Royal London Independent Governance Committee

ANNUAL REPORT 2016

ROYAL LONDON'S INDEPENDENT GOVERNANCE COMMITTEE

Annual Report

CONTENTS

PERSONAL INTRODUCTION FROM THE CHAIRMAN

On behalf of the Royal London Independent Governance Committee (IGC) I am pleased to present the second annual report covering the Committee's work during 2016. Our first annual report was published on 2nd March 2016. In that report, we described our work during 2015 as well as providing background material on Royal London, its workplace pensions, and the role of an Independent Governance Committee.

In this report we build on that work, showing how we ensured Royal London implemented the improvements to value for money that we recommended while continuing to identify other areas for improvement.

It has been key to our work this year that we increased our understanding of Royal London's workplace pension customers. This is important to us as we want to ensure Royal London continue to develop in ways which make a difference to what really matters to workplace customers.

To assist us in the work on understanding customers, we asked Royal London to consider adding another independent member with a customer focus to the IGC. I am delighted that Royal London agreed to this proposal and this led to the appointment of Myles Edwards to the IGC as of 1 November 2016. Myles is a customer of Royal London and has a successful career in customer service within financial services.

In addition to our value for money and customer research work we also considered a number of regulatory developments such as the fair treatment of long-standing customers, exit charge cap requirements on pension products and new guidance on transaction costs. We also kept up to date with market developments which relate to workplace customers.

I can advise that Royal London has reported to the IGC on its developments in these and other areas relevant to workplace customers. The IGC is confident that the actions Royal London has taken to date and those planned for the future will result in better short, medium and long term benefits for customers.

We will continue to work with Royal London on seeking improvements for workplace customers and will ensure that all costs are appropriate and that developments are in line with the emerging requirements including best practices.

I welcome your feedback on the work we are doing and your thoughts on this report. You can get in touch using a dedicated email address which is **royallondonIGC@royallondon.com**. I look forward to hearing from you.

In closing, I would like to thank both employees and members of Royal London for their continued support of the IGC throughout the year.

Phil Green
Chairman
2nd March 2017

1. SUMMARY

In our first report published in March 2016, we explained that, in addition to our clear Terms of Reference and specific obligations laid down in the Financial Conduct Authority's Rulebook, we expected our work to evolve over time. This has been the case.

A priority in 2016 was to ensure that Royal London implemented the improvements to workplace pensions that were agreed last year. We can confirm that this is the case, and these changes will lead to improved customer outcomes for the affected customers.

We continue to encourage Royal London to make other improvements, and Royal London has also been proactive in seeking such improvements. As a result, a number of other improvements have already been made. In particular, Royal London has introduced **ProfitShare**[1] and the **Annuity Bureau**[2]. You can read more about this in section 2 of this report.

As we explained last year, determining value for money is more complex than just the charge made by the provider. Ensuring customers have a meaningful fund at retirement depends on more than cost alone. Value for money is determined by three key factors: Contributions, investment returns and appropriate charges for benefits and services. It is for these reasons, together with feedback from customers, that we continue to refine the value for money principles used in our work.

We have also encouraged Royal London to carry out a significant amount of work to increase the understanding of their workplace customers. We believe that increasing the level of engagement with these customers is critical in encouraging greater levels of contribution into pension plans, which in turn is necessary to improve the outcomes for customers.

We have investigated and challenged Royal London's Investment Advisory Committee on their investment approach and performance. Where any component fund held in the key defaults which workplace customer invest in fell below the benchmark we reviewed the position and asked for further information and for answers to appropriate questions. This approach and the responses the IGC has received has satisfied us that there are no strategic or structural issues that need to be addressed. The Investment Advisory Committee and Royal London Asset Management are aware we will continue to actively monitor performance against benchmark in 2017.

We also asked for more information from Royal London about transaction costs within the funds. We are satisfied that the levels of costs are consistent with our value for money principles. However, we will be doing more work on transaction costs in 2017 in line with emerging regulatory requirements and market practice.

We identified customer engagement and communication as key areas of focus for us this year. As a first step in addressing this, Royal London agreed to expand the IGC to ensure we had both the depth and the breadth of expertise for this work. We agreed with Royal London that it would be useful to have a member of the IGC who was also a Royal London pension customer. You can read about the appointment process and the new committee member in section 6.

We believe that the issue of customer engagement we highlight in this report is symptomatic of the workplace pension industry generally and not just a challenge for Royal London. However, we want to highlight this issue and ensure that it has additional focus in the coming year. Improving customer engagement has the potential to enhance the value for money to workplace customers. Enhanced engagement can lead to increased savings that in turn should lead to better outcomes for customers.

In this report, we have set out the research findings which have led us to this view. We are having discussions with Royal London on how engagement can be improved and expect this to feature in plans for 2017.

After completing our work this year, we have concluded that Royal London continues to provide value for money to its customers through its workplace pensions.

We have made every effort to ensure our report is easy to read and have tried to avoid using jargon. However, some technical terms are difficult to avoid. These are highlighted in bold throughout the report and are explained in a Glossary in Appendix 5.

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1 https://www.royallondon.com/profitshare/profitshare-explained/how-it-works/

2 https://www.royallondon.com/products/retirement-page/planning-for-retirement/prod-serv/our-products-and-services/

2. OVERVIEW OF ROYAL LONDON'S WORKPLACE PENSIONS AND RECENT CHANGES

2.1 Products and distribution

Last year we provided a significant amount of information on the nature of Royal London's workplace business and its customers. We have summarised that and provided an update in Appendix 1. Key points to note are:

- Royal London's workplace pension business has continued to grow significantly in 2016, primarily through attracting new automatic enrolment schemes from employers.
- Average charges for new workplace pension plans have continued to fall and we note that Royal London has set charges for many employers' schemes below the maximum required in the automatic enrolment regulations. This is covered in more detail later in the report.

Royal London continues to attract new workplace pension business solely through financial and corporate advisers, and does not offer its products and services direct to employers. In 2016, the company continued to support advisers, employers and customers while focusing, in our view, on the provision of a quality core pension arrangement based on the perceived needs of customers. You can read more about this in section 3. Based on the feedback we gathered, this approach is welcomed by advisers, employers and customers alike.

Further information regarding the size and mix of Royal London's workplace pensions is set out in Appendix 1.

2.2 Progress on the recommendations we made last year

Last year, we agreed an implementation plan with Royal London to make various improvements to its workplace pensions. This plan, designed to deal with the findings of the Independent Pension Board's Report of December 2014, along with other findings from our review of Royal London's workplace pensions, was submitted to the Financial Conduct Authority (FCA).

The improvements in the plan were:

1. the removal of plan fees on workplace pensions that were no longer receiving contributions,

2. the removal of some exit charges,

3. increasing the level of fairness in some of the more complex charging structures, and

4. improving how the loyalty bonus structure works in some products.

We monitored the implementation of the changes promised last year and can confirm that the changes were made during 2016 as agreed and on time. The cost of these changes was estimated to be around £15M.

2.3 Other changes introduced during 2016

2.3.1 ProfitShare

The introduction of the ProfitShare arrangement in 2016 is a significant improvement to the benefits customers can expect from Royal London's workplace pensions. Royal London wrote to all affected customers to explain how this will work and you can find out more **here**[3]. We note that the level of the ProfitShare for 2016 is 0.18%. ProfitShare could be seen to represent a material level of additional investment return in a customer's plan.

2.3.2 Annuity Bureau

During 2016 Royal London also introduced their **Annuity** Bureau service, increasing the options available to customers reaching retirement. Royal London recognised that most customers purchasing an annuity without the help of an adviser were not shopping around for the best deal. The new Royal London Annuity Bureau offers customers access to a panel of providers drawn from the leading annuity providers in the market place. Customers have access to telephone support to help them assess their needs and both standard and **enhanced annuities** are available to them.

The customer does not need to accept any of the rates offered by the Annuity Bureau and can still choose to shop around for themselves. Where a customer does want to go ahead with the annuity purchase, Royal London helps make this happen. Royal London covers the cost of this service and any commission due is used solely to improve the terms for the customer. At the time of writing Royal London has assisted over 1000 customers through this service. Overall the IGC consider this an added value service which has the potential to improve value for money for those customers wanting to purchase an annuity but do not have access to an adviser.

3 https://www.royallondon.com/profitshare/profitshare-explained/how-it-works/

2.3.3 Helping customers bring their pension pots together

Royal London carried out research to identify potential barriers to customers bringing their pension pots together in one place, particularly where the customer is not supported by a financial adviser. The IGC was keen to learn of the actions Royal London has taken as a result of this research.

Royal London has developed a service which helps members bring their pension pots together more easily, if it is appropriate for them to do that. The service has been designed to look at the previous scheme assets and charges (amongst other things) when an employer moves their pension scheme and regular pension contributions to Royal London. Royal London check on features of the scheme the member is transferring funds from to ensure there are no important benefits to be lost on transfer and to identify any charges which apply. This is compared against the Royal London scheme and if appropriate Royal London will make an offer to members where an appropriate suitability test has been met. This service does not provide advice or a recommendation to the customer, but gives them enough information to allow them to make up their own mind whether a transfer is right for them. This service is intended to complement any adviser-based transfer process that might be in place, and it will only be offered where the adviser has specifically confirmed they do not want to be involved. At the time of writing Royal London has assisted over 4000 customers with this service.

