

**Response from
the Independent Governance Committee (“IGC”) of Phoenix Life Limited, Phoenix Life
Assurance Limited, ReAssure Limited, ReAssure Life Limited and Standard Life
Assurance Limited**

**to
FCA and TPR Joint Discussion Paper DP21/3
“Driving value for money in defined contribution pensions”**

Introductory comments

The IGC is grateful for the opportunity to respond to the FCA’s Discussion Paper, joint with TPR, DP21/3. We are supportive of any developments that increase, in a proportionate and effective way, the amount of benchmarking information that we can use in our value for money assessments. However, before presenting our responses to the questions posed in the DP, we would wish to highlight two points:

1. We would urge caution over the apparent emphasis on “backward-looking metrics” in the DP (cf paras 25 and 26). We see the concept in COBS of “ongoing value for money” as being a forward-looking measure that, in particular, depends on culture and effective governance. While past performance can be helpful in a number of ways, it is not a guide to the future.
2. We would find it helpful if the FCA and TPR could be clearer over what the value for money (VFM) issue(s) are. Both the FCA and TPR have stated that for them, “delivering VFM in pensions is a key strategic priority”. Does this priority focus on the outcomes that contract-based workplace customers are getting, or only on the benchmarking evidence that exists across the industry? Given the price of workplace pension savings plans compared to other retail savings products, it is not immediately obvious that the VFM issues identified by the IPB in 2014 are still a feature of the marketplace. Is it the outcomes being delivered in other areas of the pensions landscape that are of greater concern to the two regulators?

	Question	Response
1	Do you agree that consistent disclosure of performance is necessary to enable better decision making?	Consistent disclosure of performance would certainly be helpful to decision-making about VFM. However, this information alone is not sufficient to enable better decision making, as it does not provide insight into key issues, such as the design of the strategic asset allocation (SAA) being followed or the risk level targeted. Performance data on its own also does not necessarily tell the user about how effective investment governance processes are at dealing with any periods of underperformance. Finally, comparison of historic investment performance across different providers could be very misleading, where the metrics tracked ignore the impacts of life-styling strategies.
2	Do you agree that comparisons should be of net rather than gross investment performance?	Yes, ideally, but net of which charges? How do you have meaningful comparisons when charges vary by scheme size and quality? It would be much more effective to show gross performance figures, and then the range of charges to deduct in order to get net performance.

3	<p>Do you have any suggestions on how to make disclosure of net investment returns effective given that there may be varying charges for the same funds within multi-employer schemes? For example displaying a range, or requiring disclosure of each level of net investment performance?</p>	<p>See answer to question 2. Given the range of charges that can apply, disclosure of net investment returns alone is not going to be effective, unless it is straightforward for a pension saver to see which net performance figure applies to their pension pot.</p> <p>Where the gross investment performance is the same, irrespective of the level of charges that apply to individual pension pots, what additional insight would be gained by showing each level of net investment performance?</p> <p>A possible compromise might be to require performance to be quoted net of a standardised level of charge for comparison purposes (which would at least acknowledge that no-one receives gross returns), alongside the range of charges actually incurred.</p>
4	<p>Would it be helpful to mirror the DWP's approach in terms of reporting periods?</p>	<p>Perhaps, but SAAs change over time, so 10, 15 and 20 year historic performance is likely not to tell the user much about the appropriateness of the current SAA or the effectiveness of its implementation. Also, the impact of life-styling strategies in the later years of accumulation (which are not restricted just to annuity-targeting, but which could be targeted on a range of outcomes) mean that simple comparisons of historic performance are of limited relevance to many/most users.</p>
5	<p>Would publishing a set of metrics based on age cohorts bring investment performance reporting closer to the saver's investment performance experience of a pension scheme/product? If not, is there a better alternative we have not considered?</p>	<p>Possibly, but there are so many different approaches to life-styling (e.g. regarding length of transition and risk levels targeted, both before transition and after transition), that one has to question how comparable and useful the information would be.</p> <p>However, it may be that benchmarking on the basis of specified "indicative" (i.e. age-based) pension saver profiles may prove a helpful compromise.</p>
6	<p>When considering which age cohorts to consider, is the example we have provided appropriate?</p>	<p>The comparison is clear, but it will end up comparing apples with oranges, since it combines performance relative to SAA with the risk level inherent in the SAA. Would it not be better to concentrate on better explanations of the level of investment risk inherent in the different funds available?</p>

