

AVC Monitoring Report

Clwyd Pension Fund

November 2023

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A business of Marsh McLennan



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AVC Valuation



Overview – Valuation

	Clwyd Pension Fund (the “Fund”)				
AVC Provider	2023 Asset Value	2022 Asset Values	Unit-linked / With profits	Guarantees applying	Number of Members ²
Utmost	£282,002	£296,657	Unit-linked	No guarantees applied	43
Prudential ¹	£6,332,493	£6,329,825	Unit-linked (c.52%) With-profits (c.48%)	With profits guaranteed bonuses depending on date purchased	Unit-linked (375) With-profits (290)
Overall Total	£6,614,495	£6,626,482			

Source: Prudential, Utmost.

Note: Utmost 2022 values as at August 2022. Utmost 2023 values as at November 2023. Prudential 2022 values as at July 2022. Prudential 2023 values as at March 2023.

- 1) The asset value includes Terminal Bonus (2022 c. £849,380 and 2023 c.£739,691) applied for the With Profit funds. This bonus, which is only applied at the time benefits become payable, is not guaranteed. The asset value also includes any Market Value Reduction (MVR).
- 2) Member splits: Utmost data as at November 2023. Prudential data as at March 2023.

Performance and charges

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Prudential – Fund Performance (unit linked)

Prudential have confirmed that the following unit-linked funds are invested in by members of the Fund:

Fund	Annualised Performance (%)	1 Year (%)		3 Year (% p.a.)		5 Year (% p.a.)	
		Benchmark	Fund	B'mark	Fund	B'mark	Fund
UK Equity Passive	FTSE All-Share Index	2.2	2.9	12.9	13.8	4.4	5.0
UK Equity	FTSE All-Share Index	-0.9	2.9	12.0	13.8	3.4	5.0
Global Equity	Composite	0.2	2.3	13.3	13.8	4.6	6.1
International Equity	Composite	1.8	1.1	15.0	13.7	6.4	7.7
Positive Impact	MSCI ACWI Index	1.4	-0.9	14.4	16.0	n/a	n/a
Discretionary	Composite	-4.4	-0.0	8.7	9.1	3.6	5.1
Dynamic Growth I	Composite	-5.1	-4.8	2.4	1.6	1.6	1.8
Dynamic Growth II	Composite	-4.2	-3.7	4.4	3.5	2.4	2.6
Dynamic Growth IV	Composite	-2.3	-1.4	8.3	7.5	3.9	4.3
Fixed Interest	iBoxx Sterling Gilts Index	-16.4	-17.0	-9.0	-9.4	-3.2	-3.2
Index-Linked	iBoxx UK Gilt Inflation-Linked Over 5 Year Index	-30.1	-30.1	-8.7	-9.1	-4.0	-4.1
Long-Term Gilt Passive	iBoxx Sterling Gilts (15+) Index	-29.9	-29.6	-16.8	-16.3	-6.8	-6.3
Cash	SONIA 1W	1.7	2.2	0.3	0.7	0.2	0.6
Deposit	Bank of England Base Rate	2.1	2.3	0.8	0.9	0.8	0.8

Source: Prudential. Performance as at 31/03/2023 net of TER for funds invested by members.

Note: Funds that have performed within an acceptable tolerance range or outperformed are highlighted green. Funds that have underperformed are highlighted orange.

Comments and Considerations

There has been mixed performance for the unit linked funds over the last 5 years, with some funds underperforming their benchmarks

Prudential– Fund Charges (unit linked)

Prudential have confirmed that the following unit-linked funds are invested in by members of the Fund:

Charges to 31 March 2023	AMC (% p.a.)	TER (% p.a.)	Transaction costs (% p.a.)
UK Equity Passive	0.55	0.57	0.03
UK Equity	0.65	0.66	0.01
Global Equity	0.65	0.67	0.06
International Equity	0.65	0.69	0.12
Positive Impact	0.65	0.66	0.07
Discretionary	0.65	0.70	0.11
Dynamic Growth I	0.62	0.63	-0.02
Dynamic Growth II	0.62	0.63	0.00
Dynamic Growth IV	0.62	0.63	0.01
Fixed Interest	0.65	0.66	-0.04
Index-Linked	0.65	0.66	0.44
Long-Term Gilt Passive	0.55	0.56	0.04
Cash	0.55	0.55	0.00
Deposit	N/A*	N/A*	0.00

Source: Prudential. AMC and TERs as at 31/03/2023. Transaction costs as at 31/12/2023 as the latest available. TER covers all costs to the provider.

