REDINGTON

THE DEFINED CONTRARIAN

A fresh perspective on Defined Contribution pensions

Q2: 2020

FRESH PERSPECTIVES, GROUNDED IN A LOGICAL METHODOLOGIES

As our world becomes more complex, a clear perspective based on fresh insight has never been more important. In this document we seek to strike the right balance of great insight that doesn't just follow the heard with a deeply grounded logical methodology.

Events of this first quarter have certainly kept decision makers very busy, including those of Defined Contribution (DC) pension schemes.

In this roundup we will provide a summary not just on the events that relate to the effects of COVID-19 but other topics such as ESG and Independent Governance Committees' (IGCs), that remain important during these unprecedented times.

If you have any questions or want to dig a little deeper into a particular area, please do not hesitate to get in touch.

INDEPENDENT GOVERNANCE COMMITTEES: ANNUAL REPORT

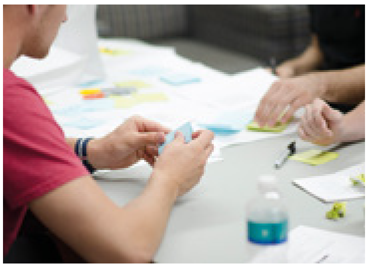
It's IGC reporting season and most annual reports have now been published.
We've summarised some interesting findings from each of the main reports and links:

PROVIDER NAME (Click for link to reports)	**REPORT PUBLISHED**	**OBSERVATIONS**
Aegon	✓	• Helen Parker joined the IGC as an Independent Member during 2020. • IGC believes value for money is being delivered with some noted improvement on previous years. • IGC are working with Aegon to further understand its policy on ESG and how managing these financial risks can improve customer outcomes.
Aviva	✓	• There were no personnel changes to the IGC made over the year. • Value for money assessment indicates good value is being provided across policies with further focus on improvements to older policies. • Aviva are looking to deliver climate friendly default funds by the end of 2021.
Fidelity	✓	• Rachel Brougham resigned from the board in October 2019 and David Felder retired at the end of March 2020. Dianne Day and Gerald Wellesley subsequently appointed. • IGC believes value for money continues to be delivered through the quality of investment review and monitoring processes however does note several areas do not fully meet expectations, notably communications. • IGC are actively engaged in considering ESG; FutureWise was given an average ESG rating and a high response rate noted for a member ESG survey with results to be scrutinised.
Legal & General	✓	• Kim Brown joined in February 2020 as Pension Scheme Director to replace Adrian Spann, and Sarah Pengilley joined in January 2020 as a second Pension Scheme Manager, working alongside Tessa Watson. • IGC concluded L&G offer good to very good value for money and pleased that the range of default funds was comprehensively reviewed and improved, moving 75,000 members into a more modern and diversified default fund – the Multi-Asset Fund. • IGC expecting an emerging theme of increasing exposure to ESG within default strategies.
Old Mutual	✓	• Jon Greer and Anthony Scammell left the IGC on 31 December 2019 following ReAssure's acquisition Old Mutual Wealth. • IGC considers value for money has been maintained during the year with improvements seen in communications and engagement. Value for money will subsequently be reviewed by ReAssure's IGC. • During 2019 Quilter, the parent company of Old Mutual Wealth, formed a working group to consider how they can embed responsible investment (including ESG) principles across their business.

