



# A CLOSER LOOK AT YOUR FUND

Annual Update for  
the Scottish Life Fund  
June 2017

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# WELCOME TO YOUR ANNUAL UPDATE

This update is to keep you informed of the investment performance of the **Scottish Life Fund** in the year ending 31 December 2016 and the benefits under your with profits plan.

We will refer to '**the Scottish Life Fund**' as 'the fund' throughout the rest of this update.

New solvency rules came into effect on 1 January 2016. These changes reduce the level of Estate distribution the fund can afford in the short term. This means that we have had to reduce payouts. We encourage you to read the details about why this is the case on page 7 of this booklet.

# INVESTMENT MIX

## What is the investment mix of the fund?

The fund is invested in a mixed portfolio of assets which includes Government and other bonds, company shares (both UK and overseas) and property. The aim of the investment strategy is to maximise the long term return on investments for with profits planholders whilst recognising the need for the fund to meet the guarantees provided to planholders.

Table 1 shows the current investment mix for traditional with profits plans and how we have changed the mix of the investments backing the asset shares of traditional with profits plans in the fund since 2012.

Prior to 2016 the asset mix for an individual plan varied according to its outstanding term and the level of guarantees. We mentioned last year that we were considering making changes to simplify this approach. Now, with interest rates at or close to historic lows we have moved away from varying the asset mix by outstanding term. The asset mix now depends on the type of plan you have. Those policies with higher levels of guarantees are invested more conservatively.

**Table 1 – Investment Mix**

	Company shares %	Property %	Government and other bonds %	Cash and other investments %
31.12.2016	13	2	80	5
31.12.2015	21	3	73	3
31.12.2014	25	2	70	3
31.12.2013	30	2	65	3
31.12.2012	22	2	74	2

By **asset share** we mean the accumulation of premiums paid into a with profits plan after taking off expenses and charges and allowing for the profits and losses earned by the investments backing the policies each year.

# INVESTMENT PERFORMANCE

## What was the average investment return of the with profits plans in the fund for 2016?

The fund's overall 2016 investment return, before tax and charges, was +6.2%.

Table 2 below shows the average investment return, before tax and charges, on the investments backing the asset shares of traditional with profits policies in the fund from 2012 to 2016.

**Table 2 – Investment Return**

	Investment return before tax charges %
2016	+6.2
2015	+1.8
2014	+6.3
2013	+4.2
2012	+6.6

Shares and property performed very well during 2016 which helped to boost the more modest positive investment returns from bonds and cash.

We don't know what investment returns will be in the future; you should not assume that they will be the same as they were in previous years. However, we believe that the current investment mix of the fund is appropriate in the current economic conditions.

# HOW DO I SHARE IN THE PROFITS AND LOSSES OF THE FUND?

Any profits or losses in the fund are shared out to the relevant planholders through a system of bonuses. There are two types of bonus that may be added to your plan:

- **annual bonuses**, which we may add during the lifetime of your plan and which increases the guaranteed amount payable when your plan matures or when the life assured dies, and
- **final bonuses**, which we may add on maturity or when a death claim is made. Final bonuses are not guaranteed and may go up or down.

The annual bonus rate for 2016 was 0.1% for traditional with profits plans.

There is more information on asset shares and how we decide annual and final bonus rates in the leaflet '**A guide to how we manage our with profits fund**'. We tell you how to get a copy at the end of this leaflet.

# DEMUTUALISATION ENHANCEMENT

To help with the technical language used in this section the key terms are highlighted and explained clearly at the bottom of this page.

## What is the demutualisation enhancement?

When Scottish Life demutualised and was acquired by Royal London in 2001 there was a commitment to distribute the **Estate** fairly over the expected lifetime of qualifying plans. The **demutualisation enhancement** was the process agreed to achieve that distribution.

The **demutualisation enhancement** was 0.75% for all years prior to 2008. From 2008 to 2011 the rates were 0.5%, 0.7%, 2.4% and 6.0%. However, from 2012 we changed our approach and stopped making enhancements to the asset shares themselves. Instead we aimed

to distribute the **Estate** by paying an additional amount over and above the asset share as a final bonus. To achieve this aim we used the **target payout**.