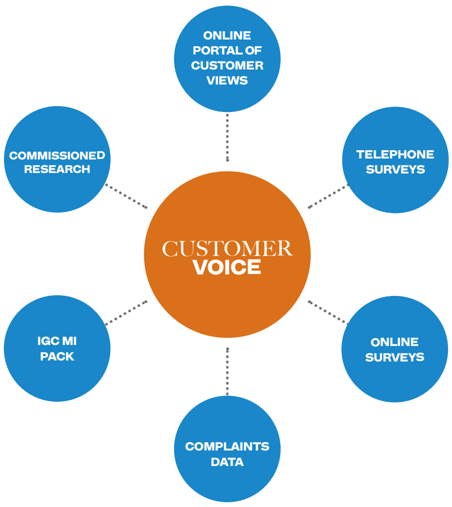
As a result of this review we are confident this is a positive addition to the Royal London proposition, allowing pension pots to be brought together as part of a pension scheme move. Increasing the overall pot size in one place has the potential to increase customer engagement and can often ensure better value overall.

2.3.4 Scheme Governance Reporting

Royal London has developed a scheme governance report which helps advisers provide good governance to their Royal London pension scheme on an ongoing basis. In our view, it is important that employers, in conjunction with their advisers, keep their scheme under review. This report provides a significant amount of management information which is necessary to be able to undertake this review efficiently.

3. CONSIDERATION OF THE INTERESTS OF CUSTOMERS AND ACCESS TO THEIR VIEWS

The IGC recognises the importance of understanding the views of the customers who rely on Royal London to run their pension arrangements. This customer input is provided to the IGC regularly and comes from a number of sources as shown in the following diagram:



Although a lot of information was already available, we wanted to delve deeper to understand precisely which benefits and services customers believe make up the components of "value for money" and specifically how Royal London is delivering against those components. We also wanted to understand what would encourage customers to be more actively involved and have more control over their retirement savings. To achieve this, we worked with Royal London to set up a programme of research during 2016. This is described in sections 3.2 and 3.3.

3.1 Monitoring customer views of service provided by Royal London

Royal London regularly collects feedback from customers who have called them. Customers are asked a number of questions including:

- how likely they are to recommend Royal London to family and friends,
- how easy it was to deal with Royal London and
- whether they got the answers they were looking for during their call.

The feedback is used to calculate a transactional **"Net Promoter Score" (NPS)** as well as **"Ease"** and **"Resolution"** scores: together these three measures are used to determine customers' satisfaction with the service they received from Royal London.

All three scores have consistently met the expectations of the IGC throughout 2016 and show that the customers taking part in the survey are satisfied with the level of service they have received.

Customers can leave their own comments as part of the survey, giving valuable additional information. The scores and the comments are available for review through an online portal. This portal is monitored monthly by the independent members of the IGC. This gives us added reassurance on service quality and helps our understanding of customer needs and views. The IGC is satisfied that Royal London takes action if this information highlights areas which require attention. This is in addition to the information in the regular Management Information pack which Royal London provides for each IGC meeting.

3.2 Provider group research

We asked Royal London to take part in an extensive industry-wide research project into what workplace customers see as value for money. This involved 11 major workplace pension providers and gathered the views of over 13,000 workplace pension scheme members, including 820 Royal London customers. The project included both qualitative and quantitative research to understand:

- What aspects of a workplace pension are regarded as being important by customers,
- How customers decide what is, and what is not, value for money from their perspective, and
- How Royal London specifically is delivering on their customers' expectations.

Information on what customers said was important to them is included in Appendix 3.

The qualitative research involved in-depth, facilitated and focused discussions with customers. The information from this research was particularly important. It showed that customers' understanding of workplace pensions, and their desire to engage with their pension savings, could be improved through personalised and targeted material and explanations.

The quantitative research, done through an online questionnaire, was also useful as the large sample size meant we could identify some differences in responses depending on aspects such as the size of a fund. However, for customers taking part in the online questionnaire, there was no opportunity to help them understand the product and some of the complexities of pensions. As a result, there were some discrepancies between the findings from the qualitative and quantitative research. In particular, those customers taking part in discussion groups appear to be better informed than those who completed the online questionnaire.

Overall the research findings tell us there are four main building blocks that workplace pension customers believe add up to “value for money”. These building blocks and the things that affect them are shown below:

Security 1 | **Product** 2 | **Support** 3 | **Charges** 4

Higher ← **Level of importance** → **Lower**

Security	Product	Support	Charges
Controls and safeguards to ensure my pension scheme is safe and secure and working as it should be	A good return on my money	Clear and understandable communications about my pension	Charges in line with the market average
Accurate administration and reporting of my pension scheme	My employer pays in at least as much as I do	Access to online calculators and tools that help me work out how much I should be contributing (to my pension)	The option to receive a premium service and experience for a higher charge
A reputable, financially-strong pension provider	Access to a range of funds with different levels of risk, meaning I have a choice on where my pension money is invested	Email updates telling me how my pension is doing	
	A guarantee that I will get back at least as much as I pay in – even if this potentially means lower investment growth on my pension pot	A mobile app that allows me to check how my pension is doing	
	A standard fund where my money gets automatically invested so I don’t need to make any decisions	Telephone support to answer my questions	
	The option to choose a fund that is higher risk and higher cost but that can potentially produce a larger pot for me at retirement	Seminars at work to help me understand my pension	
	Flexible options for how I can take my pension income in retirement	An easy way to change the amount I pay into my workplace pension	
	Rewards and special offers for being a loyal customer	A simple process for transferring my old pensions into my current one	
		The option for personalised financial advice about my pension (at extra cost)	
		I receive tax relief (government top up) on my pension contributions	

This shows the main areas that workplace customers find important. It is clear that, in addition to a good return on the funds, security and controls were seen as key. Price in isolation was seen as of less importance. However, it should be noted that although it was seen as of lower importance, there is a point at which customers see the cost as too expensive to consider. Regardless of this finding on how the customer views charges the IGC does, and will continue to, challenge Royal London on the level of charges relative to the product quality and service provided.

The pension product itself and support from their provider were the next two most important building blocks.

- Product: customers need to feel their pension is flexible and will meet their lifelong needs. This includes:
  - being able to change the amount they pay in easily,
  - having a choice of where to invest their pension money
  - having flexibility on how they take their pension income.
- Support: it is important to customers that they can get support when they need it and this includes:
  - having access to tools and calculators to help them understand the impact of making changes,
  - being able to choose how to receive information from their pension provider, and making sure that information is clear and understandable,
  - having access to telephone support.

The final building block is Price. This was seen as less important than Security, Product and Support although it does of course impact overall returns.

In addition to this industry-wide research, we asked to see detailed information on which aspects are important specifically to Royal London's workplace customers and how Royal London is delivering against these.

The results showed that, in all key areas, Royal London customers have a positive view of how Royal London is performing. However, there are interesting variations in how customers with older Royal London workplace products feel about how the business is meeting their needs. Although still favourable, they are less positive than customers that have more modern pension products. We have asked Royal London to consider these findings and provide us with details of how they intend to improve the position for older products.

The research also helped us identify other areas where Royal London could improve customer satisfaction, in many cases by improving communication with customers. We had anticipated that the research would highlight more effective communications and better engagement of customers as a challenge, both for Royal London and the industry as a whole. We had therefore set ourselves the goal of gaining a better understanding of this area as a priority for 2016.

In our view, the workplace pension industry has not communicated well enough with its customers in the past and has not built the strong relationships needed to help customers get the very best out of their pension savings. Engaging customers and building an ongoing relationship with them is critical to encouraging customers to save appropriate amounts to ensure a good retirement outcome.

We therefore asked Royal London to commission additional research on our behalf to find out:

- what type of relationship customers want with their pension provider,
- what the barriers are at present, and
- how the desired relationship may be fostered.

This is covered in the next section.

3.3 Additional research into Royal London customers

The results from the industry-wide research were consistent with those from other research that Royal London has undertaken with its own workplace customers. In particular, the lack of involvement customers have with their workplace pension savings and the lack of interaction they have with the company that runs the pension for them were common themes. Royal London also found that its workplace pension customers had a lower perception of its overall service than that held by its customers with other products e.g. products such as life assurance where the customer has actively purchased rather than receiving it through the workplace. These findings prompted us to ask Royal London to do more work in this area.

The key findings from this additional research told us:

- Customers largely feel detached from their workplace pension. There are a number of factors that contribute to this including:
  - The lack of understanding of pensions: the product is seen as complicated
  - There is a perceived lack of control over the pension because the employer has usually chosen the company that provides it
  - People tend to focus on current rather than future financial needs, which can mean saving for the future is sacrificed in favour of current spending
  - Royal London is not well known as a workplace pension provider and customers do not know very much about them.
- Customers said they liked the communication materials they received from Royal London when they first joined the pension scheme. They find the material easy to read and understandable, but there is not much interaction after this initial contact. Customers do understand that pensions are important and they want to interact with Royal London more, but are not sure how to do that
- Customers feel they need more frequent and personalised communication and more opportunities to interact

We consider that this picture is representative of the market rather than being specific to Royal London. The main reason for this stems from the way that workplace pensions are set up: although the customer has the pension plan with the provider, their employer will almost certainly have chosen the provider, often in association with a consultant or adviser. The customer may therefore not feel particularly involved with the provider. We understand this, but have asked Royal London to create a stronger, longer-term, two-way relationship with customers by making the opportunities for interaction clear and taking account of how customers want to receive communication. This will include greater personalisation of customer material.

