A Guide to Personal Pension Policies (including Free-Standing Additional Voluntary Contribution Policies and those formerly contracted-out of the State Earnings Related Pension Scheme)

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1. Introduction

On 31 July 2013 Royal London completed the acquisition of Co-operative Insurance Society Limited from Co-operative Banking Group Limited. Following the acquisition Co-operative Insurance Society Limited was renamed Royal London (CIS) Limited.

On 30 December 2014 the policies of Royal London (CIS) Limited were transferred into a separate sub-fund of the Royal London Long Term Fund called the Royal London (CIS) Sub-Fund. At the same time, the Royal London (CIS) Sub-Fund was closed to new policies.

The Royal London Long Term Fund consists of the Royal London Main Fund, which is open to new business, and sub-funds which are all closed to new policies.

We will manage the Royal London (CIS) Sub-Fund in accordance with the Transfer Scheme; this is one of the legal documents that transferred the business of Royal London (CIS) Limited to Royal London. The Transfer Scheme states that Royal London will manage the Royal London (CIS) Sub-Fund as if it was a stand-alone fund, operating within the constraints of its own capital.

The Royal London (CIS) Sub-Fund itself consists of three funds:

- the RLCIS OB & IB Fund;
- the RLCIS With-Profits Stakeholder Fund; and
- the RLCIS With-Profits Pension Fund.

This guide covers with-profits personal pension policies (including Free-Standing Additional Voluntary Contribution policies and those policies formerly contracted-out of the State Earnings Related Pension Scheme) in the RLCIS OB & IB Fund.

In this guide we call the RLCIS OB & IB Fund, 'the fund'.

2. What is this guide for?

This guide tells you how we manage the fund.

It should answer most of the questions you might have. If you have any further questions then please contact us – our details are shown at the end of this guide.

The guide explains the main aspects of how we currently manage the fund for customers who have a with-profits personal pension policy. It covers the key points from the detailed technical guide called the Principles and Practices of Financial Management (PPFM) document, but is not a replacement for it. Please see the PPFM for a fuller description of how we manage the fund. If this guide is inconsistent with the PPFM, the PPFM overrides this guide.

You can download all of our guides, including the PPFM documents, from our website, **www.royallondon.com** or you can contact us for a copy.

If we make a significant change to our approach to managing the fund in the future, we'll write to tell you.

3. What is a with-profits policy?

A with-profits policy is a type of insurance policy that lets you share in the profits and losses of the fund's long-term insurance business, which includes life assurance and pensions business.

Your money, together with other policyholders' money, is invested in the fund. By investing in a range of assets (types of investment), we aim to make profits for the fund which we will then share with with-profits policyholders by adding bonuses to their policies. The fund also has policies which do not share in the profits or losses of the fund, known as non-profit policies.

Your with-profits policy benefits from a special feature known as smoothing. Smoothing is designed to protect with-profits policyholders from the direct impact of some of the sudden movements in the stock market, but it cannot get rid of the strong link between the underlying market investment returns, and with-profits returns.

For policies such as yours, in deciding what the bonuses should be, we smooth (or average) the investment profits or losses over a number of years. This means that we hold back some of the profit made when investment returns are good, so that we can increase returns if investment returns are lower. We do this so that your investment should provide a steadier return from day to day than if you invest in a fund which fully reflects the rise and fall in stock markets, such as a unit trust.

Smoothing does not protect against prolonged falls in the stock market, because the profits held back from periods of good returns may not provide sufficient protection against investment losses. Also, unlike simpler stock market investments, your policy contains some guarantees about the amount of money available to provide retirement benefits on the retirement date you originally selected for your policy. So, for example, if the stock market falls heavily before this retirement date, your fund at retirement will be at least the guaranteed amount at that time.

4. What are the guarantees?

Your policy benefits from valuable guarantees.

