

HSBC Life (UK) Limited Statement of Principles and Practices for Unit-Linked Business

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2. Glossary of terms

Annual Management Charge

A regular charge that is reflected in the price of the units. This covers the costs of managing the assets and administering the fund.

Bid/Offer Spread

The difference in price between the offer and bid prices of units in a fund each day, usually fixed at 5%.

Bid Price

Where funds quote a separate offer and bid price, the bid price is the price at which units can be surrendered.

Business Day

Is any day other than a Saturday or a Sunday or Public Holiday in England or Wales.

Internal Unit-Linked Fund

An identifiable and segregated pool of assets forming part of the long term business funds of HSBC Life (UK) Limited ("HSBC Life")

Offer Price

Where funds quote a separate offer and bid price, the offer price is the price at which units can be acquired.

Open Ended Investment Companies (OEIC)

Collective investment vehicles, which allow investors to pool their money in a single fund, spread the risk and access professional fund management with lower costs than direct investment. OEICs are structured as companies that issue shares, which can be bought or sold by investors. The value of the shares is directly related to the underlying assets held by each OEIC, and changes with the relative performance of these assets.

SICAVs

Similar to OEICs but operating from offshore territories, for example, Luxembourg.

Unit Trusts

Collective funds which operate similarly to OEICs, but are structured as trusts which issue units of equal value, rather than companies.

3. The purpose

- 3.1.** This statement sets out the principles and the practices that HSBC Life (UK) Limited ("HSBC Life") applies in the operation of its internal unit-linked funds.
- 3.2.** In this statement "we" or "us" refers to HSBC Life.
- 3.3.** The aim is to give the reader an understanding of the principles applied by HSBC Life in managing its internal unit-linked funds together with the practices applied to day-to-day management of these funds. In applying the principles, HSBC Life aims to ensure that its duties to unit-linked policyholders are met, and that the business can adapt to changes in the business and economic environment in both the short and medium term. To assist in achieving this, HSBC Life is able to exercise discretion over certain aspects of its internal unit-linked fund operation, for example with regard to the basis used to determine prices and the allowance for taxation in the pricing of the funds.
- 3.4.** The practices describe in detail the day-to-day operations carried out in managing the funds. Specific issues that are covered and addressed include:
- How HSBC Life exercises its power of discretion.
 - How the competing and conflicting interests of different groups of policyholders and shareholders are managed so that policyholders and shareholders are treated fairly.
 - How the mechanics of investing in a unit-linked fund operate.
- 3.5.** This statement also sets out the range of internal funds available on our unit-linked policies. Appendix A lists each of these funds.
- 3.6.** To obtain a full understanding of the operation of our unit-linked principles and practices, this statement must be read in full. However this statement is not a comprehensive explanation either of the management of HSBC Life's unit-linked business or of every matter which may affect that business.
- 3.7.** This statement can be amended, without notice, to reflect changes in our practices from time to time due to, for example,
- new product or fund launches
 - changes in corporate structure
 - changes in business environment
 - changes to the management of our unit-linked funds.

No part of this statement should be relied upon when making decisions relating to investments in our unit-linked funds.

- 3.8.** No part of this statement forms part of, or varies, the terms and conditions of any policy issued by HSBC Life. In the event of any inconsistency between this statement and any policy, the terms and conditions of the policy will prevail.
- 3.9.** Marks and Spencer Life Assurance Limited (MSLA) business was incorporated within HSBC Life from 1 October 2011 as part of a formal process of the transfer of business between two insurance companies, known as a Part VII transfer. From this date, MSLA Funds came within the HSBC Life (UK) Limited Statement of Principles and Practices for Unit-Linked Business. For the purposes of this document they will be referred to as MSLA funds.
- 3.10.** A copy of this statement and additional information in respect of the funds can be obtained by telephoning our Life Helpline on 0345 745 6125* (Lines are open 8am to 6pm Monday to Friday (excluding public holidays). To help us continually improve our service and in the interest of security, we may monitor and/or record your communications with us.
- 3.11.** Alternatively the statement can be viewed by visiting our website at hsbc.co.uk.

4. Corporate structure

4.1. HSBC Life (UK) Limited

- 4.1.1. HSBC Life is wholly owned by HSBC Bank plc ("HSBC Bank"). It manufactures life and health insurance, and life investment products sold to UK customers via HSBC Bank's distribution network and other distributors.

