

PPFM COMPLIANCE FOR THE PERIOD 1 JANUARY 2020 to 31 DECEMBER 2020

Board report to with-profits policyholders.

The Board of Management's report to with-profits
policyholders for the year 2020

The Shepherds Friendly Society Limited

Registered Office: Haw Bank House, High Street,
Cheadle, Cheshire, SK8 1AL.

1 Introduction

The Society's Principles and Practices of Financial Management ("PPFM") describes how the Society manages its with-profits business.

The PPFM is available on the Society's website at www.shepherdsfriendly.co.uk or copies may be obtained by writing to The Company Secretary, Shepherds Friendly Society, Haw Bank House, High Street, Cheadle, Cheshire SK8 1AL.

The Society is required to produce a report for with-profits policyholders stating whether, throughout the financial year covered, it believes it has complied with the obligations relating to the PPFM and its reasons for that belief. This report covers the period from 1 January to 31 December 2020.

2 Compliance with the PPFM

The Board of Management confirms that it has complied with its obligations relating to the PPFM throughout 2020. In particular, it confirms that:

- (a) the Board's discretion in the conduct of the Society's with-profits business has been applied in accordance with the PPFM, and
- (b) any competing or conflicting rights, interests or expectations of the Society's policyholders have been addressed through the application of the PPFM in a reasonable and proportionate manner.

In so doing the Society confirms that it has maintained fairness between different categories of policy and policyholder.

In making this declaration we have taken into account:

- (a) advice from our With-Profits Actuary on compliance with the PPFM and discretion exercised throughout the period. A statement from her is attached to this report,
- (b) judgement from our Fair Members Benefit Committee on our compliance with the PPFM throughout the period,
- (c) the Directors' overall assessment of the business,
- (d) the materiality of individual aspects of compliance.

The main reasons for believing we can make this statement are covered below.

3 Governance

The Society is required to maintain governance arrangements designed to ensure that, in the conduct of our with-profits business, we comply with, maintain and record our PPFM.

The Board of Management takes overall responsibility for the management of the with-profits fund and ensuring that compliance with the PPFM is maintained. In doing so, advice is taken from the With-Profits Actuary, particularly on key aspects of the exercise of discretion in management of the fund. Throughout 2020 the With-Profits Actuary has been Cara Spinks. The With-Profits Actuary is required to report annually to policyholders on the management of the fund and her statement is attached to this report.

Since 1 January 2011 all key decisions are reviewed by a With-Profits Committee who have provided comments on compliance with the PPFM and the fairness of treatment of policyholders over 2018. During 2018 the Society changed the name of the With-Profits Committee to the Fair Members Benefit Committee to reflect the wider scope of issues it considers. The FMBC can confirm the fair treatment of policyholders over 2020.

4 Reasons for Board's confirmation of compliance with the PPFM

Having taken advice from the With-Profits Actuary and the Fair Members Benefit Committee the Board has reviewed the key provisions of the PPFM. The Board has considered each element of the PPFM and our conclusions on each area are as follows.

Payouts and bonus rates

Payouts made from the with-profits fund during the year broadly reflected asset shares, subject to meeting any guaranteed benefits and allowing for smoothing in accordance with the PPFM. The calculation of asset shares has been consistent with the PPFM and no departures from the methodology set out in the PPFM were made during 2020.

All bonuses were set following advice from the With-Profits Actuary.

Annual bonus rates for conventional policies declared for the 31 December 2019 distribution applied on an interim basis throughout 2020. The rates were reviewed in October 2020 and the decision was made to reduce the existing rates for all business. This decision is consistent with the long-term sustainable rates that the With-Profits Actuary believes these policies can support.

The final bonus rates that applied to payouts throughout 2020 were set on the advice of the With-Profits Actuary. When setting final bonus rates, the aim over the longer-term is that at least 90% of maturity and surrender payouts will fall within the PPFM's stated target range (80%-120% of asset share).

The With-Profits Actuary has notified us that 86% of all payouts were within range overall for 2020. This is a reduction on the figures for 2019 which showed that 94% of claims overall were within target range.

The main reason for the reduction is the increase in the number of contractual maturities falling outside the target range. The bonus recommendations at the end of 2019 broadly implemented a 10% reduction in maturity payouts during 2020 when compared with those in 2019. This reflected reduced investment returns experienced by the with-profits fund in recent years.

In March 2020, the Covid-19 pandemic caused volatility in asset values and introduced significant uncertainty into the assessment of the profits on the Society's income protection portfolio. The Board took various mitigating steps with regards to final bonuses and market value reductions in order to ensure that policyholders leaving the fund did not leave with materially more than their fair share, and to ensure continuing fairness for the remaining policyholders in the fund.

