



# A guide to how we manage our with-profits fund

# Its aims

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## **This guide:**

- explains briefly how our with-profits fund works
- helps you decide whether a with-profits investment is right for you
- will help you discuss with-profits with your financial adviser

## **When to read this guide:**

You may wish to read this guide after you have read:

- the key features document, which covers such things as the risks, our charges and where your payments are invested
- your illustration, which explains what you might get back from your investment

Please keep this guide in a safe place with your other policy documents.

# What does this guide cover?

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## **This guide covers:**

- investing for your future in our with-profits fund through a Tax-Free Savings Plan, Investment ISA or With-Profits Bond
- how our approach to managing our with-profits fund affects the amount you get back

Our approach can change from time to time, so we'll write to you if we make alterations that may significantly affect your with-profits investment.

# What is a with-profits investment?

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## **'With-profits' is an investment that, depending on the product you have, provides:**

- the possibility of medium or long-term growth (by 'medium term' we mean at least 5 years, by 'long-term' we mean at least 10 years), however the growth is not guaranteed and you could get back less than you have invested
- some protection against the ups and downs of the stock market (known as smoothing)
- in respect of the Tax-Free Savings Plan and With-Profits Bond, but not the Investment ISA, some guarantees of the minimum final amount you will receive

# How does the with-profits fund work?

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After taking any initial charges from your money, we pool the remainder with that of many other investors in our with-profits fund. Each investor is credited with a share of the with-profits fund.

The size of your share depends on how much you have paid in and when you paid.

The with-profits fund invests in different types of investments (called the mix of assets) such as company shares, property, bonds (types of loan, usually to the Government or companies) and cash deposits. What proportion we put into each type of investment will vary over time.

We currently invest a significant portion of the with-profits fund in company shares and property. We limit the maximum amount that can be invested in any one particular share or property.

We review our mix of assets at least once a year.

## Meaning of 'with-profits fund' and 'group'

### In the rest of this guide:

- **with-profits fund** means the with-profits fund as a whole
- what **group** you're in depends on the type of policy you have and when you started it

## Fairness to all investors in the with-profits fund

We aim to pay all investors their fair share of the profit in the with-profits fund.

We calculate each investor's fair share by looking at a sample of policies and working out for each of these what the fair share would be.

We look at samples for each group of investors, including your group. When deciding what is a fair share, we take into account a number of factors including:

- how much has been invested in those sample policies
- the with-profits fund's past investment performance
- the charges we have made
- the with-profits fund's gains and losses
- any guarantees or promises we have made
- taxation

We also use these fair shares to help us decide what bonuses to pay to different investors and what market value reductions or investment performance adjustments to apply (see pages 6 and 7).

# What are the bonuses?

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We can add two types of bonus to your policy.

- **annual bonuses**, which increase the amount you'll receive. For our Tax-Free Savings Plan, once added we cannot take the annual bonus away provided that the policy is held to maturity
- a **final bonus**, which we use to make sure you get your fair share of the profit in the with-profits fund when you move out of with-profits or if you die

We have wide discretion in deciding bonuses and don't guarantee that we will always add bonuses.

Different types of policy receive different bonuses. We usually decide bonuses once a year, but we may change them at any time. In some years we may decide not to allocate a bonus. We may add an interim bonus on the closure of a plan due to maturity (where applicable), early closure or death. Interim bonuses are not guaranteed and the percentage rate may change at any time or may be zero.

The yearly statement we send you will include information about the bonuses already allocated for your policy.

## Annual bonuses

When deciding how much annual bonus to pay, one of the most important things we look at is how investments will perform in the future. For example, if we expect investment returns to fall, we're likely to reduce bonuses. This would happen even if actual returns in previous years had been higher.

We might make the reductions in several stages.

## Final bonuses

We may pay a final bonus if the amount we have already guaranteed to pay you is less than a target value we have set for with-profits policies. We aim to top up what investors get from their with-profits policies to this target value. In the case of our ISA, the final bonus may be negative, which would reduce the amount payable to you.

We set the target value by considering the following main factors:

- the 'fair share' of the with-profits fund for the relevant with-profits policy
- the adjustment we make for the smoothing (see page 6) of recent investment returns
- how we expect investments to perform over the coming months
- a reduction (if necessary) to help meet the extra payments we expect to make from time to time because of the guarantees attached to some policies

# What affects the value of my policy?

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Many factors affect how much you'll get back from your policy. These are the main ones:

## **a) Investment performance**

The biggest factors are investment performance and the gains and losses of the with-profits fund.

Gains and losses depend on several things, including how much of the with-profits fund we invest in different types of investments. We hold some higher-risk investments such as shares and property, which could produce higher returns than some other types of investments but could also produce greater losses.

The rest is in lower-risk investments, such as fixed-interest bonds issued by companies or the Government, and cash in deposits that earn interest.

Over time, the performance of different types of investments varies significantly and we may change the balance of the investments to:

- improve long-term performance
- make sure that the with-profits fund can always meet its guarantees

## **b) Guarantees**

We guarantee a minimum amount that you will get back from your National Friendly Tax-Free Savings Plan or With-Profits Bond, but the guarantee applies only if:

- you move out of with-profits on a date on which a guarantee applies to your policy
- or
- you die before that date

The guaranteed minimum amount will depend on the terms of your policy.