4.2. HSBC Global Asset Management (UK) Limited

- 4.2.1. HSBC Global Asset Management (UK) Limited provide the investment management services for the majority of the internal unit-linked funds. HSBC Global Asset Management (UK) Limited's services are provided under an investment management agreement between HSBC Global Asset Management (UK) Limited and HSBC Life.

4.3. HSBC Bank plc – Securities Services division ("HSS")

- 4.3.1. The Institutional Fund Services division of HSS act as pricing agents for HSBC Life, and have responsibility for the daily valuation and calculation of unit prices for the majority of

the unit-linked funds. HSS provides a range of custody services in respect of each unit-linked fund's underlying assets.

4.4. External Fund Managers

4.4.1. Marks and Spencer Unit Trust Management Limited ("MSUTM")

MSUTM is a registered limited company that undertakes the investment management and daily administration of the Unit Trust Funds in which MSLA (now part of HSBC Life) invests. MSUTM is a wholly owned subsidiary of Marks and Spencer Retail Financial Services Holdings Limited.

5. Governance structure

5.1. HSBC Life Committees

- 5.1.1. The Board of directors ("the Board") has overall responsibility for the management of HSBC Life's unit-linked business.
- 5.1.2. The Insurance Executive Committee ("IEC") – This is a formal committee of the Board with responsibility to act as the management committee on matters of business management and development, risk management and operational control, including the operational aspects of the unit-linked funds.
- 5.1.3. Life Investment Forum ("LIF") – This is the primary forum (risk committee) for monitoring all high level aspects of investment operations, including fund performance, appointment of fund managers, fund selection and high level fund governance. This is the committee that would review changes to high level principles relating to the unit-linked funds.
- 5.1.4. Fund Pricing Forum ("FPF") – The LIF has ultimate responsibility for the operation of the unit-linked funds, and has delegated this responsibility to the FPF. This committee has responsibility for monitoring the operational aspects of the unit-linked funds, including:
- Monitoring compliance with the Association of British Insurers' general guidance to its members on the operation of their unit-linked funds.
 - Reviewing areas of discretion.
 - Monitoring performance of outsourced activities; and
 - Consideration of any proposed changes to unit-linked fund structures.

5.2. Conflicts of Interest

- 5.2.1. 'HSBC Group' means HSBC Holdings plc and its subsidiaries, associated and affiliated companies. The HSBC Group is a global organisation, which provides a wide range of financial services. As such, it, or a company

with whom it has an association ('HSBC'), may from time to time have interests which conflict with its clients' interests or with the duties that it owes to its clients.

These include conflicts arising between the interests of HSBC, its associates and employees on the one hand and the interests of its clients on the other and also conflicts between clients themselves.

5.2.2. HSBC has established procedures, which are designed to identify and manage such conflicts. These include organisational and administrative arrangements to safeguard the interests of clients.

A key element of this policy is that persons engaged in different business activities involving a conflict of interest must carry on those activities independently of one another.

5.2.3. Where necessary, HSBC maintains arrangements which restrict the flow of information to certain employees in order to protect its clients' interests and to prevent improper access to client information.

5.2.4. HSBC may also deal as Principal for its own investment account and may be matching transactions with another client. Procedures are in place in order to protect the client's interest in this instance.

5.2.5. In some cases, HSBC's procedures and controls may not be sufficient to ensure that a potential conflict of interest does not damage a client's interests. In these circumstances, HSBC may consider it appropriate to disclose the potential conflict to the client and obtain the client's formal consent to proceed. However, HSBC may decline to act in any circumstance where there is residual risk of damage to the interests of any client.

5.3. Internal Audit

5.3.1. The operation and pricing of the unit-linked funds fall within the remit of HSBC's Group Financial Services Audit function and are subject to periodic internal audit inspections. The findings of such audits are reported to the LIF, the risk committee and to the IEC and the Board by exception.

5.4. Compliance

5.4.1. HSBC Life's compliance department carry out periodic monitoring reviews which include the operational aspects of the unit-linked funds.

5.5. Other Service Providers

5.5.1. HSBC Life conduct their own internal compliance monitoring visits at least once a year to the fund pricing function and receive periodic management information from both HSS and HSBC Global Asset Management (UK) Limited in order to track performance against agreed service standards.

