VFM Policy Team

Financial Conduct Authority
12 Endeavour Square
London
E20 1JN

Lane Clark & Peacock LLP

95 Wigmore Street
London
W1U 1DQ

By email only to: vfmconsultationpaper@fca.org.uk

17 October 2024

Dear VFM Policy Team

LCP's response to Consultation Paper CP24/16 – The Value for Money Framework

LCP is a firm of financial, actuarial, and business consultants, specialising in pensions, investment, insurance, energy, health and business analytics. We have around 1,000 people in the UK, including 160 partners and over 300 qualified actuaries.

The provision of actuarial, investment, covenant, governance, pensions administration, benefits advice, and directly related services is our core business. About 80% of our work is advising trustees and employers on all aspects of their pension arrangements, whether DB or DC, including investment strategy. The remaining 20% relates to insurance consulting, energy, health and business analytics. LCP is authorised and regulated by the Financial Conduct Authority and is licensed by the Institute and Faculty of Actuaries in respect of a range of investment business activities.

Introduction

We welcome the opportunity to respond to the consultation CP24/16: Value for Money Framework. We advise on over £60bn of DC assets across a variety of DC schemes from Master Trusts to GPPs and Single Employer Trusts. We have therefore provided perspective from all DC arrangements.

Whilst we answer your specific questions below, we have taken the opportunity to summarise our key messages:

1. A Value for Money framework that allows employers, Investment Governance Committees and scheme members to review and assess their schemes is an important development for the industry and we support its implementation. However, it will cost money for schemes to comply with the framework and, particularly for commercial providers, this cost will ultimately be passed on to the individual saver The framework **needs to be proportionate and executable**. We have provided suggestions on which areas should be extended and others that should be modified. Therefore, we believe that this level of review should occur less frequently than annually, or alternatively, the depth of the review could be staggered to ease the burden in certain years, particularly for those where prior years show a history of delivering good value.

2. We strongly believe that should this framework but put in place, the DC Chair's Statement should be removed to mitigate some of this additional compliance burden.

3. We also believe **efforts should be made to standardise reporting to ease the burden on the industry** to gather this data and on a compliant basis. We would be happy to discuss our thinking in this area further.

4. We view the required inclusion of all costs and charges as unnecessary and misleading for a true value assessment and further, note that it will be virtually impossible to provide a comprehensive assessment of all costs and charges across scheme design, particularly for employers where they take governance of their scheme more seriously. This particularly applies to trust-based schemes where the employer will typically be subsiding their unique scheme rather than a commercialised scheme. The required inclusion of these costs and charges would likely disincentivise employers in undertaking any additional work and **we strongly urge you to only focus on member borne costs and charges** – the far more important element of any cost assessment.

5. The Value for Money framework is an assessment of schemes against the value of the pension products they offer, however, the current proposal is for this to be assessed on a quantitative basis. As such, **it feels to us that the assessment is focused on what can be measured rather than on what is most important**.

6. In particular, we **strongly believe that schemes should be required to demonstrate their commitment to and consideration of Environmental, Social, and Governance (ESG) risks and opportunities, as well as stewardship,** as part of the assessment of a default strategy. Given that much of this assessment will inherently be qualitative, we have proposed an initial remedy for consideration in Question 30.

7. While it is easy to focus on the costs that members incur, the central focus of the Value for Money framework should be on the value that is delivered for scheme members. While we recognise the importance of assessing costs, **we are pleased to see that the assessment focuses on value first, and then cost second** as part of the assigning of the RAG status. We are supportive of your approach here.

8. That said, **the proposed RAG ratings are too blunt**. We believe these need to be broader to allow for short-term areas for improvement, which could be rated as Amber without having a specific closure action attached or an additional rating. Otherwise, this will ultimately lead to all schemes being rated as Green.

9. We have concerns that all of the metrics and disclosures are backwards looking and, hence, do not have our preferred perspective of delivering future outcomes. This is particularly relevant when considering past performance rather than assessing likely future performance of default arrangements. **Assessing forward-looking metrics is a fundamentally important addition to the Framework** and look forward to seeing your progress in this area.

