



**PRINCIPLES AND PRACTICES OF  
FINANCIAL MANAGEMENT  
FOR WITH PROFITS BUSINESS**

**ROYAL LONDON (CIS) SUB-FUND**

**REPORT TO WITH PROFITS  
POLICYHOLDERS  
ON COMPLIANCE FOR 2018**

**JUNE 2019**

## **CONTENTS**

1.	INTRODUCTION.....	3
2.	GOVERNANCE.....	3
3.	EXERCISE OF DISCRETION.....	4
4.	COMPETING OR CONFLICTING RIGHTS, INTERESTS AND EXPECTATIONS...	6
5.	COMPLIANCE WITH PPFM.....	6
6.	CONCLUSION .....	7
	REPORT FROM THE WITH PROFITS ACTUARY.....	8

## **1. INTRODUCTION**

On 31 July 2013 The Royal London Mutual Insurance Society Limited ('Royal London') completed the acquisition of The Co-operative Insurance Society Limited ('CIS'). CIS was originally held as a direct subsidiary of Royal London, and renamed Royal London (CIS) Limited ('RLCIS'). On 30 December 2014, the life insurance business of RLCIS was transferred to Royal London. The transfer was structured in such a way that the business of RLCIS was placed into a newly created sub-fund within the Royal London Long Term Fund, the Royal London (CIS) Sub-Fund ('the fund'), and this was closed to new business at the same time.

On 30 December 2014 Royal London published three Principles and Practices of Financial Management ('PPFM') documents covering the fund as follows:

- a PPFM for the RLCIS OB & IB Fund
- a PPFM for the RLCIS With-Profits Stakeholder Fund
- a PPFM for the RLCIS With-Profits Pension Fund

The most recent versions of the PPFMs were published in December 2017.

The Directors must provide a report each year to with profits policyholders giving information on compliance with the PPFMs. The Directors have reviewed the operation of the fund for 2018 and in their opinion the PPFMs have 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 issues, and compliance with the PPFM.

## **2. GOVERNANCE**

Appropriate governance arrangements to monitor compliance with the PPFMs 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 PPFMs.

A short report to policyholders from the With Profits Actuary confirming his view is attached.

### **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, setting smoothed unit prices, allocation of expenses and the management of the estate.

#### *SETTING BONUS RATES*

For all accumulating and traditional with profits contracts, we carried out a process, in line with the PPFM, to set annual and final bonus rates. These were implemented on 1 April 2018.

We have made some minor changes to final bonus setting methodology for AVC pensions to reflect a decreasing number of maturities and changing business mix:

- Previously we used aggregate policy data to set bonus rates but we have switched to using specimen policies to reduce volatility.
- We usually base the bonus scales for AVC policies on both single and regular premium business. For a subset of policies (Series A), we have based rates on regular premium policies only as they represent 97% of the total value in force.

Pay-outs were monitored throughout 2018, and no additional changes to bonus rates were required.

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 or close to the target size.

A common statistic used to categorise the level of investment risk is the proportion of the assets that are invested in equity and property. The overall proportion backing the different categories of with profits business at the end of 2018 is set out below:

RLCIS OB & IB Fund	AWP business	58%
	TWP business excl. Table P	42%
	TWP Table P business	23%
RLCIS With-Profits Pension Fund	All WP business	52%
RLCIS With-Profits Stakeholder Fund	All WP business	59%

These proportions remain broadly similar to those at the end of 2017.

*Different asset mixes continue to be attributed to different business lines, reflecting the nature of the guarantees provided for each contract.*

### *SETTING OF SURRENDER VALUES*

The regular reviews of market value reduction (MVR) factors were carried out over the course of 2018 although no changes were required to these factors over the year.

### *SETTING OF SMOOTHED UNIT PRICES*

Policies in the With-Profits Pension Fund and With-Profits Stakeholder Fund have their benefits calculated using smoothed unit prices. The methods used to smooth the prices were not changed during 2018. However, we have updated the parameters to ensure they are consistent with current market conditions.

Checks were performed regularly to ensure the smoothing reserves remained below the 12% trigger specified in the PPFM.

### *ALLOCATION OF EXPENSES*

Over the course of 2018 the expenses allocated to with profits policies were maintained in line with those set out by the Part VII Transfer. Throughout 2018 the allocation of expenses to policies has been in line with the PPFMs.

Charges for policies covered by the RLCIS With-Profits Stakeholder Fund PPFM were no more than the maximum permitted under the Stakeholder regulations.

### *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.

### *MANAGEMENT OF RISK*

Royal London continuously seeks to obtain independent assurance that its systems of risk management and internal controls 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 and adequacy of the risk management processes and ensuring compliance with policies and procedure. The effectiveness of internal controls and the risk management infrastructure is also specifically considered by our external auditors in the context of their review of our financial statements.

There are 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*

Updated versions of the PPFMs were published on 31 December 2017. No changes were made to the Principles and Practices for the RLCIS fund during 2018.

## **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 relevant With Profits Actuary, the Chief Actuary and the relevant 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 2018, the Directors continued to distribute the estate in order to meet the aims set out in the PPFM. This was achieved by targeting pay-outs at 106% of the smoothed asset share for 2018.

### *INVESTMENT STRATEGY*

During 2018 the Investment Strategy Committee met 15 times. Technical papers on investment strategy were presented during the year and advice from the relevant 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 PPFMs. 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 96% of policies were within target range during 2018 as detailed below, satisfying requirements for compliance.

	No. of claims	Proportion of claims		
		Below Target Range	Within Target Range	Above Target Range
TWP Maturities & Surrenders	25,122	2%	96%	2%
AWP Surrenders	1,999	1%	90%	9%

## **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 PPFMs 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 the With Profits Policyholders of the Royal London (CIS) 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 (PPFMs) of the Royal London (CIS) 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 Royal Liver Sub-fund and in respect of the PLAL With Profits Sub-fund.

**Brian Murray BSc FFA**

**With Profits Actuary**

**June 2019**