6. Calculating unit prices

6.1. Introduction

6.1.1. This section describes the way that we value the assets within our unit-linked funds and calculate the unit prices from the asset value.

6.2. Principles

6.2.1. We operate our valuation and pricing policy according to the following principles:

- Assets within each unit-linked fund are valued on a fair basis.
- Charges and expenses are borne by each unit-linked fund in an appropriate manner.
- Pricing methods are fair to policyholders.
- Unit prices are calculated on a fair basis.
- Pricing methods and policy are operated and disclosed in an open and transparent manner.
- Cross subsidy between individual unit-linked funds is avoided.

6.2.2. These principles may be subject to change in future as necessary, to ensure customers continue to be treated fairly, subject to the approval of the IEC.

6.3. Practices

6.3.1. We use one of the following two bases to calculate the price for each of our unit-linked funds.

6.3.1.1. Single priced funds – where the fund quotes one price each day for both allocating and surrendering units.

6.3.1.2. Dual priced funds – where separate prices are used each day for the allocation and surrender of units, known as "Offer" and "Bid" prices. The difference between the two prices is termed the "Bid/Offer spread".

6.3.2. The policy document and associated product literature set out which basis is used for the pricing of the units in each unit-linked policy issued by HSBC Life.

6.4. Single Priced Funds

6.4.1. Asset Valuations

6.4.1.1. Under normal circumstances, our unit-linked funds are valued every business day using market prices supplied by third party data providers. The normal valuation point for each fund is detailed in Appendix A. There may

be exceptional circumstances when our unit-linked funds cannot be valued every business day. This may be caused by non-receipt of market prices due to specific system/operational issues or widespread market disruption. Valuations will not be carried out under any circumstances at intervals greater than one month.

- 6.4.1.2. The value of the fund is derived from the value of the underlying assets in which the fund is invested.
- 6.4.1.3. Where a fund invests in a collective investment scheme, the unit price used in the fund valuation is derived from the latest unit price available from the managed fund or the latest share price available from the collective investment scheme. If a single price is quoted for buying and selling units or shares, the most recently quoted single price is used. If separate buying and selling prices are quoted, the mid of the two prices is used, provided that the buying prices have been reduced by applying any initial charge, and the selling prices have been increased by applying any exit charge.
- 6.4.1.4. For investments quoted on a recognised investment exchange (for example, the London Stock Exchange), the value used will be the average of the buying and selling prices most recently quoted. There are no unquoted investments or direct property investments in our unit linked funds.
- 6.4.1.5. Any cash holdings in current and deposit accounts and in other time-related deposits will be valued at their nominal values.
- 6.4.1.6. Each unit-linked fund's value will also include the value of any debtor balances, for example, income receivable, and any liabilities relating to the fund including those in respect of the annual management charge (AMC), other expenses and taxation.
- 6.4.2. **Fund Pricing**
- 6.4.2.1. For unit-linked funds that are single priced, the unit price is initially calculated using the mid-market prices of the underlying assets held by the fund, as described above. This price is then adjusted to reflect the cost of purchasing assets if there is a net inflow of money or the cost of selling assets if there is a net outflow of money. These allowances for dealing costs are based on recent experience of dealing costs and are subject to regular review. This pricing method is known as "swinging single pricing".
- 6.4.3. **Rounding of Prices**
- 6.4.3.1. The single price is calculated and then rounded to the nearest 0.1p or 0.01p depending on the policy terms.