*There are no explicit charges for the Deposit Fund.

In addition, Prudential offer several other fund options, including a lifestyle option.

Fund Performance and Charges (with profits)

Fund	Annualised Performance (%)	1 Year (%)		3 Year (% p.a.)		5 Year (% p.a.)	
	Benchmark	Fund	B'mark	Fund	B'mark	Fund	B'mark
Prudential With-Profits	N/A	4.5	-	6.9	-	4.9	-

Source: Prudential. Performance as at 31/03/2023 and reflects average overall yield % per year (including terminal bonus).

Charges to 31 December 2022	AMC (% p.a.)	TER (% p.a.)	Transaction costs (% p.a.)
Prudential With-Profits	1.0%	1.0%	0.20%

Source: Prudential as at 31/12/2022.

Comments and Considerations

The with-profits fund has seen positive performance, over the long term, noting that with-profits funds provide smoothed performance. In 2023, the regular annual bonus declared was 1.50%.

Utmost – Fund Charges & Performance

Utmost have confirmed that the following unit-linked funds are invested in by members of the Fund:

Charges to 31 March 2023	AMC (% p.a.)	TER (% p.a.)	Transaction costs (% p.a.)
UK Equity	0.75	0.75	0.02
Managed	0.75	0.75	0.01
Multi-Asset Growth	0.75	0.75	0.00
UK Government Bond	0.50	0.50	0.00
Money Market	0.50	0.50	0.00

Source: Utmost as at 31/03/2023. TER covers all costs to the provider.

The table below shows performance to 31 March 2023:

Fund	Annualised Performance (%)	1 Year (%)		3 Year (% p.a.)		5 Year (% p.a.)	
		Sector Comparator	Fund	Sector	Fund	Sector	Fund
UK Equity	ABI UK All Companies	1.5	-1.6	13.6	12.3	3.9	2.5
Managed	ABI Mixed Investments (40-85%)	-1.9	-4.2	9.3	8.1	4.0	3.6
Multi-Asset Growth ¹	ABI Flexible Investment	-4.8	-3.1	8.9	10.7	n/a	n/a
UK Government Bond	ABI UK Gilts	-16.5	-17.9	-9.6	-8.9	-3.4	-3.1
Money Market	ABI Deposit & Treasury	1.8	1.6	0.4	0.8	0.3	0.6

Source: Utmost, from Provider website. Performance as at 31 March 2023 net of fees for funds invested by members.

Note: Funds that have performed within an acceptable tolerance range or outperformed are highlighted green. Funds that have underperformed are highlighted orange.

¹) Performance not available for 3 and 5 years. Fund inception is 01/01/2020.

Comments and Considerations

Performance for the unit linked funds has been broadly in line with or above the sector comparator over the last 5 years. More details on the use of ABI sectors as comparators and potential drawbacks are shown in the appendix.

Mercer Commentary – AVC Providers



Prudential Assurance Company

Unit linked

As at April 2023	https://www.pru.co.uk/existing-customers/products/additional-voluntary-contributions/
Ownership and background	Prudential is the Life & Pensions provider within the M&G Group. With profits funds are offered alongside a range of mutual funds and bespoke segregated and pooled mandates.
Current issues/recent developments	Service performance in 2022 improved towards the end of the year with the majority of processes being completed within SLA and call response times much reduced. The focus is now on maintaining these levels whilst looking to make further improvements. A key focus in 2023 is to increase the level of on-line data provision and interaction with clients that will include the phased roll out of a self-service website.

Prudential Assurance Company

With Profits Funds

As at April 2023	Prudential With-Profits Fund Investment Guide
Ownership and background	Prudential is the Life & Pensions provider within the M&G Group. With profits funds are offered alongside a range of mutual funds and bespoke segregated and pooled mandates.
With Profits Fund	Prudential Assurance Company Ltd With-Profits Sub-Fund is open and is the largest with profits fund in the UK.
Management of With Profits fund	The Prudential Portfolio Management Group, part of the M&G Treasury and Investment Office, is responsible for the strategic and asset management of the with profits funds. Assets are managed by a range of external managers together with M&G Investment Managers. Governance oversight is provided by the With Profits Committee. The Committee is appointed by the Prudential Assurance Company Board and will have at least three members, all independent and external to PAC.
Current issues/recent developments	Service performance in 2022 improved towards the end of the year with the majority of processes being completed within SLA and call response times much reduced. The focus is now on maintaining these levels whilst looking to make further improvements. A key focus in 2023 is to increase the level of on-line data provision and interaction with clients that will include the phased roll out of a self-service website.

