Vanguard Asset Management Independent Governance Committee

Annual Report for 2020

APRIL 2021

Contents

Introduction

This is the first report by Vanguard Asset Management's Independent Governance Committee (IGC). Under an extension of responsibilities beyond Workplace pensions, IGCs must now cover customers who take money from their pension pots without taking advice and choose one of the prescribed "Pathways". Vanguard Asset Management (Vanguard) launched its Drawdown and Pathways solution as part of its Self-Invested Personal Pension "SIPP" in November 2020 and established its IGC in October to exercise oversight.

IGC work to date and its findings:

Vanguard offers an investment platform for investors to make investment transactions. Investors may or may not have received regulated investment advice. Typical customers have the confidence to choose their funds and execute transactions, but Vanguard has no specific knowledge of customers' investment expertise, risk appetite or risk capacity, or of their total portfolio of wealth. Vanguard believes (and the IGC has seen no evidence to challenge this belief) that its customer base is likely to be weighted to the mass affluent and high net worth cohorts who are likely to be investing only part of their total wealth with Vanguard and whose investment beliefs coincide with the funds which Vanguard offers.

We have studied Vanguard's Pathways solutions and are satisfied that they are appropriate for the type of customers likely to be using them.

Our full report covers specific areas we have examined to come to this conclusion and sets out our work plan for continuing to examine those areas which the FCA expects us to report on. Our full report contains some technical terms but we have added a "jargon buster" to help explain what they mean.

At this initial stage, despite few customers having entered drawdown and selected the Investment Pathways, the IGC believes the Vanguard Pathways offer good value for money.

Get in touch

We have been able to send copies of our report to all customers using the Investment Pathways and would welcome any feedback. Please send any questions, suggestions or comments via the help section on the website: https://www.vanguardinvestor.co.uk/need-help.

Lawrence Churchill CBE
Chairman, Vanguard IGC

1. Background and Scope

Independent Governance Committees (IGCs) were initially set up six years ago by the Financial Conduct Authority (FCA) to oversee that members of Workplace pension schemes (which had been introduced by the Government in 2012) received Value for Money. The IGC acts solely in your interests and independently of Vanguard.

Following two reviews by the FCA, the first into Retirement Outcomes and the second into IGC effectiveness, the FCA mandated that all consumers entering income drawdown without taking financial advice should be offered four specified investment choices among their investment options – called Pathways.

If consumers say they want to invest in the Investment Pathway funds they are asked what they plan to do with the money in their pension account within the next five years. They are asked to choose the option that best fits their current retirement goal.

Option 1: I have no plans to touch my money

Option 2: I plan to use my money to buy a guaranteed income (annuity)

Option 3: I plan to start taking my money as long-term income

Option 4: I plan to take out all of my money

Based on the option they select the customer is offered an investment solution which is designed to help them meet their goal.

The FCA extended the responsibilities of IGCs to provide oversight of the investment solution behind each Pathway including to

- assess whether they give Value for Money,
- review the charges customers paid,
- comment on the adequacy of risk disclosure and
- comment on whether customer communications were fit for purpose.

They also asked for comment on the firm's approach to Environmental, Social and Governance (ESG) considerations and Stewardship.

Vanguard does not offer Workplace pension products so did not need an IGC until November 2020 when it launched its income drawdown and Pathways product as part of its Self-Invested Personal Pension. Following an induction programme, it established the IGC in October and the IGC met on three occasions to review the Pathways product and the associated communications material, thus having the opportunity to inform Vanguard's board of directors if it had any substantial concerns before the product was launched. There were no significant concerns raised.

The members of the IGC and their suitability for the role are set out in Appendix 1. The committee is composed of five members, three of whom are independent of Vanguard. The two Vanguard members have received a variation to their standard employment contract to the effect that when they act as members of the IGC, their sole concern is the interests of customers using Pathways. This composition of an IGC is in line with regulation and is commonly adopted by other firms. The independent members were appointed after an open competitive process.

2. How we Assess Value for Money (VfM)

IGCs overseeing Workplace pensions have evolved mechanisms for assessing VfM consisting of three parts:

a) The design and performance of the investment fund

b) The charges levied for the investment, including transaction costs

c) The quality of support services delivered (including customer communications).

The FCA has endorsed these components. This approach to assessing VfM has been used for Workplace pensions in the pre-retirement phase when pensions savers were building up their pension pots.

