

SCOTTISH FRIENDLY ASSURANCE SOCIETY LTD



# Scottish Friendly's annual report to with-profits policyholders 2017

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## 1. Purpose

- 1.1. The purpose of this report is to explain how the Scottish Friendly with-profits fund has been managed during 2017 and to demonstrate that we have followed our published 'Principles and Practices of Financial Management' (PPFM).
- 1.2. The Conduct of Business sourcebook of the Financial Conduct Authority ('FCA') requires firms to establish and maintain PPFM documents to govern their conduct of their with-profits business.
- 1.3. The FCA also requires the firm to report to its with-profits policyholders stating whether, throughout the financial year to which the report relates, the firm believes it has complied with its obligations relating to PPFM and setting out the firm's reasons for that belief.
- 1.4. The PPFM documents are available electronically on the Scottish Friendly website: [www.scottishfriendly.co.uk](http://www.scottishfriendly.co.uk).
- 1.5. Throughout 2017 Scottish Friendly has published and maintained separate PPFM documents covering the management of the Unitised With-Profits (UWP) Policies and Conventional With-Profits Policies written within the Scottish Friendly Main Fund. In addition, separate PPFM documents have been published and maintained throughout 2017 for the Rational Shelley, LANMAS, Scottish Legal and Marine & General sub-funds.
- 1.6. The Principles are high-level statements that reflect the general approach adopted in managing the with-profits fund and are not expected to change often.
- 1.7. The Practices are statements of specific practice employed in managing the with-profits fund. They reflect the current approaches given the particular circumstances and economic conditions. Practices are likely to be revised in response to changes in the regulatory, business and economic environment and as new methods and techniques are developed in the life and pensions industry. However, the different Practices would still need to conform to the Principles.
- 1.8. There were no changes made to the PPFM documents during 2017.

## 2. Compliance with PPFM

- 2.1. In the opinion of Scottish Friendly, the management of the with-profits fund during 2017 has been in compliance with the obligations relating to the PPFM. The reasons for reaching this opinion are detailed in section 3.
- 2.2. To ensure compliance with the PPFM during 2017 Scottish Friendly has maintained appropriate governance arrangements.
- 2.3. Scottish Friendly has established an appropriate with-profits governance arrangement to ensure that its Board of Directors can satisfy itself at regular intervals that the with-profits business is being managed in accordance with the PPFM. This governance arrangement is the With-Profits Actuary, David Lechmere of OAC Actuaries and Consultants, and an Independent Person, Christopher Critchlow of OAC Actuaries and Consultants. The terms of reference for this arrangement are available on the Scottish Friendly website. Minor revisions to the terms of reference were made during 2017 to refer to Marine & General and Solvency II, which is the regulatory regime for insurers and reinsurers in the European Union, introduced on 1 January 2016.
- 2.4. The With-Profits Actuary gives advice and recommendations to the Board on matters relating to with-profits business and the Independent Person reviews PPFM compliance.
- 2.5. A report from the With-Profits Actuary to with-profits policyholders is annexed to this report.

### 3. How we have complied with our PPFM

#### Bonus policy and payouts

- 3.1. The Bonus Declaration agreed by the Board, based on the recommendations made by the With-Profits Actuary in his Bonus Recommendation Report, met the requirements of the PPFMs in terms of the bonus and smoothing policy detailed therein.
- 3.2. For most classes of with-profits business payouts are determined having regard to asset shares to endeavour to ensure that fairness is maintained between different groups and generations of policies. The PPFM contains target ranges for maturity and surrender payouts relative to their asset shares.
- 3.3. The target ranges for each class of business are detailed below:

Sub-fund	Target Range
Scottish Friendly OB	80% to 120% unsmoothed asset share
Scottish Friendly IB	75% to 200% unsmoothed asset share
Scottish Legal Life	70% to 130% unsmoothed asset share
LANMAS	80% to 120% unsmoothed asset share
Rational Shelley	Not applicable as set by bonus reserve
Marine & General Conventional Business	80% to 120% unsmoothed asset share
Marine & General UWP Business	90% to 110% unsmoothed asset share

