PENSIONS AND LIFETIME SAVINGS ASSOCIATION

IMPROVING OUTCOMES FOR MEMBERS OF DEFINED CONTRIBUTION PENSION SCHEMES

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EXECUTIVE SUMMARY

The PLSA is very pleased to respond to this consultation. Pension schemes take delivering in the best interest of members very seriously and the Association works with pension schemes and the rest of the industry to drive up standards in governance and cost disclosure. We strongly believe that well governed schemes are able to deliver value for money for their members.

We welcome the Government's proposal to introduce new statutory guidance for trustees on how to complete 'value for members' assessments. Trustees will benefit from greater certainty around what is expected of them; which key issues they should consider; and when to make appropriate comparisons with other schemes. However, trustees are likely to need further guidance on the data and other evidence they should make use of, as well as the methodology to use for assessing specific factors and making a 'holistic', overall assessment. Having a sound evidential and methodological basis will be especially important in cases where trustees declare that it would be in scheme members' interest to move to a better value scheme.

Trustees should never assume that a larger scheme will always entail better value for members. For some there may be benefits arising from economies of scale. But not, for example where they are on a platform with a bundled provider. In addition there are a range of other value factors to consider including less tangible benefits for members, such as those which arise from a closer relationship with the sponsoring employer.

We would also encourage the Government to undertake further work to ensure that, where possible and appropriate, the approach to value assessments is consistent with the approach currently proposed by the Financial Conduct Authority (FCA) in CP20/9 'Driving value for money in pensions', for contract-based schemes; as well as any additional proposals and guidance from the Pensions Regulator (TPR).

Summary of our response

- Consolidation or scheme scale should not be an end in and of itself. Though we agree that there can be benefits to scale in terms of governance, access to expertise and availability of particular investment approaches, it is quality – and not the size of the scheme – which matters. Quality could include scheme benefits and guarantees that are available to members of smaller schemes, and the costs of wind-up should receive due attention. It is possible that these could be met by the trusts' funds.
- Trustees will need further clarity and appropriate guidance on how to ensure the views of sponsoring employers, and also of scheme members, are incorporated into any subsequent decision to wind up a scheme and consolidate.
- Additional reporting of net returns could be helpful to members where the information is presented in a meaningful way, as well as to other schemes in order to compare net returns for the purposes of value for money assessment. The Government should also design requirements for net returns that are based on information easily accessible to schemes, reflect the purpose for

which the reporting is intended, as well as with appropriate flexibility – in for example, time horizons - for the circumstances of different investments.

- We have been very supportive of the Government's intent to facilitate DC schemes' investment in illiquid assets, private markets and other alternative investments. We therefore believe proposed calculation adjustments for performance fees and additional guidance on costs excluded from the charge cap while holding physical assets will provide clarity for schemes and, in the fullness of time, could make an impact on illiquid asset investment in DC. However – as DWP points out in the consultation – many other, wider factors are at play and work should continue to consider these barriers holistically to deliver the best outcomes for members.
- We continue to support the additional clarity provided on cost and charges disclosure through the updated statutory guidance.

We would like to thank the Government for their willingness to engage with our members on the issues raised in this consultation.

About the PLSA

The Pension and Lifetime Savings Association (PLSA) represents more than 1,300 workplace pension schemes serving 20 million savers and pensioners. Our members include defined benefit (DB) and defined contribution (DC) schemes, master trusts and local government pension funds, together controlling £1 trillion of investments in the UK and global economy. Our membership also includes asset managers, investment consultants, law firms, fintechs and others who play an influential role in governance, investment, administration and the management of people's financial futures.

Our mission is to ensure that everyone has a better income in retirement. We work to get more people and money into retirement savings, to get more value out of those savings and to build the confidence and understanding of savers.

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ENCOURAGING CONSOLIDATION

We support schemes assessing value for members and that where schemes are unable to meet good standards, or to make necessary improvements, we believe consolidation may be an option.

We agree that where schemes are not currently able to demonstrate that they are delivering good value schemes should act to improve both rapidly and cost effectively.

