Consultation Questions: Consultation on Value for Money: A framework on metrics, standards and disclosures

Name of respondent/s / organisation (please provide):

Lane Clark and Peacock LLP

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We are pleased to respond to this important consultation and are content to be quoted in the government's response.

Pension Scheme type(s) (please cross all those that apply)	
Master Trust (500 or more employers approx.)	
Master Trust (fewer than 500 employers)	
Single-employer trust-based defined contribution (DC) workplace pension scheme	
Contract-based DC workplace pension scheme (500 or more employers approx.)	
Contract-based DC workplace pension scheme (fewer than 500 employers)	
Contract-based DC non workplace pensions	

Defined benefit pension scheme	
Hybrid pension scheme	
Your role (please cross all those that apply)	
DC pension scheme trustee or manager	
Member of Independent Governance Committee (IGC) or Governance Advisory Arrangement (GAA)	
Administrator	
Investment consultant	X
Financial advisor	
Employer	
Employee benefit consultant	X
Consumer organisation	
Law firm	
Pension saver	
Other (please state)	

Responses to consultation questions are optional. We ask that you provide your reasoning for your answers to the consultation questions that you respond to.

Please indicate, next to any responses given, if you are ***not*** *content for DWP to publish relevant sections of your responses in the future. Without a specific request for anonymity, we reserve the right to publish your response in full.*

Chapter 3: Scope, criteria, and outcomes

Question 1: Do you agree with the proposed phased approach?

Given the overwhelming majority of DC savers are in a default strategy we agree it is sensible to start with default arrangements.

However, we believe that decumulation and non-workplace pensions (ie consolidators) should also be covered in phase 1. For example, it would be unfortunate for years of good VFM governance to be undone by a saver's decision to transfer out, before or at retirement from a low-cost default arrangement to an expensive and poor value retirement product and we feel that this area of the market currently has much less scrutiny applied to it.

In many instances, market competition has already driven down costs in the accumulation phase but that has not yet happened to the same degree to decumulation products, many of which are retail products.

We are pleased that you state it is not proportionate to apply the framework to defaults with very small numbers of savers or low assets, including arrangements that become defaults "unintentionally". However, we note that the problem of these "unintended defaults" is an issue that goes beyond the VFM framework and is one that we (with the PLSA) have been speaking directly with DWP recently about. There are a range of scenarios which result in "unintended defaults", largely due to uncertainties over the legislative definition of an "arrangement". This scenario has occurred, as the consultation references, not just following property fund suspensions, but also following other transfers without consent, e.g. when trustees wish to change investment manager, the investment manager increases ESG focus, or when members are moved between schemes (ie when consolidation occurs). As a result, there are numerous "unintended defaults" which still will fall within scope of the VFM framework.

We also agree that in phase 1 the VFM framework will be targeted at the decision makers. Experience has clearly shown that, for example, the DC Chair's Statement is not read by the overwhelming majority of scheme members – just other pension professionals. We expect a similar situation to occur with VFM reports.

Although you haven't directly asked for views about your criterion and outcome, we would like to make some general observations (which you will be aware we have made in previous discussions with you):

- "Cheap does not mean good". This is particularly relevant when considering illiquid investments for DC schemes, which as you know has been a regulatory focus in recent years and which we strongly support.
- The "race to the bottom" on charges needs to stop. Market competition means that many providers now offer terms materially below the charge cap but when choosing a provider, many employers will still focus on charges as their primary consideration.

Chapter 4: Investment performance

Question 2: Do you agree with our focus on and approach to developing backward-looking investment performance metrics?

The proposal to report returns for 1, 3, 5, 10 and 15 year returns for members aged 25, 45, 55 and one day before SPA means 20 return figures need to be produced. This would likely be burdensome for most schemes and may not be possible in many cases, since the default strategy may have changed many times over the longer-term periods and returns for previously used funds may not be available. In some cases, sourcing the returns may mean needing to request figures from one or more legacy provider or fund managers, and providers/ managers may not be responsive to requests from ex-clients.

