

Conduct of Business Sourcebook

Chapter 20

With-profits

20.1A The with-profits fund

'Other liabilities' in the with-profits fund

20.1A.1 **R** For the purposes of calculating any *with-profits funds surplus* and the *rules and guidance* in ■ COBS 20, including ■ COBS 20.1A.5 R, ■ COBS 20.1A.6 R and ■ COBS 20.2.17C R, a *firm* must include the following non-exhaustive list as 'other liabilities':

- (1) liabilities arising from its regulatory duty to treat *customers* fairly (where not already included in *technical provisions*); and
- (2) the value of any prospective future transfers out of the *with-profits fund* properly attributable to shareholders in accordance with ■ COBS 20.

Sub-funds

20.1A.2 **R**

- (1) Where the *firm*:
 - (a) identifies particular assets as forming a distinct part of its *with-profits fund*; and
 - (b) restricts participation in the profits or other experience of that distinct part of the fund to a particular category of *with-profits policies*;
 then, provided that:
 - (c) such identification and restriction is consistent with the considerations in (3), and
 - (d) the *firm* treats each affected category of *with-profits policyholder* fairly, having regard to those considerations;
 each such part constitutes a separate *with-profits fund*.
- (2) Notwithstanding (1), each different part of its *with-profits fund* constitutes a separate *with-profits fund* if that is necessary in order to treat each affected category of *with-profits policyholder* fairly, having regard to the considerations in (3).
- (3) The considerations referred to in (1) and (2) are the terms of the relevant *with-profits policies*; the *firm's* established practice; its *PPFM* and/or other relevant communications to affected *with-profits policyholders*, and the terms of any arrangement formally approved by a court of competent jurisdiction, *appropriate regulator* or *previous regulator*.

- 20.1A.3** **R** (1) For a *Solvency II firm* operating a with-profits fund prior to 1 January 2016:
- (a) assets in the with-profits fund held in accordance with *INSPRU* on 31 December 2015 are deemed to be items in a *with-profits fund* for the purposes of **COBS 20** from 1 January 2016, provided that any transfers out of, and any outgoings from, the fund up to 31 December 2015 were made in accordance with, and/or do not as at 31 December 2015, constitute, or continue to constitute, a breach of **INSPRU 1.5.21 R** and **INSPRU 1.5.27 R**;
 - (b) any assets transferred out of the fund in breach of **INSPRU 1.5.21 R** and **INSPRU 1.5.27 R** are deemed not to have been transferred out of the fund and remain part of the *with-profits fund*;
 - (c) to the extent that the assets in (b) have also been transferred out of the *firm* then, before (a) can apply to the *firm*, the *firm* must transfer into the *with-profits fund* assets equal to the value of the assets referred to in (b), and of a similar quality, having regard to the PRA Rulebook: Solvency II Firms: Investments.
- (2) *Firms* to which (1)(a) applies must, in any event, comply with **COBS 20.1A.2 R**. Paragraph (1)(a) does not apply to the extent that it would be inconsistent with the operation of **COBS 20.1A.2 R** where the effect is to require a *firm* to create or make changes to sub-funds amounting to separate *with-profits funds*.

Governance arrangements for the with-profits fund

- 20.1A.4** **R** A *Solvency II firm* effecting or carrying out *with-profits insurance business* must identify the assets relating to all the business written in, or transferred into, each *with-profits fund* which it is required to hold under **COBS 20.1A.5 R** or PRA Rulebook: Solvency II firms: With Profits rule 2.1.
- 20.1A.5** **R** A *Solvency II firm* must ensure that it holds assets in each of its *with-profits funds* of a value at least sufficient to cover the "with-profits policy liabilities" defined in the PRA Rulebook: Glossary and as required by PRA Rulebook: Solvency II firms: With Profits rule 2.1, and any other liabilities in respect of all of the business written in, or transferred into, that *with-profits fund*.
- 20.1A.6** **R** A *Solvency II firm* must maintain separate accounting records for each of its *with-profits funds*. The accounting records must identify:
- (1) all of the assets of that *with-profits fund*;
 - (2) the best estimate component of *technical provisions* for the *with-profits policies* written in, or transferred into, that *with-profits fund*;
 - (3) the best estimate component of *technical provisions* for the *non-profit insurance contracts* written in, or transferred into, that *with-profits fund*;
 - (4) any other liabilities of the *with-profits fund* not covered by (2) or (3), and their value calculated in accordance with PRA Rulebook: Solvency II Firms: Valuation and applicable parts of the *Solvency II Regulation* (EU) 2015/35 of 10 October 2014.

