An annuity is an insurance policy which usually converts the premium you have invested into an income which is paid throughout your life. Under a with-profits annuity, the amount of income you receive each year (called the total gross annual annuity) reflects the performance the with-profits fund has achieved and the bonus rate that you anticipated when you started the policy. The total gross annuity can be made up of three parts:

- the basic annuity guaranteed under the policy;
- the declared bonus annuity; and
- the final bonus annuity.

Basic annuity

We set the basic annuity guaranteed under the policy at the start of the contract. For most policies, this annuity reduces each year at a constant rate. This rate is the anticipated bonus rate you chose before the annuity started. We describe this reduction in the policy document. The higher the rate of anticipated bonus you choose, the higher the starting level of your basic annuity, but the higher the automatic reduction each year. Some policies have a basic annuity which starts:

- at a low level and so does not need to reduce at a constant rate; or
- at an even lower level and so needs to increase at a constant rate.

Declared bonus annuity

In past years, the board has added a declared bonus to with-profits policies. This adds to the basic annuity. This declared bonus is based on a number of factors including the performance of the with-profits fund. Once added, the declared bonus annuity is guaranteed, although it changes in line with the basic annuity each year, as described above.
Final bonus

The final bonus is another type of bonus that we can add to with-profits policies. It is not guaranteed, and we can reduce or remove it. The final bonus is the amount that we need to add to the basic annuity, and the declared bonus annuity, to arrive at the total gross annual annuity.

Total gross annual annuity

Currently, the total gross annual annuity is:

- the guaranteed benefits (basic annuity and declared bonus annuity described above); or
- the amount we work out using the interim rate of growth set by our board on the annuity value on the previous 31 December, for which an annuity value has been set;

whichever is higher.

When a bonus decision comes into force, it sets the annuity value on 31 December of the previous calendar year.

As with the declared bonus, we decide on the level of the total gross annual annuity (and so the final bonus) using a number of factors including how the with-profits fund has performed.

Effect of the anticipated bonus rate on total gross annual annuity

As we explained above, the total gross annual annuity is at least as great as the guaranteed benefits under the policy. If the guarantees did not apply, the total gross annuity in one year would be the total gross annuity from the previous year reduced by the anticipated bonus rate and increased by the bonus added.

This means that if we add an overall return of 3.5% a year, policies that came into force before 1 July 1996 with an anticipated bonus rate of more than 0% will tend to reduce each year. Similarly, policies that came into force after 30 June 1996 with an anticipated bonus rate of more than 3.5% a year will tend to reduce each year.
1. Can you give me an idea of how my income payment will be affected by the final bonus rates announced?

Unfortunately, we cannot give exact percentages of the levels of reduction in income before the change comes into force because:

- current bonus rates are not guaranteed in the future; and
- there is a wide range of policies available.

However, we have produced some examples in the table opposite which we hope will help you.

To use the table opposite you need to know the date your policy started (the start date) and also the anticipated bonus rate (ABR) you chose when you took your policy out. For convenience, your ABR is quoted in the letter enclosed with this leaflet.

Find your start date in the first column and then look for the ABR that is equal to or is closest to the ABR which applies to your policy. Then run along the row for the start date and down the column for the ABR. The percentage range is a guide to the approximate reduction to your gross income which will apply from the first policy anniversary after 1 February 2004.

For example, Mr Smith began his policy on 15 April 1997 with an ABR of 4.5% (please see the sheded box). His current annual gross annuity is £4800, which means he receives a gross income of £100 on the first of each month. On 1 May 2004, the first payment date after the next policy anniversary, we will reduce his income by between 4% and 10%. This would mean his new monthly gross income would be between £364 (£480 less 4%) and £380 (£480 less 10%).

<table>
<thead>
<tr>
<th>Start date of the policy</th>
<th>Anticipated bonus rate (ABR)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2.5%</td>
</tr>
<tr>
<td>1 January 1997 to 31 December 1997</td>
<td>8% to 14%</td>
</tr>
<tr>
<td>1 January 1993 to 30 June 1996</td>
<td>2% to 10%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Anticipated bonus rate (ABR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.5%</td>
</tr>
<tr>
<td>1 July 1998 to 31 December 1997</td>
</tr>
<tr>
<td>1 January 2000 to 31 December 2000</td>
</tr>
</tbody>
</table>

Notes:
1. The anticipated bonus rate is the rate you chose before the annuity started. The figure is given in the letter enclosed with this leaflet.
2. We will always pay, at least, the guaranteed benefits under the policy (the basic and declared bonus annuity).
3. The reductions shown are not the largest or smallest which could arise as the range depends on future bonus rates.
4. N/A stands for 'not applicable' or 'does not apply'.
Your questions and answers (continued)

2 When will the reductions first affect me?
The major reduction we announced in November 2002 will apply from the first income payment we make after the first anniversary of your policy after 1 February 2003. Depending on the date of your policy anniversary, this may not have happened yet. The second reduction we announced in January 2004 will apply from the first income payment we make after the first anniversary of your policy after 1 February 2004. We will write to you (as we do every year) just before we make the first payment at the new level.

3 I have already suffered bonus reductions. You have greatly reduced your investments in stocks and shares so why should I suffer any further reductions?

There were very substantial falls in stock markets when we held a significant investment in shares. We had hoped to phase in the effect on you over the length of your policy. However, it became impossible for us to phase in the effect on you over as long a period as we had hoped. The special reduction that will apply on the first anniversary of your policy after 1 February 2004 will complete the process of bringing bonuses under with-profits annuities back into line with other with-profits policies.

After these special reductions come into force, your income will continue to vary. This reflects the difference between the anticipated bonus rate you chose and the bonus rate that we apply from time to time.

4 You said that following the compromise scheme, the fund was £1 billion stronger and the uncertainties had reduced. What’s changed?
The compromise scheme we put in place in February 2002 did greatly improve our financial position at the time. But, now, we have less money available because of the fall in investment markets (which, occurred during 2002) and increases in the amounts we have to set aside for potential claims for compensation.

5 Why are you only making such large reductions to with-profits annuity policies?

Until February 2003, we had largely protected you from the immediate effect of losses in the with-profits fund which are a result of investment-market conditions and our financial position. The changes we have announced will bring your situation into line with the position of our other policyholders.

6 I want to transfer my pension elsewhere. How do I go about it?

Unfortunately, it is not possible to transfer with-profits annuities.