



How we invest your money

Your guide to the Scottish Friendly With-Profits fund

Introduction

This guide explains to you how we manage our With-Profits fund. It contains important information about how your policy works and how you can expect us to manage it. You may wish to read it alongside:

- your policy or Key Features document, which gives essential information
- your personal illustration (where appropriate), which shows what you might get back in the future

After you have read this guide, please keep it in a safe place.

What is the With-Profits fund?

Our With-Profits fund is an investment fund where your money is combined with that of other customers. We manage the fund on behalf of all with-profits policyholders and pay all policy benefits and costs from the fund.

By investing in the fund through one of our with-profits products, you become a member (owner) of Scottish Friendly.

As a mutual organisation, we have no shareholders and all the profits from the With-Profits fund are used for the benefit of our members.

What does the With-Profits fund invest in?

The fund invests in a range of carefully selected assets including:

- the shares of UK and overseas companies
- bonds issued by the UK Government and overseas governments as well as those issued by companies
- property investments
- cash

What will my final return be?

The final return will be broadly equal to the amount you would have received had you invested directly in the assets backing your policy.

The return will be calculated after the deduction of running costs; including the cost of setting up and administering policies as well as providing benefits such as life insurance.

Our principle aim is to provide a fair return on your money and we, of course, aim to treat all our members fairly.

Your final return will be made up of:

- the basic value of the units that are held by your policy (that is the number of units multiplied by the unit price at that time)
- any additional final bonuses that may be added on the end date of your policy

What are my guarantees?

After the deduction of charges your premiums will purchase units in the unitised With-Profits fund.

The price of these units is guaranteed not to fall provided you maintain your policy for the agreed period (or death if earlier). At this point, the guaranteed minimum that will be paid on your policy will be the units multiplied by the current unit price.

If your policy does not have a fixed term then your policy documents will provide you with details of the date upon which you can cash in your policy on this guaranteed minimum cash sum basis.

If you cash in your policy at any other time, it may incur a Market Value Reduction (see below for more details).

You should consult your policy or Key Features document for more details.

How are regular bonuses determined?

Regular bonuses are normally set once a year although in extreme circumstances they may be changed more frequently.

We add regular bonuses to your policy by increasing the price of the units. This increases the value of the units held by your policy.

The amount of regular bonus is set at a level that takes account of the investments within the fund and the projected final payout on policies. The level is set with the intention of allowing Scottish Friendly to pay a final bonus.

In severe market circumstances, such as a significant and prolonged fall in the stock market and/or interest rates, the regular bonus rate could fall to zero.

Every year you will receive a statement that will provide you with details of any bonuses that have been added to your policy.

How are final bonuses determined?

A final bonus may be paid on your policy end date and is paid through the addition of new units into your policy.

The actual final bonus (if any) will depend on the performance of the With-Profits fund. The final bonus could make up a significant part of the total payment although where the performance has been poor there may be no scope to pay a final bonus.

What is a Market Value Reduction?

If you take your policy proceeds on the policy end date, the basic benefits are guaranteed (see above) then the minimum payment will be the unit price multiplied by the number of units held by the policy at that date.

However, if you decide to cash in your policy at any other date a Market Value Reduction (MVR) may apply. This effectively reduces the unit price of the units held by your policy.

If an MVR is applied it will reduce the cash in value of your units to bring your policy value into line with the amount you would have received had you invested directly in the assets backing your policy.

If your policy does not have a fixed period then your policy documents will provide you with details of the date upon which you can cash in your policy without any Market Value Reduction. For example this may be 10 years after you took the policy out.

What is smoothing?

When applying a final bonus, or an MVR, Scottish Friendly will aim to ensure that payouts remain in line with the amount that you would have received had you invested directly in the assets backing your policy.

To help smooth out these adjustments, rates are normally rounded to the nearest 5%.

Who looks after my money?

Scottish Friendly manages the With-Profits fund and the Board of Directors oversee it.

The fund is managed to maximise growth whilst minimising risk. Additionally the fund is managed to ensure it can afford to meet all existing policyholders' guarantees and that Scottish Friendly satisfies all legal and regulatory requirements.

The investment strategy is reviewed at least once a year and the investment outlook and performance are monitored at least monthly.

Every year the Board will report to members confirming that the fund has been managed in accordance with its principles and practices and also noting any discretion that they have exercised, under advice from the fund's With-Profits Actuary.

The fund will be managed according to the full Principles and Practices of Financial Management (available on the Scottish Friendly website or on request).

You will be notified three months in advance of any changes to the principles governing the fund.

How does Scottish Friendly decide what the With-Profits fund will invest in?

The mix of investments held takes account of the current and projected financial strength of the fund. Additionally Scottish Friendly will take account of the expected returns and risks available from different types of investment.

Normally between 20% and 70% of the assets backing your policy would be invested in shares and property with the rest in cash, government and corporate bonds.

Scottish Friendly closely monitors the value of the assets backing policies against the amount required to pay all guaranteed benefits.

Should the amount fall close to this minimum value then the proportion of assets held in shares and property could be significantly restricted.

What are the support assets?

Scottish Friendly will always hold more assets than it needs to meet the benefits promised to its members.

These additional assets are known as support assets.

Support assets are used to provide additional security to policyholders. For example the cost of unforeseen risks (see “How are business risks managed?”) will initially be met from the support assets.

Support assets also fund the smoothing policy and can be used to meet the cost of any guarantees promised to policyholders.

Generally Scottish Friendly aims to ensure that these support assets are between 5% and 25% of the size of the with-profits fund.

How are business risks managed?

The With-Profits fund is exposed to a number of risks:

- new business: this may cost more than the immediate charges which will flow from each policy
- existing costs: should the cost of administering new business increase, the costs will be borne by with-profits policyholders
- other business ventures including Scottish Friendly’s business process outsourcing operations, partnerships, new product launches and mergers and consolidations with other friendly societies will impact the overall profitability of Scottish Friendly
- should the assets set aside for specific policyholders become unable to support their guaranteed benefits then the assets of the With-Profits fund may be used.

These risks are initially met from the support assets. After this, they may impact on the policy returns.

There are extensive controls in place to carefully manage these risks.

Any proposal to embark on a special business venture will be subject to the detailed scrutiny of the Board of Directors and require their approval.

Is there more than one With-Profits fund?

Scottish Friendly has a single With-Profits fund, however part of the fund has been set aside to provide benefits to customers who have certain types of policy.

This document covers the operation of the main part of the With-Profits fund in respect of those customers who have what is known as a unitised with-profits policy.

Separate documents outline the operation of the fund in respect of other types of with-profits policy and you should ensure that this guide relates to your policy.

Where can I get more detailed information?

You can find additional information about the way in which your individual policy will invest in the With-Profits fund in the Key Features or policy document.

This document is a summary of the more detailed Principles and Practices of Financial Management for Scottish Friendly's With-Profits fund. Copies of this document are available on request from Scottish Friendly or simply by downloading it from the Scottish Friendly website.

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Services Authority. Details can be found on
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