The Equitable Life Assurance Society – 2018 Run-off Plan

1. Introduction

This document sets down the Society's run-off plan as at 30 November 2018.

The 2018 Run-off Plan has been produced in accordance with COBS 20.2.56R and COBS 20.2.57G in the FCA's Handbook of rules.

2. How the Society manages the run-off of the Equitable Life with-profits fund

The Society announced in June 2018 that it intends to complete a Scheme of Arrangement to fully and fairly distribute all of the Society's inherited estate to With-Profits policyholders. That will involve uplifting policy values, removing investment guarantees and converting With-Profits policies to Unit Linked. Immediately afterwards, the Society would execute a Part VII transfer of the business to Reliance Life, a subsidiary of LCCG.

The transfer to Reliance Life is expected to complete towards the end of 2019. However, should the Scheme not be accepted by With-Profits policyholders, the Society would rollback to run-off.

The project to effect the Scheme of Arrangement and Part VII transfer to Reliance Life is referred to as "the Scheme".

Under run-off, the Society's overall strategy is:

- Distributing all of the assets amongst with-profits policyholders as fairly and as soon as possible.
- Carefully managing solvency to enable capital distribution and only then seeking to maximise return;
- Providing a best value for money cost base;

The Society currently manages c£4.3bn of assets in respect of c250,000 with-profits policyholders, around half of whom are members of group pension schemes. In addition, the Society manages c£1.7bn of unit linked business. The Society also has a reassured non-profit book of c£0.4bn of assets with Scottish Widows Limited, a subsidiary of Lloyds Banking Group (LBG)

We expect that the Society's with-profits assets will run off by approximately 30% over the next 5 years, and by another 30% over the following 5 years. The remaining assets will run off from then on over about another 20 years.

Our strategy at the Society is to recreate policyholder value. We, therefore, look to establish methods of reducing risk which, in turn, reduces capital requirements. That releases excess capital for distribution to with-profits policyholders.

Around 80% of with-profits business by value has a 3.5% guaranteed interest rate, which leads to onerous capital requirements. Our most pressing strategic challenge, therefore, is to balance the need to meet our contractual obligations under the guarantees far into the future against the fair distribution of our capital to those policyholders leaving over the next several years.

The Society has successfully reassured all of its mortality and longevity risk with Swiss Re and Scottish Widows. As a result, capital is no longer required to protect against these risks.

A regular review of charges for unit-linked business and the small number of unit linked funds ensures limited cross-subsidisation of this business by the with-profits policyholders. The Society continues to provide an appropriate unit-linked fund choice for policyholders.

In 2011, the Society introduced a mechanism for capital distribution through a claims enhancement factor (CEF), whereby the underlying Policy Value was enhanced by 12.5% payable when a claim was made. This rate for capital distribution was increased to 25% in 2014 and to 35% in 2015. Since then, it has remained at 35%. The Policy Value plus the capital distribution is compared with the underlying policy guarantee and the greater amount is paid. Any future changes will be determined in line with the Capital Distribution Framework.

The introduction of the CEF in 2011, and the increases in 2014 and 2015, represent a key strategic development for the Society to provide fairness in run-off. If CEF does not increase, however, it becomes less valuable to most with-profits policyholders as time goes by. That is because the additional value it provides is eroded in a low interest rate environment by the 3.5% guaranteed interest rate growth.

The Transitional Deduction gives the Society greater certainty about maintaining its current level of capital distribution in a low interest rate environment.

Following the UK’s decision to exit the EU, the Society intends to set up a subsidiary, Equitable Life Ireland. The intention is to carry out a Part VII transfer of all Irish and German business to Equitable Life Ireland (ELI) in March 2019 should there be no transitional arrangements. The Society would reassure all with-profits liabilities from ELI and transfer sufficient assets for all other liabilities. ELI would be likely to transfer to Reliance Life if the Scheme of Arrangement and transfer of the Society’s business is successful.

3. The Society's Risk Management Arrangements

Ultimate responsibility for oversight of management of risk within the Society rests with its Board. The Board has adopted the three lines of defence governance model to support it in the discharge of these responsibilities. Roles and responsibilities for risk management under the three lines of defence are set out in the Society's Risk Management Policy. This policy is expanded upon in our Enterprise-wide Risk Management (ERM) Framework which describes the Society's approach to ERM and sets out the way in which we identify and understand our risks, and ensure that they are monitored and managed effectively.

Under the three lines of defence, the first line of defence is our staff, all of whom have a responsibility for identifying risks. Staff are helped in their understanding of these responsibilities by regular compulsory computer-based training, a key focus of which is risk management. Responsibility is placed on line managers within the Society to ensure that all staff in their business areas follow the Society's policies and processes and this is reinforced through performance management scorecards. The Society's Executive Committee, chaired by the Chief Executive, is responsible for managing material risks and ensuring that the Society's risk management arrangements continue to be suitable, proportionate and effective.

The second line of defence is the Risk function which is responsible for providing the framework of risk policies, processes, methodologies and reporting to be followed by the Society's staff. The Risk function must also provide both support and challenge to the use of these tools.

The third line of defence is Internal Audit who review risk management arrangements in line with the annual Assurance plan approved by the Audit and Risk Committee, and will report to the Audit and Risk Committee on the effectiveness of the design, operation and embeddedness of the ERM framework.

4. Source documents

Consistent with our current strategy, the Society's "Principles and Practices of Financial Management" (PPFM) provides a description of the Society's current plans to manage its with-profits business in run-off. The PPFM is reviewed annually or, if circumstances require, at other times.

Towards the end of each year, the Society produces a Business Plan containing:

- plans and proposals for the next three years to execute the Society's strategy and to mitigate actual or potential risks and challenges;
- three year financial projections.

An essential part of the implementation of the Scheme of Arrangement and transfer to Reliance Life or a successful run-off is the active management of risk in the Society's business.