Vanguard's IGC has considered and will continue to consider whether this approach is appropriate for the at-retirement and post-retirement phases. Our initial conclusion is that it is appropriate, but that different aspects could be weighted differently for investors choosing Pathways. For example, it could well be the case that the risk of a sudden drop in the fund value is of more interest to an investor at retirement than it would be to an investor early on in their savings journey, or that the sophistication of retirement planning tools is more significant when decisions about drawing down funds are being made compared to times earlier in the saving process. Another possible variation is that the criteria we use to assess each Pathway may be weighted differently depending on the Pathway. We explore this further in Section 3.

The FCA has highlighted four areas for specific IGC assessment with regard to Pathways:

- The quality of risk disclosure
- Whether communications are fit for purpose
- How Vanguard gathers and responds to customers' concerns on ESG issues
- Vanguard's approach and practice in stewardship.

We have incorporated these factors in our assessment of VfM, and have summarised them in the Framework we set out in Appendix 2

3. Report on Pathways Solutions

3.1 Design and Performance of Investment Solutions

We took the approach of listing the likely needs of investors choosing each of the four Pathways, and asking ourselves the extent to which their needs were met and how well the risks to their choice were mitigated. The IGC was satisfied that the design of each of the four Pathways catered for typical needs and mitigated risk appropriately. At this stage we do not know how many investors will choose each Pathway and so we will monitor this during 2021.

The Pathways address the four options in answer to the question "What do you plan to do with the money in your drawdown account within the next five years?"

Pathway 1 – "I have no plans to touch my money".
This Pathway is the most similar to the accumulation phase of investing. The key needs are for the continued real growth in fund value through a well-diversified fund, combined with some de-risking as the time to take pension withdrawals approaches, and the key risk is not achieving real growth. For example, this Pathway might be considered by an investor who has sufficient pension from other sources and plans to use this part of the portfolio to pass down to dependants instead.

Vanguard's solution is to put clients into the Target Retirement Fund ("TRF"), from its existing range nearest to the investor's selected retirement age. The default can be changed if the investor wants to.

Vanguard believes the TRF range to be appropriate for an Investment Pathway as the funds are explicitly designed with an appropriate replacement ratio in mind. They are single funds and consistent with the Vanguard Pre-Retirement Approach. Importantly, the fund offers inherent de-risking within the fund – so the asset allocation is appropriate for selected retirement ages and supports future fund growth to sustain future income requirements. They offer a diversified solution with a Green Rating across all seven of the FCA's Assessment of Value Criteria – including performance and costs and charges.

Vanguard runs eleven different Target Retirement Funds targeted at 5-year intervals. Investors using Pathways are unlikely to be invested in the longer term target dates, so we have shown the performance of two nearer term funds below. The figures are taken as at the end of December 2020 and are net of charges.

Fund	1 year return (%) to 31/12/2020	3 year return (% p.a.) to 31/12/2020	5 year return (% p.a.) to 31/12/2020
Vanguard Target Retirement 2025 Fund – GBP Accumulation Shares	7.39	6.26	9.00
Vanguard Target Retirement 2050 Fund – GBP Accumulation Shares	7.65	6.82	10.41

Source: Vanguard

Fund	01/20 to 01/21 (%)	01/19 to 01/20 (%)	01/18 to 01/19 (%)	01/17 to 01/18 (%)	01/16 to 01/17 (%)
Vanguard Target Retirement 2025 Fund – GBP Accumulation Shares	6.30	12.17	0.21	8.41	19.19
Vanguard Target Retirement 2050 Fund – GBP Accumulation Shares	7.35	13.26	-0.27	10.23	24.13

Source: Vanguard

Investment performance for the Target Retirement Funds is managed as a process, which is set out below:

- Performance of the TRFs is monitored against their daily target allocations, which take account of glidepaths, but also consider UCITS rules.
- Target allocations of the underlying funds are rebalanced daily to take account of daily changes in market valuations.
- The Vanguard product teams provide oversight from a fund health perspective, and focus performance oversight around peer/competitor analysis.

Vanguard does not formally benchmark the TRFs as they are multi-asset funds. The IGC has taken a pragmatic reference point for assessing their value for money to see whether growth has matched the Consumer Prices Index +3% pa. As can be seen from the table, this hurdle rate has been surpassed for all the cumulative multi-year periods shown.

