

**CONDUCT OF BUSINESS SOURCEBOOK (REATTRIBUTION OF
INHERITED ESTATES) 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 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 Glossary

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

Citation

- F. This instrument may be cited as the Conduct of Business Sourcebook (Reattribution of Inherited Estates) Instrument 2005.

By order of the Board
20 January 2005.

Annex A

Amendments to the Conduct of Business sourcebook

In this Annex, an entire section of text is being inserted; the place where the change will be made is indicated and the text is not underlined.

After COB 6.12 insert the following section:

6.13 Process for reattribution of inherited estates

Application and purpose

Application

- 6.13.1 R (1) This section applies to a *firm* that carries on *with-profits business* and is proposing to make a *reattribution* of its *inherited estate*.
- (2) Notwithstanding (1), this section does not apply to a *firm* if, and to the extent that, it would require the *firm* to breach, or would prevent the *firm* from complying with, an order made by a court of competent jurisdiction.
- (3) If a *firm* proposes to seek an order, from a court of competent jurisdiction, that would allow or require it to act in a way that is contrary to the *rules* in this section (through, or because of, the exception in (2)), the *firm* must:
- (a) tell the *FSA* that that is what it proposes to do; and
 - (b) seek the order at the earliest opportunity.
- (4) If a *firm* wishes to take a step that would be contrary to the *rules* in this section, in anticipation of such an order, it must secure a *waiver* before it does so.

Purpose

- 6.13.2 G The *rules* and *guidance* in this section are intended to:
- (1) help *firms* to understand the arrangements, or the types of arrangement, that the *FSA* regards as appropriate when a *firm* makes a *reattribution* of its *inherited estate*; and
 - (2) ensure that *policyholders* are treated fairly during the *reattribution* process.

- 6.13.3 G The *FSA* accepts that the interests of *policyholders* may be protected in a number of ways, depending on the circumstances of the *firm* and the type of *retribution* that it proposes to make. In many cases, this will involve the sanctioning of an *insurance business transfer scheme* under Part VII of the *Act*, but that will not always be the case. The *rules* and *guidance* in this section are therefore intended to be sufficiently flexible to be capable of delivering the objective of ensuring that *policyholders* are treated fairly, regardless of the particular type of *retribution* and whichever legal process is used. *COB* 6.13.1R(2) also recognises that in some cases, for example, in connection with an *insurance business transfer*, the courts have the power to make procedural and other orders that may affect the application of the *rules* and *guidance* in this section.
- 6.13.4 G A *firm* may propose alternative arrangements to those set out in this section by applying for a waiver under section 148(4) of the *Act* (Modification or waiver of rules).
- 6.13.5 G Whether or not a *waiver* is required, a *firm* should consult the *FSA* about its intentions, before it begins a *retribution* process, if it wishes the *FSA* to consider whether the *firm's* detailed proposals are consistent with the *Principles for Businesses* and, in particular, *Principle 6* (Customers' interests). The *FSA* will endeavour to respond to a *firm's* proposals, including by giving *guidance* (if appropriate), within a reasonable time.
- 6.13.6 G Although the *FSA's* approval is not required before a *firm* can make a *retribution*, the *FSA* has the power, under section 45 of the *Act* (Variation etc. on the Authority's own initiative), to impose a *requirement* on a *firm's* *permission* if it appears to the *FSA* that it would be desirable to do so in order to protect the interests of consumers. If the *FSA* considers that some, or all, of a *firm's* *retribution* is inconsistent with the *Principles for Businesses*, the *FSA* may use that power to require a *firm* to modify, or to refrain from carrying out, some or all of its *retribution*.
- 6.13.7 G The way in which the *FSA* may use its power to vary a *permission* on its own initiative is explained in *SUP* 7 (Individual requirements). One ground for using the power is that the *FSA* considers it desirable to do so in order to protect the interests of *consumers*. In assessing whether there are grounds for exercising such powers in connection with a *retribution*, the *FSA* will have regard to whether or not a *firm* has acted in accordance with the *guidance* in this section and, if a *firm* has not done so, whether it has been able to demonstrate that compliance with that *guidance* would have been inappropriate or impracticable in its particular circumstances.

