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Submitted via email to:
pensions.charges@dwp.gov.uk

16 July 2021

Dear Sir/Madam

Permitted charges within Defined Contribution pension schemes

I am writing on behalf of the **Association of Consulting Actuaries (ACA)** in response to the above-named consultation.

The ACA is the representative body for UK consulting actuaries. Our members are all qualified actuaries, mainly Fellows of the Institute and Faculty of Actuaries. Members provide advice to thousands of employers and pension schemes with assets exceeding £1 trillion, including most of the country's largest schemes as well as thousands of smaller arrangements.

We welcome the opportunity to comment on this consultation. The ACA wholly supports pension savers receiving good value, and we believe that facilitating ease of comparison across different pension providers and charging structures is important.

However, as we have stressed in previous responses to consultations and calls for evidence on matters relating to costs and charges, charges alone (and standardisation of these) are just one element of a good quality scheme, and standardised charges will not deliver value for members in isolation. Indeed, such an approach could have negative consequences for members and for industry innovation. Instead, DC governance standards must continue improving, focussing on value rather than just costs and charges.

Our comments on specific questions raised in the consultation are set out below.

We hope that you find the contents of this letter of assistance. We would be happy to discuss them further if that is helpful. In that event, please contact me on 07557 031198 or at tessa.page@mercer.com.

Yours sincerely

Tess Page
Chair, Defined Contribution Committee
On behalf of the Association of Consulting Actuaries Limited

Association of Consulting Actuaries (ACA) response

1. *Do you agree with our proposal that the de minimis should apply to all active and deferred pots? If not please outline why.*

   We agree with this proposal.

2. *Do you envisage any challenges for members and providers if the de minimis is applied to multiple pots within the same scheme?*

   Applying the de minimis across pots within the same scheme should in principle be straightforward for many schemes. However, some older schemes and / or those with legacy providers (bundled AVC type arrangements, for example) may struggle to implement this as records may not be digitised and member data can be poor compared to newer schemes.

   The consultation also states that "if a member has multiple pots with other providers, who charge flat fees, the de minimis would apply **across all of their pots**." This would be more challenging to implement and there would be data sharing and security issues (some of which would be addressed by pensions dashboards).

3. *Would proposed implementation in April 2022 create any business or operational challenges?*

   Bandwidth is a significant issue for many trustee boards and scheme providers. In short order, governance bodies and other relevant stakeholders have to prepare for simpler annual benefit statements, pensions dashboards, changes to the requirements in relation to value for members, consolidation considerations, taking action on climate risk (including TCFD reporting for schemes in scope), and the new code of practice. This is alongside existing matters such as Chair's Statement and Implementation Statement obligations and triennial reviews of scheme investment strategies.

   It would be helpful to align the existing initiatives in relation to small pots and pensions dashboards with the timelines, so that these activities can be tackled hand in hand.

   Very clear communications to governance bodies and scheme members will also need to occur in advance of implementation, and this should be built into the timeline.

4. *Does the draft Occupational Pension Schemes (Charges and Governance) (Amendment) Regulations 2021 achieve the policy intent for implementing the de minimis?*

   We are comfortable with the draft regulations.

5. *What are the full financial costs of adopting the de minimis for your business? Outline which costs are one-off or ongoing. Please outline how many pots will be affected within your business and the types of members who own these pots below £100?*

   As the ACA is not a direct pension scheme provider, this question does not apply.

6. *What are the non-financial or indirect impacts to businesses and members? Please outline how many pots will be affected within your business and the types of members who own these pots?*

   As the ACA is not a direct pension scheme provider, this question does not apply.

7. *In introducing a de minimis the policy objective is not intended to inhibit scheme consolidation of multiple deferred small pots. Could you tell us if you think there would be any impact?*

One potential unintended consequence would be the risk that the de minimis limit may make some individuals' funds and / or bulk scheme demographics less appealing to providers on a financial basis. This might prompt a refusal from some providers to accept transfers in of a certain size (either individual transfers or bulk business).

We have observed some providers declining to bid for schemes where contribution flows and pot sizes are modest, and where employee turnover is high (e.g. retailers). The new de minimis system may exacerbate this issue. We are also concerned that a particular demographic, for example women who have had career breaks, could be disproportionately impacted.

8. *Do you think that members (in particular AE) have an understanding of your scheme costs and charges? If so, what evidence do you have to support this?*

We note three points:

- Interactive Investor's report into pension transparency of December 2020[1], highlighted that 48% of pension savers do not know how much they pay to their provider in charges. In the qualitative research that formed part of this report, individuals were able to locate their scheme charges and costs easily, but once found did not understand the percentages. We note that the different language in this area is not helpful (charges, costs, fees, spreads, AMC, TER, AFEs, OCFs are all terms used in this context).

