



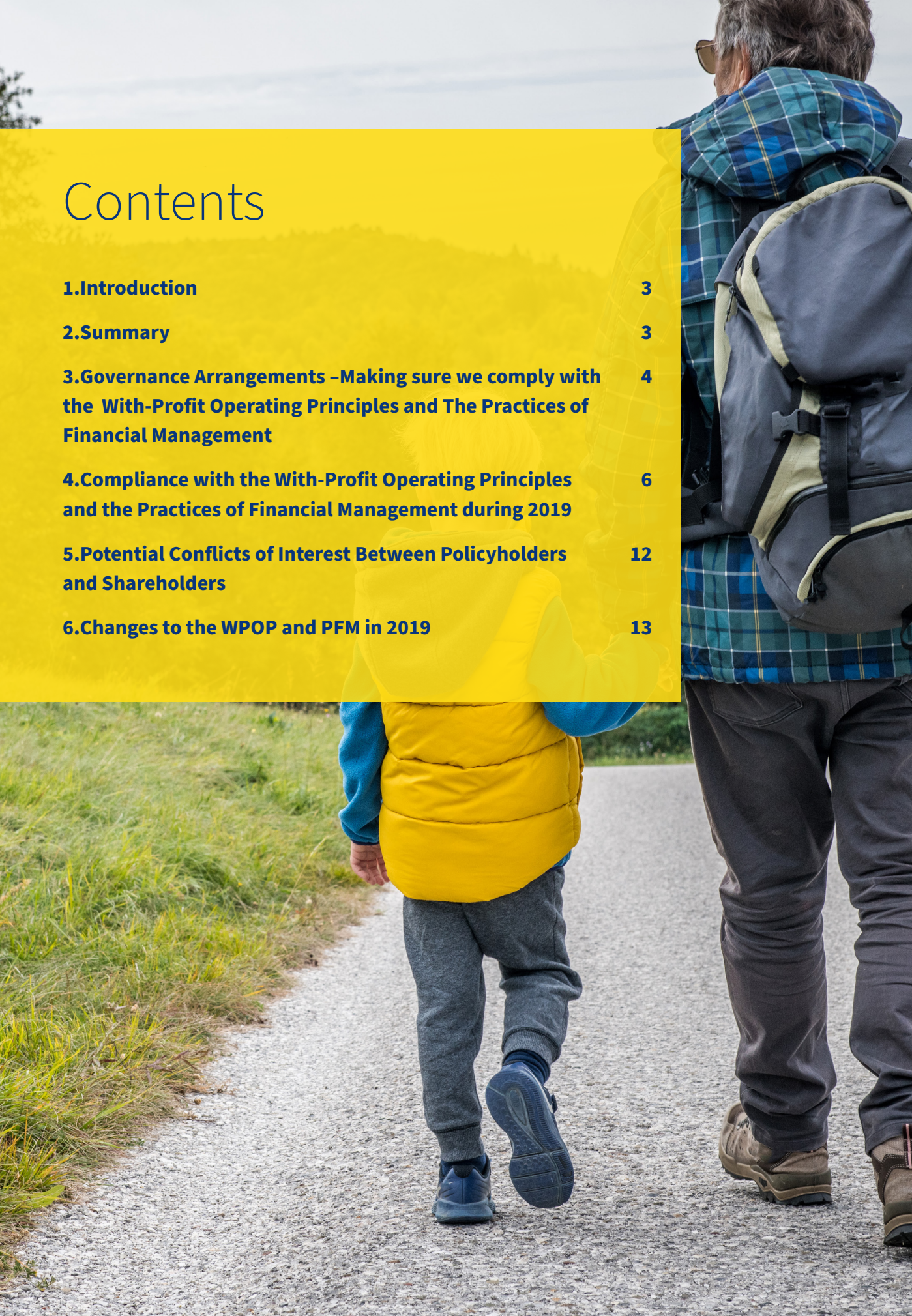
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**Report from the Board of
Aviva Life & Pensions Ireland (ALPI)
Designated Activity Company (DAC)
to its With-Profits Policyholders in the
Irish With-Profits Fund for 2019**



Contents

1.Introduction	3
2.Summary	3
3.Governance Arrangements –Making sure we comply with the With-Profit Operating Principles and The Practices of Financial Management	4
4.Compliance with the With-Profit Operating Principles and the Practices of Financial Management during 2019	6
5.Potential Conflicts of Interest Between Policyholders and Shareholders	12
6.Changes to the WPOP and PFM in 2019	13



1. Introduction

The business in the Irish With-Profits Fund was transferred from Aviva Life & Pensions UK Limited to Aviva Life & Pensions Ireland DAC on 29th March 2019. All policyholders received communications regarding the transfer.

