Bonuses

The Equitable Life Assurance Society

Founded 1762

31 December 1993

The Equitable Life's approach to With-profits business

The Society's with-profits contracts effectively provide the opportunity for investment in an actively managed and wide-ranging portfolio of assets covering fixed-interest securities, equities (both U.K. and overseas) and property. The essential feature of with-profits business is that it smooths out fluctuations in earnings and asset values which are generally associated with investment in such portfolios.

With every contract a certain minimum level of benefit is guaranteed. The exact nature of that guarantee depends upon the precise type and form of contract. Earnings on the assets in the form of interest, dividends and rent, as well as appreciation in their market value, are averaged out and are passed on to the policyholders by way of guarantees and bonuses of various kinds.

Each year, bonuses are declared by the Directors on the advice of the Appointed Actuary, following his valuation of the Society's assets and liabilities. These bonuses, once allotted, increase the guaranteed benefits under the contracts.

A final share of profits is also allotted at the point the benefits become contractually payable. The rates of bonus used to allocate a final share of profits are determined by the Directors from time to time.

The major part of bonuses arises from the activity associated with the investment of the premiums or contributions on with-profits contracts. Since, however, the Society has no shareholders the with-profits policyholders effectively stand in the position of proprietors sharing in any profits made or losses incurred in running the business.

How the Society's bonus system operates

The Society offers two broad types of with-profits contract under which either:

(A) each contribution paid secures its own slice of benefit independently of other benefits (often referred to as **recurrent single contribution** contracts)

or

(B) regular, fixed premiums are payable with the benefits being secured by the overall premiums payable (often referred to as level **annual premium** contracts).

The bonus system operates in different ways depending upon the type of contract.

(A) Recurrent Single Contribution Contracts

(1) *Bonus system*

(a) The Society determines an overall rate of return for the calendar year. That is made up as follows.

Guarantee under the policy

Each contribution, after a deduction for expenses, accumulates at a rate of interest (which may be zero) guaranteed explicitly or implicitly in the policy.

Declared bonus rate

This is equivalent to an additional rate of guaranteed accumulation but determined and applied retrospectively. The rate applies for one year at a time and is declared at the end of each year, on guaranteed benefits secured and previously declared bonus.

Final bonuses

Final bonuses are also determined and applied retrospectively. The final bonus is calculated so as to top up the growth arising from the policy guarantees and the declared bonus rate for the year to the full overall rate of return announced for the year. Final bonuses do not add a guaranteed element to the contract, and the final bonus element of a policy can be varied up or down in future.

(b) Interim overall rate of return

Following a valuation of the Society's assets and liabilities, policy value calculations are carried out as at 31 December. The resulting declared and final bonus additions become due on the payment of benefits in the year beginning on I April following a valuation. The policy value at the 31 December prior to that I April is accumulated to the actual date of payment at the appropriate interim overall rate of return. The interim overall rate of return includes the rate of interest guaranteed in the policy.

(2) *Con tract terms*

Under the terms of the contracts, benefits are guaranteed to be payable at full value at certain dates only. The examples which follow assume that the calculations are done at such a date.

(3) *Results of the Declaration at 31 December 1993 for pension contracts*

These rates apply for the major classes of the Society's pension contracts.

Overall rate for 1993	**13% on total benefits purchased up to 31 December 1993.**
Declared bonus rate for 1993	**4% (applied to the guaranteed policy value plus previously declared bonus).**
Interim overall rate of return (untilchanged)	**10% per annum accruing on a daily basis (applied to the total policy value).**

(4) Examples

(a) **Pension contract** (ignoring explicit expense deduction)

Assume £1,000 paid on 1 July 1993, on a new contract with a guaranteed accumulation rate of 3 1/2% per annum.

The value of the benefit as at 31 December 1993 on rates in force from 1 April 1994 would be calculated by accumulating the £1,000 for 183 days at 13% per annum to give £1,000 x (1 + $^{183}/_{365}$x.13) = £1,065.18.