6.5. Dual Priced Funds

6.5.1. Asset Valuations

- 6.5.1.1. Under normal circumstances, our unit-linked funds are valued every business day using market prices supplied by third party data providers. The normal valuation point for each fund is detailed in Appendix A. There may be exceptional circumstances when our unit-linked funds cannot be valued every business day. This may be caused by non-receipt of market prices due to specific system/operational issues or widespread market disruption. Valuations will not be carried out under any circumstances at intervals greater than one month.
- 6.5.1.2. For dual priced funds, two fund values are calculated, one on an "Offer" basis, reflecting the prices at which assets can be purchased plus an allowance for buying costs, and one on a "Bid" basis, reflecting the price at which assets can be sold less an allowance for selling costs. These two values are derived from the value of the underlying assets in which the fund is invested.
- 6.5.1.3. Where a dual priced unit-linked fund invests in a life insurance managed fund or a collective investment scheme, the unit price in the managed fund or the share price in the collective investment scheme which are used in the valuation of the unit-linked fund are derived from the most recently quoted buying and selling prices, provided that the buying prices have been reduced by any initial charge, and the selling prices have been increased by applying any exit charge.
- 6.5.1.4. For investments quoted on a registered investment exchange, the prices used will be the most recently quoted buying and selling prices at the fund valuation point.
- 6.5.1.5. Holdings in derivatives contracts are valued at the price at which we calculate that the counterparty would close out the contract.
- 6.5.1.6. Any cash holdings in current and deposit accounts and in other time-related deposits will be valued at their nominal values.
- 6.5.1.7. The fund values will also include the value of any debtor balances, for example income receivable, and any liabilities relating to the fund including those in respect of annual management charges (AMC), other expenses and taxation.
- 6.5.2. **Fund Pricing**
- 6.5.2.1. For dual priced unit-linked funds, either a creation or a cancellation price is calculated for each fund each valuation day.
- 6.5.2.2. The creation price is derived from the "Offer" basis fund valuation, reflecting the prices at which assets can be purchased plus dealing costs and levies, any cash balance in the fund and any amounts accrued due

to the fund from its debtors (eg, income payments) and less any amounts accrued due from the fund to its creditors. The cancellation price is derived from the "Bid" basis fund valuation, reflecting the prices at which assets in the fund can be sold plus cash balances, as well as any amounts accrued due to the fund from its debtors, and less any amounts accrued due from the fund to its creditors.

6.5.2.3. We will normally value a fund using the creation price if we believe the fund is expanding over the medium term, and using the cancellation price if we believe the fund is contracting over the medium term. A fund will be expanding if more money is entering the fund in new or additional investments than is leaving it in withdrawals, surrenders or redemptions, and vice versa for a contracting fund. A decision to change the pricing basis is generally taken only after a period of expansion or contraction against the current basis.

6.5.2.4. If the fund is expanding, it will normally be priced on an "Offer basis". The Offer Price will be set equal to the creation price. The Bid Price is then calculated by applying the Bid/Offer spread, to the Offer Price. Where the Bid/Offer spread is 5%, the Bid Price = Offer Price x 95/100.

6.5.2.5. If the fund is contracting, it will normally be priced on a "Bid basis". The Bid Price will be set equal to the cancellation price. The Offer Price is then calculated by applying the Bid/Offer spread to the Bid Price. Where the Bid/Offer spread is 5%, the Offer Price = Bid Price x 100/95.

6.5.3. **Rounding of Prices**

6.5.3.1. Creation and cancellation prices are normally calculated each Business Day, in Sterling, and are quoted in pence. The prices are rounded to the nearest 0.1p or 0.01p depending on the policy document and other terms and conditions.

6.5.4. **Charges and Expenses**

6.5.4.1. Annual Management Charge (AMC)

6.5.4.1.1. Where appropriate, the unit price for each unit-linked fund includes an allowance to take account of the AMC. The AMC is normally taken daily by multiplying the net asset value of the fund by the annual charge divided by 365 (366 in a Leap year). The unit price is quoted after allowing for the AMC.

6.5.4.2. **Additional Expenses**

6.5.4.2.1. A number of unit-linked funds charge additional expenses over and above the annual management charge. These cover expenses in connection with valuation, maintenance, management of and dealing in the assets of the fund, together with any other expenses which have been or shall be incurred in the running of the fund.

6.5.4.2.2. In the case of these unit-linked funds, these expenses result in an additional annual charge of 0.024% for each fund.

6.5.4.3. **Initial Charges**

6.5.4.3.1. For unit-linked funds that are dual priced, there is an initial charge, which is the Bid/Offer spread, described in more detail in Section 6.5.2. The spread is a maximum of 5% of the Offer Price plus a rounding adjustment of no more than 0.1p.

6.5.4.3.2. There is no initial charge for single priced funds.

6.5.4.4. **Underlying Funds**

6.5.4.4.1. Many of our unit-linked funds invest in other underlying funds, such as unit trusts, OEICs, SICAVs, investment trusts and exchange traded funds. These underlying funds may incur expenses as part of their operation, and these expenses will be allowed for when we price our unit-linked funds.

