

# 2022 participating policyowner dividend scale announcement – questions and answers

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For further details on the management of the participating (par) account, see [Financial facts](#) (form 46-4758) and [supporting materials](#).

## 2022 dividend scale announcement

Par policies	Dividend scale interest rate	Dividend scale <sup>1</sup>
Canada Life policies in the combined open account <sup>2</sup> , issued on or after Jan. 1, 2020	Increase from 5.1% to 5.25%	Increase
Policies issued before Jan. 1, 2020:		
<ul style="list-style-type: none"> <li>Policies in the combined open account, formerly belonging to the Canada Life open account, issued on or after Nov. 5, 1999<sup>3</sup></li> </ul>	Increase from 5.1% to 5.25%	Increase
<ul style="list-style-type: none"> <li>Canada Life policies in the closed account, issued before Nov. 5, 1999</li> </ul>	Increase from 5.0% to 5.15%	Increase

The dividend scales will decrease for former Crown Life and New York Life policies.

### Notes

1. Any change in dividends for a particular policy will vary, depending on factors such as the year a policy was issued, plan type, basic risk classification, issue age and others. Past results shouldn't be considered indicative of a par account's future performance. The dividend scale interest rate (DSIR) is only one of many factors that contribute to an individual policy's performance. The actual cash value growth in any policy varies, based on a number of factors such as type of product, product features, premium-paying period, issue age, rating, dividend option, the dividend scale and others.

2. On Jan. 1, 2020, we combined the Great-West Life, London Life and Canada Life Canadian open accounts to form the new Canada Life combined open account.

3. Wealth Achiever and Estate Achiever policies issued after amalgamation are included with the in-force policies formerly belonging to the Canada Life open account issued on or after Nov. 5, 1999.

### 1. What were the main drivers behind the increases in the 2022 dividend scales for the combined open par account and the Canada Life closed account?

Exceptional equity market performance in 2021, as well as changes to our investment strategy, drove positive experience. In addition, interest rates continue to rebound after their pandemic lows from 2020.

Non-investment experience was generally unchanged for the 2022 dividend scale.

### 2. What's the outlook for the dividend scale for 2023?

We don't know what will happen in the future. At least once a year, we review the participating policyowner dividend scale. This includes reviewing experience related but not limited to investments, insurance claims, expenses and other factors. Each year, Canada Life may distribute some of these earnings, if any, in the form of participating policyowner dividends, as approved by the Board of Directors. The amount to be distributed is influenced by the earnings experienced, and by other considerations such as the need to retain earnings as surplus and to reduce short-term volatility in dividends.

Here are some observations about some specific factors that could affect the dividend scale for 2023:

- Interest rates – So far in 2022, interest rates have continued to increase, which could benefit the par account. The account could see higher yields when acquiring fixed income assets. With our fixed-income laddering strategy, we could benefit more from rising interest rates than companies with longer-duration fixed-income assets. Compared with those companies, we could re-invest more of our fixed income assets into the rising interest rate environment.
- Inflation – In today's inflationary environment, the par account could benefit from our investments in non-fixed income assets. Several of these asset classes are considered strong hedges against inflation. For example, real estate values can increase with inflation. And higher prices are often correlated with higher earnings for public equities. However, performance depends on the pace and level of inflation increases. Both asset classes may face headwinds if inflation rises rapidly and remains high.
- War in Ukraine – Our par accounts have no direct exposure to Ukrainian or Russian assets. In fact, they have less than 1% of their assets outside Canada and the United States. The accounts remain very focused on quality companies and assets in strong jurisdictions.
- COVID – So far, COVID-related mortality has had a relatively small effect on the dividend scale. It's still too soon to know what the long-term effect will be. We'll continue to monitor the pandemic's effect on our mortality experience and its financial impact.

