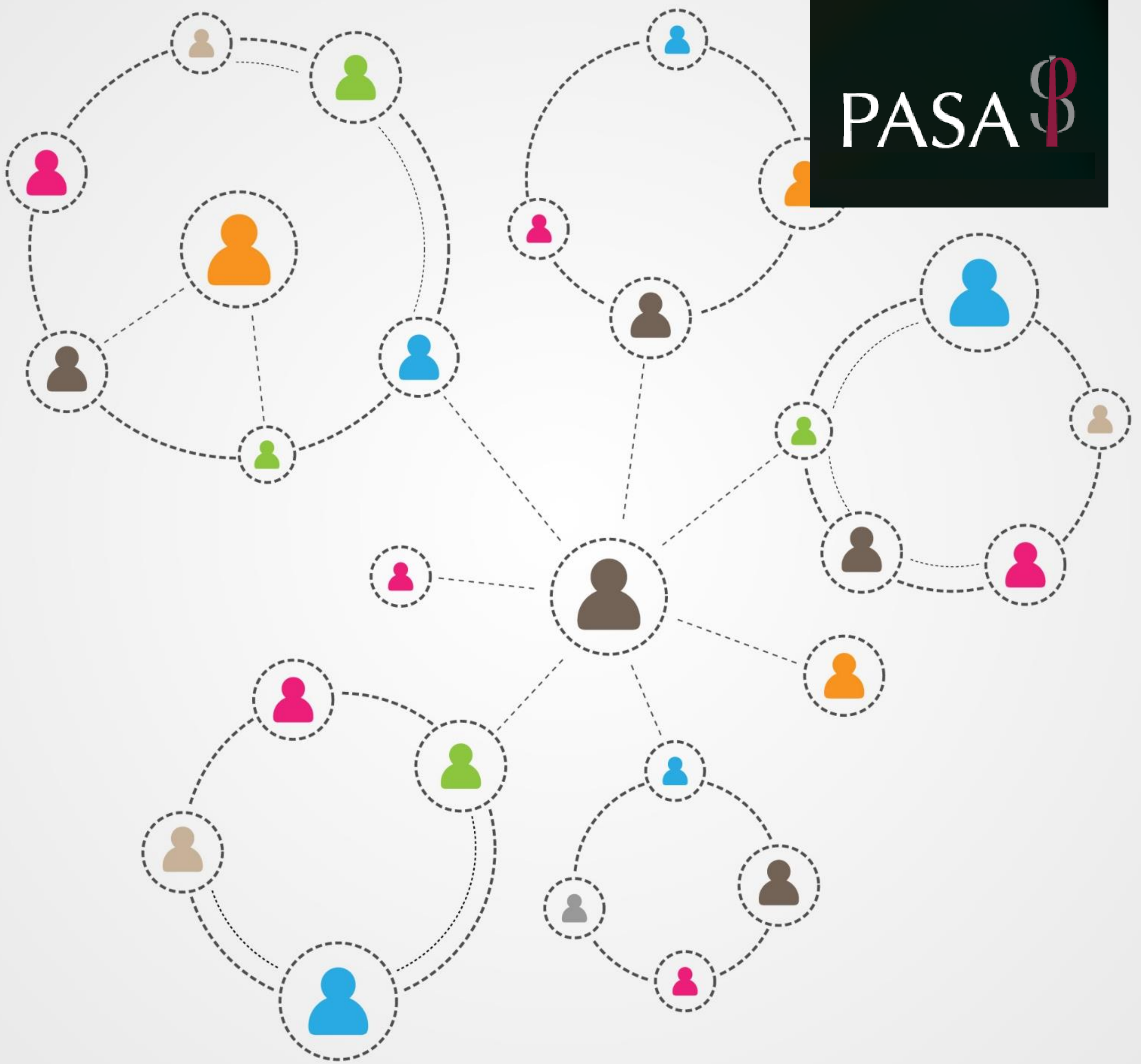

PASA DC Governance Working Group Consultation response

Helping Savers understand their pension choices at Retirement

September 2023

Helping savers understand their pension choices at Retirement

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About PASA

The Pensions Administration Standards Association (PASA) was created to provide an independent infrastructure to set, develop, guide and assess administration standards.