10. While we appreciate the steps required of a contract-based provider where a Red status is assigned, we are concerned that this may not persuade all members and/ or employers to take action. This would require employers to engage and select a new arrangement for their auto-enrolment obligations, which is likely to incur time, effort and costs. However, in our view, **without a requirement for full closure or a similar action placed on employers, new employees will likely still be enrolled into a scheme which has a Red status**, which is unlikely to be in line with Consumer Duty requirements. As we set out in Q.34 we also strongly support enabling legislative changes that would permit providers to move savers out of Red-rated arrangements where it is in the best interests of savers and subject to appropriate safeguards.

Scope and thresholds

Question 1: Do you agree with the proposed scope, thresholds and exclusions? Why or why not? If not, what alternatives would you suggest?

We agree that it is important to focus the framework on default and “quasi-default” arrangements in workplace pension schemes in the accumulation phase in order to get as much initial coverage by the framework as possible. However, we believe that the framework should be extended to cover non-workplace pensions as soon as possible in order to extend saver protection. Savers in workplace pension schemes are frequently targeted by campaigns and incentives from non-workplace pension providers to transfer their pensions and in order to ensure that such transfers are not disadvantageous these non-workplace pensions should also be subject to VFM assessments.

The framework should be extended to cover decumulation solutions because, as the “DC generation” reaches retirement age, decumulation will become as important as accumulation has been over the last couple of decades – we are encouraged by your comment in paragraph 12.8 that the framework could be relevant here as well but suggest that extending the framework to cover decumulation should be developed alongside the initiatives for schemes to offer default guided retirement products.

We do believe that it is important that there is parity between VFM requirements for both contract and trust-based arrangements. We acknowledge that you state you are working with DWP/ TPR to ensure this is the case but would urge you to make sure this does happen. This is likely to be particularly important for some Master Trust providers which are regulated by both the FCA and TPR.

We would like you to provide guidance about what counts as a “minor variation in the terms” of different packages of services as referred to paragraph 3.8.

We agree with the decision to exclude EPPs for the reasons you state.

LCP powering possibility

Question 2: Do you agree with the proposed application of the 80% threshold to determine whether legacy arrangements are quasi-defaults? Why or why not? If not, what would you propose?

Overall, we agree with this in principle.

However, the wording in paragraph 3.9 may need some clarification. It currently refers to “at least 80% of employees and ex-employees (active and deferred) of at least 1 employer in the arrangement”. It is unclear to us how a provider will be able to determine whether 80% of an employer’s **employees** are in an arrangement. Should this be changed to “at least 80% of the participants (active, deferred and pension credit members) linked to at least one employer in the arrangement”?

For trust-based arrangements, care needs to be taken as to how this will apply to “unintended default” arrangements that occur. In brief, this situation can arise when members who are not in a default arrangement have been invested in a fund(s) without their specific consent – usually driven by the need to urgently protect members or improve member outcomes. However, as a result of regulations these investment arrangements are then deemed to have become default arrangements and could impact over 1,000 members within larger arrangements, triggering in scope requirements under the consultation. We have had extensive discussions with DWP about this and would be happy to expand on it with you if that would be helpful.

Question 3: Do you agree with the proposed 1,000 member threshold? Why or why not? Do you think there are risks around this level, for example excluding too many savers? If you don’t agree, what would you suggest?

We acknowledge that you have set this threshold for proportionality and that the additional sole and largest arrangement tests will apply to small trust-based schemes. However, from the perspective of an individual saver, VFM should not depend on whether they happen to be in a large or a small arrangement and therefore we suggest that consideration is given to removing this threshold number, so that coverage of savers is maximised. Further, it is often in sub-1,000 member arrangements that poorer VFM is found and therefore this threshold could run counter to any policy intention to improve VFM in these smaller schemes.

Should this framework be made mandatory for trust-based schemes, we request clarity about whether this threshold is set at employer level *within* the provider’s scheme or at provider level. To give an example, consider where Firm A and Firm B both have default arrangements in the same scheme with Provider P. Firm A has 1,500 members enrolled in its default arrangement and therefore the framework will apply to it. However, Firm B only has 800 members in its default arrangement *within the same scheme as Firm A.* Our reading is that Firm B’s default arrangement would be *exempt* from the framework. Is that your intention?

