# How Pegging & Substitution Can Benefit You

Guardian's current practice is to pay a dividend that is higher than the "formula" dividend amount when certain conditions apply.[1] The practice is called "Substitution" if it applies to the dividend paid on the second and third policy anniversaries and "Pegging" if it applies thereafter.

## Background

- Guardian uses Substitution and Pegging to add an extra degree of stability to policies.
- Substitution and Pegging apply only to the base policy's non-loaned dividend and not to dividends on Paid-Up Additions.
- Substitution and Pegging apply only during the premium-paying period of the policy (e.g., before year 21 for a 20 Pay Whole Life policy).
- This practice is not guaranteed. Like the dividends themselves, the use of Substitution and Pegging are subject to annual approval by Guardian's Board of Directors.

## Substitution

In a declining dividend scale environment, Substitution improves policy performance in the early policy years. For example, for policies illustrated and effective in 2016, the base policy non-loaned dividend that will be paid in 2018 and 2019 will not be less than the base policy dividend amount illustrated on the policy date. This applies to all policies except Single Premium Whole Life.

## Pegging[2]

Pegging allows for a smoother transition from year to year in a declining dividend scale environment. Pegging does not guarantee that the dividend will increase from year to year, but its use does "soften" the decline in the dividend that would otherwise occur if only the dividend formula were used.

## What this means for a policy owner

Guardian calculates its total whole life dividend using the following three components:

- Investment performance;
- Mortality; and
- Expenses.

Since mortality and expenses tend to remain relatively stable, investment performance has been responsible for the majority of dividend fluctuations over the last few years.

Investment performance tends to track broad movements in market interest rates because the majority of Guardian's portfolio is invested in high-quality, fixed-income instruments. While the use of Pegging and Substitution isn't guaranteed, Guardian has used these practices for many years to mitigate any decreases that might occur in a declining dividend scale environment.

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## Example Using Pegging and Substitution:

A Life Paid Up at Age 99[3] contract was issued with a policy date in September 2014. The 2014 dividend interest rate (DIR) was 6.25%.

The 2015 DIR was **6.05%** and this example assumes that going forward, the DIR will be below 6.25%.

### What Dividend Interest Rate Would Guardian Use?

- **September 2015:** No First-Year Dividend on Base Contract
- **September 2016:** 6.25% Base Policy Dividend (Using Substitution)
- **September 2017:** 6.25% Base Policy Dividend (Using Substitution)
- **September 2018:** 2018 Scale Base Policy Dividend (with Pegging, if applicable)

## Contact your local Guardian representative today to learn more about Guardian's many advantages.

[1] Dividends are not guaranteed. They are declared annually by Guardian's Board of Directors.

[2] Beginning with the base policy non-loaned dividend paid on the fourth policy anniversary.

[3] Policy form number L99 (14-L99).

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