PENSIONS AND LIFETIME SAVINGS ASSOCIATION

THE OCCUPATIONAL AND PERSONAL PENSION SCHEMES (GENERAL LEVY) REGULATIONS REVIEW 2023 PUBLIC CONSULTATION: PLSA RESPONSE

NOVEMBER 2023

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ABOUT US

The Pensions and Lifetime Savings Association is the voice of workplace pensions and savings. We represent pension schemes that together provide a retirement income to more than 30 million savers in the UK and invest more than £1.3 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs, and others who play an influential role in people's financial futures. We aim to help everyone achieve a better income in retirement.

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INTRODUCTION

The PLSA agree with the belief that good regulation results in well run schemes. This is an idea that we have long championed. The PLSA also remain supportive of the work of the Pensions Regulator, the Pensions Ombudsman, the Money and Pensions Service. There is a clear need to address the funding deficit, however, it is disappointing that the Government has not listened to the calls from pension schemes to first conduct a full structural review of the General Levy before any increase is implemented.

In 2020, the government stated that it would focus its attention on reviewing the structure of the levy and consulting with industry. This full structural review has yet to take place. It is firmly the view of our members that the principles for the review should be:

1) To place bounds on cross subsidy. Cross subsidy is an inevitable feature of levies and is in some cases desirable. But it should be limited in the following ways:
    - The costs of "greater good" regulation should not fall disproportionately on any one group of levy payers.
    - Schemes should generally fund the regulation of the benefits they offer.
2) Distribution of costs should be consistent with government policy for the pensions market. It should not focus on any one market sector. It should not create perverse commercial incentives.

In our response to the previous DWP consultation on the General Levy, we made it very clear that our members believe that greater transparency is required. This should come in the form of how costs are apportioned to service different parts of the pension sector. The bodies that are funded by the levy must set out how they intend to control costs so that we are not in a similar situation for the next review whereby more demands are placed upon schemes to fill an ongoing deficit. Further to this, the consultation gives mention to the Starks recommendation, which has been accepted by the Government. If pension schemes are eventually expected to fully fund the running of TPR, the industry's calls for transparency and accountability become all the more important. Our members look forward to being able to give their feedback on this topic when the Government decides to launch a consultation.

In addition to the above points, the proposals will still leave automatic enrolment providers paying on a per member basis, when they currently have mass membership and low assets under management. The General Levy, the Fraud Compensation Scheme (FCF) levy and the Financial Reporting Council (FRC) levy are all calculated around the per-member basis. When the per-member basis for levies was devised, Master Trusts did not exist. Now, they are an integral part of the pension market, with many millions of members. They have the greatest number of member accounts, however, they hold a relatively small proportion of the assets in the occupational scheme sector, and their member balances are generally low.

Under Option 1, as a result of the levy being calculated on a per-member basis, despite the levy fee remaining unchanged, Master Trusts will be disproportionately impacted as their total contributions will rise by 33.5%. The result of this is that Master Trusts, for example, will see their total contributions to the levy rise by 33.5% under Option 1. This figure worryingly grows to 60.9% under Option 3.

The proposals also have no regard for the challenge of inactive small pots, which we hoped to see excluded from per member calculations as an initial reform. Whilst the government is making progress on the issue of inactive small pots, it will be a number of years before the stock of these start to be addressed.

Finally, the inclusion of a £10,000 premium fee being added to schemes under 10,000 members, from April 2026, seems wholly inappropriate. The PLSA, and our members, are concerned with this for the following reasons:

- The proposed premium will inevitably make some good schemes appear – according to the new Value for Money framework – poor value purely as a result of the fee. It may force good value schemes to wind up, which can ultimately cost members more money in the process.
- This would appear to be an aggressive attempt to inappropriately force consolidation of small schemes via an indirect mechanism.
- All schemes with fewer than 10,000 members fall in scope, however, DWP highlight it is generally schemes with 2-11 members that have poor governance.
- Uncertainty whether TPR will require even more funding in order to be properly equipped to take action in the event of a large number of schemes not paying the £10,000 fee.