5. Information required by SUP App 2.15

SUP App 2.15.2 – Funding
A description of how the firm manages the run-off of the with-profits fund including:

- details of the expected duration and costs of fully running off the fund's liabilities;
- an explanation as to how a solvent run-off will be funded; and
- details of the firm's future strategy for managing the risks associated with the run-off of the fund.

Information for SUP App 2.15.2 – Funding

1. Managing the business and distribution of assets

The Society aims to manage its business in a sound and prudent manner for the benefit of all policyholders and, in particular, so that it can continue to meet contractual obligations to policyholders and other creditors as they fall due.

It is the intention of the Society that all of its assets, after providing for its contractual liabilities, including those to holders of non-profit policies and other creditors, will be distributed as fairly and as soon as possible amongst the holders of its with-profits policies over the lifetime of those policies. This means that amounts distributed amongst with-profits policies can exceed the contractual guaranteed entitlements of with-profits policyholders. Any amounts distributed amongst with-profits policies in excess of contractual guaranteed entitlements are decided after allowing for the requirement to meet the Society's contractual obligations as they fall due, and the need for the Society to maintain an appropriate level of solvency capital to operate its business.

The Society's bonus policy is described in section 1 "Distributing the Society's assets" of the information provided in section "SUP App 2.15.7(11) – Capital distribution" below.

2. Strategy

The Society's strategy is:

- Distributing all of the assets amongst With-Profits policyholders as fairly and as soon as possible.
- Carefully managing solvency to enable capital distribution and only then seeking to maximise return;
- Providing a best value for money cost base;

In furtherance of the three elements shown above, with the objective of releasing solvency capital that can be distributed to with-profits policyholders, the Society has:

Information for SUP App 2.15.2 – Funding

- Increased, in April 2015, the rate of capital distribution to with-profits policyholders to 35% of the Policy Value;
- Increased the annual management charges and rationalized the fund range of unit-linked business to reduce expense cross-subsidy by the with-profits fund;
- Reduced reinsurance counterparty risk by recapturing some of the remaining unit-linked business reinsured with Scottish Widows Limited;
- Transferred, in February 2016, the Society's non-profit annuity business to Canada Life;
- Applied for, and received approval for, a Transitional Deduction from technical provisions; and
- Reassured, in November 2016, all remaining mortality risk with Swiss Re.

The change of strategy in 2018 to implement the Scheme would distribute all the assets amongst policyholders and achieve fair customer outcomes. Under the Scheme, the Society has also:

- Purchased payer swaptions to protect the Scheme uplift against interest rate increases;
- Sold all corporate bonds redeeming after 30 September 2019 to reduce the impact of credit risk on the Scheme uplift; and
- Purchased spread locks to protect against a widening of the gilt-swap spread.

Were the Society in run-off, it would continue to initiate business simplifications to achieving cost economies and ensure that costs vary more in line with policy run off.

3. Investment policy and risks

The Society operates a conservative investment policy as a result of its solvency position. The Society accordingly invests mainly in fixed interest securities (both gilts and corporate bonds) and, were it to continue in run-off, would be unlikely to alter this policy. This strategy is helpful in reducing risk, and in helping to maintain solvency within risk appetite. It protects with-profits policyholders from the worst effects of falling stock markets, but also limits the returns that will be achieved in rising stock markets. The large holding of gilts also means that the liquidity risks of a closed fund are mitigated.

Under run-off, the Society's Asset and Liability Committee (a committee of executive management) would manage corporate bond investment so that short-term liabilities are matched with corporate bonds and longer-term liabilities are matched with gilts.

To protect against interest rate changes and fluctuations in policy uplifts under the Scheme, the Society purchased £100m of payer swaptions in August 2017. Should interest rates fall or remain at the same level as they were when the swaptions were purchased, they will expire with nil value.

Information for SUP App 2.15.2 – Funding

Under the Scheme, the Asset and Liability Committee instructed BlackRock in mid-2018 to sell all corporate bonds with redemption dates after 30 September 2019.

In November 2018, the Society purchased spread locks to protect against changes in gilt-swap spreads.

Unit-linked liabilities are matched with investments in unit-linked funds.

4. Business risks

With-profits policyholders share in all the profits and losses of the Society. These are passed on through the Society's Policy Value system. The Board aims to manage risk where possible to minimise any negative impacts on policy payouts and so that the Society can continue to be able to meet its contractual obligations to policyholders and other creditors as they fall due. The Society's strategy in respect of business risks, some of which are outside the control of the Society, is to seek opportunities to reduce or limit the risks, whilst being fair to all policyholders.

There are limited circumstances in which the Society would accept additional business risks, being either where it is satisfied that the rewards are sufficient and the risks are not high, or where the taking of a new (lower) risk would mitigate an existing business risk.

5. Duration of the with-profits liabilities

A graphical projection of the liability cash flows, starting from 30 June 2018, is provided in the paper 'Matching Interim Review and Year-End Proposal'.

6. Managing the risks

For the active management of risk during run-off, the Society has

- investment guidelines for managing investment risks, and
- an over-arching Risk Management Policy together with specific risk policies which cover Credit Risk (including counterparty risk), Insurance Risk (including reinsurance risk), Liquidity Risk, Market Risk and Operational Risk, and
- an Enterprise-wide Risk Management Framework setting out the Society's approach to risk management.

More information on the Society's management of risks can be found

- in the information provided below for SUP App 2.15.3, SUP App 2.15.4, SUP App 2.15.5, and SUP App 2.15.6,
- in the copies of the Society's current investment guidelines and risk policies, and
- in the ORSA Report.

Information for SUP App 2.15.2 – Funding

7. The costs of the Scheme or run-off

We define our budget as the current annual expenses that would be incurred under run-off if the Society was in a stable, long-term state and was not carrying out any strategic projects. Costs for a Scheme of Arrangement and Transfer to Reliance are covered by exceptional expenses for strategic projects. Exceptional Expense also cover the cost of the Part VII transfer of the Irish and German business to ELI.

