UK Funerals (2022) Trust

Solvency Assessment Report
as at 11 July 2023

22 September 2023

pwc

Important Notice

This report has been prepared by PricewaterhouseCoopers LLP based on the instructions provided by the Trustees of the UK Funerals (2022) Trust ("the Trust") ("the Trustees") and, where appropriate, incorporates the advice of the responsible Actuary, Emma Morton, who is a Partner at PricewaterhouseCoopers LLP, for the sole purpose that is set out in the Executive Summary.

We do not, in providing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Should any other person access and read this report, by reading this report such person accepts and agrees to the following terms:

1. The reader of this report understands that the work performed by PricewaterhouseCoopers LLP was performed in accordance with instructions provided by our addressee client and was performed exclusively for our addressee client's sole benefit and use.

2. The reader of this report acknowledges that this report was prepared at the direction of our addressee client and may not include all procedures deemed necessary for the purposes of the reader.

3. The reader agrees that PricewaterhouseCoopers LLP, its partners, employees and agents neither owe nor accept any duty or responsibility to it, whether in contract or in tort (including without limitation, negligence and breach of statutory duty), and shall not be liable in respect of any loss, damage or expense of whatsoever nature which is caused by any use the reader may choose to make of this report, or which is otherwise consequent upon the gaining of access to the report by the reader. Further, the reader agrees that this report is not to be referred to or quoted, in whole or in part, in any prospectus, registration statement, offering circular, public filing, loan, other agreement or document and not to distribute the report without PricewaterhouseCoopers LLP's prior written consent.

A copy of this report has been sent to Dignity Funerals Limited ("the Company") as set out in our agreement with them dated 17 April 2023. Under the basis of that agreement, the Company accepts that the work we have carried out is for the Trustees only and we do not accept any responsibility to any other party for it. In particular, we note that the Company will share this report with the FCA and will place it on its website, in its entirety only, as required by the FCA but PricewaterhouseCoopers LLP accepts no responsibility to anyone who may view the report other than the Trustees.

Contents

1. Executive summary

The purpose of this Solvency Assessment Report ("SAR") is to advise the Trustees of the UK Funerals (2022) Trust ("the Trust") ("the Trustees") of the results of a Solvency Assessment completed with an effective date of 11 July 2023 ("the valuation date"). This report is produced in line with the FCA regulations that took effect on 29 July 2022, and follows the requirements set out by the FCA in the FCA handbook and specifically FPCOB 3.2.

The solvency assessment values a "cover level" for each plan held by the Trust, which includes both:

- New Business plans: those sold directly to new plan holders; and
- Rescue plans: plans that originated from providers that chose not to apply or did not meet the standards required by FCA regulation and where plan holders were offered the option to transfer to a Dignity plan (see page 5 for further information).

The liabilities valued in this valuation are the liabilities of the Trust, rather than the Company. In valuing the liabilities of the Trust we have only considered the plans in force at the valuation date.

The FCA requires that liabilities are measured on a "best estimate" basis, which is a basis where there is an equal chance that actual results will be either better or worse than assumed. The FCA's definition of the "solvency level" (used in this report) is the ratio of trust assets over trust liabilities, measured on a best estimate basis.

The market value of the Trust's assets as at 11 July 2023 has been calculated to be £119.1 million (including £77.7 million for the discounted value of outstanding instalments for existing plans, and £15.2 million for the discounted value of funds expected to be received in respect of the Rescue plans). The best-estimate liabilities of the Trust have been calculated to be £108.3 million, which results in:

A **surplus** - i.e. assets less ongoing liabilities - of **c. £10.8m**

A **solvency level** (as defined by the FCA) of **110%**

As at 11 July 2022 there were no liabilities in the Trust however the Company had made a contribution into the Trust of £1 million. The surplus as at 11 July 2022 was therefore £1 million.