We have already been provided with details of initiatives Royal London intends to deliver over the short to medium term. We believe these are well thought through and appropriate. Monitoring the development and delivery of these plans will be an area of priority for the IGC during 2017.

4. ASSESSING VALUE FOR MONEY

4.1 Set of principles

Last year we developed a set of principles to assess the value for money customers receive from their workplace pension. These principles were developed in line with the requirements of the FCA and using the customer feedback outlined in the previous section. As the workplace pensions market continues to develop and our understanding of Royal London's customers continues to grow, we will continue to review these principles. While we believe that their core elements remain valid, we have changed the emphasis where we felt this was required and added to the principles where appropriate. The updated principles are set out below.

These principles continue to recognise that value for money is not simply about the level of charges associated with workplace pensions. This has been validated by the customer research, as described in section 3. Factors such as the governance and controls, quality of administration and the nature of the services provided are important to customers.

The following summarises the principles applied to assess value for money in 2016:

Principle	Examples of what this means in practice
1. Workplace pension contracts should be regularly reviewed for their continued relevance, given the changing needs of customers in the long term savings market. These include: a. Consideration of the changing market environment. b. Consideration of the customer experience taking account of different customers needs. c. Consideration of any inappropriate results or potential results for customers.	Long-standing customers are not ignored. One example of this was the agreement by Royal London to remove the monthly plan fee on plans that are no longer receiving contributions. Planning around Brexit and what this means for advisers and their customers. Not all customers are the same. Having support in place to identify and help vulnerable customers. Ensuring customers can still get a good outcome from their plan even when things change.
2. Ongoing charges must continue to offer value for money relative to the benefits provided by the contract. Benefits and services will be considered in light of what customers view as important and how Royal London delivers against these.	The results of the customer research carried out in 2016 will inform further changes. Further regular research into customer views will be carried out.
3. Any deduction from the face value of a pension on exit must be fair and designed to recoup no more than any costs incurred by Royal London caused by the early exit of the customer.	Most exit charges have been removed and those that remain are regularly assessed for fairness. Appendix 1 shows the number of plans affected by any deduction on exit.
4. Any assessment of value for money should make allowance for the need for some cross-subsidies between workplace pension plans where appropriate and in the interest of customers.	Royal London has a charging structure based on the overall membership size of the workplace scheme, the level of contributions and other factors which indicate the likely costs of running the scheme and likely returns through the charge it levies. In practice this means that customers with proportionately smaller funds will benefit from a lower charge than if they had an equivalent individual plan. The converse applies for long standing customers with larger funds.
5. Communication with customers must be clear, timely and designed to meet the stated needs of the customer, which may change over time.	Royal London clearly strives to achieve engaging communications with customers. While this ambition is met for the initial communications with new customers research has shown that other communications are not achieving the standard desired. We have asked Royal London to prioritise this area and show their plans in this respect for the short, medium and long term.
6. Investment returns should be appropriate relative to the level of risk a customer has taken.	When we look at investment returns for any particular fund, we consider the level of risk that that fund is designed to accept – and whether customers are made fully aware of the risks they are accepting. We also look at the reasons for the returns over a number of time periods.
7. The service provided by Royal London should make it easy for customers to manage their pension and engage with them effectively when they need help.	As we have mentioned, we see meaningful engagement as being essential in workplace schemes. We have asked Royal London to report back to the IGC on a regular basis on progress made in improving their customer engagement throughout 2017.

4.2 Investment strategies for default funds

All IGCs are required to assess whether the investment strategies for default funds (that is, the funds into which customers' investments are placed unless they specifically select another fund) are designed and executed in the interests of customers and include clear statements of the funds' aims and objectives.

The IGC continues to review the work of Royal London's Investment Advisory Committee (IAC), which plays a key role in overseeing Royal London's investment strategy and performance for all its workplace pension customers (not just default funds). This includes regular discussions between IGC and the IAC chair and attendance at IAC meetings to assess firsthand the oversight that the IAC delivers. The discussions and meetings cover investment strategy and performance over the short, medium and long term. The IGC has a good working relationship with the IAC and can raise areas of concern, for example over the investment manager's response to the EU Referendum vote. The IAC operates independently of the investment manager (Royal London Asset Management or RLAM), which undertakes the day-to-day management of the funds. Further information on the IAC can be found **here**[4]. The minutes of the IAC are made publicly available and can be found **here**[5] on the Royal London website.

Royal London offers a range of default investment options to its workplace pension customers so an employer and its investment adviser can select the most appropriate one for its workforce. As at 31 December 2016, there were 30 standard default options available, and, in aggregate, these funds accounted for 47% of the total workplace pension funds under management and 90% of new members.

We found the aims and objectives of each of the default options to be clear. Each strategy aims to deliver above inflation growth in the value of the fund at retirement consistent with the level of risk taken. Risk is measured as a volatility target and the IGC is satisfied that the level of risk taken for each default fund is appropriate and that returns are commensurate with this level of risk. Full details of the funds are shown in fact sheets available to customers **online**[6].

We also considered the necessity of having such a large number of default funds but were satisfied that, given the variety of employers and customers involved and their goals and objectives, it was appropriate to offer such a range. In particular managing this number of default funds did not result in additional costs for the workplace pension customers but did offer wider choice.

Royal London has actively reviewed whether the investment strategies of its default funds remain appropriate in light of the changes introduced by Government in April 2015 to give customers greater choice in how to use the proceeds of their pensions. We are satisfied with the results of this review by Royal London.

This year we also reviewed how Royal London ensures that, where advisers are taking responsibility for selecting a default fund, the adviser continues to review its appropriateness for customers. We were satisfied with the general procedures Royal London has in place, but will be doing further work in this area during 2017.

Overall, we have concluded that the investment strategies and governance arrangements for the default options are designed and executed in the interests of customers. There are also clear statements of the default funds' aims and objectives.

Further information regarding the numbers of customers invested in the default funds is included in Appendix 1.

4.3 Reviews of investment strategies and performance

In 2016 we continued to review the work of Royal London's existing committees to assess whether Royal London regularly considers the characteristics and investment performance of all relevant strategies and funds (not just default options) to ensure they are aligned with customers' interests.

In order to assess strategies and performance, we examined supporting documents and carried out face-to-face discussions with members of the IAC and Royal London's Investment Committee. The relevant papers from Royal London's IAC and Investment Committee are supplied to the IGC at each meeting.

As part of a review in 2016 Royal London increased the range of investments which could be held within the **Governed Portfolios**. These portfolios form the building blocks for most of the default investment options offered by Royal London, for example the Balanced Lifestyle Strategy. The changes mean customers now have exposure to **commodities** and **absolute return funds** (including cash strategies), together with a wider variety of bonds. This broader mix means the Governed Portfolios are now less exposed to negative developments in individual asset classes. This is expected to reduce investment volatility and risk, which in turn is expected to bring benefit to workplace customers over the long term. We are in agreement with these changes.

We have also continued to monitor the overall investment performance of the default strategies and underlying funds offered by Royal London, although the detail of this work is carried out by the Investment Committee and the IAC.

It is important to keep in mind the long term nature of a workplace pension product, however it is also essential to consider short and medium term investment performance, the reasons for such performance and the investment objectives.

The table below shows performance of the most popular default – the Balanced Lifestyle Strategy (Annuity). Whilst absolute returns during 2016 were strong the strategy is below benchmark over one year due to poor performance from the underlying UK equity fund.

4 https://adviser.royallondon.com/pensions/investment/investment-governance/investment-advisory-committee/
5 https://adviser.royallondon.com/pensions/investment/investment-governance/
6 https://adviser.royallondon.com/pensions/investment/fund-information/factsheets-and-prices/governed-range-factsheets/

Investment performance to 31 December 2016: Balanced Lifestyle Strategy (Annuity)

	1 year performance %	3 year performance %
15 years to retirement[7]		
Performance	15.08	8.94
Benchmark	16.80	8.99
Difference	-1.72	-0.04
10 years to retirement		
Performance	14.23	8.63
Benchmark	15.77	8.68
difference	-1.55	-0.05
5 years to retirement		
Performance	11.66	7.47
Benchmark	12.24	7.36
difference	-0.58	0.11

Source: Lipper, bid to bid, as at 31.12.2016, Royal London, as at 31.12.2016. All performance figures shown have been calculated net of a 1% annual management charge. In practice customers will have some of this charge rebated to reflect the actual terms of their particular scheme.

The reasons for under performance have been explored and understood and are being addressed by RLAM. More detailed performance data and commentary for the key underlying funds and default funds are included in Appendix 2 and Royal London continues to publish detailed information on its **website**[8].

This default strategy has only been available since 2012 so longer term performance figures are not available. However the underlying portfolios which make up the strategy were launched in January 2009 and since then have delivered between 7-11% per annum in line with their stated objectives and our value for money principles (as shown in Appendix 2).

Overall, we are satisfied that the long term investment performance of the key strategies and funds is in line with the value for money principles set out in section 4.1.

7 The components of this fund vary by how long a member has before their nominated retirement date and so various sets of results are shown

8 https://adviser.royallondon.com/pensions/investment/fund-information/fund-performance/

4.4 Processing of financial transactions and service operations

The research described in section 3 showed that customer service is an important aspect of value for money. We therefore regularly review key management information and reports from Royal London about its performance in this area, and challenge Royal London to improve its performance where necessary.

The independent members of the IGC have also spent two days with Royal London's service teams to experience the service customers get first hand. This included listening to workplace pension customers calling Royal London to carry out financial transactions or other plan administration tasks. We can confirm that the service experience we observed helped us understand why Royal London is highly regarded for its customer service.