The Society increased annual management charges on unit-linked funds from 1 April 2016. This has enabled overall costs and the subsidy from the with-profits fund to be reduced.

Information on the budget is provided in the Business Plan and in the Board Paper on valuation expenses.

8. Sources of information for SUP App 2.15.2

Information on the Society's management of risks for run-off and the Scheme is also provided by:

- the Society's current Principles and Practices of Financial Management (PPFM)
- the Business Plan
- the Society's investment guidelines
- the capital distribution framework
- the Society's risk policies
- the Society's current Management Actions Grid
- the 2017 year-end valuation expenses paper
- the ORSA Report

SUP App 2.15.3 - Investment risk

An explanation of the firm's future investment strategy, including:

- Its strategy of matching the with-profits fund's liabilities with appropriate assets; and
- Any changes it expects to make to the with-profits fund's investment strategy as a result of the closure of the with-profits fund, including any changes to the proportions of different types of investments.

Information for SUP App 2.15.3 - Investment risk

Under the Scheme, the Society operates an asset strategy to enable a smooth and efficient transition from with-profits to the post-Scheme asset mix. It has recently sold most of the corporate bonds to reduce credit risk and is currently holding only short term corporate bonds that will redeem before 30 September 2019. The Society has also purchased payer swaptions to protect the Scheme uplift against interest rate increases and spread locks to protect against a widening of the gilt-swap spread. Were the Scheme not successful, the corporate bonds would likely be repurchased, the payer swaptions sold and spread locks unwound.

Under run-off, the Society operates a conservative investment policy as a result of its solvency position as measured under the ORSA and Solvency II frameworks. The Society accordingly invests mainly in fixed interest securities. The Society carefully matches the outgoings from maturities with the income from its assets.

The investment strategy under run-off is fundamental to reducing risk, and in helping to maintain solvency within risk appetite. It protects with-profits policyholders from the worst effects of falling stock markets and maintains the capital distribution amount. However, it also limits the returns that will be achieved in rising stock markets.

Investment strategy is determined by Board. The Asset and Liability Committee (ALCo), a committee of executive management, has delegated authority from Board to oversee the implementation of that strategy.

The Society's investment manager for the with-profits fund is BlackRock and, for a de minimis property investment, Schroders. Since the recapture of the unit-linked business in March 2015, Aberdeen Standard Investments has been the investment manager for this business.

ALCo defines the investment objectives for the investment managers and the parameters within which the investment managers may manage the assets of the with-profits fund. Those instructions for the with-profits fund include:

- Details of cashflow matching requirements;
- Details of acceptable credit or liquidity quality;
- Limitations on investments in relation to counterparty exposure;

Information for SUP App 2.15.3 - Investment risk

- Limitations on exposure in respect of derivatives and other instruments that may alter the economic out-turn from assets;

For unit-linked business, the Society has no appetite for any mismatching risk and holds assets which match the policy liabilities as closely as possible.

ALCo meets monthly to review investment performance and controls. Solvency and the desire to have a close match of asset and liability proceeds are key drivers of investment strategy, so it is kept under regular review, and reported formally to the Board at least every six months. A more thorough and formal review of the Society's financial position, the risks it faces, including investment risk and the solvency capital required is carried out at least twice a year, and reported to Board. Any changes to the investment strategy resulting from these reviews would be implemented by the ALCo on behalf of the Board.

The current investment objectives and parameters within which the Society's investment managers may manage the assets of the with-profits fund are provided by the Society's current Investment Guidelines.

Sources of information for SUP App 2.15.3

Information on the Society's investment risk management is also provided by:

- Section 7 "Investment Policy" in the Society's current Principles and Practices of Financial Management (PPFM);
- the Society's Investment Guidelines;
- the asset-liability matching described in the BlackRock report and the paper "Matching Interim Review ";
- Note 15 on pages 70 to 78 of the Society's 2017 Annual Report and Accounts;
- the Society's 2018 Own Risk and Solvency Assessment Report, which shows the financial effect of the Society's investment risks.

SUP App 2.15.4 - Credit and counterparty risk

An explanation of the firm's strategy for managing the with-profits fund's counterparty and credit risk, both within and external to the firm's group.

Information for SUP App 2.15.4 – Credit and counterparty risk

1. Ownership and Governance

Ultimate responsibility for the management of prudential risks rests with the Society's Board. Asset and Liability Committee (ALCo) sets the basic investment strategy and policy for the Society in the light of its liabilities (including future bonus policy) and its credit, market and liquidity risk policies and risk appetite as approved by the Board. The Board is responsible for the overall risk, including credit risk, from the relationship with Scottish Widows Limited and its parent Lloyds Banking Group.

Management of credit risk relating to assets has been delegated to ALCo. Oversight is achieved by the receipt and review of management information which enables adherence to the policy to be monitored.

2. Identification of credit risk

Analysis of the Society's activities and its associated sources of credit risk is carried out as appropriate by the Chief Investment Officer. ALCo reviews the investment policy in the light of any internal or external changes and considers the credit risk implications of any material changes.

3. Sources of credit risk

There are two key sources of credit risk for the Society, arising from:

- Reinsurance counterparty risk
- Investment of assets

Reinsurance counterparty risk

The Society has reinsurance arrangements with LBG which were entered into in 2001 for

- the reinsurance with Scottish Widows Ltd of most of the Society's non-profit business;
- the reinsurance with Scottish Widows Limited of Equitable group pension benefits linked to the Clerical Medical Unitised With-Profits Fund,

such that, currently, c£9m of unitised with-profits liabilities and c£377m of non-profit liabilities are reinsured with Scottish Widows Limited. Equitable Life therefore has a significant counterparty risk with Scottish Widows Limited.

