With-Profits Summary

A guide to how we manage our with-profits business

Aviva Life & Pensions UK Limited FLAS With-Profits Sub-Fund – October 2017

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Background

Within Aviva Life & Pensions UK Limited, we have a number of separate with-profits sub-funds. This guide applies to the FLAS With-Profits Sub-Fund.

Aims of this guide

This guide tells you how we manage the FLAS With-Profits Sub-Fund. It is a summary of the key points in our 'Principles and Practices of Financial Management' (PPFM) document. The Principles are statements of the overall standards we adopt; the Practices describe our current approach to managing the with-profits sub-fund.

The PPFM itself is available from our website, **aviva.co.uk/ppfm**, or we can send you a copy if you ask us to – please see the contact details at the end of this booklet. The terms of the PPFM apply in the case of any differences between it and this document.

Why this guide is important

Please read this guide. It gives important information about how our with-profits policies work and what policyholders can expect from them.

Please keep this guide in a safe place with your other policy documents. When reading this guide you may find it helpful to have your policy documents ready to refer to.

If, having read this guide, you need more information, please:

- call us using the phone number shown on the documents provided with this booklet;
- contact your financial adviser; or
- call **0117 989 9000** giving your policy number. Calls may be recorded.

Contents

How does your policy work?

With-profits policies share in the profits made in the FLAS With-Profits Sub-Fund. There are three main types of with-profits policy in the FLAS With-Profits Sub-Fund (called the with-profits sub-fund in the rest of this booklet) :

- conventional with-profits policies;
- unitised with-profits policies; and
- deposit administration policies, which are used in connection with some pension schemes.

Your yearly statement or bonus notice will help you tell which type you have. If your statement shows units and unit prices, then you have a unitised policy. If you are an employer with a pension scheme, you may have a deposit administration contract. Otherwise, your policy is a conventional one.

If you are unsure about what type of policy you have, and need more information, please use the contact details given at the end of this booklet.

Conventional policies

If you have a conventional policy, we pay you a guaranteed amount on your policy's maturity date or on your death. This may be:

- a lump sum payment (called a 'sum assured'); or
- a series of payments (called an 'annuity' or 'pension').

We may add regular bonuses once a year to the guaranteed amount. On your policy's maturity date or on your death, we may also add a final (terminal) bonus to the guaranteed amount.

Unitised policies

If you have a unitised policy, we use your premiums to buy units in the with-profits sub-fund. We add bonuses, if any, by either buying extra units or by increasing the price of the units, depending on the type of policy that you have.

For most unitised policies we add regular bonuses, if there are any, once a year by adding extra units. For the remaining unitised policies we add regular bonuses, if any, at least monthly by increasing the unit price. We may also include a final (terminal) bonus when your policy ends, on top of any guaranteed amount we have agreed to pay you.

Deposit administration policies

For deposit administration policies, we keep an account for each scheme. We credit the account with payments into the scheme, any guaranteed interest payments due and bonuses allocated. We debit the account with the cost of members' benefits and charges.

Guarantees

There are likely to be guarantees under your policy. These apply if certain events happen or on specific dates stated in your policy document. For example, the event may be your policy's maturity date as agreed when you took it out. Or, for a pension policy, it may be the date you intended to retire when you started the policy.

Non-profit policies

There are also a large number of policies in the with-profits sub-fund which are not entitled to a share in the profits of the sub-fund ('non-profit policies'), so do not receive bonuses. With-profits policyholders share in the profits and losses from all types of policy, including these non-profit policies.

How are bonus rates determined?

Our overall aim is to make sure that all guarantees are met and that all policyholders are treated fairly. Future bonuses can not be guaranteed as they come from profits that have not yet been earned. This means that it is possible that no bonuses will be added.

Regular bonus rates for conventional and unitised policies

To determine regular bonus rates for conventional and unitised policies, we estimate the future investment return we expect to earn in the long term on the assets of the with-profits sub-fund. Regular bonus rates are then set taking this into account, together with other factors such as tax and expenses. Our aim is to allow a big enough margin to pay final bonus on most policies of each particular type when they end. If we consider that the expected final bonus is too low then we will reduce regular bonus rates (if necessary to zero). Similarly, if we consider that the expected final bonus is too high then we will increase regular bonus rates.

