



**PRINCIPLES AND PRACTICES OF
FINANCIAL MANAGEMENT**

ROYAL LIVER SUB-FUND

**REPORT TO WITH PROFITS
POLICYHOLDERS**

ON COMPLIANCE FOR 2018

JUNE 2019

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1. INTRODUCTION

On 1 July 2011 all of the with profits business of Royal Liver Assurance ('RLA') was transferred to The Royal London Mutual Insurance Society Limited ('Royal London'). The Royal Liver Sub-fund ('the fund') became a sub-fund in Royal London and the Principles and Practices of Financial Management ('PPFM') for the fund was published. The most recent version was published in February 2019.

The Directors must provide a report each year to with profits policyholders giving information on compliance with the PPFM. The Directors have reviewed the operation of the fund for 2018 and in their opinion the PPFM has been complied with in all material respects. It is also their opinion that the exercise of discretion over the period was appropriate and that any issues involving competing or conflicting rights, interests and expectations of policyholders were resolved fairly.

In coming to this view the Directors have taken account of internal and external professional advice provided during the year, including advice from the With Profits Actuary, the With Profits Committee and the Chief Actuary. This report sets out the main reasons for the Directors' opinion and the following sections consider, in turn, governance, the exercise of discretion, competing and conflicting interests, and compliance with the PPFM.

2. GOVERNANCE

Appropriate governance arrangements to monitor compliance with the PPFM have operated throughout the period in question.

The Directors seek opinions as appropriate from the With Profits Actuary, from the Chief Actuary and from the With Profits Committee which was established by the Directors to provide independent advice on the way the fund is managed, to provide an independent view when the Directors are considering the interests of with profits policyholders and to monitor compliance with the PPFM.

The Supervisory Committee which monitors that the fund is managed in accordance with the Instrument of Transfer was in operation during the period. The Committee was content that all aspects of the Instrument of Transfer had been complied with, with one exception. The Service Standards, codified as times to answer telephone calls and respond to correspondence, applied to the Liver business were those consistent with other lines of Royal London business. The Instrument of Transfer sets out more aggressive Service Standards and these were not met in a small number of cases. There was no material customer detriment as a result. The Royal Liver Supervisory Committee has agreed that the Liver Service Standards should be relaxed, and the Royal London standards should be complied with from 2019.

The With Profits Actuary confirmed his view in the attached report to policyholders.

3. EXERCISE OF DISCRETION

The main areas in which discretion is exercised in the operation of with profits business are setting bonus rates, investment strategy, setting surrender values, allocation of expenses, the management of the estate and the treatment of contingent reversionary bonus policies.

SETTING BONUS RATES

For conventional contracts, a process was carried out in line with the PPFM, to set annual and final bonus rates for 2018. New final bonus rates were implemented on 1 January 2018 and 1 July 2018. The rates implemented in January 2018 were first approved on an interim basis, and declared formally at the end of March 2018.

The inherited estate was above the upper capital threshold, so the excess capital was eliminated through an 8.5% asset share enhancement. Therefore, new final bonus rates were declared in July 2018 to allow for the enhancement made to asset shares. These rates were formally signed in August 2018.

For unitised contracts, annual bonus rates were reviewed at the end of 2017 with an implementation date of 1 January 2018. Monthly reviews of final bonus and market value reduction (MVR) rates were carried out throughout 2018. The only change made was in July 2018 due to the 8.5% asset share enhancement.

In making these declarations the Directors took account of advice from the With Profits Actuary, the Chief Actuary and followed the requirements of the PPFM. The Directors also took account of advice from the With Profits Committee.

INVESTMENT STRATEGY

The aim of the investment strategy remains to maximise the long term return on investments for with profits policyholders whilst recognising the need for the fund to meet its guaranteed liabilities and commitments to policyholders and maintaining the estate at an appropriate size.

A common statistic used to categorise the level of investment risk within a fund is the proportion of the fund's assets that are invested in equity, property and alternative assets. This proportion was 45% at the end of 2018.

SETTING OF SURRENDER VALUES

No changes were made to the formulae underlying surrender values during 2018.

ALLOCATION OF EXPENSES

Over the course of 2018 the expenses allocated to with profits policies were maintained in line with the original transfer agreement between Royal London and RLA. Throughout 2018 the allocation of expenses to policies has been in line with the PPFM.

MANAGEMENT OF THE ESTATE

There were no material changes to the methods of monitoring and managing the estate during 2018 as they continue to operate effectively.

Since 2009 a charge to cover the cost of providing guarantees has been applied to asset shares on some types of with profits policy. No changes were made to the guarantee charges in 2018.