Policyholder advocate: appointment and function

- 6.13.8 R A *firm* that is seeking to make a *retribution* of its *inherited estate* must appoint a policyholder advocate to negotiate with the *firm* on behalf of relevant *with-profits policyholders*.
- 6.13.9 R The *policyholder advocate* must be nominated or approved by the *FSA* before he is appointed.

- 6.13.10 G The *FSA* is likely to nominate a *policyholder advocate* if it considers that the *retribution*, or any part of it, is likely to be complex or controversial. If the *FSA* does not nominate a person to be the *policyholder advocate*, the *firm* should nominate a suitable candidate for *FSA* approval.
- 6.13.11 G The *FSA* expects the *policyholder advocate* to be a natural person who:
- (1) is free from any conflict of interest that might be, or might appear to be, detrimental to the interests of *policyholders*; and
 - (2) has the skills and knowledge necessary to act as the *policyholder advocate* on the proposed *retribution*.
- 6.13.12 G The *FSA* may wish to have preliminary discussions with the *policyholder advocate* nominated by the *firm* to help the *FSA* to determine whether he is suitably qualified and experienced to act as the *policyholder advocate* for the proposed *retribution*. The *FSA* will consider the suitability of the nominee and inform the *firm* that nominated him whether it approves him. Since the nature of the proposed *retribution* is a factor in determining the suitability of the nominee, the *FSA* cannot approve a nominee before a broad outline of the *retribution* has been determined. If the *FSA* rejects a nominee it will normally tell him why it has done so and, if the nominee agrees, the *FSA* will also tell the *firm*.
- 6.13.13 G The *FSA* considers that it is desirable for a *firm* to include an independent element in the *policyholder advocate* selection process. That might include consulting representative groups of *policyholders* or using the services of a recruitment consultant. When considering an application for approval of a nominee to perform the *policyholder advocate* role, the *FSA* will have regard to the extent to which the *firm* has involved others in the selection process.
- 6.13.14 G The precise role of the *policyholder advocate* in any particular case will depend on the nature of the *firm* and the *retribution* proposed. A *firm* will need to discuss with the *FSA* the precise role of the *policyholder advocate* in a particular case. However, the role of the *policyholder advocate* should include:
- (1) negotiating with the *firm*, on behalf of the relevant *with-profits policyholders*, the aggregate value of the benefits to be offered to them in exchange for the rights or interests they will be asked to give up;
 - (2) commenting, to *with-profits policyholders*, on:
 - (a) the methodology used for the allocation of benefits amongst the relevant *with-profits policyholders*, or groups of *with-profits policyholders*, and the form of those benefits;
 - (b) the criteria used for determining the eligibility of the *firm's* various *with-profits policyholders*;
 - (c) the terms and conditions of the proposals (to the extent that they have a material effect on the value of the benefits to be offered, or on the bonuses that may be added to *with-profits policies*); and

- (d) the views expressed by the *independent expert* or the *retribution expert* (as the case may be), and the *actuary* appointed by the *firm* to perform the *with-profits actuary function* on the allocation of any benefits amongst the relevant *with-profits policyholders*; and
- (3) telling *with-profits policyholders*, or each group of *with-profits policyholders*, with reasons, whether the *firm's* proposals are in their interests.