	Alternatively, would it be more effective to mirror the DWP's approach?	
7	What disclosures, if any, should be made for self-select options?	Those pension savers who have self-selected non-default fund options are still entitled to know how their pension pot has performed relative to appropriate benchmarks, and after whatever charges apply. However, it is perhaps less of an imperative (for self-select funds) to be able to carry out consistent comparisons with equivalent funds from other providers, at least as far as workplace DC VFM is concerned.
8	Do you think reporting based on age cohorts would be enhanced through the use of risk-adjusted returns as an element of a scheme's VFM assessment or would risk-adjustment then become unnecessary?	No. Risk targeted is a fundamental part of the comparison. As noted in the answer to Q6, the use of cohorts does not negate the need for risk-adjustment in order to arrive at comparable results. However, such information won't help assess the adequacy of the returns being generated, but just tell you something about the efficiency of their generation.
9	If risk-adjustment is used, what risk-adjustment metric(s) would you suggest? For example, the Sharpe ratio as i) a standalone factor, or ii) in combination with other risk metrics?	While we publish Sharpe ratios in one of our annual reports, we see that detail as being of relevance mainly to a subset of more informed readers. For most policyholders within our scope, we would expect the riskiness of the default SAA to be of more interest than the riskiness of the implementation of the SAA.
10	Is there any reason why it would be impractical to report on risk-adjusted performance metrics in addition to providing a metric based on actual performance returns?	While it is not impractical to report such metrics, we would question to what extent most pension savers would understand what the metrics are trying to tell them and how helpful or effective in decision-making their publication would be.
11	What are your view on presenting returns as an annual geometric average to provide consistency with the DWP's requirement?	See answer to Q10
12	We would welcome views on how you see this developing. Would it be	Comparisons against a market average, particularly one that does not allow for any life-styling changes over time, are extremely limited in their usefulness. As an IGC, what we are interested in is how the strategies chosen perform:

	<p>helpful/possible to establish a benchmark, or would you prefer to compare cohorts against a market average or against a few selected similar schemes? If so, how would that selection be made?</p>	<ul style="list-style-type: none"> • against stated benchmarks/comparators; • compared to other accumulation defaults in the market; and • against an absolute return target (e.g. CPI + target) <p>We also review the design of the SAA and, in particular, what level of risk is targeted, how wide the range of asset classes is, and how the investment strategies to be followed within each asset class are chosen.</p> <p>Finally, we assess the ongoing governance that is applied to the asset managers and how effective it is at addressing periods of poor performance.</p>
13	<p>Do you think a commercial benchmark is likely to emerge if these data are made publicly available?</p>	<p>Possibly, but, as noted above, we are sceptical over what value it would actually add.</p>
14	<p>Do you agree the quality of communication is a relevant factor to consider in VFM assessments?</p>	<p>Yes – and we have done so since 2015. The recently-introduced “fit for purpose” assessment requirement on IGCs has been a helpful addition.</p>
15	<p>Do you agree administration is a relevant factor that contributes to long-term VFM?</p>	<p>Yes – and have done so since 2015. However, getting consistent data from other providers is not straightforward.</p>
16	<p>Do you agree the effectiveness of governance is a relevant factor that contributes to long-term VFM?</p>	<p>Yes, very much so. Forward-looking value for money assessment depends on confidence that the provider will deliver the outcomes expected and, where issues arise, has appropriate processes in place to address any (temporary) short-comings. For example, the ongoing governance in place around investment management delivery is arguably more important than the detail around recent performance. Past performance is not a guide to the future, but confidence around effective governance might well be.</p>
17	<p>In your opinion, are there any obvious service standards missing from the above list? Please explain how your suggestion contributes to scheme value.</p>	<p>D&I and trustee knowledge etc strike us as being hygiene factors that should be in place and not really VFM factors.</p>
18	<p>Do you agree this is not a role for the regulators at this stage?</p>	<p>The devil will be in the detail. If the regulators think they have sufficient knowledge to impose standards that will be relevant and comparable, then this could be helpful. However, as the many years of IGC benchmarking discussions have shown, there is no simple set of metrics which is readily available for comparison purposes. Either</p>