As pension investments are long term in nature, we suggest the removal of the 1-year return figures so as not to encourage short-term thinking across the industry, we are also aware that some providers cannot calculate 1 day to SPA returns and suggest this is simplified to SPA or a clearer time point, for example it might be easier for schemes to report to their NRA.

There is also questionable value in looking back at returns on strategies that are very different to what members are currently invested in. The purpose of a VFM review is to assess whether members are getting good value today, and so considering returns of old investment approaches is not particularly relevant. If a strategy had not changed for the periods under assessment, then it is relevant and worthwhile to consider those returns and compare them to alternatives as a way to evaluate how good they have been for members and determine whether any changes are needed, but considering returns of old investment approaches is not relevant. That said, to take the returns of the current strategy and back-test it to show what members would have received had it been in place has the drawback of being subject to “gaming” as providers could adjust the strategy to what has done well in the past, even if this is not what they would consider optimal for future returns.

We agree with your comment that all returns data should be reported to the same end date. However, we note that this will require fund managers producing data at that date and making it available to trustees in a timely manner. Our past experience shows that getting data at a specific point is not as straightforward as it should be so it would be prudent to place a duty on fund managers to provide such data as is requested by trustees in the required timeframes. In particular, schemes can have different valuation points, for example, midday or end of day which can have an impact on comparability.

It should also be noted that performance will only be accurate and comparable across strategy types if the calculations take into account glidepath phasing or de-risking.

We strongly support not having employer-level disclosures in multi-employer schemes, due to the huge volume of data and commercial agreements which would prevent this. As such, disclosing through employer AUM cohorts is one potential compromise, and we would prefer to see prescribed bands than calculations of those bands.

Although you have not asked about It, we also want to address your initial proposal in paragraph 58 that employer subsidies should be discarded when considering VFM as **this is our most significant concern**. We do understand that for professional advisers looking at underlying investment costs that this provides clarity on what is being paid overall as the two cost models are different. However, we strongly urge you to reconsider this for any disclosures made to members – as these performance figures are not what they receive. Typically, these costs relate to administration, and we strongly believe that employers who pay administration costs for their members should have these costs reducing the apparent VFM in their scheme. We are also very concerned that if this subsidy were to be removed from published comparisons that it may lead to members making poor decisions to opt-out of a scheme for which they pay no fees at all. We also believe that if employers get no “credit” from their employees then scheme sponsors may stop providing the subsidies, again leading to worse outcomes for their employees.

Question 3: Do you agree with our proposals to use Maximum Drawdown and/or ASD as risk-based metrics for each reporting period and age cohort?

The proposal to report maximum drawdown and ASD over the same periods and ages of members as returns would mean 60 figures need to be calculated. Aside from the points previously mentioned about the ability to obtain the return figures, there is questionable value in reporting these risk figures over very short-term periods or indeed very long-term periods. We are also concerned that the volume of figures here will mean this is unclear and not be useable.

Members don't receive risk, they receive return, and for members far from retirement these figures are less relevant since any downturn is expected to revert before it will make a difference to their outcomes. However, drawdowns and ASD are relevant for members close to retirement, as a market crash at that point may mean permanent impairment to their outcomes. Therefore, we suggest these risk metrics are only reported for members at age 55 and SPA, and they are reported over 3 and 5 year periods only.

The metric is also questionable as presenting a misleading picture, since sharp drawdowns tend to be followed by a recovery (eg pandemic driven drawdown around March 2020 and quick recovery).

In terms of assessing risk along with return, a more straightforward approach would be to look at a "return divided by risk" ratio for various ages and time periods. We suggest risk here is ASD and hence this could be reported, but to not report maximum drawdown.

It should be noted that risk analysis will only be accurate and comparable across strategy types if the calculations take into account glidepath phasing or de-risking.

As an aside, we note that "Drawdown" has a very different meaning in pensions and this could lead to unfortunate confusion in some circumstances. Therefore, clear distinction should be made as to which definition is being referred to.

Question 4: Do you agree with our proposals on "chain-linking" data on past historic performance where changes have been made to the portfolio composition or strategy of the default arrangement?