PROVIDER NAME (Click for link to reports)	REPORT PUBLISHED	OBSERVATIONS
[Phoenix Life]	✓	• IGC members were aligned with Standard Life in April 2019 (See Standard Life below). • Notable improvements in governance and investment performance, along with communications enabled Phoenix to conclude it offers value for money. • Over the last year, Phoenix Group has made significant progress to embed ESG considerations (as part of wider "Sustainability" developments) into its business practices, particularly around investment of customer money.
[Prudential]	✓	• There were no personnel changes to the IGC made over the year. • IGC believe good value for money is being achieved and state 'better value than 5 years ago' however noted a possible increase to charges in the future which the IGC are watching closely. • IGC note Prudential are making some short-term changes regarding ESG as the longer-term view develops. Prudential believes it should take responsibility for ensuring the default solutions offered take appropriate account of ESG factors and embed ESG strategy within.
[ReAssure]	✓	• Following the August 2019 announcement that Old Mutual Wealth Life Assurance Limited and its subsidiary, Old Mutual Wealth Pensions Trustees Limited, would be sold to ReAssure, the deal completed on 31 December 2019. • 1% charge caps implemented in 2017 are leading to improved value for money outcomes for members and customer service improvements also benefiting members. • ReAssure have developed and adopted a new ESG policy which IGC will report on next year.
[Royal London]	✓	• Jon Macdonald resigned from the IGC on 26 April 2019. Elizabeth Boardall (head of Customer Engagement Communications in Royal London's legacy team) filled the role of non-independent member from June 2019 – October 2019. Cat Read was then appointed to replace Elizabeth as a non-independent member of the IGC on 10 December 2019. • Investment returns led to an improvement in the value for money rating. • The IGC received regular updates on Royal London's approach to Environmental, Social and Governance (ESG) issues including Climate Change, in anticipation of greater focus on this in 2020.
[Scottish Widows]	✓	• Babloo Ramamurthy ended his term as chair of the committee and was succeeded by Mark Stewart from 1st January 2020. Babloo will remain as a committee member for a short period whilst a new Independent Member of the committee is recruited. • IGC considers Scottish Widows to have access to good product features with reasonable charges that overall represent good VFM. • IGC were encouraged that Scottish Widows has recently significantly increased the number of people in their investment team that will be focused on ESG.
[Standard Life]	✓	• Following Phoenix Group's acquisition of Standard Life Assurance Limited, the Boards of Phoenix and Standard Life decided to align the membership of their respective IGCs, resulting in the appointment of the previous Phoenix IGC chair, Dr David Hare, to chair the aligned IGC with effect from April 2019. • The IGC saw improvements in value for money scoring, with investment and customer services noted as more favourable. • IGC wish to have more visibility of how ESG considerations impact in-scope members' funds.
[Zurich Assurance]	✓	• Anita Fernqvist joined the IGC during 2019. • Value for money rating remains Amber and further improvement across 2 of 3 key areas were highlighted: Investments and enabling members. • IGC continue to monitor the implementation of Zurich's ESG policy as it continues to be developed.

SO WHAT?

IGCs have a challenging role in assessing 100s or even 1000s of workplace pension arrangements. This has just gotten even tougher with the introduction of new FCA rules which broaden responsibilities to include ESG and post-retirement. We would recommend asking your DC provider to comment on the IGC report at your next governance meeting.



EXTENSION OF REMIT

With effect from 6 April 2020 the FCA has extended the remit of IGCs with:

- a new duty to consider and report on their firm's policies on environmental, social and governance (ESG) issues, member concerns, and stewardship; and
- a new duty to oversee the value for money of investment pathway solutions for pension drawdown (pathway solutions).

The policy statement can be found here.

From October 2020 trustees must produce an implementation report

STATEMENT OF INVESTMENT PRINCIPLES (SIP) IMPLEMENTATION REPORTS

Following changes to legislation for DC schemes, The Pensions Regulator (TPR) guidance was updated requiring trustees to make their Statement of Investment Principles (SIP) available free of charge on a website from October 2019.

Importantly, we wish to remind you that from October 2020 trustees must produce an implementation report which explains how they have followed and acted on the investment policies outlined in the SIP.

This is a brand new document which most DC trustees are required to produce.

The updated guidance also provides further clarity around what is meant by financial material considerations, stewardship and provides more information about preparing an implementation statement. A link to the SIP section can be found here.

OTHER REGULATORY NEWS

FCA's Pensions and Retirement Income Guidance

April 2020 saw the publication of guidance to help DC pension providers have the right kind of discussions with their customers when having meaningful conversations about the risks and implications of changing or accessing their pension in the current circumstances. The guidance also highlights what firms are already required to do (Retirement Risk Warning rules (COBS 19.7)).

Investment Pathways Delay

The Financial Conduct Authority (FCA) has delayed the introduction of investment pathways until February 2021.

Climate Change Disclosures

During March, the Financial Conduct Authority (FCA) published proposals (CP 20/3) outlining new climate-related disclosure requirements for premium listed issuers. The approach taken would be based on those set out by the Taskforce on Climate-related Financial Disclosures (TCFD). The consultation period was set to end on 5 June 2020 with the policy statement published before the 26th session of the Conference of the Parties (COP 26) in Glasgow. Unfortunately, both of these have fallen victim to COVID-19, so the consultation for the FCA has been put back to October 2020.

