



# Your guide to with-profits

Important information  
about investing in  
our with-profits fund  
using one of our  
range of unitised  
pension plans.



We have written this guide to give you more information about investing in our with-profits fund through one of our 'unitised' pension plans or 'policies'.

These include the following types:

- Executive Pension
- Free Standing Additional Voluntary Contributions (FSAVC)
- Group Personal Pension
- Pensionbuilder
- Pension Solutions
- Personal Pension
- Section 32 (Buy Out) Plan

The type of plan you have will be set out in the original documents that you were given when you took out your plan. 'Plans' are often referred to as 'policies' but for simplicity we will call them plans in this guide.

This guide explains how your unitised with-profits pension plan works. You should read through all of this document as it contains important information about your plan, but here is a brief summary.

When you invest your money, it is pooled with the money invested by many other planholders in part of our with-profits fund. What you get back from your plan depends on the fortunes of the with-profits fund, in particular how well the investments have done in the relevant part of the fund.

Your with-profits plan:

- has guaranteed minimum values at the times explained later in this guide;
- may have bonuses added to these guaranteed minimum values; and
- will normally be cushioned from the daily ups and downs of the stock-market (we call this 'smoothing').
- After meeting its obligations, the with-profits fund will over time be distributed in full to with-profits planholders. Our aim is that different groups of planholders receive their fair share of the fund.

This guide is a summary of a longer, more detailed, document called our Principles and Practices of Financial Management ('PPFM'). We have tried to make sure that this guide accurately reflects the PPFM. But the PPFM will apply if there is any difference between the information in it and the information in this guide.

The full PPFM is on our website at [www.scottishwidows.co.uk/about\\_us/investor\\_relations/our\\_principles\\_and\\_practices/scottish\\_widows\\_ppfm.html](http://www.scottishwidows.co.uk/about_us/investor_relations/our_principles_and_practices/scottish_widows_ppfm.html) or you can ask us to send you a copy. Our address is given at the end of this guide in the section "How can I get more information?" Also at the website are some 'Questions and Answers' that can help you check what sort of plan you have.

We've set out the information in this guide as answers to the following questions.

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For many of the plans covered by this guide, the with-profits fund is just one of the investment choices we offer. It is possible that only some of your money is invested in the with-profits fund. The documents you were given at the start of your plan will tell you if it gives you this choice of alternative investments. This guide only covers the with-profits part of your investment.

It may be that your plan is held by the trustees of a pension scheme set up by your employer. If this is the case, you may well still find this guide useful but where we say 'you' we will often mean the trustees acting on your behalf.

# What is meant by with-profits?

We use the term 'with-profits' to mean a type of investment. It provides medium to long-term growth potential with some guarantees (see "What are the guarantees?" on page 5). By medium to long-term we mean investments that last at least 5 years.

We have added units to your plan each time you have made a payment into it. If you have a Pensionbuilder plan all your units will be with-profits. For other types of plan you may have decided to make some or all of your investment in with-profits. Your units will stay with-profits until one of the following happens:

- you retire and take a pension from your plan;
- you transfer your plan to another company, or another plan with us;
- you die; or
- you change from with-profits by switching your investment to other funds (not all plans allow this).

The units we have added to your plan have a guaranteed minimum value in certain circumstances. A description of this guarantee and the circumstances when it applies is given in "What are the guarantees?" on page 5. We may add regular bonus to your units, which you will see as an increase in their value (or 'bid price'). This increases your guarantees.

We may also add final bonus to your plan when you move out of with-profits in one of the ways listed above. Further information on bonuses is given in "What types of bonus may be added to my plan?" on page 6. When guarantees do not apply we may make a 'market value reduction' (see page 10).

While you have with-profits units, your money less any initial charges is pooled in part of our with-profits fund with the money invested by many other plan-holders. Our approach to managing our with-profits fund can change from time to time. It's not exactly the same for all types of plan.

## The with-profits fund

The with-profits fund invests in a mix of assets such as company shares, property, bonds and cash deposits. Bonds are a type of loan, usually to the Government or companies. You may have heard Government bonds referred to as gilts. The proportion of the with-profits fund that is put into each of these different types of asset will vary over time. The mix of assets can be different for different parts of the with-profits fund.

While shares and property have usually risen more in value than bonds and cash over long periods such as 20 years, the return has also been much more variable.

One year the investment may do very well, but the next could see a big fall in value – this is often called ‘investment risk’.