We also note your comments that the “sole or largest arrangement” tests will be relevant for small trust-based schemes and therefore we expect that TPR will want to confirm they are content with this.

Investment performance

Question 4: Do you agree with the proposed investment performance metrics? Why or why not? If not, what alternatives would you suggest?

We are generally supportive of the requirements contained in the proposed investment performance metrics. However, we have the following key observations:

- We strongly believe disclosing performance data for other cohorts should be considered. It is quite typical that an investment strategy will look very different at other ages. As such, we propose that a further data point for reporting should be at 15 years also.

- To ease the collation of data and reduce the concerns of the burden of reporting and the quality of such data, **we believe service providers should be required to provide this data according to a specified template, and by a specific deadline**. We have experience of previous data reporting initiatives where service providers were unable and/or unwilling to provide the necessary data, in the required format and/or within the required timeline. The use of a template will make it apparent that data received is in the correct format for schemes to use and the deadline for the completion of the data would be clear.

- Our view is that the absence of a forward-looking metric leaves the VFM framework limited in supporting a fully rounded view of the arrangements, as a forward-looking metric would shift the focus to the future

rather than always focusing on the past. In particular, updates to default arrangements will be presented to employers and members using out of date information, which limits the benefits to schemes of future design and innovation. **We provide further comments in question 8.**

- We view the required inclusion of all costs and charges as unnecessary and misleading for true value assessments and further, note that it will be virtually impossible to provide a comprehensive assessment of all costs and charges across scheme design, particularly for employers where they take governance of their scheme more seriously. Many single employers we work with have dedicated teams who support the day to day running of their pension arrangement, which is not a cost paid for by members, in a similar way that administration costs are typically paid for by the sponsoring employer. Even smaller schemes undertake a level of governance outside of their scheme provider, particularly where they have bespoke default arrangements. Further, how would change-project related costs feature in any assessment. The required inclusion of these costs and charges would likely disincentivise employers in undertaking any additional work and **we strongly urge you to only focus on member borne costs and charges** – the far more important element of any cost assessment.

Question 5: Do you agree with the proposed calculation methodology? Why or why not? If not, what alternative methodology would you suggest?

While we generally view the use of a monthly return series as appropriate for this type of performance reporting, we note the use of monthly return data is a compromise, which is likely to affect the quality of the risk calculations as, for example, it could mask the level of drawdowns impacting members intra month particularly where there are market shocks. We believe this aspect to the reporting should be kept under review.

We also note that there is no specific requirement for which data points should be used to undertake this calculation, which means that performance will vary due to the pricing point used, for example mid-day or end of day pricing; Trade Price or Net Asset Value. This eases the reporting process for schemes, however, this variation in reporting period could affect performance and as such, determining a rating based on this data should be treated with caution.

While Annualised Standard Deviation ('ASD') is a common measure of risk, we do not believe that it provides the appropriate focus of risk for members. We provide our clients with risk on a Value at Risk ('VaR') basis, which provides clarity on risk more in line with what members are concerned about i.e. potential losses and tail risks. **We believe VaR is a more appropriate risk measure than ASD.** Members are not worried about risk if they savings are increasing.

As a broader theme for the new requirements, we note the amount of data being reported is significant. While we agree that this reporting is needed, the industry should be encouraged to seek ways of mitigating this impact on schemes, for example, using a standardised template for reporting.

Question 6: Do you agree with the proposed requirement for chainlinking? Why or why not? If not, what would you propose?

Yes, we are generally in favour of your proposals as the requirement to chainlink performance will stop schemes from changing defaults just to remove weaker longer-term performance.

However, the approach to merging in-scope arrangements seems at odds, given members will be in the retained default arrangement and not a 'merged' default design. Hence, **we believe members should be moved to the better default arrangement, regardless of the type of arrangement they are in, and that performance should be used for reporting**. We also note that the example in Situation 2 will significantly impact on the complexity of reporting where in-scope arrangement mergers take place.

Question 7: Do you agree with the approach to in-scope legacy arrangement features? Why or why not? If not, what alternative approach would you suggest?

