Principles and Practices of Financial Management

Professional Provident Society Insurance Company Ltd
(PPS Insurance)

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1. Introduction

The Professional Provident Society was established in 1941 as a mutual Society providing benefits to its members. Following a restructuring during 2001 the Professional Provident Society Limited (PPS Limited) was established as the holding company representing members' interests. In 2011 PPS Limited was converted into the PPS Holdings Trust. PPS Insurance operates as a subsidiary of the PPS Holdings Trust and undertakes to provide long term insurance business exclusively for graduate professionals.

PPS Insurance has no external shareholders, and all profits earned by the business are allocated to PPS Holdings Trust ordinary members via their PPS Profit-Share Accounts, a policy benefit of PPS Insurance policies.

This document outlines the PPS Insurance PPFM in order that our policyholders can better understand the bonus allocation principles and practices in place for PPS Insurance, as well as the investment strategy adopted by the PPS Insurance Board.

2. Principles and Practices of Financial Management (PPFM)

This document, which is available on our website and can also be sent to you on request, is intended to explain how we will manage bonus allocations by PPS Insurance to its policyholders. PPS Insurance supports the establishment of the PPFM as an important part of the overall governance and financial management of discretionary policyholder benefits.

PPS will each year certify that we have operated our business in line with the Principles and Practices of Financial Management (PPFM) and inform policyholders if we make changes to it.

We firstly set out the "Principles" and then the "Practices".

Principles are high level, enduring statements of the standards we adopt and are not intended to change very often. When they do we will inform affected policyholders at least 31 days in advance.

Practices describe our approach to managing bonus allocations and these may change more often. When they do, we will inform affected policyholders within a reasonable time period thereafter.

If you have any queries about this document, please call us at +27 860 123 777, +27 11 644 4300 or email us at memberservices@pps.co.za.

3. Governance of the PPS Insurance PPFM

The adherence of PPS Insurance to the Principles and Practices as set out in this document is the responsibility of the PPS Group Audit Committee, who is required to conduct a review on an annual basis.

The PPFM may change as the economic or business environment changes. Any change to a Principle or Practice will be approved by the PPS Insurance Board, on recommendation from the PPS Insurance Corporate Actuarial Department, the Head of Actuarial Function, the PPS Group Actuarial Committee and the PPS Group Audit Committee.

At least 31 days before a change to a Principle is implemented, affected PPS Insurance policyholders will be informed and the proposed change will be published on our website. Any change to a Practice will be published on our website and policyholders will also be informed of such a change in our annual communication to policyholders.

4. Approval of Unvested Bonus Allocations

The PPS Insurance bonus allocations are recommended by the PPS Insurance Corporate Actuarial Department and the Head of Actuarial Function, following the Principles and Practices outlined in this document. The bonus allocations are declared annually after the completion of the financial statements of the PPS Holdings Trust, PPS Insurance and its subsidiaries. The bonus allocations are discussed at the Group Actuarial Committee, the Group Audit Committee and are finally considered and approved by the Board of PPS Insurance.

5 Bonus Allocations

5.1 Overriding Principles

The following overriding principles will take precedence over any other principles.

5.1.1. PPS will meet all its contractual obligations, and legal and regulatory requirements. In the event of a conflict arising between the PPFM, as outlined in this document, and the policy conditions, the policy conditions will prevail. Similarly, in the event of any conflict between the PPFM and the legal and regulatory requirements, the legal and regulatory conditions will prevail.

5.1.2. Any decisions regarding the allocation of surplus will first consider the long-term solvency of PPS Insurance.

5.1.3. Bonus allocations will be declared having regard to policyholders' reasonable benefit expectations which have arisen from original contractual entitlements as well as past practice by PPS Insurance, relevant industry practice and official PPS Insurance documentation made available to policyholders by PPS Insurance. The needs, interests and expectations of the policyholders must be considered in balance with the broader strategic needs of the business. These needs and interests will include ensuring the continued solvency of the company, new business sales and other business development needs.

5.2 Principles

5.2.1. Because of their importance both to the holders of discretionary participation policies and to the financial strength of the PPS Insurance, bonus allocations are approved by PPS Insurance Board.