Information for SUP App 2.15.4 – Credit and counterparty risk

Scottish Widows Limited is a regulated insurance entity and is required to hold Solvency II capital in order to meet policyholder expectations in a 1 in 200 event. If there was such a 1 in 200 event, we would expect any losses for Scottish Widows Limited to be met from its capital holdings. A more extreme event would be required before the assets became insufficient to meet liabilities. In that scenario, it might reasonably be expected that Scottish Widows or potentially LBG, as the ultimate parent company, would make good the shortfall to prevent reputational damage.

Notwithstanding these considerations, the Society recognises that under the standard formula in the Solvency II regime, the Society is required to hold capital for reinsurer counterparty risk. This was a key driver for the Society's strategic recapture from LBG of the reinsured business with benefit links to the Equitable unit-linked funds and reinsured pension temporary assurance benefits, in March 2015.

The Society reinsured all remaining mortality risk with Swiss Re in November 2016. The counterparty risk with Swiss Re is trivial.

Investment of assets

The main source of credit risk arising from the Society's investments is the potential default of bond issuers and cash deposit counterparties directly or within liquidity funds. The Society's revised approach to corporate bond investment described above, in the information on investment risk provided for SUP 2.15.3, will also mitigate the Society's exposure to credit risk.

Of lesser significance is the risk of loss from stocklending counterparties.

Derivatives

Derivatives may be used following a full assessment and approval by ALCo. Substantial use of derivatives will require Board approval. Interest rate receiver swaptions purchased by the Society have the effect of mitigating the exposure to policyholders with 3.5% Guaranteed Investment Return (GIR) deferring their retirement in low interest rate conditions. The credit risk is the potential default of the issuing Investment Bank and this is mitigated by "margining" to provide appropriate collateral. Swaptions are reviewed by ALCo annually and were restruck in mid-2016.

The Society purchased £100m payer swaptions in 2017 and spread locks in 2018 to protect the Scheme uplift. For all these derivatives, margining mitigates the risk of default of the issuer.

Other sources of credit risk

The key source of settlement risk, in the context of an Insurer, is the risk of the loss of cash relating to the sale and purchase of investments. This is covered by counterparty exposure which is considered below. Other potential sources of credit risk have been considered and are either not relevant or insignificant. This is kept under regular review to ensure that any new sources of risk are identified and managed.

Information for SUP App 2.15.4 – Credit and counterparty risk

4. Overview of credit risk appetites

The level of credit risk that the Society is prepared to take is described in the following sections in general terms.

Reinsurance

The credit exposures to LBG are those that exist because of historic reasons. For the avoidance of doubt, these are in respect of the sale agreements (and any associated disputes) entered into in 2001, including those for reinsurance of most of the Society's non-profit business (other than immediate annuities) and unit-linked business.

The impact of a Scottish Widows, or potentially LBG, default would be significant. The risk has been accepted and we hold counterparty risk capital against it.

The counterparty risk with Swiss Re is trivial. No counterparty risk capital is held.

Bond default and counterparty exposure

The risk of default of bond issuers and deposit counterparties is reflected to some extent in published credit ratings. A related risk would arise from over exposure to individual entities (concentration risk). Under run-off, the Society expresses its appetite to this risk by setting out:

- benchmark levels for the aggregate value of holdings at the various credit ratings
- maximum concentration levels for exposure to individual entities
- limits for holdings in individual issues.

The concentration levels include aggregate limits for exposure to individual entities (including groups) across their bond issues and cash deposit facilities.

The Society's current credit risk appetite under the Scheme is to have only exposure to quality bonds maturing before 30 September 2019. The current levels are set out in the Investment Guidelines.

These levels are kept under review and could be changed, along with market risk, on rollback to run-off. The broad principles are set out in the PPFM. The levels are documented in the Investment Guidelines provided as instructions to the Investment Managers. Exceptions approved by ALCo are recorded in an appendix of the Guidelines.

The Society is exposed to the risk of default of third parties which provide administrative services to the Society. The failure of any of these would lead to additional administration costs to find replacements, but not of a material nature.

Information for SUP App 2.15.4 – Credit and counterparty risk

Stock lending

The Society lends stock to third parties in order to increase the return on these investments. The lending is through an agreed agent, to parties of an agreed quality. The lent stock is backed by collateral of at least 102%.

Gilts are the only asset type that the Society is prepared to lend, or receive as collateral in current circumstances.

Stock lending is considered an acceptable means of improving returns. Any changes to this policy, including the type of collateral, must be reviewed and approved by the ALCo. The risk is further reduced by certain indemnities from the agent in the event of counterparty default or process failure.

5. Credit risk measurement

As described in "Risk monitoring and reporting" below, credit risk is measured by the Investment Manager to ensure that actual exposure by issuer and credit quality is maintained within appetite. This is achieved by using key risk indicators (KRIs) and the issuer and credit quality limits set out in the Investment Guidelines.

Under run-off, the following limits applied to securities other than gilts and securities issued by "AAA" rated governments:

Maximum investment in any other individual group or entity ("issuer limits")	% of Fixed Interest Securities within the Portfolio
Supranational and Government guaranteed "AAA" rated	5.00%
Other "AAA" rated	2.00%
"AA" rated	2.00%
"A" rated	1.40%
"BBB" rated	0.70%

All credit risks are measured and reported monthly to ALCo.

Counterparty assessment

The key measure of credit risk arising from counterparties is the credit ratings sourced from professional rating agencies. The Society relies upon the Investment Manager to assess the ratings, to provide ratings where they are not available from the major agencies and monitor any movements. The KRIs also highlight downgrades in ratings and any actual bond defaults. The Investment Manager is responsible for actively measuring and managing credit risk within the Bond portfolio.

Information for SUP App 2.15.4 – Credit and counterparty risk

6. Risk monitoring and reporting

Monitoring to ensure that the exposure to individual counterparties remains within the limits set by the Society is the responsibility of the Investment Manager and significant events are reported to the Society at the regular meetings held with management.