6.5.4.4.2. These expenses include:

- Registrar fees
- Custody transaction charges
- Handling charges
- Trustee fees
- Bank charges
- Interest charges
- Audit fees
- Stamp duty reserve tax
- Broker commission
- Administration charges

The approval of FPF is required for any expenses to be charged to our unit linked funds

6.5.4.4.3. The impact of these expenses on our unit-linked fund prices will vary depending on the fund and which underlying fund it invests in.

6.5.4.4.4. Where our unit-linked funds invest in underlying funds, our pricing mechanisms ensure that there is no double charging of the AMC.

6.5.4.5. **Dilution Levies**

6.5.4.5.1. Where unit-linked funds invest in underlying OEICs, the manager of the underlying OEIC will reserve the right to impose a dilution levy. This is a charge placed against any trade that could impact the value of the assets in the underlying OEIC to the detriment of the remaining investors in the underlying OEIC, because it would either reduce the amount of assets which could be purchased or reduce the sale proceeds for assets sold.

6.5.4.5.2. If the manager of an underlying OEIC charges a dilution levy on any trades made by HSBC Life funds, the cost of this levy will be borne by the fund.

6.5.5. **Creation and cancellation of Units**

- 6.5.5.1. For unit-linked funds that are dual priced, if the number of units in a fund is increasing, the additional units will be created at the creation price. Conversely units will be cancelled at the cancellation price if the number of units in the fund is reducing. Policyholder transactions are unaffected by a delay in creating/cancelling units.
- 6.5.5.2. For unit-linked funds that are single priced, units are created or cancelled at the single price quoted for that day.
- 6.5.5.3. Any profit generated or loss incurred as a result of delays in creating or cancelling units due to administrative issues or backdated transactions, will be borne by HSBC Life and not by the relevant unit-linked fund(s).

6.5.6. **Policyholder Unit Allocation**

- 6.5.6.1. When a policyholder transacts in a dual priced unit-linked fund, we create units at the Offer Price and cancel units at the Bid Price. For unit-linked funds that are single priced, units are created or cancelled at the quoted single price.
- 6.5.6.2. Whereas the pricing basis of the fund is determined periodically, (see section 6.5.2) there may be individual days where the fund's net cashflow is of opposite sign. For example, a fund is priced on an expanding basis but on a given day the cash flow is negative so that more units are cancelled than created. HSBC Life will bear any net cost of these transactions, but may hold a box (see section 8) to minimise the cost of this.

6.6. **Forward and Historic Pricing**

- 6.6.1. Unit-linked funds may be operated on a forward pricing basis or on an historic pricing basis. Forward pricing is where the price calculated for each day's transactions is based on the valuation once all transactions are known. This means that policyholders receive the most up to date value for their investment when transactions are made, but there is a short delay before the price is confirmed. Historic pricing is where the price calculated for each day's transactions is based on the valuation as at the previous business day. Processes are in place to prevent transacting policyholders from dealing by selecting prices to the detriment of the remaining policyholders. Appendices A and B specify the pricing basis in operation for each of the HSBC Life's internal unit-linked funds.

6.7. **Internal Deals between Unit-linked Funds**

- 6.7.1. Some of our unit-linked funds hold units in other funds in the same range. This allows the fund to gain exposure to a certain type of investment without the extra costs involved in directly investing in the relevant assets.

- 6.7.2. For unit-linked funds that are single priced, internal deals take place at the single price. For unit-linked funds that are dual priced, internal deals take place at the creation price for purchases and at the cancellation price for sales.

- 6.7.3. Where one of our unit-linked funds invests in one of our other unit-linked funds, pricing mechanisms are established to ensure that there is no double charging of the AMC.

6.8. **Valuation Point, Pricing Point and Publication of Prices.**

- 6.8.1. All our unit-linked funds are normally valued and priced each business day.
- 6.8.2. For all daily priced funds, the price is usually based on a valuation at 2pm each business day. This may vary in certain circumstances such as early closure of markets, during public holidays, or if funds are being restructured.
- 6.8.3. In respect of unit-linked funds (excluding MSLA funds) that are priced on a forward pricing basis, all instructions to allocate or surrender units must be received by 9.30am to be processed using the price quoted that business day. For MSLA all instructions to allocate or surrender units must be received by 2pm to be processed using the price quoted that business day.
- 6.8.4. For unit-linked funds priced on an historic pricing basis, policy terms and conditions may state that instructions will be held over until the business day after receipt before being processed in order to prevent policyholders being able to select against the fund by transacting based upon known information.
- 6.8.5. Individual policy valuations are available on request to policyholders by contacting the helpline number stated in Section 3.10.