PASA acts as a focal point and engages with industry and Government to create protocols for understanding good administration - but also appreciates there's no one size fits all. PASA develops evidential Accreditation practices allowing benchmarking across and between the industry regardless of how the administration is being delivered.

As well as raising the profile of pension administration generally, PASA focuses on three core activities:

1. **Defining good standards of pensions administration relevant to all providers, whether in-house, third party or insurers**
2. **Publishing Guidance to support those standards**
3. **Being an independent Accreditation body, assessing the achievement of good standards by schemes**

There's no organisation providing such services across schemes, yet there's a demand for evidence of service quality from scheme trustees, sponsors, administrators, insurers, savers and regulators.

1 Summary

Through a competitive and well regulated market, innovation has led to great improvements in delivering good saver outcomes. Legislation should be used wisely not to undo the good work achieved so far. Enhancing options for members can be achieved by the market but only with the right framework in place. The proposed changes should consider the role of trustees being best placed to decide on options and for the market to develop those options, together with Government enabling product development. Helping savers means more than offering further options and flexibility, and must also translate into supporting savers in understanding additional options. Introducing CDC as a decumulation option will invariably add complexity to operations and administration, it also has potential to add more confusion to savers. Therefore the prospect of unintended consequences should be considered at the outset.

2 Consultation questions and answers

Question 1. Should it be up to trustees to determine the other suitable suites of products?

Yes, the trustees are responsible for overseeing and administering the scheme in the best interests of savers using their existing knowledge of their scheme's demographics. Trustees shouldn't be obliged to provide a particular product or benefit where it's not possible or practical to administer. For instance, there may be problems with entering into a new contract with their administrator to provide a particular product, or the administrator may not be able to provide the service, resulting in the trustees needing to enter into a new contract to provide the product.

The approach may increase concern among trustees given the potential risk where a member considers their support and associated services/products and deems them as unsuitable. Therefore, a clear framework is required in order to provide both trustees and savers with reassurance and also achieve consistent standards across the industry. For these reasons, the DWP could encourage trustees to provide certain services, but ultimately it should be up to trustees to decide what these should be.

Question 2. What can Government do to help a CDC -in-decumulation market emerge?

When coupled with the other papers issued as part of the Mansion House proposals, particularly the paper on "Extending opportunities for collective defined contribution pension schemes[1]", it's clear Government is interested in creating a market for savers to choose CDC at retirement. This would be a positive step but it's trustees' responsibility to decide what options to make available for their own scheme members – including whether CDC should be part of a range of options, and for the market to provide and develop these solutions.

CDC is part of the solution to enable the best outcomes for savers, but the development of the market relies on getting clarity in two areas:

1. What's needed to meet the authorisation requirements for a CDC in-decumulation scheme and how that may be impacted by existing master trust authorisation criteria (where the two potentially overlap)
2. The timetable for when such authorisation can start to happen

Without this it will be difficult for potential providers to know what they must do and when. Making it more challenging to undertake feasibility discussions and to plan for and cost out the development involved in setting up such arrangements.

Question 3. We would welcome views to understand what are the minimum requirements that trustees should put in place for members facing decumulation?

Trustees should assess the needs of their membership based on evidence and put in place options best suited to their own members. They should then be required to report on the reasoning behind the options they decide. The Chair's Statement would be an obvious place.

[1] Extending opportunities for collective defined contribution pension schemes

Schemes should offer a full range of options, or have good (evidenced-based) reasons for not doing so. Where schemes are unable to , they should have an arrangement in place to signpost to a suitable provider. Trustees should undertake regular due diligence ensuring the selected provider remains a suitable vehicle for their own members. The suite of options should cover full encashment, UFPLS, flexi access drawdown and access to an annuity.

Trustees should also consider whether savers would benefit from a soft default option and ensure they have access to information on their options, guidance to understand the implications of taking each option and access to advice. This should be delivered through a properly designed choice architecture.

Question 4. What factors should a trustee/scheme take into account when developing their decumulation offer?

Trustees must already take the demographics and needs of their own membership into consideration when designing their benefit structures and investment offerings. Therefore the factors to consider are relatively straightforward - age, wealth, pot size, engagement level, financial literacy, life expectancy, employee base of scheme and the age people take benefits.

Question 5. We would welcome views to understand if these are the right questions to capture the majority of ways an individual will want to use their pension wealth?

The questions provide a very good start in gaining an understanding of what an individual would like to get at retirement.