Risk Reporting is carried out monthly by the Risk Department, informed by KRIs maintained by the Actuarial Department. The Risk Report is reviewed bimonthly by the Asset and Liability Committee, and reported to the Business Executive Committee and the Board. The KRIs are designed to provide an early warning of increased risk and to highlight where exposure has exceeded or might exceed appetite. These then trigger mitigating actions where appropriate ("7. Risk mitigation" below provides more information).

As part of the Society's assessment of the adequacy of its financial resources, credit risk exposures are subject to stress testing and scenario analysis which form part of Solvency II SCR and ORSA valuations. The results of these are reported to the Board, Audit and Risk Committee, Executive Committee and Asset and Liability Committee (ALCo).

ALCo also receives monthly Investment Reports from the Investment Managers.

Stock-Lending counterparties are reviewed annually by ALCo.

7. Risk mitigation

For all credit risks except LBG, the Asset and Liability Committee is the key decision making body responsible for risk mitigation. Following review of reporting (as above), actions required to mitigate the risk are devised and responsibilities allotted. This may result in adjustments to policy or strategy.

For the LBG credit risk, the Board sets risk appetite and monitors appropriately.

Executive Committee reviews the actions being taken to mitigate material credit risks.

8. Systems and controls

Many of the activities involved in managing credit risk are carried out by BlackRock and Northern Trust to whom the investment management and custody services of the Society have been outsourced. In relation to the Society's unit-linked funds, State Street and Aberdeen Standard Investments have been appointed to provide global custody, investment accounting and management services. Oversight mechanisms to provide the Society with the required reassurance over the systems and controls operated by third parties include:

Information for SUP App 2.15.4 – Credit and counterparty risk

- Attendance at and presentations to the Asset and Liability Committee and Unit Pricing Committee;
- Regular meetings with Finance and Actuarial to review cashflow matching and other BlackRock activities and outputs;
- The Chief Investment Officer's role to manage Equitable Life's interests in respect of BlackRock, Northern Trust, State Street and Aberdeen Standard Investments;
- Provision of audit reports by State Street and Aberdeen Standard Investments, monthly exchange of information on procedures and investigation of errors.
- A Joint Investment Committee meeting with Aberdeen Standard Investments and Operational Group meeting with State Street and Aberdeen Standard Investments
- A Reassurance Governance Group meeting with LBG and quarterly questionnaires.

Sources of information for SUP App 2.15.4

Information on the Society's management of credit and counterparty risks is also provided by:

- the Society's policy on credit risk
- the Society's investment guidelines
- the Society's 2017 Annual Report and Accounts in
  - the section "Credit Risk" on page 10, and
  - note 15d "Credit Risk" on pages 74 to 75.

SUP App 2.15.5 - Operational risk

An explanation of how the firm will address any additional operational risks that may flow from the run-off of the with-profits fund including:

- any proposed changes to staffing arrangements for the run-off;
- an estimate of the cost of proposed operational changes including redundancy costs;
- any material outsourcing arrangements it proposes to enter into explaining how the firm will address any specific operational risks created by those arrangements.

Information for SUP App 2.15.5 – Operational risk

1. Ownership and governance

Operational Risk Governance

The Society operates a Risk and Control Self Assessment process (RCSA) which is the primary tool for identifying and assessing risks, particularly operational risks, and the controls in place to mitigate them. This process applies to both business areas and projects, and an attestation process is in place. Functional heads must attest quarterly that the risks in their area of responsibility have been identified and are properly controlled and operating effectively. Risks associated with staff reductions or other changes in staffing arrangements would need to be considered as part of the RCSA. In addition, risk workshops are held from time to time, for example to consider new risks associated with changes in the business such as new outsourcing arrangements.

Material operational risks identified from RCSA, risk workshops and other risk processes are passed to Executive Committee. The Committee is responsible for reviewing and assessing the adequacy of controls in place to mitigate these risks and for investigating risk events such as incidents or breaches to ensure that causes are properly identified and understood and that appropriate and timely remedial actions are undertaken. Executive Committee monitors the execution of the Society's Human Resources strategy including the implications of changes to the organisational design and/or staffing levels of the Society. Executive Committee is also responsible for reviewing the effectiveness of the Society's arrangements for treating its policyholders fairly.

The Society uses a Scenario Analysis-based approach to establishing capital requirements for operational risk. Scenarios are reviewed annually by the Executive Committee.

Information for SUP App 2.15.5 – Operational risk

Changes to staffing arrangements

Each Executive is responsible for identifying any additional operational risks that may flow from proposed changes to staffing arrangements. Material risks are referred to the Executive Committee.

2. Estimated cost of proposed operational changes including redundancy costs

Details of our 2018 costs and our projected costs for 2019 are provided in the Business Plan, where Redundancy costs are shown separately. Variances from the projected costs in the previous 3 year Business Plan and commentary on those variances are also provided by the Business Plan.

3. New outsourcing arrangements

IT services

The Society signed agreements with Atos and Lloyds Banking Group (LBG) in November 2012 for Atos to take over the provision of computer systems to Equitable Life.

The Society’s Third Party Management Policy and Framework is in place to manage the risks associated with outsourcing including the outsourcing arrangement with Atos.

Unit-linked business

Outsourcing agreements were signed with State Street and Aberdeen Standard Investments as part of the preparation for the recapture of the unit-linked business which took place in March 2015. State Street provides global custody and investment accounting services for unit-linked funds. Aberdeen Asset Management provides management of the Society’s unit-linked funds.

The Society uses subject-matter experts, including the Unit Pricing Committee (UPCo) and its Internal Audit Function to review pricing operations and to mitigate the risk of pricing errors.

4. Sources of information for SUP App 2.15.5

Information on the Society's operational risk management is also provided by:

- the Society's Risk Management Policy;
- Enterprise-wide Risk Management Framework**;**
- Risk and Control Self Assessment (RCSA) Guide**;**
- Third Party Management Policy and Framework**;**
- the Business Plan;
- the Society's Risk and Control Self Assessment (RCSA) for the third quarter of 2018.