We also conducted an in-depth review of how customers' complaints are managed and resolved. It is important that all customer complaints are dealt with appropriately and specifically and are also used as an opportunity to make general improvements in the administration process where relevant. We found that Royal London uses its complaints experience in this way. The complaints information we saw also provided reassurance that any significant issues were addressed.

We are also required to assess whether the financial transactions involved with investing a customer's pension are processed promptly and accurately. This includes receipts of contributions, investment allocations, payment of benefits and allocation of charges.

To help us with this, we have been supplied with internal reports, given details of independent reviews and have been taken through relevant controls and policies which support Royal London's operations. This has shown us that the information we review is accurate and the positive view we have of the service provided by Royal London to workplace customers is justified. We have seen that where there are recommendations for improvement in any area, plans are brought forward to deliver on these. We are satisfied with the actions being taken to remedy any underlying issues. We have found no evidence of any negative impact on customers, or any failure to recognise and address recommendations.

The Government and the media have recently highlighted that non-income tax payers are being disadvantaged where a **net pay arrangement** is used rather than a **relief at source arrangement**.

We investigated how Royal London manages the tax treatment of its workplace pension customers' contributions. We found that Royal London is able to offer both net pay and relief at source arrangements based on the employer (and adviser) needs. Royal London has confirmed that only a very small proportion of its workplace customers have elected to operate an occupational pension using a net pay arrangement. This means that for over 99% of its workplace customers still contributing to their pensions (and all of the customers in scope of our work) Royal London automatically enhances the contributions received by the amount of basic rate tax. This means that even those customers who are non-tax payers will benefit from this treatment. High rate tax payers can also claim the additional relief from HMRC via self-assessment.

One aspect of customer service that we will be asking Royal London to consider during 2017 relates to customer annual statements. We consider that it would improve the customer's engagement with their pension for these to be issued quicker than at present and the statements should engender a stronger sense of ownership from the customer. As we described previously, Royal London has conducted significant research in the area of engagement and we look forward to seeing their plans coming to fruition in 2017.

4.5 The level of charges

We continue to assess the level of charges on workplace pensions and the impact this has on value for money.

Royal London's workplace pension charging policy remains unchanged from 2015. The charges are based on the different characteristics of employees and employers, rather than offering a single price for all schemes and members. Those characteristics include levels of contribution, numbers of employees and employee turnover rates. This ensures that the actual cost of providing workplace pensions for each employer and its employees is taken into account.

We explained in section 2 of this report how Royal London has implemented the improvements to charges we recommended in our previous report.

The one area of Royal London's charges we have asked them to re-examine for 2017 is exit charges on older products sold prior to April 2001. Exit charges were a necessary feature of the market in some older contracts before that date in order to ensure fairness across customers and to recoup expenses where members left the scheme early. Royal London has made some reductions in exit charges as set out in our previous report. The justification for Royal London's remaining exit charges, and the nature of the forthcoming regulatory changes, is set out in Appendix 4.

We encouraged Royal London to consider whether reductions should be made to exit charges, particularly in relation to any outliers. This was in addition to forthcoming regulatory restrictions on these charges. We are satisfied that the remaining exit charges are consistent with our value for money principles and in particular are not a source of profit for Royal London. Nonetheless we will monitor the progress of Royal London's additional commitments and proposals in this area as they develop in the early part of 2017.

In the meantime Appendix 1 provides some information on the level of exit charges that applied during 2016.

4.6 Transaction costs and other direct and indirect costs within the investments

The IGC have undertaken a significant amount of work in 2016 to improve their understanding of transaction costs on the investment funds and consider if they are consistent with our value for money principles. This has involved meetings with professional bodies, key industry figures and the regulators to understand the potential eventual industry-wide standards for measuring and reporting transaction costs. In addition we have encouraged Royal London to develop additional internal capability for measuring and controlling these costs.

We were pleased that the FCA published guidance to provide direction on how transaction costs could be measured and reported more consistently. They issued a Consultation Paper (CP16/30) on transaction costs in workplace pensions in October 2016. This Consultation Paper proposed rules and guidance to improve the disclosure of transaction costs in workplace pensions. It sets out draft standards to enable IGCs and trustees to obtain, for the first time, a standardised disclosure of the transaction costs that pension investments incur. The consultation period closed in January 2017 and a Policy Statement which is expected to set out the rules on transaction costs in workplace pensions is expected in the second quarter of 2017.

Despite the current absence of industry-wide standards or rules from the FCA we wanted to carry on with our work on transaction costs and publish our findings in this report. We have therefore used the best available developing industry standards from work co-ordinated by the Investment Association to assess the transaction costs on the main default funds into which the vast majority of Royal London's workplace pension customers are invested, as well as the underlying component funds. We also concluded that the Investment Association's eight principles on which its methodology was based are aligned with the principles for transaction costs that we set out in section 3.6 of our previous annual report and repeated below; this can be viewed as building on the work we already started in 2015.

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Transaction costs – current status of work against principles		
Principle	**Description**	**Status for 2016**
Relevant and in the Customer Interest	• Any trading or associated cost should be undertaken or incurred in the interest of the customer • Provides an informed view for IGC to fully understand costs and charges associated with Workplace Pensions	
Reasonable and transparent	• Transaction costs should be reasonable relative to the return and objectives of the fund • Transaction costs should be separately identifiable from the Annual Management Charge (AMC) or other administration costs of the product provider	
Proportionate	• The information on cost should be sufficient to ascertain whether the transaction costs could have a significant impact on investment returns • The cost of obtaining the information should not be disproportionate to the likely significance or impact on return	
Measurable and controlled	• Information supplied should be clear, measurable, verifiable and have appropriate controls around the expected outcomes	
Common standards and benchmarking	• The information supplied should meet common standards developed and agreed by industry bodies and the regulator • The information should be capable of being benchmarked against peer funds and providers	

Although the Investment Association's work is continuing, draft templates have been agreed with key industry stakeholders and we asked Royal London to ensure that reporting to us was in line with these standards. We also asked for additional information on its investment operations and to receive monthly updates on the project which developed the additional transaction cost reporting capability. This has been done. As a result we have improved the score for the "common standards and benchmarking" status to amber from last year's red. We expect further work in the next few years to consider how best to benchmark transaction costs across different funds and continue to engage directly with key industry stakeholders.

The Investment Association (and Local Government Pension Schemes) transaction costs templates that Royal London has completed for us report by asset class on a fund by fund basis and include costs at both **portfolio level** and **product level**. This goes further, and is more detailed, than the level of disclosure proposed in CP16/30.

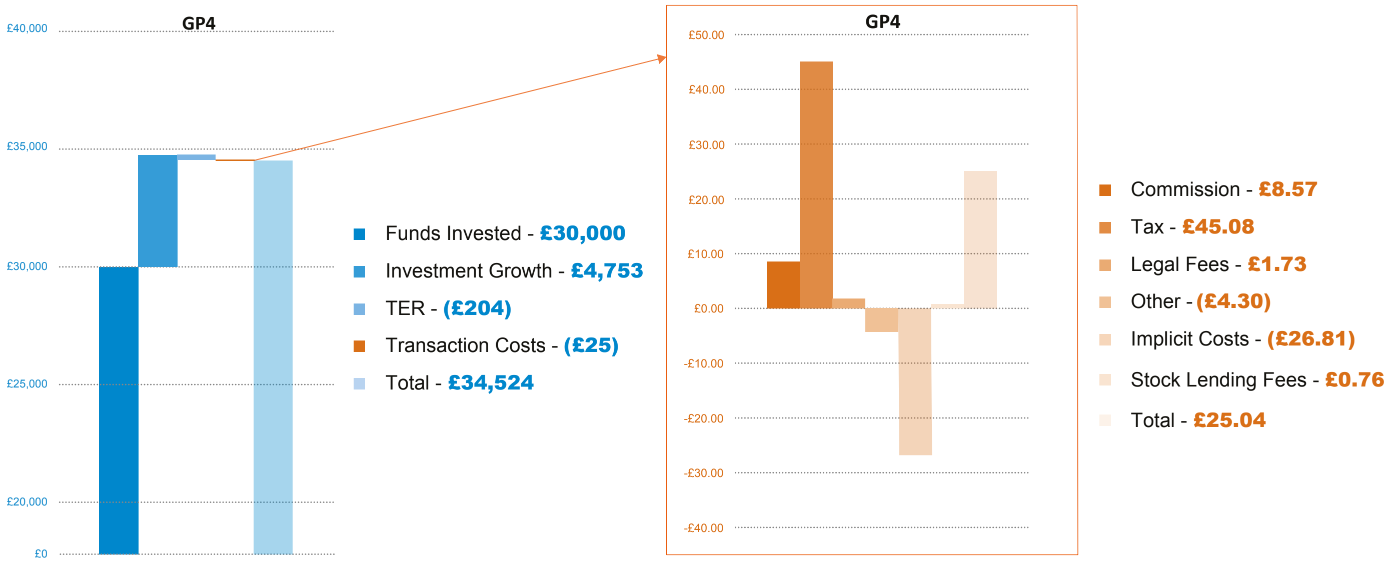
Having supplied the templates and information we have requested, we are satisfied that Royal London has appropriate control over the transaction costs applicable to its workplace customers. We intend to continue to develop our work in this area during 2017. We will work closely with Royal London as they develop their capability further on transaction costs in line with, and in some respect beyond, the emerging regulatory requirements. We would like to see the market and industry bodies develop their templates and standards of calculation sufficiently so that benchmarking of like costs can be established. We will continue to press appropriate regulatory and market stakeholders to move this forward in 2017.