We strongly urge DWP to rethink these proposals and have a full structural review prior to any levy increases.

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QUESTION 1 – Which option do you prefer?

PLSA has chosen to only answer this question as it would not be appropriate for us to answer the other ones given our role as a trade association. We have encouraged our members to respond to all questions relevant to them.

A key request of the PLSA when we last responded to DWP proposals on the General Levy was that increases should not take place in the absence of a structural review to establish a settled and long-term approach to the levy. As the Department continues to put forward options that increase the levy, without addressing industry's concerns, the PLSA do not support any of the three proposed options.

The principles for the structural review should be:

1) Place bounds on cross subsidy. Cross subsidy is an inevitable feature of levies and is in some cases desirable. But it should be limited.
   - The costs of "greater good" regulation should not fall disproportionately on any one group of levy payers.
   - Schemes should generally fund the regulation of the benefits they offer.
2) Distribution of costs should be consistent with government policy for the pensions market. It should not focus on any one market sector. It should not create perverse commercial incentives.
   There also needs to be greater transparency in respect of:
   - What part of the levy costs relate to which bodies, areas of activities, projects;
   - How the levy costs relate to other funding - such as for the Pensions Dashboard Programme, and the Master Trust Authorisation fee;
   - Which costs are incurred in respect of specific scheme types; and
   - Which costs are borne for the greater good.

Pension schemes are expected to meet high standards of financial governance with DC schemes operating the creation of the deficit within charging caps and DB schemes operating to the DB funding code. Master Trusts have been through a rigorous authorisation regime with capital reserves and continuity strategies. For the schemes that fund the levy there is a significant gap in transparency about how this deficit has accrued and how costs are apportioned to service different parts of the pensions sector.

There does not appear to be appropriate checks and balances on expenditure, with a large deficit built up and projected, and further costs likely with fresh legislative obligations. We are keen to see a cost benefits analysis for any increase in levy and commitments for better financial management with controls that check and report spending. This request of ours becomes even more necessary in light of the Government's acceptance of the Starks Recommendation. Our members would like to see a fair and long-term settlement being reached as this would help to prevent a situation such as the one we are currently in repeating itself. It doesn't seem wise for Government to come back to industry every three years with funding options to address shortfalls. A long-term settlement would

prevent any future deficits growing at TPR. This promotion of good money management at the regulator would come with the added benefit of providing schemes with clarity and confidence. This will ultimately help their members outcomes in retirement as the schemes will be better financially prepared and will not have to worry about being hit with high funding requests at relatively short notice.

The need for a clear settlement is also important in light of the growth of responsibilities and regulatory duties, without clear evidence that the costs on schemes have been properly accounted for, or the overall costs of the regulator and other bodies are being managed within the budgeted envelope. A structural review of the Levy system would provide the opportunity for inefficiencies to be brought to attention and resolved. This would economically benefit the governmental pension bodies, pension schemes and pension members.

PLSA view on Option 1:

Option 1 is fundamentally unworkable. Whilst schemes are concerned about the lack of accountability surrounding the ever-growing deficit, they equally understand the important role that they play in funding the work of the regulator. To simply cap contribution rates to the General Levy at the current level would mean that this issue will be even greater when it is inevitably revisited at the next review. In addition to this, schemes need to have confidence in the ability of their regulator. An option that does not address funding issues with TPR could serve to undermine that confidence. This option also disproportionately impacts Master Trusts as, owing to the fact that the Levy is paid on a per member basis and the trajectory of Automatic Enrolment and consolidation, they would see their total contributions rise by 33.5% in just three years, despite the levy remaining unchanged. This would appear to be contradictory to the Governments intentions to foster an environment that is conducive to consolidation.