This report, taken together with our data letter, assumptions paper and supplementary paper, has been prepared in accordance with the Technical Actuarial Standards, issued by the Financial Reporting Council, that are relevant to the scope of this work insofar as they apply. These are TAS 100 V2.0 (Principles for Actuarial work, dated March 2023) and TAS 400 V3.0 (Funeral plan trusts, dated July 2023).

2. Description of plans

The UKFT was created in June 2022 as a new trust, designed to fulfil the requirements of the FCA regulations that came into force in July 2022.

The Trust's liabilities relate to pre-paid funeral plans sold or taken on by Dignity Funerals Limited since July 2022.

New Business plans The Trust includes plans sold directly by the Company to new plan holders ("New Business plans").

Rescue plans As part of the process to move to the new FCA regulated regime for funeral plan providers, a number of existing operators did not obtain authorisation and were unable to continue providing funerals to plan holders. The Company arranged with some of these providers to offer their plan holders a new, replacement plan - these are referred to as "Rescue plans" in this report, with the original providers referred to as "former providers".

Rescue plan holders were allocated a new Dignity plan which best matched their previous plan.

Some of the Rescue plan holders will have paid for their plan in full to the former provider, but many of them have instalment plans where the payment plan is ongoing and instalments are now being paid into the Trust. The Company is expecting to receive, and pay into the Trust, some funds from the former providers in respect of payments made by the plan holders to their former provider.

Types of cover

The benefits provided under each plan can be categorised into three components as set out in the Trust rules:

- ***"Funeral cover"*** is cover for specified funeral plan items to be provided directly by Dignity, for example an attended funeral service, coffins and transport options. This includes unattended cremations (i.e. cremations that take place privately without any mourners present).
- ***"Disbursements"*** relate to specified funeral plan items which are provided by third parties, and cover attended cremations (i.e. cremations that take as part of a funeral service with mourners present) and burials.
- ***"Options payments"*** are separate pots of money that the plan holder can allocate to put towards a particular purpose but do not relate to a particular product, for example a certain amount to put towards flowers or stationary.

Dignity Promise

All plans are covered by the "Dignity Promise", which means that plan holders who pay in instalments and who die before they are fully paid up (but after 12 months of taking out the plan) will be provided with a funeral and their estate will not need to pay the outstanding instalments.

Cancellation

On cancellation of a plan the plan holder receives back all of the payments made to Dignity to date. For Rescue plans, this sum is capped at the amount of money received in relation to the plan from the former provider and any subsequent payments made into the UKFT by the plan holder.

3. Summary of plan holder data

Plan holder data was supplied in electronic format by the Company on 25th July 2023. The data included prices of the funeral plan components within each plan holders' plan, and an "**outstanding balance**", for those plan holders still paying instalments, which is the total amount the plan holders owe in outstanding instalments as at the valuation date.

There were no plan holders as at the last valuation date of 11 July 2022 as the Trust was new.

The liabilities valued are the "**cover levels"** for the benefits purchased by individual plan holders which will be paid by the Trust to the Company when a plan holder dies. The Trustees have instructed us to derive the cover levels for funeral cover (as defined on page 5) in the following way:

- For New Business plans, an amount considered sufficient to secure the funeral plan components with Dignity or a third party provider on an estimated wholesale basis.
- For the Rescue plans, at a lower level than the wholesale cost, as Dignity has committed to providing funerals for a lower cost for this subset of plans - in large part due to them not having incurred the marketing and other administration costs otherwise incurred in the selling of new plans.

Cover levels for disbursements (as defined on page 5) are set in line with Dignity's current at-need price for the relevant component. Options payments are valued as the original amount contributed, increased with the Consumer Prices Index ("CPI") up to the valuation date.