Pathway 2 – "I plan to use my money to buy a guaranteed income (annuity)".
The key need is to preserve (and if possible grow) the value of the annuity which can be purchased. At the point of buying an annuity, the key needs are to shop around, to think about maximising value for the investor and dependants and to consider enhanced annuities if the investor is in poor health.

The Vanguard solution for this Pathway is to invest in the UK Short-Term Investment Grade Bond Index Fund, which aims to protect the value of the fund and add a small return. Vanguard is aware that there are a number of different types of annuity which may eventually be chosen and it is impossible to track all of these in a single fund. We agree with this approach.

This is an existing Vanguard fund and has the following performance (net of charges) and benchmark:

Fund	1 year return (%) to 31/12/2020	3 year return (% p.a.) to 31/12/2020	5 year return (% p.a.) to 31/12/2020
Vanguard UK Short-Term Investment Grade Bond Index Fund – GBP Acc	2.98	2.13	2.35
Spliced Bloomberg Barclays GBP Non-Govt 1-5 Yr 200MM Float Adjusted Index in GBP (Benchmark)	3.15	2.29	2.54

Source: Vanguard

Fund	01/20 to 01/21 (%)	01/19 to 01/20 (%)	01/18 to 01/19 (%)	01/17 to 01/18 (%)	01/16 to 01/17 (%)
Vanguard UK Short-Term Investment Grade Bond Index Fund – GBP Acc	2.32	3.47	0.69	1.45	3.22
Spliced Bloomberg Barclays GBP Non-Govt 1-5 Yr 200MM Float Adjusted Index in GBP (Benchmark)	2.53	3.89	0.84	1.35	3.52

Source: Vanguard

The performance level is very slightly below benchmark. In terms of risk profile, Vanguard rates this as 2 on a seven-point scale (that is, at the safer end of the range). Vanguard does not anticipate a high take-up of this Pathway, and does not offer annuities, so these will have to be purchased in the open market.

Pathway 3 – “I plan to start taking my money as a long term income”.

The key need is for continued real growth in the fund. Individual investors may have different needs; for example, an investor may want the fund to provide an income for life, while another investor may want to draw income to match variable spending patterns and may not worry if the fund is exhausted during their lifetime as they have other pension provision. As an execution only investment platform, Vanguard holds no information about a client’s total wealth or their risk appetite in relation to the Vanguard portion of their portfolio.

As it is difficult to design a fund to meet both objectives above, the IGC has evaluated the Vanguard solution on the assumption that the investor would like a lifelong income. For investors with more flexibility in their financial requirements, Vanguard offers other funds outside of the Pathways range.

So the key need is to take out money at a level which is sustainable; this level may well vary from year to year as investment returns change and longevity assumptions vary, perhaps with changes in health. Returns in the first ten years after the consumer begins to withdraw their money are the most important factor determining the level of sustainable income which the customer can take throughout their retirement. The key risk is to take out too much too early, particularly if this is during a period of poor investment returns. Investors are particularly exposed to falls in value of their funds in the early years of drawdown (sequencing risk).

Vanguard’s solution is to use the Target Retirement Fund nearest to the half-way point between today and the selected retirement date. The 2025 fund illustrates this well and its performance is set out on page 5.

Pathway 4 - “I plan to take out all my money”.

The key needs are the preservation of the fund value and minimising the amount of tax payable on withdrawal.

The key risk in investing in cash is that the purchasing power of cash reduces with time as the interest on cash deposits is less than the rate of inflation.

The Vanguard solution is the Sterling Short-Term Money Market fund, launched in 2019, which has performed ahead of benchmark, but with a very low yield since launch.

This fund is suitable for short-term imminent withdrawals and Vanguard has noted that five years is a long time to be invested in this fund; it will remind investors regularly, as described below (see section 3.3.3). If customers change their mind about taking all their money and decide to leave it invested then it is important that they select a solution more appropriate for their long-term needs.

