

Annual report for 2007 from the Board of Liverpool Victoria Friendly Society Limited (“LVFS”) to its with-profits members

1. Introduction

On 31st March 2004 we published our Principles and Practices of Financial Management (“PPFM”) which describes how we manage our with-profits business. The PPFM was subsequently amended in October 2005, mainly to reflect the introduction of the All-In-1 Investment Bond, and at 31st December 2005, mainly to reflect the introduction of “target ranges” (payouts as a percentage of Asset Shares) and at 31st December 2006 mainly to reflect a change to the smoothing period for With Profit Pension Annuities, and a change to allow the investment strategy of the inherited estate to differ from that of the with-profits fund. Further changes from 11th October 2007 are described in Section 6 of this report.

We have reviewed the operation of the with-profits business of LVFS during 2007.

It is our opinion that:

- LVFS has complied with its obligations relating to the PPFM in force during 2007;
- the manner in which discretion was exercised over the period was appropriate; and
- competing rights, interests or expectations of with-profits members or groups of with-profits members have been addressed appropriately.

Our opinion takes account of the way that payouts have been made and how with-profits assets have been managed. This report sets out the reasons for our opinion by reference to the key areas of discretion set out in the PPFM.

The LVFS With Profits Actuary advised on the operation of our with-profits business throughout the period while the With Profits Committee provided independent judgement to the exercise of discretion.

In preparing the report we have taken advice from the LVFS With Profits Actuary. A separate report from the LVFS With Profits Actuary addressed to with-profits members is annexed to this report.

2. Key areas of discretion in the PPFM

The key areas of discretion in the PPFM are discussed in the following sections of this report as follows - Management of Policy Payouts (Section 3), Management of Assets in the With-Profits Fund (Section 4), Asset Share Charges (Section 5), Changes to our PPFM (Section 6), With-profits Members Communications (Section 7) and Other Aspects of the PPFM (Section 8)

3. Management of Policy Payouts

We determine the level of policy payouts after taking into account the current and projected financial position of the fund.

With-profits policies typically contain guarantees, usually in the form of a minimum guaranteed amount to be paid on maturity, retirement or death and made up of a guaranteed amount plus the addition of annual bonuses. In addition, for most policies, a final bonus payment may be made.

3.1 Annual and Interim Bonuses

Investment markets produced before tax investment returns, in respect of assets backing asset shares, of 11.2% in 2006 and 5.7% in 2007. However, for some policies, particularly conventional pension policies, the guaranteed benefits already provided generally remained high compared to the underlying investment values, or exceeded them. As we expect investment returns in the future to be at lower levels than we saw over the 1980s and 1990s, we reduced the rates of annual and interim bonus on conventional pension policies at the declaration in February 2007. The rates on other business generally remained unchanged.

These reductions mean that we limit overpayment where the guaranteed amount already exceeds the underlying investment value and we limit the risk of future overpayment where the guaranteed amount is below the current investment value. We believe these reductions are necessary in order to maintain fairness between different generations of with-profits members and different policy types and provide us with greater flexibility in the way the fund is managed.

No new pricing series were introduced during the year. A new bonus series was introduced for the launch of the With Profits Pension Annuity (Series 3).

3.2 Final Bonus Rates and Payouts at Maturity

We determine final bonus rates using specimen current and projected Asset Shares for sample policies as a guide, allowing for the smoothing of investment returns and payouts consistent with the practice stated in our PPFM. Specimen Asset Shares are calculated as the accumulation of the plan's investments in the fund at the rate of growth achieved by that part of the fund backing Asset Shares, allowing for factors such as our expenses, the cost of death benefits, the cost of guarantees and the impact of taxation.

For some major classes of policies, where it is not appropriate to use Asset Shares, other methods were used that do not affect the resulting payouts materially.

We reviewed final bonus rates in January 2007, at which time rates were generally reduced. In determining these bonus rates the Board used its discretion to pay more than would be indicated by Asset Shares by allocating miscellaneous surpluses arising from business risks. The Board did not consider it necessary to review final bonus rates again during 2007.

No changes were made to the historical assumptions or parameters used in Asset Share calculations or other methods used during 2007, as none were necessary.