We may also use ‘derivatives’, which are specialist forms of investments. We apply strict controls over how we use derivatives and use them to reduce investment risk. For example, some derivatives give the with-profits fund the right to buy or sell assets at a fixed price at a future date.

## Your group

When managing the with-profits fund we often look separately at different groups of planholders. The group you’ll be in will depend on the type of plan that you have and when you started it.

## The shareholders

Scottish Widows plc is a ‘proprietary company’. This means that we have shareholders. Our shareholders receive the charges that we make on plans like yours and in return meet the cost of looking after your plan.

# What are the guarantees?

Your plan has some guarantees. When these guarantees apply, each unit added to your plan will have a minimum value. This value is the 'bid price' of the unit. It is a minimum amount and we may pay out more than this. The guarantees apply:

- if you die while you still have with-profits units; and
- on the dates that are set out within the documents you got at the start of your plan.

The guarantees do not apply at other times.

Each plan has one main guarantee date. It will usually be on the retirement date you chose when you started your plan. The date will be set out in your plan's documents and will depend on the type of plan that you have. For example, it might be called the 'selected pension date' or the 'with-profits maturity date'. For simplicity in this guide we will call all of these dates a 'guarantee date'.

Some plans may allow you to change this guarantee date but, if this is the case, you will need to tell us in good time. Some plans may have more than one guarantee date. In some plans the guarantee only applies if you start receiving your pension on the guarantee date. You can find out if any of these apply to you by checking the Key Features or other information that we gave you at the start of your plan.

If your plan is a Pensionbuilder plan, a special guarantee applies for any units added to it before 1 July 1994. For each of those units, on a guarantee date, we guarantee to pay the higher of:

- the initial value of the unit rolled up at 4% a year; and
- the initial value of the unit plus any regular or final bonus added in line with our standard practice.

The initial value of the unit is its bid price on the day it was added to your plan.

# What types of bonus may be added to my plan?

Two types of bonus may be added to your with-profits units. They determine what you will be able to get back when guarantees apply. They are:

- regular bonus, which we may add daily as permanent increases in the guarantees that apply to your with-profits units; and
- final bonus, which we may add on top of those guaranteed amounts when with-profits units are cashed in.

Different groups of investors may have different levels of each type of bonus. We usually adjust levels of regular and final bonus twice a year, but we may sometimes change them at other times.

Future rates of bonus are not guaranteed.

The yearly statement we send you includes information about the current bonus rates for your group.



# How do you decide the bonuses?

Regular bonuses and final bonuses have different purposes, and we decide them differently.

## Regular bonus

Over time the regular bonuses increase the bid-price of the with-profits units in your plan. This increases the guarantees.

The size of the regular bonus depends mainly on what bonuses we have already added to units, past investment performance and what we expect in the future. When setting a rate of regular bonus we consider all the plans that receive that bonus and not each plan or unit by itself. We aim to set the regular bonus rate so that there is scope in the future for final bonuses if the relevant assets of the fund provide steady growth. We may set rates at a lower level than this when it is necessary to limit losses to the with-profits fund.

We expect higher-risk assets to give a better, but less predictable, return over the long term. If we were to set rates of regular bonus at higher levels, we'd have to invest more of the with-profits fund in more predictable lower-risk assets (see "Investment performance" on page 12). We would then expect to have less to pay out to planholders.

We may raise or lower rates of regular bonus in several stages. There could be no regular bonus in some years.

## Final bonus

Final bonus may be added to top up the bid price of units to help make a fair level of payouts to all planholders.

We apply different levels of final bonus for with-profits units bought in different periods (a year or part of a year). This means different rates of final bonus may apply to units in your plan that were added at different times.

We take 'sample units' added in each of these different periods. The sample units are chosen to be representative of the units of the plans in your group. Next, we set a 'target payout level' for the sample units from each period. We then compare this target level with the corresponding guaranteed amount and pay a final bonus if the target level is bigger. In other words, we aim to 'top up' what planholders get from each unit to reflect the sample units' target levels.

To help us to work out the target levels we:

- take the ‘asset share’ of the sample unit (see “Asset shares” on page 11);
- increase it so the final bonus includes the investment returns we expect to earn between when we set the final bonus and when units are cashed in;
- make the adjustment for the smoothing of recent investment returns described below, which gives us a ‘smoothed asset share’; and
- make a small reduction towards the cost of the extra amounts we expect to pay from time to time because of guarantees.