However, because contractual maturity values had already reduced since the previous year, reflecting reductions in investment returns and lower expectations of longer-term investment returns, we agreed to leave the final bonuses for policies maturing in 2020 unchanged. This decision was taken on grounds of fairness to those policyholders leaving the fund (the timing of which was not in their control) and also in recognition of the Society's practice in recent years to uplift payouts in respect of underpayments in previous years.

The With-Profits Actuary has confirmed that, having reviewed these factors, and the size of the overpayment overall, she believes there has been no material detriment to the remaining with-profits policyholders and the Society’s principles for smoothing have been broadly met.

We expect that the overpayment will have been addressed through the recent bonus declaration for claims over 2021, although it is noted that there is still volatility in investment markets which may impact this assessment. The situation continues to be regularly monitored with regards to final bonuses and market value reductions.

In setting final bonus rates and market value reductions (“MVRs”) we have followed the approach set out in the PPFM and have differentiated between classes and generations of policy in a reasonable and proportionate manner.

Investment policy

The overall gross asset mix of the fund at the start and end of 2020 is shown in the table below.

Investment Class	Percentage of Fund at 31 December 2020	Percentage of Fund at 31 December 2019
Equities	12%	17%
Property	2%	2%
Fixed Interest	73%	73%
Cash and other investments	13%	8%
Total	100%	100%

The return on the invested assets over 2020 was -1.13% (2019: 7.8%).

During 2019 the Society moved the majority of its investments into a multi asset fund managed by Royal London. The aim of the fund is to generate growth whilst managing the downside risk. The fund invests in an asset mix including UK and overseas equities, commodities, bonds, money market instruments, deposits and cash, with a blend of active and passive funds and exchange traded funds.

This move remained consistent with PPFM principles and didn't represent any significant departure from the limits set out in the PPFM practices.

The Board is satisfied that the Society has abided by the principles and practices set out in the Society's PPFM during 2020 and in a manner consistent with the Society's desire to treat its policyholders fairly. However, we will continue to review its PPFM ranges to ensure they are consistent with the current investment climate and the stance of the Board in managing the Society's assets.

Business risk

Risks were monitored regularly during the year.

The Society continues its investment in the growth of its non-profit business. Profits on these initiatives are being paid to with-profits policyholders in the form of increased investment returns credited to members' asset shares.

The Society continually reviews ways in which risks can be managed within the business. During 2020, in response to the Covid-19 pandemic, the Society stopped sales of short deferred period income protection business and strengthened its controls around claims. Additionally, the Society implemented a reinsurance arrangement on the Society's income protection business alongside the existing arrangement on the Over 50s business.

No new material ventures were undertaken.

Expenses and charges

Expenses continued to be charged to the with-profits fund in line with the provisions of the PPFM.

Management of the Society's surplus

The amount of surplus has continued to be monitored and the level remained within the target range set out in the PPFM.

The investment strategy of the surplus has been maintained in line with the fund's overall investment strategy.

The surplus has not been used for any purpose in 2020 other than the enhancement the Directors agreed in November 2020 should be distributed to asset shares in respect of surplus arising on the fund (primarily from non-profit business).

New business

Although the decision was taken to stop sales of short deferred period income protection business in response to the Covid-19 pandemic, volumes of new business during 2020 were sufficient to justify the with-profits fund staying open to new business according to criteria included in the PPFM.

Changes to the PPFM

Version 12 of the PPFM was effective from 1 January 2020 to 15 December 2020. A new version of the PPFM came into force on 16 December 2020. Although the look and feel of the PPFM was very different, the update did not reflect any significant changes to the way in which the with-profits fund is being managed. Policyholders were informed about the change via a notification which was sent out with bonus notices during the year together with a report which was published on the Society's website in July 2020.



Ann-Marie O'Dea

Chief Executive Officer

30th March 2021

With-Profits Actuary's report to with-profits policyholders for the year 2020

As With-Profits Actuary to The Shepherds Friendly Society Limited ('the Society') I am required to report to the with-profits policyholders every year on whether, in my opinion, the with-profits business of the Society has been managed over the year in a way that takes their interests into account in a reasonable and proportionate manner.

Policyholders should not rely solely on the information contained in this report when making financial decisions and this report does not represent financial advice.

I have been With-Profits Actuary to the Society throughout 2020.

I can confirm that, throughout 2020, I have had full access to the Board of the Society to discuss matters relating to with-profits business.

In preparing this report I have taken account of the rules of the Financial Conduct Authority and the guidance requirements of the Actuarial Profession and the Financial Reporting Council.

In my opinion, the annual report by the Society to its with-profits policyholders, and the discretion exercised by the Society in respect of 2020, may be regarded as having taken the interests of the Society's with-profits policyholders into account in a reasonable and proportionate manner.



Cara Spinks FIA

With-Profits Actuary to the Society
15th March 2021

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