However, the question “do you want to do something else?” is too vague to be able to provide helpful and suitable guidance to their next steps. An individual could wonder what the other options are and think they’re missing out on a better benefit/offer, thereby rendering their answers to the other questions irrelevant. This would also be difficult to build robust operational processes around.

The question “do you only want flexible access to your pension benefits?” assumes the individual understands what flexible access means. Without context an individual could assume there’s total flexibility and not understand there are still limitations and regulation. A better question would be “would you like the option to receive ad hoc payments?”

Question 6. Are there any other questions we should include in the framework?

The framework should work as a flowchart to ask different questions based on the answer to the last. This should lead to a better understanding of what an individual is trying to achieve in their retirement before providing guidance and possibly signposting to a suitable drawdown option.

A helpful question would be ”how long do you want your income to last?”. Dependent on the answer - lifetime or fixed term – the product option would be adjusted for the individual’s requirements.

Question 7. We welcome views on whether you see any issues with this approach and whether there are potentially any implications due to the advice/guidance boundary.

There are a broad range of issues which the proposal could give rise to depending on the particular approach taken by trustees in complying with the new duty. However trustees choose to approach the new duty, they (and their administrators) will be concerned to ensure any assistance to savers in decision-making about retirement doesn't constitute regulated advice.

Trustees need to ensure they don't breach the requirements in relation to financial promotions. This is likely to be a particular issue in the context of partnering arrangements implemented as part of complying with the new duty.

Advice/guidance

As part of complying with the new duty, trustees would be required to decide which decumulation services are appropriate for their savers and how these should be provided. Savers tend to place a degree of trust in trustees and employers of occupational pension schemes, and may be more likely to choose the option put in place by trustees if they feel this has been 'vetted' by them. It would be helpful for guidance to be updated in due course to confirm taking this decision wouldn't, in and of itself, constitute regulated advice. It should also make clear what trustees can communicate to savers about the new option.

The boundary of guidance versus advice will come into play where an individual's personal circumstances are taken into consideration, and a product is recommended as a result. It's important to consider the administration practicalities as the process would need to ensure it doesn't involve the administrator exercising any sort of judgement or discretion.

Trustees would, as part of complying with the new duty, need to communicate to savers they would continue to have the option to access services on the open market. Presumably, the current statutory requirements in relation to pension guidance which trustees must comply with would continue to be relevant (ie provision of risk warnings, signposting to Pension Wise, delivering stronger nudge).

When putting together relevant communications, trustees are likely to feel hesitant about providing any support over and above complying with minimum legal requirements in case this strays over the boundary into regulated advice. Generally, trustees feel cautious when communicating with savers about retirement choices and will stick to the statutory minimum requirements. A similar hesitancy has been observed by some FCA authorised firms in relation to the personal recommendation boundary and guidance was published for them on 08 August 2023. But this isn't relevant for trustees and further guidance should be provided to them. For example, by updating the section on providing support on accessing pensions in the joint TPR/FCA guide for employers and trustees.

Partnering

Although some trustees have partnered with providers for services to their membership, others are still nervous. They're concerned about being perceived as endorsing a particular provider. Trustees are also concerned about

breaching FCA regulatory requirements, particularly breaching the financial promotion restriction (Section 21 Financial Services and Markets Act 2000[2] (FSMA)). As well as the risk of undertaking regulated activities as an unauthorised person (in particular arranging deals in investments and, potentially, providing regulated advice). Trustees are generally not familiar with the underlying legislation or the FCA's Perimeter Guidance and are concerned about what happens if they get things wrong.

Certain aspects of the current guidance could make trustees particularly nervous about implementing partnering arrangements and it would be helpful to revisit these in the context of the new duty. For example, in the joint FCA/Regulator guide for employers and trustees on providing support with financial matters, there are several references to the fact trustees shouldn't steer savers towards a specific provider. For example on page 5 under the heading providing support on accessing pensions the guidance states: "*However, if you steer them towards a specific product or provider, you could misdirect members to a product that does not meet their needs.*" There's further reference to this on page 10 in the context of providing factual information. These statements are likely to make trustees particularly nervous in the context of implementing partnering arrangements.

There's an element of regulatory arbitrage under the current system. For example, rights under FCA regulated personal pension schemes, such as Group Personal Pension Schemes, qualify as specified investments/controlled investments for the purposes of Sections 22 and 21 FSMA respectively, whereas rights under occupational pension arrangements (other than stakeholder arrangements) aren't.