GROWTH STAGE DEFAULT PERFORMANCE (40YRS FROM RETIREMENT)

We have assessed eight leading DC providers (including master trusts) over a three-year period, focusing on members who are 40-years from retirement and in the growth stage of the default. With more than 95% of members of trust-based schemes invested in their default, we have highlighted the importance of making sure you have the most suitable default in place to achieve the best outcomes for your members.

FIGURE 1.1

Default Growth Stage Performance of Workplace Pension Schemes 3-Year Period (to 8th May 2020)

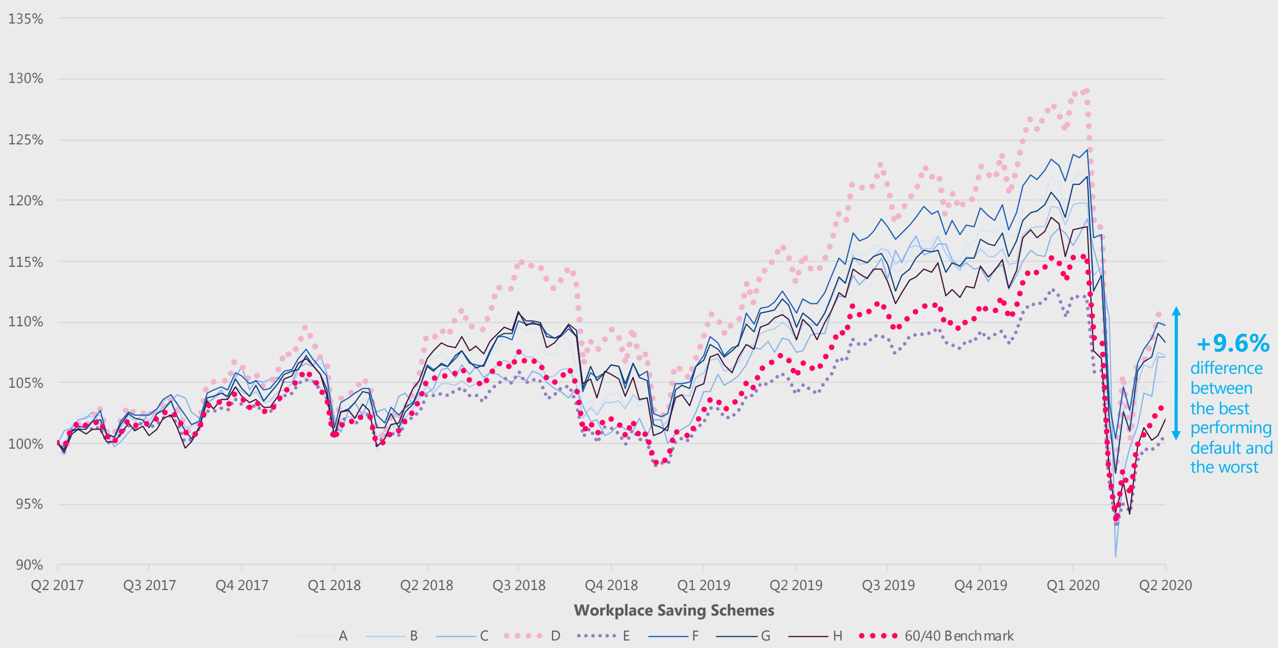
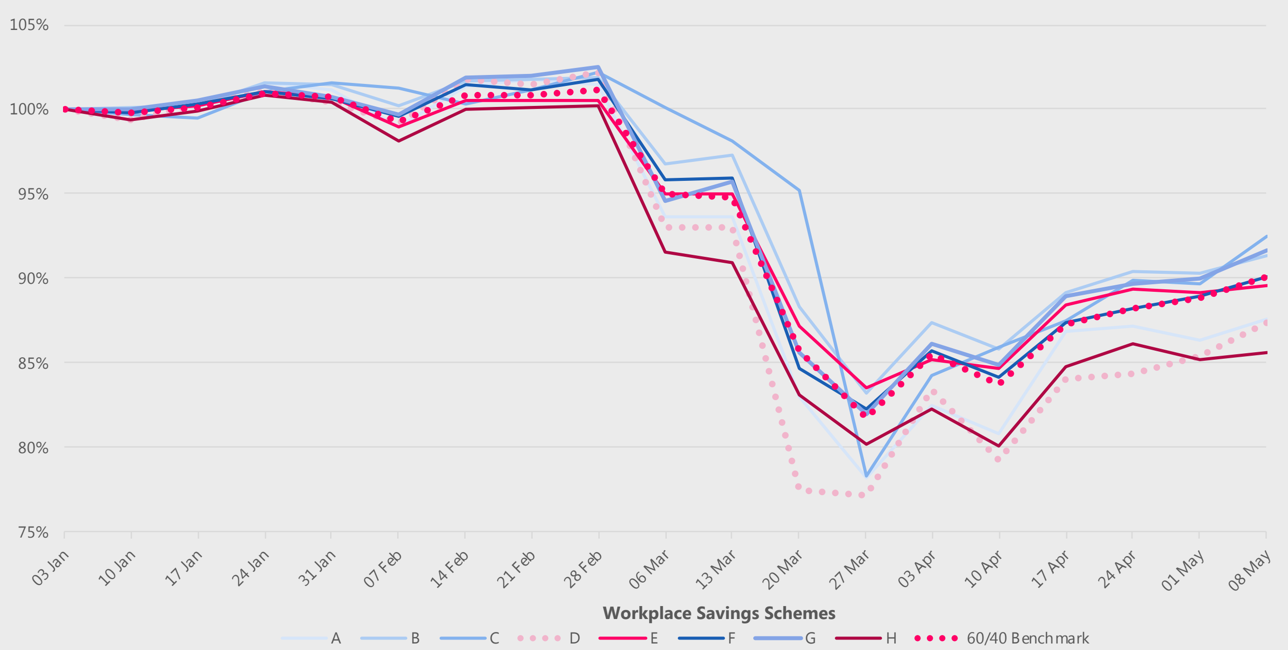


