Aviva Life & Pensions UK Limited FP With-Profits Sub-Fund

Summary of changes to the Principles and Practices of Financial Management (PPFM)

Introduction and Background

This document summarises changes made to the FP With-Profits Sub-Fund PPFM document in recent years.

The PPFM was originally published in March 2004 as the PPFM for Friends Provident Life and Pensions Limited. It then consisted of two separate documents, one for policies sold before Friends Provident ceased to be a mutual company (in 2001) and one for later policies. These were combined in 2012 and have since been amended on several occasions. The Aviva website now displays the latest version of the PPFM.

1. Changes effective from 1 January 2019

The PPFM was amended 1 January 2019. A number of practices were amended following an internal review.

(a) General changes

Where possible we have standardised wording and removed any Practices that are no longer applicable. These have not been described here as they make no material change to the PPFM.

(b) Practices 2.2 & 3.4

We have made some changes to the way we apply smoothing of payouts to better achieve the way smoothing is described in the Principles.

(c) Practices 5.2 & 5.4

We have clarified the approach to reviewing investment strategy and how it is described within the PPFM.

We have also clarified our investment approach relating to assets backing asset shares (“return assets”), and assets backing other liabilities (“non-return assets”).

(d) Practices 5.6

We have clarified how derivatives may be used.

(e) Practices 5.9

We have clarified the investment controls that are in place as outlined by the funds own investment mandate.

2. Changes effective from 1 January 2018

(a) General changes

The PPFM has been amended from 1 January 2018. The changes have not been described here as they were minor corrections or clarifications to wording and make no material change to the PPFM.

3. Changes effective from 1 October 2017

The PPFM was amended with effect from 1 October 2017. Most of the changes were as a result of the transfer of the policies of the FP With Profits Fund into a newly established fund in Aviva Life & Pensions UK Limited called the FP With-Profits Sub-Fund, and the closure of the FP With Profits Fund to new business.

(a) General changes

As a result of the transfer, some general changes were made throughout the document, as follows:

- ‘The newly established fund is called the FP With-Profits Sub-Fund
- ‘Fund’ was changed to ‘sub-fund’ in line with the new name, which is consistent with other fund names within Aviva Life & Pensions UK Limited.
- The transfer was made through a Court scheme, and reference in the PPFM is now to the new Scheme under which the sub-fund is managed rather than to the previous 2013 Scheme, and any references have been updated to refer to the relevant section of the new Scheme
- References to Friends Life Limited (‘FLL’) where the FP With Profits Fund was previously held were replaced by ones to Aviva Life & Pensions UK Limited, which is generally referred to as ‘the Company’.
- To reflect the change in the name of the company which provides administration services, from Friends Life Management Services Limited to Aviva Management Services UK Limited.

(b) Introduction and Overview

The previous introduction and overview sections (sections 1 and 2) were replaced by a new introduction (section 1) that is common to all PPFM documents for Aviva Life & Pensions UK Limited. This provides a brief overview of the Company, an explanation of PPFM documents and their governance and some general information on with-profits policies.

(c) Principles 3.1

The wording relating to 'post-demutualisation' business was updated to explain that if past deductions for the cost of guarantees are deemed to have been excessive, these will be refunded to remaining post-demutualisation policies by targeting more than 100% of asset share.

(d) Principles 4.1

The previous Principles required us to maintain three separate Bonus Smoothing Accounts; two for different classes of pre-demutualisation policies and one for post-demutualisation policies. We no longer need to maintain explicit Bonus Smoothing Accounts to enable us to implement our smoothing practices fairly for pre-demutualisation policies. We also wish to be able to operate the Bonus Smoothing Account and Guarantee Charge Account for post-demutualisation policies as a single account when this would be fair and simpler. We thus removed from the Principles the ability to reintroduce this practice.

(e) Principles 5.1

At the end of 2016, we amended our Practices such that rather than aiming to pay out 95% of Adjusted Asset Shares on average on some surrenders, we now aim to pay 100% of Adjusted Asset Shares on average on all surrenders. Having given appropriate notice, we amended the Principles to allow this.

(f) Principles 7.1

This section was updated to note that with effect from 1 October 2017, the FP With Profits Fund was closed to new business. We still accept increments to existing policies and new members to existing group pension schemes.