5.2.2. Bonus allocations will be determined annually.

5.2.3. Bonus allocations will apply to qualifying policyholders who hold qualifying products only and will broadly reflect the investment and operating experience of the business. Qualifying policyholders are ordinary members of PPS Holdings Trust that have purchased a PPS Provider Policy.

5.2.4. For the purposes of this document, profits are taken to mean both profits and losses. Similarly, gains are taken to mean both gains and losses. Bonus allocations may be positive or negative.

5.3 Practices

5.3.1. Each qualifying PPS Provider policyholder will be assigned a notional non-vesting account called the PPS Profit-Share Account. The PPS Profit-Share Account comprises two elements, the Apportionment Account and the Special Benefit Account.

5.3.2. Each year PPS Insurance's operating profits are allocated to the Apportionment Accounts and investment returns are allocated to the Special Benefit and the Apportionment Accounts.

5.3.3. PPS Insurance's operating profits are allocated to the Apportionment Accounts via a Bonus Allocation. The Bonus Allocation for each product is determined with reference to the value of the insurance cover and takes into account various factors such as the number of Units of Benefit, the amount of the Sum Assured, the premiums payable and/or the size of the Special Benefit and Apportionment Accounts.

5.3.4. A portion of the net investment income is allocated to the Apportionment Accounts by means of the Interest Allocation. The amount of the allocation to each policyholder will depend on the size of the member's PPS Profit-Share Account at the end of the financial year of the bonus allocation.

5.3.5. Net realized and unrealized capital gains, and the balance of the net investment income, are allocated to the Special Benefit Accounts by means of the Special Benefit Account Allocation. The amount of the allocation to each policyholder will depend on the size of the member's PPS Profit-Share Account at the end of the financial year of the bonus allocation.

5.3.6. The Bonus, Interest and Special Benefit Account Allocations are nett of any allowance for amounts required to build up the actuarial liabilities.

5.3.7. A degree of balancing is permitted between the different products to prevent excessive volatility in the declared Bonus Allocation rates.

5.3.8. All allocations are non-vesting. Future bonus allocations may be either positive or negative depending on whether profits / gains or losses occur. A negative allocation is equivalent to removing previously allocated profits / gains.

A special “RA Bonus” may be allocated to the Apportionment Accounts of PPS Provider policyholders who are also premium paying members of the PPS Retirement Annuity Fund. This bonus is allocated in a similar manner to the Bonus Allocation, with the exception that the allocation is based on the members’ PPS Retirement Fund premiums in the financial year. The bonus is allocated at the discretion of the PPS Insurance Board and is dependent on the income received by PPS Insurance in respect of the PPS Retirement Annuity Fund less the expenses of running the Fund.

5.3.9. A special “PPS Investments Bonus” may be allocated to the Apportionment Accounts of PPS Provider policyholders who also have, or are the member on record for, investments with PPS Investments. This bonus is allocated in a similar manner to the Bonus Allocation, with the exception that the allocation is based on the assets with PPS Investments in qualifying products. Further, where these assets are invested in PPS Investments portfolios they may receive an additional bonus allocation. These bonuses are to be allocated at the discretion of the PPS Insurance Board and are dependent on the profits earned by PPS Insurance from the PPS Investments’ business, and further dependent on the profitability of the qualifying products and the PPS Investments portfolios.

5.3.10. A special “PPS Medical Aid Products Bonus” may be allocated to the Apportionment Accounts of PPS Provider policyholders who are also members of the Profmed Medical Scheme. This bonus is allocated in a similar manner to the Bonus Allocation, with the exception that the allocation is based on the members’ contributions in the year to the Profmed Medical Scheme. This bonus is to be allocated at the discretion of the PPS Insurance Board and is dependent on the profits earned by the Professional Medical Scheme Administrators, a wholly owned subsidiary of PPS Insurance, in the administration of the Profmed Medical Scheme.

5.3.11. Important to note is that the policyholder is only entitled to their full Apportionment and Special Benefit Accounts on attaining the age of 60 (or on earlier death or full disability claim resulting in natural termination of their policy).

5.3.12. Subject to paragraphs 5.3.13, 5.3.14 and 5.3.15, on termination of the policy prior to the age of 60 (other than for the reasons noted in paragraph 5.3.11), a reduced benefit will be payable (Reduced Termination Benefit) to the policyholder. The reduced termination benefit is calculated with reference to the notional profit share balances of the Apportionment Account plus the Special Benefit Account at the time of the early termination of the policy. This ensures that allowance is made for the duration that the policy was in force prior to its termination.