With Profits Funds	Financial Strength	Future Performance	Transparency
Prudential Assurance Company Ltd With-Profits Sub-Fund (See slide in Appendix for more info)	5	5	5

The ratings shown above were originally prepared by AKG Financial Analytics Limited (AKG), and are contained within AKG's 2022 UK Life Office With Profits Report. They are shown here with AKG's prior consent. Further information on AKG's With Profits Report is available at: <https://www.agg.co.uk/information/reports/with-profits-reports> and in the appendix.

Utmost Life & Pensions

Overview

As at April 2023	Home (utmost.co.uk)
Ownership and background	ULP was established in 2017 by Utmost UK Group Holdings Ltd. (UUGH) as a newly authorised UK life company 'run off' specialist – expected to be the operational base for further acquisitions of traditional books of life business. The first of these transactions was announced in June 2018 with the agreement with Equitable Life to transfer all of Equitable's business to ULP – which completed on 1 January 2020 and significantly increased ULP's size
With Profits Fund	Equitable With Profits Fund. Immediately prior to their transfer to Utmost, the Equitable with profits policies were converted to unit linked funds. The company's growth focus includes enhancing its product offering and resources were focused on this in 2019, with a view in particular to widening the choice available to customers seeking to access their pension savings.
Management of With Profits fund	JP Morgan Asset Management is Utmost's investment partner, responsible for the design and management of the unit linked fund range which has been expanded to include a Flexible Drawdown product.
Current issues/recent developments	Response times to requests for information can be lengthy. In common with most of their peers, updates in respect of developments in respect of the fund range are intermittent.

Next Steps

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Next Steps

It is recommended that AVC members are sent a communication to remind them of their AVCs, the purpose of AVCs and the choices available to them.

It should be noted that members in with-profits funds with Prudential have terminal bonuses applying on their policies, which are not guaranteed. Market Value Adjustments may also be applied at the point of withdrawal. Members should be periodically reminded of characteristics of with-profits funds and the risk of disinvesting before maturity.

We also recommend continuing annual monitoring of the AVCs.

Date of next review
November 2024

More generally, we recommend that the Fund regularly reviews the AVCs held, to check whether members have drawn on their Defined Benefit funds. If this is the case, they may benefit from a reminder that their AVCs are still available and invested.

Please note: This report does not contain regulated investment advice or regulated non-investment related advice. It sets out recommendations deemed appropriate based on the analysis provided in this presentation. Any actions to be taken from these recommendations need to be accompanied by regulated advice in accordance with Section 36 of the Pensions Act 1995.

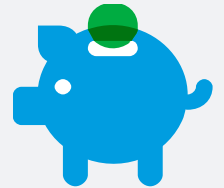
Appendix



Unit Linked Funds

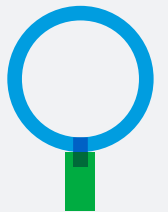
What are Unit Linked Funds?

- Members purchase units in funds which invest according to their particular objective.
- Returns to members are in the form of changes in the value of the unit price.
- Members realise a profit or a loss from an investment when the units in the fund are sold.
- Within the Clwyd Pension Fund, members are invested in 14 unit linked funds with Prudential and 5 with Utmost.