If you took out your plan on or before 3 March 2000, when we demutualised, we may add a small amount to the final bonus. The current level of this addition can be located on the with-profits section of our website.

Overall, we aim that the total payouts over many years are at least equal to the asset shares.

## Smoothing

With-profits investing includes a special feature called ‘smoothing’. The stock-market goes up and down daily and can move a lot in a short space of time. We aim to smooth out some of the effects of these short-term peaks and troughs. We only consider movements in the last two years. So smoothing will not lessen the effects on your return of longer-term changes in the stockmarket.

We use smoothing whenever the guarantee applies but it may also apply if you choose to move your investment from the with-profits fund at other times. Smoothing is complex and more details of our approach are in our PPFM.

We constantly monitor investment conditions, and may change levels of final bonus at any time. For instance, we’d consider a change if asset shares move more than 15% away from the smoothed asset shares we had used for the current bonus rates. We’d also consider a change if it was necessary to limit losses to the with-profits fund. We may limit the smoothing when setting final bonus rates to reduce the likelihood of a further final bonus change within the following six months.

Final bonuses can sometimes change very significantly, even within a few months, in spite of smoothing.

# What if I decide to move my plan from with-profits or cash it in on a date when guarantees don't apply?

You can choose to make a change that results in your investment leaving the with-profits fund at a date which is not a guarantee date. This may happen because you decide:

- to retire before or after the guarantee date;
- to move your investments from the with-profits fund to another investment fund, if your plan allows you to do this; or
- to transfer to another plan with us or with another company.

Whatever the reason, we will still aim to give you fair value for your investment. However, there is no minimum guarantee of what your plan will pay and you will not get anything for the guarantees you are giving up. In fact, it is possible that you could get back less than you invested if markets are low enough.

How much you get back from each of your with-profits units will depend on:

- the bid price of the units, which includes the regular bonuses we have already added;
- plus any final bonus that we add;
- less any 'market value reduction'.

If you have a Pensionbuilder plan, charges may apply if you transfer your investment out of your plan early. These charges help us to recover costs and are not covered in this guide. They will be described in the Key Features or other information that we gave you at the start of your plan.

## Market value reductions

Our aim is to maintain a fair level of payout to everyone investing in the with-profits fund.

In other documents we have sometimes referred to market value reductions as 'market level adjustments'. Different levels of them apply for different groups of planholders and for with-profits units bought in different periods (a year or part of a year).

We take representative sample units for each different period for the plans in your group. We set 'target payout levels' for the sample units from each period. The target levels are the asset shares of the sample units adjusted for smoothing. If you took out your plan on or before 3 March 2000, when we demutualised, we may add a small amount to the target level. This results from our demutualisation and the current level of this addition can be found on the with-profits section of our website. If this target level is lower than the bid price of the unit plus any final bonus, then we may apply a market value reduction.

The adjustment we make to the asset share for smoothing is similar to the one used when deciding final bonuses, although there are three main differences:

- We only look at stockmarket movements over at most the last six months. This means that there would be a quicker fall or rise in the amount you could get back if there were a large fall or rise in the value of the relevant assets.
- The terms of your plan restrict the size of any market value reductions. So we may need to restrict the smoothing adjustment we make.
- The smoothing adjustment is, in any case, limited to 5%.

Again there are more details in the PPFM.

We constantly monitor investment conditions, and may introduce or change market value reductions at any time. For instance, we'd consider a change if payouts differ by more than 5% from the relevant asset shares. We'd also consider a change if it were necessary to avoid excessive profits or losses to the with-profits fund.

If we introduce a market value reduction, we'll check after not more than three months to see if it should still apply. We'll also check whenever rates of final bonus change.

For Pensionbuilder plans held by the trustees of an employer's pension scheme, we may apply individually-calculated market value reductions.

# What affects how much I might get to buy a pension?

## Asset shares

Asset shares help us decide the bonuses to pay and the market value reductions to apply. The way this works is described earlier in this guide.

Very broadly, asset shares are an accumulation of the amounts invested. So when deciding what an asset share would be, we look at the following three main factors:

- the amounts invested in sample with-profits units (see below);
- when they were invested; and
- the past investment performance of the 'relevant assets' (see "Investment performance").

We also make adjustments for:

- the charges we have made to cover the cost of managing your plan;
- any profits and losses from 'business risks' (see "What are the risks of investing in the with-profits fund?" on page 13); and
- taxation.