SUP App 2.15.6 - Reinsurance risk
An explanation of how the firm will use and manage reinsurance, including:

- any new inwards or outwards reinsurance it proposes to enter into identifying, in each case, the proposed counterparty and the counterparty's relationship to the firm (if any); and
- managing the risk that the reinsurance will not perform as expected.

Information for SUP App 2.15.6 – Reinsurance risk

A new reinsurance contract would be entered into only for managing down existing risks, if it was in the interests of policyholders and in line with the risk framework.

In the event that there are no transitional arrangements to aid the UK's exit from the EU, and the subsidiary, ELI, is set up, a reassurance treaty would come into effect to reassure all Irish and German With-Profits liabilities from ELI to ELAS. The treaty is required to enable the Society to continue to administer its Irish and German business and to service its policyholders. This treaty would cease under the Scheme.

In November 2016, the Society entered into a new reinsurance treaty with Swiss Re to remove mortality risk from most of the Society's term assurance and flexible life assurances recaptured from LBG in 2015. This largely removed mortality risk from the balance sheet.

The Society's management of reinsurance risk is part of the Society's insurance risk management.

SUP App 2.15.7(1) - Corporate governance
A description of any changes to the firm's corporate governance as a consequence of closure and run-off.

Information for SUP App 2.15.7(1) – Corporate governance

No information is provided given the Society closed to new business in December 2000.

SUP App 2.15.7(2) - Cost charges
An explanation of how the costs charged to the with-profits fund may change during run-off.

Information for SUP App 2.15.7(2) – Cost charges

All of the expenses and taxation of the with-profits business fall to the with-profits policyholders, and directly reduce the amount available for distribution to with-profits policies. In addition, any profits and losses arising from expenses or tax on the rest of the business, that is not reassured, also flow through to with-profits policyholders.

Expenses and tax will typically be applied to with-profits policies by an appropriate deduction from investment returns otherwise available to increase Policy Values and their equivalents. This allows all with-profits policies to share in the expense performance, profits and losses, roughly in proportion to their share of the with-profits fund. The expense deduction has been 1% per annum for many years, and this level is reviewed regularly to ensure it remains appropriate. This level charge has funded an expense reserve. The intention is that this reserve plus future 1% per annum deductions will be sufficient to meet future expenses, even as these become a higher percentage of the fund over time. This approach allows the costs of administration to be spread across different generations of policyholders fairly.

A review of expense charges was carried out in 2018, and the results presented to the Board in December 2018. This concluded that no change in the expense deduction was required.

The Society's policy on cost charges is explained in section 5.2.2 "Expenses and taxation" of the PPFM.

SUP App 2.15.7(3) - Guarantee charges

An explanation of any changes the firm will make, as a consequence of closure, to any charges for guarantees including:

- the circumstances in which those charges may be varied in future;
- the manner by which the level of any appropriate variation to those charges may be determined.

Information for SUP App 2.15.7(3) – Guarantee charges

When setting Policy Values, the Society currently makes a charge of 0.5% per annum to provide solvency capital and to meet the expected cost of guarantees, now and in the future.

For the short-term at least, changes to Policy Values are expected to be net of a charge for guarantees of 0.5% each year. This charge can be expected to increase if the cost of guarantees increases significantly (for example as a result of adverse investment conditions), or solvency capital requirements increase.

The level of the charge for capital and cost of guarantees will be kept under regular review by the Board before deciding any changes to Policy Values. As stated in the

PPFM if the expected charge exceeds 1.5% per annum, the change would be communicated to policyholders.

A review of guarantee charges was carried out in 2018, and the results presented to the Board in December 2018. This concluded that no change in the charge for guarantees was required.

The Society's policy on guarantee charges is explained in section 5.2.3 "Charge for capital and cost guarantees" of the PPFM.

SUP App 2.15.7(4) – With-profits target ranges

An explanation of any actual or potential changes in the maturity or surrender payment target ranges that the firm will apply to determine benefits under its with-profits policies.

Information for SUP App 2.15.7(4) – With-profits target ranges

There are currently no planned changes in the methodology applied by the Society to determine benefits under its with-profits policies.

The Society's current policy on setting payout levels is described in section 4.2.1.1 "Setting the level of payouts" and section 4.2.1.2 "Setting the level of Capital Distribution Amount" of the Society's PPFM.

SUP App 2.15.7(5) – Smoothing

An explanation of any actual or potential changes in the firm's smoothing policy as a consequence of closure and run-off.

Information for SUP App 2.15.7(5) – Smoothing

There have been no changes in the Society's smoothing policy in recent years and no changes are planned.

The Society's current policy on with-profits smoothing is described in section 6 "Smoothing" of the Society's PPFM.

SUP App 2.15.7(6) – Projection rates
An explanation of changes to the firm's projection rates as a consequence of closure.

Information for SUP App 2.15.7(6) – Projection rates

Since closure to new business in December 2000, the Society's with-profits fund has moved from a fund predominately invested in equities and property to a fund that is nearly all invested in fixed interest securities. Correspondingly, the Society's projected rates of returns for with-profits benefits have been reduced to reflect the lower rates of return provided by fixed interest securities.

The Society's projected rates of return for illustrations of pension with-profits benefits, before allowing for future inflation, are currently 0.5%, 3.5% and 6.5% p.a. (compared to the maxima of 2%, 5% and 8% p.a. in COBS 13 Annex 2 "Projections" in the FCA Handbook).

For Statutory Money Purchase Illustrations currently, the projected rate of return is 3.5% p.a. for with-profits benefits (equivalent to a projected long-term bonus rate of 2% p.a. net of the 1.5% deduction for expenses and guarantee charge).

The projection rates were approved by the Society's Executive Committee (ExCo) in March 2018.

