



**PRINCIPLES AND PRACTICES OF
FINANCIAL MANAGEMENT**

**ROYAL LONDON LONG TERM FUND
(EXCLUDING
'THE CLOSED FUNDS')**

**REPORT TO WITH PROFITS
POLICYHOLDERS
ON COMPLIANCE FOR 2016**

JUNE 2017

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1. INTRODUCTION

On 30 April 2004 The Royal London Mutual Insurance Society Limited ('Royal London') first published its Principles and Practices of Financial Management ('PPFM') for the Royal London Long Term Fund ('the fund'). The most recent version was published in December 2016 reflecting changes that permit more freedom to invest in new asset types.

The operations of the SL Closed Fund, the PLAL With-Profits Sub-Fund, the Royal Liver Sub-Fund, and the Royal London (CIS) Sub-Fund, collectively known as 'The Closed Funds', are described in separate PPFMs.

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 2016 and in their opinion the PPFM has been complied with in full. 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.

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, allocation of expenses and the management of the estate.

SETTING BONUS RATES

For conventional contracts, we carried out a process, in line with the PPFM, to set bonus rates for 2016. These were implemented on 1 January 2016 and were not changed during the year. The annual bonus rates were first approved on an interim basis and declared formally at the end of March 2016.

Last year we refined the methodology for calculating some conventional whole of life final bonus rates. We extended this to UF Ordinary Branch whole of life business in 2016. The new method directly uses asset shares of whole of life policies weighted by the probability of a claim occurring, rather than the previous practice of basing bonus rates on similar endowment contracts. No other changes to methodology were made in 2016.

For unitised contracts, annual bonus rates were reviewed at the end of 2015 and implemented from 1 January 2016 onwards. Monthly reviews of final bonus and market value reduction (MVR) rates were carried out throughout 2016, with changes being made on a couple of occasions during the year.

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

INVESTMENT STRATEGY

Since 1 January 2010 we have applied a lifestyling investment strategy which involves changing the asset mix of individual policies as they approach their expected claim date. In 2016 we decided to move back towards using a single asset mix for all policies.

We decided to make this change because interest rates are at all-time low levels and many of the policies remaining in the fund don't have fixed end dates. We started to bring it in during 2016 and will gradually move towards this new single asset mix over the next few years.

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 within a fund is the proportion of the fund's assets that are invested in equity and property. The overall proportion in each of the sub-funds at the end of 2016 is set out in the following table:

Royal London OB & IB	Open	54%
United Friendly OB	Closed	30%
United Friendly IB	Closed	57%
Refuge IB	Closed	38%

SETTING OF SURRENDER VALUES

Changes were made to the formulae underlying surrender values for three lines of business during 2016

- Royal London Industrial Branch Whole of Life
- Former Refuge Assurance Industrial Branch Whole of Life
- Former United Friendly Industrial Branch Whole of Life

All of these changes were designed to align surrender values more closely with asset shares.

ALLOCATION OF EXPENSES

For policies that are not covered by expense agreements as part of previous schemes of transfer our aim is to allocate expenses to policies that correspond to the actual expenses incurred. Over the course of 2016 the expenses allocated to with profits policies were compared to the actual costs of administering those policies. The expenses allocated to with profits policies were confirmed as being appropriate and in line with the PPFM.

MANAGEMENT OF THE ESTATE

There were no material changes to the methods of monitoring and managing the estate and the additional accounts of the closed sub-funds during 2016 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.

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

An updated version of the PPFM was published on 31 December 2016 reflecting changes that permit more freedom to invest in new asset types. All changes to the PPFM are approved by the Directors.

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 2016, the Directors were provided with information and actuarial reports on a regular basis regarding the current and projected financial position of the fund.

Continued good performance and strong operating profits during the year enabled the Directors to allocate a 'profit share' of £114m in respect of 2016.

In line with the requirement to distribute the additional accounts over the lifetime of the remaining United Friendly IB and Refuge IB policies, the Directors again targeted payouts on a value in excess of their asset shares. In addition, enhancements to asset shares were made for these policies as part of the year end 2016 bonus declaration.

For United Friendly OB, the Directors decided to continue the distribution of the additional account by targeting payouts on a value in excess of their asset shares.

NEW BUSINESS VOLUMES

No specific volume limitations were deemed necessary on new business, whether with profits or non-profit business. The volume and mix of new business was regularly monitored throughout the year against the planned volume and business mix. The profitability of new business was also monitored regularly throughout the year, to ensure that there was no detriment to the interest of with profits policyholders.

INVESTMENT STRATEGY

During 2016 the Capital Management Committee met 20 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 Capital Management 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, complied with the relevant schemes of transfer where appropriate and addressed the competing interests of Royal London policyholders, and policyholders whose policies were transferred to Royal London under a scheme of transfer. The bonus rates declared differed between product types and classes.

The final bonus rates declared reflected the distribution of the additional accounts for United Friendly OB, United Friendly IB and Refuge IB, as described under 'Management of the estate' above.

An exercise to review compliance with the target ranges for maturity and surrender payouts published in the PPFM was carried out. This demonstrated that 97% of policies were within target range during 2016, satisfying requirements for compliance. A breakdown by policy groups are detailed below. The policy groupings are described in the PPFM.

Group of Policies	No. of claims/Total asset share included in investigation	Proportion of claims		
		Below Target Range	Within Target Range	Above Target Range
Group A	11,437	3%	97%	0%
Group B	595	3%	94%	3%
¹ Group C	£32.7m	0%	100%	0%
Group D	6095	2%	96%	2%
Group E	41	0%	100%	0%
Group F	1,652	2%	95%	3%

¹The method used for target range gives the asset share of claiming policies rather than the no. of policies

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 full. 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

28 June 2017

REPORT FROM THE WITH PROFITS ACTUARY

To with profits policyholders in the Royal London Long Term Fund, excluding ‘The Closed Funds’

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 London Long Term Fund (excluding ‘The Closed Funds’) in full.

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. In particular I can confirm that my report is compliant with the Technical Actuarial Standards (TAS R and TAS I) issued by the Financial Reporting Council.

Separate reports confirm compliance in respect of the Scottish Life Closed Fund, in respect of the PLAL With-Profits Sub-Fund , in respect of the Royal Liver Sub-Fund and in respect of the Royal London (CIS) Sub-Fund.

Brian Murray BSc FFA

With Profits Actuary

5 June 2017