

Sun Life Assurance Company of Canada (U.K.) Limited (“SLOC”)

# The Directors’ Report to Plan-holders

SLOC With-Profits Fund in 2020



Sun Life Financial  
of Canada

## Introduction

This report explains:

- How we managed the SLOC With-Profits Fund (the “Fund”) in 2020.
- Whether we complied with the Principles and Practices of Financial Management (“PPFM”) that sets out how we manage the Fund, how we respond to long-term economic changes, and how we meet plan-holders’ needs.
- How we made key decisions during 2020.
- Whether we took plan-holders’ expectations into account appropriately.

We have taken advice from our With-Profits Actuary and there is a separate With-Profits Actuary’s statement at the end of this report.

## Summary

We considered the advice and reports of the With-Profits Committee and the With-Profits Actuary, and are satisfied that, for the financial year 2020:

- We managed the Fund in line with the PPFM.
- We made key decisions and used management discretion in a way that was consistent with the PPFM.
- We have taken into account all plan-holders and their rights, interests and expectations properly, as described in the PPFM.
- We have treated plan-holders fairly and, where there are competing or conflicting interests and expectations of different groups of plan-holders, we have complied with the PPFM.

## Investment management

### Information for endowment and whole of life plan-holders

The investment strategy of the Fund is to provide the highest potential investment return whilst preserving the financial condition of the Fund and paying any guarantees promised to plan-holders when these are due. To do this the Fund invests mainly in a diverse range of longer-term assets. These include government and other high-quality bonds, which are loans to the UK and foreign governments and companies that are raising money. These assets are referred to as fixed interest investments because we know the income that we expect to receive from them, although their market value will change over time.

We also invest some of the Fund in company shares and property. Owning shares means that the Fund is a part-owner of these companies and so receives a portion of their profits. Property investments usually receive income in the form of rent. Both of these types of asset have the potential to provide investment growth but also carry a higher risk of their value going up or down.

We consider the Fund to have been financially strong throughout 2020 and have therefore maintained the target for the portion of the Fund invested in higher risk company shares and property at 35%.

The table below shows how much we invested in different types of assets for endowment and whole of life plans.

**Table 1**

Asset class	End 2019	End 2020
Fixed interest and other assets *	61.6%	61.2%
UK company shares	19.8%	18.6%
International company shares	7.7%	7.9%
Property	8.7%	9.0%
Cash	2.2%	3.3%

\*Other assets include plan loans, where policyholders have borrowed against the early exit value of their plan.

We review these amounts regularly to make sure we continue to meet our aims.

The Fund’s net return in 2020 was +4.5% (after tax and investment expenses).

Returns by asset class over 2020, before tax and expenses, are shown below and compared to market performance.

**Table 2**

Asset class	Fund	Market
Fixed interest	+8.9%	+7.1%
UK company shares	-7.9%	-9.8%
International company shares	+11.6%	+13.4%
Property	-0.8%	-0.1%
Cash	+0.4%	+0.2%

### Information for pension plan-holders

The investment strategy of the Fund in respect of pensions business is to provide a stable investment return through investment in fixed interest investments. It is necessary to take account of the financial condition of the Fund and the minimum guaranteed interest rates applicable to each type of plan during the period before retirement, and also the cash flow requirements of the plans. During 2020, we made no material changes to the investment strategy for the Fund’s pensions business. It continues to provide a stable return through investment in fixed interest assets and cash. We continue to invest in derivatives that give the Fund a fixed rate of interest; this protects the Fund from fluctuations caused by changes in interest rates. We also invest in fixed interest bonds held in euros. This helps to protect the Fund’s Irish Pension Plans from fluctuations caused by changes in

currency exchange rates. Most pension plan-holders have benefits fixed at guaranteed levels, so are not affected by the investment strategy.

## Management of payouts – whole of life and endowment plans

A key part of management discretion is to decide the annual and final bonuses paid to plan-holders.

**Smoothing** – In determining bonus rates, we use a process known as ‘smoothing’, which provides a cushion against the short-term ups and downs of investment markets. We do this by reinvesting some of the profits from ‘up’ years to smooth out any losses in the ‘down’ years. Smoothing, however, cannot protect against the impact of persistently low investment returns.

**Distributing the Fund's excess assets** – Since 2016, we have distributed all of the Fund's excess assets to plan-holders by enhancing the benefits for all whole of life and endowment plans. It is possible, in sufficiently adverse circumstances, that we could reverse these enhancements.

**Calculating payouts** – Bonus rates depend on both the past and expected future performance of the assets. From April 2020, final bonus rates were reduced slightly due to our lower expectations for future returns from the assets in the Fund.

