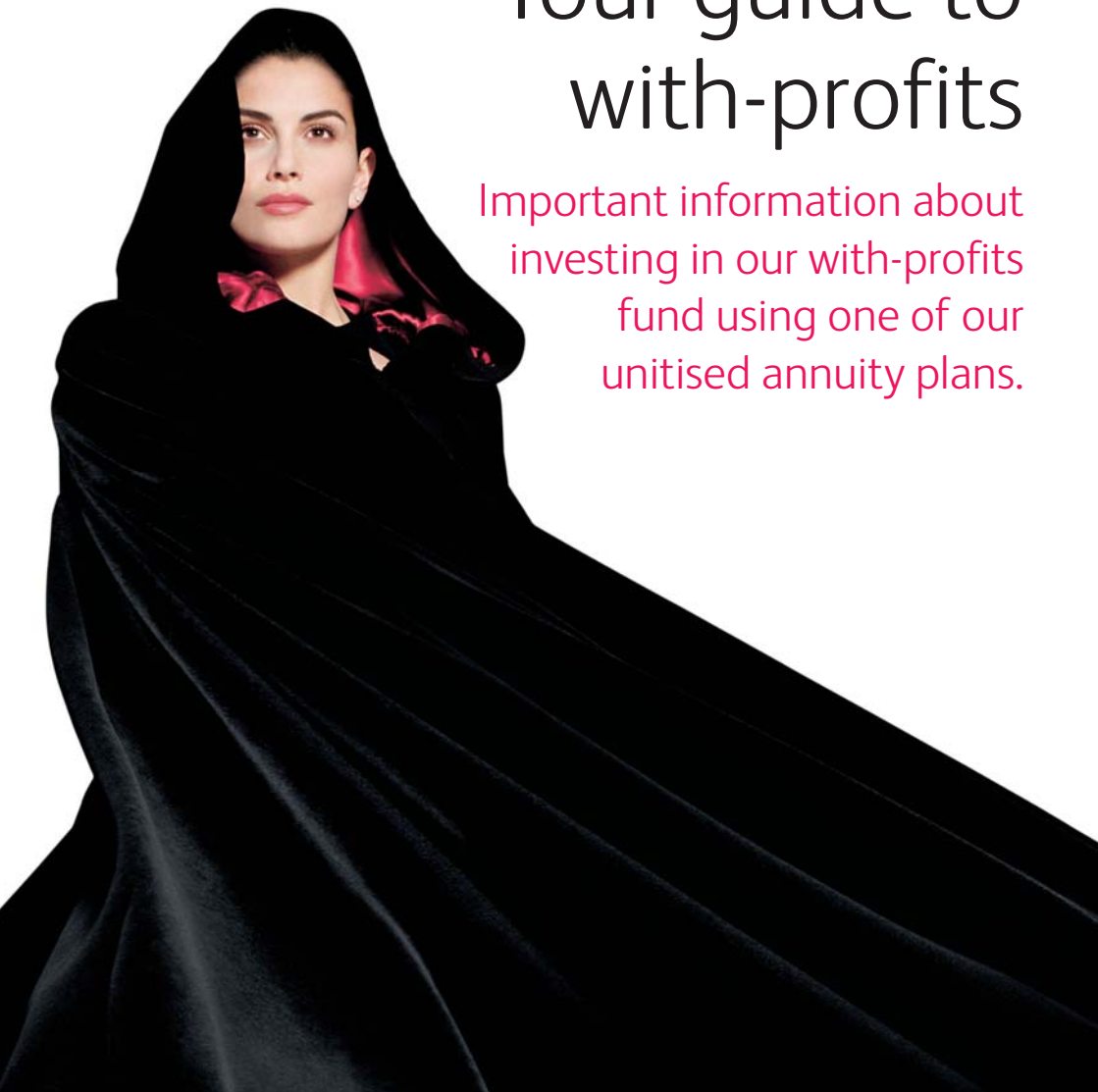


**SCOTTISH WIDOWS**  
preparation is everything  
*official pensions and investment provider*



# Your guide to with-profits

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



We have written this guide to give you more information about investing in our with-profits fund through one of our ‘unitised’ annuity plans. ‘Plans’ are sometimes referred to as ‘policies’ but for simplicity we will call them plans in this guide.

This guide explains how your unitised with-profits annuity 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 provides guaranteed minimum pension payments to which bonuses may be added. These payments will normally be cushioned from the daily ups and downs of the stockmarket (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/PPFM](http://www.scottishwidows.co.uk/PPFM)**, 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?”

