ROYAL LONDON SAVINGS LIMITED

# Pillar 3 Disclosure

## 31 December 2021

# Contents

# 1. Introduction

## Background

The Capital Requirements Directive (CRD) and Capital Requirements Regulation (CRR) – usually referred to together as CRD IV – formalised the regulations for investment firms to disclose additional information relating to their risk management approach and capital adequacy. The aim of the CRD IV is to promote the market standards for information disclosures which ensure clarity, meaningfulness, consistency over time and comparability across different institutions.

The disclosure of this information is known as Pillar 3 and is designed to complement the two other pillars of the CRD, namely the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2). The disclosure has been prepared in accordance with the requirements laid out in Part 8 of the CRR.

The three pillars are summarised below:

- Pillar 1 – Sets out the minimum capital requirements, through the application of measurement rules, of firms to cover credit, market and operational risk;
- Pillar 2 – Requires firms to undertake an Internal Capital Adequacy Assessment Process (ICAAP) to determine whether the financial institution needs to hold additional capital against risks not adequately covered in Pillar 1; and
- Pillar 3 – Complements the other two pillars and effects market discipline through public disclosure showing an institution's risk management policies, approach to capital management, capital resources and an analysis of its credit risk exposures.

This statement is for the financial year ended 31 December 2021 and as such will be the last issued under CRD IV. Starting from financial years commencing 1 January 2022, RLS will be applying disclosure requirements as set out within the new Investment Firm Prudential Regime (IFPR).

Royal London Savings Limited (RLS) was established in November 1998 and is a subsidiary of The Royal London Mutual Insurance Society Limited (RLMIS). The Board is supported in its duties by the operation of staff within Royal London Asset Management (RLAM) and RLMIS to provide an appropriate level of oversight and governance. RLS is authorised and regulated by the Financial Conduct Authority (FCA) and is categorised as a non-significant investment firm under IFPRU 1.2.3.

The principal activities of the company were, initially, to act as the marketing associate for the sale of Individual Savings Account (ISA) products and to act as the ISA manager for those products. During 2004 the company ceased to sell ISA business and it now acts as an ISA manager for those products previously sold.

RLS manages the legacy book of ISA business previously sold by the direct sales force of RLMIS from 1999 to 2004. No new business is taken on and the only income received is commission on an on-going basis comprising increments to existing products.

Whilst the administration of this book of business was originally undertaken internally within the Royal London Group, this activity has since been outsourced. The administration of this book of business is undertaken by Link Asset Services.

With effect from 1 October 2021, RLS also acts as an ISA manager for the life insurance ISAs provided by Royal London (CIS) that were until this date managed by RL Marketing (CIS) Limited. The administration of this book of business is undertaken by Capita.

## 2. Governance

As part of RLMIS, RLS is subject to the formal governance hierarchy that is in place across the Royal London Group to ensure effective escalation of issues through different business lines. The principal decision-making body for RLS is the RLS Board; its Board of Directors are responsible for the ICAAP. The responsibility for governance and business oversight rests with the directors of RLS and the relevant FCA Approved Persons.

The FCA's Principle for Business No. 3 requires the Directors to take reasonable care to organise and control the affairs of the company responsibly and effectively, with adequate risk management systems.

The RLS Board of Directors has responsibility for the overall risk governance and management of RLS. The RLMIS Board has ultimate responsibility to define the Royal London Group's risk appetite, benchmarks, tolerances and underlying limit controls.

As a wholly owned subsidiary of RLMIS, RLS adheres to the risk management objectives and policies set out for companies within the Royal London Group. The Annual Report and Accounts for RLMIS detail the governance structure in place for the Royal London Group and the approach taken to risk management generally. This specifically covers the Royal London Group's management of the various categories of risk faced by the Group.

The Annual Report and Accounts for RLMIS can be found on the Royal London website at www.royallondon.com/about-us/corporate-information/key-financial-information/annual-reports/

The RLS Board of Directors determines whether actual performance was above, below or in line with RLS' tolerance level. They determine whether any adjustments need to be made, either to the statement of risk appetite, budget or forthcoming business plan. The Royal London Group maintains a Risk Appetite statement which is applicable to all Royal London Group entities, including RLS.

The RLS Board is responsible for setting the RLS strategy and ensuring that all key risks are effectively and efficiently controlled. Systems of internal control are designed to ensure effective and efficient operations, including financial reporting, and compliance with laws and regulations. The RLS Board delegates responsibility for the implementation of the RLS strategy and the day to day management of risk to senior management working on its behalf.

The remuneration policy of RLS is under the oversight of the Group's Remuneration Committee. Information on the remuneration policy, the link between pay and performance, and quantitative information can be found on the Royal London website at:

http://www.royallondon.com/about/corporategovernance/remuneration/

# 3. Disclosure

This information has been prepared purely for the purpose of explaining the basis on which RLS has prepared and disclosed certain capital requirements and information about the management of risks relating to those requirements, and for no other purpose. It therefore does not constitute any form of financial statement on RLS nor does it constitute any form of contemporary or forward-looking record or opinion of the RLS business.