The amount of £1,065.18 would be made up as follows:

Guaranteed basic benefit	1,000 x (1 + $^{183}/_{365}$x .035)	=	£1,017.55
New declared bonus	1,017.55 x $^{183}/_{365}$x .04	=	£20.41
Final bonus	1,065.18 - 1,017.55 - 20.41	=	f27.22
			£1,065.18

The benefit statement issued in February 1994 would then show a value as at 1 April 1994 of £1,065.18 accumulated for 91 days at 10% per annum (the interim overall rate of return applicable at 1 April 1994) to give

$$£1,065.18 \times (1 + .10 \times \frac{91)}{365} = £1,091.74$$

If that benefit were payable on 1 June 1994, then, assuming no change in final bonus rates, the value would be

$$£1,065.18 \times (1 + .10 \times \frac{152)}{365} = £1,109.54$$

(b) **Pension contract** (ignoring explicit expense deduction)

Assume a contract effected before 31 December 1992 with a value as at that date of £1,500 (on rates in force from 1April 1993) made up as follows:

Guaranteed basic benefit	£1,000.00
Attaching declared bonus	£200.00
Final bonus	£300.00
	£1,500.00

N.B. The benefit statement issued in early 1993 would have shown a value on 1 April 1993 calculated by accumulating the £1,500 for 91 days at 10% per annum (the interim overall rate of return applicable at 1 April 1993) to give

£1,500 x (1 + $^{91}/_{365}$x .10) = £1,537.40

The value of the benefit as at 31 December 1993 on rates in force from 1 April 1994 would be £1,500 x 1.13 = £1,695 made up as follows:

Guaranteed basic benefit	1,000 x 1.035	= 1,035.00 (where 3 1/2% is the guaranteed rate of interest)
Attaching declared bonus	200 x 1.035	= 207.00
New declared bonus	(1,035 + 207) x .04	= 49.68
Final bonus	1,695 - 1,035 - 207 - 49.68	= 403.32

The benefit statement issued in early 1994 would then show a value as at 1 April 1994 of £1,695 accumulated for 91 days at 10% per annum (the interim overall rate of return applicable at 1 April 1994) to give

$$£1,695 \times (1 + .10 \times \frac{91)}{365}$$

= £1,737.26

(c) With-profits annuity

Assume a policy was effected on 1 April 1989.

Assume a bonus rate of $6^1/_2$% per annum was anticipated, so that payments remain level if declared and final bonus rates are $6^1/_2$% per annum. The initial amount of annuity was £1,000 per annum.

The payments in the year commencing as shown are as follows:

Year beginning 1 April	1989	1990	1991	1992	1993	1994
See *note*	£	£	£	£	£	£
(1) Guaranteed annuity	1,000	938.97	881.66	827.85	777.32	729.88
(2) Bonus annuity added as a result of 1990 declaration	-	52.87	49.64	46.61	43.77	41.10
Bonus annuity added as a result of 1991 declaration	-	-	69.85	65.59	61.59	57.83
Bonus annuity added as a result of 1992 declaration	-	-	-	61.10	57.37	53.87
Bonus annuity added as a result of 1993 declaration	-	-	-	-	47.00	44.13
(3) Bonus annuity to be added as a result of the 31 December 1993 declaration at 4% per annum	-	-	-	- -		37.07
Total annuity now guaranteed	1,000	991.84	1001.15	1001.15	987.05	963.88
Final bonus annuity	-	90.61	90.78	105.89	119.79	170.80
(4) Total payable in year beginning 1 April	1,000	1,082.45	1,091.93	[illegible]	1106.84	1,134.68
	(already paid)	(already paid)	(already paid)	(already paid)	(already paid)	

Notes

(1) $938.97 = \frac{1,000}{1.065}$; $881.66 = \frac{938.97}{1.065}$ etc.

(2) Bonus was declared at 7.5% for the two years 1989 and 1990.

$52.87 = 938.97 \times \frac{7.5}{100} \times \frac{274}{365}$; $49.64 = \frac{52.87}{1.065}$ etc.