Policyholder advocate: terms of appointment

- 6.13.15 R A *firm* must notify the *FSA* of the terms on which it proposes to appoint a *policyholder advocate*, whether or not the candidate was nominated by the *FSA*.
- 6.13.16 G A *firm* should include with its notification:
 - (1) a copy of its proposed contract with the *policyholder advocate*;
 - (2) a copy of its proposed terms of reference for the *policyholder advocate*;
 - (3) details of the proposed negotiation timetable and the *policyholder advocate's* budget;
 - (4) the *policyholder advocate's* confirmation that he is content with the proposed contract, terms of reference, plan and budget, if he is, or with a summary of his reservations, if he is not; and
 - (5) any other information that the *FSA* may reasonably require when it considers the proposed terms of appointment for the *policyholder advocate*.
- 6.13.17 G The *FSA* will respond to the *firm*, including by giving *guidance* (if appropriate), as soon as it has reached a view on the proposed terms of appointment.
- 6.13.18 R A *firm* must ensure that the terms of appointment for the *policyholder advocate*:
 - (1) stress the independent nature of the *policyholder advocate's* appointment and function, and are consistent with it;
 - (2) define the relationship of the *policyholder advocate* to the *firm* and its *policyholders* respectively;
 - (3) set out the arrangements under which the *policyholder advocate* is to communicate with *policyholders*;
 - (4) make provision for the resolution of any disputes between the *firm* and the *policyholder advocate*; and
 - (5) specify when and how the *policyholder advocate's* appointment may be terminated.

- 6.13.19 R A *firm* must ensure that the *policyholder advocate's* terms of appointment allow him to communicate freely and, at his discretion, in confidence with the *FSA*.
- 6.13.20 G It may be necessary, or desirable, for the *policyholder advocate* to discuss the terms of the proposed *retribution* directly with the *FSA*, or for him to be able to participate in the *FSA's* meetings with the *firm*. COB 6.13.19R is intended to ensure that the *policyholder advocate* is free to do that whenever he, or the *FSA*, regards that as necessary or appropriate.
- 6.13.21 G A *firm* may agree to include, within the terms of appointment for the *policyholder advocate*, arrangements for the *policyholder advocate* to be indemnified in respect of certain claims that may be made against him in connection with the performance of his functions. If such indemnity is given, it should not include protection against any liability arising from acts of bad faith.

Reattribution expert

- 6.13.22 R Where a *firm* is not otherwise required to appoint an *independent expert* to assess its *retribution* proposals, it must appoint an expert (referred to as the 'reattribution expert') to undertake an objective assessment of them, taking into account:
- (1) the nature and extent of any restructuring of the *firm's with-profits fund*;
 - (2) the benefits that will be allocated to relevant *with-profits policyholders* in exchange for the rights and interests they are being asked to give up; and
 - (3) any other factors that may be regarded as material by the *FSA* or the expert.
- 6.13.23 G Many transactions involving a *retribution* will involve an *insurance business transfer scheme* that requires court approval under Part VII of the *Act*. In those cases, the *firm* will be required to appoint an *independent expert* who has the responsibilities set out in the *Act* and SUP 18. The *independent expert's* function is to assess objectively, and then prepare a report on, the relevant *insurance business transfer scheme* for the benefit of the court, although the *firm's with-profits policyholders*, others affected by the scheme and the *FSA* will, or may, also rely on it. The *reattribution expert's* function is broadly the same and it contrasts with the role of the *policyholder advocate*, who is appointed primarily to negotiate the benefits to be given to *with-profits policyholders* in exchange for the rights and interests they are being asked to give up.
- 6.13.24 R A *firm* must not appoint a *reattribution expert* who has not been nominated or approved by the *FSA* to act as an expert in relation to the *firm's* proposed *retribution*.
- 6.13.25 R If a *firm* appoints a *reattribution expert*, it must ensure that the expert's terms of appointment allow him to communicate freely and, at his discretion, in confidence with the *FSA*.
- 6.13.26 G The *FSA* expects a *reattribution expert* to be a natural person who:

