

skandia's guide to investment in our unit-linked funds

how we price our unit-linked funds

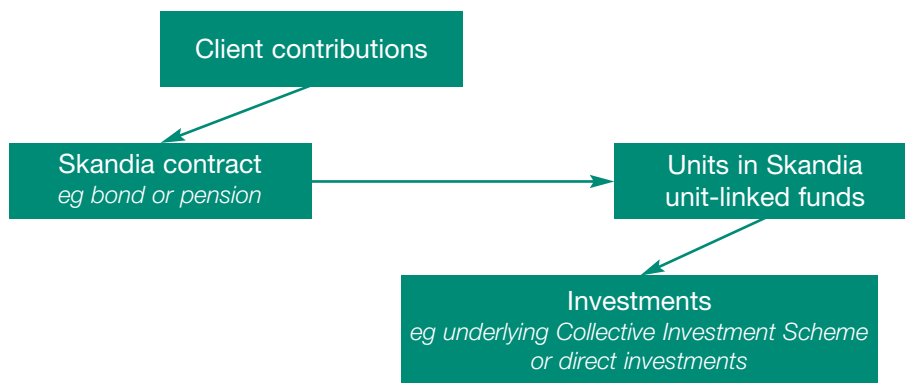
The aim of this guide is to explain how unit prices are calculated for the funds offered by Skandia Life Assurance Company Limited (SLAC) and our current approach to managing them.

A full list of SLAC funds can be found on the company's internet site or is available on request. The relevant Skandia policy or plan Terms and Conditions, issued when you purchased your contract from Skandia, should be regarded as the definitive source of information if there is any conflict between this document and the Terms and Conditions. Please note that this leaflet does not cater for the way the Guaranteed Pension Fund works or for any investments or products available through the Skandia Investments Solutions platform. Please refer to our separate literature or website www.skandia.co.uk for more information.

unit-linked funds

Unit-linked funds are offered by life assurance companies as a way of making a range of investment opportunities available to their customers within an insurance product, including pension contracts.

Skandia's unit-linked funds invest on behalf of clients in a wide range of underlying Collective Investment Schemes (CIS), such as Unit Trusts¹ or open-ended investment companies (OEICs)². Skandia clients purchase a product from Skandia where the performance is determined by the performance of the funds they select. They do not invest directly into the underlying CIS³ (see diagram below).



- 1 *Unit Trust* – private individuals pool their contributions with those of others, which combine to form a large fund that invests in a spread of different assets to minimise the risk of loss. Also known as collective/pooled investments or investment funds.
- 2 *OEIC* – open-ended investment companies. These are very similar to unit trusts, but are constituted as companies rather than trusts. The principal difference is that there is usually a single price.
- 3 Within the unit-linked fund range, there is a small assortment of funds that invest directly into stocks, shares and bonds. Details of these are available on request.

unit-linked funds *(continued)*

Each fund in our range is made up of units, the value of which is calculated by the process outlined below. Skandia calculates a series of prices for its unit-linked fund range, which are then applied to the relevant products, as set out in the Terms and Conditions.

Due to Skandia's scale and consequential buying power, reduced initial charges (preferential dealing terms) can be negotiated with CIS providers⁴. The outcome of any reduced charges is reflected within our unit-linked fund prices, benefiting our clients.

In addition, Skandia utilises its scale to negotiate reductions in the underlying CIS managers' Annual Management Charges⁵ (AMCs), some or all of which may be passed back into the Skandia funds by means of a rebate.

The price of units in a Skandia unit-linked fund will not mirror the price of the underlying CIS. Skandia unit-linked funds will commonly be launched at £1 per unit, irrespective of the price of the underlying CIS at that point.

Once launched, the Skandia unit-linked fund will perform broadly in line with the underlying CIS in which it invests. If the value of the underlying CIS rises or falls, so will the price of Skandia's unit-linked funds. The performances of Skandia's unit-linked funds do not correlate exactly to those of underlying CIS for a number of reasons:

- For non-pension funds, allowances for taxation are applicable – see [Taxation allowances](#) later in this guide for more detail.
- Skandia product or plan charges that are taken within the fund pricing.
- The effect of AMC rebates from the underlying CIS managers.

how skandia calculates unit-linked fund prices

This document covers our single manager and MultiManager unit-linked funds (the full list of SLAC funds can be found on the company's internet site or is available on request). The unit pricing process for each of these is described below.