However, the Government should be reminded that not all small schemes will find they are failing to deliver good value. We do, however, note the finding that most smaller schemes fail to meet standards of governance and trusteeship, with only 4% of micro schemes (which have between 2 and 11 members) and 1% of small schemes (which have between 12 and 99 members) meeting all of the governance standards[1]. However, it is unclear how many of these schemes will be caught within the estimated[2] 2,120 DC 'specified schemes' definition of £100m and at least three years old.

Whilst we appreciate that the Government has made clear its intention to cause greater consolidation, appropriate value assessments (and, where relevant, comparisons with other schemes) is something which all schemes should already undertake. Value for members assessments can lead to a variety of possible outcomes, many of which will amount to improvements to the scheme for the benefit of members; and only one of which will be a transfer to a different scheme (consolidation). Therefore, it is important to bear in mind when designing a value for members assessment that it should not be undertaken solely with the prospect of consolidation in mind.

We believe that the Government should also provide additional clarification around the scope of the intended provisions and to the different types of scheme to which the provisions will apply, including whether the membership is active or deferred. (We comment on this further below.)

Question 1: We would welcome your views on the reporting of net returns – how many past years of net returns figures should be taken into consideration and reported on to give an effective indication of past performance?

The PLSA agrees that the proposal to report net returns tackles an important aspect of value for members assessment, however, it is important that such information is delivered in a meaningful and readily understandable way for the intended audience, and in the context of other measures. We find it unclear whether the Government's intent is for members to better understand net return, or whether the publication is purely intended to aid scheme to scheme comparison.

We support reporting of net returns as an important part of facilitating comparison between schemes (where the proposal requires) on factors wider than cost. A holistic consideration of charges in the context of overall performance, particularly where risk adjusted, are welcomed. Trustees are already required to assess and review both past performance and expected future performance[3] and may well

[1] https://www.thepensionsregulator.gov.uk/en/media-hub/press-releases/new-figures-show-why-small-schemes-must-quit-the-market

[2] https://www.gov.uk/government/consultations/improving-outcomes-for-members-of-defined-contribution-pension-schemes/impact-assessment-improving-outcomes-for-members-of-defined-contribution-pension-schemes#fn:10

[3] See, for example, https://www.thepensionsregulator.gov.uk/en/trustees/managing-dc-benefits/investment-guide-for-dc-pension-schemes-/#d4d6456c3fdc4984890bad2725141938

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provide factsheets to members including the performance of all funds. The proposals about publication therefore appear to address the issue that publicly available information about investment performance of default funds may not be widely available. It is worth noting that this may, necessarily, be limited by restrictions as a result of bespoke and/or commercially sensitive arrangements. However, without publication the practicalities and feasibility of sharing information – which would require significant costly and time consuming data sharing protections for all parties including trustees, employers, advisers and so on - would likely be a significant barrier to relevant comparisons being made between schemes.

Currently we have found public data often focuses on master trust performance, and we find only limited public anecdotal evidence about investment performance (and indeed investment strategies) of smaller DC default schemes. If schemes are expected to compare themselves with others, particularly on net returns, then public disclosure appears needed. That said, disclosure as proposed would not make it straightforward to do so as the information would not be held in a central place that would be possible to interrogate.

Effective indications of past performance periods will depend on the circumstance of the investment and the time horizon over which it is designed to deliver its stated outcome. For example, a short term (one-three year time horizon) medium term (five years) and longer term (complete past history since inception of the investment). Given the long-term nature of pension saving a longer term past performance and net return assessment would be more appropriate, and we would like to see this reflected in the proposals. However, at a most basic calculation level, net returns should always be based on complete 12-month periods to deliver consistency with other fund reporting requirements, and reporting every three years may fit well with the requirement to assess defaults on this periodicity.

Care should be taken to clarify expectations on the Chairs' statement to avoid the risk that the compliance to avoid TPR enforcement drives scheme governance on this area. The Government should clarify both the intent for both schemes and members, and what is meant by 'reporting' rather than 'stating' net returns. In both cases we ask for this clarity given the intention for inclusion in the Chair's statement which therefore has associated compliance and enforcement considerations.