Following the market volatility caused by the Covid-19 pandemic, we regularly monitored investment conditions to determine whether we should need to reduce plan payouts any further. Due to the continued strength and the smoothing aims of the Fund, we decided to make no change.

Overall, there was a modestly positive return over 2020 (fixed interest assets and international equities delivered positive returns, which were partially offset by negative returns on UK equities and property). However, long-term interest rates reduced significantly in 2020 and so our expectations of future investment returns have reduced.

To protect the Fund in the long term, we cannot maintain the current levels of final bonus. To address this, we have implemented a further reduction to final bonuses from April 2021. We will continue closely monitoring the situation over 2021.

**Early exit values** – We review early exit values to make sure they meet the PPFM objectives. For whole of life and endowment plans, we use the prospective value of benefits to determine fair early exit values. Over 2020, early exit values were on average approximately 97% of the prospective value of benefits for all life plans. Similarly to payouts, we did not make an immediate change to early exit values following Covid-19, but we have implemented a reduction to them from April 2021 to protect the Fund in the long term.

The With-Profits Actuary gave advice to the With-Profits Committee about the impact of the recommended bonus scales and basis for early exit values.

## Management of payouts – pension plans

Interest rates for Individual Money Purchase plans did not change in 2020. Interest rates on premiums paid before 1 April 2018 remain at 4.25% a year. Interest rates on premiums paid on or after 1 April 2018 remain at 2% a year for business written in the UK and 1% a year for business written in Ireland.

We use two different interest rates for Personal Pension Plans. A lower interest rate (currently 0% a year) applies to contributions paid in the first 12 months\* and a higher rate (1.25% a year) to all other contributions. We did not change either rate in 2020.

(\*If the contribution level increases later on, this lower interest rate also applies to the increased portion of the contribution for the first 12 months after the increase.)

The interest rate for other plans also stayed the same (Individual Transfer Plans at 6% a year, Deferred Annuity at 4% a year and the Staff Additional Voluntary Contributions at 4.25% a year) where these rates are set to honour the minimum guaranteed interest rates.

## Management of expenses

In line with the PPFM, and with the advice of the With-Profits Actuary, we continued to charge the Fund for its fair share of the company's ongoing costs. In 2020, we paid out 0.6% of the Fund in expenses.

## Revisions to the PPFM over 2020

The changes to the PPFM over 2020 include:

- Removing references to the Confederation Life Fund. The commentary was historical and has no impact on the Fund.
- Adding a reference to the expense cap, which is an agreement between the Fund and the Company to limit the size of certain expenses that the Company can charge to the Fund, allowing for movements in the Retail Price Index.
- Improving descriptions of smoothing and the distribution of Excess Assets to better reflect practice since the move to a prospective method for determining bonuses.

## Further information

If you would like a copy of the PPFM referred to in this report, or the latest bonus notice which briefly explains how we manage the Fund, please visit our website [sloc.co.uk](http://sloc.co.uk) or call us on 0345 072 0223 (or 01256 841414 from a mobile phone).

## Report of the With-Profits Actuary of the Fund to the with-profits plan-holders

As the With-Profits Actuary (“WPA”) for SLOC With-Profits Fund (“the Fund”), it is my responsibility to advise the Board on the key aspects of discretion that it exercises on with-profits business in the course of its management of the Fund.

Under the rules of the Financial Conduct Authority (“FCA”), I am required to report annually to the with-profits plan-holders of the Fund on the Board’s exercise of discretion in relation to that business for the period covered by the report, and whether, in the course of the exercise of discretion, the Board has taken account of the interests of the with-profits plan-holders in a reasonable and proportionate manner.

I have considered the annual report from the Directors of the Fund to with-profits plan-holders. In my opinion:

- The report is a fair reflection of how the with-profits business has been managed during the year.
- The discretion exercised by the Board in respect of the Fund in 2020 may be regarded as having taken the interests of the with-profits policyholders into account in a reasonable and proportionate manner.
- SLOC has, in all material respects, complied with the Principles and Practices of Financial Management in 2020.

In reaching this opinion, I have relied upon the accuracy and completeness of the data and information provided to me by SLOC. I have also considered the relevant rules and guidance issued by the FCA and the Prudential Regulation Authority, and applicable standards issued by the Financial Reporting Council and the Institute and Faculty of Actuaries.

Oliver Gillespie, FIA  
Principal, Milliman LLP  
With-Profits Actuary for SLOC With-Profits Fund  
29 March 2021