(g) Practices 7.2

The Practices previously noted a risk that Friends Life and Pensions Limited ('FLP'), to which some of FLL's policies were reinsured, could fail to meet its liabilities, resulting in losses to FLL. This risk will not exist after 1 October 2017 as the business of FLP was transferred to Aviva Life and Pensions UK Limited at the same time as that of FLL. Mention of it was therefore deleted.

There was a guarantee provided by Friends Life Limited over some loan instruments issued by Friends Life Holdings plc. and Aviva plc. The guarantee is now provided by the Company. The risk that these guarantees will be called upon, and the risk that the Company will be unable to repay its own debt instruments, was previously controlled by the requirement for a repayment plan five years before the end date of the debt and is now mitigated by Aviva's forward planning strategy and by a requirement for the With-Profits Actuary to report annually to the With-Profits Committee on the financial impact of the Company's plans, including those for the repayment of loans, on policyholder security. We amended the PPFM accordingly.

The Practices now note that there is an internal arrangement so that the Non-Profit Sub-Fund will absorb any losses arising from the default of external reinsurers of unit-linked business in the FP With-Profits Sub-Fund. This replaced the previous arrangement under which that business was reinsured to FLP, which would have been responsible for meeting any loss.

(h) Practices 7.3

Following the closure to new business, wording relating to the volumes of new business and processes for stopping writing new business was removed.

(i) Principles 9.1

We had a method of determining the amount of capital FLL needed to hold in addition to the regulatory minimum, known as the FLL Capital Policy. There were two parts to this, assessed relative to the risk of FLL not being able to meet its best-estimate liabilities and not being able to meet the regulatory minimum capital requirements. The second part was assessed using what is known as the Solvency Risk Appetite. After 1 October 2017, only the Solvency Risk Appetite applies and the Principles have been amended to reflect this.

Any future changes to the Solvency Risk Appetite which might materially weaken it will require the Company to take account of appropriate actuarial advice, consult the With-Profits Committee and notify its regulators. This is the same protection as previously applied to the key parts of the FLL Capital Policy.

The Principles previously described how Support Accounts and an Additional Account are required to be available within FLL to support the sub-fund. The Support Accounts will continue to be available but the Additional Account, which was in practice of very limited potential benefit to the sub-fund, is no longer required. We amended the Principles to reflect this change and other changes in the operation of the Support Accounts.

(j) Practices 9.2

The Practices previously contained a paragraph to explain that when the value of the liabilities of the FP With-Profits Sub-Fund become sufficiently small, below £250m, we may declare a one-off bonus to use up the surplus in the sub-fund, determine to add no further bonuses, and move the policies to the Non-Profit Sub-Fund. This Practice was changed so that the £250m limit refers to the value of the assets of the sub-fund (excluding those backing non-profit policies) rather than the value of liabilities, as we believe that this is a more appropriate measure. It also allows the option of a series of fixed future bonuses to be paid instead of a single one-off bonus.

In addition, we added the information that, at any time after 1 October 2017, we may merge any with-profits or non-profit sub-funds, subject to certain constraints including taking appropriate actuarial advice and consulting the With-Profits Committee to ensure that the proposal is fair to policyholders.

(k) Practices 9.3

The existing description of the FLL Capital Policy was replaced by wording reflecting the Solvency Risk Appetite, which as described above, replaced it.

The updated wording still states that the sub-fund will be managed on the basis that the FP Support Account is available to support the sub-fund and includes the amount of the account.

As previously, an additional support account is available for post-demutualisation business (policies issued after 9 July 2001). The amount of this account was reduced to £20m as at 31 December 2016 and will reduce in future in accordance with a fixed schedule, as does the main FP Support Account.

Changes were also made to the Practices on how and when a transfer from the FP support accounts may be made and repaid.

(l) Glossary

The glossary was updated to reflect the changes described above.

(m) Appendices

We added appendices to show the new sub-fund structure within Aviva Life & Pensions UK Limited and to summarise the company history including that of the FP With-Profits Sub-Fund. We also updated the appendix of original issuing companies to include those associated with all the with-profits sub-funds in Aviva Life & Pensions UK Limited.

4. Changes effective from 1 January 2017

(a) General changes

References to Friends Provident International Limited ('FPIL') have been removed as it is no longer a subsidiary of Friends Life and Pensions Limited ('FLP').