These disclosures have been taken from historical and projected information based on the year end statutory accounts as at 31 December 2021.

RLS regards information as material in disclosures if its omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions. If RLS deems a certain disclosure to be immaterial, it may be omitted from this Statement.

RLS regards information as proprietary if sharing that information with the public would undermine its competitive position. Proprietary information may include information on products or systems which, if shared with competitors, would render the firm’s investments therein less valuable. Further, RLS must regard information as confidential if there are obligations to customers or other counterparty relationships binding the firm to confidentiality. In the event that any such information is omitted, we shall disclose such and explain the grounds why it has not been disclosed.

This information has been subject to internal review but has not been audited by the Group’s external auditors.

Although Pillar 3 disclosures are intended to provide transparent capital disclosures on a common basis, the information contained in this document may not be directly comparable with other companies of a similar nature.

This disclosure document has been provided by RLS in accordance with the requirements of Pillar 3 and Part Eight of the Capital Requirements Regulations (CRD IV) (Articles 431-455). Unless otherwise stated, all figures are as at 31st December 2021.

## 4. Risk Management Objectives and Policies

RLS, as a separate subsidiary of RLMIS, follows the Governance principles and practices prescribed by the Group. The Group's approach to risk management can be found within the notes to the Group's Annual Report and Accounts, which may be accessed at https://www.royallondon.com/about-us/corporate-information/key-financial-information/annual-reports/

All functions supporting the RLS operation have participated and self assessed their own risks and these assessments are subject to challenge from Group Risk. Senior management have acted proactively in identifying the material risks and assessing the capital requirements taking into account the future business and risk profile. The Board receives regular information to help it determine whether effective risk mitigation is being achieved.

The ICAAP is formally reviewed by the Board.

For financial years commencing 1 January 2022, RLS is implementing the new IFPR. As part of the new regime, ICAAP will be replaced by an ICARA (Internal Capital Adequacy and Risk Assessment) process. This will see RLS refocus its assessments from the risks it faces to also consider and mitigate the potential for harm it can pose to consumers and markets.

## 5. Key Risks

In addition to the capital adequacy reporting requirements of the Financial Conduct Authority, RLS has prepared an ICAAP. The ICAAP, which sets out RLS' approach to assessing the adequacy of its internal capital combined with a range of stress testing scenarios, is subject to at least annual review by the RLS Board and any material events that may impact the ICAAP are subsequently raised at the appropriate Board Meeting.

Senior management intend to manage the RLS capital base so that the majority of assessed risks have sufficient capital provided to allow RLS to maintain its business without further capital injection. The Board meet regularly and receive quarterly financial reports on capital availability.

The paragraphs below show RLS' defined risk categories and provide a statement of the level of risk exposure assessment, together with a summary of the risk mitigants in place where applicable.

### 5.1. Credit Risk

Credit risk is defined as the loss resulting from a counterparty's failure to repay amounts in full when due. All of RLS' investment holdings are in an open-ended investment company (OIEC); the majority of investments are short dated, highly liquid and high quality. Fees and other balances due from clients are regularly reviewed and the potential impact on the profit and loss account is evaluated on a monthly basis. All amounts that have been recognised to be at risk or overdue for more than 90 days are monitored regularly, but, as the majority of fees are deducted from funds under management, there is no history of RLS being unable to recover debts.

*Concentration risk*

Concentration risk is any single or group of exposures that may have the potential to produce losses large enough to threaten an institutions' health or ability to maintain its core business. This includes large (connected) individual exposures or significant exposures to groups of counterparts, whose likelihood of default is driven by common underlying factors, e.g. sector, economy, geographical location and instrument type.

The exposures within RLS are considered to be quite small, due to the small period of time between trading and settlement. No amounts held are significant enough to threaten the ability of RLS to continue business and there is no significant concentration to an individual counterparty. As a result the nature of RLS' business gives rise to low exposure to this risk.

### 5.2. Market Risk

Market risk is the risk of loss arising from fluctuations in the value of assets or income. RLS does not hold investments in its own name and as a Limited License Investment Firm does not hold the necessary permissions to trade on its own behalf. Therefore the exposure to market risk is low. Where RLS is exposed to the impact of market changes is through its funds under management which are managed on its behalf by RLAM via OEICs. The impact of these market movements on RLS' fee income is considered within the stress tests. No capital is set aside for Market Risk in either Pillar 1 or 2.

## 5.3. Operational Risk

Operational risk is the risk of loss or negative impact to RLS resulting from inadequate or failed internal processes, people and systems or from external events (such as regulation, business environment). This includes legal and financial crime risks.

These operational risks have been identified through assessments and scenario analysis. Due to the nature of RLS' operations, the key operational risks for RLS are in relation to the outsourcing of key activities to:

- Royal London Group Functions, e.g. for the provision of financial reporting, compliance with regulatory requirements as well as operational oversight;
- RLAM with regard to the management of investments; and
- Third Party outsourcers for administrative handling of the ISA book of business.

