



Principles and Practices of Financial Management of Metropolitan's Discretionary Participation Products

Client summary

Smoothed Bonus Business

This document summarises how Momentum Metropolitan Life Limited ("Metropolitan") manages its smoothed bonus business, and explains where and how we invest, how we smooth investment returns and what bonus rates we declare. It focuses on the management of the pooled investment portfolio and not on all the other features of the different policies.

Metropolitan follows the obligations stated in the policy contract and complies with any legal and regulatory requirements. If there are any differences between this summary document and the policy contract and legal requirements, the contract and legal requirements will be considered final and correct.

What are discretionary participation products?

These are products that rely on the ability of the insurer to use its discretion (i.e., decide what is in the best interest of all the policyholders invested in those portfolios) to manage them with regards to investment of assets, the smoothing of returns and bonus declarations.

Managing discretionary participation products requires trust between policyholders and Metropolitan. We take decisions that are in the best interests of policyholders and the sustainability of the portfolios. Sustainability of the portfolios means that we will use and invest the policyholders' money wisely, and that investment returns are smoothed appropriately.

What is a smoothed bonus portfolio?

A smoothed bonus portfolio is an investment in which your money is pooled with other policyholders' money. The returns to policyholders are 'evened out', or smoothed, over a number of years. This means that the bonus rates declared in one year may be higher or lower than the actual investment returns in the portfolio.

How does a smoothed bonus portfolio work?

Metropolitan invests the pool of money contributed by you and other policyholders in a range of suitable assets such as equity, bonds, property, cash and offshore assets, and we manage the portfolio for all the policyholders. The actual investment returns in the market earned on the pool of assets will vary from year to year and may sometimes be negative.

Metropolitan distributes the smoothed bonus portfolio's returns to policyholders by a process known as a bonus declaration. We declare bonus rates that are more stable than the actual investment returns in the portfolio, which is why the bonus rates we declare within a given year are likely to be higher or lower than the actual investment returns in the portfolio in the same year. The bonus rates declared are in the form of a total bonus rate and a vested bonus rate. These terms are explained further below.

Who should invest in a smoothed bonus portfolio?

A smoothed bonus portfolio is a suitable choice for policyholders who are looking for long-term (more than five years) growth on their investments, and who also want protection against sudden and unpredictable changes in the equity, property and bond markets.

How does smoothing affect my policy?

Your policy has an investment account where your premiums (minus appropriate fees) are guaranteed and grow with the bonus rates that Metropolitan declares, but shrinks when money is paid out to you in claims and when we charge fees. In rare circumstances, your investment account may also shrink if we have to reduce the non-guaranteed (non-vested) portion of your account. An example of a rare circumstance is a severe market crash with little to no recovery.

What fees do Metropolitan charge?

Metropolitan charges you to administer the policy and in some cases to pay shareholders for providing guarantees (see below). The charges depend on the type of policy you have. Your policy contract will explain this in more detail.

What are the guarantees?

On some types of policies, Metropolitan guarantees a minimum payout when you claim due to death or when your policy reaches its end date as stated in your policy contract (known as maturity or retirement date). When your policy matures, you will receive the higher amount between your investment account and the guaranteed maturity value. Your policy contract explains the guarantees that apply to your policy.

How does smoothing affect my payout?

Metropolitan pays you the benefits from your policy if you were to die, retire, become disabled or when your policy matures. Because of smoothing, the payout may be higher or lower than the market value of your policy's share of the assets in the portfolio at the time. This will work in your favour if investment markets are down, but if investment markets have performed well before we pay out, you may have received bonus rates lower than the actual returns on the assets.

What will happen to my policy if I decide to cash it in before the maturity date?

Your payout will be subject to an early termination fee (also known as a surrender penalty) in line with South African law. Please speak to your adviser for more information about the 'early termination' fee.

The payout may also in some circumstances be subject to a market value adjuster ("MVA") which is explained below, and means that the money in your investment account will be reduced further upon payment.

What is a market value adjuster?

The market value of the assets in the pooled smoothed bonus portfolio can be lower than the value of all the policyholders' investment accounts that share in the pool in some circumstances, for instance, when investment markets are down. If this is the case, we may reduce the investment accounts of policyholders who cash in their policies (entirely or partially) early by the MVA.

If Metropolitan did not apply the MVA when policyholders cash their policies in, these policyholders would receive more than the actual value of their policies at that time. This would mean that the policyholders who still have policies invested would receive lower bonus rates in future, which is not fair to them.

An MVA will not apply on a contractual claim such as a death, disability, maturity or retirement claim.

How does Metropolitan decide on the bonus rates to declare?

Depending on the economic outlook and interest rate forecasts, Metropolitan decides what a sustainable level of bonus would be. We may use returns that were earned in previous years, but which have not been distributed as bonus rates, to increase the bonus rate in the current year or in future years. Similarly, we may hold back part of the returns earned in the current year and use these to increase bonus rates in future years.

Returns not distributed as bonus rates in a particular year stay in the pool of assets, and we may distribute these to policyholders at a later stage. Metropolitan will not keep any of these undistributed returns.

When we declare bonus rates, different groups (called a bonus series) of policyholders may receive different bonus rates. The bonus series that your policy falls into depends on when you took out your policy, the type of policy (for example, whether it is an endowment or a retirement annuity), the fee structure and the tax treatment of your policy.

Metropolitan declares bonus rates based on the recommendation from the Head of Actuarial Function.

When are bonus rates declared and applied?

Metropolitan declares bonus rates once a year shortly after the end of its financial year end on 30 June. The date on which bonus rates are declared is called the declaration date. We apply the bonus rates retrospectively for the bonus year just completed up until the declaration date.

The payment date for benefits to your policy often is not the same as the declaration date. For this reason, we may add an interim bonus to your investment account from the last declaration date to the date of the claim event (e.g., death, disability, maturity, surrender, or retirement) to make sure that your policy also receives the benefit of investment returns since the last bonus declaration. We can revise the interim bonus rates at any time during the year, such as upon a significant change in market conditions.

Can bonuses be taken away?

Metropolitan declares two bonus rates each year; a total bonus rate and a vested bonus rate. The total bonus rate is applied to the total fund and the vested bonus rate is applied to the vested fund. Vested bonuses cannot be reduced or removed if a contractual claim occurs, however it is not guaranteed in the case of non-contractual claims, e.g., full surrenders, partial surrenders or other withdrawals of funds before the policy terminates, as a market value adjuster may be applied.

The difference between the total bonus rate applied to the total fund and the vested bonus rate applied to the vested fund is the non-vested bonus, which is the portion that can be reduced or removed in rare circumstances. An example of a rare circumstance is a severe market crash with little to no recovery.

How are the underlying assets invested?

Metropolitan invests the assets underlying smoothed bonus products in a range of suitable assets. The assets chosen will enable us to meet the guaranteed benefits when they fall due while maximising expected returns and at the same time limiting the risk of large falls in the value of the assets.

How Metropolitan manages policyholder interests?

If the market value of the assets in the smoothed bonus portfolio drops significantly below the value of all the policyholders' investment accounts that share in the pool, and the investment returns in the market are unlikely to recover soon, in order to protect the portfolio and make sure all policyholders are treated fairly, other than applying a market value adjuster, Metropolitan may:

- change how the underlying assets are invested;
- reduce or remove non-vested bonuses;

- inject money into the portfolio on a temporary or permanent basis; or
- declare lower bonus rates going forward.

How can I get more information?

You can view a more detailed document called Principles and Practices of Financial Management of Metropolitan discretionary participation products (PPFM) at www.metropolitan.co.za or request it from your financial adviser or from our head office.

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