No since as previously mentioned, what members had as a strategy before is not relevant to VFM today, what matters is where they are invested now and is that VFM. If what they are invested in today has not materially changed over the long term, then reporting long term returns makes sense, to help evaluate whether the current strategy is good VFM or whether changes should be considered. But if the strategy has materially changed then we suggest not going back and looking at these legacy strategies, particularly if this means contacting fund managers that have been terminated.

We also point out that the complexity and volume of work needed to achieve this is likely to rise steeply over time since it is now normal for default arrangements to be changed relatively frequently for example post freedom and choice almost all DC defaults changed dramatically to move away from targeting annuity purchase and since then we've seen evolution in integration of ESG and now illiquid assets.

Question 5: Do you agree with proposals for the additional disclosure of returns net of investment charges only?

We do not agree that this disclosure is necessary. The schemes will have already have a requirement to publish their returns, so we suggest you request them to disclose their costs associated with the funds, rather than restating their performance figures.

We would note again that some own trust schemes pay for these costs for their members to enhance the value they receive so this would need to be clear in order that employers are not penalised for offering better value to their members.

Question 6: Do you agree with requiring disclosure of asset allocation under the eight existing categories for all in-scope default arrangements?

As you mention, disclosure of these eight asset classes is now a requirement of the Chair's Statement. Requiring schemes to disclose the same information as part of its VFM return would therefore cause duplication we therefore suggest that the emphasis is placed on one document – either do this in the VFM framework or the Chairs statement, not both. And, if it is required, our preference would be for it to be in the VFM framework, with the complete abolition of the Chair's statement.

Question 7: Do you think we should require a forward-looking performance and risk metric, and if so, which model would you propose and why?

Yes, we believe a forward-looking analysis should be included since the expected outcomes for members is key. However, care needs to be taken to ensure the figures produced are consistent which requires return assumptions and the basis for the models to be set centrally. We support a deterministic approach since stochastic modelling can become complex and difficult to compare, however, note that this offers a more basic forward-looking measure.

Similar to our earlier point, over time providers may "game" the system by increasing their allocations to riskier assets, and hence, increasing outcomes. Therefore, a return and risk metric is important to consider across the different ages within the strategy to allow fair comparisons.

However, we do not believe the Risk at Retirement is an appropriate risk measure on its own as it is unlikely in our view that members will actually delay their retirement age in practice. As such, the focus is not appropriate compared to the other measures.

It should be noted that these risk metrics will only be appropriate if they take into account glidepath phasing and de-risking.

Chapter 5: Costs and charges

Question 8: Are there any barriers to separating out charges in order to disclose the amount paid for services?

We agree with the principle because this will make the comparison between bundled and unbundled services more transparent and fairer. However, some providers have told us that either they cannot disaggregate the costs as the different business areas cross subsidise or others have said they cannot disclose the investment only costs as they have confidential commercial contracts with the underlying investment managers. We would also note for unbundled schemes employers may pay per transaction not on an AUM basis.

However, as we noted in our answer to Q.2, when it comes to disclosure to members, we are not in favour of excluding employer subsidies.

Question 9: Do you have any suggestions for converting combination charges into an annual percentage? How would you address charging structures for legacy schemes?

There are many different charging structures for legacy schemes. Any attempts to convert these to a single annual percentage are likely to be either overly complex or not accurate. We leave it to legacy providers to provide their suggestions as to how to deal with this.

Question 10: Do you agree with our proposal to provide greater transparency where charging levels vary by employer? Do you agree that this is best achieved by breaking down into cohorts of employers or would it be sufficient to simply state the range of charges?

We agree that greater transparency should be provided. We think that doing so by breaking charges down by cohorts of employers will lead to greater transparency then just stating a range of charges.

However, this is likely to create a substantial data processing task for master trusts with thousands of participating employers, but we feel this suggestion is much easier than individual level disclosure.

Chapter 6: Quality of services

Question 11: Are these the right metrics to include as options for assessing effective communications? Are there any other communication metrics that are readily quantifiable and comparable that would capture service to vulnerable or different kinds of savers?