- We guarantee to provide a cash sum, plus all annual bonuses we may have added. We'll do this at the retirement date you originally selected for your policy provided you've paid all your premiums on time. Currently personal pension policyholders are able to take up to 25% of their retirement benefits as a tax-free lump sum, with the remainder of their benefits being used to purchase a pension, which is taxable. However, in the future you may be able to take a larger proportion of your benefits in the form of a lump sum, although it is likely that no more than 25% of your retirement benefits will be able to be taken as a tax-free lump sum, with any residual lump sum being subject to tax. The types of benefit available to you and the tax position of the benefits are subject to change by the Government. As you approach the retirement age that you have selected for your policy, we will inform you of the retirement options available to you.

- For some policies, we also guarantee to pay on the retirement date originally selected on the policy a minimum rate at which part or all of the fund at retirement is converted into a pension (known as a guaranteed annuity rate). Such guarantees apply only to policies, and increases to premiums for existing policies, where the application form for the policy or premium increase was signed before 1 March 1999. A guaranteed annuity rate means that we will pay at least a minimum pension amount each year for every £1,000 of fund at retirement.

5. What are the investments in the fund?

The fund is invested in a wide range of carefully selected assets with the aim of achieving growth. A wide range of assets is held to help reduce the risk to the value of the fund that would arise if most or all of the assets were invested in a single category of assets.

Investments include:

- UK and overseas shares
- government bonds (loans to the government)
- company bonds (loans to companies)
- property (which may also include our business premises)
- subsidiary companies owned by the fund
- cash deposits
- more complex types of assets that are used to help reduce investment risk such as derivatives.

Our Responsible Shareholding programme is an important part of how we manage the investments in the fund.

We aim to influence the companies in which the fund invests on a range of social, ethical and environmental issues. This means that we will engage with companies on a broad and challenging ethical agenda, reflecting the issues that our customers would expect the businesses in which we invest to address. We consider such influence to be for the benefit of the companies in which the fund invests and therefore for the benefit of the fund itself.

In the 1980s and 1990s, when stock market investment returns were relatively high, a high proportion of the assets of the fund was invested in shares and property with the aim of achieving above average investment returns. Although shares and property investments are riskier than other types of investments such as bonds and cash deposits, over the longer term they tend to produce higher investment returns (although this is not guaranteed).

As a result of the generally much lower investment performance of the world stock markets since the year 2000 and following a general decline in interest rates, a lower proportion of shares and property assets has been held in the fund in recent years. Also, since 2004 the assets of the fund have been allocated in different ways to different groups of policies. We do this to take account of a number of factors such as the value and nature of policy guarantees.

As a result, different groups of policies might be invested in a different mix of assets.

For policies such as yours, we currently aim to hold between 40% and 60% of the assets obtained by investing your premiums in shares and property, with investments in property normally representing no more than 40% of the total invested in shares and property. We hold the rest of the assets in less risky assets such as bonds, cash deposits and suitable derivatives.

The current mix of assets held for your type of policy is usually shown with your statement and is also available on request.

6. What affects the bonuses that may be added to my policy?

The bonuses are affected by the level of policy guarantees, the charges that we make, how we smooth payouts and any distributions from the fund's working capital. (See section 10.)

The bonuses added to your policy represent your share of the profits and losses of the fund.

The main factor that affects the level of bonuses that we may add to different groups of with-profits policies is the investment profits or losses of the assets held in respect of those policies.

Other important factors are:

- the charges we make
- the effect of the guarantees we offer to you and to other policyholders.

Other factors, such as the profits (or losses) that result from other types of business in the fund and any difference between the amount we have paid to investors moving out of the fund and the fair share (see section 8) of the total fund value for those plans at the time, may also give rise to profits or losses within the fund. (See section 9.)

The charges which we make allow for, amongst other things:

- our costs of acquiring and administering policies
- tax
- the costs of helping to meet policy guarantees.

Before 1 August 2013 the costs of acquiring and administering policies arose from the direct management of the fund. Since 1 August 2013 such costs have been based on fees and charges levied by the Royal London Main Fund as part of the terms of Royal London's purchase of CIS.