Single manager unit-linked funds

We calculate Skandia single manager unit-linked fund prices each working day based on the following process:

- **Stage 1**
The manager of the underlying CIS calculates the purchase price for units in the fund at its valuation point⁶.
- **Stage 2**
Using the fund manager price, Skandia calculates the value of its holding in the underlying CIS.
- **Stage 3**
This value is then adjusted for any capital gains tax (CGT) applicable to our fund (only non-pension products). In addition we make an allowance for any dividends or rebates that are due to the fund.
- **Stage 4**
The sum of all these calculations gives us the 'internal fund value'.
- **Stage 5**
The internal fund value is divided by the number of units which have been allocated to all Skandia clients who have holdings in the fund to arrive at the price of individual units. Skandia's AMC⁷ is deducted at this stage if applicable (specific product Terms and Conditions will state if the Skandia AMC is taken within the fund pricing or by deducting units from the client policy).
- **Stage 6**
For 'single priced' SLAC unit-linked fund products (see product Terms and Conditions for more details) the price created in Stage 5 will be the quoted price, and price applied to all transactions in the unit-linked fund.

For 'initial priced' SLAC unit-linked fund products (see Terms and Conditions for more details), the price created in stage 5 is set as the bid price and will be increased by 5% to derive an offer price (see [Skandia fund prices](#) on next page).

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⁴ *CIS Provider* – the firm which offers the Collective Investment Scheme.

⁵ *AMC (Annual Management Charge)* – a charge made by a CIS provider which covers the cost of investment management and administration – this is reflected in the daily price of underlying CIS.

⁶ *Valuation Point* – The name given to the time of day that unit trusts or OEIC's are valued and then priced.

⁷ A product charge applied by Skandia. This may be deducted daily within the fund price by multiplying the current fund value by the AMC% rate and dividing by the number of days in the year, or by regular unit deduction from a client policy.

how skandia calculates unit-linked fund prices *(continued)*

Skandia fund prices

Unit-linked funds can have different prices for selling and buying units. These are known as the 'bid' (selling) and 'offer' (buying) prices. When clients first invest into an initial-priced Skandia product they will be allocated units using the *offer price* of the unit-linked fund and therefore pay the initial charge. Any subsequent valuation, switch, withdrawal or cancellation of units to pay for charges within that product will be carried out at the *bid price*. Thus, a client will only pay the initial charge once – when new money is invested in the product.

Single priced SLAC unit-linked funds only have one price, with product charges being taken via unit deductions.

Skandia MultiManager unit-linked funds

A Skandia MultiManager unit-linked fund is made up of a portfolio of Skandia single manager unit-linked funds. The proportion of each of these is determined in accordance with the objectives of each MultiManager fund.

We calculate Skandia MultiManager unit-linked fund unit prices each working day based on the following process:

- **Stage 1**
For each single manager unit-linked fund in the portfolio, a value is calculated based on the Skandia MultiManager unit-linked fund's holding, using the single manager unit-linked fund price calculated in stage 5 above. This is done BEFORE any Skandia AMC is deducted, to ensure no double charging occurs.
- **Stage 2**
The sum of all the portfolio holdings gives us the 'internal fund value.'
- **Stage 3**
The internal fund value is divided by the number of units which have been allocated to all Skandia clients who have holdings in the fund to arrive at the the price of individual units. The Skandia AMC is deducted at this stage if applicable. (Specific product Terms and Conditions will state if the Skandia AMC is taken by adjusting the unit price or by deducting units from the client policy.)
- **Stage 4**
For 'single priced' SLAC unit-linked fund products (see product Terms and Conditions for more details) the price created in stage 5 will be the quoted price and the price applied to all transactions in the unit-linked fund.

For 'initial-priced' SLAC unit-linked fund products (see Terms and Conditions for more details), the price created in stage 5 is set as the bid price and will be increased by 5% to derive an offer price.

Note: Rounding – the Skandia fund offer price is truncated to one decimal place and the bid price rounded up to one decimal place ensuring the bid/offer spread never exceeds the set level eg 5%. No rounding charge is levied in the price calculation.

factors involved in the pricing process

Fund basis

The price at which units in Skandia unit-linked funds are bought and sold may vary according to whether the unit-linked fund has an overall cash inflow or outflow at the time of the transaction.

Where a Skandia unit-linked fund has a positive cash flow – more money being invested into a fund than being taken out – the Skandia unit-linked fund will be valued using the price used to buy the underlying investments (as set out in the examples above). This is what is known as valuing on an 'expanding basis', and is the way Skandia normally values its unit-linked funds.

Where there is negative cash flow – more money leaving a fund than being invested – the Skandia unit-linked fund will be valued using the selling price of the underlying CIS. This is what is known as valuing on a 'contracting basis'.

The process of Skandia moving its unit-linked fund from an expanding to a contracting basis is called a 'basis move'. The principle behind these adjustments is to provide equal treatment for all clients in a unit-linked fund, those withdrawing money and those remaining. If this adjustment did not take place, it would result in the fund bearing the costs associated with the sale of the underlying CIS, which would be inequitable to the remaining policyholders.

continued

factors involved in the pricing process *(continued)*

Charges applicable to the unit-linked funds

The true cost of running a fund is represented by a percentage known as the 'Total Expense Ratio' (TER). TERs provide clients with a clearer picture of the total annual costs for running a CIS. It consists principally of the CIS Manager's AMC, as well as the additional fund running expenses, which include charges for administration costs associated with the running of the funds, depository and custodial charges, and audit, registration and compliance fees.

