Sources of earnings

The following is provided in accordance with the OSFI guideline requiring Sources of Earnings (SOE) disclosure. SOE is a non-IFRS (International Financial Reporting Standard) financial measure. There is no standard SOE methodology. The calculation of SOE is dependent on, and sensitive to, the methodology, estimates and assumptions used.

SOE identifies various sources of IFRS net income. It provides an analysis of the difference between actual net income and expected net income based on business in-force and assumptions made at the beginning of the reporting period. The terminology used in the discussion of sources of earnings is described below:

Expected profit on inforce business

The portion of the consolidated pre-tax net income on business inforce at the start of the reporting period that was expected to be realized based on the achievement of the best-estimate assumptions made at the beginning of the reporting period. Expected profit for asset management companies is set equal to their pre-tax net income.

Impact of new business

The point-of-sale impact on pre-tax net income of writing new business during the reporting period. Issuing new business may produce a gain or loss at the point-of-sale, primarily because valuation assumptions are different than pricing assumptions and/or actual acquisition expenses may differ from those assumed in pricing. For example, new business losses in individual life insurance would emerge where valuation margins and acquisition expenses are relatively high.

Experience gains and losses

Pre-tax gains and losses that are due to differences between the actual experience during the reporting period and the best-estimate assumptions at the start of the reporting period.

Management actions and changes in assumptions

Impact on pre-tax net income resulting from changes in actuarial methods and assumptions or other management actions.

Other

Impact on pre-tax net income not addressed under the previous categories. Examples include acquisition/integration/restructuring and other related costs.

For the Year Ended December 31, 2018 (in millions of Canadian dollars)	**SLF Canada**	**SLF U.S.**	**SLF Asset Mgmt**	**SLF Asia**	**Corporate**	**Total**
Expected Profit on Inforce Business	**882**	**451**	**1,264**	**507**	**(106)**	**2,998**
Impact of New Business	**108**	**5**	**–**	**(98)**	**–**	**15**
Experience Gains and Losses	**424**	**(7)**	**–**	**(17)**	**(46)**	**354**
Management Actions and Changes in Assumptions	**31**	**(498)**	**–**	**76**	**145**	**(246)**
Other	**(1)**	**(51)**	**(71)**	**(14)**	**(13)**	**(150)**
Earnings on Operations (pre-tax)	**1,444**	**(100)**	**1,193**	**454**	**(20)**	**2,971**
Earnings on Surplus	**127**	**98**	**–**	**164**	**151**	**540**
Earnings before Income Taxes	**1,571**	**(2)**	**1,193**	**618**	**131**	**3,511**
Income Taxes	**(308)**	**19**	**(284)**	**(51)**	**27**	**(597)**
Earnings before Non-controlling Interests, Participating Policyholders' Net Income and Preferred Share Dividends	**1,263**	**17**	**909**	**567**	**158**	**2,914**
Less:						
Non-controlling Interests	**–**	**–**	**–**	**–**	**–**	**–**
Participating Policyholders' Net Income	**321**	**(35)**	**–**	**12**	**–**	**298**
Preferred Share Dividends	**–**	**–**	**–**	**–**	**94**	**94**
Common Shareholders' Net Income (Loss)	**942**	**52**	**909**	**555**	**64**	**2,522**

For the Year Ended December 31, 2017	SLF Canada	SLF U.S.	SLF Asset Mgmt	SLF Asia	Corporate	Total
Expected Profit on Inforce Business	840	407	1,256	435	(132)	2,806
Impact of New Business	133	(11)	–	(81)	–	41
Experience Gains and Losses	97	(79)	–	70	30	118
Management Actions and Changes in Assumptions	164	(835)	–	284	62	(325)
Other	(16)	(105)	(150)	–	(76)	(347)
Earnings on Operations (pre-tax)	1,218	(623)	1,106	708	(116)	2,293
Earnings on Surplus	155	91	–	160	90	496
Earnings before Income Taxes	1,373	(532)	1,106	868	(26)	2,789
Income Taxes	(197)	392	(453)	(62)	18	(302)
Earnings before Non-controlling Interests, Participating Policyholders' Net Income and Preferred Share Dividends	1,176	(140)	653	806	(8)	2,487
Less:						
Non-controlling Interests	–	–	–	–	–	–
Participating Policyholders' Net Income	213	4	–	28	–	245
Preferred Share Dividends	–	–	–	–	93	93
Common Shareholders' Net Income (Loss)	963	(144)	653	778	(101)	2,149

Analysis of results

For the year ended December 31, 2018, the pre-tax expected profit on inforce business of $2,998 million was $192 million higher than 2017. The increase in expected profit was largely driven by business growth in Canada, US, and Asia, as well as currency impacts from the change in the Canadian dollar relative to foreign currencies.

The new business gains in 2018 was $15 million compared to $41 million a year ago. The change was mainly due to sales level in Canada and sales mix in Asia.

The 2018 experience gain of $354 million pre-tax was primarily due to favourable Participating policy experience in Canada, interest on par seed capital in Canada and the U.S., favourable morbidity experience in the U.S. Group Benefits business, positive net credit experience and gains from investing activity on insurance contract liabilities. This is partially offset by unfavourable equity market impacts.

For the year 2018, management actions and changes in assumptions resulted in a pre-tax loss of $246 million. In Canada, the pre-tax gain of $31 million reflected favourable changes to mortality assumptions in Group Retirement Services, the favourable change to provision in the Canada participating account, offset partially by model enhancement and methodology changes. In the U.S., the pre-tax loss of $498 million reflected updates to policyholder assumptions and the strengthening of reinsurance provision, offset partially by the favourable change to the provisions in the U.S. participating account. In Asia, the pre-tax gain of $76 million reflected favourable mortality, offset partially by updates to policyholder assumptions, both items were in Asia International business. In Corporate, the pre-tax gain of $145 million reflected favourable mortality in U.K.

Other in 2018 resulted in a pre-tax loss of $150 million. In the U.S., the loss of $51 million was due to the impact of integration costs related to the U.S. employee benefits businesses acquired. In the Asset Management pillar, the loss of $71 million was related to fair value adjustments on MFS's share-based payment awards. In Asia, the loss of $14 million mainly pertains to a distribution arrangement in India for asset management. In Corporate, the loss of $13 million was primarily due to the restructuring charge related to actions to enhance business processes and organizational structures and capabilities.

Net pre-tax earnings on surplus of $540 million in 2018 was $44 million higher than a year ago. The increase was mainly due to increasing investment income from Cash & Short-term and Bonds, partially offset by weaker Available-for-Sale asset gains.

The 2018 Sources of Earnings has been changed to reflect the International business move to Asia from the U.S. In addition, expected profit on inforce business and impact of new business reflect a change in presentation for U.S. employee benefits business. Amounts in expected profit on inforce business and impact of new business in 2017 was previously $467 million and $(71) million for U.S. excluding International, and $2,866 million and $(19) million for the Total Company, respectively, with a net change of $60 million between the two categories.