Report of the Board to With-Profits Policyholders 2015-16

FCA Rules require the Directors of LICI to report to the with-profits policyholders of its UK Branch on how their interests have been looked after during the year. This report covers the period 1st April 2015 to 31st March 2016, the last full financial year for LICI.

In April 2005 LICI published its Principles and Practices of Financial Management (PPFM). These set out the way in which the company intends to manage its with-profits business and how it ensures that customers are treated fairly. A consumer-friendly version of the PPFM is also available on our website. You can also request a copy from us.

There were no changes made to the PPFM or to its consumer friendly version during the year.

This report follows the various sections in the PPFM.

Over-riding principles

The Branch has four key financial objectives. These are:

(a) To meet the contractual obligations to policyholders

(b) To meet the tests of solvency and capital adequacy as required by regulatory bodies

(c) To treat policyholders fairly and meet the reasonable expectations of with-profits policyholders

and

(d) Subject to (a), (b) and (c), to maximize the financial returns to with-profits policyholders and the shareholders.

During the period the Branch has ensured that all contractual obligations are met and has comfortably met the various regulatory capital requirements throughout the year.
The Branch has also ensured that it has treated its policyholders fairly by paying them the claim values in accordance with its bonus policy.

Amounts payable

Asset shares show the amount the premiums paid by policyholders would have accumulated to, allowing for the investment return achieved by the Branch and deducting a share of the expenses of the Branch and allowing for the cost of any risk benefits and tax.

The Branch calculates individual policy asset shares for each participating policy (except accumulating with-profits contracts, including ISAs) within the Branch with profits portfolio. The individual policy asset shares are aggregated by product type to assess whether maturity payouts are falling within the target range in the PPFM. The asset share model has been amended during the year to more accurately reflect the renewal expenses, particularly with regards to those subsidised by the shareholder, and a revision in how the historic investment has been calculated in order to have a consistent methodology. These have resulted in a slight increase in the asset shares.

FCA rules concerning payouts require the Board to set target ranges for payouts and to ensure that most payouts fall within that range. These ranges are 80% to 120% of asset share for maturing policies and 75% to 115% for policies which surrender.

The Branch has been in a situation for a number of years where, for policies sold prior to April 2004, the guaranteed benefits exceeded their respective asset share. As the sums assured and attaching declared reversionary bonuses are already guaranteed these cannot be changed. Over recent years, bonus rates have been reduced to rectify this situation. However, payouts still exceed the asset shares for these policies.

Many of the policies maturing within the 2015-16 financial year have payouts greater than 120% of the asset share. This position may change once positive investment returns are achieved in future and the impact of lower bonuses reduces payouts for maturities in the coming years.

Annual and final bonuses

Having analysed the asset shares and policy payouts for both Series 1 and Series 2 conventional policies, the annual bonus rate for policies has been kept the same as last year for the year ending 31st March 2016. The final (terminal) bonuses are reduced for Series 2 pre 2008 endowments from 15% to 10% as the amounts set aside by the corporation in respect of these policies are a greater proportion of asset shares than those for other policies, as are the overall payouts for maturing policies.

On account of low redemption yields of UK government bonds, the reversionary bonus rate for ISA contracts remained at 0.25% from 1stApril 2015 to 31st March 2016. The terminal bonus rate methodology for ISA contracts has been changed during the year with the aim of achieving fairness between the policyholders.

Smoothing

The UK Branch aims to smooth the fluctuations of investment return and other sources of surplus over the period of the contract. The branch restricts the amount by which claim values on identical policies maturing in consecutive years can change to 10%pa except in extreme circumstances.

In the year2015-16,payouts on a group of sample regular and single premium endowment policies for terms of 5, 10, 15 and 20 years increased between 0% to 5%.However, for a group of sample regular and single premium endowment policies for terms of 25 & 30 years the reduction in payouts was around 1%.

The change in asset share values for the same sample policies during the year is dependent on both term and whether a policy is a regular or single premium policy. Asset share values for these sample policies have all reduced during the year. The reduction is due to the reduction in investment returns and increase in expenses.

A Market value reduction (MVR) has been applied to some ISA contracts during the financial year 2015-16.