### 3. What effect has COVID-19 had on mortality experience in the par accounts so far?

Like other insurance companies, we've seen higher mortality experience during the pandemic, including COVID-related deaths. So far, however, the financial impact of this experience has been relatively small. This is due to factors such as:

- COVID-related mortality demographics – COVID-related claims have largely been on policies with older ages, later durations and larger reserves. This reduced the financial impact of these claims.
- Mortality from other causes – There were reductions in mortality related to some other causes, for example, accidents.
- Reinsurance – Our use of reinsurance continues to help reduce volatility in our claims experience in the par accounts.

It's still too soon to know what COVID's long-term effect will be. We'll continue to monitor the pandemic's effect on our mortality experience and its financial impact.

### 4. Why did we increase the policy loan interest rate?

This increase is in line with recent actions by the Bank of Canada to increase its benchmark interest rate.

### 5. When does the change in the variable policy loan interest rate come into effect?

The variable policy loan interest rate update is effective as of May 30, 2022. This rate will be applied as follows:

- The new variable interest rate of 4.7 % will apply to new policy loans taken on or after May 30, 2022, on policies that do not have an existing loan.
- Existing loans, or loans added to policies with existing loans, will not receive the new variable interest rate of 4.7% until the policy anniversary that falls on or next after May 30, 2022.

## 6. Why did the dividend scale decrease for the former New York Life and Crown Life policies?

The decrease in the dividend scales for these policies is driven by the continued low interest rate environment. The investment strategy for the assets in these accounts is 100% fixed income. This strategy is consistent with the treatment outlined in the demutualization agreement.

The effect of changes in the dividend scales varies by policy. To understand the effect on illustrated values and premium offset for a specific client's policy, please get an updated illustration.

## 7. Do changes in the dividend scale affect illustrated values or premium offset dates?

Yes. With increases in the dividend scale, illustrated non-guaranteed values may be higher. Full premium offset may be available sooner. A policy may be able to remain on premium offset longer.

For former Crown Life and New York Life policies, decreases in the dividend scale mean illustrated values may be lower, and premium offset may be available later or for a shorter time. As in previous years, we'll send advisors early warning reports for premium offset for these policies.

The effect of changes in the dividend scale varies by policy. To understand the effect on illustrated values and premium offset for a particular policy, please get an updated illustration.

For more information on premium offset, see [How to talk to your clients about premium offset](#).

## 8. How does the dividend scale increase affect the enhanced coverage and ADO maximums available on new policies?

Enhanced coverage maximums will increase or remain unchanged. Additional deposit option (ADO) maximums will decrease or remain unchanged.

## 9. How does the dividend scale increase affect ADO payments for in-force policies?

For some in-force policies, we may not be able to accept all of a client's ADO payment, due to tax-exempt limits.

## 10. Have there been any changes to one-year term purchase rates for enhanced coverage dividend options?

There are no changes to one-year term rates for these dividend options.

## 11. Can we expect DSIRs to remain the same for all policies in the combined open account – including policies that formerly belonged to the Great-West, London Life and Canada Life open accounts?

Since amalgamation on Jan. 1, 2020, all policies in the combined open account and the Canada Life closed account share the same investment experience and pool of assets. However, there are factors that can cause the DSIRs to be different.

One of these factors is investment experience before amalgamation. This experience continues to be smoothed into the dividend scale for policies formerly belonging to our open accounts. Over the next several years, the influence of this experience will decrease.

There are also other investment-related factors reflected in the DSIRs that could cause future variations in DSIRs. For example:

- Dividend accumulation option – The usage level of the dividend accumulation option is different for policies that formerly belonged to each of the Great-West, London Life and Canada Life open accounts and the Canada Life closed account.
- Policy loans – Policy loan usage is different for policies belonging to the Canada Life combined open account and the Canada Life closed account.
- Variations that specifically apply to the Canada Life closed account, including:
  - Factors set at the time of demutualization.\*
  - The impact of smoothing investment gains and losses in the closed account is different than in the combined open account, which is a growing account.

To ensure policyowners are treated fairly and equitably, the specific experience attributed to these groups of policies will continue to be factored into their DSIRs.