- (1) is free from any conflict of interest that might, or might appear to, undermine his independence or the quality of his report;
 - (2) has relevant knowledge, both practical and theoretical, and experience of the types of *insurance business* transacted by the *firm*; and
 - (3) is an *actuary* familiar with the role and responsibilities of an *actuary* appointed under *SUP* 4 (Actuaries).
- 6.13.27 G The general principles in *SUP* 5.4.8G, regarding the suitability of a *skilled person*, also apply to the appointment of a *retribution expert*.
- 6.13.28 G A *firm* should co-operate fully with a *retribution expert* and provide him with access to all relevant information and appropriate staff.
- 6.13.29 R (1) A *firm* that appoints a *retribution expert* must require him to prepare a report.
- (2) The report required by *COB* 6.13.29R(1) must be made available to the *FSA*, the *policyholder advocate* and the court (if it is relevant to any court proceedings).
- (3) An adequate summary of the report required by *COB* 6.13.29R(1) must also be made available to the *firm's with-profits* and other *policyholders*.
- 6.13.30 G A *retribution expert's* report, required by *COB* 6.13.29R(1), should comply with the applicable rules on expert evidence and contain the following information:
- (1) the information detailed in *SUP* 18.2.33G(1) to (10), (12) and (13), and *SUP* 18.2.39G; and
 - (2) his opinion of the likely effect of the proposals on *with-profits policyholders* or, where relevant, each relevant group of *with-profits policyholders*, having particular regard, where relevant, to the matters set out in *SUP* 18.2.36G, as if in each case, a reference to:
 - (a) the '*scheme report*' was a reference to the '*retribution expert's report*';
 - (b) the '*independent expert*' was a reference to the '*retribution expert*'; and
 - (c) the '*scheme*' was a reference to the proposal for a '*retribution*'.
- 6.13.31 G The amount of detail that it is appropriate to include in the report required by *COB* 6.13.29R(1) will depend on the complexity of the proposals, the materiality of the details themselves and the circumstances.

- 6.13.32 G Where the proposal for a *retribution* forms part of a wider proposal for restructuring, it may not be appropriate to consider the *retribution* in isolation. In those cases, the *retribution expert* should seek a sufficient explanation of the *firm's* plans to enable him to understand, and report on, the wider picture.

Negotiation timetable

- 6.13.33 G When a *firm* decides, in principle, to appoint a *policyholder advocate*, it should give him sufficient time to select the professional advisers he regards as necessary to enable him to perform his functions. It should also give him an opportunity to make preliminary enquiries about the *firm*, its *long-term insurance fund*, the nature of its proposals and the factual background to them.
- 6.13.34 G At an appropriate time, a *firm* should announce the appointment of the *policyholder advocate*, marking the formal start of the negotiations. In the first instance, the arrangements under which a *policyholder advocate* is appointed should require him to take such steps as he considers necessary to communicate with, and receive views from, relevant *with-profits policyholders* about the proposed *retribution*. Only when he is satisfied that he has had adequate time to communicate with relevant *with-profits policyholders* should a *policyholder advocate* expect, or be expected, to begin negotiations with a *firm*.
- 6.13.35 G The *FSA* would not normally expect the period from the announcement of the appointment of a *policyholder advocate* to the conclusion of a prospective deal to be less than three *months*.

Information to policyholders: the policyholder advocate and the negotiations

- 6.13.36 R A *firm* must make arrangements so that every *policyholder* that might be affected by the proposed *retribution* will receive appropriate information about the *retribution* process, and any offer that will be made to him, in a timely way.
- 6.13.37 G Relevant *with-profits policyholders* should be given clear information about the proposals, including an explanation of the wider picture, for example if the *retribution* is linked to the restructuring of a *firm*.
- 6.13.38 G When a *firm* makes information available to its *policyholders*, it should have regard to *Principle 7* (Communications with customers). It should also explain the benefits and disbenefits of its proposals, for each relevant group of *policyholders* and for the *firm* if, and to the extent that, that is appropriate in the context of the information that it will be providing at any particular time.
- 6.13.39 G The information given to *policyholders* should explain the role and background of the individuals who have been appointed to perform particular functions, including those of the *policyholder advocate* and the *independent expert* or the *retribution expert*, as the case may be.