Course of business

One way of increasing trustees' (and employers') confidence of not being at risk of straying into the regulatory perimeter in relation to these proposals could be to revisit the guidance on when trustees and employers are acting in the course of business. For instance, it could be clearer in the FCA/Regulator Guidance – if trustees (and also employers) aren't acting in the course of business when providing support for retirement planning, this means they're not at risk of undertaking regulated activities or being in breach of the financial promotion restriction as part of the complying with the new duty. Currently, the Guidance includes a statement to this effect, but then continues on the basis trustees are still caught within the regulatory perimeter.

Question 8. Do you have any suggestions for key metrics or areas that would need to be included if the proposed value for money framework was extended to decumulation or suggestions for where proposed metrics may no longer be required?

The proposed Value for Money (VFM) framework covers saver experience and administrative practices and provides a useful benchmark of what 'good' should look like. Extending this to cover decumulation and any retirement support offered makes sense to ensure a consistent and transparent view, highlighting those schemes providing excellent service and those where concerns may exist. Savers need easy access to these metrics to facilitate their

[2] https://www.legislation.gov.uk/ukpga/2000/8/section/21

understanding, forward planning and decision making. As a minimum, metrics should exist on choices, i.e. take up and response/turnaround times for where information is requested and provided, and outcomes are being finalised.

Since the introduction of pensions freedoms, greater choice for savers comes with associated risks sitting with the individual. The support schemes have in place to communicate and guide savers throughout accumulation and decumulation is central to this policy and framework. Assessing this support and the resulting saver engagement may be complex and difficult to quantify, but nevertheless a form of qualitative assessment will be required as a measure. For example, scheme offerings and member satisfaction may be assessed using standardised surveys and results. Administrators will be key to gaining this vital management information.

Question 9. Do you have safeguards in place for members in the decumulation stage? If so, what are these safeguards and what information do you provide to members?

As we're not a scheme, this question isn't relevant to our response. However as an industry body, we would expect to see safeguards in place and schemes to have a communication strategy in place to deal with savers' requirements at retirement.

Question 10. Do you use the same charge structure as you do in the accumulation stage?

Not applicable.

Question 11. We would welcome views to understand what are the practical considerations of partnering arrangements?

As mentioned in the consultation, single trust schemes are already using master trusts as an option for the provision of drawdown for savers, as both legally and practically it's difficult to offer this option via the existing construct. The principle of partnering arrangements seems most logical and having the savers' interest forefront is the most important aspect. However, there remains a nervousness amongst trustees as to how far they can go in signposting to a master trust offering. Other practical issues include the lack of providers willing to partner with a scheme due to the uncertainty of numbers, i.e. how many of the retiring savers will take this option and are there sufficient funds and savers for it to be economically viable for the master trust? We expect to see more master trusts offering a drawdown only product but only where the scheme has the demographics and pot sizes making drawdown attractive to savers.

The attraction of partnering with a master trust for drawdown is trustees responsibilities cease once the saver transfers. This then leads to a question of who's responsibility it is to ensure the master trust remains the suitable partner for the scheme. Should it continue to report on service and satisfaction to the trustees, or is it acceptable for the trustees to leave it to the established governance structure of the master trust to provide a continued quality service to those savers? Or should the trustees carry out formal due diligence checks on a periodic basis, as it would with any other scheme provider?

Another consideration is what happens if/when a partnering arrangement breaks down. What impact does this have on the saver and would there need to be remedial/recourse activity?

Question 12. Should Government set out a minimum standard partnering arrangement?

A minimum standard of partnering could restrict creative and innovative arrangements and would bring limited value. As with any arrangement, the metrics around choice, performance, etc should be looked at to encourage consistency and comparison to ensure the best option is selected.

Government should look to make partnering between single trust arrangements and master trusts easier, not harder.

Question 13.

a) **Should all schemes be allowed to establish partnership arrangements or only schemes of a certain size?**
b) **If only a certain size what should that be?**

Partnering arrangements should be open to all schemes and would benefit the smaller ones, opening up greater choice and flexibility for savers. However, as highlighted in our response to question 11, there are a multitude of aspects to consider.

Question 14. Is there a role for a centralised scheme to deliver decumulation options, where trustees are unwilling or unable to offer these directly?