5.3.13. The value of the Reduced Termination Benefit is calculated by taking:

a) the sum of the balances of the Apportionment Account and Special Benefit Account, at the time of the early termination of the policy;
b) subject to 5.3.15, deducting the interest allocations to the Apportionment Account as PPS Insurance in its discretion may decide;
c) deducting the net of, the Special Benefit Account balance less an amount determined by PPS Insurance taking into account the number of years until age 60.

5.3.14. The forfeiture amount under the Reduced Termination Benefit will not exceed the amount of interest allocations credited to the policyholder's Apportionment Account during the last two financial years as a policyholder of the PPS Provider™ Policy.

5.3.15. No payment will be made from the Special Benefit Account where cover is terminated by PPS Insurance in terms of the provisions of the PPS Provider™ Policy or where, for a reason other than death, cover ceases within three years of the Policyholder becoming a policyholder of the PPS Provider™ Policy.

5.3.16. Interim Bonuses: where a policy is terminated or matures during the course of the year, interim Bonus Allocations are added on a pro-rata basis, based on the previous year's Bonus Allocation declarations.

5.3.17. Interim investment income and capital gains or losses are added based on the actual performance (net of taxes and expenses) of the underlying assets of the PPS Profit-Share Account up until the month prior to the policy termination or maturity. Should there be significant market movements in the subsequent period up until exit, there may be an adjustment made to the final benefit payable to reflect this.

5.3.18. **Final bonuses**: No final bonuses are applicable.

6 Investment strategy

6.1 Principles

The PPS Insurance investment strategy (encapsulated in the PPS Insurance Investment Management Policy and Investment Mandates) aims to maximize long-term returns subject to acceptable levels of investment and solvency risk, having regard to:

- the nature and term of the PPS Insurance liabilities, and the management of cashflows;
- the results of the annual investigation into the matching of PPS Insurance's assets and liabilities, which includes sensitivity tests of different investment scenarios. These results may indicate the need to change existing mandates and the overall investment policy;
- Policyholders' Reasonable Benefit Expectations. Importantly, every effort is taken to emphasize to policyholders the long term view of PPS Insurance in the setting of its investment policy objectives;
- regulatory solvency requirements;
- the advice from the appointed fund managers and consultants;
- the long-term anticipated returns from different asset classes and long term inflation;
- the expected volatility of various different asset classes;
- the current and expected future level of contractual guarantees, if any;
- statutory limitations on exposure to asset classes and individual entities.

PPS Insurance's assets will be invested in an appropriate and broad range of suitable investments in accordance with the Investment Policy and Investment Mandates as approved by the PPS Insurance Board.

The PPS Insurance Investment Management Policy and Investment Mandates are reviewed from time to time and revised as required to ensure these documents remain relevant and appropriate.

Maximum and minimum exposures for different asset classes are set in accordance with the PPS Insurance Investment Management Policy objectives. Maximum exposures to any one counter party are specified.

Investments may be made in derivatives or similar instruments if they are appropriate to the objectives of the investment portfolio and meet the related investment restrictions as set out in the investment mandates.

6.2 Practices

An investment management mandate and agreement exists between PPS Insurance and each of its asset managers, which sets out the required investment strategy, guidelines and benchmarks, fees payable and related requirements. The benchmarks are set taking into consideration the levels of risk inherent in each asset class.

The PPS Insurance Board reviews the performance of the asset managers and is responsible for approving significant investment related decisions (including the appointment, assessment or termination of asset managers and the approval of changes to the PPS Insurance Investment Management Policy). PPS Insurance has an investments department which conducts the fund accounting and compliance functions required.

Currently, the assets backing the PPS Profit-Share Account are invested in a mix of listed equities, property, fixed interest investments, international assets and cash. Asset allocation ranges are set, along with performance targets and benchmarks. The mix of different asset classes is premised on the long-term investment view of the PPS Insurance Board, and as such short term fluctuations in performance can be expected.

The PPS Insurance Board reviews the investment performance and ongoing appropriateness of PPS Insurance's assets regularly.