We agree that legacy arrangements with special features should be included in the VFM framework and this includes other aspects such as being part of a hybrid benefit arrangement. However, we do not agree with your proposed approach that seems to ignore the benefits of these features (with-profit sharing, smoothed returns, and guaranteed returns) for the **saver**. As we discuss elsewhere in our response, we believe that VFM should be based on what the end-user, ie the actual saver, perceives.

Question 8: Do you have further feedback on the incorporation of forward-looking metrics within the Framework? If included, how prescriptive do you think we should be on assumptions and methodology, and what would you propose?

We recognise there is complexity and different views about incorporating forward-looking metrics within the framework. However, there is also the well-used investment mantra that "past performance is not a guide to future performance" so, given that, it is overly simplistic just to use backward-looking metrics.

Some of the issues around "gaming" forward-looking metrics could be mitigated by being relatively prescriptive about how these are used. We note your reference in paragraph 4.36 about consistency with SMPIs and also your intention to look at forward-looking metrics more holistically in the future. We are keen to be part of that process and discuss these issues further.

Asset allocation disclosures

Question 9: Do you agree with the approach to asset allocation disclosures? Why or why not? If not, what would you suggest? Do you think asset allocation disclosures will support better decisions in the interests of savers?

Your consultation is clear that the asset allocation disclosures "do not form a direct part of the assessment process that determines the VFM rating". Given this, we question why you have included them. We are not against providers and trustees knowing where they are investing saver money – indeed we would be astonished if this wasn't a significant consideration of any professionally run scheme. But your proposals would add a considerable compliance burden to schemes and since the asset allocation is not to be directly used in the VFM assessment we question whether this is the correct place to be considering it.

We are mindful that reporting this data is likely to be used as a comparison for schemes when designing their own default arrangements and hence, will make schemes more susceptible to herding. We do not agree that this asset allocation disclosure will aid the assessing of the significant impact allocations will have on returns as asset classes are still very broad and hence, returns could be very different indeed. Further, strategy design and asset allocation is likely to change over time and hence, the asset allocation data is only helpful for recent performance and snapshot analysis.

We do not believe schemes should be required to report this data.

A more minor point, we believe the table in 5.20 should be listed by order of priority as noted in 5.16 for ease.

Question 10: Do you agree that asset allocation disclosures should be limited to firm designed in scope arrangements only? Why or why not? If not, how would you broaden this requirement and to what arrangements?

We agree with this limitation and that the requirement should not be broadened.

Question 11: Do you agree that we should require the disclosure of the overall asset allocation of the whole arrangement, as well as for the YTR points? Will this be of use to firms, and will it be an added burden to disclose?

We are not convinced that disclosing the overall asset allocation of the arrangement serves much purpose and hence, **do not believe this should be included in the reporting requirements**. The framework will create significant compliance work for providers and we believe that unless there is a clear benefit in providing additional disclosures, this burden should not be added to.

Question 12: Do you agree with the proposed definitions for UK assets? If not, what would you propose?

Firstly, we are positive about schemes investing in productive/private assets which includes UK assets, but only where it is likely to lead to better saver outcomes.

Secondly, we are concerned about the motivation behind these disclosures. The reasons you give in paragraph 5.10 will already be being considered by any professionally run scheme when making investment decisions. Disclosure of a UK/ non-UK split will not assist these decision makers.

Having said that, if you do proceed with this then we are broadly content with the definitions. However, a listing on a UK market does not necessarily indicate that the company's business mainly derives from and is based in the UK. It is widely recognised that many firms listed in the FTSE100 are global businesses and therefore disclosure of investments in the FTSE100 simply discloses that – nothing more, nothing less – and is not indicative that a pension scheme is investing in UK based businesses. In fact, the UK index is a significantly more global index when it comes to revenue than many of the other country or region indices.

Question 13: Do you think we should break out 'Quoted but not listed' (eg AIM) and if so, how would that be useful? Would there be additional cost to doing this and can you indicate how much?

We see no material benefit to this further disclosure and again would oppose disclosures that are unlikely to have a tangible benefit to saver outcomes.

Costs and charges

Question 14: Do you agree with the proposed costs and charges metrics? Why or why not? If not, what alternative metrics would you suggest?