Rules for the management of the with-profits funds of Aviva Life & Pensions Ireland DAC are set out in our With-Profits Operating Principles (“WPOP”) and our Practices of Financial Management (“PFM”). (In prior reports these were referred to as Principles and Practices of Financial Management (“PPFM”). These are available from [aviva.ie/ppfm](https://www.aviva.ie/ppfm).

We also publish some simplified guides on how we manage the with-profits funds, and these are also available from the same website.

This Report from the Board, prepared in consultation with the With-Profits Committee, sets out how we managed the Irish With-Profits Fund in 2019. For the purposes of this report, it has been treated as if the Irish With-Profits Fund had been part of Aviva Life & Pension Ireland DAC for the whole of 2019. This Report does not cover the Participating Fund or Closed Fund, which will be covered by a separate report to the policyholders in those funds.

A printed copy of this report can be obtained by sending a written request to:

Aviva Life & Pensions Ireland DAC, One Park Place, Hatch Street, Dublin 2.

If you have any questions about your policy, please call us on the number shown on your annual statement.

2. Summary

In the opinion of the Board of Aviva Life & Pensions Ireland DAC, throughout 2019 the Irish With-Profits Fund has been managed in accordance with the WPOP and PFM.

The Board is also of the view that the decisions made in managing the Irish With-Profits Fund were both appropriate and treated with-profits policyholders fairly.

3. Governance Arrangements – Making sure we comply with the With-Profits Operating Principles and the Practices of Financial Management

The Board of Aviva Life & Pensions Ireland DAC has overall responsibility for the management of the Irish With-Profits Fund and takes all the key decisions that affect the funds.

Before making these decisions, the Board must seek and consider the advice of the Head of Actuarial Function. The Head of Actuarial Function provides advice to the Board on how discretion in the management of the Irish With-Profits Fund should be applied. The Head of Actuarial Function looks to balance the interests of Aviva's policyholders and shareholders and to ensure that it's with-profits policyholders are treated fairly.

The With-Profits Committee provides oversight of the management of the Irish With-Profits Fund and the application of discretion. The majority of the Committee's members are independent of Aviva and this helps the Committee provide robust challenge to Aviva on its management of the with-profits funds. The views of the Committee on the management of the funds are provided to the Board to help it make the key decisions for the with-profits funds.

Further information on the With-Profits Committee can be found at [aviva.ie/ppfm](https://www.aviva.ie/ppfm).

The activity of the With-Profits Committee

During 2019, the With-Profits Committee considered a wide range of topics. These included:

- The investment strategy of the fund (see section 4.2 below).
- Proposals for bonuses to be added to policies (see section 4.3 and 4.4 below).
- The level of expenses charged to the fund (see section 4.5)
- The management of the Estate, including the level of distributions to policyholders (see section 4.6), which included a first distribution from the Irish With-Profits Fund.
- The transfer of the Irish With-Profits Fund to Aviva Life & Pensions Ireland DAC.
- The review of certain policyholder communications.
- The correction of errors made by the Company that would otherwise have led to policyholder detriment. In particular, the Committee considered the issue discussed below (see section 4.8).
- The ongoing plans to manage the fund as the volume of business in it reduces, known as a “run-off plan”.
- The risk appetite framework used to ensure the security of benefits and to manage the estate distributions.
- The proposals for changes to the PPFM to reflect, mainly, the transfer to Aviva Life & Pensions Ireland DAC (see section 6 below).

In some cases, these matters were considered before the transfer of the IWPF on 29 March, but the Head of Actuarial Function was consulted, and the decision approved by the Board of Aviva Life & Pensions UK Limited, which was responsible for the IWPF up to 29 March 2019.

The With-Profits Committee, in reviewing management recommendations and actions, endeavours to ensure that all policyholders are treated fairly and that an appropriate balance is struck between the interests of different groups of policyholders and between policyholders and shareholders.

The With-Profits Committee is satisfied that it was consulted on the development of the Company's proposals during 2019 and that the views of the With-Profits Committee have been taken into account in the proposals presented to the Board. The Company values the input provided by the With-Profits Committee.