Regular bonus rates for deposit administration policies

We set regular bonus rates on deposit administration policies by taking into account the actual return on the assets and any guaranteed interest payments due. Our aim is to produce a fair return for policyholders over the medium term.

Final (Terminal) bonus rates for conventional and unitised policies

We normally review final bonus rates twice a year. However, final bonus rates can change at any time and we may review them more frequently if there are large changes in investment markets.

To determine final bonus rates on conventional and unitised policies we group similar policies together. We compare the total guaranteed benefits with the total asset share of the group.

Asset share

The asset share is an amount we work out for a policy by looking at how much has been paid into the with-profits sub-fund and the investment returns earned in respect of the policy. We then take away certain deductions which include expenses, tax, our shareholders' profit, and the cost of providing the agreed benefits for the policy (such as death or sickness benefits). For more information on expenses, please see the 'What are the charges and expenses?' section on page 10.

We aim to pay out, on average, the asset share of a policy plus any uplift which may be available when it reaches the end of the term. However, we may pay more or less than this as a result of smoothing.

An uplift is an extra amount that we include in your final bonus from surplus assets within the with-profits sub-fund. The uplifts apply fully only to policies that have been in force for a minimum number of years. We currently expect to pay significant extra amounts in the future, although they are not guaranteed.

We aim for your payout to be between 80% and 120% of the uplifted asset share when it leaves the with-profits sub-fund.

Smoothing

Over time the value of the investments held by the with-profits sub-fund will rise or fall. We do not change bonus rates as often as the value of the investments changes. Thus we aim to even out some of the highs and lows in investment values and to cushion our policyholders from large fluctuations in regular and final (terminal) bonus rates. This is known as 'smoothing' and could lead to payouts being temporarily different from our target payouts.

We normally aim not to change payouts for similar policies by more than 15% from one year to the next. This protects payouts temporarily against falls in asset share greater than this.

If your policy is not entitled to any final (terminal) bonus, its regular bonuses may vary more than other policies' because we cannot use a final (terminal) bonus to adjust the overall amount we pay you. When setting regular bonus rates we take into account the same factors as when setting final bonus rates, although with a margin when necessary to protect other policyholders. Policies where we do not pay final (terminal) bonuses include With-Profits Annuities, Deposit Administration Plans, and policies invested in the Group With-Profits Fund.

Over the long term, we would not expect the with-profits sub-fund itself to gain or lose from smoothing and we adjust final bonus rates to ensure this.

What happens if you leave the with-profits sub-fund early?

You may decide to move some or all of your investment out of the with-profits sub-fund early. For example you might:

- cash in your policy;
- transfer to another company; or
- switch to another type of Aviva fund.

We would then work out how much to pay you using the asset share as a guide. Our aim is to be fair to you and other policyholders leaving the with-profits sub-fund, and to those policyholders staying in the with-profits sub-fund.

If you leave the with-profits sub-funds early we aim for your payout to be between 80% and 120% of the uplifted asset share.

Conventional policies

We reduce your policy's guaranteed benefits to reflect that you have been invested in the with-profits sub-fund for a shorter time and have paid fewer premiums than we expected when you took out your policy. We may add a final (terminal) bonus as described earlier. In adverse financial conditions, for example if investment markets fall significantly, we may change the way we determine how much is due to you. This may mean that we reduce the amount we pay you in order to be fair to all policyholders.

Unitised policies

We work out the cash-in, transfer or switch value by looking at the value of the units in your policy and then apply any reduction as described in your policy booklet. We may then add a final (terminal) bonus as described earlier.

If the assets in the with-profits sub-fund which back your policy have performed worse than we assumed when we added regular bonuses to your policy then we may reduce your payout by applying what is known as a 'Market Value Reduction' (MVR). We apply an MVR to make sure that:

- the cash-in, transfer or switch value is fair compared to the asset share of the policy; and
- a fair share of the with-profits sub-fund is left for the remaining policyholders.