CONTINGENT REVERSIONARY BONUS POLICIES

Under the PPFM a final bonus will only be applied to these policies if a discretionary allocation from the estate is made. A special distribution of surplus was made on 1 July 2013 and bonus additions of 10.5% were made to claims on these policies after this date. On 1 July 2018 an additional 8.5% special distribution of surplus was made.

MANAGEMENT OF RISK

Royal London continuously seek to obtain independent assurance that our systems of risk management and internal control are operating effectively. In addition, we obtain independent opinions on the effectiveness of the key systems and controls throughout the organisation. This includes evaluating the effectiveness of, and the adequacy of, the risk management processes and ensuring compliance with policies and procedure. The effectiveness of internal control and the risk management infrastructure is also specifically considered by our external auditors in the context of their review of our financial statements.

We have previously developed a number of actions to mitigate the business risks that are run within the fund including exposures to investment, expense, mortality, morbidity and lapse risks.

CHANGES TO PPFM

The latest version of the PPFM in force during 2018 was published in December 2016. The PPFM was subsequently updated in February 2019 to reflect changes Royal London made as a response to Brexit

4. COMPETING OR CONFLICTING RIGHTS, INTERESTS AND EXPECTATIONS

In any with profits fund, different groups of policyholders could have competing or conflicting interests. For example, holders of

- policies of different types (such as life or pension policies or regular or single premium)
- policies of different sizes or different policy terms
- policies which started in different years or mature in different years

or policyholders

- of different ages
- claiming for different reasons (for example maturity, death, surrender)
- exercising different policy options

could receive different benefits relative to each other depending on how discretion is exercised.

Any conflicts which have arisen have been appropriately and fairly resolved, in the Directors' opinion, after taking expert advice, where necessary. This expert advice has been provided by the With Profits Actuary, the Chief Actuary and the With Profits Committee as appropriate.

5. COMPLIANCE WITH PPFM

MANAGEMENT OF THE ESTATE

During 2018, the Directors were provided with information and actuarial reports on a regular basis regarding the current and projected financial position of the fund.

In particular the Directors considered information on the financial strength of the fund as at the end of 2017. At this point the estate was above the upper capital threshold. The surplus was distributed to policyholders through an asset share uplift of 8.5% to with profits policies and an 8.5% contingent bonus to contingent reversionary bonus policies.

For policies originally sold by Friends Provident (London & Manchester), the Directors agreed for payouts to be targeted at 105% of the asset share throughout 2018 in order to distribute the ring-fenced smoothing account in line with the Instrument of Transfer.

INVESTMENT STRATEGY

During 2018 the Capital Management Committee met 15 times. Technical papers on investment strategy were presented during the year and advice from the With Profits Actuary and the Chief Actuary was obtained where appropriate.

The performance of the investment manager was monitored by the Investment Strategy Committee, the Investment Committee and the Directors. Changes to benchmarks were approved by the Directors.

POLICY BENEFITS PAYABLE

The methodology used to set bonuses and policy benefits followed the approach set out in the PPFM and complied with the Instrument of Transfer. The bonus rates declared differed between product types and classes.

An exercise to review compliance with the target ranges for maturity and surrender payouts published in the PPFM was carried out. This demonstrated that 93% of policies were within target range during 2018, satisfying requirements for compliance. Of the 7% of policies that were outside the target range 2% were below and 5% were above. 5,922 claims were included in this analysis.

6. CONCLUSION

In the opinion of the Directors, the management of the with profits business in the fund over this period has complied with the PPFM in all material respects. It is also their opinion that the exercise of discretion over the period was appropriate and that any issues involving competing or conflicting rights, interests and expectations of policyholders were resolved fairly.

P LONEY

GROUP CHIEF EXECUTIVE

June 2019

REPORT FROM THE WITH PROFITS ACTUARY

To with profits policyholders in the Royal Liver Sub-fund

In my opinion the discretion exercised by the Directors in respect of the period covered by their report has taken policyholders' interests into account in a reasonable and proportionate manner. It is also my opinion that the Directors have complied with the requirements of the Principles and Practices of Financial Management (PPFM) of the Royal Liver Sub-fund in all material respects.

I have based these opinions on the information and explanations provided to me by the Directors and management of Royal London and on my own knowledge and investigations. In doing so I have taken into account the relevant rules and guidance of the Financial Conduct Authority, of the Prudential Regulation Authority, of the Financial Reporting Council and of the Actuarial Profession regarding the management of with profits business.

Separate reports confirm compliance in respect of the Royal London Long Term Fund (excluding the Closed Funds), in respect of the Scottish Life Closed Fund , in respect of the PLAL With-Profits Sub-fund and in respect of the Royal London (CIS) Sub-fund

Brian Murray BSc FFA

With Profits Actuary

June 2019