The With-Profits Committee provides its views to the Board on Compliance. The Committee has approved the report of the Head of Actuarial Function referred to below.

These governance arrangements, with their combination of Board level decision making, advice from the Head of Actuarial Function and oversight and challenge from the With-Profits Committee, help ensure that Aviva manages the Irish With-Profits Fund in accordance with its WPOP and PFM and treats its with-profits policyholders fairly.

The Board has received a report from the Head of Actuarial Function (HoAF) on the ongoing compliance of the IWPF with the Principles contained in the WPOP. The report also considers compliance with the PFM.

The HoAF has confirmed that, in his opinion, discretion in relation to the IWPF has been exercised fairly and in accordance with the WPOP/PFM. In the HoAF's opinion the Company has complied with the WPOP/PFM in all material respects but notes the error mentioned below. The HoAF confirms that, in his opinion, the discretion exercised by the Board during 2019 may be regarded as taking, or having taken, the interests of the with-profits policyholders of ALPIDAC into account in a reasonable and proportionate manner with appropriate management of any conflicts. The HoAF notes that the Board agreed to his recommendation to commence distribution of the Estate and requests that it be covered in the Annual Report.

The HoAF identified that the IWPF was incorrectly paying reinsurance premiums in respect of a product in another fund and requested that the Board agree to refund these premiums with interest, which it has agreed to do.

4. Compliance with the With-Profits Operating Principles and Practices of Financial Management during 2019

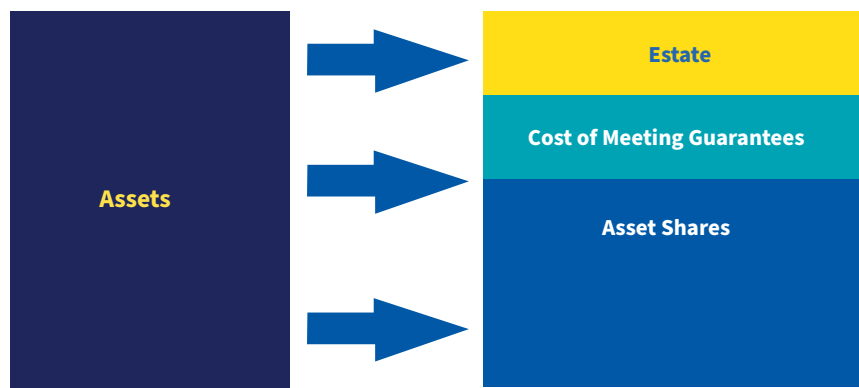
4.1 Introduction

With-Profits Terminology

In broad terms, the assets of the Irish With-Profits Fund are used to back the:

- **Asset Shares** (see below)
- **Cost of Meeting Guarantees**
- **Estate** (see below).

How the assets of the with-profits fund are used



Note: This diagram is for illustrative purposes only and is not to scale.

An explanation of these terms will help you understand how the with-profits fund is managed.

The **Asset Shares** represent the amounts paid in by policyholders whose policies are still in the fund, less deductions for expenses, claims, charges and tax, plus investment earnings on those amounts. This is the value of the policyholders' net contributions to the fund and is the main driver for determining the amounts paid to policyholders.

In some cases, the guarantee that applies to a policy can mean that the amount paid to a policyholder exceeds the policy's **Asset Share**. Where this is expected to happen in the future, assets are put aside to cover the additional **Cost of Meeting Guarantees** (over and above **Asset Shares**).

The assets of the fund in excess of the **Asset Shares** and the **Cost of Meeting Guarantees** are referred to as the **Estate**. The **Estate** provides a buffer against adverse experience, helping to maintain the security of policyholders' benefits. The size of the **Estate** directly impacts the amount of flexibility that the Board has in managing the funds. For instance, the larger the **Estate**, the greater the freedom to invest in assets with uncertain but potentially higher returns, such as company shares and property.

Further information on the Asset Shares and the Estate is provided in the WPOP and PFM.

Areas of Discretion

The principal areas of the management of the fund where the Board has some flexibility or can exercise its discretion are:

- The funds' investment policy, and in particular the investment policy for the **Asset Shares**.
- Setting bonus rates.
- Setting surrender value terms.
- Charging costs and expenses to the funds (including any charges applied to contribute to the **Cost of Meeting Guarantees**).
- The management of the **Estate**, including the investment policy for the Estate.

