

Barnett Waddingham response to the Pension Schemes Bill Call for Evidence

Introduction

Barnett Waddingham (BW) is a leading UK professional services consultancy with expertise across risk, pensions, investment and insurance.

Offering a full range of services to trustees, pension schemes and sponsors, BW provides tailored, pragmatic and proactive advice and support in all aspects of actuarial consulting, funding and investment strategy, pension scheme management, administration and endgame journey planning. BW builds strong, trusted relationships with a wide range of clients, across the public and private sectors – including 22% of FTSE 100 and 15% of FTSE 350 companies.

With a team of more than 1,750 people across 10 offices, BW works to deliver exceptional service through a commitment to trust, integrity, and quality.

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Below are our thoughts and recommendations regarding three of the five policies relating to the defined contribution schemes. We have not commented on the other two policies as we are broadly in agreement with them, although we do have some concern that setting a minimum size for multi-employer DC default pension funds could reduce competition and stifle innovation.

1. Policy: Consolidate individuals' small DC pension pots through multiple default consolidators.

- 1.1. We agree that multiple small pension pots are not conducive to achieving good member outcomes.
- 1.2. It may be that in time pensions dashboards and wider industry consolidation measures (e.g. dashboards, mega funds, value for money) naturally drive consolidation but given that those with small pots are least likely to engage with their savings it feels this initiative can expedite matters if implemented successfully.
- 1.3. **Authorisation of consolidator schemes/and market competition** – this assumes schemes will want to be consolidator schemes and apply. One of the big challenges here is making these small pots profitable and interaction with the megafunds initiative. The two could support each other, but only if the providers who are likely to achieve scale wish to participate. These small pots could be unattractive for some providers and some providers may be concerned that net outflows will hit their attempts to achieve scale. Consideration may need to be given to compulsion (to create a consolidator market) or relaxation of scale for would-be consolidators (depending on response from providers).

- 1.4. Consideration also needs to be given to the number of consolidators that will be authorised. Too many and the commerciality of being a consolidator might be impacted; too few and we may lose innovation and competition.
- 1.5. **Legacy pension arrangements** – it makes sense for this legislation to start with auto-enrolment as a) this is what created the small pot challenge and b) these schemes are generally free of characteristics that would cause problems with a transfer (guarantees, protections, exit charges). However older schemes will be some of the worst offenders for poor value – it's vital these get picked up through other paths (Value for Money etc).
- 1.6. **Investments** – any automatic transfer carries investment risk, particularly for those closer to retirement/in de-risking mechanisms. Whilst this should not be a barrier to consolidation (and authorised consolidators should, by definition have suitable investment defaults and retirement pathways), communication to members should clearly set out relevant considerations.
- 1.7. **Value** – consolidators should be subject to competitive charges, and the size of these pots does minimise the impact of charges in absolute terms, but it is possible that members have access to a particularly advantageous arrangement. Noting members can opt out and that Value For Money and consolidation will help here it is still important that members understand not just the current charges of their scheme but how it rates on a VFM basis. We note schemes can override the mechanism where "the trustees or managers of the scheme that holds it determine that it is in the best interests of the individual for whom the pot is held that it should not be transferred in accordance with small pots regulations" but this should not become onerous for Trustees to check.
- 1.8. **Engagement** – as is noted this exercise could be used to increase pensions engagement which can only be a positive. Communications should be clear (and unbiased) whilst also being concise. Whilst certain things should be covered members should not be scared off by risk warnings. It is after all likely to be in member interests to consolidate.
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2. Policy: Allow contract-based pension providers to override a member's contract to change a member's contract or transfer them to a new arrangement. This would include measures to protect savers.

- 2.1. We are supportive of the principle of contractual override and its aim of facilitating consolidation and addressing the issue of high charges and/or underperforming pension pots. However, there is clearly a risk that savers transferred under a contractual override could end up in a new arrangement that is worse than their previous one, impacting their retirement income.
- 2.2. It is therefore essential that the planned safeguards, including a "best interests test" are robust and truly effective in protecting members' interests.
- 2.3. Independent expert - the bill states that a provider will only be able to use the override if it concludes, with confirmation from an independent expert, that the change is likely to lead to better outcomes for affected members and no worse outcomes for others.

- 2.4. Our concern with this section of the bill is the definition of the term independent expert. The bill states that the person appointed must a) be independent of the provider, and b) have such expertise as is specified in general rules made by the FCA.
- 2.5. The FCA Handbook PERG 10 already deals with persons involved in the establishment or running of a pension scheme or in providing services to such persons, and this should be extended to build in specific guidance on contractual overrides and bulk transfers.
- 2.6. To support this, we feel that the definition of independent expert should be more prescriptive, and that person should be authorised and regulated by the FCA.
- 2.7. Certification - the bill states that the independent expert must issue a certificate to the provider to confirm that the proposed unilateral change can proceed. To ensure cross-industry consistency we recommend that a pro forma of this certificate is drafted and approved.
- 2.8. Unilateral changes – we believe there should be greater emphasis placed on the other provisions laid out in the bill regarding unilateral changes. Much of the discussion has centred around transfers, whereas the bill also includes provisions to allow pension providers to make changes to schemes without members' consent. These changes could include updating pension terms, reducing fees or switching investments and we believe these changes should be considered as part of the certification process.
- 2.9. Costs - we do not believe that the cost of a unilateral change (transfer or otherwise) should be explicitly borne by the saver, considering that in many cases, low individual fund values may be involved in the move.
- 2.10. We would expect the costs involved to include:
- pre-funding for investment transitions to ensure minimal out of market risk exposure
 - transaction costs for the change of investments
 - advisory costs for the involved providers to confirm the "best interest" nature of the transfer
- 2.11. The providers involved in the transfer should agree how the costs will be met and this should form part of the certification process.
- 2.12. Protection – It needs to be recognised that those advising on transfers or changes to contractual terms could face retrospective risk that the 'old' solution performs better than the new one. The advice or sign off by independent experts should only be judged based the information that is known or could reasonably be known at the time of the transfer and not on any future performance, which would clearly be unknown. This point should be made clear in the legislation.

3. Policy: Place a duty on DC scheme trustees to offer default retirement products to members known as guided retirement.

- 3.1. We support the intention to make it easier for members to access retirement products that are deemed suitable for them, without having to take financial advice, which they may not be able to afford.
- 3.2. However, we are concerned about the additional duty this places on trustees and the liability that comes with that duty. We believe the bill should provide protection for trustees in this regard.

- 3.3. Trustees will need to determine a number of factors such as the rate of drawdown, the default investment strategy for the remaining capital, the extent of tax-free cash a member might take and, the age at which a later life annuity might commence, and whether such annuity should include additional features like dependants' benefits and index linking.
- 3.4. A significant concern is the fact that trustees will be creating solutions for cohorts of members but could be doing so without knowledge of members' other pension arrangements.
- 3.5. The bill should state clearly what actions trustees are expected to take regarding the gathering of additional financial information and how this information should be stored and accessed.
- 3.6. It's also worth noting that whilst large parts of the bill are focused on scale within the accumulation phase we don't see how this translates into the decumulation phase. More clarity on this point would be welcomed.

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