Measuring quality of service on a consistent basis is necessary but very challenging. We agree with the concept of creating a metric that all providers are able to capture. However, we do not believe the proposed options are the right ones since we believe that the percentage of members who take the actions you suggest will be so low as to be not statistically material to measure and compare against. We would also be concerned that for example a scheme with a very high number of members updating their retirement choice or age could actually signify a poorly run scheme as the majority of members are selecting something other then the default suggesting it may not have been designed with the membership in mind. Taken to an extreme, for example, in order to achieve a good score on the “updating retirement age” metric, schemes might set their default retirement age to be very low or very high, driving their members to make a change which “improves” this metric for the scheme.

We do agree that NPS scores are effective here, as long as the question(s) that make up the NPS are consistent, and therefore we suggest that using a standard member satisfaction survey across the industry should be considered.

Alternative measurements for assessing the quality of member communication might be:

- Percentage of members who first log in then use the scheme website or app;
- Percentage of member queries that are dealt with by the first administrator who deals with it, without needing it to be referred elsewhere; or
- the number and type of complaints received.

Question 12: Are these the right metrics to include as options for assessing the effectiveness of administration and/or are there any other areas of administration that are readily quantifiable and comparable?

As you point out, these metrics have been in place for several years now and so are broadly understood. However, there can still be differences in interpretation which may need to be clarified if they are to be used for industry-wide comparison. For example, when assessing member-initiated transactions, how should the timescale for measuring this be determined, eg "end-to-end", "stop the clock" or only when the scheme has received <u>all</u> information it needs to process the transaction?

We would, however, add a note of caution about using SLAs to compare schemes: different schemes may have different agreed turnaround times in their SLAs so direct comparisons using SLAs could be misleading.

Some of our suggestions above for measuring member communication also overlap with measuring administration.

Chapter 7: Disclosure templates and publication timings

Question 13: Do you agree with a decentralised or a centralised approach for the publication of the framework data? Do you have any other suggestions for the publication of the framework data?

A centralised approach is sensible given most professionals will want to see the information held in one place.

Under the centralised approach, we are unclear whether you intend that schemes will be identifiable in the public domain from the publication of this framework data. We suggest that consideration is given to publishing the centralised data anonymously. This will avoid schemes being concerned about "naming and shaming" and thus reduce the incentive to "game" the system. But since schemes would still be evaluated against comparator schemes there will still be meaningful assessment. (In suggesting this, we note in paragraph 158 that you say something similar happens for contract-based schemes.)

Another advantage of a centralised approach as you set out in paragraph 135 is that it would reduce the concern about whether a document is compliant or not. This concern has led to an enormous amount of extra work for schemes when drafting Chair's Statements and we strongly do not want the same situation to arise for the VFM framework.

Question 14: Do you agree with the proposed deadlines for both the publication of the framework data and VFM assessment reports?

We are opposed to your proposal to publish net returns data as at 30 June. We understand the need for data to be comparable so if you are going to require publication at one specific date then we think this should either be calendar year or any date between 30 March – 6 April which will coincide with many scheme year ends for which data will be being collected for anyway. (To clarify our second suggestion, we mean that legislation will permit schemes to choose any date between 30 March – 6 April to encompass a variety of scheme year ends within that period.)

We also question whether VFM assessments are needed annually. As we have indicated throughout our response, the additional work to comply with the proposed framework is substantial. Pensions are meant to be a long-term product and we suggest that measuring VFM every three years would be sufficient, noting that other parts of pensions legislation envisage a review every three years, for example for the Statement of Investment Principles.

Chapter 8: Assessing Value for Money

Question 15: Do you think we should require comparisons against regulator-defined benchmarks or comparisons against other schemes and industry benchmarks?

There are advantages and disadvantages to both.

However, on balance we favour comparison against three other schemes of the assessors choosing. The industry has become familiar with this concept since its introduction for the enhanced VFM assessments for sub-£100m schemes. It has not always been easy to find suitable comparators for small schemes – particularly when it comes to finding comparators willing to receive a transfer from the small scheme – but we think this problem will be much less for schemes of a bigger size which are more attractive propositions for commercial providers to take on.

Question 16: Do you agree with the step-by-step process we have outlined, including the additional consideration?