The effect of the CIS TER may be reduced by rebates received by Skandia from the underlying CIS provider. These rebates represent a return of some of the AMC deducted by the manager of the underlying CIS. These negotiated rebates are regularly applied to the fund, wholly or partly, as income at least once a month.

Taxation allowances

An allowance for taxation is made within the unit-linked fund price to reflect the tax Skandia expects to pay on investment returns in respect of that fund. This allowance for tax is only applicable to non-pension funds and is intended to be a fair provision for the tax Skandia will be required to pay on investment returns. Investment returns on unit-linked 'pension' funds are not usually subject to UK tax, so no allowance is made within the value of the fund's assets. The basis for this tax allowance is intended to provide fairness between different generations of policyholders and shareholders.

Gains and losses – investment growth will be charged at the prevailing tax rate set by Skandia and may include an allowance for inflation which can reduce the tax chargeable to the fund. Conversely, if there has been a reduction in the fund's value since the purchase price, the fund may receive a tax credit for losses or expected losses, which will have the effect of reducing the amount of tax allowed for in the fund price.

Price miscalculation

Skandia makes every effort to calculate prices accurately and has a rigorous validation process in place to minimise instances of error. Sometimes miscalculations can occur in the pricing of units, either in the valuation process of the underlying CIS manager or Skandia, or merely because of a timing delay.

In the event of an incorrect price being identified, through internal monitoring or notification by the CIS manager, Skandia will record the error and assess for significance and client impacts. Our aim is to correct the error(s) as soon as possible in line with pre-determined tolerances and to compensate clients accordingly in cases where an error has resulted in material loss. The considerations and principles we use in applying any such correction are in accordance with the Association of British Insurers (ABI) and FSA guidelines, our policy Terms and Conditions and our commitments to treating our customers fairly.

In cases where an error is discovered, an assessment will first be made to determine the scale of the error and the impact on policyholders involved. This assessment will include a detailed review of every price throughout the period to ensure all impacts are incorporated into the decision-making process. If the pricing error is deemed substantial enough to warrant a retrospective re-pricing of the Skandia unit-linked fund on a given day or period, policyholders who conducted a transaction during the revaluation date(s) will have their transactions reworked at the corrected price. We generally consider a significant loss to be an impact of 0.5% or more on the unit price on a specific day.

We aim to put client policies back into the position they would have been in had the pricing error not occurred, subject to *de minimis* limits, meaning that in cases where the effect on the client's policy is too small to warrant the administrative costs, we will not make an adjustment.

We will not routinely advise clients of these changes unless the correction of prices results in the removal of units exceeding £50. It should be noted that occurrences of this nature are infrequent; however, in such cases we will seek to advise the client via a formal letter, as soon as reasonably practicable.

In the case of former policyholders who are found to have been affected by such an error, we will seek to make ex gratia cash payments to those who have been disadvantaged by £10 or more. At our discretion, we may seek repayment from former policyholders who have been materially advantaged.

continued

factors involved in the pricing process *(continued)*

Fund launches, closures, mergers and objective changes

Skandia offers an exceptionally wide range of investment funds, designed to meet the needs of each investor. The fund range may vary as more are added to our platform to offer more choice and diversity. It may occasionally be necessary to close or merge funds for commercial or practical reasons, normally at the request of the CIS manager. We will advise you and your financial adviser as soon as reasonably practical before any such closure, to give you time to reconsider your needs.

Where a material change to a fund's objective has been made, Skandia will notify you in writing as soon as is practicably possible. This will also be the case where, for example, there is an increase in the CIS manager's AMC.

Significant events

Where circumstances prevent us calculating fair and accurate unit prices for a particular transaction, we may defer the transaction to a date we consider appropriate and equitable. For example, this may occur where a CIS provider has had to suspend dealings in a fund because of liquidity issues. When considering the action we will take, we will consider the circumstances, your interests and the interests of all our clients. In such circumstances, we reserve the right to defer any request for a switch or encashment by up to two weeks. If a fund holds real property directly or indirectly, we may exercise a longer deferral period (maximum 12 months) because the property on the fund may not be readily realisable.

The purpose of this guide is to set out the main criteria and standards by which these unit-linked funds are operated, with specific reference to the scope of Skandia's discretion relating to unit pricing. This document is intended to provide an explanation of Skandia's operational practice and does not form part of the product Terms and Conditions.

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Calls may be monitored and recorded for training purposes and to avoid misunderstandings.

Skandia Life Assurance Company Limited is registered in England & Wales under number 1363932. Registered Office at Skandia House, Portland Terrace, Southampton SO14 7EJ, United Kingdom. Authorised and regulated by the Financial Services Authority with FSA register number 110462. VAT number 386 1301 59.

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