For certain policies we guarantee not to apply an MVR on certain dates. Your policy booklet will tell you if this is the case.

How is your money invested?

Our investment strategy for with-profits policies is to invest in a broad range of assets. We aim to provide the best possible investment returns for the benefit of policyholders generally, allowing for:

- the level of guarantees within the with-profits sub-fund; and
- the amount of surplus assets in the with-profits sub-fund.

The with-profits sub-fund invests in a mixture of assets: mainly shares, property, bonds (loans to governments, known as gilts and loans to companies, known as corporate bonds), and money market investments (such as bank deposits). Historically, shares and property have produced higher returns than bonds and money market investments over long periods such as twenty years. However, bonds and money market investments are considered lower risk and are more suitable for backing guaranteed payments.

We set guidelines for our investment managers to tell them the proportions of the with-profits sub-fund that should be invested in each type of asset. We also control any potential risks to the with-profits sub-fund by setting guidelines covering the quality of the assets, and setting limits on the amount that we invest in any one asset or with any third party.

We review our long-term investment strategy at least yearly but may do so more often if market conditions change quickly.

How are business risks managed?

The with-profits sub-fund is exposed to a number of risks. The cost of risks is normally allocated to the with-profits sub-fund as a whole not to individual policies. Our biggest risks come from the need to pay the guaranteed payments on all with-profits and non-profit policies when they become due, and from the possibility of falls in asset values.

We control the risks to the with-profits sub-fund by monitoring the various risk factors, and taking action to reduce our exposure to risk, for example by changing our investment strategy or entering into arrangements to transfer the risk to other companies.

What are the charges and expenses?

For conventional policies, policy charges will have been allowed for in the premium that you pay. For unitised policies, these will have been set out in your policy document.

Expenses are what it actually costs us to look after your policy. When we calculate your policy's asset share the expenses we allow for include:

- fees we pay for administration;
- commission paid to intermediaries;
- fees for investment management services;
- other investment related expenses, for example the cost of buying and selling assets; and
- part of the general expenses of the with-profits sub-fund, such as fees we pay to the financial regulators.

What are the estate and the capital support?

The estate consists of the assets in the with-profits sub-fund over and above those required to cover the amounts we expect to pay out to policyholders, including bonuses we expect to add in the future.

Over time we aim to pay out all the assets in the with-profits sub-fund in a way that is fair to all policies, so that the estate will be zero when all policyholders have left the sub-fund.

If at any time we believe that the amount of the estate is too low then we will take action to increase it, for example by reducing future bonus rates or changing our investment strategy.

Similarly, if we believe that the amount of the estate is too high, we will take action to reduce it, for example by increasing the amount we allocate to bonuses over a period of time.

In addition, certain capital support assets are available within other parts of Aviva Life & Pensions UK Limited, in all but extreme circumstances. Support assets may be used to pay policy benefits of the sub-fund, should the reserves and estate prove insufficient.

In certain circumstances the support assets will be transferred to the sub-fund. The assets will also be repaid when no longer required.

The estate and capital support assets:

- provide us with investment flexibility;
- enable bonuses on with-profits policies to be smoothed; and
- enhance the security of policy benefits generally.

Are new policies still being issued?

Subject to policy conditions, existing policyholders can still top-up their plans and new members can still join existing group pension policies. We closed the with-profits sub-fund to new customers on 31 July 2009.

Although we no longer sell new policies, the with-profits sub-fund will continue to be managed in line with our PPFM.

How much profit are our shareholders entitled to?

Both policyholders and our shareholders share in the profits of the with-profits sub-fund.

For every £9 of bonus we add to your policy, our shareholders are entitled to a maximum of £1.

How can you find out more?

This guide is a summary of our 'Principles and Practices of Financial Management' (PPFM) document, which gives a more detailed description of how the with-profits sub-fund is managed.

If you would like a copy, please use the contact details below. Or you can read it on our website **aviva.co.uk/ppfm**

If, having read this guide, you need more information, please:

- call us using the phone number shown on the documents provided with this booklet;
- contact your financial adviser; or
- call **0117 989 9000** giving your policy number. Calls may be recorded.

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