3.3 Surrender Values for Conventional Business

Surrender payouts are regularly monitored against target ranges; these reviews did not indicate that changes were needed. As a result, surrender value bases for conventional with-profits policies were not revised during the year. The basis on which conventional pension policies are converted to paid-up policies was revised in February 2007. The revised basis continues to provide with profits members with a fair return but is now more transparent.

3.4 Surrender Values for Unitised Business

Where policy conditions permit, we may apply Market Value Reduction factors (“MVRs”) to unitised with-profits policies to reduce their face value if this exceeds the underlying asset value and if this is necessary in order to treat all with-profits members fairly. MVRs reduce surrender payouts to the plan’s Asset Share allowing for the smoothing of investment returns, these are calculated automatically on an individual policy basis. We have been applying MVRs since the extreme equity market falls of 2000 to 2002. During 2007 the level of MVRs fell significantly, as a result of increases in equity markets over recent years and in many cases Terminal Bonuses are now added.

3.5 Target Ranges

The LVFS PPFM states that we aim to make payouts on maturing, surrendering and transferring policies that are between 75% and 135% of Asset Share with a least 90% of payouts being between these levels. We can confirm that the payouts made during 2007 satisfied these requirements.

4. Management of Assets in the fund

We determine the investment strategy for the fund after taking into account the current and projected financial position of the fund.

We instruct our investment managers to carry out the strategy and challenge them to deliver returns in excess of an appropriate benchmark.

During 2007 the return achieved in respect of assets backing Asset Shares was 5.7%, before tax, and we have credited this return to Asset Shares. This represents an out-performance of 1.9% against the benchmark set.

We delegate investment decisions to our investment managers, Liverpool Victoria Asset Management, who operate within the limits that we prescribe. During the year there were no material changes to these limits in respect of assets backing with-profits Asset Shares.

Asset type	Assets backing Asset Shares as at -	
	31 st December 2007	31 st December 2006
Equities	60%	63%
Fixed Interest and Other	25%	22%
Property	15%	15%

The fund also holds fixed interest assets backing non-profit liabilities written within the fund. We made no change to the general nature of these assets, which are designed to match the liabilities.

The fixed interest assets held within the fund during 2007 were managed within the credit rating limits detailed in the PPFM.

The fund also holds assets that are not normally traded including physical assets such as the Society's office buildings, subsidiary companies and any actual or potential loans or guarantees provided. The out-turn from these investments does not directly impact the amounts payable under with-profits policies. There were no significant changes to these assets during the year.

The fund has the resources to meet fully the reasonable benefit expectations of all our with-profits members and has working capital to enable it to withstand adverse events in most reasonably expected scenarios, although specific returns cannot be guaranteed.

5. Asset Share Charges

During 2007 the Society made explicit charges for the cost of any guarantees selected on All-In-1 Investment Bond policies and implicit charges on some unitised with-profits policies for any product guarantees. During the year the Society, although it is able to, decided not to make a charge for the cost of guarantees or for the use of capital in its Asset Share calculations for any other type of policy.

6. Changes to our PPFM

We made some changes to our PPFM at 11th October 2007. No changes were made to the Principles. The changes made to the Practices were largely to improve the clarity of the Practices in respect of the approach to setting bonuses for the With Profits Pensions Annuity following the introduction of Series 3.

Details of all changes to the PPFM can be found at:

http://www.lv.com/upload/lv/lv_equals/pdfs/Savings/LVFSPPFM_Changes_doc_3-0.pdf

7. With-profits Members Communications

All communications are sent to the last recorded known address of our members.

7.1 Bonus Notices

Most with-profits members receive an annual bonus notice giving details of the bonus added to their policy and other important information relating to their policy and the management of the fund.

7.2 Consumer Friendly PPFM

On 31st December 2005 we published a Consumer Friendly explanation of the PPFM called "Your Guide to how we manage our With-Profits Fund", this is a less technical guide to help members understand how the fund is managed. Separate versions are available for conventional, unitised, accumulating and All-In-1 Investment Bond policies. These are available at http://www.lv.com/savingsandinvestments/ppfm/manage_wpf and were mailed to with-profits members during 2006 with their bonus notice. If we make a material change to these documents in the future then we will distribute an updated version with a future bonus notice.