Fund	1 year return (%) to 31/12/2020	Since inception (17/12/2019) return (% p.a.) to 31/12/2020
Vanguard Sterling Short-Term Money Market Fund - GBP Income Shares	0.29	0.39
Spliced LIBID/SONIA Index (Benchmark)	0.07	0.22

Source: Vanguard

Fund	01/20 to 01/21 (%)	01/19 to 01/20 (%)	01/18 to 01/19 (%)	01/17 to 01/18 (%)	01/16 to 01/17 (%)
Vanguard Sterling Short-Term Money Market Fund - GBP Income Shares	2.23	-	-	-	-
Spliced LIBID/SONIA Index (Benchmark)	2.02	-	-	-	-

Source: Vanguard

3.2 Charges and Transaction Costs

3.2.1 Vanguard Charges

Vanguard's charging structure comprises two components – an account fee of 15 basis points up to a maximum of £375 a year and a fund management fee which is variable dependent on the fund. For the three types of fund backing the Pathways solutions, the charges are:

Fund	Account fee (%)	Fund management fee (%)
Sterling Short-Term Money Market Fund	0.15	0.12*
UK Short-Term Investment Grade Bond Index Fund	0.15	0.12
Target Retirement Funds	0.15	0.24

Source: Vanguard

* Effective 15 September 2020, Vanguard has voluntarily agreed to temporarily limit certain expenses in the Vanguard Sterling Short-Term Money Market Fund. This means investors will benefit through zero or positive net returns in instances where the charges would otherwise result in a negative yield or return in the current low interest rate environment. Should UK official interest rates or market yields remain low or become negative for a longer-term period, Vanguard may remove the fee waiver at any time.

Transaction Costs are best viewed as the cost of delivering the investment performance net of fees quoted above, and the transaction costs are reported internally for ongoing monitoring to make sure they are appropriate. The level of transaction costs reported by Vanguard is between 4 and 9 basis points for the Target Retirement Funds, 2 basis points for the UK Short-Term Investment Grade Bond Index Fund and 4 basis points in the Sterling Short-Term Money Market Fund. The level of these transaction costs raises no immediate concerns and the IGC will conduct more analysis of the disaggregated level of transaction costs in the coming year.[1]

3.2.2 Comparative Market Data for Pathways

We have reviewed some comparative market data on total charges for some firms which have launched their Pathways solutions, and set out this information below.

Pathway	Charges (in basis points) for			
	Firm 1	Firm 2	Firm 3	Vanguard
1	56	60	60	39
2	39	60	N/A	27
3	56	75	95	39
4	39	50	50	27

This data gives the IGC comfort that the Vanguard charges are lower and underpin value for money.

This level of total charges, between 27 and 39 basis points, is low in comparison to charges for personal pensions in the broader market. Indeed, we have seen a market pricing analysis from Platforum from November 2020 which assesses Vanguard as the cheapest provider (except for balances above £250k).

3.2.3 Comparative data for SIPPs and Workplace Pensions

The level of charges is also competitive with many workplace pension schemes, where the DWP found that the average charge for qualifying workplace pension schemes was 48 basis points.[2]

Data from the Platforum research November 2020 indicates that Vanguard is typically the lowest-cost provider for balances less than £100,000.[3] This means that for the Vanguard customer with the average sized pension fund in drawdown, Vanguard is the lowest-cost provider. Where it is not the lowest cost provider, Vanguard is typically within 1 to 5 basis points of the lowest-cost provider.

1 https://www.vanguardinvestor.co.uk/content/documents/legal/vanguard-full-fund-costs-and-charges.pdf.

2 https://www.gov.uk/government/publications/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes/pension-charges-survey-2020-charges-in-defined-contribution-pension-schemes.

3 This is based on the size of the pension fund invested in the Target Retirement Pathway from Platforum research.

3.3 Customers

3.3.1 Customer Profiles. As a digital investment platform, Vanguard believes that its investors will have sufficient knowledge, skill and confidence to make their own investment choices, if they are not receiving regulated financial advice. SIPP customers age 55 and over have pension pots averaging £64k and those over age 75 have pension pots averaging over £100k. The customer research referred to in the next section was conducted among the self-employed or investors with more than £100k invested.

3.3.2 Customer Research. Before launching its drawdown product and Investment Pathways, Vanguard conducted consumer research over several years through two specialist agencies which included prototypes of its planned communications to check whether they were clear and understood. It is worth noting at this point that an important component of Vanguard's communication architecture is the Vanguard website, as it is a digital business.

One of the key findings of the research was that customer understanding was highly variable, with different customers doubting their understanding of a wide range of pensions technical concepts and terms. In particular, although most had a good understanding of what a SIPP was and what the accumulation phase meant, there was less awareness of issues around decumulation and accessing their pension. There was little consistency across the terms which customers struggled with. So, although the research was helpful in designing a more natural flow to the online screens, it became clear that Vanguard needed to do something extra (see section 3.3.3 below).