Data as at 11 July 2023	***New Business plans***		***Rescue plans***	
	Number of plans	**Total cover level (£)**	**Number of plans**	**Total cover level (£)**
Funeral cover	14,660	21,998,627	58,061	69,563,845
Disbursements	8,538	7,758,660	49,529	44,581,774
Options payments	4,408	1,561,028	8,468	2,219,173
Total	**14,660**	**31,318,315**	**58,061**	**116,364,792**

A summary of plans split by payment type is given below:

	Number of plans	**Total cover level (£)**	**Average cover level (£)**
Lump Sum	37,110	73,777,064	1,988
Instalment (fully paid)	783	1,595,869	2,038
Instalment (outstanding)	34,828	72,310,174	2,076
Total	**72,721**	**147,683,107**	**2,031**

* FPCOB 3.2 requires disclosure of 'plan value' in this report. 'Plan value' is not defined by the FCA and so we have interpreted it to refer to cover levels (as defined in this report). However, we believe that other interpretations are possible.

Whilst we carry out reasonableness checks on the data we are not in a position to independently verify it and so we rely on what has been provided by the Company. For a relatively small number of plans the data was incomplete or invalid. After consultation with the Company we have made appropriate estimates. Any error caused by the estimates is unlikely to be material.

4. Assets

Details of the assets held by the Trust were provided by the Company on 14 and 19 July 2023. We have also been provided with unaudited management accounts dated 30 June 2023. Audited accounts are not available as at or near the valuation date and so these figures have not been independently verified.

The total asset value includes:

- £77.7m in future instalments due from plan holders and not yet received, and
- £15.2m in respect of funds that the Company is expecting to receive from the former providers of Rescue plans, which are currently in administration.

Because the Trust is relatively new, the assets held by the Trust are in cash funds, mostly with LGIM, as at 11 July 2023. The Trustees are in the process of developing an appropriate long term investment strategy which they expect to implement within the next 12 months.

We understand that no monies have been deducted from the Trust over the year to 11 July 2023, other than some cancellation amounts which have been netted off instalment income. The assets include an adjustment for accrued payments that are due to be paid out, as set out on the right (see notes 2-5).

As at 11 July 2023	£000s	Notes
Cash held	29,194	1
Estimate of tax payable	(44)	2
Accrued fees	(557)	3
Pending death payments due to Company	(2,377)	4
Pending payment due to Company in respect of cancellations	(65)	5
Adjusted value of assets currently held by the Trust	**26,151**	
Present value of outstanding instalments due	77,737	6
Total assets at 11 July 2023, including outstanding instalments	**103,888**	
Present value of funds expected from the former providers of Rescue plans	15,227	7
Total assets at 11 July 2023, including expected future instalments and assets from former providers	**119,115**	

1: Taken from LGIM asset statements and bank account statements provided by the Company.

2: Estimate of tax due from the Trust to date based on information from management accounts.

3: Relates to advisor and Trustee fees, and was provided by the Company.

4: An estimate of funds to be reclaimed from the Trust in respect of plan holders who died prior to the valuation date, assuming the Trust pays an amount to Dignity consistent with the cover levels used in this valuation.

5: Provided by the Company, representing refunds due to plan holders who cancelled prior to the valuation date.

6: The present value of outstanding instalments expected to be received by the Trust (taking into account the Dignity Promise).

7: The present value of the £15.4m Dignity is expecting to receive from former providers within the next 12 months. There is uncertainty over the amount and timing of these payments and so a guarantee has been provided by the Company to provide these funds if they have not been received from the former providers by 31 December 2024, and there is a shareholder guarantee to provide Dignity with the funds to do that should it not have them.

5. Valuation method and assumptions

Liabilities

For the valuation we have assumed that the Trust continues to fully support existing plans and does not wind up during the lifetime of any current plan holders. Liabilities have been valued by:

1

Projecting future cover levels allowing for CPI increases between the valuation date and the date of payment.

This part of the method applies only to benefits payable on the death of a plan holder, as the projected cancellation amounts do not change.