SUP App 2.15.7(7) – Surrender deductions
Details of any new deductions to be made from the firm's surrender payments together with an explanation as to how those deductions are consistent with

- Principle 6 (Customers' interests)
- COBS 20.2.11G to COBS20.2.16R (Amounts payable under with-profits policies: Surrender payments)

Information for SUP App 2.15.7(7) – Surrender deductions

The Society has no plans to introduce any new deductions from surrender payments, and has not introduced any new surrender deductions in recent years.

Since April 2014, a zero financial adjustment has applied to the Policy Value and the Capital Distribution Amount in the event of a non-contractual termination. For group pension scheme bulk surrenders of more than £2m, a scheme-specific financial adjustment may be calculated.

The Society reserves the right to re-introduce a financial adjustment at a later date if required by future economic or other relevant circumstances.

SUP App 2.15.7(8) – Clusters of MVR-free dates

If there are groups of unitised with-profits ("UWP") policies in the with-profits fund with a similar market value reduction free date, an explanation as to whether:

- the firm expects surrenders to peak around any of those dates; and
- if it does, how the firm proposes to deal with those peaks.

Information for SUP App 2.15.7(8) – Clusters of MVR-free dates

- Personal Investment Plans have a guarantee date at the 10th anniversary of the plan effective date and at each 10th anniversary thereafter.
- At each of these 10-yearly guarantee dates, the full with-profits benefits can be withdrawn from a Personal Investment Plan without any financial adjustment (market value reduction).
- The next potential cluster of Personal Investment Plan maturities on a guarantee date could be at the 20th plan anniversaries in 2019.
- At 30 September 2018, the total guaranteed value of Personal Investment Plan benefits was c£9m and with a corresponding total claim value (Policy Value plus CEF of c£13m.
- A cluster of maturities at the 20th anniversary of these plans in 2019 would have no significant impact on the Society's with-profits fund. If the Scheme is close to its effective date, it is unlikely there would be significant levels of termination at their 20th anniversaries.

SUP App 2.15.7(9) – Open Market Option for annuity purchase

Details of the information that the firm gives to its with-profits policyholders to use policy proceeds to purchase an annuity on the open market when the relevant contracts or schemes vest or mature.

Information for SUP App 2.15.7(9) – Open Market Option for annuity purchase

Many policyholders now take benefits in the form of cash or as partial withdrawals from their policies. This change has occurred since the Pensions Freedom Reforms introduced from 6 April 2015.

The Society has an arrangement with Canada Life where, as part of the information provided to policyholders taking retirement benefits, an illustration of an annuity purchased with Canada Life is provided to the Society's policyholder. The Society does not advise policyholders to purchase their annuity benefits with Canada Life, and any arrangement fee from Canada Life is currently rebated in full to enhance the annuity secured with Canada Life.

A monthly benchmarking process forms part of the contract with Canada Life. This compares Canada Life’s annuity rates with the rest of the market.

Information for SUP App 2.15.7(9) – Open Market Option for annuity purchase

The Society no longer writes annuity business, but highlights the availability of open market options to other providers who can provide annuities or drawdown options.

SUP App 2.15.7(10) – Mis-selling costs

Details of how the firm will deal with any potential mis-selling costs that may arise in future.

Information for SUP App 2.15.7(10) – Mis-selling costs

Mis-selling costs are paid from the with-profits fund.

The likelihood and potential impact of future significant mis-selling costs is now relatively small given that the Society closed to new business in December 2000 and that substantial reviews of potential mis-selling (e.g. for income drawdown plans and personal pension plans) were completed several years ago.

SUP App 2.15.7(11) – Capital distribution

An explanation of how the firm:

- anticipates capital will become available for distribution to policyholders;
- will ensure a full and fair distribution of the closed fund including any inherited estate;

  including details of:
  - how the firm plans to provide in the long term for annuity payments on any with-profits and non-profit policies under which benefits have vested; and
  - how the firm will address future adverse circumstances in relation to these annuity payments (e.g. increased annuitant longevity).

Information for SUP App 2.15.7(11) – Capital distribution

1. Distributing the Society's assets

It is the Society's plan that all of its assets, after providing for its contractual liabilities (including those to holders of non-profit policies and other creditors), will be distributed as fairly and as soon as possible amongst the holders of its with-profits policies over the lifetime of those policies. This means that amounts distributed amongst with-profits policies can exceed the contractual guaranteed entitlements of with-profits policyholders. Any amounts distributed amongst with-profits policies in excess of contractual guaranteed entitlements are decided after allowing for the requirement to meet the Society's contractual obligations as they fall due, and the need for the Society to maintain an appropriate level of solvency capital to operate its business.

In determining bonus policy, the Society aims to balance the objectives of continuing to meet its obligations to policyholders and other creditors as they fall due and of distributing the Society's assets, including the solvency capital, over the lifetime of its policies as fairly as possible. Consideration is given to the overall financial position of the Society which is affected by many things including, inter alia, investment returns and outlook, actual and expected expense levels, the expected cost of guarantees, miscellaneous profits and losses (including those from the non-profit business) and changes in the level of provisions. The rate at which surplus is distributed may vary depending on the Society's requirement for solvency capital, and the general level of uncertainty (for example, in the various provisions). The rate of capital distribution is set in accordance with the Society's Capital Distribution Framework.

For the foreseeable future, any new distributions of surplus will be made in non-guaranteed form, and there is no expectation of any further reversionary bonus being awarded in the near to medium term. This applies across all product types and all territories. This approach aims to maximise the likelihood of the Society being able to meet all its future contractual liabilities.

2. Policy Values

For Recurrent Single Premium (RSP) policies, the Society has for many years used the concept of the "Policy Value" and the Society's administration system generates a Policy Value in respect of each policy. A Policy Value represents a smoothed investment return (net of charges for expenses and tax and for the cost of guarantees) applied to the premiums paid into a policy and is used to determine payout levels in relation to with-profits benefits. Types of policy that do not use the concept of the Policy Value apply methodologies that are designed to have a similar effect.

