A GUIDE TO CONVENTIONAL WITH-PROFITS

NFU Mutual
INSURANCE | PENSIONS | INVESTMENTS

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HOW WILL THIS GUIDE HELP?

This guide explains how our with-profits fund works for our conventional with-profits contracts and will help you to decide whether this type of investment is right for you. Please keep it in a safe place with your other documents, to refer to in the future. It is also available on our website nfumutual.co.uk

If you would like more information on how we manage our with-profits fund please read our principles and practices of financial management, available at nfumutual.co.uk, or from our customer services team on 0800 622 323.

IS THIS THE RIGHT GUIDE FOR YOU?

A with-profits investment can either be conventional or unitised. We call a with-profits policy conventional when we guarantee to pay out an agreed amount when the policy matures. This could be a lump sum (the sum assured) or a series of payments (an annuity or pension).

NFU Mutual conventional with-profits policies include:

- Endowments (a regular savings contract that promises to pay a minimum amount at the maturity date), including minimum cost endowments
- Whole of life policies (a regular premium policy that promises to pay out a minimum amount on death), including low cost whole of life policies
- Any other with-profits policy taken out before 1 July 1988.

If you need to check which type of policy you have, please call us on 0800 622 323.

This guide does not cover:

- Unitised with-profits policies – where your payments to us are used to buy units in the with-profits fund
- The capital access bond (CAB)
- With-profits annuities.

1. WHAT IS A WITH-PROFITS INVESTMENT?

A with-profits policy shares in the profits and losses of our with-profits fund.

We share our profits and losses by adding bonuses to your policy. As bonuses are added to your policy, valuable guarantees build up. These are described in section six '**What do we guarantee?**' and are a feature of a with-profits investment.

THE WITH-PROFITS FUND

When you invest in our with-profits policies, we pool the money with the money from other policyholders in the with-profits fund. The with-profits fund is invested in a wide range of assets including company shares, property and bonds. For more details please read section two '**What affects how much I get?**'.

Part of the with-profits fund covers the amount we owe to policyholders. The rest of the fund is called the estate and provides working capital for the fund. To find out more please see section nine '**The estate and how we use it to manage your investment**'.

SMOOTHING

Smoothing is one of the unique features of a with-profits investment. Investment values can be volatile so the value of the with-profits fund can fluctuate considerably. Instead of simply sharing out what the fund makes or loses each year to policyholders, we even out some of the fluctuations. We describe this in section four '**What is smoothing?**'.

GUARANTEES

Our conventional with-profits contracts offer guarantees of the minimum amount of money you will receive when the policy matures or for certain contracts on death. This is explained in section six '**What do we guarantee?**'

Over the life of your policy we aim to increase the value of the guaranteed amount by adding bonuses.

PAYOUTS

The main factor that affects the amount your policy will pay out is what your share of the with-profits fund is worth. Your share depends on profits and losses earned by the fund over the period of your investment. We look at the share for groups of similar policies and use these results to help us decide the bonuses we will pay.

2. WHAT AFFECTS HOW MUCH I GET?

How much you get back depends on:

- The investment return earned on the fund over the period you invest
- The effect of any guarantees
- The way we smooth payouts
- Policy charges and expenses
- The business risks the with-profits fund takes
- The tax we have to pay.

The value of investments may fall as well as rise, you may receive back less than your original investment.

HOW YOUR MONEY IS INVESTED

Our with-profits fund pools your payments (less any deductions to cover charges) with those of other with-profits policyholders.

The with-profits fund invests in a wide mix of different types of assets, such as:

- UK and overseas company shares (equities)
- Commercial property
- Government and company bonds (loans to the government or companies)
- Deposits.

The investment strategy of the with-profits fund reflects what our Board of Directors believes is an appropriate balance between the risks of different investments and the potential reward they offer. Our investment managers aim to maximise the returns on our assets, whilst working within the overall investment strategy.

Higher risk assets, such as equities and property, offer the potential for higher returns over the long-term than lower risk assets such as deposits and bonds. Currently we invest a significant proportion of the with-profits fund in equities and property in order to try and increase returns for our with-profits policyholders.

We may also invest some of the assets in non-traditional assets to optimise the investment returns whilst managing risk by investing across a diversified range of investments. These assets are also known alternative assets. An example of alternative assets is Infrastructure, which comprises investment in physical assets, facilities, and services such as roads, bridges, tunnels, and drainage systems, which are considered essential to the functioning and economic productivity of a society. We only invest in alternative assets if the overall expected return, or the reduction in overall risk, is better than expected on an investment in similar traditional assets. Any such investment will be subject to being able to meet our regulatory capital and liquidity requirements.

The actual mix of assets may change over time, depending on the risks our Board are willing to take and the investment managers' view on potential future returns from different types of asset. (Go to nfumutual.co.uk for information on the current mix).

