when participants updated their payouts and market volatility during the first two quarters of the year.
- The inclusion (and quantum) of estate distribution within the payout, similarly to the 2021 survey, we saw on average that payouts from funds including estate distributions were, on average, higher than those without, and
- The approach adopted in respect of smoothing payouts (e.g. the extent of smoothing applied and the duration of the timeframe window used over which smoothing is applied).

The results of this comparison show a wide spread of payouts across the industry for similar policies, with the spread and level of payouts increasing as duration increases. There are outliers on the 20 and 25 year CWP endowment payouts which are considerably higher than the other payouts.

Conventional With-Profits



Unitised With-Profits



5. Comparison of payouts, expenses and charges

5.1 Payouts (continued)

To help with comparisons to prior years we have created a table setting out the change in average payouts across the last three surveys, including this one.

Where payouts have reduced and ranges of payouts have increased, this may have been driven by market volatility arising from the economic shock following the Chancellor's mini-budget in September 2022.

When comparing the payouts information from this year's survey to that provided as part of the 2021 survey, we observed the following:

Payouts are slightly higher for CWP products and the spread of payouts is generally wider when compared to last year's data, and

For UWP, there is less of a clear pattern, with some products showing similar payouts, and others showing payouts are slightly higher or lower than compared to last year's responses. The spread of payouts were similar or wider compared to last year's data, varying slightly by product.

5.2 Table illustrating change in average payouts over time

	2020		2021		2023	
	Mean	**Median**	**Mean**	**Median**	**Mean**	**Median**
20 year regular premium (£200 per month) UWP pension	88,171	88,028	90,178	85,453	90,519	90,824
25 year regular premium (£200 per month) UWP pension	120,190	121,445	127,726	120,567	119,651	121,154
25 year regular premium (£50 per month) UWP endowment	29,463	29,355	28,228	27,802	32,419	30,449
30 year regular premium (£50 per month) CWP endowment			49,050	45,045	50,367	45,648
30 year regular premium (£50 per month) CWP whole of life	63,449	55,867	55,650	44,391	57,495	58,851
40 year regular premium (£50 per month) CWP whole of life	144,734	140,975	135,913	114,499	132,013	116,623
5 year single premium (£10,000) UWP bond	12,031	12,258	11,965	12,186	11,198	11,206
10 year single premium (£10,000) UWP bond	18,388	17,415	17,250	17,102	15,8491	16,169
25 year regular premium (£50 per month) CWP whole of life	41,733	35,958	28,026	26,879	35,855	33,690

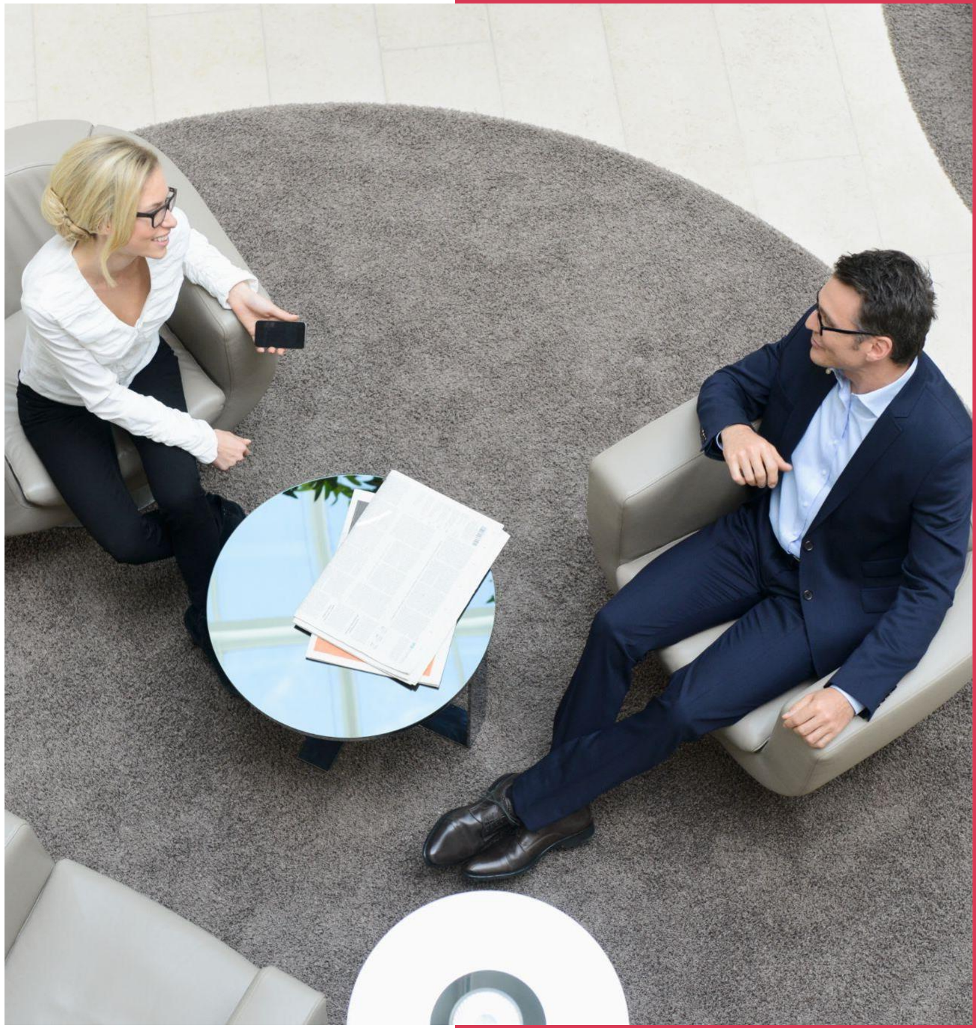
5. Comparison of payouts, expenses and charges