3.3.3 Processes to Protect Customers. Customer research clearly indicated that there was no single ideal communication solution which suited all customers. As a result, Vanguard has instigated a process whereby all customers choosing a Pathways solution have to speak with a Vanguard Consultant who can check understanding and help the customer to make an informed decision; the Consultant also recommends that the customer speaks with PensionWise. The conversation with the Consultant is a mandatory part of the drawdown process.

The process involves:

- Identity verification;
- Confirmation that the customer has read their retirement pack and understood their options.
- Verification of the customer's understanding of the 11 regulatory questions "FCA Retirement Risk Warnings".
- Confirmation that they have understood the impact of the option they have chosen.
- Confirmation that they wish to proceed.
- Explanation of the expected timeframes for payment.

The checklist completed by the customer will be covered in the call with the Consultant. The customer will be sent an illustration and then this will be discussed in a second call with the Consultant.

As additional risk mitigation for customers intending to cash in their pension within five years (Option 4), Vanguard has decided to write to them at six-monthly intervals to remind them of their choice and the implicit risks of low returns and real reduction in the purchasing power of their funds in the intervening period.

3.3.4 Communication of Risk. The major written information on the risks associated with the Pathways funds is contained in the Fund fact sheets. The IGC view is that the investor would already need to be competent and experienced to understand the information set out (which is fully compliant with MIFID II regulations).

The risk disclosures in the Key Investor Information Documents (KIIDs) use the standard Synthetic Risk and Reward Indicator (SRRI) seven-point scale (with 1 the least risky and 7 the most risky). The Pathway funds are rated as 1 for the Money Market Fund, 2 for the Short-Term Bond Fund and 4 for the multi-asset Target Retirement Funds. The KIIDs also set out those risks which were not included in the assessed score.

Risks are also discussed with the Vanguard Consultant and this acts as a welcome additional support.

The IGC are aware of the difficulty of effective and intelligible risk disclosure around the world. We are satisfied that the current risk disclosure is adequate for experienced investors but we would have reservations that less experienced investors or investors who have become vulnerable may not fully appreciate the potential impact of fund risks if they were to use the Vanguard platform.

Many of the risks lie outside of the funds backing each Pathway e.g. the risk of not getting an enhanced annuity if you qualified, the risk of customers or their dependants living longer than average, the risk of falling for a pension scam or the risk of not anticipating the tax consequences of cashing in the fund. Customer Communication material and the discussion with the Vanguard Consultants describes such risks at the point of choosing a Pathway and we will review the after sales service as we go forward.

3.3.5 Are Customer Communications Fit for Purpose?
The IGC has had the opportunity before Pathways were launched to review all of the customer "literature". This includes the website and also the "call scripts" which the Consultants use. We have reviewed the efficacy of Vanguard's policy and process for identifying vulnerable customers and the way in which potential scams are highlighted.

The IGC has also listened in to a number of the customer calls with Consultants and found that customers generally had a strong view of what they wanted to do, having recently moved to the SIPP and actively chosen their funds; they were therefore generally seeking reassurance on the process that they needed to follow online in order to action their decisions. Although a small number of calls to date, which were generally simple in nature, the IGC noted the good quality of guidance provided: personable, factual, not rushed and clear.

In summary, customer communications are fit for purpose, for the experienced investors likely to be using the platform. We will do more to investigate and confirm this during 2021.

3.3.6 Customer Satisfaction

We have some initial customer feedback on their satisfaction with the drawdown and Pathways processes, and the feedback is favourable, although it is early in the process to have seen sufficient volumes through Pathways to draw any conclusions at this stage.

The Vanguard SIPP has been named as a "Recommended Provider" by Which? as it offered high customer satisfaction combined with competitive charges.

3.4 Environmental, Social and Governance (ESG) Considerations and Stewardship

With so little business being written in the Investment Pathways, we have only just begun to receive presentations from the ESG specialists. It will take some time for the assets under management under IGC oversight to become material.

From the presentations to date, it seems that the issues are understood but that the practices are perhaps less well developed than at some other investment houses, particularly with regard to the funds available under Investment Pathways. Historically, Vanguard has offered "whole of market" solutions, and has not historically detected a strong demand among its investors for more ESG centric offerings; this situation may well change as ESG has entered the mainstream only in the last year or so and has recently gathered momentum. Vanguard does offer some funds with ESG exclusions and tilts but not in the fund ranges used to support Pathways.