- 6.13.40 G The information should also explain the steps in the *retribution* process, the timetable for the proposed *retribution* and any interdependencies. A *firm* should also consider the information needs of *policyholders* who will not be directly affected by the *firm's* proposals.
- 6.13.41 G A *firm* should ensure that appropriate arrangements are put in place for *policyholders* of the *firm* to have access to further information, including over the internet and through helplines. These should remain operational throughout the *retribution* process and be able to provide *policyholders* with information on demand. A *firm* should take reasonable steps to ensure that the information provided to *policyholders* is kept up-to-date.
- 6.13.42 G The *FSA* does not consider it necessary for *policyholders* to receive regular updates on the progress of negotiations between the *firm* and the *policyholder advocate* if they are completed within a relatively short timescale. However, in the case of protracted negotiations, *policyholders* should receive an update at least every six *months*, commencing with the announcement of the appointment of the *policyholder advocate* (see *COB* 6.13.34G).

Notification to policyholders: conclusion of negotiations and consent

- 6.13.43 R When a *firm* and a *policyholder advocate* complete their negotiations about the benefits that will be offered to relevant *with-profits policyholders*, in exchange for the rights and interests they will be asked to give up, the *firm* must:
- (1) tell relevant *policyholders* that the *firm* and the *policyholder advocate* have completed their negotiations;
 - (2) explain the outcome of the negotiations and, if appropriate, the *firm's* final proposals for the *retribution*; and
 - (3) give relevant *with-profits policyholders* the chance to:
 - (a) individually accept or reject those proposals; or
 - (b) (if the legal process to be followed allows the majority of *policyholders* to bind the minority) vote on whether the *firm* should go ahead with those proposals.
- 6.13.44 G A *firm* should also:
- (1) explain the essence of its proposals, including details of:
 - (a) the context or background to the proposals and how the final version has been arrived at; and
 - (b) any material changes or departures from the information that it has already supplied;

- (2) explain the effect of the negotiations on *policyholders*, including a description of any benefits they are likely to receive and the rights and interests that they are likely to be asked to give up;
 - (3) include a report from the *policyholder advocate*, which explains the basis of his negotiations with the *firm*, whether he considers that the *firm's* proposals are in the interests of relevant *with-profits policyholders*, or groups of *with-profits policyholders*, and gives reasons for the conclusions that he has reached; and
 - (4) include information about the report by the *independent expert* or the *retribution expert*, as the case may be, including a summary of the report and details of how *policyholders* can obtain a copy of the full report, if they wish to do so (see *COB 6.13.29R*).
- 6.13.45 G The *retribution* process may redefine the rights of certain parties. There are established legal processes that enable such rights to be redefined by majority vote. If a *firm* proposes a *retribution* that follows some other process, the *FSA* considers that, for that *retribution* to be fair, *policyholders* should be given the chance to decide whether or not to accept the *firm's* proposals and, if they decide not to accept, their existing rights should be protected. The *FSA* therefore expects *firms* to offer individual choice, or to follow an established legal process where the majority can bind the minority (with the sanction of the court, if applicable).
- 6.13.46 R If a *firm* chooses to make an offer to its *policyholders*, when the *firm* and the *policyholder advocate* have not been able to agree the value of the benefits to be offered to *with-profits policyholders* in return for the rights and interests they are being asked to give up, it must also explain the fact of, and reasons for, the *policyholder advocate's* disagreement.
- 6.13.47 G Where a *firm* proposes an elective process under *COB 6.13.43R(3)(a)*, and a minority do not accept the proposals in the first instance, the *FSA* would expect the *firm* to make arrangements to allow those *policyholders* a further opportunity to elect to be a party to the *retribution* at a later date.
- 6.13.48 G Where a proposal is put to the vote of *policyholders* in accordance with *COB 6.13.43R(3)(b)*:
- (1) the voting arrangements should allow relevant *with-profits policyholders* the opportunity to vote by post or, if the vote is to take place at a meeting, for those *policyholders* to be able to appoint proxies to represent their views; and
 - (2) the notice period, the closing date for votes submitted by post or, as the case may be, the time for appointing proxies should normally be at least eight weeks after the prospective deal has been announced.

