Public Bill Committee on the Pension Schemes Bill – Aviva written evidence

Overview

Aviva provides pensions, life insurance, general insurance, health insurance and asset management to 18 million customers. We are the UK's leading insurer, serving one in every four households. We help more than five million people save for their retirement through workplace and private pensions and meet the pension needs of more than 20,000 companies, ranging from large multinationals to small start-ups. We are also one of the leading providers in the Bulk Purchase Annuity (BPA) market having entered the market nearly 20 years ago and have successfully executed over 800 buy-in or buy-out transactions.

We welcome the opportunity to provide written evidence to the Public Bill Committee on the Pension Schemes Bill. We are supportive of the Pension Schemes Bill and the policy agenda it aims to deliver, which will help strengthen pensions investment and help savers manage their pensions more effectively. There are however measures in the Bill we believe need further review which we have set out below.

Defined Contribution (DC) measures

Value for Money Framework (Part 2, Chapter 1)

- We are fully supportive of the Government's aim of driving better value across the workplace DC market through greater scrutiny and competition based on long-term value. It is important that pension schemes deliver good value for members and that we drive greater market consolidation.
- We agree that the market must shift its focus away from cost towards a more wide-ranging assessment of overall value that includes investment performance and customer service. A framework which focuses on this allows for more investment into a wider range of assets which could generate better returns for savers and support the government's objective to boost growth.
- It will be important to ensure the Framework is designed and implemented in a way that doesn't drive certain behaviours, for example, creating a risk averse investment culture which is focused on performance against set benchmarks rather than overall returns.
- There are important learnings here from the Australian Annual Performance Test and regulator-prescribed benchmarks, which have driven investment herding and lack of appetite to invest in certain private market asset classes (e.g. social housing) that don't deliver the right returns against the test.

Consolidation of small dormant pots (Part 2, Chapter 2)

- We are pleased to see a solution for the small pots issue being prioritised through the Pension Schemes Bill. The Government has proposed a multiple default consolidator model – ensuring that savers deferred small pots (under £1,000) are brought together into one pot through a small number of providers becoming 'authorised' consolidators. This is an important step to deliver better outcomes for members.

- One of the reasons the exchange of small pots between scale master trusts did not previously proceed was due to concerns over the extent to which trustees needed to protect the interests of members with small pots from potential detriment (no matter how small).
- Clause 23 (1) (b) states that a small dormant pension pot is "exempt" from consolidation if the trustees or managers determines it is in the "best interests" of the individual that the pot is not transferred. We believe that the "best interests" test is too low a threshold to determine that a transfer should not take place. Trustees may judge that they can't confirm whether the transfer would definitely be in the best interests of the member given how hard it may be to determine this with very small pot sizes. We would suggest this is replaced with a less onerous exemption test that still protects against poor outcomes for the member e.g. where the trustees determine the member is "likely to suffer material financial detriment" if a transfer takes place.
- Clause 23 (3) states that small pot regulations may include further provision about how determinations under 1 (b) are to be made. These regulations will need to be carefully drafted to avoid a requirement for trustee determinations of relative value that risk undermining the policy intent.

Asset Allocation requirements (Part 2, Chapter 3)

- We understand that the Government's policy intention for asset allocation requirements is to ensure that the Mansion House Accord is delivered, with a reserve power to address to any market failure which fundamentally impacts its delivery.
- However as currently drafted in **Section 28C**, the power in the Bill goes far beyond this policy intent and the scope of the Accord, with very limited constraints on how, and under what circumstances, the requirements could be introduced. For example:
  - There are no limits set out in the Bill on the percentage of assets the Secretary of State could prescribe, thereby allowing minimum allocations that are higher than the Accord
  - All assets within the registered scheme are in scope, which is considerably broader than the scope of the Accord
  - The Secretary of State can introduce the requirements to achieve any purpose – not just the purpose served by the Accord.
- Our view is that the power and the circumstances under which it can be used should be narrowed to mirror the Government's stated intention.

Contractual override powers (Part 2, Chapter 4)

- As the UK's largest pension provider, we welcome the consolidation measures set out in the Bill, which will help get more savers into larger schemes that can offer better value and more opportunities for productive investment.
- The contractual override for contract-based arrangements could be a 'game changer' for the efficient management of Group Personal Pensions (GPPs).
- However, the timeline for implementing these measures is critical. We need guidance and an enabling regime as soon as possible that gives contract-based providers the explicit ability to use these powers, and prior to Value for Money Assessments, where

they, and the independent expert, view this to be in the best interests of members. This will more closely align the governance powers of GPP providers with master trust trustees.
- Any delays could impact the pace at which the industry can deliver consolidation and therefore hamper progress against the Mansion House Accord.