Our main concern here is about your proposed approach for treating employer subsidies as member-borne charges. From the saver's perspective that is simply not the case and doing so will seriously distort the VFM assessments of schemes where sponsoring or participating employers are going the extra mile to voluntarily improve their scheme's VFM for their employees. We are not keen on advocating additional disclosure to the already lengthy framework proposals but in this instance, we believe that you need to review your position on this issue.

Clarity is also needed about what is meant by an "employer subsidy". Whilst it is clear that an employer paying a provider a sum of money to reduce the percentage charge incurred by employees is a subsidy, what about other costs associated with pension provision that employers frequently pay for, such as communications campaigns, provider reviews by an advisor or, for trust-based schemes, paying the fees of a third-party administrator?

And whilst you say that 10 and 15 year costs and charges can be reported "if reasonably practical to obtain" we see little benefit in going this far back in history in any circumstance and therefore we suggest that the reporting periods are just limited to 1, 3 and 5 years.

Question 15: Do you agree that historic costs and charges information should be calculated in the first year of implementation, rather than waiting for this data to build over time? Please explain your answer. If you do not agree with either approach, what alternative would you suggest?

Providers should already have the bundled costs and charges data to hand, but should you require the costs to be split between administration and investment, this could be difficult for some. Therefore we suggest that you obtain historic costs and charges on a bundled basis initially, then ask for more detailed information in say 2 to 3 years' time.

Question 16: Do you agree with our proposed approach to converting combination charging structures to annual percentage charges? Why or why not? If not, what alternative would you suggest?

We are not convinced with this approach and believe it would need to be quite prescriptive in order to prevent the possibility of schemes using combination charging to "game the system" for a possible unfair competitive advantage. You have recognised the difficulties of using forward-looking metrics for investment performance so it is unclear to us why you are proposing what is an analogous approach when it comes to combination charging.

Please also see our comments in Q.25 about using such schemes as comparators.

Question 17: Do you agree with the proposed approach to unbundling? Why or why not? If not, what alternative would you suggest?

As commented in question 15, some providers are currently unable to provide an unbundled cost so will need time to be able to provide this. We also have concerns that a methodology requiring approximations and estimations may not be sufficiently robust for use in comparing costs and charges against other comparators using a different method.

Question 18: Do you agree with the proposed approach to multi-employer cohorts? Why or why not? If not, what alternative would you suggest?

We are not convinced that so many reporting bands are needed, nor that reporting is needed both by asset size and number of members. We suggest that the reporting bands are consolidated and that either asset size or member numbers are chosen as the sole reporting requirement. We also question the assertion in paragraph 6.33 that the cohort table still need to completed even where charges do not vary between employers. Where this is the case, why can a simple declaration to this effect not just be made?

Quality of services

Question 19: Do you agree with the proposals on scope? If not, what alternative approach would you suggest?

We agree with the principles of your proposals and also acknowledge your comments that measuring service quality is very challenging. We would expand on that to say that there could be some difficulties in attempting to fit the same metrics across the entire workplace pensions space to fairly and equally apply to both contract and trust-based arrangements (not to mention non-workplace pensions, should the framework be expanded to include that).

Similarly, the proposal to use a calendar year reporting period may not fit well with many trust-based schemes own year ends. Therefore, we consider it is likely that TPR will want to carefully review these proposals when considering an analogous framework for trust-based schemes.

Question 20: Do you agree with the five proposed indicators of service quality? If not, what alternatives would you suggest, with metrics?

Again, we agree with the principles of your proposals but believe that some will be less applicable to trust-based schemes should this framework capture them.

We believe that the FCA should undertake to review these indicators after, say, five years of the framework being in operation to determine if the indicators are working as intended. The indicators should also be reviewed as and when the framework is expanded to include decumulation.

Question 21: For each of the five proposed indicators, do you agree with the proposed metrics for measuring these? If not, what metrics would you suggest? We would particularly welcome views on these metrics.

For the promptness of core financial transactions, we note that several of the metrics are compared against either a service level agreement or internal policy. This does, of course, raise the possibility that these agreements and policies could be made more generous by providers so as to avoid a poor assessment in the VFM framework. We suggest that FCA needs to consider ways to mitigate against this.

In addition, memberships of schemes will be different, for example some memberships may have older members and therefore will interact with the providers more frequently than younger members and so could skew reported data. In order to mitigate this, you could consider asking for further information behind the data (eg member demographics).

