GUARDIAN®

To:	All Field Associates
From:	Jess Geller, FSA, Vice President & Actuary
Subject:	How Guardian Calculates Individual Life Dividends
Date:	November 20, 2014

Background
Guardian was founded in 1860 and became a fully mutual company in 1925. As a mutual life insurance company, Guardian has no outside stockholders and is chartered to operate in the best interests of its participating policyowners. Owners of participating life insurance policies share in Guardian's actual financial results through annual dividends.

During 2015, Guardian will distribute approximately $784 million in dividends to participating individual life insurance policyowners.

This memorandum explains key terms, describes the calculation of policy dividends, and provides a sample dividend calculation. Note that dividends are not guaranteed as they are declared annually by Guardian's Board of Directors.

Contribution Principle
Guardian allocates the dividend fund to policies in accordance with the contribution principle. This principle is designed to allocate dividends to each participating policy in the proportion that the policy contributed to Company earnings. This principle is the accepted standard of practice for mutual insurance companies in the United States. Guardian is a well-diversified company. Profits from other lines of business play an important role in determining dividends that are passed through to policyowners.

Dividend Substitution and Pegging
Guardian's current practice is to pay a dividend that is higher than the basic dividend formula amount when certain conditions apply. The practice is called Substitution if it applies in the first three policy years and Pegging if it applies thereafter. The intent is to add an extra degree of stability to policies. These adjustments apply to basic policy dividends only and do not apply to dividends on paid-up additions. This practice is not guaranteed as it is approved each year by the Board of Directors.

Substitution
In an environment of a declining dividend scale, Substitution improves early policy year dividend performance by eliminating dividend reductions that would otherwise occur. For policies illustrated in 2015, the basic non-loaned policy dividend that will be paid on the second and third policy anniversaries will not be less than the basic dividend amount

illustrated at the time the policy was made effective. Substitution does not affect the dividends on paid-up additions.

Pegging
Beginning with the non-loaned basic dividend paid on the fourth anniversary, Guardian currently employs a strategy called Pegging. Pegging allows for a smoother transition from year to year in a declining dividend scale environment. Pegging does not guarantee that the dividend will increase from year to year, but does soften the decline in the dividend that would otherwise occur. Pegging does not affect the dividends on paid-up additions.

<u>**Dividend Calculation**</u>
Every policy has a dividend fund. The dividend fund forms the basis for the calculation of the interest and mortality components. The base policy dividend fund grows with net premiums and interest and is charged for mortality costs. The dividend fund values for all policy years are set at issue based on a fixed interest rate and mortality rates from the applicable CSO table. The net premiums and dividend fund values may be different from the policy gross premiums and guaranteed cash values. These differences are accounted for in the loading component.

The example shown below is based on a 2014 form L99 Whole Life policy, insuring a male who was age 45 at issue and qualified for Guardian's most favorable risk classification. The face amount is assumed to be $500,000. The policy is assumed to be in its 20th year.

Non-Loaned Interest Component
During 2015, the non-loaned dividend interest rate is 6.05%. The dividend interest rate reflects a contribution from other Guardian lines of business. The difference between the non-loaned dividend interest rate and the interest rate underlying the dividend fund, which is 4.00% for this policy, is applied to the policy's dividend fund at the beginning of the year. In our example, this dividend fund is $340.86.

1) Take the difference between the non-loaned DIR and 4.00%.
   o 6.05% - 4.00% = 2.05%
2) Apply 2.05% to the dividend fund to get the interest component per $1,000 of face.
   o 2.05% x 340.86 = 6.988
3) Multiply 6.988 by the face amount to get the interest component in dollars.
   o 6.988 x $500 = $3,494

Mortality Component
Guardian's actual mortality experience is better than the guaranteed mortality. Excess mortality charges are returned to the policyholder through the dividend. The mortality return is the difference between the guaranteed mortality rate and the dividend mortality rate multiplied by the net amount at risk. The net amount at risk is the policy's face amount less the end-of-year dividend fund. In the calculation below, the end-of-year dividend fund is $344.06

1) Take the difference between the guaranteed mortality and dividend mortality rates.
   o 0.015234 – 0.00520 = 0.010034
2) Calculate the net amount at risk per $1,000 of face.
   o 1,000.00 – 344.06 = 655.94
3) Multiply 0.010034 by 655.94 to get the mortality component per $1,000 of face.
   o 0.010034 x 655.94 = 6.582
4) Multiply 6.582 by the face amount to get the mortality component in dollars.
   o 6.582 x $500 = $3,291

Loading Component

The Loading Component recovers the Company's expenses, including taxes, and assesses a contribution to policyowner's surplus, a profit charge.

The Loading Component for this sample policy is $560.

Putting It Together

The dividend at the end of policy year 20 is:

Dividend   = Interest + Mortality + Loading
                 = $3,494 + $3,291 + 560
                 = $7,345

I hope you have found this information useful. Please contact me for more information on this topic.