Whilst the Board can make choices or exercise its discretion in these areas, it must do so in accordance with the rules set out in the WPOP and PFM.

4.2 Investment Policy for Asset Shares

Setting Investment Strategy – How it Works

The investment strategy for the Asset Shares is set by the Board and must observe the procedures and limits set out in the WPOP and PFM. The investment strategy reflects the fund's capacity to take risk, which in turn is dictated by the value of its assets and the level of guarantees provided to its policyholders.

Should the fund have the capacity to take risk then part of the Asset Shares can be invested in assets such as company shares and commercial property, in the expectation that these assets will, in the longer term, provide superior returns. When setting investment strategy, the Board also takes into account current and expected future investment conditions, as well as the advice of our investment managers.

Investment Strategy in 2019

Following the financial crisis in 2008, the investment strategy for the fund has been quite conservative, mainly investing in government bonds. The financial position of the fund has improved in recent years and in 2019 it was agreed to gradually increase the holding in company shares.

The mix of assets is available on our 'with-profits updates' available from aviva.ie/ppfm.

The gross of tax returns achieved on the Asset Shares of the fund in 2018 and 2019 are shown in the table below.

	2019	2018
Conventional business	2.8%	0.7%
Series 1	2.8%	0.7%
Series 2	8.9%	0.0%

The mix of assets backing the Asset Shares and the investment strategy is monitored closely throughout the year.

Conclusion

During 2019, the assets backing Asset Shares were managed in accordance with the requirements of the WPOP and PFM and the Board is satisfied that the investment strategy followed is appropriate for the with-profits policyholders.

The mix of assets backing the Asset Shares and the investment strategy is monitored closely throughout the year.

4.3 Bonus rates

Setting Bonus Rates – How it Works

What are bonuses?

- We add your share of the returns which the with-profits fund earns to your investment, through a system of bonuses.
- Bonuses cannot be negative, but they can be zero, and this provides policyholders with some protection from losses made by the with-profits funds.
- There are two main types of bonus:
 - Regular Bonus
 - Terminal Bonus

What's the difference between Regular and terminal bonuses?

- Regular Bonuses are designed to provide steady growth in the value of your guaranteed benefits over the lifetime of your policy. They are not intended to fully reflect the performance of the fund.
- Terminal Bonuses aim to pay any balance between the Regular Bonuses which we have already added to your policy and the performance of the fund over the whole period of your investment.
- Asset Shares are used as a guide to set Terminal Bonuses and this means that the Terminal Bonuses reflect the performance of the fund. Terminal Bonuses are payable when you cash in or switch your investment out of the With-Profits fund, but they are not guaranteed.
- Our aim is to use Regular and Terminal Bonuses together to provide a balance between the guaranteed and non-guaranteed policy benefits. The guarantees provided protect your benefits from adverse conditions such as investment market falls or poor investment returns.

Where guaranteed benefits exceed Asset Share, it is likely that the Terminal Bonus will be zero. Whilst the Terminal Bonus is zero, policyholders will have benefitted from the guarantee provided to them.

Bonus rates are set for groups of policyholders as opposed to individual policyholders. In this way, policyholders share in the performance of the fund and benefit from the pooling of risk with other policyholders. Changes in bonus rates are smoothed over time with the aim of smoothing out some of the ups and downs that result from the volatility of the funds' asset values.

Smoothing does not, however, protect policyholders from prolonged falls in investment returns which, other than where guarantees apply, will be shared with policyholders.

Bonus rates are set by the Board, having taken the advice of the Head of Actuarial Function and having considered the views of the With-Profits Committee.

Bonus Rates in 2019

At the end of 2019, Regular Bonus rates for some policies were adjusted to provide a better balance between the policies' guaranteed and non-guaranteed benefits in light of market movements and further falls in long-term interest rates. For most products this meant that the Regular bonus rates were either unchanged or there was a modest reduction. The revised Regular Bonus rates provide an appropriate but prudent addition to guaranteed benefits.

Terminal bonus rates were reviewed twice in 2019. Reflecting movements in the investment returns over time, terminal bonus rates generally reduced slightly at the mid-year review, but then increased at the end year review. In 2019, the Board approved the start of distributions from the Estate from July 2019 (see Section 4.6 below for more details), as a result of this, payouts were generally increased over the year.