Providing net returns as proposed in the Chair's statement should only be done with careful consideration to the members' needs and understanding. For example, if the disclosure is intended for the benefit of members gross to net return illustrations should provide accessible definitions of included and excluded costs. Where the intent is for members to understand the full context of other information existing requirements for net annual return disclosures in other contexts, will be informative to the Government in understanding how members are likely to understand this information. Many of the regulatory disclosures in the investment fund space have undergone extensive testing, are delivered consistently by asset managers already and the information could in some cases therefore be available for schemes to use already in a format more easily comprehensible to investors.

Assessment at age cohort level, as proposed, should be approached with care as it could unhelpfully present members with information that appears to, but does not, provide them with an indication of net return on an individual level. This risks confusing members. The Government should consider whether this disclosure is intended for members to understand, or for other schemes for the purposes of their value for money comparison, and design and implement the approach accordingly and proportionately.

Question 2: Do you think that the amending regulations achieve the policy aims of encouraging smaller schemes to consolidate into larger schemes when they do not present good value for members?

The PLSA supports value for members and good governance and, where a scheme is unable to make necessary improvements, consolidation may be appropriate. We believe the amending regulations may help to achieve the aim to encourage smaller schemes to consolidate where a larger scheme represents demonstrably better value for members. We welcome the recent emphasis placed on schemes considering consolidation, but only where there is evidence that this improves member outcomes. We have therefore previously supported the idea that where small schemes are not able to improve their performance, they should consider whether consolidation is in members' best interest.

Some efficiencies of scale and scope are evident and, where it is the case that a smaller scheme cannot emulate or deliver greater value in some other way to members under the proposals we believe that it may be appropriate to seek consolidation into other, likely larger schemes.

However, we believe that the proposals confuse different models by which a relative assessment of value could be undertaken and the reasons for doing so. There is an absolute assessment of value – which under the proposals will now specify a comparison relative to other similar schemes - but also an assessment of value relative to other larger schemes, which might enable efficiency gains to be identified. The proposals appear to be designed to deliver a relative assessment. This may confuse the matter, as the final strand of the relative assessment of value appears to require comparison with a specific consolidation vehicle, which is likely in practice to be more akin to a procurement assessment.

On the one hand, a value for money assessment can be used by trustees to identify areas where a scheme is underperforming, and to seek to rectify those through specific actions; and on the other hand it can be used to provide an overall assessment that members would obtain better value elsewhere and to promote switching. These different objectives should be made clearer for trustees, notwithstanding the Government's overarching policy intention to promote consolidation.

While we appreciate that the policy intent behind the proposals is to encourage consolidation, the intended approach to value assessment appears to be driven by the premise (or starting point) that consolidation may be the expected outcome; whereas the purpose of such an assessment should be to determine whether a scheme is achieving value for its members, and how that can best be achieved (and where consolidation is only one possible option).

Approaching at least one provider that trustees have 'reason to believe… would accept the…scheme' suggests that schemes are expected to 'shop around' for future homes for their trustees as part of their assessment of their own quality. This will strongly nudge them to consider consolidation into that scheme – and risks creating a mini request for proposal/'beauty parade' process before the decision has even been taken to consolidate. Any later consolidation decisions risk fettering trustees' discretion – and this potentially limits the incentive for trustees to 'shop around' at a later consolidation stage. Guidance should make it clear that relying on the value for members assessment is not sufficient where only one possible 'home' for members has been considered in advance.

The Government's assessment of the cost to schemes on the trustees' consideration of the potential 'homes' for members included in the impact assessment - just over £60,000[4] per year - as is based purely on trustee time which we do not believe would be appropriate or realistic. One hour of trustee time per scheme is a significant underestimation of the costs of finding, considering and then assessing a potential consolidation vehicle. Additionally, we believe it is likely to be inappropriate in most cases that trustees do not take advice on identifying an appropriate scheme that they believe 'would take them on'. This guidance is also silent on how trustees should manage this relationship on an ongoing basis; we would expect further guidance to clarify that an open and fair process for selecting a consolidation vehicle is not prejudiced by previous consideration of providers for the purposes of value for money assessment.

