Customer Friendly Principles and Practices of Financial Management
Order Insurance With Profits Fund

Straightforward financial solutions with a human touch

Foresters
Friendly Society

What are the Principles and Practices of Financial Management (PPFM)

The Society manages a number of funds for its members and these funds have different uses such as managing our insurance business and running the Society's branches. Four of the Society's funds are with profits funds; this means that the with profits policyholders of each particular fund participate in any profits or losses that are generated within the fund. This guide is an outline of how we manage one of these with profits funds, the Order Insurance Fund (OIF).

Principles and Practices of Financial Management (PPFM)

The PPFM is a document describing, in detail, how we manage our with profits funds. Because the PPFM is a long and very detailed document, this guide only highlights its key points.
The PPFM covers:

- Principles: High-level statements that describe our long-term approach to managing the funds.
- Practices: Specific statements on how we intend to put the Principles in place.

We do not expect to change the Principles often, but will do so if we think they could lead to members being treated unfairly, or if they could stop us managing the funds properly. If we do intend to materially change any of our Principles, we must inform you at least three months in advance. This ensures that you will know if our long-term approach is changing.

Practices change more regularly, as we need to be able to respond to how the economy is performing and new rules and regulations. We will publish any changes to Practices on our website and tell you about them in our next letter to you. In this way, you will be kept informed of how our approach has changed.

A copy of the PPFM can be found on our website at: www.forestersfriendlysociety.co.uk

What is the Order Insurance Fund (OIF)?

The OIF is a fund where your money is combined with that of other members and then invested in a range of different assets. Our main objective is to ensure that we are able to pay all the guaranteed benefits, including any annual bonuses added to the policies within the OIF at all times. At the same time we want to maximise the financial returns to policyholders without taking undue levels of risk. Profits are distributed to with profits policyholders by way of annual and final bonuses, although neither is guaranteed in advance.

Annual bonus – This is set by taking into account what the OIF can afford to pay both now and what we can expect it to be able to afford in the future. Annual bonus rates are then set to make sure that we can meet all the guaranteed amounts when they need to be paid and to build a cushion for any final bonus.

Once an annual bonus has been added to a policy it increases the guaranteed benefit and so cannot be taken away. However it is only guaranteed as described in the policy conditions, and is not guaranteed at other times, such as on surrender. An interim bonus may be added if you claim during a period for which an annual bonus has not yet been declared.

Final bonus – When you claim on your policy, if what we calculate as a fair payout on your policy exceeds your total guaranteed benefits then we may add a final bonus to make up the difference.

How do we determine payouts?

In determining what we consider to be a fair payout, the first stage is determining the policy's asset share.

Asset shares are calculated for groups of similar policies by taking into account: the premiums paid; the investment returns earned; deductions made for the charges that we make to cover expenses and guarantees; and adjustments made for tax if appropriate.

Any profit or loss generated by the OIF will be passed on to policyholders by increasing or decreasing the investment return earned.

On most claims we set final bonuses so that on average we pay out the full asset share to policyholders on maturity or surrender. We also use smoothing to make sure that payouts, wherever possible, do not alter significantly from year to year or between similar policies. This may mean the actual payout is higher or lower than the asset share.

The position is slightly different for regular premium whole life policies with guaranteed death benefits but no maturity date. As these policies' asset shares will build up over time as premiums are paid in we would naturally expect some members to die while their asset share is lower than their guaranteed benefit. Final bonus rates are therefore set so that the estimated future cost of providing the benefits payable on death is equal to the asset share for this group of plans.

What is smoothing?

The Society smoothes the returns paid to with profits policyholders with the main aim of protecting policyholders from short term fluctuations in the value of assets within the OIF. However, this approach does not protect policyholders from long term and sustained falls in asset values.

The two main ways that the Society smoothes returns are: setting annual bonus rates that are fairly constant year on year, and aiming to limit the change in payouts on similar policies to a maximum of 10% year on year (subject to meeting the guaranteed benefits of the policies). The Society may make more rapid changes than these in times of significant market or regulatory change.