A strong control environment, supported by skilled staff, is designed to mitigate the possibility of these risks materialising. This ensures that regulatory returns and statutory accounts are promptly and accurately completed, SLAs setting out the quality of service to be provided to RLS are in place and monitoring of service standards are regularly undertaken.

## 5.4. Liquidity Risk

This represents the risk that adequate liquid funds are not available to settle liabilities or when the firm experiences sudden unexpected cash outflows. For the purposes of the ICAAP, the approach adopted by RLS has been incorporated into the projection of cash flows and the adaptation of these to stressed environments. The majority of RLS assets are held in high quality, highly liquid, short-dated cash instruments and there is limited liquidity risk exposure. At a minimum, RLS holds sufficient Tier 1 capital in cash which provides assurance that enough liquid funds are available if this type of risk were to crystallise.

## 5.5. Business Risk (earnings and costs)

The risk arises from changes in the firm's business, including the risk that the firm may not be able to carry out its business plan and its desired strategy. In a narrow sense, business risk is the risk to a firm that it suffers loss because its income falls or is volatile relative to its fixed cost base. Other than a significant change in business strategy, probably leading to a wind down, RLS as a closed book of business does not deem it necessary to carry capital for business risk.

## 5.6. Interest rate risk arising from non-trading activities

RLS is exposed to risks to earnings and capital arising from adverse movements in interest rates. RLS holds investments in highly liquid cash instruments via an OEIC; the interest income from which is affected by interest rates. Whilst the risk is acknowledged, it is considered that any movements in interest rates are unlikely to have a material impact on RLS.

## 5.7. Pension obligation risk

Pension risk is the risk resulting from the firm's contractual liabilities or moral obligations with respect to a pension scheme. RLS is part of the Royal London Group which has a defined benefit pensions scheme that scheme closed to future accruals on 1 April 2016, the Royal London Group Pension Scheme (RLGPS). The responsibility for cash injections arising as a result of the Trustees' funding decisions, Section 75 employer debt provisions or any other reasons lies with RLMIS. The triennial valuation of RLGPS as at the end of 2019 concluded that the scheme had a funding surplus therefore no capital injections were required. RLMIS continues to set aside capital against pension obligation risk therefore there is no additional capital provision held for this risk in RLS.

## 5.8. Contagion risk

Contagion (or Group) risk is the risk that the financial position of the firm could be adversely affected by its relationship with other entities in the same group or by risks which may affect the financial position of the whole group. The Royal London Group offers a diverse product range and operates across a number of market sectors, and the different legal entities forming the Royal London Group do not reflect a uniform front that would be materially impacted by contagion. However, legal entities within the group operate under the same brand. It is recognised that in case of a reputational event and subsequent negative publicity relating to the Royal London brand could result in some impact on RLS. However, RLS is a company in run-off maintaining its own policies and procedures and is supported by RLAM with a discrete investment management business and is therefore unlikely to be affected by contagion risk. All of the Companies within the Group set aside appropriate risk capital within their individual prudential requirements, or within the RLMIS Group Solvency II submission.

# 6. Capital Requirements and Resources

## 6.1 Capital requirement

As at 31 December 2021, RLS' Pillar 1 capital requirement was £0.1m being the higher of its base own funds requirement of €125k, fixed overhead requirement and the total of its credit risk requirements.

The fixed overhead requirement was calculated at 25% of relevant expenditure. Credit risk is calculated using the Risk Weighted Assets Approach as per the relevant CRR articles. The credit risk exposure values were calculated according to the table below: -

| | Risk weighting | £m |
|---|---|---|
| Current assets | 20% - 75% | |
| **Total at 8% capital requirement** | | **0.1** |

## 6.2 Capital resources

As at 31 December 2021, Tier 1 capital after deductions was £4.2m which consisted of paid up share capital of £2m plus £2.2m of disclosed reserves and audited retained profits.

| Tier | Element | £m |
|---|---|---|
| Tier 1 | Paid up share capital | **2.0** |
| | Disclosed reserves & current year's retained profits (verified by external auditor) | **2.2** |
| | Total Tier 1 Capital | **4.2** |
| Tier 2 | Total Tier 2 Capital | **-** |
| | Total deductions | **-** |
| | Total capital base | **4.2** |

At 31 December 2021, RLS therefore held £4.1m of capital in excess of its Pillar 1 requirement and throughout the year, RLS complied with its individual capital requirements as set out by the FCA.

## Summary

The Board has concluded that RLS has sufficient financial resources in terms of both capital and liquidity to ensure that there is no significant risk that its liabilities cannot be met as they fall due.

## 7. Notices

These disclosures were approved for publication by the RLS Board on 21 April 2022 and are subject to periodic review and update. The information contained in this disclosure has not been audited by RLS's external auditors.

RLS is a subsidiary of the RLMIS and is authorised and regulated by the Financial Conduct Authority (reference number 191237). The registered office address of the company is 55 Gracechurch Street, London EC3V 0RL.