Question 22: Do you agree with our proposal to include a non-employer related email address and phone number when defining common data? If you don’t agree, please explain why not.

In our view this proposal has some difficulties to it. Firstly, there are GDPR issues to consider since personal email addresses and phone numbers are likely to count as personal data. Secondly, schemes are less likely to hold this data than the other common data items, for several reasons such as the saver (or employer) not providing them, or the saver simply not having either of these. Therefore, if you do include these items as common data then there needs to be an option for schemes to record that they have attempted to obtain this data but that it is unavailable. This will avoid schemes being penalised for matters beyond their control.

Question 23: Do you agree with our proposals for an event-based member satisfaction survey? We would particularly welcome feedback on the trigger events and proposed questions.

We are pleased that you recognise in paragraph 7.28 that many savers will not interact with their provider, and that is our biggest concern about mandatory member satisfaction surveys. Experience shows that individuals are more likely to complete such surveys after a negative experience, rather than a positive, and this can skew results. And in terms of comparing against other schemes, a specific scheme's membership profile (eg wealth and other demographics and overall engagement with pensions) is very likely to affect the results of a survey.

The wording in the final standard question of the survey should be modified to clarify that the question is about satisfaction with the service received from the scheme, eg "*Overall, I am satisfied with the service I have received from my scheme*". Otherwise, there are many reasons why a saver may be dissatisfied with their scheme, including, for example, why their employer is not paying substantially more contributions to the scheme – but that is a different issue from a survey about the scheme's service!

Question 24: Do you think that a firm should be able to provide a saver specific view of access to tools and saver use across its digital offerings? If not, what metric would you suggest?

We are unclear what this question is actually asking but we would agree that – where providers or schemes have made digital tools available – metrics measuring use of these tools should be included.

Assessment and outcomes

Question 25: Do you agree with our proposed conditions for the selection of comparator arrangements? If not, what would you suggest?

We broadly agree with the proposed conditions although we will raise some further considerations. Requiring not one but two of the comparators to have total DC workplace pension assets above £10bn will limit comparisons to a handful of schemes primarily run by commercial providers and could skew comparisons and/ or lead to an oligopolistic situation. This requirement seems to run counter to your view in paragraph 8.12 that "comparator arrangements should be chosen from across the market…".

The requirement to compare against both contract and trust-based schemes will require that VFM frameworks be launched in both spaces in the same timescale and must be comparable and equitable with each other.

You will be aware that one of the largest master trusts in the market and which is likely to be chosen as a comparator operates a combination charging structure. This is one of the main reasons why we have expressed our concerns about your approach to these schemes in Q.16 above. We believe that your proposals for these schemes could lead to distortions in the comparison process if combination charging schemes can assess themselves using estimated future charges.

We are also unclear how straightforward it will be for IGCs and trustees to analyse the arrangements of each comparator scheme and then "choose the largest by assets" as set out in paragraph 8.9.

Clarity is also needed about what "provider-designed" means when choosing a comparator arrangement. We assume this is when the provider creates and manages the arrangement for many schemes, rather than it being created specifically for one scheme only?

Question 26: Do you agree with the assessment process we have outlined above? Do you have views on what should be considered a material difference in value relative to comparator arrangements? If you think that RAG ratings will not be sufficiently comparable, what refinements would you suggest?

Overall, we agree with the steps of the assessment process.

However, the RAG rating system you propose is too simplistic and blunt, particularly when receiving an Amber rating is almost as severe as receiving a Red rating.

We strongly believe that either the Amber rating needs to be less penal on providers or that there needs to be further graduation of the rating system. For the former we suggest that Amber is modified to still require communication to employers and with a detailed action plan for how VFM will be improved within a short time period, but the arrangement can continue to accept new business.

Alternatively, for the latter suggestion, we propose that a five-point rating scale is introduced which includes a band sitting between Green and Amber that indicates that arrangements need to improve VFM within a certain timescale

but no explicit notification to participating employers is triggered and there would be a further “Super-Green” band sitting above Green to indicate an arrangement that has been assessed as providing not just “good” but “exceptional/ market-leading” VFM. We believe that the introduction of this “carrot” is more likely to drive VFM improvements through competition between providers rather than just the “stick” to avoid Amber or Red ratings.