To give an example, if the exemption for costs and charges disclosure applies for schemes less than 100 members – like comparison between very small schemes is not assumed by this proposal. Very small schemes will therefore necessarily undertake costs and charges comparisons relative only to larger schemes, one of which must be a consolidation vehicle (and therefore a very much larger scheme) which are likely to necessarily achieve greater economies of scale. Therefore the comparison appears to be designed, on some components of the assessment, to deliver results that will necessarily result in unfavourable comparisons by design rather than trying to compare schemes with a similar profile; this kind of comparison will have a homogenising effect on the overall market (trending towards larger schemes).

It is also important to recognise that some small schemes may have features which benefit the scheme members, by virtue of their small size and that any 'holistic' assessment, as proposed, should take these into account, alongside costs and charges. For a scheme with an active membership, these might include, for example, intangible benefits such as employer engagement or links to DB scheme benefits, governance, processes and investment options. Similarly, smaller scheme may have a more sympathetic attitude to hardship cases, or ill health retirements, or provide the comfort of speaking to a known member of the administration team (rather than a call centre). Members may value such subjective features highly. Trustees should take particular care to consider such aspects and whether members value them.

[4] https://www.gov.uk/government/consultations/improving-outcomes-for-members-of-defined-contribution-pension-schemes/impact-assessment-improving-outcomes-for-members-of-defined-contribution-pension-schemes#fn:10

Additionally, and significantly, schemes which have a closer employer connection may also have higher contribution levels. Transferring such a scheme to another provider may remove the incentive, and ease of employer support, for the scheme.

Under the proposals, trustees would be expected to benchmark their scheme against a provider's own value for members assessment, which is heavily dependent on asset size, membership demographics and contributions characteristics. We therefore question how easy it would be in practice for trustees to make genuine, like-for-like comparisons, given such variables. Benchmarking against such comparator schemes would necessarily be imperfect, meaning that any conclusion drawn is also likely to be imperfect and trustees should be conscious of these limitations.

Further consideration also needs to be given to the commercial and practical implications of transferring. The proposed comparison is with a small number of schemes (which are typically larger and include Master Trusts). But given that the assessment is undertaken prior to a full discussion with the comparator schemes, it may be hard for trustees to estimate accurately the true costs and value which the transferring members might receive. The value for members of a particular scheme under comparison is always specific to the bespoke costs associated with that scheme and reflects its specific characteristics – especially those of its membership. For example, publicly available pension costs data does not take account of the commercial discounts given to many (if not most) customers.

The fact that the proposed comparison would take place prior to working out the details of any consolidation (as well as a thorough examination of whether the 'receiving scheme' would be amenable to consolidation, and on what terms), means that trustees may not have a clear and full understanding of the value scheme members will receive if they are transferred to a new scheme.

We are also concerned that under the proposals trustees are not expected to consider the costs associated with wind up and transfer and, while we understand the difficulties complexities associated with this, in some cases (especially where transfer costs might end up being met from members' pots) it would not seem to be a full, overall assessment to decide whether a transfer would be in members' interests without factoring this in. We believe there should be additional protection for members to avoid additional costs to members which do not represent overall good value.

There may be additional difficulties for hybrid schemes (which may have only a relatively small DC offering), where options to wind up the scheme could be limited by the scheme rules. Similarly, hybrid schemes may have a larger than threshold total AUM despite the DC scheme assets being under £100 million.

The assessment overall also has a heavy focus on the past and not the future even though there is a requirement for trustees to consider where members will be better off in the long run. We acknowledge that future projection of value is difficult to develop, but more could be done to encourage an assessment which takes account of past circumstances as well as future scenarios; this will be particularly important where a (currently) small DC is projected to grow significantly over the next five/ten years.

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Question 3: Do you believe that the statutory guidance increases clarity about the minimum expectations on assessing and reporting on value for members for specified schemes? Are there any areas where further clarity might be required?

We believe that the guidance proposed will provide welcome additional clarity for schemes assessing and reporting on value for members for specified schemes. As above, however, trustees would benefit from further clarity around the intended objectives of the value assessment and methodology to use when undertaking it. We believe that the main objective of a value for members assessment should be to determine whether or not a scheme is offering good value to its members, not solely whether scheme members should benefit from consolidation.

We also suggest that further consideration needs to be given to the views of scheme members, and how these are included in any value assessment. This is especially important, given the overall assessment is intended to be about outcomes for members – as denoted by the terminology used ('value for members', as opposed to 'value for money').