7. **Discretionary powers**

7.1. **Introduction**

- 7.1.1. This section sets out the extent of and the limits to HSBC Life's discretionary powers in relation to the operation of the unit-linked funds. The FPF is responsible for the monitoring of the operational aspects of the unit-linked funds, which include the application of these discretionary powers and monitors them accordingly.

7.2. **Principles**

- 7.2.1. HSBC Life's primary objective in the use of our discretion is to ensure that all policyholders are treated fairly. We look to operate the funds according to published criteria and standards, including the scope of our discretion.

7.2.2. The scope of our discretion is reviewed on a regular basis, with a full review carried out if any significant changes to the funds or the investor base occur. Changes will be made if deemed necessary to ensure policyholders continue to be treated fairly.

7.3. Practices

7.3.1. Launching Funds and Seeding with Capital

7.3.1.1. We reserve the right to add additional unit-linked funds to our range to reflect changing policyholder requirements.

7.3.1.2. We may seed new unit-linked funds with a nominal amount of capital to launch each fund prior to receiving investments from policyholders, and/or with sufficient capital to allow the fund to hold a sufficient range of investments to operate in accordance with its investment strategy.

7.3.1.3. Once the unit-linked fund has received sufficient investments to enable it to operate effectively, the seed capital will be removed.

7.3.2. Taxation

7.3.2.1. Details of our tax policy are set out in Section 9.

7.3.3. Charges and Expenses

7.3.3.1. Policy documents outline any discretion we may have in setting the levels of charges and expenses that can be applied to the fund. Policy documents also set out our power to alter the level of charges applying.

7.3.3.2. We will give at least 30 days prior notice to policyholders if we decide to change the annual management charge on any of our unit-linked funds.

7.3.4. Rounding

7.3.4.1. Policy documents set out the basis on which unit prices are rounded, and the basis on which we can alter their rounding terms if we wish to.

7.3.4.2. The aim of the rounding policy is to be neutral to both the policyholder and HSBC Life.

7.3.5. Criteria for moving funds between bid and offer bases

7.3.5.1. Where a unit-linked fund quotes a Bid Price and an Offer Price, we have the discretion to move the basis of these two prices from an "Offer Basis" to a "Bid Basis". How this discretion is exercised is summarized in Section 6.5.2 depending on whether we consider the fund to be expanding or contracting over the medium term. Any change in basis is subject to the approval of FPF.

7.3.6. Closing or Merging Funds

7.3.6.1. We may at any time decide to close a fund, subdivide a fund or to merge together funds that have similar objectives.

7.3.6.2. We will normally give policyholders at least 60 days prior notice of any such change, although the specific minimum notice period is stated in the policy document. We will offer affected policyholders the opportunity to switch to alternative funds.

7.3.6.3. In the event that no switch instruction is received on closure of a fund, the customer's fund will default to being switched into the fund which we deem as appropriate. We will advise customers of the default fund as part of the prior notice communication.

7.3.7. Ability to defer transactions

7.3.7.1. Policy documents give us the power to defer transactions in unit-linked funds in certain circumstances, for instance:

- Deferral of allocation of payments to units in a particular fund; and
- Deferral of cancellation of units.

This may apply, for example, if stock markets are not open for business and we cannot buy or sell quoted stocks. The conditions relating to such deferrals, including the maximum deferral periods and requirement to provide notice, are set out in the policy document.

7.3.7.2. We will only exercise this discretion in exceptional circumstances, where there could be a detrimental effect on existing policyholders if the transaction was allowed to take place at that time.

7.3.7.3. Transactions will only be deferred for as long as necessary to protect the interests of other policyholders by ensuring that assets can be bought or sold, subject to any maximum periods set out in the policy document.

7.3.8. Change of Pricing Point

7.3.8.1. We may decide in future to alter the daily pricing point of some or all of our unit-linked funds. This may occur, for example, if systems are altered, or if changes need to be made to accommodate investments in external funds.

7.3.8.2. Any such changes to the pricing point, and if appropriate, the dealing time for transactions, will be communicated to policyholders with reasonable prior notice where possible.