- 3.4. The target ranges are set so that the business can be appropriately managed by allowing flexibility in the setting of bonus rates to smooth returns when markets are volatile, and to give confidence to policyholders that payouts will be fair. We set our bonuses with the aim of keeping our payouts within the target range and ensure that we have good reason to believe that 90% of payouts are or will be within the target range.
- 3.5. Some target ranges, such as Scottish Legal Life and Scottish Friendly IB, are wider than for other blocks of business. For Scottish Legal Life there is a predominance of whole of life policies within this sub-fund, which means that it is more difficult to achieve payouts within a small target range. For Scottish Friendly IB the target range is wider as it is expected that payouts will be greater than asset shares for most of this business.
- 3.6. During 2017 the payouts for maturities and surrenders for the majority of business blocks fell within the target ranges. For blocks where payouts fell outwith the target ranges, further investigations have been carried out, and we are comfortable that payouts to policyholders are fair.

#### Investment strategy

- 3.7. Monitoring investment performance and investment strategy is the responsibility of the Board, and the Board delegates responsibility to the Investment Committee. The Investment Committee monitors the investment performance and strategy regularly. For 2017 the investment strategy has been carried out in accordance with the PPFM.
- 3.8. The investment strategy for Scottish Friendly can be found in the PPFM and the asset allocations can be found on the Scottish Friendly website.

### **Business Risk**

- 3.9. As members of a friendly society, with-profits policyholders ultimately bear the risks and rewards of all business undertaken by Scottish Friendly. Any significant additional business risks to be undertaken by Scottish Friendly require the approval of the Board and Executive, acting on the advice of the With-Profits Actuary. The Board and Executive take into consideration the risks to which with-profits policyholders are and may become exposed, as well as the expectations of achieving appropriate returns for the with-profits policyholders commensurate to the risks borne.
- 3.10. Business risks are monitored regularly throughout the year and an annual review of business risks was carried out during 2017.

### **Charges and expenses**

- 3.11. Scottish Friendly aims to allocate expenses to with-profits policies in a fair manner by giving consideration to the expenses incurred in administering the with-profits business, as well as an appropriate amount of overhead expenses. Consideration is also given fairness between policies and classes of policies.
- 3.12. The approach used to setting charges and expenses is regularly reviewed and remains in line with the PPFM.

### **Management of the estate**

- 3.13. Each sub-fund has an excess of assets over liabilities known as the estate. The management of the estate for each sub-fund is described within the PPFM. The management of the estate has been carried out in line with the PPFM during 2017.
- 3.14. For Scottish Legal Life and LANMAS business, enhancements to asset shares were proposed based on the bonus declaration as at 31 December 2016. These enhancements were implemented during 2017, in line with the intentions of the PPFM, with regard to distribution of the estate.

### **Volume of new business**

- 3.15. New business is written in the Scottish Friendly Main Fund only. All sub-funds are closed to new business.
- 3.16. The volume of new business written over 2017 is in line with the new business plan and meets the requirements set out in the PPFM.

Martin Pringle

Company Secretary

30 May 2018

# With-Profits Actuary's report to with-profits policyholders for the year 2017

As With-Profits Actuary to Scottish Friendly I am required to report to the with-profits policyholders every year on whether, in my opinion, the with-profits business of Scottish Friendly has been managed over the year in a way that takes their interests into account in a reasonable and proportionate manner.

Policyholders should not rely solely on the information contained in this report when making financial decisions and this report does not represent financial advice. I can confirm that, throughout 2017, I have had full access to the actuarial team and the Board of Scottish Friendly to discuss matters relating to with-profits business. In addition, in preparing this report, I have taken account of the rules of the Financial Conduct Authority, the relevant standards published by the Financial Reporting Council and the Practice Standards of the Actuarial Profession.

In my opinion, the annual report by Scottish Friendly to its with-profits policyholders, and the discretion exercised by Scottish Friendly in respect of 2017, has taken the interests of its with-profits policyholders into account in a reasonable and proportionate manner. I believe that the Society has complied appropriately with the requirements of its Principles and Practices of Financial Management for the Main Fund and the notional funds for transferred business. I also consider that the Society has paid due regard to the information needs of its members.

**Presented by the With-Profits Actuary, David Lechmere FIA to the Board of Scottish Friendly Assurance Society Ltd on 30th May 2018**