The amount of risk our Board is willing to take will be influenced by the size of our estate (the excess of our assets over our liabilities) as this offers a cushion against volatility in asset values.

Company assets from outside the with-profits fund may be available both to transfer into the with-profits fund and to support the solvency position of the with-profits fund.

3. WHAT ARE BONUSES?

We aim to increase the amount we guarantee to pay you at maturity by adding bonuses to your policy. There are two types of bonus. These are annual bonus and terminal bonus.

ANNUAL BONUS

Annual bonus is normally added to your policy each year. The level of annual bonus can go up and down and there is no guarantee that a bonus will be added each year.

We announce the level of bonus at least once a year.

Once we have added an annual bonus it is guaranteed to be paid at the maturity date along with the original amount we guaranteed to pay you, unless you alter the terms of the policy. It can not be taken away.

The level of annual bonus may be different for different products and for similar policies taken out at different times.

TERMINAL BONUS

A terminal bonus may be added to your policy when you leave the with-profits fund because, for example, your policy matures, you retire or you surrender your policy.

The level of terminal bonus can go up and down and there is no guarantee that a terminal bonus will be added. We can change terminal bonus levels at any time.

Currently we review terminal bonus levels twice a year or more often if investment conditions change significantly from what we were expecting.

Although we aim to smooth payouts, terminal bonus levels can be volatile and change significantly. This is because we invest a significant proportion of the with-profits fund in higher risk assets (such as equities or property).

We set separate terminal bonus rates for different products. There are also different rates for:

- Similar policies that have been invested for different lengths of time
- Regular and single investments that start in the same year
- Policies with different charging structures
- Whole of life policies for different ages at entry and the length of time premiums were due to be paid.

HOW DO WE SET BONUSES?

A share of the total fund is notionally allocated to your policy, based on:

- How much you have invested
- When you made the investment
- The fund's performance over time, allowing for taxation
- The costs related to running our business
- Various profits and losses (see section eight '**Managing risks the with-profits fund is exposed to**').

This is known as the asset share and is used to decide what bonuses to add to each policy.

Our aim when adding bonuses is to pay out, on average, the asset share of your policy when you leave the with-profits fund. We do this by using asset shares to decide what bonuses should be added to each policy.

To work out the actual bonus level we group similar policies together, and determine a fair return for those policies. Different groups of policies may receive different levels of bonus.

ANNUAL BONUSES

We aim to set annual bonus rates so:

- They are sustainable over the long term, considering current and future expected investment returns
- They will not vary too much from year to year
- Normally there will be scope to add a terminal bonus.

TERMINAL BONUS

Paying a terminal bonus enables us to pay out your share of profits that have not already been paid out as annual bonus. When your policy reaches maturity, or you want to retire, surrender or transfer your policy, we aim to pay out, on average, the asset share of your policy.

The things we consider when setting terminal bonus rates include:

- The asset share compared to the amount already guaranteed (the original guaranteed amount and any annual bonuses already added) for groups of similar policies. This allows us to see how much of the value we haven't given to you already in annual bonuses
- What we expect investment returns to be for the period we intend the terminal bonus rates to apply
- The change in payouts for similar policies from one year to the next. We aim to restrict the change in the amount we pay out to policyholders in consecutive years to what we believe is a reasonable level.

4. WHAT IS SMOOTHING?

Investments values can be volatile so the value of the with-profits fund and your asset share can fluctuate quite a lot. This is because we invest a significant proportion of the with-profits fund in higher risk assets (such as equities and property).

Instead of simply sharing out what the fund makes or loses each year, we even out some of the fluctuations. This is known as smoothing. In practice we may keep some of the growth back when investment conditions have been good, so that we can add it back when investment conditions are poor.

Although the actual amount of smoothing will vary between different types of with-profits policy, the principle remains the same. We also adjust the level of smoothing to maintain fairness between policyholders who voluntarily leave the fund, by for example surrendering or transferring, and those who remain in it. This is to ensure that remaining policyholders are not disadvantaged.

Although smoothing helps to even out some of the fluctuations in investment values, it can not fully protect you from poor investment conditions or long-term market falls. When the value of the asset shares fall, the value of pay outs may also fall. On your maturity date or for certain contracts on death, we guarantee to pay out a minimum amount, this is described more in section six '**What do we guarantee?**'.

We aim to pay out on average, the asset share of your policy. However, as described above, the actual amount we pay will be subject to smoothing. Your payout will usually be between 75% and 125% of the asset share of your policy.

5. SURRENDERING YOUR POLICY

If you decide to leave the with-profits fund early by surrendering or transferring your policy, we aim to pay out, on average, the asset share of your policy. This average is taken over different groups of policies, and over a number of years. We also aim to have a smooth progression from the surrender value to the maturity value, in the years leading up to maturity. Thus in any one year the amount we pay out on surrender may be more or less than 100% of the asset shares of those policies.