Similarly, we suggest that further clarity also needs to be given to the intended role of sponsoring employers, and how they should be consulted. It is certainly not a given that an employer will automatically agree with the trustees that wind up and consolidation is the best course of action – and this may be especially the case under current market conditions, where employers have many competing pressures and priorities. For schemes with active members, the scheme is likely to be part of an employer's benefits package which is likely to carry advantages for members – employer consent may be especially important in such a situation. As discussed above, there are often clear benefits for members arising from the close relationship a smaller scheme has with a single employer. We therefore suggest that the exact nature of the duties for trustees to consult with employers should be made clear and explicit.

Further consideration should also be given to differences in the type and size of schemes to which the requirements would apply. There are likely to be significant differences in the needs of members between those schemes which have a large, active book; and those which have a large, deferred book.

It is common for a scheme with a large, active book to be relatively strong and stable and to enjoy many aspects of good employer support. Whereas, a scheme with a large deferred book is more likely to meet its costs out of the savings of past employees, and to contain a high proportion of members to which the sponsoring employee has less of a natural affinity. Additionally, such a scheme may be vulnerable to high volumes of future transfers out, which has the potential to make them more unstable.

In other cases, an older scheme without a sponsoring employer might have very different implications for wind up and consolidation, with wind up or transfer costs potentially being met from members pots. (We note that the proposals do not require trustees to consider the costs of transfer.)

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GUIDANCE ON THE GENERAL PROPOSED APPROACH TO ASSESS VALUE FOR MEMBERS

A combination of the charge cap, the public discourse on costs and charges, and the absence of a consistent way to measure and compare value for money, has encouraged trustees to focus on reducing costs rather than seeking performance. We believe that costs should not be a proxy for value on its own. Because the proposals remain relatively silent on the methodology for trustees to use, there is a risk that trustees will resort to using either a proxy, or too simplistic a 'formula', to come up with a single value rating. This is clearly not the Government's intention but might be an adverse outcome.

We have long been supporters of driving up quality in schemes and, though there are some benefits of scale that cannot and should not be ignored, we do not feel that small is a suitable proxy for poor. As above, small schemes may have advantages (other than those relating to economies of scale savings) which are features of their small size and scheme member characteristics. For example, scheme members often feel more connected and appreciate being part of a smaller, well-run workplace scheme.

TPR guidance has previously encouraged less complex schemes with a small number of members to consider whether it is more proportionate to take a simplified approach to value for member assessments[5]. The proposals appear to take the opposite strategy to former TPR guidance and place a greater administrative and resource burden on some of the schemes with the fewest resources. It therefore should not be underestimated how significant the changes proposed in this consultation may be for some small schemes.

Any effective and thorough value for members assessment is extremely time and resource intensive. We are not persuaded that the Government has fully appreciated, or thoroughly costed, the projected outlays involved for schemes. Some of the PLSA's members have commented on the considerable time and resource commitment needed to identify the data needed to make such comparisons. Without sufficient time and resource, there is a risk that trustees may feel pushed into making value assessments (with potentially critical implications for members), which are not fully evidenced.

Lastly, the costs of administration borne by the employer in the small scheme should not be ignored as it would not be in members' best interests to ignore this. We previously argued this and are pleased that DWP have taken it on board.

GUIDANCE ON THE SPECIFIC FACTORS INCLUDED IN THE ASSESSMENT OF VALUE FOR MEMBERS

Following a period of consultation with the pensions industry, the PLSA set out its initial views on what elements should be included in a value for money assessment in its report 'Hitting the Target' (2018). These elements include: engagement, investment governance, scheme governance, and administration. Since then, the PLSA has held numerous discussions with its members and other stakeholders about what they find most effective to include in value for money assessments.

[5] https://www.thepensionsregulator.gov.uk/en/trustees/managing-dc-benefits/5-value-for-members

The PLSA also believes that it is important to try to achieve a level of consistency to VFM across the pensions markets, and is supportive of the collaborative approach taken by the FCA and the Pensions Regulator (TPR) in their 'Joint Regulatory Strategy', as well as in working closely with the Department for Work and Pensions (DWP). Whilst the PLSA recognises that a 'one size fits all' approach may not be appropriate for VFM assessments across different types of pension scheme, it would be helpful if areas of difference can be clarified and explained, so that trustees and IGCs can better understand expectations.