# Contents

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

- What is meant by with-profits? 3
- What are the guarantees? 5
- What types of bonus may be added to my plan? 5
- How do you decide the bonuses? 6
- What affects investment performance? 9
- What are the risks of investing in the with-profits fund? 9
- What if I decide to change my with-profits pension to another type of pension? 11
- What is the capital support for the with-profits fund? 12
- How can I get more information? 13

For many of the plans covered by this guide, the with-profits fund was just one of the investment choices we offered. It is possible that only some of your money was invested in the with-profits fund. 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.

Most people choose to have their pension income paid monthly. You may have chosen to receive it less often than this but for simplicity this guide is written assuming a monthly income.

## 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.

## How does it work?

### Your pension

Under your plan we promise to pay you a regular series of with-profits pension payments for the rest of your life. (The documents you received when you started your plan will describe the payments, if any, that we'll make from your plan after your death.)

Each of your pension payments is based on a number of with-profits units that was set when you bought your plan. We call these units the 'base units' for your plan. The size of each of your pension payments will depend on the value of the base units at the time of the payment. There is a minimum value to each base unit (see "What are the guarantees?" on page 5). We may add regular bonus to your base units, which you will see as an increase in their value (or 'bid price'). This increases your guarantees. We may also increase each

pension payment with a top-up bonus. Top-up bonuses can go up or down and so the value of each base unit, and hence the size of each payment, can rise or fall. Further information on bonuses is given in "What types of bonus may be added to my plan?" on page 5.

The size of each pension payment will also depend on how many base units your plan has at the time of the payment. When you started your plan you may have chosen to allow in advance for some future growth in the value of the base units. In this case your plan will have started with more base units and a higher pension, but since then this number will have steadily reduced. The statement we send you each year shows how many base units your plan has. If they are reducing, the statement will show the rate at which they reduce. The statement calls it the 'anticipated growth rate'.

You may have chosen a pension that continues to your partner or a dependant after your death. If you have, then after you die further payments will be a fixed proportion of the value of the base units. You will have already chosen this proportion and the details will be in the documents that you got at the start of your plan. You may be receiving your pension income because of such circumstances, in which case the adjustment will have already been made.

The general principles and practices of this guide apply to your pension payments as well.

The investment backing your pension is pooled in our with-profits fund with the investments of many other planholders. 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 when you started your plan.

## 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?

As well as our promise to make regular pension payments there are other guarantees. These guarantees define a minimum pattern of pension payments to you and your dependants.

- The amount of each pension payment will be at least as much as the guaranteed value of the base units on which it is based. It is a minimum amount and we may pay out more than this.

The guaranteed value of each unit is often referred to as the 'bid price' of the unit. This price will have been increased by the regular bonuses we have added since your plan started.

The number of base units in your plan may reduce each month (see "Your pension" in "How does it work?" on page 3). This means the guaranteed amount of your pension may fall.

- If your pension continues to be paid to a dependant after you die, we will pay at least a fixed percentage (up to 100%) of the guaranteed value. The fixed percentage is shown in the documents you got at the start of your plan.
- If you started your plan on or after 9 May 2000 and the number of base units reduces each month, then

there's another guarantee. The size of the pension payments from your plan won't fall below a certain fixed level during your lifetime. The documents you received when you started your plan will state this minimum level.

These guarantees don't apply if you change your with-profits pension into another type of pension (see page 11).

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

Two types of bonus may be added to your with-profits base units. The bonuses are:

- regular bonus, which we may add daily as permanent increases in the guarantees that apply to your with-profits base units; and
- additional 'top-up' bonuses, which we may add to the guaranteed amounts when we make each pension payment.

Top-up bonuses are not added permanently. They apply separately to each pension payment and may be changed or removed at any time.

Different groups of investors may have different levels of each type of bonus. We usually adjust levels of regular and top-up 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 top-up bonuses have different purposes, and we decide them differently.

### Regular bonus

Over time the regular bonuses increase the bid-price of the with-profits base 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 top-up 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 "What affects investment performance?" on page 9). 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.

### Top-up bonus

We work out rates of top-up bonus for each group of plans, including your group. This means we apply different rates of top-up bonus for base units bought in different periods (usually a year or part of a year).

For each group of plans we set a total 'target value', which we explain below. We pay a top-up bonus if the total value we have already guaranteed to pay is less than this target value.

In other words, we aim to 'top up' the pensions that planholders will get so that they reflect the target value for their group of plans.

## Target value

You can think of target values as representing the money available to make all future payments from the plans in each group. The starting point for a target value is something called the ‘asset share’ of the group of plans. Very broadly, asset shares are an accumulation of the amounts invested for these plans less the pension amounts already paid out. So when deciding what an asset share would be, we look at the following four main factors for each group of plans:

- the amounts invested by all the planholders in the group;
- when the amounts were invested;
- the past investment performance of the ‘relevant assets’ (see “What affects investment performance?” on page 9); and
- the pension payments we have already made to all the planholders in the group.