The Policy Value is not a guaranteed amount - it can be reduced as well as increased, and it can be more or less than the value of guaranteed benefits under a policy. Policy Values are calculated at benefit level, and each premium net of explicit charges adds to the Policy Value. Withdrawals reduce the Policy Value.

Information for SUP App 2.15.7(11) – Capital distribution

The levels of Policy Values are kept under regular review, and the Board may change them at any time if circumstances require it, though efforts are made to avoid frequent changes. Different rates can apply to different policy classes where it is judged fair to do so (for example, applying a net of tax rate for life policies). The Board may at its discretion choose to vary the rates awarded according to other factors (such as age or term or level of guarantee) if this is judged to result in a fairer allocation.

3. Capital Distribution Amount

Since 1 April 2011, the Policy Value has been supplemented by an enhancement for the distribution of solvency capital, the Capital Distribution Amount. This enhancement is essential to the Society's strategy to distribute assets as fairly and as soon as possible over the lifetime of policies and as fairly as possible between different generations of maturing with-profits policies. The level of the Capital Distribution Amount and the way it is applied is at the discretion of the Society and the Board keep both under regular review so as to be as fair as possible to those policies leaving the with-profits fund and those remaining in it.

The rate of Capital Distribution is set in accordance with the Society's Capital Distribution Framework.

The level of Capital Distribution will depend, among other things, on the following factors:

- intergenerational fairness and the development of the tontine
- the current and future anticipated solvency position
- the current risk environment
- policyholder expectations both in the medium and longer term
- assumptions and limitations underlying the DDM not accurately reflecting events which might occur in practice. Alternative feasible assumptions could be made, leading to different levels of CEF.
- whether the current solvency coverage is temporarily high or low, eg as a result of, for example, unusual economic conditions.
- potential effect of the level of CEF on policyholder behaviour and consequent impact on the Society's capital position.
- avoidance, as far as possible, of multiple CEF reductions.

The Society regularly reviews the appropriateness of the Capital Distribution Amount, the Capital Distribution Framework, and the way the Society determines payouts. The Capital Distribution Amount can be varied or withdrawn at any time without prior notice to policyholders.

Under the Scheme, all assets would be distributed to with-profits policyholders before converting their benefits to unit-linked. The fairness indicators used to assess the benefits of the Scheme are provided in the paper entitled Application of Fairness Indicators.

Information for SUP App 2.15.7(11) – Capital distribution

4. Equity between groups and generations of policyholders

The Society aims to set bonuses and payout levels which are fair across different groups and generations of policyholders. Profits and losses are typically shared across the whole of the with-profits business, not just among the policies concerned. For example, the cost of administration is shared across the whole of the with-profits business. Changes to Policy Values plus any Capital Distribution Amount and their equivalents are often the same for all policies within a particular class, but it is possible that they will vary between different groups and generations of policyholders.

5. Business Risks – Annuitant Longevity Risk

With-profits policyholders share in all the profits and losses of the Society. These are passed on through the Policy Value system. The Board aims to manage risk where possible to minimise any negative impacts on policy payouts and so that the Society can continue to be able to meet its contractual obligations to policyholders and other creditors as they fall due.

In February 2016, the Society completed the transfer of most of its remaining non-profit and unit-linked annuities to Canada Life. The Society’s remaining non-profit annuity portfolio is reinsured with Scottish Widows Limited. The Society therefore has almost no exposure to annuitant longevity risk.

No new annuity policies are now written when existing Equitable Life policyholders take the proceeds of their retirement policy. This follows an arrangement with Canada Life described above in the information provided for "SUP App 2.15.7(9) – Open Market Option for annuity purchase".

6. Sources of information for SUP App 2.15.2

Information on the Society's management of capital distribution and business risks is also provided in the Society's PPFM and, in particular, in

- Section 4 "Principles";
- Sections 5.1 "Bonus Policy - Principles" and 5.2 "Bonus Policy - Practices";
- Section 9 "Business Risks".

SUP App 2.15.7(12)

Differences between the run-off plan and PPFM following the closure of the with-profits fund

Information for SUP App 2.15.7(12)
No information is provided given the Society's with-profits fund closed to new business in December 2000.

SUP App 2.15.7(13)

Expansion of other business following closure of the with-profits fund

Information for SUP App 2.15.7(13)
The Society did not expand any other aspects of its business following the closure of its with-profits fund in December 2000.

SUP App 2.15.8A - Financial projections

A Solvency II firm should include the following information:

(1) a forecast revenue account for the with-profits fund, in accordance with PRA Rulebook: Non-Solvency II firms: Run Off Operations 6.1(3)(a);

(2) a forecast summary balance sheet and "eligible own funds" as defined in the PRA Rulebook: Glossary and any notional SCR or the with-profits fund, in accordance with PRA Rulebook: Non-Solvency II firms: Run Off Operations 6.1(3)(b);

(3) "eligible own funds", "MCR" (as those terms are defined in the PRA Rulebook: Glossary), forecast summary balance sheet and SCR for the entire firm, in accordance with PRA Rulebook: Non-Solvency II firms: Run Off Operations 6.1(3)(b) and 6.13(c) to (e);

in each case for at least a three-year period, beginning on the date of closure.

Information for SUP App 2.15.8A – Financial projections
No information is provided given the Society's with-profits fund closed to new business in December 2000.

SUP App 2.15.12
Details of: (1) intra-group balances held by with-profits fund; (2) group company investments held by with-profits fund; and (3) guarantees given by the firm; which, in each case, have value in excess of 5% of firm's gross technical provisions

Information for SUP App 2.15.12
The Society's with-profits fund has no intra-group balances, no group company investments, and no (non-policy) guarantees given by the Society which have a value of more than 5% of the Society's gross technical provisions.

SUP App 2.15.13 - Other relevant information
Any other information that is considered relevant to the run-off of the with-profits fund

Information for SUP App 2.15.13
All relevant information is provided elsewhere in this document.