- 7.3.9. **Complaints**
- 7.3.9.1. Any complaints relating to the operation of unit-linked funds will be dealt with in accordance with our internal complaint resolution procedures.
- 7.3.9.2. The principles and practices relating to the correction of errors in pricing our unit-linked funds are set out in Section 10.
- 7.3.10. **Valuing Assets**
- 7.3.10.1. Where a fair market value for assets is not available (for example, shares which have been suspended from trading) we may decide, as an alternative to deferring transactions, to obtain independent professional valuations where possible.
- 7.3.10.2. Where stated in the policy document, if an independent professional valuation is not available, we will use our best estimate of the value of the asset.
- 7.3.11. Determining appropriate distribution rates for income**
- 7.3.11.1. Some unit-linked funds distribute income to policyholders on a regular basis. The amount distributed is based on the income earned during the period, but is also impacted by other factors (such as previous distributions, expected income and cash available). Policyholders may in certain cases have the option of having the distributions reinvested, in which case the income is reinvested in units.
- 7.3.12. Stock Lending**
- 7.3.12.1. Stock lending by the internal unit-linked funds is not permitted.

8. Box Management

- 8.1. Introduction**
- 8.1.1. This section describes how we use a “box” in the management of our unit-linked funds. This, however, does not relate to the MSLA funds as a box management process is not employed.
- 8.1.2. A box exists where we hold additional units in our unit-linked funds in excess of those allocated to policyholders.
- 8.2. Principles**
- 8.2.1. We may hold a box to reduce the expense to the fund of making a series of small transactions.
- 8.2.2. We do not seek to make a profit in the running of any box.
- 8.3. Practices**
- 8.3.1. Where possible we will deal in a box rather than directly with the underlying assets to reduce the dealing expenses to the relevant unit-linked fund.

- 8.3.2. The limits for each box for each unit-linked fund are reviewed periodically, based on the size of the relevant fund and the level of dealing activity.
- 8.3.3. We do not allow boxes to become negative.

9. Taxation

9.1. Introduction

- 9.1.1. This section describes the way in which tax is allowed for when we price our unit-linked funds.

9.2. Principles

- 9.2.1. We deal with the tax liabilities of each fund on a discrete basis, and look to avoid cross subsidies between funds. This ensures that the policyholders in each fund are treated fairly, and one group of policyholders is not subsidising another in respect of tax due.
- 9.2.2. We aim to ensure that each fund pays the actual tax charge incurred. We will estimate the tax charge if it is not possible to calculate the exact tax liability.
- 9.2.3. We will not give any immediate tax credit to policyholders for unused realised losses in the fund. This reduces the complications of allowing for tax in pricing and hence the risk of pricing errors. To the extent that such losses have a value determined on reasonable actuarial assumptions, then they will be carried forward and offset against future realised gains in the fund.
- 9.2.4. We will change the scope and the policy of taxation of our unit-linked funds if required to do so to remain compliant with tax legislation.

9.3. Practices

- 9.3.1. Investment Income Taxation
- 9.3.1.1. Investment income comprises:
- Dividends from shares
 - Coupons from debt securities
 - Rebates of management charges from underlying unit trusts and OEICs
 - Distributions from underlying unit trusts and OEICs
 - Profits and losses on debt securities; and
 - Profits and losses on unit trusts and OEICs that hold over 60% of their assets in debt securities. Unit trusts and OEICs that hold more than 60% of their assets in debt securities are currently taxed under the loan relationship scheme regime and are taxed as income on a marked to market basis, rather than under the deemed disposal regime (see 9.3.2.9).
- 9.3.1.2. Tax is charged on investment income at the policyholder rate of tax (currently 20%). Dividends from UK and qualifying overseas equities and the income element of UK and qualifying overseas dividends from unit trusts and OEICs are not currently subject to tax.