We also make adjustments for:

- other profits and losses described in “What are the risks of investing in the with-profits fund?” on page 9;
- the charges we have made to cover the cost of managing your plan; and
- taxation.

To help us to work out the target levels we then:

- take the ‘asset share’ of each group of plans;
- increase it so the top-up bonus includes the investment returns we expect to earn between when we set the top-up bonus and when units are cashed in;
- make the adjustment for the smoothing of recent investment returns described overleaf, 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 top-up bonus. The current level of this addition can be located on the with-profits section of our website.

## How we use target values to decide top-up bonuses

We look at the corresponding total value of what we have already guaranteed to pay. This is what we expect the total of all future pension payments to be if we add no future bonuses. It allows us to compare the money in the with-profits

fund available for future payments with the minimum needed to pay the guaranteed level of payments. We pay a top-up bonus if the money available adjusted for smoothing (the target value) is more than this minimum amount.

How many pension payments are made in the future will depend on how long planholders live. So the size of top-up bonus we add can depend on our view of how long we expect groups of planholders to live.

We may have changed our view since the plans in your group started. How or whether this will affect your plan will depend on when it started:

- If your plan started on or after 9 May 2000 then we will allow for any change in our view when deciding on what future pension payments are expected. If we expect planholders in your group to live longer than we did previously, your top-up bonuses are likely to fall. If we expect them to live for a shorter time, top-up bonuses are likely to rise.
- If your plan started before 9 May 2000, changes in our view don't affect bonuses.

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

## Smoothing

With-profits investing includes a special feature called 'smoothing'. The stockmarket 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 pension income of longer-term changes in the stockmarket. Smoothing is complex and more details of our approach are in our PPFM.

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

We constantly monitor investment conditions, and may change levels of top-up 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 top-up bonus rates to reduce the likelihood of a further top-up bonus change within the following six months.

## What affects 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 how much your pension will be. 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 planholders.

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 12.)

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 profits, or losses, to the fund arising from these business risks can add to, or reduce, future bonuses for continuing plans like yours. Different business risks can affect different groups of plans.

## Plans that started after 3 March 2000

There are two main business risks for these plans:

1. Planholders in your group may live longer or be expected to live longer than we previously anticipated. The amount in the with-profits fund to make pension payments would then be spread over a larger number of payments than expected. This would reduce the bonuses.

If fewer planholders live, or life expectancy reduces, then the same amount would be spread over fewer payments. This would increase bonuses.

These possible losses or profits do not affect plans that started from 4 March 2000 up to and including 8 May 2000.

2. Each pension payment that we make to planholders in your group leaves less in the with-profits fund to make later pension payments. When smoothing or guarantees increase the payments we make, this also leaves less in the with-profits fund to make later pension payments. The future bonuses will then tend to reduce.

Future bonuses will tend to increase when the payments we make now are reduced by either smoothing or by the small reductions we make when setting top-up bonuses (see page 6).

## Plans that started on or before 3 March 2000

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 following:

3. 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.
4. 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.

However, any profits or losses arising from these four business risks would not affect the asset shares of transferred plans. Instead they would be paid into or taken from the 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 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 types of unithised pension. 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 if I decide to change my with-profits pension to another type of pension?

If you started your plan on or after 9 May 2000 you can choose to change your with-profits pension to another type. If you started your plan before this date then you do not have this option and the rest of this section does not apply to you.

If you choose, we can convert your with-profits pension into one that will pay a fixed pattern of pension payments. In other words it will not depend on the future performance of the with-profits fund.

You can only convert your pension on an anniversary of the date you started your plan. It must be at least 2 years after the start of your plan and before your 75th birthday.

If you ask to change to a fixed pattern of payments, those payments will be set at a level that gives fair value for the with-profits pension you are giving up. This level will be set at the time you request the conversion. We'll take into account the latest asset share of your group of plans. We also take into account a number of other factors, including:

- a reduction to allow for the future charges we had expected to receive; and
- any further adjustment we need to make to be fair to the plans in your group that stay with-profits.

We're unlikely to apply smoothing to the asset share when deciding the terms to offer. This means that if there is a large fall in the value of the relevant assets there is likely to be a large fall in the amount of alternative pension that we offer.

There is no guarantee of the terms that we'll offer.

## 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 "What affects investment performance?" on page 9. 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**  
*preparation is everything*  
*official pensions and investment provider*



As part of the Lloyds Banking Group, Scottish Widows is proud to be an Official Provider of the London 2012 Olympic and Paralympic Games.  
Scottish Widows plc. Registered in Scotland No. 199549. Registered Office in the United Kingdom at 69 Morrison Street, Edinburgh EH3 8YF.  
Telephone: 0131 655 6000.

Scottish Widows plc is authorised and regulated by the Financial Services Authority. Our FSA Register number is 191517.

44624 11/08