On the surface a centralised scheme delivering simplified offerings, such as an annuity, CDC and drawdown looks like it could be a good option for smaller schemes with limited resources. However, all trustees have a responsibility to be willing to offer the best retirement options for their membership and any not doing so should question whether they should be in the market at all. We appreciate the difficulty of offering the full range of options due to legal advice and administrative complexity but many are currently providing options for their savers through signposting to master trusts, so Government should be making this easier for those schemes to do so.

Having a centralised scheme offering drawdown would reduce competition in the market, a market which is already looking to address this area. This should lead to innovation and improved service to savers whereas a centralised scheme would provide an out for trustees/schemes leading to potential complacency rather than striving for continual improvement.

In addition the market, trustees and providers alike are wary of who would decide what the centralised scheme would be and how it would be able to maintain its appropriateness for all while considering VFM.

Question 15. We would welcome views on if there is an alternative to our approach for legislation that would achieve the same results?

The market is naturally developing flexible solutions. But it needs assistance with making partnerships easier for single trust schemes to enter into. . If the Government were to force schemes to offer all flexible solutions, it would

fundamentally be forcing their hand, ensuring many well run and governed single trust schemes would close and transfer to master trusts.

Question 16. We want to work with industry during the implementation of these proposals; what timeline should we work to implement these changes?

The sooner the timeline can be shared the better. The timeline will be driven by how this aspect of the Mansion House proposals is prioritised against other aspects of government policy. It will be extremely challenging (and perhaps unrealistic) to seek to meet all the Government's objects at once and in short order.

It will take some time to settle on what the authorisation criteria looks like for CDC schemes, before expanding to create the criteria for decumulation options. It's clear this process will need to be measured in years rather than months, particularly if primary legislation needs to be put in place first.

It's worth noting CDC schemes are still in their infancy and not well established within the industry. Without a number of CDC schemes being established and options available, trustees/schemes would be unable to conduct thorough due diligence and comparisons. It would therefore be difficult to consider a timeline for proposals involving CDC schemes as it would have to follow on from the timing for bringing in CDC decumulation schemes.

It could be at least three or four years before the industry would be ready for this aspect of retirement choices – perhaps longer if other Mansion House initiatives take priority as there's only so much bandwidth available to deal with proposed changes and continue to meet existing statutory and regulatory requirements.

Question 17. When we introduce legislation should this apply to Master Trusts in the first instance?

Master trusts may be a suitable candidate to deal with these new requirements first (as they've done with other aspects of policy such as TCFD disclosure requirements) due to their larger scale and existing support structures. However, if this approach was taken, it could lead to a risk of creating a two tier retirement sector, with those in a well-run master trust receiving better retirement support than those in other kinds of pension arrangements.

A factor for consideration is master trusts currently tend to have smaller pots, particularly those with an AE focus, where they may not benefit from a wider range of options. Whereas more established single trust schemes have savers with larger pots. As the market consolidates, more and more individuals will likely have at least some of their pension savings held within a master trust. This means even if the new requirements were to apply only to master trusts to start with, it would still give many people access to better retirement support than they receive at present.

Question 18. Do you have views and evidence on how this can be delivered in ways that achieve our policy aims of stimulating CDC in decumulation, enabling Nest to provide the services outlined in this consultation, while ensuring a healthy competitive market place?

Not applicable.

Question 19. Are you able to quantify any of the one off or on-going costs at this stage?

Not applicable.

Question 20. Are you able to provide a breakeven point in pot size for certain decumulation products or services? Would this be different for decumulation only CDCs?

Not applicable.

Question 21. What benefits do you expect there to be from the proposals members/schemes/wider? Do you think they are quantifiable?