We are currently charging policies such as yours an amount to help meet the cost of the policy guarantees provided. This charge is allowed for when we set bonuses by reducing the investment return achieved on the assets backing policies such as yours by 0.5% each year. We regularly monitor the effect of this charge and we may vary it in the future, for example, to reflect changes in the level of working capital. (See section 10.)

We deduct a small policy fee when we set the guaranteed cash sum for your policy. The level of policy fee depends on how often you pay premiums and when you started your policy. A one-off policy fee of £26.50 is charged to annuity contracts. We may vary the level of policy fees in the future.

We use all the profits of the life assurance and pensions business in the fund for the benefit of the fund's life assurance and pensions policyholders only. This includes adding to reserves to strengthen the fund for its life assurance and pensions policyholders.

Similarly, any losses incurred within the fund are met by the policyholders, either through a reduction in the working capital (see section 10) of the fund or through a reduction in their benefits.

7. What types of bonuses may be added to my policy?

There are generally three types of bonuses:

- **Annual bonuses,** which we may add to policies each year and which increase the guaranteed minimum amount that we will pay out
- **Interim bonuses,** which we may add when a claim is made, to cover the period since any annual bonuses were previously added and
- **Final bonuses,** which we may add when a claim is made**.**

Unless any special conditions apply as described in documents provided to you, the cash sum available to provide retirement benefits on the retirement date you originally selected for your policy is the guaranteed cash sum plus any annual bonuses already added to the policy, plus any interim and final bonuses.

8. How do we decide what the bonuses should be?

Bonuses are set so that payouts represent a fair share of the fund, allowing for smoothing. In setting annual bonuses, we also aim to ensure that the fund is large enough to cover all our liabilities to policyholders at any time and has enough working capital. (See section 10.)

Annual and interim bonuses

We set annual bonuses on 1 April each year. These bonuses pay out part of the profits of the fund, increasing a policy's guaranteed benefits.

We set annual bonus rates with the aim of holding back part of the policy's share of the profits of the fund to be paid as final bonus. When we set annual bonuses, we take account of factors such as our long-term view of future investment conditions, the level of guarantees applying to policies and the level of working capital in the fund. Annual bonuses increase the level of guarantees applying to policies such as yours.

Current investment returns remain much lower than those earned during the 1980s and 1990s and, with the current and expected future low rates of inflation, they are expected to remain lower in the future.

Therefore, we are not currently adding any further annual bonuses to the valuable guaranteed benefits that already apply to your policy.

Interim bonuses are usually set at the same time and at the same rates as annual bonuses.

However, interim bonus rates could be changed more frequently than annual bonus rates, or set at rates that are different from the rates of annual bonus. As with annual bonuses, we are not currently adding interim bonuses to policies such as yours.

Final bonuses

These represent a fair share of the profits and losses arising over the lifetime of policies which we haven't already distributed as annual or interim bonuses. In setting final bonuses, we also aim to ensure that the fund is large enough to cover all our liabilities to policyholders at any time and has enough working capital.

We normally set final bonuses on 1 April each year, but we also review final bonus rates at least once more during the year, and may change them if necessary.

There are a number of different factors that contribute to the fund's profits and losses and we have to decide how to share these profits or losses when we set the bonuses. We do this by calculating a 'fair share' of the assets of the fund for typical policies and using the results to fix a scale of final bonuses to apply to all similar policies.

The fair share depends on the profits earned by policies such as yours over the period of the investment. In calculating the fair share, we smooth the investment return earned by averaging the annual return over a period of years.

We also look at the total fair share for different groups of investors and use the results to decide the level of bonuses we pay to each group.

We aim to set final bonuses so that, in total, payouts on retirement are equal to their fair share of the fund. Some final bonuses might be zero, for example when the guaranteed benefits are greater than the fair share.

We may smooth final bonus rates further.

