

A Guide To How We Manage Our With-Profits Fund

For Conventional With-Profits Policies

This guide is known as our “Consumer Friendly Principles and Practices of Financial Management”, or CFPPFM for short. It is intended to give you an overview of how we manage our With-Profits Fund and how bonuses on our conventional with-profits policies are calculated.

It is an important document that will help you understand how our with-profits policies work, what factors are considered when deciding how much you will get back, and how we manage your money in the meantime. Further copies are available either from our website www.teachersassurance.co.uk - click on the Savings or Investment section, click on With-Profits and then click on the Conventional With-Profits section - or from our Helpline on the number shown below.

If you need any further information, please call our Customer Support Team on 0800 056 0563.

Introduction

This document is a guide for customers with conventional with-profits policies, this type of policy was sold by Teachers Assurance until the end of June 2005.

This document describes how Teachers Provident Society (trading as Teachers Assurance) manages its With-Profits Fund (the Fund). It presents the most important information from our Principles and Practices of Financial Management (PPFM) that applies to conventional with-profits policies. Should there be any differences between this document and the PPFM, the PPFM will apply. The PPFM deals with two main areas:

- **Principles** – these are high-level statements about the general approach we take in managing the Fund, which rarely change.
- **Practices** – these give more information on the way we currently manage the Fund, and can change depending on the economy, regulation, and changes in our business.

A copy of the PPFM can be found on our website www.teachersassurance.co.uk - click on the Savings or Investment section, click on With-Profits and then click on the Conventional With-Profits section – and is also available in print from our Customer Helpline team on 0800 7311093.

This document uses a number of special terms. To help you know which these are, they are shown in **bold**.

Whilst reading the following sections you may want to refer to your policy document and regular bonus certificates or statements.

How do we decide how much your policy pays out?

Teachers Assurance is a mutual friendly society, which means that all of our profits are used for the benefit of our members (who include with-profits policyholders), not shareholders. The amount of these profits helps us to determine the level of payouts to give with-profits policyholders.

For each type of policy we aim to pay an amount that is fair considering the financial and business performance of the Fund over the period while you have held your policy with us, subject to your **guaranteed benefits** and the **smoothing process**. We calculate something called the **asset share** of a policy to help us make decisions about what this amount should be.

Each conventional with-profits policy has a sum assured which is fixed when you take the policy out, and depends on the premium you pay, the term of your policy, your age and your sex. Providing you continue to pay premiums for the agreed period, the sum assured will not change. We aim to increase the sum assured each year by adding **annual bonuses** (sometimes called 'reversionary bonuses'), which, once added, cannot be taken away unless you stop paying premiums. At maturity, the sum assured and **annual bonuses** (these are the **guaranteed benefits** of your policy), and possibly a **final bonus** (sometimes called a 'terminal bonus'), are paid.

For conventional with-profits policies the **asset share** is the amount of the premiums paid, less the cost of providing benefits and the expenses incurred in relation to your policy, increased by the actual return achieved by the Fund. Various adjustments can be made to this **asset share** to reflect other profits or losses made by Teachers Assurance, for example profits from selling other life insurance products.

At maturity, our aim is to pay out approximately 100% of **asset share** however payouts can range from 85% up to 115% of **asset share**. On earlier surrender we aim to pay out between 80% and 120% of **asset share**.

How do we decide what annual bonuses should be?

For conventional with-profits policies we aim to review **annual bonus** rates once a year. In deciding what **annual bonus** rates to set we look at the experience of the Fund (in particular, the investment return earned over the year, and what we expect future returns may be) and the level of **guaranteed benefits** on policies already built up.

In helping us to decide what level of **annual bonus** can be declared, our aim is that the **guaranteed benefits** do not form an unduly large proportion of **asset shares** of policies, in order to help us maintain a healthy solvency position of Teachers Provident Society.

We currently declare two **annual bonus** rates each year, one as a percentage of your sum assured, and the other as a percentage of your previous **annual bonuses**. Once added **annual bonuses** are guaranteed to be paid on death or maturity.

We aim not to alter **annual bonus** rates by more than 1.5% per annum from year to year, (this is part of our process called **smoothing**, described later). However, in adverse circumstances **annual bonus** rates may be reduced by a larger margin and to low levels, possibly even to zero.

You will receive a bonus certificate or statement each year which will show the **annual bonuses** that have been added to your policy.

What is a final bonus?

A **final bonus** may be paid when your policy matures or if you claim beforehand. **Final bonuses** are reviewed at least annually although they may be reviewed more frequently. **Final bonuses** are not guaranteed.

The aim of a **final bonus** is to increase the current value of your policy so that it is approximately equal to the **asset share**.

We look at the sum assured plus **annual bonuses** previously declared on your policy, and if this amount is less than the corresponding **asset share** we may top up the payout with a **final bonus**. However, if previous **annual bonuses** mean that the payout is more than the corresponding **asset share**, we may decide that no **final bonus** is payable. It is important to realise that a **final bonus** is not guaranteed.

For conventional with-profits policies, the **final bonus** is applied as a percentage of the total **annual bonuses** added to your policy up to the date of claim.

How do we manage your money?

Our aim is to obtain long-term growth. This means investing in a range of assets including equities (company shares), fixed-interest bonds (both government and corporate), index-linked bonds, property and cash. It is our intention to invest in a wide spread of investments so if one asset class performs poorly, the returns on other asset classes may compensate. This is known as diversifying our investments.