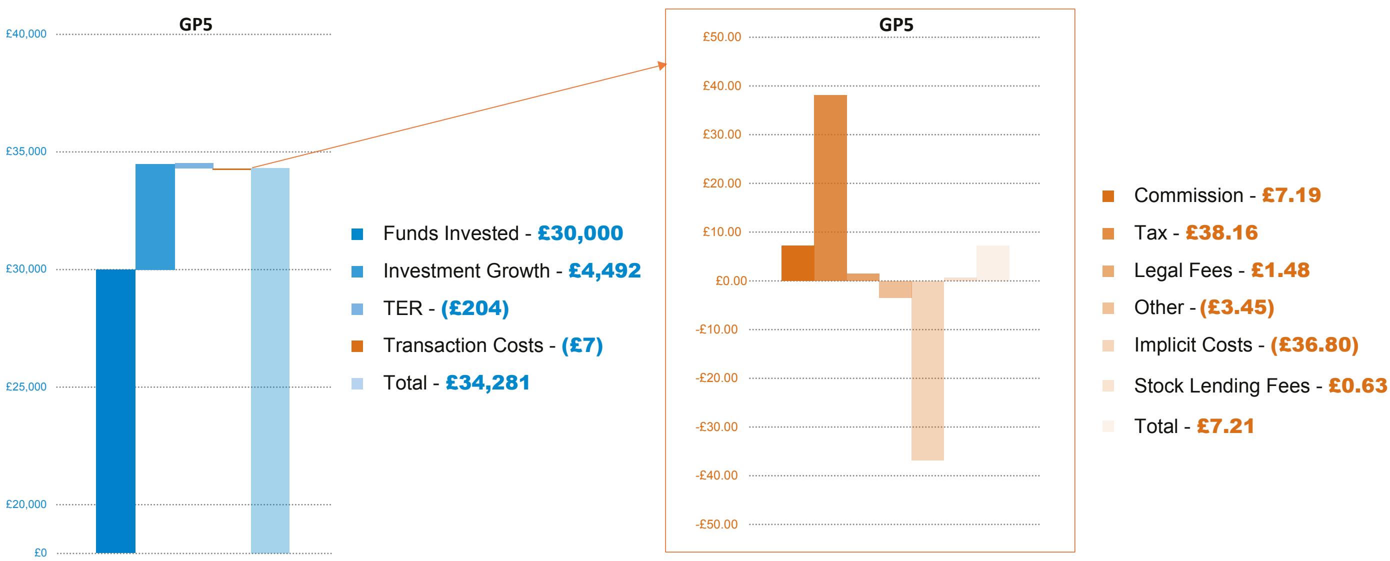
We were keen to disclose actual costs within this report and have worked with Royal London to agree a format to present these costs in a meaningful way to customers. Since most customers are invested in one of the default funds we have concentrated on reporting transaction costs in this area.

We have also shown the transaction costs for several of the core underlying funds. Other pension providers may have different mix of investments in their default funds and hence direct comparisons with other pension providers may result in misleading conclusions.

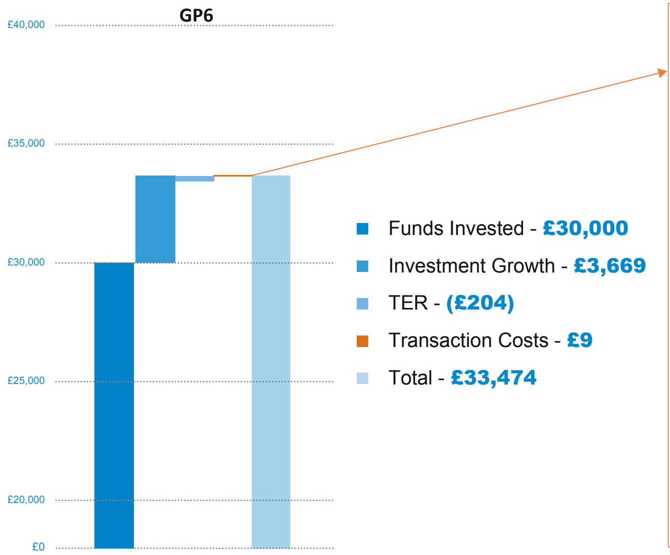
The first graph for each portfolio below show the amount of transaction costs incurred during 2016 by a typical customer based on an investment of £30,000 into Governed Portfolio 4, 5 and 6. These are multi asset portfolios holding a mix of equities, property, corporate and high yield bonds, index linked gilts, commodities, absolute return and cash, this is typical of the default investments held by workplace pension scheme members. The investment of £30,000 is based on the median pot size of active members in default schemes.

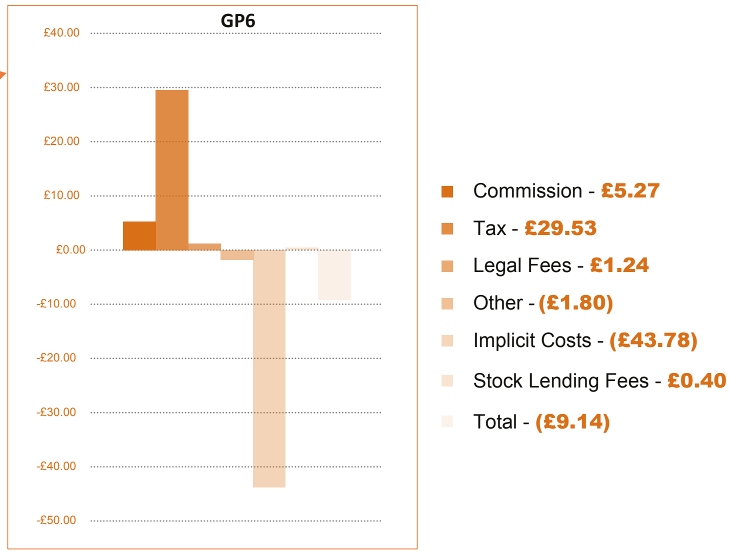
The second graph for each portfolio shows a breakdown of the transaction costs. This shows that during 2016 the biggest impact was tax whilst **implicit costs or market impact** had a positive effect and reduced the overall costs. This item, explained further in the glossary, is an indirect cost calculated from considering the movements in asset prices around the time of the transaction. It can be either positive or negative depending how market prices move around the time of the transaction, as well as how efficiently the fund manager implemented the transaction. All performance and transaction costs data shown is for the whole of 2016.





Brackets in the descriptions above indicate negative values.





This information is for Governed Portfolios 4, 5 and 6, which make up the Royal London default Lifestyle Strategy. Further information for these Governed Portfolios and some of the key component funds is included in Appendix 2.

Overall, based on the absolute levels of transaction costs across different funds that we have examined we consider that the transaction costs incurred are consistent with our value for money principles for such costs, as set out previously.

Technical terms used in the labels to these graphs are explained in the glossary section of the report.

5. INTERACTION BETWEEN THE IGC AND ROYAL LONDON

The IGC met formally on six occasions between 1 January and 31 December 2016, with over 87% attendance from all members and 100% attendance from independent members. In addition, two training sessions were held for our new independent member as were a number of supplementary teleconferences. The latter were used extensively to consider particular technical issues in depth.

Regular communication via teleconference between the independent members of the IGC and Royal London ensured we were kept abreast of plans affecting workplace customers and to deepen our understanding of the business and Royal London's customers. Committee members also actively participated in various industry forums that have been set up to discuss IGC matters, as well as attending meetings with the FCA. In particular independent members of the IGC were very involved in commissioning and organizing the Provider Group research, so that it was focused as much as possible on areas that were of most relevance to Royal London workplace pension customers.

This activity ensured that the IGC was well informed about developments across the industry.

Independent members also attended formal meetings of relevant internal governance committees and met extensively with key Royal London staff and management.

During our discussions we asked Royal London for a significant amount of information on its workplace pension schemes. Royal London has again supplied all the information requested and provided access to the relevant subject matter experts.

To supplement these reports and other information, the independent members of the IGC had several detailed practical working sessions with members of the workplace pensions administration team on-site in Wilmslow. This enabled an improved and practical understanding of customer service to be obtained.

During the year, our work and meetings focused on the key elements required to meet our terms of reference and to fulfil Royal London's regulatory requirements.

We produced written reports to Royal London's board following each of our formal meetings and these reports were presented to the next board meeting. The IGC is required by its terms of reference to raise any areas of concern to the board. No issues were required to be formally raised to the board during 2016.

6. THE NATURE OF THE IGC

Since April 2015, every workplace pension provider has had to establish an IGC, or a similar arrangement, under FCA rules. Royal London's IGC was established with effect from April 2015, and, as already mentioned, expanded in November 2016 through the recruitment of Myles Edwards.

6.1 Terms of reference

The scope of the committee covers assessing value for money for all of Royal London's relevant schemes and relevant customers. Relevant schemes and customers are defined by FCA regulations and are covered in more detail in the committee's terms of reference. The committee must report and escalate issues that are identified and provide annual reporting. In particular, the committee must act at all times solely in the interests of relevant customers. The full terms of reference for the committee can be found on Royal London's website **here**[9] .

6.2 Structure and recruitment

The committee is made up of both Royal London employees and independent members not previously connected to Royal London. This brings a range of experience and skills to the committee. The majority of members are independent and an independent member chairs the committee. As noted earlier in the report we have strengthened the balance of the independent members by the addition of a new independent member in 2016.