(b) Overview section 2.6

The Capital Policy sets out the level of capital that the company aims to hold in all but the most extreme circumstances. As the previous version of the PPFM foreshadowed, we carried out a review of the policy during 2016 and made some minor changes, which are reflected in the current PPFM.

(c) Practices 3.2 and Practices 5.2

In the past, we aimed to payout 95% of Adjusted Asset Shares on average on some surrenders. We now aim to pay 100% of Adjusted Asset Shares on average on all surrenders (or, in some cases, a higher value which takes account of a guaranteed maturity value which would shortly be available).

(d) Practices 3.3 and 7.2

In respect of the actions the Company may take in extreme circumstances, section 3.3.2.1 and the table in section 7.2 were amended to reflect a change in approach for 'pre-demutualisation' policies. We may now reduce the percentage of asset share targeted on maturity and surrender to less than 100% rather than introducing an annual deduction from asset share.

(e) Practices 3.4

Some changes have been made to the asset share calculations for the UKP and FPLMA series, removing most of the remaining differences in the way asset share rolls forward or is uplifted.

(f) Practices 4.4

For 'pre-demutualisation' policies, we have decided that we no longer need to maintain explicit Bonus Smoothing Accounts and Guarantee Charge Accounts to enable us to implement our smoothing practices fairly. We intend to amend the relevant Principles later in 2017. However, we have amended the PPFM now to reflect our current practice of only using these accounts in the management of 'post-demutualisation' business, where we note that we may combine the two accounts for the purposes of adjusting asset share.

(g) Practices 6.7

Asset Share shorting helps protect the Fund against the increased costs of providing guaranteed policy benefits in adverse market conditions. The wording has been changed to clarify our approach.

(h) Practices 6.8

Secured funding and securities lending activities entail receiving a payment from other financial institutions in return for lending assets to them. The wording has been changed as we have widened the range of these activities we may carry out.

5. Changes effective from 1 January 2016

(a) General changes

- Some minor updates were made in terminology as a result of new regulations which came into force from 1 January 2016.
- We have noted that the With Profits Committee now comprises at least five members.

(b) Practices 3.3

We made changes to allow more flexibility in setting the margin taken into account before determining whether asset shares should be enhanced from the estate, given that the existing margin was based on values calculated under regulations which no longer apply.

(c) Practices 6.9

Changes were made to the internal governance of investment matters and the investment managers for the fund.

(d) Principles 9.1 and Practices 9.3

We've included a fuller description of capital policy, including those as a result of repaying the capital support held within the fund in 2015, and support arrangements that Friends Life Limited provides for the fund. These arrangements give investment flexibility and improve the security of policy benefits generally and have been updated to reflect changes resulting from the new financial reporting regulations which came into force on 1 January 2016.

(e) Practices 8.2

Details of the expense review, effective from 1 October 2015. From that date, the charges to the fund include a contribution to meeting a shortfall in a closed defined-benefit pension scheme (the Friends Provident Pension Scheme) which staff who manage (or used to manage) the fund's policies belong to. As well as the normal charges from 1 January 2015 we may also make certain one-off charges for significant developments, either for the benefit of with-profits policyholders or to comply with changed regulations.

6. Changes effective from 1 July 2015

(a) General changes

- Changes were made to reflect the fact that Friends Life Limited is now owned by Aviva Life Holdings UK Limited, which in turn is ultimately owned by Aviva plc.
- We have noted that the majority of the With Profits Committee must be independent of Aviva plc and Friends life Limited.

7. Changes effective from 31 December 2014

(a) General changes

Some minor changes were made to improve clarity.

(b) Practices 3.2

Section 3.2 was updated to reflect a new method for targeting payouts when setting the bonus rate for conventional group pension policies that do not provide a final bonus.

(c) Practices 7.2 and 7.3

The business risk of a deficit arising in the staff final salary pension scheme was added to the table in Section 7.2 and new business risks were clarified in Section 7.3.

(d) Practices 8.2

This section was updated to reflect a change to our investment managers.

8. Changes effective from 30 October 2014

(a) General changes

Some changes were made to the introductory sections to reflect the fact that Lombard International Assurance SA has been sold by the Friends Life group.

9. Changes effective from 9 May 2014

(a) General changes

- A number of changes were made to reflect that Resolution Limited was renamed Friends Life Group Limited and Friends Life Group plc (FLG) was renamed Friends Life Holdings plc (FLH).
- Some minor changes were made to improve clarity.