		we continue to explore what can be done on a voluntary basis, or the regulator needs to impose what MI needs to be collected by each firm, following a suitably thorough Cost Benefit Analysis to justify the development costs.
19	Would it be helpful to appoint a neutral convenor to develop a service metrics standard? If not, who do you think should create metrics on service in pensions?	<p>Possibly, but we are not convinced that such an approach would prove any more effective than the industry efforts on developing consistent benchmarking that seeks to compare apples with apples. There has been, and continues to be, a huge amount of effort being put into this by IGCs and providers.</p> <p>Benchmarking can be difficult because different providers measure service levels differently (e.g. over different time periods, using different averaging methods etc). This is sometimes because the underlying operations systems only capture certain data points. Standardisation of service KPIs across the industry is thus likely to lead to increased costs for some providers where they aren't currently capturing the "right" data.</p> <p>We don't see how a neutral convenor (if such a thing could exist) could develop workable, relevant, benchmarking any quicker – although there could be advantages in stipulating what service metrics should be captured for cross-industry comparisons, thereby providing a regulatory justification for whatever additional systems development spend was required to comply. The only thing that might have made progress quicker would have been for the FCA to require firms to take part in a particular service benchmarking study, but such requests have been resisted up until now.</p>
20	Do you think that over time independent certification against a standard is worth exploring for benchmarking service metrics? If not, what alternative arrangement would you suggest?	<p>We are not sure what is so special about workplace pensions that the FCA's proposed "consumer duty" and existing TCF principles around products performing as they were expected to etc are not sufficient, and some additional certification is required. Also, stipulating such a standard would run the risk of essentially setting the level of service that pension savers would receive and reduce the scope for IGCs to argue (on VFM grounds) for further improvement in customer service standards and/or further development of engagement tools etc.</p>
21	Should we use the existing administration charges and transaction costs definitions in developing VFM costs and charges metrics?	<p>"If it ain't broke, don't fix it." As expected, the inclusion of slippage costs in transaction cost disclosure is not adding much value. However, in the interests of consistency, it would be better not to reopen all the cost disclosure processes.</p> <p>The one key definition that would benefit from confirmation is the meaning of "relevant scheme" for the purposes of COBS disclosure and VFM assessment purposes.</p>
22	Would splitting out the administration	<p>Why decompose a single charge? If the services being provided cannot be un-bundled, we do not see the value of</p>

	charges be a more useful metric? If not, are there other definitions you think would be more appropriate?	knowing how the costs to the provider for the package are split across the different components.
23	Do you agree we should introduce benchmarks for costs and charges?	<p>No. We would prefer that the current industry development of benchmarking which will show the range of charges being applied, split by a measure of scheme quality, be allowed to show its worth, before considering adding any new, additional, requirements to what is already in COBS.</p> <p>Also, we already have benchmarks – the “official” Auto-Enrolment cap of 0.75% p.a. for default funds, and the “unofficial” 1% p.a. that is often referred to and challenged in regulatory publications. Having clarity over the status of the 1% would be helpful, particularly if regulators feel that it should be lower.</p>
24	What are your views on our suggested options for benchmarking costs and charges? If not these options, what benchmarks should be used?	We set out our views and concerns in some detail in our responses to CP19/10 and CP20/9. We continue to be strong advocates of the current costs and charges benchmarking exercise that the industry is voluntarily undertaking through Sackers and Redington and remain confident that the results will enhance our ongoing VFM assessment and provide usable and meaningful comparisons.

D J P Hare, IGC Chair, on behalf of the IGC for Phoenix Life Limited, Phoenix Life Assurance Limited, ReAssure Limited, ReAssure Life Limited and Standard Life Assurance Limited

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