Independent Governance Committee ("IGC") of ReAssure Limited
Report on the pre-launch review of Investment Pathways

On 1 February 2021, the membership of the ReAssure IGC was aligned with that of the Phoenix and Standard Life IGCs, following ReAssure's acquisition by Phoenix Group in 2020.

The new IGC is presenting this Report, which reflects the work done and conclusions reached by the previous ReAssure IGC under its own Terms of Reference and quorum arrangements.

Background

In July 2019 one of the industry regulators, the Financial Conduct Authority ("FCA"), set out new rules requiring firms such as ReAssure Limited ("ReAssure"), which allow customers to enter 'drawdown' without taking advice, to introduce Investment Pathways. Drawdown is a means by which customers can take benefits from their pension pots in a way that suits them, for example:

- by taking money out gradually over time to provide an income;
- taking larger cash sums out over a shorter period;
- keeping money invested; or
- a combination of these options.

Investment Pathways were introduced by the FCA with the aim of improving the decision-making of non-advised customers as they enter drawdown and to promote competition amongst pension providers. Investment Pathways provide four investment options which customers can select depending on their aims over the next 5 years.

The FCA also extended the remit of IGCs, which had previously been established to review the value for money received by members of contract-based workplace pension schemes, to assess the value for money of Investment Pathways. This included a requirement for IGCs to make that assessment before Investment Pathways are offered to customers.

Investment Pathways were intended to be introduced from 1 August 2020 but, due to the Covid-19 pandemic, this was deferred until 1 February 2021. The purpose of this report is to summarise the IGC's initial assessment of the Investment Pathways being introduced by ReAssure.

The IGC reviewed the design, planned implementation and clarity of ReAssure's Investment Pathways proposition and considered it to represent reasonable value for money overall. ReAssure's Investment Pathways have been designed to help customers select from the four relatively simple choices, and it was the IGC's view that they have been designed to meet the broad retirement objectives and improve customers' outcomes. During the course of 2021, the new IGC will continue to work with ReAssure to monitor value for money and outcomes.

Views expressed in this report are the IGC's own and should not be taken as advice or guidance.

ReAssure Investment Pathways

As soon as customers start to access their pension pot, ReAssure has to offer non-advised customers four different Investment Pathway options for the investment of their remaining funds. The four options depend on how they intend to use their remaining pension pot over the next five years and determine which Pathway Investment Fund they enter as follows:

Option 1: I have **no plans to touch my money** in the next 5 years – customers selecting this option will have their pension pot invested in Pathway Investment Fund 1 (see below).

Option 2: I plan to use my money to **set up a guaranteed income** (annuity) within the next 5 years – customers selecting this option will have their pension pot invested in Pathway Investment Fund 2 (see below).

Option 3: I plan to **start taking my money as a long-term income** within the next 5 years – customers selecting this option will have their pension pot invested in Pathway Investment Fund 3 (see below).

Option 4: I plan to **take out all my money** within the next 5 years – customers selecting this option will have their pension pot invested in Pathway Investment Fund 4 (see below).

Each of these funds has been designed by ReAssure to specifically meet the statements in the options highlighted above, but the IGC recognises that not all members have objectives closely matching any one of these 4. Customers who do not wish to take regulated financial advice will need to consider carefully whether any of the Investment Pathways options offered sufficiently matches their future intentions. Customers may also elect to select their own funds rather than choosing one or more Investment Pathways.

The Basis of the IGC's Assessment

In its assessment of ReAssure's proposed Investment Pathways, the IGC considered:

- Whether ReAssure's proposed engagement with customers and communication material was designed to be as **clear and straightforward** as possible so that each customer is able to understand the objectives of each Fund and choose the appropriate Pathway Investment Fund, such that their '**journey**' is straightforward.
- Whether each Pathway Investment Fund was designed by ReAssure to **meet the aims and objectives of the customers** investing their pension pot in the relevant Pathway Investment.
- Whether the Pathway Investment Funds can be expected to provide **value for money** taking into consideration both the quality of the services provided and the **costs and charges** of each Fund.
- Whether ReAssure are committed to reviewing outcomes for customers, to ensure that the Pathway Investment Funds do remain appropriate and deliver value for money.

The IGC's conclusions in response to these questions are set out below.

