



# With-Profits Guide

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A guide to how we manage our with-profits fund

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## Definitions

**Shares:** an investment that represents part ownership of a company. Shares are also known as equities.

**Fixed interest:** loans to governments and companies that pay a predetermined rate of interest.

**Policyholder:** a person who owns a National Friendly with-profits policy.

**Property:** an investment in commercial property such as offices, shops and industrial premises.

**TESP:** our Tax-Exempt Savings Plan.

**Smoothing:** adjusting returns for some of the extreme ups and downs of short-term investment performance to provide a more stable return.

**Surplus assets:** funds that allow National Friendly to demonstrate that our with-profits fund is solvent and able to meet its obligation to policyholders even if it were to suffer significant losses.

**With-profits fund:** the with-profits fund is the fund where the National Friendly's with-profits business is written. With-profits policyholders can share in the profits of the with-profits fund through discretionary contributions.

## What is a with-profits investment?

Your National Friendly with-profits policy aims to provide steady capital growth over the medium to long term by investing in a broad range of assets, while smoothing out some of the fluctuations of investment markets.

It offers the possibility of higher returns than what you may get from an average savings account with a bank or building society.

Your money will be held in the fund as a pool of assets with others who invest in it.

The value of the fund can go down as well as up depending on the returns of the underlying mix of assets within the fund, so you may get less than has been paid in.

We share out the profits and losses of the fund through a system of bonuses, with the aim of smoothing the returns on your with-profits policy over the long term.

We explain smoothing in more detail later, but basically it helps to reduce some of the significant ups and downs of investing in the stock market. We smooth the rises and falls in value by holding back some of the investment returns in good years. We then use them to top up bonuses in poor investment years. Losses made in poor investment years may also reduce returns in good investment years.

On some policies, a guarantee applies, and this will reflect the minimum sum you will receive under the policy terms.

## What does this guide cover?

This guide explains briefly how our with-profits fund works and our current approach to managing it.

Please keep this guide in a safe place, along with your other policy documents, as you might find it useful:

- When you get your yearly statement,
- If you get an illustration of what you might get back from your policy,
- If you would like to discuss your policy with a financial adviser.

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

You can find more detailed, technical information about how we manage our fund in our Principles and Practices of Financial Management (PPFM) document, which is available on our website:

[www.nationalfriendly.co.uk/with-profits](http://www.nationalfriendly.co.uk/with-profits)

A summary of any notable past or upcoming changes to the PPFM is also available on the website alongside the most up-to-date version of this guide.

A copy of the PPFM is also available upon request from the Customer Services team at National Friendly. Our contact details are shown at the end of this document.

## How does the with-profits fund work?

We combine and invest money from all of our policyholders in our with-profits fund.

The fund has a wide range of investment types which we generally refer to as assets.

The fund your policy invests in will always contain a mixture of higher and lower risk assets to achieve its objectives.

The fund holds a certain proportion of higher asset risks such as shares (equities) and properties. The rest is in medium and lower risk investments such as fixed interest (government and corporate bonds). The actual mix of assets depends on whether you have a life or pensions policy and may vary over time.

We limit the maximum amount that can be invested in any one particular share or property and review our mix of assets at least once a year.

Our fund managers may change the asset mix to:

- Improve the long-term performance of the Fund
- Make sure that the fund can meet its obligations

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

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

When deciding what is a fair share, we take into account a number of factors including:

- how much has been paid into the with-profits fund by policyholders
- the with-profits fund's investment over the period that the policy has been in force
- our charges, such as administration costs, investment management fees and annual management cost
- any guarantees or promises we have made
- taxation

We also use these fair shares to help us decide what bonuses to pay to different groups of policyholders.

## What type of bonuses are there?

We can add two types of bonus to your policy.

- annual bonuses, which increase the amount you'll receive. Once added, we guarantee that the regular bonus will be paid at your chosen retirement date, the policy's maturity date or on death if applicable.

Please note that Tax-Exempt Savings Plans (TESPs) will only pay a return of premiums paid to date on death in all cases.

- a final bonus, which we use to make sure you get your fair share of the profit in the with-profits fund when we make a payout, including partial withdrawals if applicable, on your policy.

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 an annual bonus. We may add an interim bonus on the closure of a policy due to maturity, retirement, early closure, partial or full withdrawal, transfer or death where applicable. Interim bonuses are not guaranteed and may change at any time or may be zero.

The annual bonus statements 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 the fund's expected long term investment returns. For example, if we expect long term 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 over a number of years.

### Final bonuses

We aim to pay a final bonus to increase the value of your policy:

- if you die, with the exception for TESPs where we return the total premiums paid
- if you transfer your pension or cash-in your policy
- at maturity, for endowments, or at your chosen retirement date, for pensions.

Final bonuses aim to pay any balance between the annual bonus we've already added and the performance of the fund over the whole period of your investment. This makes sure that you get a fair share of the return your investment has earned.

We normally review final bonuses once a year. However, we may review them more frequently if there are large changes in the investment markets.

If the fund performance has been low over the period you invested, you may not receive a final bonus as you'll have already received your share of the returns through regular bonuses.