A recent report from the market research consultancy NMG, sponsored by another leading provider, found that among customers approaching or in drawdown, only "17% care about the fund's ethical stance". We note that ethical and ESG are not one and the same, but are conscious that this is a developing area with financial consequences. We will try to ascertain the views of Vanguard investors during 2021.

An unintended consequence of the current FCA rules for Pathways is that they prohibit firms from offering more than one investment solution under each of the Pathway options. This means that Vanguard cannot offer the option of funds with and without ESG exclusions/tilts as its four Pathways solutions.

Vanguard's current confirmed Stewardship policy statement is set out on the following page and more can be found on the Vanguard website via: https://www.vanguardinvestor.co.uk/content/documents/legal/vanguard-investment-stewardship-annual-report-2020-ukpi.pdf. The IGC will look at the topic in greater depth in 2021.

3.5 Other Services

3.5.1 Timely actioning of financial transactions:
Management has confirmed that these are all within service levels for Pathways investors, and in the event of any delay by Vanguard, their policy is such that the customer is given the more favourable unit price.

3.5.2 There have been no complaints received in respect of the Pathways offering or processes. Vanguard has agreed to provide the IGC with a summary of the type and number of complaints received and how they have been resolved.

3.5.3 Vanguard offers its own retirement planning calculators and has tested and improved them based on customer feedback.

3.5.4 Vanguard has processes in place to record customer vulnerabilities including health, resilience, life events and capability. The IGC has recommended that Vanguard ensures that customer vulnerability to pension scams can be recorded. Outcomes for vulnerable customers are discussed monthly at the Vulnerable Client Outcomes Group and measuring these will be particularly important in meeting the objective that vulnerable customers achieve outcomes as good as those of other customers.

Summary of Vanguard's Engagement Policy (under Article 3g of Directive 2007/36/EC)

Vanguard's Investment Stewardship team (the "Investment Stewardship Team") serves as a voice for investors in its funds to promote long-term value creation at the companies in which the equity funds managed by Vanguard invest. When a Vanguard index fund invests in a public company, it could theoretically hold that stock forever or as long as the company is listed in the underlying benchmark. With this indefinite horizon, Vanguard and its funds must focus on how companies are setting themselves up to stay relevant today, tomorrow, and well into the future.

As a long-term investor, the Investment Stewardship Team stay keenly focused on areas such as risk, strategy, executive remuneration, diversity, environmental issues, shareholder rights, and health and safety issues. The Investment Stewardship Team stewards the global equity holdings of Vanguard managed funds in three key ways:

- **Public advocacy.** The Investment Stewardship Team advocates for the highest standards of corporate governance worldwide and the sustainable, long-term value of Vanguard's shareholders' investments.
- **Engagement.** The Investment Stewardship Team conducts ongoing dialogues with portfolio company executives and directors to share its long-term orientation and principled approach, and to understand a company's governance practices and long-term strategy.
- **Voting.** The Investment Stewardship Team votes proxies at public company shareholder meetings on behalf of equity funds managed by Vanguard.

One of the key principles that Vanguard considers foundational to effective corporate governance is the oversight of strategy and risk. The Investment Stewardship Team engages with boards regarding the oversight of material risks that have the potential to affect shareholder value over the long term – from business and operational risks to environmental and social risks. Vanguard believes that companies should disclose material risks to shareholders, explain why those risks are material to their business, and disclose their approach to risk oversight. Vanguard has a responsibility to understand how business activities pose a material risk to the long-term value of its funds.

For example, Vanguard recognises that climate change represents a profound, fundamental risk to investors' long-term success. Vanguard supports climate risk mitigation, acknowledging that the goals in the Paris Agreement are widely accepted for countries and companies seeking to address climate change. Where it is a material risk, Vanguard encourages companies that it holds in its equity portfolios to set targets that align with the Paris Agreement and disclose them.

When the Investment Stewardship Team identifies a concern with how a company in its equity portfolios is overseeing a material risk, including ESG risks, it often seeks to engage with the company in order to enhance their disclosure on risk mitigation and/or encourage them to develop a more appropriate risk mitigation approach. This is all part of the effort to safeguard clients' assets against a full range of short- and long-term risks.