We track asset shares of the with-profits fund for sample with-profits units. We track them separately for the different groups of planholders, including your group, and for units that were started at different times.

## Investment performance

This guide sometimes refers to ‘relevant assets’. These make up the part of the with-profits fund whose investment performance has an important effect on asset shares and therefore on what you will get back. The performance will depend on, among other things, how much of the relevant assets are made up of each of the different types of asset. The mix of the relevant assets can be different for different groups of investors.

We hold part of the relevant assets for your group in higher-risk assets such as shares and property, to try to achieve higher returns. The rest is in lower-risk assets, such as fixed-interest bonds issued by the Government or by companies, and cash deposits that earn interest.

The performance of different types of asset varies considerably over time. So we may change the mix of the assets with the aim of:

- getting the best possible long-term performance; and
- making sure that the with-profits fund can always meet its guarantees.

When doing so we allow for support from some of our assets outside the with-profits fund, following guidelines set at the time of the demutualisation. This means we can invest more of the relevant assets in shares and property. (See also “What is the capital support for the with-profits fund?” on page 15.)

We include information about the mix of assets within the PPFM section of the Scottish Widows website. You’ll therefore be able to see how we review and change the mix of the assets over time.

# What are the risks of investing in the with-profits fund?

Your with-profits investment, by being part of our with-profits fund, is exposed to 'investment risk'. This is the risk that the value of the relevant assets of your group can fall as well as rise. There are other risks known as 'business risks'.

The main business risks for your plan come from the guarantees and smoothing of the payments that we make to other with-profits investors. When we pay some plans more because of guarantees or smoothing it leaves less in the with-profits fund for the other plans. On the other hand, when we pay some plans less because of smoothing it leaves more for the other plans.

Some of the plans covered by this guide were originally taken out with Scottish Widows' Fund and Life Assurance Society before it demutualised on 3 March 2000. At this time these plans were transferred to Scottish Widows plc and are known as 'transferred plans'.

For transferred plans there are more business risks. These are smaller and include:

- the with-profits fund's profits and losses from the non-profit policies that were transferred into it in March 2000 or that are set up when with-profits pension policies are converted to pensions at retirement; and
- the cost of compensation paid to the holders of plans sold by Scottish Widows before demutualisation, if any are shown to have been mis-sold.

Any profits or losses arising from these business risks would not affect the asset shares of transferred plans. Instead they would be paid into or taken from a separate part of the with-profits fund known as the Additional Account. This Additional Account was set up at demutualisation to cover such things. Anything left over in it would be paid out as extra final bonus to the remaining transferred plans. If the Additional Account is not sufficient to cover losses arising from business risk, any later losses would be met firstly from assets outside the with-profits fund. However in extreme cases some losses could be shared among all transferred with-profits plans.

Transferred plans are unlikely to share in the profits and losses from other, more recent plans, and vice versa.

There are naturally risks associated with your plan that apply to other sorts of investment and not just to with-profits plans. Those other risks, such as the risk that the taxation of pensions may change, would also apply to other ways of saving for your retirement.

This guide deals only with risks that are directly associated with your plan being invested in our with-profits fund. If you were given a Key Features document at the start of your plan, you can find out about the other risks there.

# What is the capital support for the with-profits fund?

We aim to hold enough assets in the with-profits fund to provide a fair level of payouts to the current investors in the fund. While we could hold some extra assets as 'working capital' in the fund, most of the working capital will be held elsewhere in the company.

Working capital provides support for the with-profits fund as and when it's needed. The support helps us to maintain the mix of assets that we describe in "Investment performance" on page 12. It also helps us to meet our aim of maintaining a fair payout to everyone investing in the with-profits fund.

For more on how all this works, see our PPFM.



# How can I get more information?

If you're still not sure about your with-profits investment, you should speak to your financial adviser or contact us direct. If you wish to contact us you can write to us at:

**Scottish Widows**

**PO Box 902**

**15 Dalkeith Road**

**Edinburgh**

**EH16 5BU**

Or you can call us on **0845 845 0845**. We're open from 8am to 6pm Monday to Friday and from 9am to 12.30pm on Saturday. We may record and monitor calls to help us improve our service.

We'll write to you if we make a change to our approach to managing our with-profits fund that might have a significant effect on your plan. We'll also write if we change any of the 'Principles' in our PPFM. We'll normally include a replacement guide.

If you've any other with-profits investments with us that aren't covered by this guide, we'll send out your guide or guides for them.



**SCOTTISH WIDOWS**  
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