$69.85 = (881.66 + 49.64) \times \frac{7.5}{100}$; $65.59 = \frac{69.85}{1.065}$ etc.

(3) Bonus was declared at 6.5% for 1991.

$61.10 = (827.85 + 46.61 + 65.59) \times \frac{6.5}{100}$; $57.37 = \frac{61.10}{1.065}$

(4) Bonus was declared at 5.0% for 1992.

$47.00 = (777.32 + 43.77 + 61.59 + 57.37) \times \frac{5}{100}$; $44.13 = \frac{47.00}{1.065}$

(5) Bonus was declared at 4.0% for 1993.

$37.07 = (729.88 + 41.10 + 57.83 + 53.87 + 44.13) \times \frac{4}{100}$

(6) Total annuity at 1 April 1993 less the accumulation at the then current interim overall rate of return of 10% per annum for the 91 days between 31 December 1992 and 1 April 1993 to give the value as at 31 December 1992.

$$\frac{1,106.84}{1 + .10 \times {}^{91}/_{365}} = 1,079.92$$

Value as at 31 December 1992 accumulated to 31 December 1993 at the overall rate of 13% per annum for 1993 taking account of the $3^1/_2$% per annum interest implicitly guaranteed in the guaranteed annuity benefits.

$$= \frac{1,079.92 \times 1.13}{1.035 \times 1.065} = 1,107.08$$

(this is the value as at 31 December 1993)

Total annuity payable from 1 April 1994

$$1,134.68 = 1,107.08 \times (1 + .10 \times \frac{91}{365})$$

(i.e. value as at 31 December 1993 accumulated at the interim overall rate of return of 10% per annum for the 91 days between 31 December 1993 and 1 April 1994).

(7) Please note that past performance is no guarantee of future performance.

(5) Results of the Declaration at 31 December 1993 for flexible protection plans, regular savings plans, critical illness plans, major medical cash plans and bonds

Overall rate for 1993	**10.25% on total benefits purchased up to 31 December 1993.**
Declared bonus rate for 1993	**5.25% (applied to the guaranteed policy value plus previously declared bonus).**
Interim overall rate of return (until changed)	**8% per annum accruing on a daily basis (applied to the total policy value).**

(6) Example

With-profits bond (ignoring explicit expense deduction)

Assume a contract effected before 31 December 1992 with a value as at that date of £8,700 (on rates in force from 1 April 1993) made up as follows:

Guaranteed basic benefit	**£ 6,500.00**
Attaching declared bonus	**£200.00**
Final bonus	**£2,000.00**
	£8,700.00

N.B. **The value on 1 April 1993 was calculated by accumulating the £8,700 for 91 days at 8% per annum (the interim overall rate of return applicable at 1 April 1993) to give**

£8,700 x (1 + 91/365 x .08) = £8,873.52.

The value of the benefit as at 31 December 1993 on rates in force from 1 April 1994 would be

£8,700 x 1.1025 = £9,591.75 made up as follows:

Guaranteed basic benefit		=	**6,500.00**
Attaching declared bonus		=	**200.00**
New declared bonus	**(6,500 + 200) x .0525**	=	**351.75**
Final bonus	**9,591.75 - 6,500 - 351.75 - 200**	=	**2,540.00**

The value as at 1 April 1994 is £9,591.75 accumulated for 91 days at 8% per annum (the interim overall rate of return applicable at 1 April 1994) to give

$$£9{,}591.75 \times \left(1 + \frac{.08 \times 91}{365}\right)$$

= £9,783.06

(B) Level Annual Premium Contracts

The declared bonus rate is applied to benefits in respect of the policy year ending during the calendar year 1993. These rates apply for the major classes of private life assurance business. There are certain other contracts (for example, deferred annuities, pension assurances and those in the minor-profits class) which are not covered here.

(1) *Declared bonus rates (vesting 1 April 1994)*

Endowment policies
For the policy year £3.50 was granted for every £100 of sum assured.

In addition, £2.25 was granted for every £100 of previous bonus additions.