As mentioned in question 5, we do not see the need to disclose investment charges net of investment costs. We believe this adds more complexity and will not necessarily be easy to obtain. We suggest that after step one, you consider step two as a disclosure of costs which can then be compared. You may want to consider focusing on a bundled cost disclosure initially, since we understand it can be difficult for providers to separate out the costs in a consistent and clear way.

The other steps seem reasonable, but we would expect snagging issues to come to light as the process begins.

Question 17: Do you agree with a 'three categories' / RAG rating approach for the result of the VFM assessment?

Whilst the RAG rating approach is well understood, we do have slight reservations that in this context just having three categories may not allow enough room for nuance and differentiation between schemes at different stages of their VFM journey. Possibly a "five-star" system would be a different approach which is also well understood.

We think that each component of the VFM assessment should be given its own rating (RAG or otherwise), and then an overall rating applied to the whole scheme – and this overall rating may be a simple binary rating of either "Yes, the scheme offers VFM to members" or "No, the scheme currently does not offer VFM to members".

We do agree that a "green" rating does not mean that there is no further room for improvement.

Question 18: How should we take into account the specific challenges of contract-based schemes while ensuring equivalent outcomes for pension savers?

We agree with your suggestion that the FCA should make new rules requiring contract-based providers to take the necessary actions in the best interests of savers not benefitting from good VFM.

Question 19: Do you agree with our proposals on next steps to take following VFM assessment results, including on communications?

We agree that it is reasonable that action should be required if a scheme shows consistent poor VFM over a number of years. However, a single year's poor VFM assessment should not be the sole trigger for excessively alarming communications to members that may lead to poor short-term decisions on their part. For example, in some scenarios, a scheme that only reports mediocre or poor VFM but has employer contributions is still likely to be better – at least in the short term - than a scheme with good VFM but to which the employer will not contribute to. The point being that members should not be unduly alarmed and transfer to such schemes as a "knee-jerk" reaction.

Our response to question 14 highlighted that we believe VFM assessments shouldn't be carried out annually, but rather, for example, every 3 years. This would remove the issue of triggering the communication of poor VFM over a single year.

We also note that in paragraph 149 you raise the possibility of TPR enforcing wind-up and consolidation where a scheme is consistently not providing VFM to its members. We have underlined "consistently" since we believe that this is critical to permitting TPR to exercise any such powers and this should be defined to mean for a specified number of years. We feel that any such proposed powers should have a full and detailed consultation before being permitted.

Chapter 9: The VFM framework and Chair’s Statement

Question 20: If the Chair’s Statement was split into two separate documents, what information do you think would be beneficial in a member-facing document?

Unfortunately, the level of comprehension about pensions of most members is extremely low. As an example, the DWP’s member engagement research published on 30 January 2023 addressed this in its findings. Therefore, a member-facing document needs to be exceptionally clear and focused on both the actions we want members to take and understand at their point in their savings journey and readability.

We believe that the current details about processing core financial transactions, investment returns and pot projections are, unfortunately, over the heads of many pension savers and we would question if they need to know these points. We believe there are other more important points like understanding they are in a DC not a DB scheme and if the contribution levels they currently are paying are adequate.

We are not convinced that there should even be a member-facing document but if there is then we believe that all a member-saving document needs to say is whether or not the scheme is providing good VFM for members - taking account of any employer subsidies - and, if it is not, what action the trustees are taking to improve it.

We think that a member-facing document should be no longer than one side of A4 paper (or digital equivalent) and be included alongside member benefit statements.

Question 21: Is there any duplication between the VFM framework proposals and current Chair's Statement disclosure requirements?

Holistically, the VFM framework proposals and Chair's Statement requirements feel like they cover a lot of similar ground, although there is not necessarily a direct correlation in some of the detail. For example, both require information about investment returns, costs and charges and the Statement also has a Value for *Members* section.

Some differences are that the Chair's Statement has a section on Trustee Knowledge and Understanding (TKU) and also covers self-select funds which the VFM framework won't, at least initially, according to your proposals. Additionally, the Chair's Statement has to include the SIP for the default arrangement, illustrations of the effect of charges and costs and, for master trusts, information about non-affiliated trustees and gathering member views.