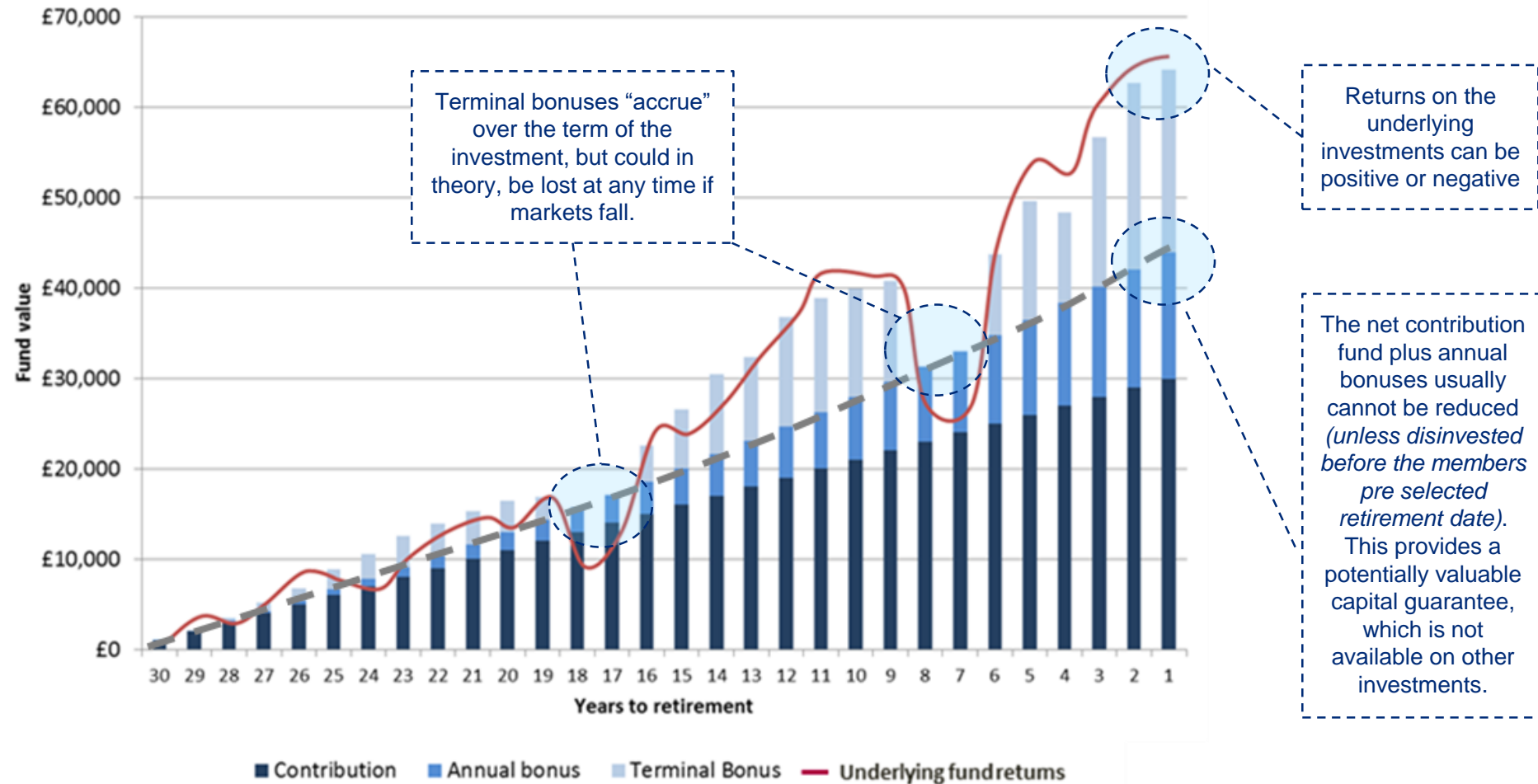
What should we consider when reviewing?

- Tracking error and performance, relative to stated benchmarks, of the funds.
- Any potential value-add from the managers e.g. online services etc.
- Fund charges.
- Mercer ratings, if available.



Overview of typical With Profit Funds

The chart below sets out the progression of a member's fund value throughout the lifetime of a typical with profits investment. The figures shown are for illustrative purposes only.



Overview of typical With Profit Funds

The Positives

- With profits funds are typically considered to be a fairly secure medium to long-term investment with reasonable potential performance from a pooled mix of assets including equities, property, bonds and cash.
- The costs of running with profits fund are largely deducted from the fund and what is left over is available to be paid to the with profits investors as “bonuses”:
 - **Annual (Reversionary) bonus**: which may or may not be partially guaranteed, and
 - **Terminal (Final) bonus**: a final bonus may be added on disinvestment (switch, transfer, retirement or death) depending on the performance of the underlying fund. These bonuses are payable by most (but not all) with profits funds.
- To avoid big changes in the size of bonuses each year, the insurer will hold back some of the return from ‘good’ years to provide a reasonable return during ‘bad’ years. This is known as “smoothing”.
- Older policies (typically pre 1990) may provide **Guaranteed Annuity Rates (GARs)** or other pension guarantees (which can be very valuable), more recent policies (up to around 2003) may also provide a **Guaranteed Interest Rate (GIR)**. These may have been withdrawn or reduced for more recent new contributors or contribution increments.