2

Identifying future cash flows by calculating the probability of a plan holder's death and cancellation in each future time period and multiplying this by the projected value of the cover level or cancellation payment in each instance.

3

Discounting each future cash flow from the date of projected payment back to the valuation date at the assumed best estimate rate of investment return (after allowing for tax).

An expense reserve is included in the value of liabilities, which has been calculated as the capitalised value of future expenses taking into account:

- An expected annual expense amount for the Trust based on expenses seen in the Company's other funeral trusts over recent years
- The expected number of existing plan holders remaining in the Trust in each future year
- Increases in expenses at a rate of CPI+2% p.a. and discounting future expenses at the rate of assumed investment return (net of tax).

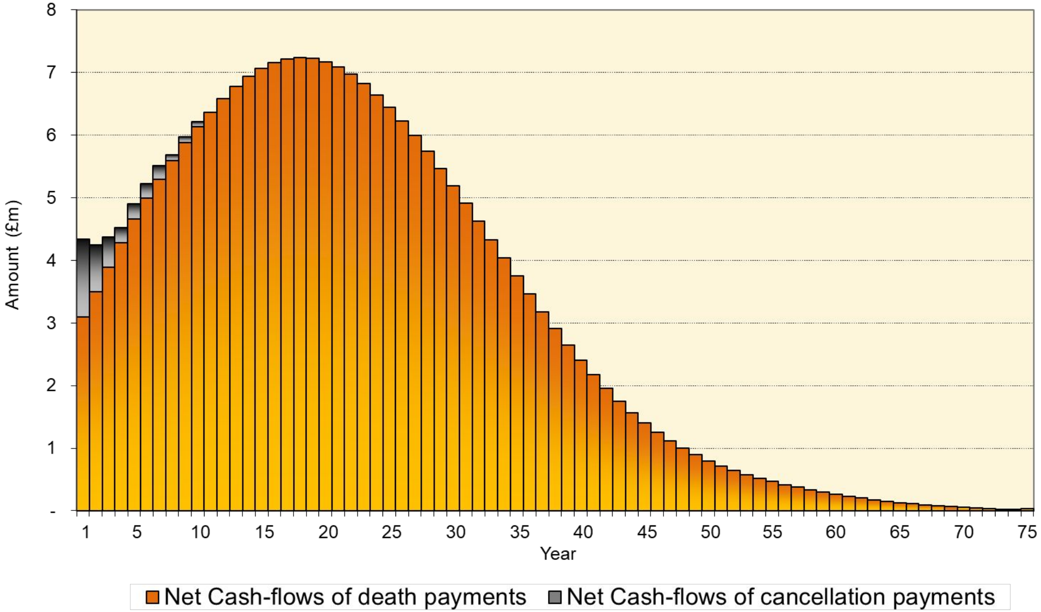
Assets

We have valued assets at their market value, with the exception that outstanding instalments due from existing plan holders have been valued by discounting the payments due in future years in line with the best estimate investment return (after tax), and the funds expected to be received from the former providers which have been valued by discounting the amounts back from the expected date of receipt of 31 December 2023.

5. Valuation method and assumptions

Expected Trust cash flows

This chart shows expected cash flows over the next 75 years using the valuation model described on the previous page.



Please note that any cash flows projected to be paid beyond year 75 have been grouped into the year 75 cash flow above, as the annual cash flows past this point are not material.

5. Valuation method and assumptions

Financial assumptions

Discount rate

The discount rate has been derived using a deterministic, asset-led approach, and represents a best estimate of the expected long-term returns on Trust assets.

As at 11 July 2023 the Trustees' best estimate is that the assets will continue to be held in cash until 31 December 2023, and then invested in line with a portfolio made up of:

- Equities (30%)
- Illiquid investments and infrastructure (23%)
- Multi-Asset and Liquid Credit (17%)
- Government Bonds (20%)
- Cash (10%)

We have therefore used a cash return up to 31 December 2023, and the weighted average return on a portfolio invested in the above assets thereafter.