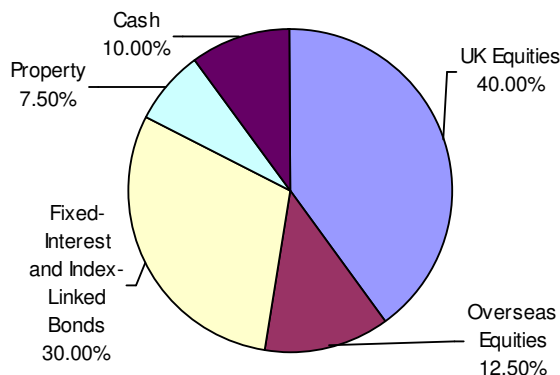
We currently use Legal & General Investment Management Limited to manage the assets within the equity and bond asset classes, with Teachers Assurance choosing the proportion of the Fund that should be invested in each class. Property and cash are managed internally.

We regularly review the appropriateness of our mix of assets in the Fund. The mix of assets may change over time, depending on the level of the guarantees given to policyholders, the financial health of Teachers Assurance and the investment return prospects for each asset class.

The overriding principles considered when setting the mix of assets are to ensure that we can meet our obligations to policyholders now and in the future, and to remain financially strong.

Over the longer-term, equities and property investments have tended to out-perform other forms of investment; we therefore aim to have a high percentage of these types of investment in the Fund, up to a maximum of 60%. However, the factors referred to above may mean that at certain times the percentage held could be lower than this, potentially down to zero.

The long-term target asset mix is as follows:

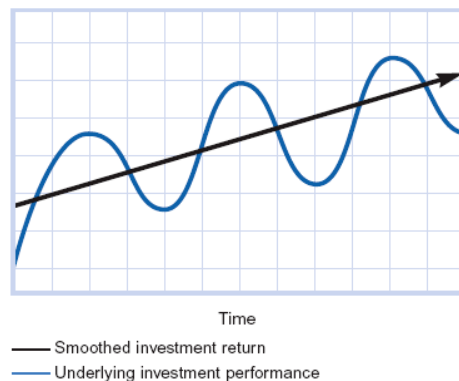


The current asset mix can be found on our website, www.teachersassurance.co.uk, - click on the Savings or Investment section, click on With-Profits and then click on the Conventional With-Profits section and select "How do you manage the Fund" - or is available from our Customer Helpline team on 0800 731 1093.

What is smoothing?

We use a process called **smoothing** to help protect our with-profits policyholders from sudden changes in the value of our investments. However, **smoothing** cannot protect with-profits policyholders against long-term poor investment returns. Because of the **smoothing** process, the amount we pay out may be higher or lower than the corresponding **asset share**.

Smoothing means that in good years we hold back some of the profits and use them to declare higher bonuses in the future years when returns may not be so good. In the long-term, the effect of **smoothing** is expected to be neutral.



This chart is for illustrative purposes only.

To be fair to all policyholders, we aim to limit the change in maturity amounts of similar conventional with-profits policies from one year to the next to 10%, subject to meeting the guaranteed benefits of the policies. During periods of exceptional circumstances the change in payouts may exceed this percentage in order to treat all policyholders fairly. Surrender value payments may be smoothed to a lesser extent than maturity payments.

How do we cover the expenses of your policy?

Teachers Assurance incurs expenses when setting up and administering your policy, which are paid for out of the Fund, and are taken into account when working out the **asset shares** of policies. We try to make sure that the expenses taken out of **asset shares** are fair and reflect the costs each type of policy has incurred. Types of expenses include:

- Policy running expenses, for example collecting premiums, paying claims and policy administration.
- Investment expenses on the assets within the Fund.
- Sales and marketing costs.

Sales and marketing costs over and above those quoted in new business illustrations, and certain exceptional costs, will not be charged to **asset shares**, but paid for out of the **free assets** (described later).

How do we control the risks we take?

Teachers Assurance encounters many risks through its day-to-day activities and the decisions it makes. It is our responsibility to ensure that these risks are well managed, and do not endanger the financial position of Teachers Assurance.

When assessing new risks, for example launching a new product or setting up a new administration system, we endeavour to make sure that expected future bonuses and returns for existing policyholders are not adversely affected, and that the return for taking the risk is acceptable. We also have to make sure that we have enough capital (**free assets**) to undertake the risks.

Profits or losses made from certain risks, for example profits made from selling other life insurance products, are accounted for in the calculation of a policy's **asset share**. Profits or losses from other risks, for example one-off expenses or exceptional costs, are borne by the **free assets**.

Your policy is a long-term one and cashing-in early may not be in your interests. The risks associated with your product are explained in your Key Features Document (where issued).

What are the free assets?

The **free assets** (sometimes referred to as the inherited estate) are the extra assets in the Fund on top of those put aside to meet expected payments to current policyholders. They fulfil some very important roles:

- Allowing us to take on new risks and sell new policies
- Giving us the freedom to invest in assets with more unpredictable short-term returns, but higher expected returns in the long-term
- Acting as a buffer to help with **smoothing**
- Being available to meet one-off expenses and exceptional costs

The size of the **free assets** also helps to demonstrate to our regulator (the Financial Services Authority) that Teachers Assurance is in good health and has a cushion against unexpected events.

If Teachers Assurance decides it has excess **free assets**, it may use part of the excess that the Board of Directors considers appropriate to ensure the ongoing strength and vibrancy of Teachers Assurance. Examples of such usage could include, but are not limited to, supporting new business to attract new customers and distributing to existing with-profit policyholders.

Further information

Our full PPFM, available in print from our Customer Helpline team or on our website – www.teachersassurance.co.uk - click on the Savings or Investment section, click on With-Profits and then click on the Conventional With-Profits section, gives a more detailed description of our approach to managing our With-Profits Fund.

You can also find more information in your policy literature.

Please refer to your policy document, regular bonus certificates or statements and the original Key Features Document (where issued) or policy brochure.

For any further information on your policy and our With-Profits Fund please call our Customer Support Team on 0800 056 0563.