\* Certain factors, such as the investment expenses charged to the closed account, were set at the time of demutualization and remain unchanged. Investment expenses applicable to the Canada Life open account have generally decreased over time as the account has grown. Another example is differences in taxation between the open and closed accounts.

## 12. Are we telling policyowners about the effects of the low interest rate environment on dividends?

Yes, this information has been in the dividend section of their annual policy statement for several years.

## 13. How does our long-term DSIR compare to our competition?

All companies have adjusted and will adjust their DSIRs at various times. Some of our competitors currently have a higher DSIR which may be due to factors such as asset mix and equity performance, as well as older, higher-yielding fixed income assets. Eventually, these fixed income assets will mature and, when they renew, will be subject to the interest rates at the time.

We manage our par accounts for strength and stability. Our DSIR is built on a foundation of rational and realistic assumptions, and it reflects the past and current investment experience of the par accounts. This approach helps manage the expectations of your new and long-standing clients.

It's necessary to consider the long-term performance and factors other than the DSIR when choosing the right participating life insurance (par) product for clients. The dividend is comprised of more than just investment experience. It includes mortality, expenses, lapse experience and more.

We have over 170 years of experience in the par market. No competitor can match that. We've paid dividends every year since 1848, even through some of the worst economic events. We've never left the par market, and our track record speaks for itself. Our long-term investment approach reflects our commitment to managing with prudence.

#### 14. How did the changes to the investment strategy in 2021 affect the dividend scale?

During the course of 2021 we transitioned our asset mix from 21.9% non-fixed income (NFI) at year-end 2020 to 30.1% NFI at year-end 2021. We gradually increased our exposure to Canadian and U.S. real estate, private equity and public equity. We reached our 30% NFI target asset mix by approximately the end of the third quarter, in line with our expectations while continuing to make progress on achieving our target asset mix for NFI **within** the 30% allocation.

Public equity markets were strong in 2021 in both Canada and the U.S. The S&P TSX Composite Total Return Index was up 25.1%. The S&P 500 Total Return Index was up 28.7%.

Real estate performance in Canada was also strong. The benchmark MSCI Canada Property Index generated a total return of 7.9% in 2021. This was the index's strongest in-year performance since 2015.

The increase in NFI weight, combined with strong performance in these asset classes in 2021, contributed favorably to par account investment performance and the dividend scale.

We continue to increase our exposure to the less liquid private equity and real estate asset classes. We remain on target to achieve our underlying target NFI allocations in the next 12 to 24 months.

As part of our investment strategy changes, we'll also continue to increase our foreign exposure. These changes will continue to increase diversification across and within asset classes, with the possibility of greater risk-adjusted returns over time.

For more details on the par account's performance in public equity and real estate, see:

- [Year in review 2021](#)
- [Investing with conviction](#)
- [Financial facts 2021](#)

#### 15. Why were the non-fixed income (NFI) and total account returns restated for 2020 in *Financial facts*?

As we strategically moved toward adding more foreign assets into our investment mix in 2020, we added new U.S. NFI assets to the par account. These were included in calculating the 2021 annual return.

For the purpose of calculating the annual return in 2020 for *Financial facts* documents, some of these assets were inadvertently excluded.

This resulted in both the NFI return and total par account return (including surplus and after investment expenses) being understated in the 2020 *Financial facts*.

This does not impact the calculation of the DSIR, as all income and returns from these assets were reflected appropriately in the 2021 DSIR. This also does not impact any par account return figures prior to 2020, as the U.S. NFI assets had not been added to the par account prior to 2020.

## General questions

### 16. How often is the dividend scale reviewed?

At least once a year, Canada Life reviews the participating policyowner dividend scale and the par accounts' insurance contract liabilities. This review determines whether they are at an appropriate level and whether the dividend scale needs to change.

### 17. Is the dividend scale interest rate (DSIR) the same thing as the dividend scale or internal rate of return (IRR)?

No. The DSIR is used to determine the dividend scale's investment component. Other factors (for example, insurance claims, terminations, expenses, taxes, and other factors) also play a role in calculating the dividend scale.