All independent committee members were assessed to be independent of Royal London according to FCA rules (i.e. not having been employed by or received payment for a role by any Royal London Group company in the five years preceding their appointment, nor having had a material business relationship of any description with the firm or with another company within the firm's group, either directly or indirectly, within the three years prior to appointment). This assessment continues to be reviewed at each committee meeting. Each independent member of the IGC has taken into account the FCA rules on independence above by considering those rules and being required to declare any reason why he or she may not be considered independent.

The two Royal London employee members of the committee are in no doubt that they are bound to act in accordance with the terms of reference of the IGC and must put aside the commercial interests of the firm when acting in their capacity as IGC members. Their contracts of employment reflect this requirement.

The current members of the IGC are as follows:

Phil Green, Independent Chairman
Phil has a broad range of experience in consumer-focused financial services in the UK and internationally. This includes 35 years in senior executive positions, predominantly with SunLife of Canada, AIG and Limra. He is currently the Non-Executive Director and Deputy Chairman of Wesleyan Assurance and Chairman of its With-Profits Committee.

David Gulland, Independent Member
David has a broad range of experience across the UK life insurance sector, with 25 years' experience as a consultant, followed by senior executive roles within the life insurance industry. He was the Chief Executive of Marine & General Mutual until that organisation's merger into Scottish Friendly on 1 June 2015. He is a Director, and the current Treasurer, of Investment & Life Assurance Group.

Peter Dorward, Independent Member
Peter has solid experience both in life insurance and institutional investments, having worked across a broad range of disciplines, including business leadership. He is now Managing Director of IC Select, a private limited company specialising in the evaluation of providers to UK pension funds. He currently holds two non-executive roles at the Citizens Advice Bureau – Chairman of the Board of Trustees, Central Borders, and Non-Executive Director, Scottish Borders Consortium.

Myles Edwards, Independent Member
Myles is a pension planholder, and therefore a member, of Royal London. Although this was a primary reason why he was appointed to the IGC, Myles brings significant experience and expertise built up during his 28 years working in financial services. Myles has a broad range of skills in product design, marketing and customer engagement and it is this wider customer focus which, along with being a Royal London customer, which makes him an ideal member of the IGC.

9 https://www.royallondon.com/igc

Isobel Langton, Chief Executive Officer, Royal London Intermediary
Isobel is the CEO of Royal London's intermediary business. Isobel's background is steeped in life and pensions. Having worked for Irish Life in a number of roles in the UK, she joined Royal London shortly after it acquired United Assurance Group (UAG) where she was responsible for integrating customer service for all of Royal London and UAG. As a member of the leadership team Isobel focused on customer experience and Business Transformation initiatives. In June 2012 Isobel was appointed Group Customer Services Director before becoming CEO of Royal London Intermediary in 2014.

Jon Macdonald, Group Risk Director, Royal London
Jon Macdonald was appointed to the Board on 14 December 2012 having joined the Group in November 2012 as Group Risk Director. He was previously Group Chief Risk Officer for both RSA and Prudential. He has held a number of senior risk and capital management roles at PwC, Aviva, Fox-Pitt Kelton, Swiss Re and Zurich and is a fellow of the Institute of Actuaries.

6.3 Chairman's views on skills and effectiveness of the committee

As Chairman of the IGC, I am satisfied with the appropriateness of the skills and expertise of the current members and the support provided by Royal London to the IGC throughout 2016.

A formal review of the effectiveness of the Committee was carried out during 2016. As a result of this review, I requested that Royal London expanded the number of independent IGC members to include a further individual with particular experience in understanding customer service and needs so as to strengthen the effectiveness of the IGC even further. This was done.

The Committee intends to continue to consider ways in which it can improve its work and act in the interests of Royal London workplace pension customers. During the period until the next annual report the committee will continue to oversee the projects in place and those planned by Royal London which are aimed at improving customers benefits. These include:

- Enabling customers to more easily understand the nature of their workplace pension, and to improve their level of engagement with Royal London
- Increase the level of information on transaction costs across all important investment funds, and develop a methodology for assessing their value for money against the funds' objective, and to benchmark their levels against comparator funds where possible
- Carry out further detailed reviews of the plan administration aspects of workplace pensions.

These projects will be in addition to the core continuing work on charges, investment management and other aspects of workplace pensions that we are required to do by regulation and under our Terms of Reference.

APPENDIX 1 SUMMARY INFORMATION AND STATISTICS

The information below summarises the scale of the changes to the size and mixture of Royal London's workplace pensions during 2016.

Workplace personal pension schemes

The number of employers with Royal London workplace personal pension schemes has increased significantly during the period. The figures below show the combined number of schemes administered through Royal London's Intermediary and Consumer Divisions.

	31 December 2015	31 December 2016	Change
Total workplace pension schemes[10]	17,399	22,038	26.7%
Workplace pension schemes subject to 0.75% charge cap[10]	5,014	12,047	140.3%

10. Workplace personal pension schemes include group personal pension plans and group stakeholder pension plans, but exclude occupational pension schemes and executive pension plans.

Workplace personal pension plans

The number of Royal London workplace personal pension plans held by customers jumped noticeably during the period. The figures below show the combined number of plans administered by Royal London's Intermediary and Consumer Divisions.

	31 December 2015	31 December 2016	Change
Total workplace pension plans[11]	576,900	767,000	33.0%
Workplace pension plans subject to 0.75% charge cap on default arrangement[12]	316,500	469,700	48.5%

11. Includes individual plans set up for customers who left employment and are no longer members of their former employers' workplace schemes. Members with multiple plans are counted separately for each plan. Plan numbers are rounded to the nearest 100.
12. This is the number of plans within automatic enrolment and qualifying schemes. Individual members could still make an active choice to select investments that carry additional charges or pay for financial advice that could take the total charges above 0.75%.

The vast majority of Royal London's workplace pension members are in modern low-charge products.

Product	31 December 2015	31 December 2016	Change
Retirement Solutions Group Personal Pension Plan[13]	455,300	643,700	41.4%
Retirement Solutions Stakeholder Pension Plan[13]	57,600	61,800	7.3%
Talisman Group Pension Plan (versions 1-6)[13]	34,000	32,600	-4.2%
Talisman Group Personal Pension Plan	1,700	1,600	-5.9%
CIS Group Stakeholder Pension Plan	9,500	9,200	-3.6%
Phoenix Life Group Stakeholder Pension Plan & Group Pension Plan[14]	18,800	18,200	-3.2%
Total[15]	576,900	767,000	33.0%

13. Includes members that have left service and have retained their own individual 'continuation' plan.
14. The number of members of the Phoenix Life Group Pension Plan is less than 100 members, so the figures have been amalgamated with the Stakeholder Pension Plan.
15. Figures rounded to nearest 100 members.

Nearly all new members in 2016 are invested in modern low-charge products.

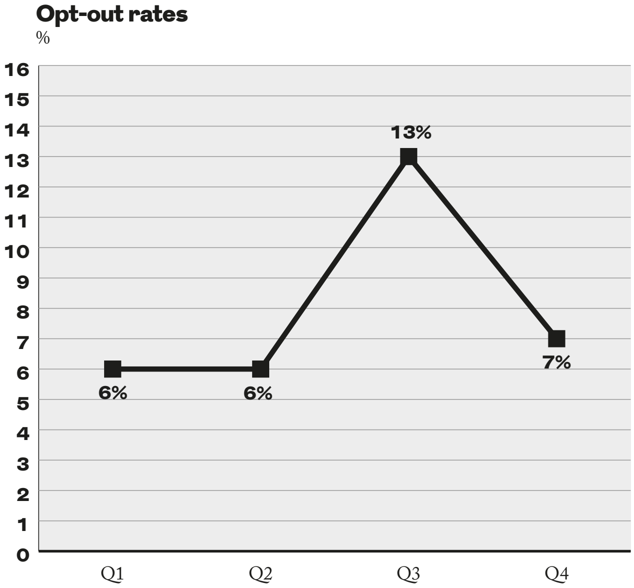
Product	New members
Retirement Solutions Group Personal Pension Plan	189,488
Retirement Solutions Stakeholder Pension Plan	5,579
Talisman Group Pension Plan (versions 1-6)	41
Talisman Group Personal Pension Plan	0[16]
CIS Group Stakeholder Pension Plan	94
Phoenix Life Group Stakeholder Pension Plan & Group Pension Plan	33
Total	195,235

16. The Talisman Group Personal Pension Plan is closed to new members

Automatic enrolment opt-out rates

The proportion of members that opted out of the employers automatic enrolment schemes has been low during each quarter of 2016 is as follows:

Opt-out rates



Member investment choice

An increasing proportion of Royal London's workplace pension scheme members are investing their pension contributions in their scheme's default arrangement. For members of automatic enrolment schemes, this means the charges are capped at 0.75% a year.

	31 December 2015	31 December 2016	Change
Proportion of members invested in scheme default[17]	82%	85%	3%

17. For most schemes, the default arrangement is a lifestyle strategy that 'de-risks' the members' pension plans by automatically switching into lower risk assets as the members approach their selected retirement ages. The figures relate specifically to Royal London Intermediary Pensions.