Most recently, the FCA has consulted on a proposal for value for money assessments to be undertaken by IGCs.

While there are similarities between FCA's and DWP's approaches, there are some differences – for example in respect of the criteria used to assess the quality of governance and administration; as well as in the approach to benchmarking costs, charges and net returns.

We acknowledge that many of the aspects which trustees should consider, under the proposals, are already within the remit of trustees, but it is important not to underestimate the significant impact on trustee time, resource and costs associated with the proposals. We do not agree that all information required for comparisons will be 'easily accessible', as described in the consultation paper.

Costs and charges.

As above, while we agree that costs and charges are a vital aspect of any value for members assessment, considering net returns over a single year, leading to consolidation would not be an appropriate approach. We therefore propose that the guidance should support a longer term period over which trustees should consider net returns – ordinarily we would expect this to be at least five years. Of the PLSA's scheme members we asked, the majority (80%) felt that costs and charges would be the most burdensome element of a value for members assessment.

We also believe the costs of administration should be further clarified in assessment guidance and we note that the charging structures of administration providers can often be hard to ascertain and compare.

It has often been savers in the smallest schemes which have benefited from the impact of the charge cap, so it may be the case that for the small schemes subject to the proposals charges may not be the most obvious point of difference and it will be important to consider other factors in conjunction. (Though we note that the consultation paper says that average charges in smaller schemes are nearly double those of the largest schemes.)

Investment returns

We believe that the proposed guidance is well constructed and sensible.

We also note that (in its consultation proposals referred to above) the FCA has proposed several factors which it considers would be important in assessing investment performance. These factors

include: investment returns delivered and expected, net of fees; investment risk profile – tailored to the needs of members, and monitored and maintained within acceptable limits; and investment objectives and strategies aligned to retirement options and choices. We believe these are important and appropriate factors to include in an assessment. This is one area where the approach across trust-based and contract-based pensions could be better aligned.

Governance factors

We welcome the inclusion of governance factors as an important part of any value for members assessment. It is well-established that a well-governed scheme is likely to lead to better outcomes for members, as well as a potential impact on net returns.

The consultation paper proposes that the level of trustee knowledge, understanding and skills within the trustee board as a whole will be used as a measure of value for members in the extended value for members' assessment. We agree that this is a vital aspect of ensuring that trustees are in a position to provider appropriate challenge and contribute to a well-run scheme and should be included in the overall assessment of the trustees' own scheme. However, the Government will need to consider further how these aspects should be included in making comparisons with other schemes, and whether trustees are likely to have the relevant information they need to assess this.

Other specific factors

Member views: As discussed above, further consideration should be given to how member views are meaningfully incorporated in a value for members assessment. For example, if a member survey is undertaken, when should this be carried out to ensure member views are allowed for?

Employer views: There should be additional clarity provided around the role of the sponsoring employer to provide their agreement and consent to any wind up and transfer, and as to how their views should be considered.

Data and sources: Some elements of the proposed value for members definition could benefit from additional explanation or clarification and there is a lack of guidance around the data and sources of information.

Balance of factors: There is no information on how to weight different metrics – but we do agree that excessive weight should not be given to costs and charges than net returns. The relationship between the three proposed elements has not been sufficiently articulated.

While we agree in principle that trustees should undertake an assessment which involves a range of different factors, the lack of a clear methodology or guidance on how to weight different factors may lead some trustees to struggle to understand expectations. The PLSA would be keen to discuss further possible guidance for trustees.

Guaranteed benefits: Though we note that those with guaranteed benefits are not necessarily going to be better value for members, we would like the guidance to be clearer that in most cases we think they are. The Government's objective to promote consolidation should not detract from the need for members to achieve good outcomes.

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Valuable benefits: We welcome the fact the Government acknowledges there are 'particular classes of smaller bespoke schemes that are highly regarded and offer valuable benefits'.