The IGC recognised that ReAssure has offered a Retirement Account product since 2015. ReAssure carried out an extensive analysis of these policies to understand the choices their customers have made and shared the findings of this analysis with the IGC. These results were considered by the IGC and, along with other debate and challenge, helped the IGC to assess how well the design and objectives of the Pathway Investment Funds matches customers' general aims and objectives.

Question 1) – Is the journey clear and straightforward?

The IGC's view was generally **YES**. ReAssure had considered the needs of customers and the appropriate method and timing of communications.

The IGC was taken through the ReAssure customer journey, reflecting on the experiences of how existing customers have behaved when taking cash from their pension pot. The IGC reviewed communications customers will receive and concluded that, given the quality, content and design, customers will be able to relate to the materials and find key information. The IGC therefore believed that customers will be appropriately guided and informed through the journey.

The IGC's concern was that all communications in respect of Investment Pathways should be clear and understandable, meet their intended purpose, and take into account the characteristics, needs and objectives of customers. The IGC was satisfied that ReAssure's communications were fit for purpose.

From the launch of Investment Pathways at the end of January, ReAssure will be monitoring all aspects of customer communication and providing information to the IGC to enable us to check that the Investment Pathway journey works for customers.

Question 2) Are the Pathway Investment Funds designed to meet the aims and objectives of members?

The IGC believed that the funds were designed taking into account the general aims and objectives of customers who will enter each of the 4 pathways. The limitation of offering a customer only one fund for each pathway, set by the FCA, means that each Pathway Investment fund cannot meet all the aims and objectives of all customers who might select the corresponding Investment Pathway option. Each Investment Pathway option is only based on the timeframe over which the customer expects to access their investment and cannot therefore reflect the range of attitudes to risk customers might have, due to their particular circumstances, for example such as other savings. So, this is a limited and qualified YES.

The IGC's comments on each of the Investment Pathways Funds offered to customers by ReAssure under the four Options are as follows:

Option 1: I have no plans to touch my money in the next 5 years

Investment Pathway Fund 1. ReAssure have designed this Pathway for customers who aren't expecting to access their pension pot in the next 5 years. Based on their analysis of existing customer accounts, ReAssure have concluded that on average Option 1 customers are likely to stay invested for 7 years.

This fund is designed to provide an opportunity for customers' pots to grow by more than inflation by investing just under half of the fund in stocks and shares, with the rest invested in corporate bonds and cash to reduce the risk of large falls in value. The current low interest rate paid on bonds means that there remains a risk that the fund may not grow enough to meet inflation.

Customers who plan to use their ReAssure pension pot alongside other sources of income in retirement or customers who have no plans to access this pot over a longer time horizon than 7 years, may wish to take more investment risk. Their aims may be focussed more on growing the fund at a rate above inflation, recognising the likely fluctuations in value. Other customers may be less comfortable with market value falls and so wish to have less invested in stock markets. This is a ‘risk versus reward’ balance that customers need to consider.

The IGC’s conclusion was that this fund will generally meet the aims and objectives of customers who are willing to take some investment risk after entering this Pathway.

Option 2: I plan to use my money to set up a guaranteed income (annuity) within the next 5 years

Investment Pathway Fund 2. The cost of an annuity generally depends on the expected investment returns (interest rates) on longer dated bonds. This fund has been designed to reduce the impact of changes in interest rates on the annuity income a customer could buy in future.

If expected returns (interest rates) go down, costs per £1,000 of income go up but the value of this fund should go up to at least partially offset this increase in cost; whilst, if interest rates go up, which is likely to mean the fund value will go down, the cost of an annuity should go down too.

Those planning to buy a guaranteed income at some stage in the next 5 years should be reasonably protected by this fund against the risks of the costs of buying such an income (an annuity) changing as a result of interest rate changes. However, due to the low current interest rates, there are risks that the return on the fund after charges will be very low. Customers who change their mind about their plans, for example deferring their retirement, may feel badly served by this fund.

The IGC’s conclusion was that this fund is designed to meet the aims and objectives of customers who expect to use the whole of their remaining fund, after withdrawing cash, to buy a guaranteed income within the 5-year time horizon.

Option 3: I plan to start taking my money as a long-term income within the next 5 years

Investment Pathway Fund 3. This fund has around 10% less invested in the stock market than Investment Pathway Fund 1. The fund is still designed to offer the potential for growth ahead of inflation but the lower allocation to stocks and shares reflects the fact that the customers who select this Investment Pathway Option are likely to be more vulnerable to market falls as they will start taking a pension income almost immediately. The greater stability and lower expected fluctuations in value are designed to sustain an income throughout a customer’s retirement. The fund has been designed on the expectation these members have only a ‘cautious medium risk’ tolerance. The protection of the fund against the potential for significant changes in value, with a substantial proportion in bonds and cash, does limit the growth opportunity, which in turn reduces the expected level of sustainable income, particularly for those who have a long retirement.