As explained in its WPOP/ PFM, Aviva aims for 90% of policyholder payouts to fall within target payout ratio ranges. These ranges are expressed as percentages of Asset Share, uplifted where appropriate to distribute the Estate, and are set out in the respective WPOP/ PFM. Where payouts fall outside the target payout range, the fund may be paying out more, or less, than it can afford, to the detriment, or to the advantage, of the remaining policyholders. It is important, therefore, that the majority of payouts are within the target payout ratio ranges. These targets were achieved in 2019 for the Irish With-Profits Fund.

Conclusion

The decisions made by the Board were consistent with the WPOP and PFM and with the advice of the Head of Actuarial Function and the views of the With-Profits Committee.

4.4 Surrender Values and Market Value Adjustments

Policyholders may choose to cash-in or surrender their policies early or to transfer benefits under their pensions policies to another provider. From July 2019, the benefits paid to policyholders who surrender or transfer their policies receive uplifts from the Estate (see section 4.6 below).

The approach for determining surrender values is set out in the WPOP and PFM, and surrender values are set with the aim of paying out Asset Shares. Surrender value rates are closely monitored throughout the year and amended if necessary to continue targeting Asset Share. During 2019 surrender values were adjusted to maintain consistency with Asset Share.

For unitised policies (other than where guarantees apply on early surrender), if the policy benefits exceed the Asset Share, Aviva may apply a Market Value Adjustment (MVA) on the early surrender of the policy so that surrender values properly reflect

the performance of the fund and the value of the underlying assets. This ensures that surrendering policyholders do not benefit from guarantees that are given up on early surrender. If they did, this could be unfair for the remaining policyholders. No MVAs were applied during 2019.

4.5 Charges and Expenses

Charges and Expenses – How it Works

Charges to cover expenses incurred in running the with-profits business are deducted from policyholder benefits. How expenses are charged varies for different blocks of business:

- Expenses are deducted directly from Asset Shares;
- Expenses are charged to the Estate, and management charges are deducted from Asset Shares and credited to the Estate to cover the expenses;
- In addition, certain expenses, such as one-off projects are charged to the estate.

The expenses covered by these charges include the costs of administering the with-profits policies and managing the with-profits investments. The administration services the with-profits policies are provided by Aviva's administration services company.

The permitted expense charges are set out in Management Services Agreements between the IWPF and Aviva Life & Pensions Ireland DAC, which provides the administration and management services for the with-profits business.

Charges and Expenses in 2019

The Management Services Agreements and Investment Management Agreements set out both the services to be provided and the fees that can be charged. An annual review is conducted by the Head of Actuarial Function to monitor fees and services for the Irish With-Profits Fund to ensure that they are in accordance with the agreements. The Company has an established process to correct any issues that arise from such reviews so that the charges made to the funds are fair and appropriate. The review of the 2019 expense charges will take place later in 2020. The review of 2018 concluded that the charges made were in line with the agreements.

Tax was allocated to the funds based on an apportionment of the total tax costs of the company, which was considered fair and reasonable and in line with the requirements of the Court Scheme and the WPOP and PFM.

Asset Share Guarantee Charges

The WPOP and PFM permit Aviva to apply an additional charge to Asset Shares to contribute to the cost of guarantees of the with-profits fund. Such charges are designed to maintain the fund's Estate at an appropriate level so that it provides an adequate level of security for policyholder benefits and provides sufficient freedom to manage the fund in the interests of policyholders.

No such charges to the Asset Shares for the cost of guarantees were made during 2019.

4.6 Management of the Estate

Management of the Estate – How it Works

The Estate provides protection for policyholders' benefits from adverse experience together with the freedom to manage the fund in the interests of policyholders.

Aviva's approach is to manage the Estate with a view to limiting the risk of the Estate being diminished by adverse investment conditions. This helps ensure that the Estates continue to provide security to policyholders in changing conditions. This includes following an investment strategy for the assets backing the cost of guarantees that limits potential losses from changing economic conditions and variations in asset values.

A Risk Appetite Framework is in place for the fund. A Risk Appetite Framework provides rules for how the risks taken in managing a with-profits fund are balanced against the size of its Estate. The Company reviewed the Risk Appetite Framework during 2019.

Management of the Estates in 2019

In 2019, the Board decided to commence distributions from the estate of the Irish With-Profits Fund. This distribution was made because the Estate was larger than the size considered necessary to provide security for policyholders' benefits. The framework for assessing the adequacy of the Estate is set out in the fund's WPOP/ PFM.

