

Eleanor Linton
With Profits Review
The Financial Services Authority
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Dear Eleanor

With-Profits Review: Issues Paper 5
Governance of with-profits funds and future role of the appointed actuary

I am responding on behalf of the Consumer Panel to the questions raised in Issues Paper 5.

The Consumer Panel welcomes the opportunity to consider the issues around the governance of with profits policies and the role of the appointed actuary.

Part 1: Governance of with-profits funds

Representation of With-profits policyholders

Q1.1 and 1.2

We agree with the issues set out in paragraphs 26 to 37. We have not identified any other issues relating to the governance of with-profits funds that we believe should be considered.

Q1.3

We have no comments on the contextual points made in paragraph 40.

Q1.4

Yes, the Panel thinks that one or more of the options for representation of policyholders' interests set out in paragraphs 41 to 68 would strengthen the governance of with-profits funds.

Q1.5-1.10

The Panel has considered the various options set out in options 1 to 5 of the paper. We do not think that option 1 by itself is sufficient although we support the approach taken in Issues Paper 4 to set out clearly the principles and practices in accordance with which discretion will be limited and exercised. We agree that a report on how

the fund has been managed in accordance with the principles and practices is desirable, but we think that this by itself will not create a line of accountability from the board to the policyholders.

We agree with the analysis of the problems in putting policyholder representatives on Boards under option 2. At best a representative could amount to a fly in the ointment and at worst a token representative easily ignored. We do not see where the expertise to perform this function will come from.

We are more enthusiastic about the idea of a With Profits Committee set out in option 3. We favour a Committee that is separate from the Board, since we think the role of the Committee is to ask difficult questions and to act as a forum in which Boards have to be accountable to policyholders for their decisions. Furthermore, we think that directors, even non-executive directors, sitting on this committee will suffer from the problem identified in options 1 and 4 that directors owe their duty to the shareholders. If there are outside members of the Committee as well as the non-executives, the conflict between the interests of shareholders and policyholders will simply be transferred from Board level to Committee level. These are disadvantages associated with option 3b.

However, we also acknowledge the problem of lack of expertise and specialist knowledge in the Committee which option 3a might result in. We have two possible solutions to this. The first is that there should be a standing panel of individuals, including policyholders, retired financial service practitioners, academics and other people with relevant skills. This panel should be trained and equipped to fulfil the role of challenging Boards in the exercise of their discretion in decisions relating to with-profits policies. For any given with-profits fund a group of people would be selected from the panel to take evidence and consider whether the principles and practices had been met. A group would consider each fund once a year at least and report to policyholders, but could also be called in where controversial matters had arisen.

We have in mind the model of the members of the Competition Commission. Panel members would have to be independent of the fund they were considering and would need to bring to the job skills that were cognate with, but not the same as, Board members. We do not see people serving on the panel as amateurs. They would need to be knowledgeable people who would be resourced to the extent necessary to allow proper time for training and examination of documents and, where necessary, formal taking of evidence from Boards. We think the solution of setting up a panel from which members of a group could be chosen would be more cost effective than setting up a committee for each fund and would allow better use of expertise. We think that the panel should be appointed by the FSA.

Because of the problem identified in the paper's exposition of option 3a - that such a committee might have the disadvantage of being 'distant' from the workings of the company - we would lay a duty on the appointed actuary to act as a conduit between the company and the group in relation to the fund under examination. (But see our

comments on 'Role of the appointed actuary' below as to who this should be). We note the FSA's view that it would not be appropriate for any With-Profits Fund Committee set up under option 3(a) or 3(b) to undertake the role of policyholder negotiator discussed in the first of the Issues Papers (on the process for dealing with the attribution of inherited estates). We agree that particular difficulties could arise if a sub-committee of the board were to be asked to negotiate on behalf of policyholders. If, however, the With-Profits Fund Committee was appointed by the FSA and constituted separately from the Board, then we do not see any reason why it could not undertake the role of policyholder negotiator; indeed, it would seem eminently suited to doing so.

We do not support option 4. We do not see that this solution provides any effective accountability to policyholders in how interests have been 'balanced'. The prospect of policyholders taking Boards to court is remote.

We think option 5 looks interesting, but that it may be more practical to think of it as a way ahead in designing new products, rather than a solution to the conflicts already existing.

We have not considered the cost implications of the various options.

Part 2: The Future Role of the Appointed Actuary

We do not feel we have had enough time to explore all the issues in this part of the paper. In particular, we would have liked an opportunity to quiz an appointed actuary on how the present system works in practice. However, here are our views:-

It appears that there are two functions for the actuary at present, one to be a resource in assessing the financial health of the business in prudential terms, and the other to advise the Board on fair treatment of customers and policyholders.

We think that the function of advising the board on fair treatment must be carried out by someone who does not have a duty to shareholders. For the same reason we do not think granting share options to the person carrying out this function is appropriate.

However, we are aware that making this function separate from the board could give rise to problems with 'distance' from the Board and the possibility of losing touch with the real issues for policyholders. It seems that this actuarial function either has to be carried out by an employee with external audit by an independent, or by an independent with a duty on employees and directors to make material available, and with a power to attend Board meetings and receive papers. Given the current debate on the efficacy in protecting shareholders' interests of auditors (external) and non-executive directors (internal), we do not see that there is an obviously right solution here. What we are convinced of is that the committee examining the exercise of

discretion needs access to someone who has the expertise and the power to make investigations. The Committee will be holding the Board to account for the exercise of its discretion, but it will need the assistance of the actuary responsible for advising on fairness to policyholders to do so.

Yours sincerely,



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Chairman

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