9.3.2. **Capital Gains Taxation**

- 9.3.2.1. When assets are sold, they give rise to either a capital gain or capital loss depending on whether each asset was sold for more or less than it was bought for. Capital gains will be subject to indexation relief where available.
- 9.3.2.2. Capital losses can be used to offset realised capital gains within a fund. Excess capital losses can be carried forward to be offset against capital gains generated in future tax years, including capital gains on deemed sales from previous years that will be brought into tax in future years.
- 9.3.2.3. No immediate cash credit is given for carried forward realised tax losses in the fund.
- 9.3.2.4. Notwithstanding that an amount of tax credit may have already been given, an actuarial reserve is held to recognise that credit may be due to the fund for the tax losses in future periods.
- 9.3.2.5. Net realised capital gains are charged to tax in the current year at the policyholder tax rate.
- 9.3.2.6. Tax is accrued on net unrealised capital gains on equities – a discounted tax rate is applied to allow for the elapsed time before the capital gains are expected to be realised.
- 9.3.2.7. When capital gains are realised we will increase our tax provision as the tax rate on realised capital gains is greater than the discounted rate used to calculate the provision for unrealised capital gains.
- 9.3.2.8. Where a fund invests in an underlying unit trust or OEIC, capital gains and capital losses on the underlying fund are taxed under the deemed disposal rules.
- 9.3.2.9. Under this process, at the end of each year, the OEIC depositary or the Unit Trust manager is deemed to have disposed of and immediately repurchased the holdings at market price as at 31 December each year, generating a capital gain or capital loss after indexation allowance. The resulting capital gain or capital loss is divided by 7 with the balance brought into tax in the current tax year and in the subsequent six tax years.

- 9.3.2.10. A tax provision is set up on the balance sheet for each fund. Amounts are deducted from this provision each time there are realised capital gains, deemed disposal gains and unrealised capital gains on OEICs/ unit trusts during the tax year.
- 9.3.2.11. Where unit-linked funds invest in other unit-linked funds, tax is charged at the lowest level of the underlying fund, and there is no offsetting of the tax positions between the lower level underlying funds.
- 9.3.2.12. Realised gains are deducted from the fund annually where the fund has overall net gains.

10. Pricing error correction

10.1. Introduction

- 10.1.1. This section sets out how we deal with pricing errors arising on our internal unit-linked funds.

10.2. Principles

- 10.2.1. We will rectify all errors as soon as is reasonably practicable after they have been identified. Compensation will be paid to policyholders if we consider that they have suffered a material loss as a direct result of the pricing error.

10.3. Practices

- 10.3.1. We operate processes to monitor our funds for pricing errors daily.
- 10.3.2. Where the error is between 0.1% and 0.5%, it is investigated for wider implications.
- 10.3.3. Compensation will be paid to a policyholder if the error is 0.5% or above and results in a loss greater than £10. For live policyholders compensation will be paid by crediting additional units in the fund that was in error.
- 10.3.4. If we discover a widespread systemic error in our pricing, and this is likely to have resulted in losses above £50 for individual retail investors, then we will consider compensation, regardless of the percentage of the error.

Appendix A

Unit-Linked Funds Operated By HSBC Life (UK) Limited

Life Funds

(Priced On An Historic Basis)

Fund	Launch Date	Annual Management Charge	Fund Valuation Point
Adventurous Fund	April 1988	1.00%	2pm
Balanced Fund	April 1988	1.00%	2pm
Defensive Fund	April 1988	1.00%	2pm
Distribution Fund	July 2000	1.00%	2pm
Fixed Interest Fund	April 1988	1.00%	2pm
International Fund	April 1988	1.00%	2pm
Money Market Fund	April 1988	1.00%	2pm
Mortgage Fund	September 1998	1.00%	2pm
Secure Fund	April 1988	1.00%	2pm
UK Equity Fund	April 1988	1.00%	2pm

(Priced on a forward basis)

Previously available through Marks and Spencer Life Assurance Limited

Fund	Launch Date	Annual Management Charge	Fund Valuation Point
UK Balanced Equity LIFE	October 05 1995	0.70%	10am

This Fund invests wholly in the Marks and Spencer UK 100 Companies Unit Trust Fund.

Trustee Investment Plan Funds

Fund	Launch Date	Annual Management Charge	Fund Valuation Point
World Selection Adventurous Fund	December 2014	0.25% *	2pm
World Selection Balanced Fund	December 2014	0.25% *	2pm
World Selection Cautious Fund	December 2014	0.25% *	2pm
World Selection Conservative Fund	December 2014	0.25% *	2pm
World Selection Dynamic Fund	December 2014	0.25% *	2pm

* Additional fund expenses and AMC in underlying funds also apply

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Designed and produced by HSBC Global Publishing Services_6868_161019