Making changes ahead of the new assessment: Demonstrating value should be possible before the new proposed assessment and duty to make comparisons. Trustees should weigh up the time, skills, capacity and costs of making sufficient improvements. They should be confident where they can raise standards to meet and continue to meet the ongoing demands of managing savers' money over the long term. Failure of this assessment should be considered exceptional circumstances – trustees should in the first instance seek to improve rather than initiating wind up.

REPORTING

We believe that in principle it may be an appropriate vehicle to include the proposed value for members assessment information in the scheme return and DC Chairs' statement. However, it will also be important to ensure that reporting is aligned where possible and takes account of the frequency of assessment. We believe that any reporting requirements should be proportionate and well-directed.

Given that the Chair's statement is produced annually we believe, this could place a heavy burden on trustees and other options should be considered further. For example, a more formal reporting structure and concise reporting requirement might provide greater clarity, both to those who are responsible for running schemes, as well as for scheme members.

There may also be circumstances where exclusion from the annual reporting requirement could be appropriate – for example, in cases where consolidation is already under consideration by the trustees. As discussed above, we believe that the Government needs to consider further the availability or otherwise of key evidence and data to enable trustees to make effective comparisons with other schemes. Whilst the consultation paper addresses comparisons using published reports, further detailed guidance is likely to be required.

EXAMPLES OF AREAS WHERE FURTHER GUIDANCE IS NEEDED

We believe there are several areas where additional guidance (or further clarity) is needed and we would like to work with the Government, industry and regulators to progress this work.

- 'Broader elements of good value' – e.g. employer contributions to members funds (above AE minimum), security of assets, employer contributions to costs of services, value over the longer term.
- Decumulation – these should be a clear area of comparison for schemes in their value for money assessment. Our recent work on decumulation, *PLSA's DC Decumulation: Evolving the Pension Freedoms – Final Recommendations*[6], calls for the establishment of a new regulatory framework to help savers with the complex decisions they face when choosing how to assess their pension at retirement. We found that schemes deliver, and savers receive, different degrees of support at-

[6] https://www.plsa.co.uk/Policy-and-Research-Document-library-DC-Decumulation-Final-Recommendations

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retirement and different access to products and solutions and, without intervention, this results in risks to savers.

- Availability of – and expectations around – data sources to enable comparisons
- How to weight objective factors such as net performance, alongside more subjective elements such as member communications
- The evidence trustees should consider to enable them to reasonably conclude they have reason to believe a comparator might be receptive to consolidation
- The role of the sponsoring employer in a value assessment (and any decisions to consolidate)
- How and when to incorporate the views of members in any assessment
- Further guidance where trustees have identified that better value can be achieved elsewhere but it has not been possible to find a scheme willing to accept a transfer

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DIVERSIFICATION, PERFORMANCE FEES AND THE DEFAULT FUND CHARGE CAP

We are pleased that the Government heeded our concerns in relation to the proportionality of any new requirements on reporting holdings in illiquid assets and the wider context of ever-increasing reporting requirements for other areas of scheme investment.

We have long been supporters of the current charge cap, but we do not believe that it should be reduced. Given the wider topics to which this consultation pertains it is worth reiterating that we have previously found evidence that an 'overly cost focused approach' is already adopted by some trustee boards in relation to their default fund selection and that there are many reasons for this. Reducing the charge cap risks entrenching either an artificial tolerance for certain charges irrespective of other pertinent factors, or encouraging clustering around an artificial charge ceiling. The message sent by reducing the charge cap could impact on trustee behaviour and investment innovation, particularly in a market where it is becoming ever more challenging to generate real returns. These outcomes would be difficult to predict and mitigate for if the charge cap were reduced, especially in the context of regulators and Government focusing on cost as a key component or proxy for value.

We are pleased that the Government has acknowledged that the uncertainty around the level of the charge cap may present a constraint on schemes from taking long term investments. We continue to urge the Government to maintain the current charge cap level, and assure schemes that the level will not change for a sufficient period to make this possible.

Question 4: Do the draft regulations achieve the policy intent of providing an easement from the prorating requirement for performance fees which are calculated each time the value of the assets is calculated?

We have long called for clarity and we think this proposal provides both the standardisation and clarity that is needed in one key and important area.