If a company is not receptive to the Investment Stewardship Team's requests, it can escalate this through Vanguard's proxy voting activity at that company's general meetings – either by voting against resolutions proposed by management or supporting shareholder proposals. As a near permanent owner with a long-term perspective, Vanguard is in a unique position to ensure that its investments are well placed to benefit from the sound oversight of ESG risks.

For more information about Vanguard's Investment Stewardship programme and how it engages with portfolio companies, please see Vanguard's Engagement Policy at: https://global.vanguard.com/documents/Vanguard-Engagement-Statement.pdf.

Adherence to international standards

UN Principles for Responsible Investment Signatory

With the growing importance of ESG issues to investors, Vanguard affirmed its commitment to responsible investment by joining the UN Principles for Responsible Investment (PRI) in 2014. The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories such as Vanguard contribute to developing a more sustainable global financial system. They have attracted a global signatory base representing a majority of the world's professionally managed investments.

The PRI reviews transparency reports and produces assessment reports, which appraise how a signatory has progressed year-on-year and relative to peers. Unlike transparency reports, assessment reports are not available on the PRI website. It is up to individual signatories to share their assessment report to demonstrate their performance or keep it in-house as an internal learning and development tool. Vanguard has elected to share its assessment report with clients upon request.

The Paris Agreement

Please see the 'Summary of Engagement Policy' section above regarding how Vanguard addresses climate risk.

4. Workplan for 2021

As Pathways are in their infancy, we will continue to develop our scrutiny in a proportionate way as issues become more material. We expect this to include

- Monitoring any changes to the underlying investments and receiving regular reports on fund performance, including Vanguard's own assessment.
- To disaggregate transaction costs and assess whether IGC believes there are any material issues. Note that Vanguard currently calculates transaction costs under MIFID II regulations, so the possibility of differences with the FCA methodology applied to Workplace schemes does arise.
- To collate comparative data on the offerings from other firms and assess Vanguard's position in relation to them.
- To try to find ways of getting customer feedback covering their needs, their understanding of retirement income processes and products, their risk appetite and risk capacity, and any beliefs or concerns they have in relation to ESG.
- To measure customers' understanding of sustainable withdrawal rates and help them develop withdrawal strategies and plans.
- To receive more in-depth presentations from Vanguard on their approach to ESG and Stewardship, and how, if at all, Vanguard has incorporated this approach into the funds supporting Pathways.
- To assess in more depth any risks to customers arising from a digital only platform, and in particular how customers who may be becoming vulnerable are identified and treated.
- To assess whether we believe that Vanguard should do more in supporting customers to cope with the external risks (beyond the risks inherent in fund design), such as might arise through scams etc.
- To try to understand customers more as the number of Pathways Investors grow. This might also include monitoring actual levels of drawdown and encouraging Vanguard to communicate with customers if the levels of drawdown are not sustainable; this could provide insight both into the behavioural characteristics of customers as well as provide an indication of their retirement resources held outside of Vanguard.
- To monitor the customer services offering to Pathways investors to continue to assess for Value for Money.

Appendix 1
IGC Membership

The IGC has been appointed by Vanguard to fulfil the duties expected by the Financial Conduct Authority and set out in its Conduct of Business Source Book. The IGC has Terms of Reference agreed with Vanguard's Board.

The IGC has five members, three of whom are independent of Vanguard, and have been selected following an open recruitment process. The Members' short biographies showing their suitability for the role are set out below.

Lawrence Churchill CBE
Independent Chairman

Lawrence has worked in pensions for over 40 years to try to make the system work well for consumers as well as providers. In his executive life, he was CEO of three insurance groups. As a non-executive he was the inaugural Chair of both the Pension Protection Fund and the National Employment Savings Trust, was chairman of the Financial Services Compensation Scheme and a member of the Board for Actuarial Standards. He currently chairs Clara Pensions and the Pensions Policy Institute.

Anna Eagles,
Law Debenture

Anna is an experienced professional trustee at Law Debenture and represents Law Debenture on a number of Boards and Committees including the Smart Pension Master Trust board. She is an Accredited Member of the Association of Professional Pension Trustees.

Anna is also a qualified actuary, with over 20 years' pensions and employee benefits consulting experience before becoming a professional trustee. She is passionate about helping improve people's retirement and savings outcomes through better governance, value for money, information, and education.

Dominic Lindley, Independent Member

Dominic Lindley is an independent consultant specialising in pensions, financial services, and consumer protection. He has worked for the Financial Services Consumer Panel, Which? and New City Agenda, delivering improvements for consumers including a cap on pension charges and stronger protection against payment scams. Following the introduction of the Pension Freedoms he has written several reports on how consumers can be helped and supported to make better decisions about how to access their pension.