We may smooth final bonus rates further by limiting the amount by which payouts for similar policies change from one year to the next. For policies such as yours, we normally make sure that retirement fund values for similar policies of the same original term don't change by more than 20% over a year. The way that smoothing works means that in any one year the amount paid out for each group of policies may be more, or less, than the amount that would be paid if there were no smoothing.

Over the longer term we aim to make the average smoothed payout equal to the average payout without smoothing, and for policies such as yours we normally expect that the majority of smoothed payouts would be within 20% of the unsmoothed amounts for each group of policies.

9. What are the risks associated with investing in the fund?

The fund is exposed to a number of risks, for example:

- how well our investments might do
- how much our costs might be
- the cost of meeting guarantees that apply to most of the fund's with-profits policies (such as basic sums assured and basic annuities together with any attaching annual bonuses); guaranteed annuity rates that apply to the majority of the fund's with-profits pension business and guarantees that apply when certain with-profits bonds are cashed in
- we might have to pay compensation to certain policyholders and meet any other costs arising from operational errors (except where any such costs are met by the Royal London Main Fund)
- risk associated with operating subsidiary companies owned by the fund, and
- in exceptional circumstances, risks arising in other funds of Royal London.

Since 1 August 2013 the risks relating to the level of our costs have been reduced by the nature of the fee arrangement with the Royal London Main Fund.

Losses from certain risks such as the cost of paying guaranteed annuity rates, certain compensation costs and any losses that arise from the subsidiary companies owned by the fund, are currently covered by the working capital of the fund. Such risks do not usually affect what you get back. But if the working capital is not enough to meet some or all of these losses, we may have to reduce bonuses and transfer values.

Similarly, if the level of working capital is more than we require, we may share out additional profits.

We actively monitor the risks and take preventative action when necessary.

We regularly monitor the level of business risks within the fund as part of our standard risk management procedures, and where we think it is necessary we act to reduce risk exposure.

10. What is the working capital of the fund and what is it used for?

The working capital of the fund is the excess of the value of the fund's assets over the amount needed to meet its liabilities.

We use the working capital for a variety of purposes, for example to ensure as far as possible that the fund is large enough to cover all our liabilities to policyholders at any time and to support smoothing of payouts. As the fund is closed to new policies, we need to balance the requirement to hold a sufficient level of working capital with the need to distribute it over the lifetime of eligible with-profits policies. The way we will distribute the working capital will be decided by our Board from time to time with the overall aim of being fair.

The overriding principle is that the fund is to be managed, so far as it is possible, within the limits of its own working capital. If we are unable to do so this, capital from the Royal London Main Fund, if available, would be used to help support the fund until we could take any available actions to address the situation.
A charge would be made to the fund in relation to such support on terms specified in the Transfer Scheme.

11. What if I decide to transfer the value of my policy to another pension provider?

**It may not be in your best interest to transfer the value of your policy to another pension provider. If you transfer the value of your policy then you will no longer be able to benefit from any guaranteed annuity rate that may apply to some or all of your policy.
(See section 4.)**

You should consider seeking financial advice before deciding whether to transfer the value of your policy.

Your policy is a long-term investment and is designed to be held until its retirement date. If you do decide to transfer the value of your policy, we will adjust your benefits to pay a fair amount taking into account factors such as our costs and investment returns over the time that the policy was held and allowing for smoothing. In exceptional circumstances we may also make a deduction to protect the interests of policyholders continuing in the fund.

Over the longer term, we aim to set transfer values so that the fund does not make a profit or loss from transfers and we normally expect the majority of transfer values to be within 20% of the unsmoothed amounts.

How to contact us

If you have any questions about the With-Profits Pension Fund, please contact us on 0345 605 7777.

Monday to Friday 8am to 8pm and Saturday and Bank Holidays 8am to 5pm.

Or write to:

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Churchgate House
56 Oxford Road
Manchester
M1 6EU

If you would like this information in large print, audio or Braille, please call us on 0345 605 7777.

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