Until the new strategy is implemented, there will be a mismatch between the Trust's actual asset allocations and the long-term allocations used to set the discount rate assumption.

Tax

An allowance has been made for expected future tax payable on investment returns in line with tax advice received by the Trustee.

CPI inflation

A best-estimate CPI inflation curve has been derived based on the Bank of England Retail Prices Index ("RPI") implied inflation curve, with deductions of:

- 0.25% p.a. to allow for supply and demand distortions in the market.
- 1% p.a. pre-2030 (nil post-2030) to allow for the anticipated difference between RPI and CPI.

The valuation model uses the full CPI curve to increase the cover levels in future years, applying the relevant spot yield from the CPI curve to the future cash flows. Using Trust cash flows, we have derived a single equivalent CPI rate for presentational purposes only (see right).

Cover level increases and expense inflation

An assumption has been made that funeral cover and disbursements will increase with CPI inflation over time. Option Payments are guaranteed to increase with CPI each year under the Trust rules.

Expenses are assumed to increase at a rate 2% p.a. higher than the assumed rate of CPI.

Financial assumptions summary (% p.a.)	
Investment return *(before tax)*	5.0% up to 31 December 2023 6.25% from 1 January 2024
Discount rate *(net of tax)*	2.75% up to 31 December 2023 5.80% from 1 January 2024
CPI inflation *(approx. single equivalent rate)*	2.80%
Funeral cover increases	= CPI
Disbursements increases	= CPI
Options Payments increases	= CPI
Expense inflation	= CPI + 2%

Last year, as no plans were in force the ongoing liabilities of the Trust were nil and no assumptions were required for the actuarial valuation.

5. Valuation method and assumptions

Demographic assumptions

Mortality

The mortality of plan holders is assumed to be in line with the English Life Tables No. 17 (“ELT 17”) tables, which has been set to reflect past experience of the Company’s other funeral trusts and will be reviewed periodically.

No allowance is made for future improvements in longevity.

Cancellation

Cancellation assumptions for the New Business plans are based on previous experience of the Company’s other funeral trusts. We use different assumed cancellation rates depending on the number of years since the plan was taken out, with an assumed rate of 5% in the first year of the plan reducing to 0.5% by year 10.

For the Rescue plans, we have assumed that cancellation rates are nil. This is because:

- All Rescue plan holders were written to by the Company as part of the rescue process and were given the option to cancel their plan at that point.
- Under the terms of the Rescue plans the plan holder will only receive as a cancellation refund the amount that has been received by Dignity, the amounts of which are currently small.

These assumptions will be kept under review as more Trust experience emerges.

6. Valuation results

The results of the valuation on the best estimate basis as described on pages 10 and 11 are shown below..

As at 11 July 2023	Best Estimate Results (£000s)
Funeral cover liability	58,257
Disbursements liability	33,555
Options Payments liability	2,316
Present value of outstanding instalments payable on death[1]	(73)
Present value of payments payable on plan cancellation[2]	3,219
Expense reserve	11,014
Total Liabilities	**108,287**
Adjusted value of assets currently held by the Trust	26,151
Present value of outstanding instalments due	77,737
Present value of funds expected from the former providers of Rescue plans	15,227
Total Assets	**119,115**
Surplus / (deficit)	**10,828**
Solvency level	**110%**

1. Outstanding instalments in respect of plan holders who die within 12 months of taking out their plan and so are not covered by the Dignity Promise. The outstanding instalments are therefore due from the plan holder's estate before a funeral is provided
2. Expected cancellations for New Business plans in line with the assumptions on page 11. The valuation assumes no cancellations for Rescue plans.