The IGC’s conclusion was that the fund’s aims and objectives match the objectives of customers who are willing to take some risk on the value of their fund in order to seek protection against inflation. However, some customers with substantial funds and other expected sources of income in retirement, or those who need a higher level of growth to sustain income through a long expected retirement period, may well be willing to take more investment risk by selecting their own funds.

Option 4: I plan to take out all my money within the next 5 years

Investment Pathway Fund 4. This fund is designed to meet the aims of customers entering this pathway by limiting the fluctuations in value likely in the fund and so, **for customers planning to take out all the money in their pension pot within the next 5 years, the IGC's conclusion was that this fund is appropriate**. However, the fund is typically invested in cash deposits and short-term bonds and, as a result, returns are expected to suffer from the ultra-low interest rates currently available. It is suitable for customers fully expecting to take all their remaining funds within the 5 years and for whom security is more important than growth. There is a risk that, after charges, the money invested in this fund will only grow minimally, and may not hold its value.

Question 3) Does each Investment Pathway Fund constitute value for money given the services provided and the costs and charges applied?

The charge on a pathway investor's pension pot will depend on the Investment Pathway chosen and will range from 0.70% to 0.75% (this is made up of an annual management charge of 0.65% and additional investment charges of between 0.05% and 0.10%). Customers should consider carefully when moving into an Investment Pathway Fund what their particular charge will be and whether they could find a better value option by moving into an Investment Pathway Fund with another provider.

ReAssure has positioned itself to be a low cost provider and the investment strategies proposed for each Investment Pathway reflect this. To keep the costs down, the fund management approach invests only in public bond and stock markets and is passively managed, which means the investment manager aims to deliver returns in lines with these markets by holding portfolios that replicate the market (rather than trying to beat the markets, while also risking underperformance).

Overall, the IGC believed that the charges on ReAssure's Investment Pathway Funds can be expected to provide value for money for the ongoing management of customers' Investment Pathway Funds. This management includes the management of the underlying investment funds, customer service and communications keeping customers informed of the ongoing progress of their Investment Pathway fund.

In addition to the explicit charge on each Investment Pathway Fund, there will be transaction costs incurred in managing each fund that are deducted within the Fund, reducing the value of customers' pension pots. As well as reducing the asset management fee, the passive approach mentioned above has the advantage of keeping transaction costs low as there is less trading carried out. The IGC considered the likely level of these costs in the Investment Pathway Funds and expected these to be reasonable. Transaction costs have been tracked over the past year for funds that are being used by the Pathway Investment Funds developed by ReAssure. The IGC was assured that no substantial changes to the level of transaction costs are expected going forward.

In carrying out this assessment, the IGC would like to have compared the costs and charges to the costs and charges on other funds in the market available to customers. At that time, however, only a small number of competitor Investment Pathway providers had launched their product and 'like for like' comparisons were difficult. The IGC intends to track product charges in the market as information becomes available.

Question 4) Are ReAssure committed to reviewing outcomes for customers to ensure that the Pathway Investment Funds do remain appropriate?

ReAssure have confirmed to the IGC that they will keep customer outcomes and Investment Pathways under continuous monitoring.

The new IGC will also continue to monitor how well the Investment Pathway Funds perform and whether they achieve their aims and objectives. In addition, we will monitor the ongoing charges and costs to ensure VFM.

Overall Conclusion

The previous IGC reviewed the design, planned implementation and clarity of ReAssure's Investment Pathways proposition and their findings are set out above. In summary, customers have flexibility in how and when they can access their pension savings, but this also means they have to make more complicated choices. The FCA identified that many consumers are focused only on taking their tax-free cash, leaving the rest of their pension pot invested in a way that may not meet their needs and intentions. ReAssure's Investment Pathways have been designed to help customers select from the four relatively simple choices, and it was the IGC's view that they have been designed to meet the broad retirement objectives and improve customers outcomes. During the course of 2021, the new IGC will continue to work with ReAssure to monitor value for money and outcomes.

The IGC would like to record its thanks to the many ReAssure colleagues who helped it review the Investment Pathways project over the course of the past months.