FIGURE 1.2

Default Growth Stage Performance of Workplace Pension Schemes YTD (to 8th May 2020)



95%

of members invest in their default investment strategies

- Millennial members across the various defaults have seen a broad range of outcomes to their pot size over the last 3-years (Figure 1.1). Notably, there is a significant difference between the top performing default strategy (D) and the strategy which has been outperformed by all (E), c.10% difference.
- The disparity can largely be attributed to the variation in asset classes both schemes use in their growth phase. Strategy D has benefited from its c.95% equity allocation vs Strategy E, which operates a more diversified asset approach, investing across a range of asset classes and only allocating c.55% of its overall portfolio to equities.
- Graph 1.2 demonstrates the variation between the rocky journey experienced across the strategies during the COVID-19 pandemic. As expected, Strategy D's high risk approach would have seen a greater fall during the height of the crisis however experienced a significantly greater 'bounce-back' compared with a strategy that takes a more diversified approach (60/40 Benchmark).

SO WHAT?

We believe it is materially beneficial, for members and those with responsability of the scheme, to be aware of the risk that is being adopted at various points in the member journey. Notably, 40 years out from retirement, members are more likely to be able to ride the volatility and take greater risk.

COVID-19

Property Funds

Following widespread suspension of direct property funds, due to the material uncertainty in physical property values, it is important to consider both the immediate remedial action and the proposed action(s) to take for when suspensions are lifted, whether the property fund is a self-select fund option or is included within the default strategy. It is not the first time the illiquid nature of direct property funds has been experienced within the UK and recent suspensions follow those of the previous financial crisis and in the lead up to Brexit.

Any trustees deciding to temporarily divert member contributions into say a cash or money market fund should take legal advice around the possibility of this alternative becoming an 'accidental default', which might have knock-on governance implications.

Stay ahead of scammers with ScamSmart

Scams

Sadly, during a period of crisis, there are increased opportunities for scammers to target individuals and families coming under financial pressures. This, combined with remote working of administrative staff, could potentially lead to an increased risk of pensions liberation cases, so it is even more important than ever to ensure checks are carried out. The Financial Conduct Authority's (FCA) ScamSmart webpage offers a useful resource for members and please also find a link to the pension scams leaflet.

Useful Links to COVID-19 Guidance and Updates from:

- The Pensions Regulator (TPR)

Finally, our best wishes to you and your families. We sincerely hope you are all safe and healthy. If we can be of any assistance, please do not hesitate to get in touch.

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