For more information on how the DSIR relates to the dividend scale, please review [The role of the dividend scale interest rate](#) (form 46-11088).

To understand more about a policy's internal rate of return (IRR), please review [Internal rate of return](#) (form 46-11111).

### 18. Why don't we post the dividend scale?

Dividends are distributed based on a policy's contribution to total par account earnings. They depend on a number of policy characteristics. A dividend scale is a set of rates that vary by product type, age at issue, gender, smoking status, and other factors. Because of this, dividends actually received at an individual policy level can vary.

### 19. Why do different companies' par accounts have different DSIRs?

DSIRs among companies may be different for three main reasons:

- Asset quality and mix – Given the same level of risk, it's expected long-term returns will be similar between accounts. A higher proportion of greater risk assets could produce higher returns but could also be more volatile. We manage our par accounts for stability and strength.
- Duration of fixed-income assets – Short-term variations may occur because of different fixed-income investment strategies. For example, a shorter duration strategy is more responsive to market movements.
- Historical versus forward-looking DSIRs – Our DSIR reflects past and current performance, not anticipated long-term future results that are optimistic or uncertain. Other carriers in the industry may take a different approach.



20. If the 10-year Government of Canada risk-free interest rates were to increase by 3% gradually over the next 10 years (from 1.4% at the end of 2021 to 4.4%), what effect would that have on open (and Canada Life closed) par account returns over the next 10 years?

If this occurred, we'd expect to see an increase in the par accounts' investment returns, and subsequently in the DSIRs, in the long-term. The impact on par accounts' investment returns, from the reinvestment of maturing assets at these gradually increasing rates would vary depending on the scenario. For example, let's assume the following:

- Risk-free interest rates increase by 3% gradually for the next 10 years from levels seen at the end of 2021 (from 1.4% to 4.4%).
- Our current outlook for credit spreads over the next 10 years doesn't change.
- We ignore the effect of smoothing of any past gains or losses from par account equity holdings and assume equities continue to earn current expected returns throughout that 10-year period.
- There are no future changes to the investment strategy/asset mix.

If this example plays out, we could potentially see long-term increases in **par account investment returns** of approximately 60-70 bps over the next 10 years as current fixed income investments mature and the proceeds are reinvested at gradually increasing rates. As noted above, several factors affect par account investment returns and the DSIR in evaluating the impact on the dividend scale.

**Caution: The example above is only one potential scenario for the evolution of the future par account investment returns and shouldn't be considered as a prediction of future performance as actual results will vary.**

**The par account investment return is not the same as the DSIR.** The DSIR includes the smoothed par account investment performance of assets backing the par account liabilities, where smoothing is the process by which past gains and losses are brought into the DSIR over time. In addition, the DSIR currently varies by pre-amalgamation open block as past investment experience accrued prior to amalgamation continues to be smoothed into the dividend scales for these in-force policies. Over time, as the influence of this previous experience diminishes, the DSIRs have moved closer together. It's important to note there are still other factors that continue to be reflected in the DSIR that could cause future DSIR variations across these blocks. Given these considerations, the actual impact of this scenario on the DSIR would be different than its impact on par account returns.

Par account investment returns are reflected in the DSIR as part of the investment component of policyowner dividends. It's also important to keep in mind that in addition to the DSIR, there are other factors that are not part of the DSIR – for example, insurance claims (mortality), terminations, expenses, taxes, and other factors – that also play a role in calculating policyowner dividends. In considering the potential impact on the dividend scale, the scenario outlined above assumes all other non-investment experience is unchanged from current levels.

21. If the 10-year Government of Canada risk-free interest rates remain at levels observed at the end of 2021, which was approximately 140 basis points (bps), what effect would that have on open (and Canada Life closed) par account returns over the next 10 years?