However, we believe the disclosure of information could be managed if the Chair's Statement is removed. For example, TKU reporting could be covered in TPR's scheme return, schemes already have to publish their SIPs online, and a requirement to link to that could be added to the VFM framework. The additional master trust information could be added to TPR's supervisory return, and we do not think that the illustration of charges and costs is particularly useful for members anyway and would not be missed if this requirement were removed.

We strongly believe that introducing the VFM framework without reducing the burden of the Chair's Statement will be more than many schemes can cope with. If the VFM framework is introduced, then **we believe that the Chair's Statement should be scrapped in its entirety**.

Chapter 10: FCA specific issues

Question 22: Should individual SIPP arrangements be excluded from the requirement on providers to establish an IGC/GAA and to publicly disclose costs and charges and, if so, under what circumstances?

We recognise and agree with your concerns that in some circumstances SIPPs would benefit from being within the VFM framework – even engaged individuals who choose their own SIPP and investments would benefit from improved VFM disclosure.

And we think in principle that there should be a level playing field for all DC pensions, including decumulation so we suggest investment pathways are looked at as part of the VFM consultation.

However, taking into consideration that the number of savers in SIPPs is relatively small compared to standard pension schemes, we believe that this should not be an immediate priority for the VFM framework and that including SIPPS could be deferred until the framework has been bedded in for mainstream pension schemes.

Question 23: Do you think there would be merit in a proposal to mandate the inclusion of a pension saver-focused summary alongside the IGC Chair's Report?

Again, we do not believe these reports are key important communications for members.

Question 24: Do you think the provider or the IGC should be responsible under FCA rules for the publication of framework data?

As you note, often the IGC relies on the provider to collate data so we think the provider should be responsible for publishing the framework data. Further, the provider should have a duty to report to the IGC when it has done so and the IGC should have a whistleblowing duty if the provider does not do this.

Chapter 11: Impacts

Question 25: Which of the metrics do you not currently produce? (This could be for either internal reports or published data). Do you envisage any problems in producing these metrics?

We represent a wide range of client schemes. Whilst we support our clients to comply with legislative disclosure requirements (and believe that they do their best to do so), they have different approaches to additional internal analysis or published data and therefore this varies significantly. However, we are employed to calculate a significant number of these figures as they are not readily available. We therefore suggest, so not to create a consultant industry here, that these figures should be disclosed on new factsheet by providers.

Question 26: Do you agree with our assumptions regarding who will be affected by the framework?

Yes, and we make the following additional comments:

- Members will also be affected because of additional disclosure from schemes, and, of course, because the intention of this VFM framework is to improve member outcomes.
- Master trusts with thousands of participating employers will almost certainly incur higher additional costs than single-employer trusts and ultimately, as many of these are commercial entities, these costs will be passed to the end member in the bundled fee.
- We agree that asset managers may also be affected – as we noted above, in the past there have been difficulties in getting the required data from managers on behalf of trustees (eg transaction costs).

Question 27: Are you able to quantify these costs at this stage? Are there additional cost components we have not considered? Do you expect these costs to be significantly different for commercial providers and multi-employer schemes?

See our response to question 26.

Question 28: Overall, do you think the benefits of the framework outweigh the costs? Are you able to quantify any of the potential benefits?

We fully support the principle of improving VFM for savers. However, we do strongly believe that this opportunity to do so must be carefully considered to achieve this aim, rather than just adding further compliance burden onto schemes.

We therefore suggest that decisions about the VFM framework are taken at the same time as those about the future of the Chair's Statement and duplication is removed. But, in fact, our preferred way forward is that this new VFM template is seen as the overall document and all required information is disclosed here. This removes the need for the Chair's Statement.

We see this framework developing over time and there may be other areas that would define value but are not explicitly included at the moment, such as ESG. Whilst schemes are required to provide ESG credentials elsewhere, it would be worth considering capturing this in future, to view it from a member's perspective.

Question 29: Are there additional benefits we have not identified?

N/A

Question 30: Do you have any comments on the potential positive and negative impacts of these proposals on any protected groups, and how any negative effects could be mitigated?

N/A