The minimum amount you will get back from your National Friendly Investment ISA is not guaranteed but will reflect your share of the profit in the with-profits fund.

## c) Smoothing

With-profits investing includes a special feature called 'smoothing'. The main result of smoothing is to reduce the effect of recent stock market fluctuations on what you get back. By recent we mean the last couple of years.

So, for example, in good years we will hold back some of the profits and use them to top up bonuses in poorer years.

However, smoothing will not stop bonuses or other payouts from getting progressively smaller if investment returns remain low over several years. So, when times are not so good, you may get reduced bonuses or no bonus at all.

We can change the way we carry out smoothing at any time, so that no matter what happens in the investment markets, we can still be fair to all investors in the with-profits fund.

Our current smoothing targets are as follows:

- For most policies, we aim to pay amounts that are within 20% of the fair share level
- For similar types of policies we aim to make claim payments that do not differ by more than 10%
- For policies of the same type paying the same premiums over the same term we aim to make claim payments that do not differ by more than 10% in successive years

## d) Market value reductions (MVRs)

We have the right to make what's called a 'Market Value Reduction' (MVR) to your With-Profits Bond. This allows us to reduce the value of your policy if you decide to leave the with-profits fund. An MVR could also come into play if the stock market falls sharply when bond holders are cashing in their policies.

If we apply an MVR, it will mean a reduction in what you get back. We do not apply MVRs to our Investment ISA, although the final bonus could be negative and this would have the same result.

We constantly monitor investment conditions, and may also apply an MVR at any time if we think it necessary. We're likely to do this whenever payouts would otherwise be above the fair-share level.

We might reduce or remove the final bonus when we introduce an MVR.

We can introduce different MVRs for with-profits policies bought in different periods (a year or part of a year) or for different types of policies.

## **e) Investment Performance Adjustments (IPAs)**

We have the right to apply what are called 'Investment Performance Adjustments' (IPAs) to your Investment ISA.

IPAs are used to adjust any significant difference between your monthly bonuses and the actual performance of the with-profits fund. IPAs are applied for each tax year when you withdraw money from your ISA. Generally they are designed to add extra value to your ISA. However, the IPAs could be negative to reflect a decline in the value of the with-profits fund which would mean the value of your ISA would fall and you could get back less than you invested.

A separate IPA rate is used for each tax year and each rate is reviewed regularly.

Because the IPA rates are only reviewed from time to time, the value of your ISA will not immediately reflect the movements up or down in the value of the assets.

However, over time the IPAs will ensure that the value of your ISA will largely reflect the performance of the with-profits fund.

## **f) Our charges**

The charges we make include administration costs and other expenses and are shown in your illustration.

## **g) Guarantees and payments to other with-profits investors**

Our guarantees and commitment to paying 'fair shares' to other with-profits investors can affect what you get back.

The guarantees could also affect how we invest the with-profits fund.

## **h) Tax**

Any tax we pay within the fund reduces the value of any growth achieved. Our aim is to spread the burden of taxation of the with-profits fund as fairly as possible, throughout the with-profits fund.

## **i) The size of the surplus assets**

The surplus assets are a pot of money that provides working capital for the with-profits fund. We build up this pot from profits that are not needed to support the with-profits fund's current and future liabilities.

If the size of the surplus asset reduced significantly, we would review the way that we manage the with-profits fund. The following issues might need to be considered:

- We may change our investment strategy to invest the with-profits fund in a higher percentage of lower risk fixed interest investments. However, these lower risk investments would be expected to give you a lower investment return
- We may restrict the amount of new business (or not accept any new business) to reduce the costs associated with writing new business
- Any expenses being met by the surplus asset may need to be taken into account in calculating what the fair share should be and may reduce what you get back

# What if I decide to move out of with-profits?

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We aim to ensure that you get fair value for your investment, but we do not guarantee the minimum that you could get. You may get back less than you invested.

How much you get back from your Tax-Free Savings Plan depends on:

- how much you paid in
- the investment return achieved on the with-profits fund
- the expenses incurred in administering your policy

How much you get back from your With-Profits Bond or Investment ISA depends on:

- how much you paid in
- plus the annual bonuses we have already added
- plus any final bonus we might add
- less any MVR or, in the case of the Investment ISA, a negative final bonus
- less any penalty charges within the first five years of opening a With-Profits Bond
- in the case of the With-Profits Bond, any guarantees attached to your policy
- less an adjustment for any withdrawals

We aim to maintain a fair level of future payouts to everyone investing in the with-profits fund.

## Where can I find out more?

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If you are still unclear about investing in with-profits, please speak to your financial adviser or contact our Customer Support Team on the numbers below.

If you would like a more detailed and technical guide to how we manage the with-profits fund, a copy of our Principles and Practices of Financial Management is available from our Customer Support Team or our website at [www.nationalfriendly.co.uk](http://www.nationalfriendly.co.uk)

To request a copy in Braille, large print or audio please call us on

**0333 014 6244** Calls from UK landlines and mobiles cost no more than a call to an 01 or 02 number and will count towards any inclusive minutes.

Lines are open 8am-6pm weekdays. Calls are recorded for training and quality purposes.



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