Default Pension Benefit Solutions (Part 2, Chapter 5)

- The Bill introduces requirements for both trust and contract-based schemes to provide one or more default pension benefit solutions for those members who choose not to make a decision at retirement. We are supportive of the aims of this measure as we need to ensure savers can effectively manage their pension wealth into and throughout retirement.
- However, any retirement pathway should be tailored to a person's circumstances and retirement needs. Sensible decisions can't be made about someone's retirement without a basic understanding of their wider income/pensions, health issues, and their domestic situation. This information is important for making sure someone is on the right retirement path, including a default solution.
- Engagement is also essential, and we believe Targeted Support (as being consulted on by the FCA) should be feature of any retirement strategy. Where possible, we need to be encouraging people to make active decisions about their retirement that are tailored to their circumstances and needs, with the default there as an important backstop.
- We understand that schemes will be required to make all decisions regarding the ongoing management of the default solution on behalf of members. Whilst we agree with the policy intent that savers should not be expected to make complex decisions to manage the default solution once they are in it, we believe that there should be more consultation on this requirement, given the challenges schemes will face in developing solutions that provide a regular income, do not require pensioner decision making, are attractive to members, and deliver value for money.
- A consultation would also allow the FCA to explore how Targeted Support could work with the default requirements, as well as help to gauge how schemes intend to meet the requirements and potential supply within the market, informing regulations.
- A later implementation date for master trust (currently proposed as 2027) may well be needed to allow providers time to develop and test high quality solutions, improving take up of the default option, and member outcomes.

Communicating with members

- Under **Clause 44** of the Bill, trustees and providers will be required to provide information on the default alongside a description of the kind of person for whom it is appropriate. While the trustees will choose the most appropriate option for a member (based on the information they have about them) the member will not be told why the trustees have chosen this option for them and they will need to recognise the similarities between their circumstances and the proposed default.
- **Clause 44 (3)** provides that regulations may make provision about how a member's default pension benefit solution is to be presented. If trustees were allowed to personalise the communications and make it more explicit for the member that they

believe a specific default is appropriate for them, we believe we will see more people take up the offer of the default, and importantly, the member will have a clearer understanding of why the trustees have decided the default option is right for them.

- However, this type of communication (i.e. designed to promote engagement, rather than passive information) is likely to be classed as marketing and therefore prohibited under the Privacy Electronic Communications Regulations (PECR) unless the members has provided marketing permissions (which very few do due to the nature of the auto-enrolment process). We think an amendment to the PECR soft opt-in exemption should be considered for inclusion in the Bill to address the barriers to communicating with auto enrolled pension customers and help them make informed decisions about their savings and retirement. We are strongly supportive of the ABI's proposed amendments to PECR in this regard.

<u>Defined Benefit (DB) measures</u>

Surplus extraction (Part 1, Chapter 2)

- The Bill includes measures to allow trustees of DB pension schemes to 'safely' release some of the schemes' surplus, if their current scheme rules do not enable this. The priority for schemes should be to ensure members' benefits are secure before the use of DB pension surpluses could be considered, and it is positive that trustees will retain the position as key decision-makers regarding surplus extraction, given their fiduciary duty to scheme members.
- The threshold for surplus-sharing will need careful consideration, as the current proposal to lower the threshold from buyout level to full funding on a low dependency basis could risk weakening protections for members. We would welcome a consultation on this as the secondary legislation is developed.

Superfunds (Part 3)

- The Bill introduces a permanent legislative regime for superfunds to provide an alternative solution for employers of schemes with lower funding levels, for whom buyout is inaccessible.
- We believe the prudential regime for insurers ensures that they are best placed to consolidate DB pension risk, particularly given their proven track record, robust regulatory oversight, and deep operational expertise. Taking on DB risk demands stringent standards around governance, capital adequacy, regulation, investment strategy, and operational capability – all areas where insurers are well equipped to deliver. The new legislative framework for Superfunds should therefore apply the same level of rigour, ensuring that the protection of scheme members remains the central priority.
- It is essential that the new framework is implemented effectively, with a clear requirement that any scheme capable of securing members' benefits through a buy-out does so via the insurance route. This offers the most secure and member-focused outcome and is the best way to avoid risk of regulatory arbitrage. We therefore strongly support the inclusion of the "Gateway test" in the Bill, requiring schemes to assess their

ability to afford a buy-out before considering transfer to a Superfund. It is essential the Gateway test is robust and cannot be “gamed” which would risk undermining the policy intent and members’ benefits. We are supportive of the ABI’s proposal to include a “foreseeable” future test regarding a schemes’ ability to afford a buy-out.

- As currently drafted, the Bill doesn’t include any reference to the “capital adequacy threshold” a superfund will need to meet to take on a schemes’ liabilities. The Secretary of State will have the power to make provisions about how to determine any financial thresholds have been met, with very limited constraints on that decision. We would propose some tighter constraints are put on the Secretary of State’s power, for example, requiring the decision to be made following consultation and on the basis of actuarial advice, given how fundamental it will be to the effectiveness of the regime and in protecting members’ benefits.