Whole-life policies
(other than flexible savings plans)
If the policy had been in force less than 12 years at the end of the year £3.75 was granted for every £ 100 of sum assured.

If the policy had been in force at least 12 years £3.75 was granted for every £100 of sum assured plus £0.30 for each complete year in force in excess of 11 at the end of the year.

Flexible savings plans
If the policy had been in force less than 16 years at the end of the year £3.75 was granted for every £100 of basic withdrawal benefit.

If the policy had been in force at least 16 years £3.75 was granted for every £100 of basic withdrawal benefit plus £0.25 for each complete year in force in excess of 15 at the end of the year.

(2) *Final bonus rates*

Endowment policies, whole-life policies and flexible savings plans
From 1 April 1994 and until changed the final bonus rate is shown in the table below.

Number of complete years for which the policy has participated in the with-profits class (at 1994 Policy Anniversary)	Final bonus as a percentage of the total of the guaranteed benefits plus declared bonus additions %	Number of complete years for which the policy has participated in the with-profits class (at 1994 Policy Anniversary)	Final bonus as a percentage of the total of the guaranteed benefits plus declared bonus additions %
1	8.5	16	85.5
2	11.0	17	90.0
3	13.0	18	95.0
4	15.5	19	99.0
5	18.0	20	102.5
6	20.5	21	1060
7	24.0	22	109.0
8	28 0	23	112.0
9	31 .0	24	115.0
10	40 5	25	117.5
11	47.0	26	1180
12	56.0	27	118.5
13	66.0	28	119.0
14	76.0	29	119.5
15	81 .0	30 or more	120.0

The above rates apply if benefits are contractually payable on the 1994 policy anniversary.

In the event of benefits becoming contractually payable on a date other than the 1994 policy anniversary, the proceeds which are eligible for bonuses will be calculated as if benefits had become payable on the 1994 policy anniversary and the amount so calculated will then be increased by 0.30% for each complete month by which the date of the claim falls after the 1994 anniversary, or decreased by 0.30% for each complete month by which the date of the claim falls before the 1994 anniversary.

Policy benefits

The following tables illustrate how policy benefits have built up as a result of The Equitable Life's bonuses.

Retirement policy (available to the self-employed and those employees who are not members of a pension scheme). Personal pension plan policies, introduced on I July 1988, are written on the same terms as retirement policies.

Benefits for male age 65 on 1 April 1994, secured by a series of contributions of £500 per annum:

Policy effected 1 April	Term of policy in years*	Total benefit including bonuses at age 65**
1969	25	£124,199
1974	20	£ 69,478
1979	15	£ 32,951
1984	10	£ 11,512

* the number of contributions paid IS one more than the term of the policy

** available for purchasing a pension

Endowment policy

Benefits for male age 30 next birthday at the outset and paying premiums of £30 a month, policy maturing 1 April 1994 (effected on normal terms):

Policy effected 1 April	Term of policy in years	Basic sum assured	Total sum assured and bonuses at maturity
1969	25	£8,504	£ 53,566
1974	20	£6,613	£ 31,545
1979	15	£4,966	£ 16,889
1984	10	£3,274	£ 6,833

Please note that past performance is no guarantee of future performance.

About The Equitable Life

The oldest mutual life office in the world
Founded in 1762 The Equitable Life is the oldest mutual life assurance society in the world, and first developed policies based on the scientific principles used by all life companies today.

The Equitable Life has never paid commission to third parties for the introduction of new business. New business, both of a private and company nature, comes to The Equitable Life mainly as a result of its high ranking in surveys of policy results carried out by various journals and through recommendations made by financial commentators, professional advisers and existing policyholders.

The Equitable service
Attached to a national network of branch offices are representatives and specialists fully trained to assist with matters related to life assurance, pensions and annuities. Whether advice is required on a particular problem or there is a preference for a comprehensive survey to establish effective solutions to a range of problems, our local branch office will be pleased to assist.

Note
The information contained in this booklet is based upon the Society's understanding of current legislation.