It is surprising that the Department has chosen to include this as an option. In the very unlikely scenario that this option is advanced, the PLSA believes that a further consultation would be required as the activities of the bodies that are indirectly funded by the General Levy would need to be urgently paired back due to the funding imbalance and this should only be done with input from industry as otherwise it would represent a material risk to savers.

PLSA view on Option 2:

As previously mentioned, DWP must take steps before our members feel comfortable supporting any of the options put forward. However, of the three presented, this seems to be the least damaging. It would help to close the deficit and it would not be applied as disproportionately across different kinds of schemes as Option 3 The fundamental issue of this proposal is that it would increase the burden on Master Trusts by over 60% in just 3 years. Master Trusts are already concerned with the funding situation and this option does not address that. At a time where the Government has made their position on consolidation and member outcomes clear, this option, without accompanying reform on how the levy is calculated, risks acting as an undermining factor. If the Levy grows at this alarming rate for Master Trusts, it could make consolidation less attractive, with it also hurting member outcomes.

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At a time when the Government is working to improve member outcomes, increasing the Levy by 6.5% year-on-year is counterproductive. DWP are right to note in the consultation that this option "*represents significant in-year increases and does not support the policy direction*". A 19.5% increase over three years will put pressure on schemes to adapt to this. This may come at the detriment of member engagement and member outcomes.

PLSA view on option 3:

This is the option that has led to the most unease amongst our members. First, the 4% increase would appear fair as this is below the current inflation level of 6.1%, - though by the time this comes into effect it may be higher than prevailing inflation. Secondly, the inclusion of a £10,000 premium fee being added to schemes under 10,000 members from April 2026 seems wholly inappropriate for the following reasons:

- Lack of justification – The justification provided in the consultation is insufficient. DWP put forward the very broad assertation that it is schemes with 2-11 members that are poorly governed, and this measure will remedy that by encouraging mass consolidation. Ultimately, this is a consultation is meant to be about the General Levy adequately funding the activity of governmental bodies. It should not serve as a back door channel for an aggressive vehicle which serves to improperly encourage consolidation of schemes with wildly varying ranges of membership figures. In addition, it is unclear how DWP has come to the conclusion that 50% of schemes under 10,000 members will choose to consolidate and the other 50% will be in a position to pay the £10,000 fee from April 2026. We would welcome this analysis being published.
- Too arbitrary - The categorisation of all schemes with under 10,000 members as 'small' is puzzling. To highlight why this is the case, one must look at how TPR defines schemes. In short, schemes with fewer than 12 members are classed as 'micro schemes', those with 12-99 members are classed as 'small' and those with over 1,000 members are classed as 'large'. This leads us to question whether this is a case of a sledgehammer being used to crack a nut. A more appropriate response would be for DWP to come out and explain what they deem a poorly performing scheme to look like and assess whether they should then contribute more towards the General Levy as a consequence. Further, it is also not clear why £10,000 is the figure that has been set for the premium. As it is designed to more than double levy funding (£93.5m in 2025/26 to £200.9m in 2026/27), one must ask why it needs to be done in 2026 if the deficit is not due to reach reach the £205m mark until 2030/31? This leads to the potential that the £10,000 premium fee, paid at the compliance rate the DWP predict, could result in a General Levy surplus. No mention of this is given in the consultation. As it stands at the moment, this option is too arbitrary.
- Inadvertent impacts -The proposed premium will inevitably make some good schemes appear – according to the new Value for Money framework – poor value purely as a result of the fee. It may force good value schemes to wind up, which can ultimately cost members more money in the process. If DWP have given consideration to this, it would be helpful if they came out and explained how this fee is meant to interact with the Value for Money framework.

- Compliance - It is not clear that TPR is properly equipped to deal with the scenario where is needs to take action in the even where a large number of ‘small’ schemes do not pay the £10,000 fee. An assessment on this needs to be made first as it could inadvertently lead to the deficit growing due to the need to hire more enforcement staff.

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