- 20.1A.7** **G** A *Solvency II* firm must ensure that the assets in its *with-profits funds* are separately identified and allocated to the relevant *with-profits fund* at all times. Assets in external accounts (e.g. with banks, custodians, or brokers) should be segregated in the *firm's* books and records into separate accounts for *with-profits insurance business* and other business. Where a *firm* has more than one *with-profits fund*, separate accounting records must be maintained for each fund. Accounting records should clearly document the allocation.
- 20.1A.8** **R** A *Solvency II* firm must not transfer assets out of a *with-profits fund* unless:
- (1) the assets represent any part of a *with-profits fund surplus*, or represent assets held in accordance with **■ COBS 20.1A.5 R** in relation to the part of a distribution that has been made which is properly attributable to shareholders, in accordance with **■ COBS 20**; and
 - (2) no more than three months have passed since the *actuarial investigation* determining that surplus.
- 20.1A.9** **G** For the purposes of **■ COBS 20.1A.8 R**, an *actuarial investigation* is required to determine any *with-profits fund surplus* for the requirements in **■ COBS 20** and remains in-date for three months from the date when the determination of the surplus was made. However, even where the investigation is still in-date, the *firm* should not make the transfer unless there is sufficient surplus at the time of the transfer to cover the value of the assets being transferred. The *actuarial investigation* carried out may rely, in part, on any relevant and sufficiently up-to-date valuation exercise carried out for the purposes of calculating *technical provisions* under the PRA Rulebook: *Solvency II Firms: Technical Provisions* and applicable parts of the *Solvency II Regulation (EU) 2015/35* of 10 October 2014, provided that the person carrying out the *actuarial investigation* considers it appropriate to do so.
- 20.1A.10** **R**
- (1) A *Solvency II* firm must use or apply an asset in a *with-profits fund* only for the purpose of the business in the *with-profits fund*.
 - (2) For the purpose of (1), applying or using an asset includes any obligation (even if only contingent) to apply or use that asset.
- 20.1A.11** **R** A *Solvency II* firm must not agree to, or allow, any mortgage or charge on the assets in any of its *with-profits funds*, other than in respect of, and for the purposes of, the business in the *with-profits fund*.
- 20.1A.12** **G** References in **■ COBS 20.1A.10 R** and **■ COBS 20.1A.11 R** to 'the purposes of the business' in the *with-profits fund* include the payment of claims, expenses and liabilities arising from that business, the acquisition of lawful access to fixed assets to be used in that business and the investment of assets. The payment of liabilities may include repaying a loan but only where that loan was incurred for the purpose of the business written into the *with-profits fund*. The purchase or investment of assets may include an exchange at fair market value of assets (including cash) between the *with-profits fund* and other assets of the *firm*. A *Solvency II* firm may also lend securities held in a *with-profits fund* under a stock lending transaction, or transfer assets as collateral for a stock lending transaction, where the *firm* is the borrower and

where such lending or transfer is for the benefit of the business written into the *with-profits fund*.

Management of the with-profits fund

- 20.1A.13** **R** A *firm*, other than a *non-directive friendly society*, which is subject to contractual terms providing for payments under a capital instrument included in that *insurer's* own funds, must:
- (1) manage any *with-profits fund* so that discretionary benefits under a *with-profits policy* are calculated and paid, disregarding, insofar as is necessary for its *customers* to be treated fairly, any requirements in such contractual terms whether or not they are absolute, contingent or at the discretion of the *firm*; and
 - (2) disclose its intention to manage the *with-profits fund* on the basis set out in (1) in the *firm's PPFM*.
- 20.1A.14** **G**
- (1) A *firm*, other than a *non-directive friendly society*, is expected to manage its *with-profits fund* so that amounts (whether interest, principal, or other outgoings) payable by the *firm* under a capital instrument included in that *insurer's* own funds (as determined in accordance with the PRA Rulebook: Solvency II Firms: Own Funds or Non-Solvency II firms: Insurance Company – Capital Resources) do not impact on the *with-profits fund's* assets or on the *firm's* ability to declare and pay under a *with-profits policy* discretionary benefits that are consistent with the *firm's* obligations under *Principle 6* (Customers' interests).
 - (2) A *firm*, other than a *mutual*, should not regard any asset held in the *with-profits fund* as necessarily available to cover payments or other obligations arising under a subordinated loan.
- 20.1A.15** **R** A *Solvency II firm* must ensure that it has adequate arrangements in place for ensuring that transactions affecting the assets of the *firm* operate fairly between *with-profits policyholders* and other persons interested in the other assets of the *insurer* and, where the *firm* has more than one *with-profits fund*, those transactions operate fairly between the *with-profits policyholders* in each of those funds.