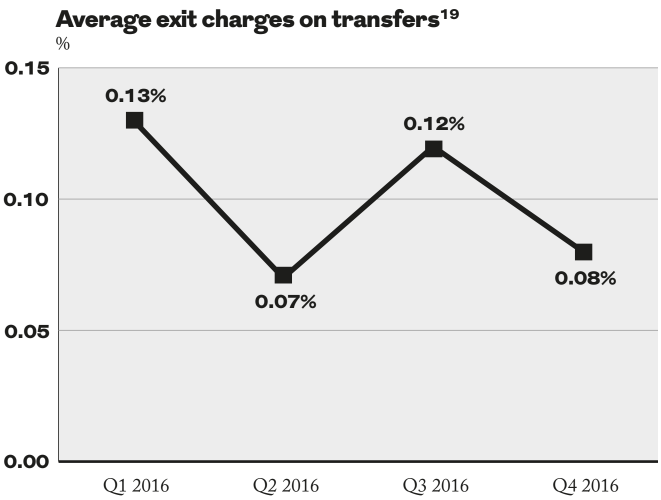
Product charges

The figures below show the average annual management charge (AMC) applying to funds built up from the current and/or previous regular contributions across all Royal London's workplace pension plans, the average AMC for new members and scheme leavers and the average exit charge for those members taking their benefits or transferring to another pension plan (where there was a charge).

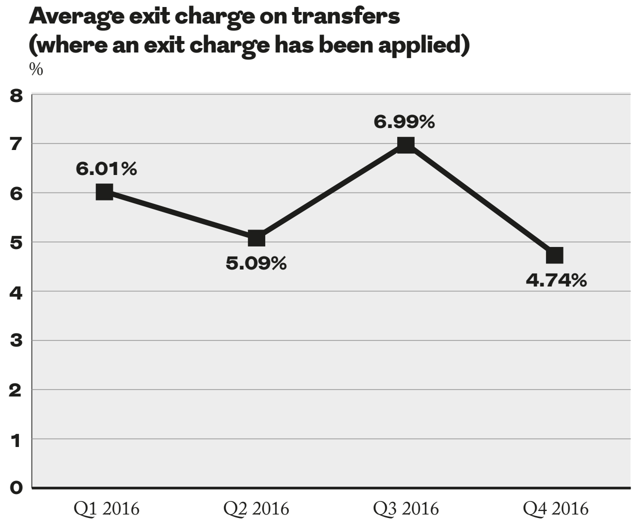
	31 December 2015	31 December 2016
Average AMC for all workplace pension plans[18]	0.74%	0.71%
Average AMC for new members[18]	0.69%	0.65%
Average AMC for scheme leavers[18]	0.68%	0.67%

18. All Royal London's workplace pension plans have an annual management charge. Some plans may also have additional charges, for example contribution-based charges, investment fund related charges and monetary member charges. These additional charges are not reflected in the figures above as they are not easily converted into an equivalent annual rate. They are however considered by the IGC when assessing value for money. Whether additional charges apply will depend on the specific product, the characteristics of the plan and the members' actions.

The vast majority (98%) of members transferring their pensions in the period had no exit charges. The following graph shows the average exit charge across all transfers:

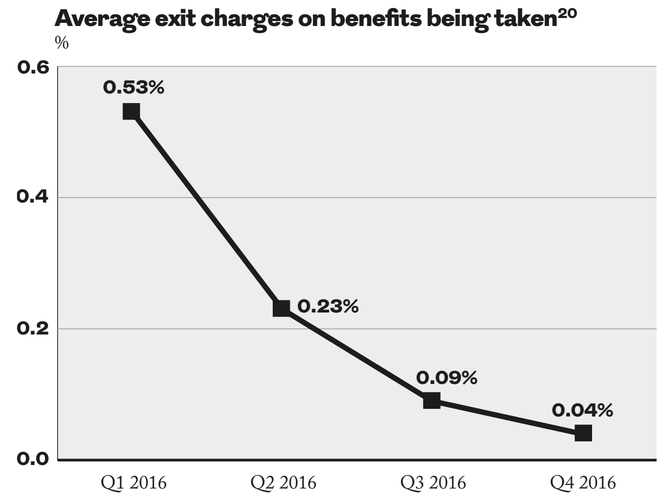


19. The figures are the averages across all transfers including those where no exit charges have been applied.



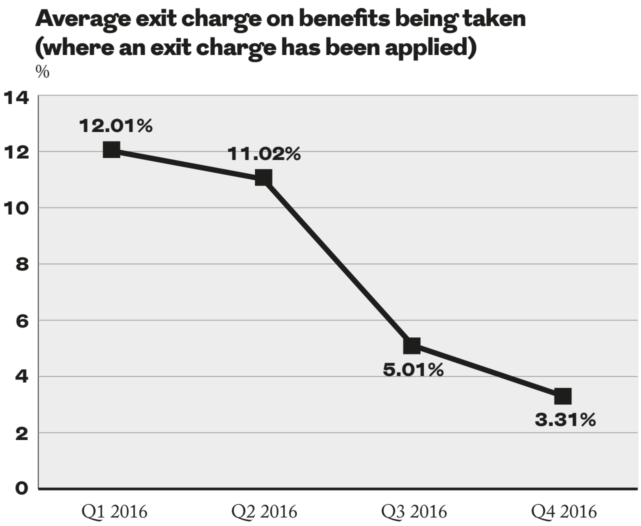
The impact of the improvements Royal London agreed to make to legacy workplace pensions in respect to exit charges on transfer is starting to show in the fourth quarter of 2016. This is as expected because the changes that reduce the size of relevant exit charges came into effect from 15 September 2016.

The impact of the improvements Royal London agreed to make to legacy workplace pensions in respect to exit charges has led to a significant reduction in these charges for customers accessing their pension benefits. Note that as with transfers nearly all members (98%) faced no exit charges for accessing their pensions.



20. The figures are the averages across all plans where benefits were taken including those where no exit charges have been applied.

The following graph shows the exit charge average where such a charge has been applied on benefits being taken.



The impact of the improvements Royal London agreed to make to legacy workplace pensions in respect to exit charges on taking benefits is starting to show strongly in the second half of 2016.

Note also that there are only a small number of plans where exit charges now apply and therefore the quarter on quarter figures can be impacted significantly by the circumstances of a small number of plans.

The reason for the exit charges is explained in appendix 4

Royal London publishes full details of its investment performance **online**[21].

This Appendix sets out some of the key figures from that information, as well as giving further details on Transaction Costs.

Summary investment performance tables

The table below shows performance against benchmark for the underlying Governed Portfolios used within the default lifestyle strategy. As a member approaches retirement the mix of the Governed Portfolios held in their account will change. Each Governed Portfolio in turn holds a variety of different asset classes, as explained in their fact sheets.

	Percentage Change					Compound Annual Growth Rate (%)		
Portfolio Name	31.12.15 31.12.16 % Chg	31.12.14 31.12.15 % Chg	31.12.13 31.12.14 % Chg	31.12.12 31.12.13 % Chg	31.12.11 31.12.12 % Chg	3 years	5 years	Since launch % Chg
Governed Portfolio 4	**15.08**	**3.77**	**8.28**	**17.22**	**9.07**	**8.94**	**10.56**	**117.19**
Composite benchmark	16.89	2.35	8.26	14.77	8.69	9.00	10.06	118.00
Difference	-1.81	1.42	0.02	2.45	0.38	-0.06	0.50	-0.81
Governed Portfolio 5	**13.97**	**3.17**	**8.40**	**14.33**	**9.32**	**8.41**	**9.75**	**110.86**
Composite benchmark	15.16	1.92	8.42	12.01	9.04	8.36	9.21	108.74
Difference	-1.19	1.25	-0.2	2.32	0.28	0.05	0.54	2.12
Governed Portfolio 6	**10.30**	**2.18**	**6.29**	**8.44**	**8.97**	**6.20**	**7.19**	**80.23**
Composite benchmark	10.41	0.94	6.86	6.60	8.64	5.99	6.64	74.57
Difference	-0.11	1.24	-0.57	1.84	0.33	0.21	0.55	5.66

Source: Lipper, bid to bid, as at 31.12.2016, Royal London, as at 31.12.2016. All performance figures shown have been calculated net of a 1% annual management charge. All performance figures shown have been calculated net of a 1% annual management charge. In practice customers will have some of this charge rebated to reflect the actual terms of their particular scheme.

Summary investment performance commentary

All portfolios continue to outperform over five years and are in line with benchmark over three years. Despite delivering strong absolute returns in 2016, relative performance over 12 months was poor.

The asset allocation process made a positive contribution to performance over the course of 2016 with relative returns benefitting from the overweight position in equities at the expense of short and medium-dated bonds and cash. However, the positive effect of this was outweighed by the negative impact of the following factors below:

- UK holdings within RLP Global Managed fund
- Overseas holdings within the RLP Global Managed fund
- Timing difference between RLP Global Managed and the benchmark
- Fixed interest performance.