- 6.13.49 R Before, or at the same time as giving notice to relevant *with-profits policyholders* of an invitation to accept the offer under *COB 6.13.43R(2)(a)* or an invitation to vote under *COB 6.13.43R(2)(b)*, a *firm* must send out details of the individual benefits to be received by each relevant *with-profits policyholder* in exchange for the rights or interests they are being asked to give up.

Notification to policyholders: final outcome

- 6.13.50 G A *firm* should, within a reasonable time, notify *policyholders* of the final outcome of the *retribution* process. This should normally be done after the court has considered the proposed *retribution*, if court sanction is required.
- 6.13.51 G Provided that any court hearing is due to take place within a reasonable time once the outcome of the vote is known (see *COB 6.13.43R(3)(b)*), the *FSA* does not consider it necessary for a *firm* to write individually to *policyholders* to explain the outcome of that vote. However, a *firm* should make the information publicly available, for example by putting a notice on its website, by giving details through its helpline, or by placing an advertisement in the national or regional press.

Limits on the need to provide information

- 6.13.52 R *COB 6.13.36R*, *COB 6.13.43R*, *COB 6.13.46R* and *COB 6.13.49R* do not require a *firm* to disclose confidential, or commercially sensitive, information nor do they require a *firm* to disclose information that relates to a third party or is irrelevant to its *retribution* proposals or arrangements.
- 6.13.53 G A *firm* will not be treated as having failed to comply with any obligation in this section to provide information if the information has been provided to relevant *with-profits policyholders* by another *person*, such as the *policyholder advocate*, the *independent expert* or the *retribution expert*.

General costs

- 6.13.54 G Subject to *COB 6.13.55G* to *COB 6.16.58G*, *retribution* and *insurance business transfer* costs (excluding *policyholder advocate* costs) should be met from shareholder funds. A *firm* may present alternative arrangements if it can show good reasons for doing so.

Policyholder advocate costs

- 6.13.55 G The *policyholder advocate's* budget, and the *policyholder advocate's* costs, should be agreed between the *firm* and the *policyholder advocate*. For these purposes, the *policyholder advocate's* costs include ancillary costs, such as the costs of professional advice and administrative and publicity costs.
- 6.13.56 G The *FSA* recognises that the treatment of costs will almost certainly affect the value of the benefits offered. The *FSA* will not normally seek to restrict the way in which *policyholder advocate* costs are divided between shareholders and *policyholders*, provided that:

- (1) the shareholder pays a reasonable proportion of them;
- (2) the arrangements are fair; and
- (3) the *policyholder advocate* confirms that he is satisfied with them.

- 6.13.57 G A *firm* may therefore agree an arrangement with the *policyholder advocate* by which relevant *with-profits policyholders* contribute to the *policyholder advocate's* costs, for example by a deduction from the aggregate value of the benefits that will become available to those *policyholders*.
- 6.13.58 G A *firm* might also propose a budget that it will fund entirely, or in part, from shareholder funds with any additional expenditure being met from funds attributable to relevant *with-profits policyholders*. Another approach would be cost sharing, so that a *firm* and relevant *with-profits policyholders* will benefit if savings are made, compared to the budget, and costs are shared if the budget is exceeded.
- 6.13.59 G If a *retribution* proposal is not successful, the *FSA* would expect the costs of the *policyholder advocate* to be met by the *person* initiating the proposal. That will usually be the shareholders of the *firm*.

Annex B

Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

inherited estate

~~the excess of assets maintained within a *with-profits fund* over and above the amount required to meet liabilities (including liabilities which arise from the regulatory duty to treat *customers* fairly in setting discretionary benefits) an amount representing the fair market value of the *with-profits assets* less the *realistic value of liabilities* of a *with-profits fund*.~~

policyholder advocate

the *person* appointed under COB 6.13.8R to negotiate with a *firm* on its proposals for making a *retribution* of its *inherited estate*.

retribution

the process under which a *firm* which carries on *with-profits business* seeks to redefine the rights and interests that the *with-profits policyholders* have over the *inherited estate*.

retribution expert

the expert appointed by a *firm* to satisfy its obligations under COB 6.13.22R.