Final bonuses can change at any time, aren't guaranteed and could be zero.

At times, we may apply a market value reduction (MVR) on our With-Profits Bonds or a negative investment performance adjustment (IPA) on our ISAs. This is a reduction we sometimes have to make so that customers who remain invested in the fund aren't disadvantaged when others choose to leave.

If a MVR or negative IPA is in place, this can reduce the effect of any final bonus and you can get back less than you invested. We'll tell you if a MVR or negative IPA is applying before you take money out of the fund so that you have the opportunity to change your mind.

## What affects the value of my policy?

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 in the with-profits fund.

Gains and losses depend on several things, including how much of the with-profits fund the Society invests in different types of investments.

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
- take into account the Society's risk appetite

### b) Guarantees

At the end of your policy term or on death, we'll pay the basic guaranteed benefit as well as any annual bonus we've already added. We'll do this even if the investment market falls significantly.

We cannot guarantee the amount you'll get back if you move out of the fund before or after your originally selected retirement date or before your maturity date.

Some pension policies may offer guaranteed annuity options such as a guaranteed annuity rate. As these guarantees are valuable, we recommend you seek financial advice before withdrawing or surrendering any benefits in the future. Please read your policy documents to find out if this applies to you.

The minimum amount you will get back from your National Friendly Investment ISA and National Friendly With-Profits Bond is not guaranteed but will reflect your share of the profit in the with-profits fund. You may get less than the total amount you invested.

### 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 lower or no bonuses may be declared.

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:

- 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) on with-profits bonds**

In cases where there is a partial or full withdrawal, and no guarantees in your policy apply, we have the right to make a 'Market Value Reduction' (MVR) to these With-Profits Bond policies. This allows us to reduce the value of these policies in cases where payouts would otherwise be above the fair-share level.

We regularly monitor investment conditions, and may apply an MVR at any time if we think it necessary.

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) on ISA policies**

We have the right to apply 'Investment Performance Adjustments' (IPAs) to Investment ISA policies.

IPAs are used to adjust any significant difference between the monthly bonuses and the actual performance of the with-profits fund. The IPAs depend on the tax year the policy started and are applied when a withdrawal is made from an ISA policy. 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 the ISA policy would fall and could be less than the invested amount.

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 an 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 an ISA will largely reflect the performance of the with-profits fund.

#### **f) Our charges**

The charges we make include costs such as administration costs, investment management fees, cost of guarantees on other with-profits policies in the with-profits fund and acquisition expenses.

Your Key Features Document will give you more information about the charges and costs that apply to your policy.

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

Our guarantees and commitment to paying 'fair shares' to other with-profits policyholders 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.

Currently, there is no UK tax payable by our Fund on assets backing pensions, ISA and tax-exempt policies, although this might change in the future.

We are basing this information on our current understanding of tax laws but if you are in any doubt on how your payments will be taxed we recommend you speak with a tax professional before making any withdrawals from your product(s).

### **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 obligations.

If the size of the surplus asset falls below, or increases above, the solvency risk appetite levels mentioned in the PPFM, we may change our investment strategy, change the levels of new business that we sell, reassess the expenses and excess surplus which may reduce or increase what you get back.

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

You may decide to move some or all of your investment out of the fund early. For example, where your policy allows, you might:

- Cash-in your policy
- Transfer to another company.

You should view with-profits investments as a long-term investment. This means leaving the fund early may be the wrong option for you, especially if you have guarantees.

On policies other than ISAs and With Profits Bonds, if you move your money out before the maturity date or selected retirement date, we'll reduce the policy's guaranteed benefits to reflect that you've paid fewer premiums and been invested in the fund for a shorter time than we expected when you took out the policy. We may add a final bonus.

There may be times in poor market conditions when we need to apply a market value reduction to the With-Profits Bonds or a negative Investment Performance Adjustment on ISA policies. It's a reduction made to ensure that policyholders who remain the Fund aren't disadvantaged when others leave.

When an MVR or negative IPA is in place, this will reduce the value of your investment and you could get back less than you've invested. We do not apply an MVR or negative IPA on death.

If you tell us you want to move your money out of the Fund, we'll let you know if an MVR or negative IPA will be applied before you take your money out of the fund. This gives you the chance to change your mind.

We apply surrender charges in the first five years of opening a With-Profits Bond and in the first year of opening a Tax-Exempt Savings Plan. These will also affect your payout if you move out of with-profits investments after that.

### **Where can I find out more?**

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

We put this guide together as a summary of how our with-profits fund works. However, because we've kept it as short as possible, we've only given you the most important information. We need to let you know that without all details you'll not have a complete picture.

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 Services Team or in the With-Profits Fund section on our website.

In the event of any conflict between this guide and the PPFM, the PPFM will take precedence.

You can see a summary of any changes to our PPFM on our website together with our yearly compliance statement.



# Here's how you can contact us

To request a copy of this report in Braille, large print or audio, please get in touch.

You can call us on:

**0333 014 6244** 8am-6pm Monday to Friday excluding bank holidays.

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.

Calls are recorded for training and quality purposes.

Or email us at:

**info@nationalfriendly.co.uk**

Or visit us at:

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