- As part of the ACA's 2020 Pension trends survey[2] of UK employers, the ACA asked respondents about the level of employee interest in the level of charges within their pension arrangements. Just 3% reported "much more interest", and 14% "more interest". The remaining 83% reported no change in the level of interest in this topic.

- Anecdotally, from our experience as advisers supporting trustees and employers with preparing cost and charge disclosures, and drafting responses to member queries, we do not believe these topics are well-understood. There is little engagement with annual cost and charge disclosures, as identified by the DWP in its recent statutory review of the Chair's Statement requirements ("there is little evidence that members know it exists").

9. *Does the current system impede members from carrying out a comparison of costs and charges between different schemes? If so should the system be reformed to allow for simple price comparison of costs and charges?*

Whilst cost disclosures have improved in recent years, particularly for workplace schemes, there remains inconsistency in the calculation basis, format, and language used. A uniform structure would improve ease of comparison.

To an extent, the requirement to now include illustrations of the impact of costs and charges in pounds and pence terms within the annual Chair's Statement has not helped with comparisons, as schemes use different assumptions for investment returns, starting pot values, inflation, etc.

A requirement for all schemes to report using industry standard assumptions would be beneficial to facilitate comparisons, alongside a consistency in the language used to describe costs and charges.

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[1] https://www.ii.co.uk/pensions/SMMM

[2] The ACA 2020 Pension trends survey included 281 responses from employers, running over 500 different schemes. Statistics are as at 31 July 2020 when data for the survey closed.

10. *Do you agree that the Government should move to a universal charging structure within the default fund arrangement? If so how best could the Government implement this change in order to manage the impact on the industry and members?*

We believe that a universal charging structure would help to support better member, trustee, and employer comprehension of costs and charges.

However, this should not be the only policy driver. The current flexibility in the permitted charging structure allows scheme providers to tailor their charges for their service proposition and membership demographics.

A move to a single charging structure, based on a single percentage charge for member borne costs, would be disadvantageous to some members and will also affect provider revenue and profitability. For some, this will be significant and there is a risk that this has a negative effect on members.

For example, providers may cut costs elsewhere (online services, communication and engagement strategies, investment sophistication, customer service support) to offset the impact. Whilst providers will be better placed to comment on the magnitude of the impact, the ACA would be against any move that restricts innovation and choice for scheme fiduciaries and for members.

Finally, we note that NEST would have an unfair market advantage as any negative impact would be supported by the UK taxpayer, whereas commercial providers do not have this luxury.

11. *What are the benefits of standardisation for other government initiatives such as simpler statements and the pensions dashboard?*

Standardisation would certainly make data gathering and the presentation of information easier for benefit statements and pensions dashboards, but please see our response to question 10 for our wider concerns regarding standardisation.

12. *Are there other ways, besides changing the charging structure, that could make a significant difference to member comprehension of charges and encourage improved member engagement?*

We would not draw a direct connection between comprehension of charges with member engagement.

Whilst good value charges are an important factor, the twin drivers of competition and the charge cap have acted to create a market where charges are generally lower than was historically the case, and the number of "high cost" schemes has, in our view, diminished.

Charges are just one feature of a scheme. Engagement would be better driven by focusing on the benefits of pension saving and the impact of contributions on good outcomes, rather than a narrow focus on charges.

13. *What other risks exist for members who may choose to make decisions on which occupational pension scheme they should save into, based purely on the level of the charges they may pay?*

Once they have joined an employer, members do not choose which occupational pension scheme they save into. The employer selects the scheme.

14. *Will this proposal to move to a single charging structure change the way employers select the pension scheme they use for automatic enrolment and would an employer continue to pay their 3% minimum contribution if the employee decides to move their pension savings to a different provider?*

Under a single charging structure, providers would need to adjust their charging rates to align with the new structure. As charges are one of the factors that employers consider (typically) when selecting their workplace scheme, then it is possible that some employers would choose a different provider then they would have done under a different charging structure.

As noted in question 13, the employer selects the scheme, and it is not generally possible for a member to elect to move to another workplace scheme (they could opt of the employer scheme and use a personal pension scheme, but in the vast majority of cases they would lose the employer contribution).

If the current framework for workplace schemes was changed such that an employee could choose from a range of different schemes, the consequences and costs of this would require much broader consideration. We would be happy to comment on such a structure separately if that would be helpful.

15. *Do employers who are choosing a pension scheme routinely negotiate the level of their own charges with the provider, and if so what impact may this have on the employee's contributions?*

This is common for medium to large employers, especially if the selection process is run as a market tender exercise. In some cases the negotiation will be undertaken by the employer's advisers and take place at the same time as a wider review of DC scheme design. We have also observed cases where it has been several years since charges were last reviewed.

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