21. https://adviser.royallondon.com/pensions/investment/fund-information/fund-performance/

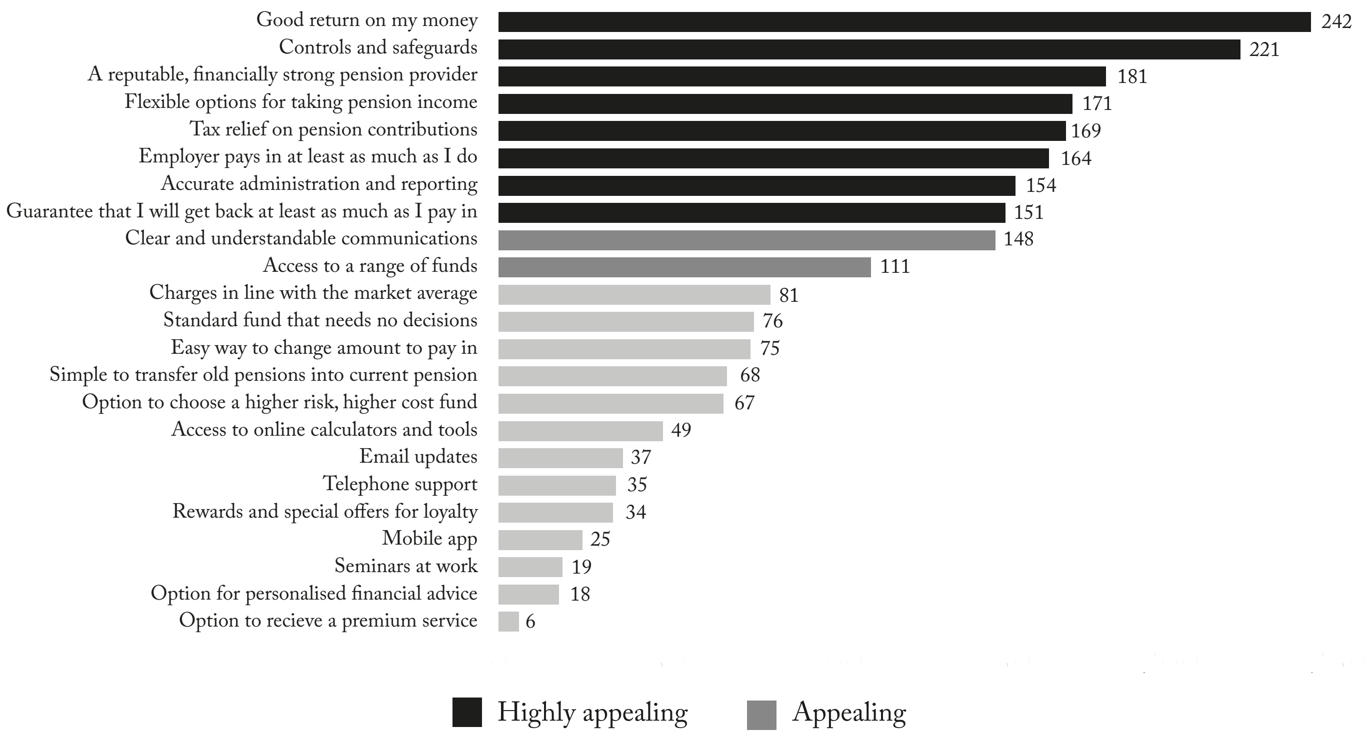
Sample transaction costs for 2016

The following table summarises transaction costs for the main Governed Portfolios, which make up Royal London's default lifestyle strategy, and some of the key component funds.

Fund	Commission	Tax	Legal fees	Other	Implicit Costs	Stock Lending Fees	Total Transaction Costs	Investment return over 2016 after all costs
GP4	0.029%	0.150%	0.006%	-0.014%	-0.089%	0.003%	0.083%	15.08%
GP5	0.024%	0.127%	0.005%	-0.012%	-0.123%	0.002%	0.024%	13.97%
GP6	0.018%	0.098%	0.004%	-0.006%	-0.146%	0.001%	-0.030%	10.30%
Global Managed	0.018%	0.057%	0%	-0.027%	-0.094%	0.004%	-0.043%	18.47%
UK Property Fund	0.093%	0.640%	0.033%	0.022%	0%	0%	0.789%	1.67%

This illustrates the wide variety of transaction costs due to the differing nature of the underlying assets, and the investment strategy being followed. High transaction costs on their own are not therefore an indication of poor performance.

Importance of attributes in terms of what Royal London customers want from their workplace pensions.



APPENDIX 4 EXIT CHARGES ON WORKPLACE PENSION CONTRACTS

The manufacture and sale of workplace pensions in the 1990s and early 2000s involved significant up-front costs. It was commonplace to recoup these costs, including the cost of commission to financial advisers, throughout the term of such contracts. If the contracts were terminated or made paid-up early then the outstanding costs were typically recovered by exit charges.

Modern contracts do not support commission payments so can be offered on a clean basis with no exit charge. The Government and the FCA confirmed in November 2016 that, from 31st March 2017 for those taking or transferring benefits when they are over 55, any exit charge has to be capped at 1% of the value of a member's benefit being taken, converted or transferred from the scheme. This was to promote pension freedoms rather than being based on any objection to the validity of such charges per se.

The cost of imposing this cap will be borne by Royal London's with profit customers and members. We have been provided with estimates of the expected cost and it is material. In addition to this regulatory cap, we are aware that Royal London are in dialogue with the FCA and ABI on how it may bring in a voluntary cap on exit charges for those who wish to transfer or convert their benefits before they are 55.

We have also been provided with estimates of the potential cost of implementing a voluntary cap for all exits in addition to the mandatory requirements. Again, as a mutual organisation, this cost would have to be borne by other customers of Royal London. Hence in our view, automatically extending the same 1% cap on exit charges to all workplace pension customers could lead to treating other customers unfairly and unnecessarily enhance the benefits for others.

Nonetheless we consider that taking proportionate voluntary action on exit charges during 2017 in respect of legacy workplace customers may be appropriate, in addition to that required by regulation. We have therefore been working with Royal London to study potential solutions that are fair across the range of customers.

APPENDIX 5 GLOSSARY OF CERTAIN TERMS

Annuity – an agreed sum of money paid to someone at regular intervals, typically for the rest of their life, in return for a lump sum.

Cross-subsidies – in this context is where a pricing policy of a product requires the charging of a higher price (or to make higher profit) from one group of customers to offset expected or potential loss from another group of customers. This can be necessary because not all assumptions about size and length of contribution period and investment will be right.

Ease Score – the "Ease" score measures how easy Royal London is to deal with. Customers are asked, on a scale of 0 and 10 (0 being not at all likely and 10 is extremely likely), "How easy would you say it was to deal with us today?". The "Ease" score is calculated as the percentage of customers who score 9 or 10.

Enhanced Annuity – an enhanced annuity is an annuity that provides a higher than normal level of income to the purchaser. To qualify for this type of annuity, the purchaser's state of health, medical history or lifestyle must be such that their life expectancy is lower than that of other annuity purchasers.

Implicit costs and market impact – when the fund manager is instructed to carry out a transaction it is important to do this at the best price possible. The available price may vary with the size of the sale or purchase, and it may also be possible to get different prices from various counter parties. Further, the actual price can vary between the time the order was made and when the transaction is actually carried out. The implicit costs and market impact item we have shown seeks to capture the impact of all of these features. The measurement of this item is of varying complexity depending on the nature of the asset – being more complex when robust independent market prices are not readily available at all times (for example property) and more straightforward for other more liquid assets (for example equities of major UK listed companies). Since prices can move up or down in the period between receiving instruction and implementation, it is possible for this item to be negative, that is it can increase overall investment returns rather than reduce them.

Legacy workplace contract – these are contracts which are no longer open to new business and which were designed and only actively promoted prior to April 2001 and are not available as an automatic enrolment or qualifying scheme.

Net pay arrangement – in this arrangement the employer takes the pension contribution and the government's contribution as tax relief from your pay before deducting tax. You pay tax on what's left. Under this arrangement if you don't pay tax, you don't get tax relief, for example because you earn less than the tax threshold.

Net promoter score – Net Promoter Score (NPS) measures how likely a customer is to recommend Royal London.

Qualitative research – qualitative research is primarily exploratory research, used to gain insights into the underlying reasons, opinions, attitudes, motivations, cultures or lifestyles of the customer. It aims to seek out "why".

Quantitative research – quantitative research is used to gather objective measurements and describes the statistical, mathematical, or numerical analysis of data collected through questionnaires, surveys and polls.

Regulatory capital – is the amount of capital a financial institution has to hold as required by its financial regulator.

Relief at source – in this arrangement the employer takes pension contribution from pay after deducting tax (and National Insurance contributions). The pension scheme provider then claims the tax back from the government at the basic rate of 20 per cent. This is added to the pension pot. If you don't pay income tax because you're on a low income, you automatically get tax relief.

Resolution Score – This score measures how well Royal London dealt with customer queries. Customers are asked, on a scale of 0 and 10 (0 is not at all likely and 10 is extremely likely), "To what extent do you agree or disagree that we were able to resolve all of your queries today?" The "Resolution" score is calculated as the percentage of customers who score 9 or 10.

Staging date – A date set in law by which an employer must meet their automatic enrolment duties. This date varies largely based on the size of the employer and their tax number.

Stock lending – stock lending is the act of loaning a stock, derivative or other security from the asset manager to an investor or other firm. The asset manager does this to generate additional income from the stock holding.

TER – Is short for Total Expense Ratio. This is a measure of the total cost of a fund to the investor. Total costs may include various fees (purchase, redemption, auditing) and other expenses. The TER is calculated by dividing the total annual cost by the fund's total assets averaged over that year, and is expressed as a percentage.

Unit-linked fund – is a form of pooled investment, combining customers' money together to buy units in a single asset or group of assets. Units in the fund are allocated to each customer depending on the amount of money they have invested and the price of the units at the time they are bought.

Unit price – the price of a single unit of a fund. The underlying assets within a fund will influence how the price of a unit will fluctuate. The amount a price can go up or down by is dependent on the movement of the underlying assets within the fund.