Investment policy

The Branch's investment policy delegates investment decisions to Investec Wealth & Investment Management Ltd. The Board believes the fund manager provides a satisfactory level of service. The Board also believes that the investment practice has been in line with the investment policy as specified in the PPFM. The Branch's investment policy allows for investment in UK equities, overseas equities, bonds and deposits within the following ranges:

Asset Class	Range
UK Equity Shares	0-36%
Overseas Shares	0-13%
Fixed Interest	55-100%
Cash	0-10%

The investment returns (yield on the fund)is low at 0.99%compared to 11.27% achieved last year mainly due to the fall in the equity markets

Business Risks

The Branch is managing its business risks in line with the PPFM. The Board in consultation with the AFH and WPA is considering various strategic options available to the Branch. It is also managing the agreement with Wapeka Ltd to ensure that good quality service is provided to the Branch and its customers.

Expenses and Charges

The expenses of running the business have been charged to policyholders' asset shares except those subsidised by the shareholder.

Transfer to shareholders

The distribution of surplus is governed by section 28 of the Life Insurance Corporation Act 1956 (of India); this section is amended by Indian Parliament; the amendments are effective from 31st March 2012. The amended section of the Act provides that 90% or more of such surplus, as the Government of India may approve, shall be allocated to or reserved for the policyholders.

For the year 2015-16, the Government of India has allowed 95% of surplus to be allocated to the policyholders in accordance with the PPFM.

Changes to the PPFM

There has been no change made to the PPFM during the year other than formatting changes.

Other issues

New business sales continue at a low level, mainly due to the implementation of Retail Distribution review (RDR), the new regulatory requirements for distribution of retail investment products that came into effect from 1stJanuary2013.

Many regulatory requirements for the Branch changed from 1 January 2016 when a new EU-wide standard was introduced. This includes different requirements for calculation of required capital and reporting to the regulator.

The Board, in consultation with the AFH and the Government of India, is currently exploring various options for the Branch, keeping in mind the best interest of policyholders.

The Board is ensuring that progress is made on the issues highlighted by the With Profits Actuary in her report to the Board.

Summary

Having reviewed the period in question, the Directors are pleased to report to the with-profits policyholders that in its opinion the affairs of the Branch have been managed in accordance with the firm's PPFM and that the interests of these policyholders have been looked after in a satisfactory manner.

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Report of the With-Profits Actuary to Policyholders of the UK Branch of Life Insurance Corporation of India

I reported to the Board of Life Insurance Corporation of India ("LICI") in accordance with the requirements of the Supervision Manual of the Financial Conduct Authority ("FCA") Handbook. This informed them of my view of the way in which the Principles and Practices of Financial Management ("PPFM") have been applied and how discretion has been exercised in respect of the with-profits policyholders of the UK Branch of LICI.

I am also required by the Supervision Manual to draft a report to with-profits policyholders to accompany the firm's annual report required by COBS20.4.7R of the FCA Handbook stating whether, in my opinion, the discretion exercised by the firm in respect of the period covered by the report may be regarded as taking the interests of the firm's with-profits policyholders into account in a reasonable and proportionate manner. In doing this, I must have regard to the rules and guidance laid down in COBS20.2 of the FCA Handbook.

I can confirm that, in my opinion, the Board has generally acted in a manner consistent with the PPFM in the year from 1 April 2015 to 31 March 2016. There are items that require further work:

1) The Board needs to ensure the Branch complies with all the requirements of Section 20 of the FCA's Conduct of Business Sourcebook on Treating with-profits policyholders fairly, especially with-profits corporate governance and ensuring that continuing to write new business is not detrimental to existing with-profits policyholders. The Board is currently considering a range of options for the Branch's future.

2) The Board needs to incorporate the individual policy asset shares within the surrender value methodology for conventional business to ensure fair values are paid to all policyholders. Work has begun on this and the methodology is expected to be adopted in the 2016/17 year.

3) The Board needs to create a ring-fenced fund for the shareholders, and instruct its investment managers to hold separate assets in respect of this fund. The Board has agreed that such a separation should be carried out and discussions have begun on the appropriate method to carry out this split.

I can confirm that, in my opinion, the Board has taken the interests of with-profits policyholders into account in a reasonable and proportionate manner and that the transfer to shareholders is consistent with reasonable expectations of policyholders.

Alison Carr, With-Profits Actuary for the UK Branch of LICI
12 July 2016