The distributions from the Estate is applied as an uplift to the with-profits benefits that would otherwise have been paid. From July 2019, the uplift to benefits was 10%. The uplift has been set at a level that is expected to be maintained, but this cannot be guaranteed. In some circumstances it may be necessary for the extra bonus to be reduced or even stopped. This may happen if economic or investment conditions change significantly.

Conclusion

Throughout 2019, the Estate was managed in accordance with the WPOP and PFM and the Risk Appetite Framework.

4.7 New With-Profits Business

The Irish With-Profits Fund is closed to new business other than a very limited amount of new business for options on and increments to existing policies, and a limited number of new members to existing group pension schemes.

4.8 Other Matters

The Irish With-Profits Fund reinsures a small number of risks on certain policies. These policies are hybrid policies containing a With-Profit element and a non-profit element. The non-profit element is outside with Irish With-Profits Fund. During 2019 the Head of Actuarial Function identified that the Irish With-Profits Fund was being incorrectly charged the reinsurance premium relating to the non-profit element. The Board has agreed with his recommendation to refund the premiums plus interest to the Irish With-Profits Fund. The payment will be made to the Estate.

5. Potential Conflicts of Interest Between Policyholders and Shareholders

Given the level of discretion that can be applied by the Board in managing the fund, there is a potential for conflicts between the interests of policyholders and shareholders to arise. Such potential conflicts include:

- Selecting a less risky investment strategy that reduces risk for shareholders but that might also reduce investment returns for policyholders.
- Choosing to allocate increased expenses and tax costs to with-profits policyholders.
- Encouraging policy exits or failing to point out the value of guarantees given up on exit, where it might be to the policyholder's benefit to retain the policy.
- Choosing to declare lower bonuses so that the cost of meeting guarantees is reduced.

Similarly, there is a potential for conflicts between the interests of different groups of policyholders. Such potential conflicts include:

- Following a riskier investment strategy that might be to the benefit of policyholders who intend to retain their policies for a long period but possibly to the detriment of policyholders expecting to exit the fund in the shorter term.
- Policyholders with policies that have high guarantees might be more relaxed about taking risks than policyholders that have policies with low guarantees.
- Smoothing changes in bonus rates over time may benefit one group of policyholders over another.
- Similarly, the sharing of risks within policy groups may benefit some policyholders to the detriment of others.

Given these potential conflicts, it is vital that:

- There are clear rules and guidelines for the management of the fund.
- Strong safeguards are in place to protect the interests of policyholders.

Rules for managing the with-profits funds are set out in the WPOP and PFM, which are published. The Court Scheme also sets out a number of rules that must be followed by the Company in managing the fund. The rules in the WPOP and PFM and the Court Scheme address many of the potential conflicts of interest.

Compliance with these rules is monitored and the outcome of this monitoring is considered by the With-Profits Committee and the Board. Any breaches are corrected so as to ensure that no policyholders suffer any material detriment.

Discretion in relation to the management of the with-profits funds is exercised by the Board, whose members include individuals who are independent of the Company, and its executive management. Advice on the exercise of discretion is provided by the Head of Actuarial Function, whose appointment must be approved by the Regulator and who must comply with regulatory requirements that are designed to ensure that policyholders are treated fairly. Oversight of the Company's management of the Irish

6. Changes to the WPOP and PFM in 2019

Some changes were made that took effect from 29th March 2019 to reflect the transfer of the business from Aviva Life & Pensions UK Limited to Aviva life & Pensions Ireland DAC.

Some changes have been made that took effect from 1 January 2020. The most significant changes were:

- To reflect the change in investment strategy.
- Changes to the target payout ranges.
- Changes to the smoothing limits.

The only material changes to the Principles in 2019 were to reflect the transfer and policyholders were informed of these changes as part of the transfer process.

Further information on changes to the WPOP/ PFM for each fund is provided in the 'WPOP/ PFM Summary of Change' documents, which can be found at [aviva.ie/ppfm](https://www.aviva.ie/ppfm).

Conclusion

The changes made were reviewed by the Board, the Head of Actuarial Function and the With-Profits Committee and are considered to treat policyholders fairly.





You're safe in the hands of Aviva

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Tel (01) 898 7950 www.aviva.ie.