If this continued, we'd expect to see a decline in the par accounts' investment returns, and subsequently in the DSIRs, over time. The magnitude of a decline in par accounts' investment returns, given the reinvestment risk headwinds from persistent low interest rates, would vary depending on the scenario. For example, let's assume the following:

- Risk-free interest rates continue for the next 10 years at levels seen at the end of 2021 (approximately 140 bps).
- Our current outlook for credit spreads over the next 10 years don't change.
- We ignore the effect of smoothing of any past gains or losses from par account equity holdings and assume equities continue to earn current expected returns throughout that 10-year period.
- There are no future changes to the investment strategy/asset mix.

If this example plays out, we could potentially see gradual downward pressure in **par account investment returns** of approximately 20-30 bps over the next 10 years as current fixed income investments mature and the proceeds are reinvested at lower rates. As noted above, several factors affect par account investment returns and the DSIR in evaluating the impact on the dividend scale.

**Caution: The example above is only one potential scenario for the evolution of the future par account investment returns and shouldn't be considered as a prediction of future performance as actual results will vary.**

**The par account investment return isn't the same as the DSIR.** The DSIR includes the smoothed par account investment performance of assets backing the par account liabilities, where smoothing is the process by which past gains and losses are brought into the DSIR over time. In addition, the DSIR currently varies by pre-amalgamation open block as past investment experience accrued prior to amalgamation continues to be smoothed into the dividend scales for these in-force policies. Over time, as the influence of this previous experience diminishes, the DSIRs have moved closer together. It's important to note there are still other factors that continue to be reflected in the DSIR that could cause future DSIR variations across these blocks. (See answer to question AAA.) Given these considerations, the actual downward pressure on the DSIR would be different than the downward pressure on par account returns.

Par account investment returns are reflected in the DSIR as part of the investment component of policyowner dividends. It's also important to keep in mind that in addition to the DSIR, there are other factors that are not part of the DSIR – for example, insurance claims (mortality), terminations, expenses, taxes, and other factors – that also play a role in calculating policyowner dividends. In considering the potential impact on the dividend scale, the scenario outlined above assumes all other non-investment experience is unchanged from current levels.

## 22. What implications could there be for policyowner dividends if interest rates remain low for a prolonged period?

Even if rising, interest rates still remain historically low. Dividends can be paid when earnings exceed what was assumed when a product was priced. If investment experience is less than the assumption used when a product was priced, the investment component of the dividend could be less than zero. The downward pressure on investment experience could be offset by positive experience from other factors, such as insurance claims, policy terminations, expenses and taxes.

If interest rates remain low, there could be pressure on the dividend scale. This could mean more policyowners receive zero dividends in future years, especially for older policies that were priced using higher interest rate assumptions. However, if interest rates increase in the future, this would have a favourable impact on the dividend scale and could result in dividends increasing for these policyowners.

Regardless of how interest rates change or how the market performs, participating life insurance offers numerous guarantees – from death benefits to guaranteed cash values – that aren't affected by adjustments to dividend scales. In addition, policyowner dividends credited to a policy are fully vested. They cannot be reduced or used for any purpose other than as authorized by the policyowner, to pay premiums, to preserve the policy's tax-exempt status or as specified under the contract.

## 23. What other implications could there be for participating policyowner dividends if interest rates increase for a period?

There remains uncertainty in terms of the direction of interest rates. So far in 2022 interest rates have continued to rise.

For the Canada Life combined open account and Canada Life closed account, each year, about 10% of the total fixed income portfolio are invested at then-current market rates. We also invest a portion of new premiums and investment income at then-current market rates each year.

The asset returns available in the marketplace in January and February 2022 for new par account investments in bonds and mortgages were about 3.29%. This is approximately four basis points above the average return for similar par account assets maturing throughout 2022.

If rates continue their increasing trend in 2022, this could positively influence our dividend scales. This may not be the case for some other companies, whose longer duration fixed-income portfolios imply a smaller amount of assets will be reinvested each year. In addition, companies with longer-duration fixed income portfolios may still have higher interest-yielding assets in their accounts, which will mature and need to be re-invested at lower rates, despite the recent increase in interest rates.