How is investment return determined?

The investment return is determined for the different types of assets held within the OIF. The investment return credited to a type of policy reflects the investment return of the assets backing that specific policy type. For example our ethical policies are backed by ethical investments and so the investment return on our ethical policies is based on the investment return on our ethical investments.

Also the level of guarantees on an individual policy type may affect which assets we use to back that policy type. If the guaranteed benefits on a policy are high we may have to adopt a safer investment approach in order to ensure that we can meet the guarantee in adverse investment conditions (for example by investing in deposits or fixed interest assets). However where guarantees are relatively low we may invest in assets that have a higher level of risk attached but over time could be expected to outperform the safer assets and thus to provide a better return.

How do we determine charges?

In determining asset shares we make deductions for charges for two main reasons: to cover expenses and to pay for guarantees. For some policy types the level of charges to cover expenses is stated in the policy conditions. Where it is not, the charge is based on what we consider to be the OIF's fair share of Foresters Friendly Society's total costs. This cost is then split between policies with different policies having different shares based on the size and type of policy.

The main guarantees that we charge for are life insurance cover for products which have a significant level of life insurance cover and maturity guarantees for endowment products and certain other products providing guarantees at maturity. The level of these charges may vary from time to time depending upon the actual cost of guarantees.

What happens if you surrender your policy early?

If you surrender your policy, we work out how much to pay you with the aim of being fair to you and to those staying in the OIF. We do this by setting surrender payouts that are broadly consistent with asset share.

What is a Market Value Reduction (MVR)?

If an ISA, Investment Bond or Child Trust Fund policy written since April 2005 is surrendered or transferred out and what we consider a fair payout on policy, when considering its asset share, is less than the contributions paid plus the annual bonuses, then we may apply a market value reduction (MVR).

An MVR reduces the face value of the policy to its fair value to ensure that a fair share of the OIF is left to those remaining in the fund.

MVRs are not applied to payouts on death, and for Child Trust Fund policies no MVRs will be applied to maturity or terminal illness payouts.

How do we invest your money?

The OIF invests in a range of different assets such as:

- equities (shares)
- property
- fixed-interest type assets (such as government Bonds and corporate Bonds)
- cash

We control the risks that come with investing by choosing assets of good quality and by setting limits on the amounts we invest in any one asset or our exposure to any third party. If we think it is right to do so, we may allocate certain assets to specific policies in the OIF. For example, we may do this to reflect the type, the amount and the timing of guarantees.

When deciding exactly what to invest in and how much, we do so by looking at:

- The OIF's current and future financial position and the need to make sure there is enough money in the fund
- The level of guarantees in the OIF
- Members' reasonable expectations, in relation to how your money is invested.

How we manage potential risks?

The OIF is exposed to a number of risks. Our biggest risk comes from the need to pay all guarantees when they are due given the possibility of falls in asset values. The OIF is also exposed to the risk of more members dying than expected - increasing the claim costs, or the risk that our expenses are higher than expected - increasing our charges.

We aim to reduce our exposure to investment risk by changing our investment strategy as market conditions dictate. Currently, we aim to spread risk over the OIF as a whole. However, if a risk arises which is related closely to a particular policy type, we may apply some or all of the cost of this risk to the policies in question as long as this is consistent with the policy conditions and the law.

The other funds of the Society may be used to reduce some of the risks the OIF faces. However the other funds are not normally available to otherwise benefit the OIF policyholders. Similarly the assets of the OIF will be maintained for the members of the OIF and not normally called upon to support other areas of the Society.

How to get in touch

Write to:
Foresters Friendly Society
Foresters House
29/33 Shirley Road
Southampton
S015 3EW

Tel: 0800 783 4162

Fax: 023 8022 9657

Visit: www. forestersfriendlysociety.co.uk

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