Overview of typical With Profit Funds

The Less Positives

- **Annual Bonuses** are a poor indicator of performance. Minimising guaranteed bonuses reduces the proportion of the with profits fund which insurers have to invest cautiously (to protect their solvency position). On the other hand, low bonuses may just reflect poor underlying investment performance and/or low solvency reserves.
- **Terminal / Final bonuses** can be a huge proportion of the overall return and, in theory at least, they could be withdrawn overnight. Equitable Life hasn't paid terminal bonuses since the 1990s, though the Capital Distribution is similarly "at risk".
- Guarantees (within the with profits fund rather than a specific policy) can necessitate a more cautious underlying investment strategy, to maintain the insurer's solvency. This can severely restrain future investment performance for other policyholders too.
- Insurers can impose a **Market Value Reduction (MVR)** if disinvestment is other than (usually) the pre-selected retirement date or prior death. This could more than negate a terminal bonus.
- Historically, payout examples (reported in later slides) were provided via insurers' regulatory returns, but these ceased to be available in 2017 due to the Solvency II Directive.



AVCs – Why this requires attention

Case Study

Client had a 1,000 person DB Scheme. AVC arrangements were not reviewed over many years

The Scheme had AVCs with:

- Prudential
- Phoenix Life

AVC investments with Phoenix Life were invested in Deposit Funds, and had been since 1998 without the Trustee undertaking a review on suitability

A Phoenix Life member made a complaint through his IFA citing the Trustee not delivering the required level of AVC governance

The Ombudsman ruled in favour of the member which involved significant investigative time from Trustees and their advisors

An agreed compensation amount was paid to the member by the Trustee. All other members invested in the Deposit Fund over this period of time were also included for a compensation payment.

The cost of investigation work to resolve the complaint was £35,000.

The compensation cost for all affected members was £140,000

The Trustee then reviewed all AVC arrangements. Issues identified were AVC members that had taken main scheme benefits, members who had died, unsuitable investment choices, poor member communications.

Changes were made as a result of the AVC review including consolidating to 2 AVC providers. Members achieved better outcomes and risks to Trustees reduced.



ABI Sector Benchmarks

What are ABI sector benchmarks?

The Association of British Insurers (“ABI”) maintains a range of sector benchmarks for unit-linked life and pension funds. As at October 2022, there were 34 ABI sector benchmarks. ABI sector benchmarks are **peer group benchmarks**. The ABI has full discretion to set and update ABI sector definitions. An independent third party, Refinitiv, categorises unit-linked life and pension funds into the sectors and monitors sectors to ensure that funds are categorised correctly on an ongoing basis. The ABI sector benchmarks are designed to facilitate comparisons between similar unit-linked life and pension funds.

What are the drawbacks of ABI sector benchmarks?

- In order to create peer groups, ABI sets minimum and maximum exposure limits to certain asset classes within each sector benchmark. In practice, ABI sector definitions are **very broad**, for example:
 - Equity sector benchmarks are typically required to invest at least 80% of assets in equities. The benchmark does not specify how the remainder is to be invested so up to 20% of the fund could be invested in any other asset class.
 - “Mixed Investment” sector benchmarks are even broader. Funds within the Mixed Investment 40-85% Shares benchmark may invest anywhere between 40% and 85% of their assets in equities with the remainder unspecified.
 - “Flexible Investment” sector has no asset class limits and affords managers significant asset allocation discretion – the dispersion of funds in this sector may be sufficiently broad as to reduce its value for relative performance assessment purposes.
- ABI sector criteria may at times **overlap**. One fund may meet the requirements of more than one benchmark.
- ABI reserves the right to **change sector definitions at any time** and without prior notice.

Due to these factors, **funds within the same peer group may exhibit significant dispersion of risk and return characteristics**. A fund benchmarked against an ABI sector may have returns that differ vastly from its sector.

With Profits AKG Ratings

The ratings shown are provided by AKG Financial Analytics Limited (AKG), and are contained within AKG's latest UK Life Office With Profits Report. They are shown here with AKG's prior consent. Further information on AKG's With Profits Report is available at: <https://www.akg.co.uk/information/reports/with-profits-reports>.

Providers are ranked out of 5 (with 5 being the highest rated) against their competitors (those With Profits funds which are broadly comparable).

Financial Strength: This is an assessment of the position and ability of a with profits fund to maintain the operational characteristics specifically required for customers.

Future Performance: The potential for future performance is made up of a variety of different factors including current investment philosophy, Company and, if available, fund-level solvency coverage position, overall size of the company, its with profits fund and its capital base, bonus philosophy and Estate distribution.

Transparency: Given there is no industry wide standard when evaluating transparency and openness AKG take a number of criteria into account. including approach to communications (for example in run off) to enable customers to make informed decisions, the extent to which they are subject to independent audit and review as well as the amount, quality and timeliness of information to the various stakeholders.

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