5.2 GAO vesting

5.2 GAO vesting

We also asked participants, given the importance to many firms, how they ensure that a fair price is charged to the with-profits funds with regards to vesting GAOs.

- Four respondents confirmed that they perform an independent assessment, three respondents noted that they outsource this to a third party (or third parties), who are contractually obliged to provide competitive rates, and
- Three respondent noted the use of external benchmarking albeit the methods to perform this assessment varied including the use of data from the Bulk Annuities market.



5. Comparison of payouts, expenses and charges

5.3 Charges and expenses

Overview of charges and expenses

We asked participants to provide the current level of expenses or charges applied to asset shares for an average sized policy, expressing this same amount in both a percentage and monetary (£) terms. The responses cover 20 funds and are shown in Figures 5.3 (monetary amount in £s) and 5.4 (% p.a. charged to the asset share). Our observations are:

Expenses/charges are on average larger for UWP products than CWP, both in monetary and percentage terms.

Expenses/charges are relatively similar across CWP endowments and CWP whole of life in monetary amounts, however this manifests as a larger percentage charge on CWP whole of life, implying smaller average policy values relative to endowments.

The spread of expenses/charges for UWP bonds tends to be wider than for UWP pensions

There is no clear trend when comparing expenses/charges in monetary and percentage terms between participants, supporting the view that expenses/charges to policyholders are dependent on a wide range of factors, including the company, size and type of policy.

Figure 5.3:

Product	Min (£)	Lower quartile (£)	Median (£)	Average (£)	Upper quartile (£)	Max (£)
UWP pensions	39.00	50.57	92.94	126.79	174.69	345.67
UWP bonds	54.45	57.40	162.45	210.90	251.43	734.76
CWP pensions	34.94	51.54	77.87	86.58	121.25	174.69
CWP endowments	13.32	36.69	49.49	67.14	107.51	165.93
CWP whole of life	3.81	19.28	26.00	58.14	100.77	165.93

We observe an increase of c25% in the average charge for UWP pensions compared to the 2021 survey. Though the median has reduced suggesting the mean increase is driven by a change in one or two participants.

For UWP bonds the average and median charges have increased by over 50%.

Figure 5.4:

Product	Min (%)	Lower quartile (%)	Median (%)	Average (%)	Upper quartile (%)	Max (%)
UWP pensions	0.09	0.34	0.81	0.77	1.00	2.00
UWP bonds	0.25	0.38	0.75	0.77	1.00	1.50
CWP pensions	0.20	0.25	0.40	0.54	0.82	1.36
CWP endowments	0.10	0.38	0.44	0.58	0.72	1.44
CWP whole of life	0.03	0.23	0.57	0.63	0.76	1.49

The charges deducted as a percentage of the asset share has decreased, when measured as the mean and median values, for all the products compared to the 2021 survey - there is a minor exception for UWP bonds where we observed a very small increase in the average charges.

Charges to asset shares are typically defined as a percentage of asset share so these should be stable, but there might've been more pressure on firms to lower their charges given regulatory scrutiny and value for money considerations.

The largest reduction in the average charge was observed for CWP Whole of Life policies followed by UWP pensions.

Thank you

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