DC schemes have historically has little to no exposure to private markets, and compliance with the charge cap has, at least in part, contributed to this constraint. Historically we have found the charge cap has meant advisers are less likely to recommend the use of a fund with a performance fee in a default fund, except where only a maximum, capped performance fee is eligible to be paid on the underlying fund.

Question 5: What should we consider to ensure a multi-year approach to calculating performance fees works in practice?

Question 6: We are proposing a five-year rolling period. Is that appropriate or would another duration be more helpful?

Question 7: We are proposing offering a multi-year option as an alternative to an in-year option for schemes. Do you have any suggestions on how to improve this offer?

Question 8: To what extent will providing a multi-year smoothing option give DC trustees more confidence to invest in less liquid assets such as venture capital?

We support the intent to deliver performance fee calculation over multi-year periods where this aligns with our wider desire to encourage and support the availability of more long term investments, such as illiquid assets, to DC savers.

Making a multi-year approach functional will require the inclusion of clear guidance about the permitted calculation methodologies, if they were to be prescribed. However – while consistency is desirable - we agree that the burden of the calculation on the scheme should be minimised as much as possible. One way to achieve this might be using existing, agreed calculation methodologies and bases for these methodologies that asset managers are comfortable and confident providing consistently across their client base. For example, in private equity markets[7] Internal Rates of Return, Modified Internal Rate of Return and Multiple of Invested Capital are more meaningful than performance measures used in public markets such as change in Net Asset Value over the period to which the report relates.

Flexibility, more generally, is likely to be desirable to achieve the desired aim, particularly where the structure and time horizon of the specific investment is likely to impact on the multi-year duration appropriate to calculation. For example, 'carry' is mentioned in the Consultation (see paragraph 63) but also target return dates and hurdle rates may impact on the reasonable timeframe over which performance measurement would be meaningful.

Where adjustments for the effect of costs and charges include performance fees that have been calculated across a multi-year basis we believe care should be taken in the explanation of this to members as it is a highly technical and is otherwise likely to confuse rather than aid understanding.

Question 9: Do the draft regulations achieve the policy intent? Do you have any comment on the definitions used?

Yes, we agree that the draft regulations should act to achieve the policy intent, though could be further broadened to better encompass non-property asset classes. However, this barrier is unlikely to be the sole impediment to DC investment in property and infrastructure. We would refer the Government to the concerns raised by respondents, particularly regarding the other constraints on investing in illiquid assets (see – for example – Chapter 3, paragraphs 29-31) perceived and potential 'conflation of public policy and fiduciary goals' (Chapter 4, paragraph 15).

The draft regulations are, however, helpful in not only providing additional clarity but also defining the scope of previous guidance on exemptions to the charge cap in holding and maintaining physical assets.

[7] https://www.bvca.co.uk/Portals/0/library/documents/BVCA%20Perspective%20Series/Private%20Equity%20Performance%20Measurement.pdf?ver=2015-04-09-105554-523

UPDATES TO STATUTORY GUIDANCE: REPORTING COSTS, CHARGES AND OTHER INFORMATION

Question 10: Do you believe that the updated statutory guidance increases clarity about the minimum expectations on both the production and publication of costs and charges information? Are there any areas where further clarity might be required?

Yes.

We support this guidance and believe it provides much more information about both the production and publication of costs and charges information.

We believe that it is important to deliver information with the objective to facilitate members taking good decisions. Context and explanation may, therefore, be very important so that the information is meaningful and schemes should not be constrained from delivering this information in the manner best suited to their membership. The disclosures as envisaged risk adding complexity for savers who may be ill-equipped either by virtue of the structure or of their understanding to take relevant decisions.

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OTHER CHANGES TO LEGISLATION

Question 11: We propose that where the default arrangement includes a promise, the trustees of the scheme should be required to produce a default SIP. We propose that this should be produced within 3 months of the end of the first scheme year to end after the coming into force date.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

No comments.

Question 12: We are proposing that, for relevant schemes, charges and transaction costs should be disclosed for any fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

Yes.

We support this policy and agree that the proposed legislation achieves the policy intent.

Question 13: Do you agree with this proposed change? Do you have any other comments on this topic?

No comments.

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