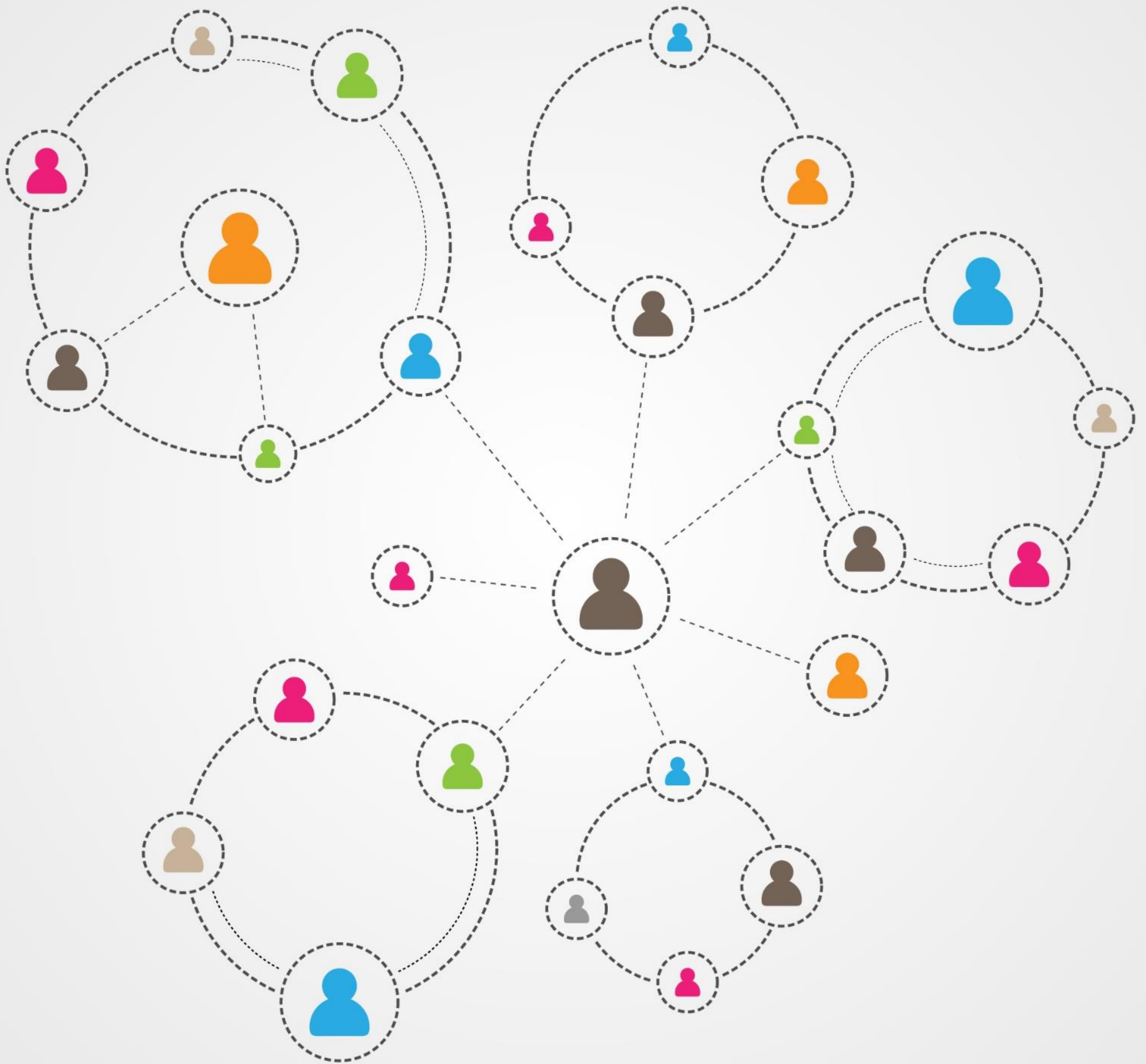
The benefits to introducing this proposal would be wide ranging and quantifiable to a degree. The proposed reforms focus on member outcomes giving savers more support both in preparation for, and at retirement. 'Freedom and choice' often comes with complexity, so it's key for savers to have clear communications giving sufficient guidance on the options and products available to them. Administrators are key stakeholders in providing this, and need to be fully involved in any measurement framework – both quantitative and qualitative.

Increasing consistency across the contract and trust-based markets will benefit savers and may result in an administrative cost saving for schemes which operate across both markets (as noted in paragraph 82). Other potential benefits include the wider plans for consistency when investing DC monies into illiquid assets (as referenced in paragraph 81).

Question 22. Do you think the benefits from the proposal changes outweigh the costs?

Overall yes, CDC is one of a range of options but care needs to be taken when implementing the proposal. Trustees remain best placed to decide which retirement options should be offered via the scheme and those to be provided via a provider, preferably one having been vetted by the trustees. Administrators will be one of the central players to providing the evidence base for trustees to make these choices.

PASA



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