The guarantees that your policy has may be valuable. Also, some policies have options that may be valuable. We strongly recommend that you take advice before acting.

6. WHAT DO WE GUARANTEE?

Our conventional with-profits policies contain guarantees. Any guarantees that your plan has are detailed in your policy documentation.

For a conventional with-profits policy we guarantee to pay out an agreed amount when the policy matures. This could be a lump sum (the sum assured) or a series of payments (an annuity or pension).

For endowment and whole of life policies we guarantee to pay a minimum amount on death.

For all types of policy, once we have added an annual bonus, it can not be taken away. It is guaranteed along with the original amount we guaranteed to pay you.

The guarantee of a minimum amount plus any bonuses added at your maturity date may be valuable in poor and volatile investment conditions.

Some conventional with-profits policies have additional valuable guarantees. Some examples are:

- Pension policies taken out between 1 January 1983 and 30 June 1988 have an annuity rate guarantee. When you decide to take your pension benefits, we will offer to convert your accumulated fund to a pension. The rate we use to convert your fund to a pension will be either the guaranteed rate applicable or the current rate we offer, whichever provides you with a bigger pension income. This means that each £1 of your accumulated fund (basic benefit plus any bonuses) will provide a guaranteed minimum income when you retire. This can be a valuable guarantee and would be lost if you transferred the pension to another provider or to another type of NFU Mutual pension policy.
- Minimum Cost Endowments taken out from 1 January 1998 guarantee to pay at least the guaranteed minimum death benefit, at your maturity date or earlier death. This is usually the amount of the mortgage that the policy was taken out to cover.
- Most Minimum Cost Endowment policies taken out before 1 January 1998 have a statement of intent applying to them. This means, as long as circumstances permit, we intend to pay at least the guaranteed minimum death benefit when the policy matures. A small number of these policies do not have the statement of intent. If you do not have the statement of intent we will have written to you.

If you decide to surrender your policy you will lose all entitlement to a maturity value or death benefit. We strongly recommend you take advice before acting.

7. CHARGES AND EXPENSES

The with-profits fund incurs operating expenses in providing advice to customers, selling, underwriting and setting up new policies and in servicing existing policies. We aim to share these costs fairly among different types of policy. The expenses are used to calculate the asset shares and therefore impact on the amount we pay out.

Advice is charged for separately on policies commencing on or after 31 December 2012 and therefore the expenses applied to the asset shares for these policies do not include any costs arising from providing advice.

8. MANAGING RISKS THE WITH-PROFITS FUND IS EXPOSED TO

The performance of the with-profits fund is affected by risks that may increase or reduce the value of the with-profits fund. These risks may change over time.

Currently the major risks facing the with-profits fund as a whole are:

- Potential losses on investments
- The cost of guarantees made on some with-profits policies being greater than expected
- Losses on our non-profit business (such as claims being more than expected)
- Expenses being higher than planned.

Our Board of Directors is responsible for actively managing any risks to the with-profits fund. They approve all significant risks after considering factors including:

- Whether the risk is worth taking
- The size of our estate (see the next section)
- The size of the potential impact on our assets and our ability to pay policyholders
- Our exposure to other risks.

The estate will normally absorb any profits or losses that arise from the risks the with-profits fund runs. However as a mutual organisation, with no shareholders, any losses (or profits) may ultimately be borne by (or credited to) the with-profits policyholders.

9. THE ESTATE AND HOW WE USE IT TO MANAGE YOUR INVESTMENT

The estate is the term we use to describe the excess of our assets over liabilities. Or in other words, what we own over what we owe. It provides us with the money (working capital) to operate our business. We carefully manage the estate so that it is big enough to:

- Provide enough money, so that we can continue to issue new business
- Cover the costs of smoothing
- Meet the costs of certain policy guarantees
- Meet any excess of expenses over charges to with-profits policies
- Provide investment freedom so we can invest in riskier assets which have potential for higher investment returns (for example equities and property)
- Cover one-off exceptional expenses

10. VOLUMES OF NEW BUSINESS

The financial soundness of the with-profits fund can be adversely affected if the company issues too many new policies. Our estate is large enough such that currently we do not set any limits on the amount of with-profits business that we sell in any year. We regularly monitor the levels of new business.

TO FIND OUT MORE

If you would like to know more about investing in the with-profits fund, you can:

- Contact your NFU Mutual Financial Adviser
- Call our Customer Service Team on 0800 622 323
- Read the principles and practices of financial management (PPFM) at nfumutual.co.uk. The PPFM overrides the contents of this guide if there are any differences between the two documents.

NFU Mutual Financial Advisers advise on NFU Mutual products and selected products from specialist providers. Financial advice is provided by NFU Mutual Select Investments Limited. They will explain the advice services and charges.

The value of investments may fall as well as rise. You may receive back less than your original investment.

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To find out more about how we use your personal information and your rights, please go to the Privacy Policy on our website.

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