## Why did we change the approach?

The change of approach anticipated the introduction of the new Europe-wide regulations known as Solvency II, which all life and pension providers must follow. The new regulations came into force on 1 January 2016. Broadly the effect of the new regulations is that we need to hold more capital to protect against the risks within the fund. This reduces our ability to distribute the Estate.

The main risks within the fund are associated with guaranteed annuity options. These are provided in many of the pension policies held in the fund.

### **Estate**

The amount by which the investments of the fund are greater than the benefits already promised to planholders. You might also think of it as the fund's available capital.

### **Demutualisation Enhancement**

The process we previously used to distribute the estate to planholders. It involves increasing the investment returns applied to the asset shares over and above the returns actually achieved.

### **Target Payout**

We currently aim to pay more than asset share to distribute the estate. The proportion of the asset share that we aim to pay is called the target payout.

### **What is the target payout for 2017?**

For claims during 2017 the target payout is 106% of asset share, down from 112% in the middle of 2016. This follows the continued falls in interest rates associated with the Brexit vote. The low interest rates require us to hold more capital.

Holding more capital affects the extent to which we can distribute the Estate. This is why we've had to reduce the target payout for claims during 2017.

We are doing all we can to reduce the level of risk in the fund so we can increase the level of Estate distribution again. We have a proposal that we are going to test with our pension planholders with guaranteed annuity options in the coming months. However if the proposal is not successful, or if the position of the fund deteriorates further then we may have to reduce Estate distribution to zero.



# SUPERVISORY COMMITTEE

One of the ways in which planholders' interests are protected is through the Supervisory Committee which was set up to monitor the management of the fund, including the investment and bonus plan. It also monitors compliance with the terms of the Scheme – the detailed principles and arrangements that governed the transfer of Scottish Life's business to Royal London and the way the fund is then managed. The Committee has again not raised any concerns about the way the fund is being operated.

# COMMITTEE MEMBERS

## Supervisory Committee members

The Supervisory Committee has five members. A majority, including the Chairman, is required to be wholly independent of Royal London's Board and Management. In carrying out their duties, the members of the Committee are required to have regard solely to the interests and reasonable expectations of the planholders in the fund. The Chairman has a casting vote if necessary.

The current members of the Supervisory Committee are:

- **Adrian Eastwood (Chair)** – Former Chief Actuary for Scottish Widows and other Lloyds Banking Group life companies with extensive experience in the life insurance and pensions sectors
- **Michael Livingston** – Chairman of Maclay Murray & Spens LLP with considerable practice experience in the life insurance sector
- **Dick Barfield** – Former Chief Investment Manager at Standard Life with extensive experience in the life insurance and pensions sectors
- **Tim Harris** – Group Finance Director of Royal London
- **Rachel Elwell** – Investment Office and Staff Pension Director of Royal London



**Brian Murray**  
With Profits Actuary

# HOW CAN I FIND OUT MORE?

## More information about the fund

You can view and download the following documents from our website [royallondon.com](http://royallondon.com):

- **‘Principles and Practices of Financial Management (PPFM)’** which is a technical document that explains the way in which we manage the fund.
- **‘A guide to how we manage our with profits fund’** which is a plain English guide to the key points of the PPFM. The version that covers your plan is **‘Guide 5’**.
- **‘The Directors report on compliance’** which is the most recent report about how we have complied with the PPFM.

To find these documents please click on **‘Welcome to Royal London’** then **‘Corporate Governance’** then **‘PPFM’**. If you prefer, you can ask us to send you copies by calling us on **0345 05 02 020**.

If you need any more information or have any questions on the **Scottish Life Fund** or your with profits plan please call us on **0345 60 50 050** between 8.00am and 6.00pm Monday to Friday, except bank holidays or visit [royallondon.com/SLbonus](http://royallondon.com/SLbonus).

## PPFM Changes

We have made a change to the Practices to permit more freedom to invest in new asset types subject to following the standard approval process. There have been a few small updates to other PPFM Practices to update terminology.



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