7.3 Other Communications

Further information is provided on our Website at:

[LV= With Profits Performance](#)

[The spread of investments in the main Liverpool Victoria With Profits Fund](#)

[With Profits Information - Savings and Investments - Principles and Practices of Financial Management \("PPFM"\) - LV= - UK](#)

covering:

- Bonus News Releases
- Investment Spread
- PPFM

In addition with-profits members have access to individual quotations and projections on request through our customer helpline on 0845 640 5279.

8. Other aspects of the PPFM

8.1 Exposure to business risk

During 2007 the Board approved the Society undertaking new business activity in the acquisition of the New Business Operations of GE Life and the acquisition of the Britannia Rescue business.

No compensation costs were paid during 2007 that affected with-profits payouts.

9. Conclusion

It is our opinion that:

- LVFS has complied with its obligations relating to the PPFM;
- the manner in which discretion was exercised over the period was appropriate;
and
- competing rights, interests or expectations of with-profits members or groups of with-profit members have been addressed appropriately.

Mike Rogers
Chief Executive
March 2008

Dennis Holt
Chairman

ANNEX

Annual Report for 2007 from the With Profits Actuary to the with-profits members of Liverpool Victoria Friendly Society Limited (“the Society”)

I have reviewed the Society’s annual report to its with-profits members. I have also reviewed the discretion exercised by the Society during 2007 so far as this affects the interests of its with-profits members.

This report is made solely for the purpose of section 4.3.16 of the FSA Supervision manual. It is made solely to the Society’s with-profits members, and accordingly, to the fullest extent permitted by law, I do not accept or assume any responsibility to any other person in connection with this report.

Respective Responsibilities of the With Profits Actuary and Directors

The directors are responsible for the establishment of governance arrangements designed to ensure that the Society complies with its Principles and Practices of Financial Management (“PPFM”) and for the exercise of discretion in the management of with-profits business. The directors must prepare annual reports to each class of with-profits member stating whether, throughout the financial year to which the report relates, the Society believes that it has complied with the obligations relating to its PPFM. The report must set out the directors’ reasons for that belief.

As With Profits Actuary my responsibilities are primarily to advise the Society on key aspects of the discretion to be exercised in respect of each class of the Society’s with-profits members. In so advising I am required by statute to cover the implications for the fair treatment of the Society’s with-profits members and to take into account their information needs and the extent to which any communication may be regarded as clear, fair and not misleading. I am required to report to the Society’s governing body once a year on key aspects of the discretion exercised by the Directors during the year affecting the with-profits business of the Society. The scope of that report includes those aspects on which I have already provided advice to the directors. I am further required to make a written report to the Society’s with-profits members, to accompany the Society’s annual report. My responsibilities as With Profits Actuary are set out in statute and in Actuarial Professional Guidance.

Basis of opinion

I have been appointed by LVFS as With Profits Actuary throughout 2007. My appointment covers all classes of with-profits business written by LVFS and by other group companies.

I report to you my opinion as to whether, based on the information and explanations provided to me by LVFS, and taking into account where relevant the rules and guidance in section 20.2 of the FSA Conduct of Business Sourcebook, the LVFS annual report and the discretion exercised by LVFS in 2007 may be regarded as taking, or having taken, the interests of the LVFS with-profits members into account in a reasonable and proportionate manner.

During 2007 I have advised LVFS on key aspects of discretion to be exercised in respect of:

- bonus rates to be applied to policies at maturity and on the death of a with-profits member
- annual bonus rates
- investment policy
- surrender value methodology (including market value reductions)
- new business and its impact on the security of benefits of existing business
- allocation of expenses to with-profits business
- changes to the PPFM
- communications with with-profits members

I have carried out a review of key aspects of the discretion exercised by LVFS in 2007 affecting each class of with-profits business of LVFS. Following this review I have formally reported to the directors that the management of LVFS with-profits business during 2007 has complied with the relevant PPFM and that the exercise of discretion over the period was appropriate and maintained fairness between different categories of policy and between with-profits members and the Society.

I have reviewed the LVFS annual report to its with-profits members for 2007.

In carrying out my reviews I have sought such information and explanations as I considered necessary in order to provide me with sufficient evidence to give the opinion required.

Opinion

In my opinion the LVFS annual report for 2007 and the discretion exercised by LVFS during 2007 takes, or has taken, the interests of the LVFS with-profits members into account in a reasonable and proportionate manner.

Ian Blanchard
With Profits Actuary
Liverpool Victoria Friendly Society Limited
March 2008