



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

ROYAL LONDON (CIS) SUB-FUND

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

JUNE 2017

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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 2016 reflecting changes that permit more freedom to invest in new asset types.

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 2016 and in their opinion the PPFMs have 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 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 2016.

The methodology for calculating final bonus rates for conventional Industrial Branch whole of life policies was refined 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.

Payouts were monitored throughout 2016, 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 2016 is set out below:

RLCIS OB & IB Fund	AWP business	63%
	TWP business excl. Table P	46%
	TWP Table P business	27%
RLCIS With-Profits Pension Fund	All WP business	62%
RLCIS With-Profits Stakeholder Fund	All WP business	62%

These proportions remain broadly similar to those at the end of 2015.

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 2016 although no changes were required to these factors over the year.

The approach used to determine surrender values for TWP contracts during 2016 was the same as that used in 2015.

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 2016. 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 2016 the expenses allocated to with profits policies were maintained in line with those set out by the Part VII Transfer. Throughout 2016 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 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.

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 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 relevant With Profits Actuary, the Chief Actuary and the relevant 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.

In 2016, the Directors continued to distribute the estate in order to meet the aims set out in the PPFM. This was achieved by targeting payouts at 103.5% of the smoothed asset share commencing with the 1 April 2016 bonus declaration.

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 relevant 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 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 2016 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	35,990	3%	96%	1%
AWP Surrenders	4,107	7%	91%	2%

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 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 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 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 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

5 June 2017