He is a member of the Pensions Dashboards Programme Steering Group which is developing data standards so consumers can use new online tools to access all of their pension information in one place.

Kate Fulker,
Head of Conduct, Vanguard

Kate Fulker is a Chartered Accountant, with more than 25 years financial services experience in the UK and overseas.

Kate is currently the Head of Conduct, Europe for Vanguard's European regulated entities. She was previously Head of European Compliance holding both the FCA's CF10 (Compliance Officer) and also the CF11 (Money Laundering Reporting Officer) approved persons designations.

Prior to joining Vanguard, Kate was the Group Money Laundering Reporting Officer (CF11) for a peer asset management firm. She was also Head of Financial Crime and served as the Chair of the Investment Association's Financial Crime Committee.

Ankul Daga,
Senior Investment Strategist, Vanguard

Ankul is a Senior Investment Strategist at Vanguard. He co-leads retirement planning research team globally and his responsibilities include publishing papers, building enterprise research models and meeting clients to provide a Vanguard perspective on long term investment implications. In addition to retirement issues such as retirement policy and life cycle planning he covers a broad range of investment topics, including, portfolio construction, passive and active investments and advisor best practices.

He has over 15 years of investment experience across trading, advisory and research functions at some of the eminent financial institutions. He joined Vanguard from Coutts, the largest wealth manager in UK where he was the Asset Allocation Director. Prior to that, he has been a Strategist with Merrill Lynch and Barclays, which is complimented with direct experience in trading and relationship management. He earned a Masters from Warwick Business School, is a CFA® Charterholder, member of Investment Association's DC Committee, member of Independent Governance Committee for Vanguard's UK investment pathways.

Appendix 2
Value for Money Framework

VfM criterion	Red	Amber	Green
Funds (Objectives & Performance)			
Money Market Fund		●	
Short-Term Bond Fund			●
Target Retirement Funds			●
Funds Charges			
Charges			●
Customer			
Processes to help provide information			●
Know the investor		●	
Retirement planning tools			●
Risk disclosure – expert investor			●
Risk disclosure – inexpert investor	●		
Satisfaction			●
Communication fit for purpose			●
ESG and Stewardship			
ESG		●	
Stewardship (insufficient information)	–	–	-
Other Services			
Complaints (number and handling)			●
Processing of financial transactions			●
Vulnerable customers		●	

Appendix 3
Jargon Buster

Annuity/annuitise: Guaranteed income purchased through a life insurance company.

Basis Points: This relates to the percentage point charge applicable, one basis point equals 0.01%.

Drawdown: The process of taking income from your pension pot while it remains invested.

Enhanced annuity: Guaranteed income purchased through a life insurance company, but with improved rates due to personal health and lifestyle conditions.

ESG: Environmental, social and corporate governance features for investment fund manufacturing.

Platforum: Industry comparator firm on investment platforms.

FCA: Financial Conduct Authority, the UK regulator for UK retail.

IGC: Independent Governance Committee, independent professionals assigned to assess value for money on Pathways.

KIID: Key Investor Information Document, Document explaining the key information of an investment fund.

MIFID II: Markets in Financial Instruments Directive.

Non-advised: Term used where a consumer has not had financial advice on their transactions and decisions.

Pathways: Pre-defined single investment funds for specific retirement choice.

Pension Wise: Government free guidance service explaining pension options to consumers. Website: www.pensionwise.gov.uk.

Sequencing Risk: the risk that the timing of withdrawals from a retirement account will damage an investor's overall return (and therefore retirement outcomes).

SIPP: Type of pension where the consumer self-selects their investments and has access to a wider range of choice and flexibility.

SRRI: Systemic Risk and Reward Indicator used to indicate the level of risk on an investment fund.

Stewardship: Relates to the management and oversight of the funds.

Target date fund/Target Retirement Fund: Investment fund which matures at a set date, normally chosen retirement data.

Transaction Costs: Underlying costs incurred when transacting in stocks and equities.

Vanguard: Investment management firm.

Vanguard consultant: Staff member who helps customers with retirement questions and process.

Vulnerable customer: Customer who may have a vulnerability through health, life events or scam.

Workplace pension schemes: Employer sponsored pension scheme.

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