7. Sensitivity analysis

The results are sensitive to the valuation assumptions, in particular to the discount rate and RPI inflation assumption. The scenarios in the table below would have the following impact on the Trust's surplus and solvency level:

Assumption sensitivity[1]	Change in assumption	Best estimate surplus / (deficit) (£000s)	Impact of change (£000s)	Solvency level
Valuation result (base case)	-	10,828	-	110%
Discount rate	+ 1% p.a.	20,564	9,736	121%
RPI inflation assumption	+ 1% p.a.	(4,229)	(15,057)	97%
Life expectancy[2]	+ 1 year	14,905	4,077	114%

1 Results show the impact on the surplus of a change in the assumption in isolation for illustrative purposes. The discount rate sensitivity allows for the impact on the present value of future instalments but otherwise we have assumed the value of assets remains unchanged. This is unlikely to be the case in reality as market movements affecting the discount rate and inflation assumption would also impact on the value of the assets held.

2 Sensitivity to life expectancy based on the assumption that all plan holders live one year longer.

Cancellation

The Trust has a small shortfall at the valuation date on a scenario where every plan holder cancelled their plan. This shortfall is broadly equal to the accruals for expenses and tax the Trust has incurred since its inception.

8. Risks and uncertainty

The Trust is exposed to the following risks which need to be managed appropriately:

Investment risk: the risk that the actual asset returns on the Trust assets are lower than the assumed rate of return over the long term. This is particularly relevant given the investment strategy of the Trust has not yet been decided, and the scenario we have modelled only illustrates one possible investment strategy. Specifically, whichever investment strategy the Trust follows, there may be a number of investment risks to consider, including:

- **Mismatching risk**: the risk that differences between the characteristics of the liability cash flows and the Trust assets result in the value of liabilities increasing as a result of certain market conditions without a corresponding increase in the assets.
- **Currency risk**: the risk of unfavourable currency movements on any unhedged overseas assets, given the liabilities are all in GBP.
- **Manager risk**: the risk that the investment manager underperforms their given benchmarks or makes asset allocation decisions that lead to the Trust assets underperforming the liabilities.

Inflation risk: the risk that a period of high inflation results in higher than expected increases to cover levels leading a deterioration of the Trust's funding position and / or the risk that cover levels are insufficient to cover the cost of providing funerals.

Closure to new business: if the Trust closes to new business in the future, it will see lower levels of cash in-flow which may introduce liquidity risk.

Data: the risk of errors in the underlying data which would directly impact the valuation of the Trust's liabilities.

Mortality and cancellation: this risk that mortality and cancellation experience may not follow the assumptions made meaning that payments from the Trust assets could be required sooner than expected.

Covenant risk: the risk that the Company is no longer able to support the Trust or provide the funerals promised to plan holders and the Trust is unable to secure funerals from another provider at the cover levels valued.The Trustees commissioned Cardano to carry out a covenant review of Dignity in August 2023 which concluded that it would be reasonable to treat Dignity as a going concern, recognising material uncertainty.

Climate risk: the risk that the physical consequences of climate change lead to earlier deaths than expected, and investment risk due to the effects of a transition to a lower carbon economy on the investment markets.

Rescue plans: the risk that the former providers do not pay Dignity the amount expected and that the Trustees are unable to call on their guarantee from Dignity to provide the expected funds (counterparty risk).

Tax risk: the risk that the tax treatment is not as expected, either due to changes to legislation or HMRC having a different interpretation of the current rules.

9. Analysis of surplus

We have not included an analysis of surplus as there were no liabilities in the Trust as at the previous valuation date of 11 July 2022, but would expect to do so in future years.

10. Conclusion

This report sets out the results of the solvency assessment of the Trust as at 11 July 2023.

As measured on the the best estimate assumptions, the results show a surplus of £10.8 million, equivalent to a solvency level of 110%.

For compliance with the documentation of the Trust and FCA regulations, we understand that the next assessment should be carried out with an effective date no later than 11 July 2024.

EmmaM.

Emma Morton

Fellow of the Institute of Actuaries

Partner at PricewaterhouseCoopers LLP

22 September 2023