We also recognise your concerns in paragraph 8.38 that fear of receiving an Amber rating could stifle recent progress made in alternative assets since the commercial risk of receiving an Amber rating is likely to outweigh any upside to alternative investment strategies for the provider (at least in the short term).

We agree that you should not **define** what a “material difference in value” is, but we would advocate you producing **guidance** as to what this means in practice. Without this guidance, different IGCs are likely to adopt different interpretations and being able to cite such guidance may help IGCs in discussions with the actual provider.

Question 27: Do you agree that a multi-employer arrangement should be rated amber if it fails to deliver value for a material number of savers in relation to at least one employer cohort? If not, what would you suggest?

No, we do not agree with this. The difference between employer cohorts within a multi-employer arrangement is likely to come down to costs and charges. It is quite likely that some employer cohorts which have been able to negotiate lower costs will be receiving VFM even if other cohorts are not. It seems more logical to determine overall VFM in these arrangements by employer cohort and take appropriate action on that basis.

Question 28: Do you have any concerns about our proposals for assessing bespoke in-scope arrangements? If you do have concerns, please explain them. If you anticipate negative effects, what can be done to address those?

We agree with the principle that bespoke in-scope arrangements would benefit from a simpler assessment process. However, having read your proposals for this, we are unclear about what you intend in detail. Therefore, we will not comment further apart from to say that we would welcome clarification on this point.

Question 29: Do you agree that IGCs should consider and report on whether their firm’s current scale may prevent it from offering value to savers? If not, what would you propose?

Whilst we do not accept the notion that scale is a panacea for all issues about pensions investments and saver outcomes, we do agree that it is reasonable for IGCs to consider and report on whether a lack of scale is detrimental to savers.

Question 30: Do you agree that IGCs should consider how ESG considerations have been taken into account across firm-designed in-scope arrangement? Do you think this is sufficient and if not, what would you suggest?

We believe that a broader interpretation of VFM is important for facilitating more sustainable investment, which is expected to help deliver better outcomes for members. **We advocate for ESG risks, opportunities and stewardship being included on a mandatory basis in the VFM assessment**. We recommend a qualitative approach, since the assessment of a scheme’s ESG approach is not well-suited to quantitative metrics.

We strongly believe that schemes should be required to demonstrate their commitment to and consideration of ESG risks, opportunities and stewardship. So, we suggest having a simple checkbox to confirm the IGC is satisfied that ESG considerations and stewardship have been taken into account in the design of each default strategy in a way that it considers appropriate for delivering long-term value to members.

In addition, we believe it is important to enable schemes to adopt an appropriate approach to ESG factors even though they may cost more in the short-term. For example:

- Across the industry as a whole, current levels of stewardship are inadequate for delivering the best outcomes for savers. A recent report, commissioned by the Principles for Responsible Investment and written by the Thinking Ahead Institute, suggested that the industry needs to double stewardship resources over time. This is likely to increase costs but is expected to deliver better value over the long-term. It is important that the VFM framework does not discourage schemes from paying more for higher quality and more extensive stewardship.

- The investments that contribute most to a more sustainable economy (eg climate solutions) tend to be illiquid, hence cost more, but may deliver better outcomes for savers. A well-designed VFM framework would therefore support our request to policymakers that "It should be easier for DB and DC pension schemes to invest in climate solutions (including growth and/or illiquid assets)". As at 14 October 2024, this request had the support of 45 asset owners totalling £183bn assets under management.

Actions for arrangements offering poor value

Question 31: Do you agree that firms should inform employers of amber and red ratings and proposed steps to address the poor value, where an employer's current and past employees are at risk? If not, why not and what would you suggest?

Notwithstanding our comments in Q.26 above we agree with this.

Question 32: Do you agree that firms should not be allowed to accept business from new employers into an arrangement rated amber or red? If not, why not and what would you suggest?

We agree that arrangements rated Red should not accept business from new employers but we again refer to our answer to Q.26 regarding modifications for actions following an Amber rating.

We also believe that this requirement would be difficult to implement for single employer trusts so TPR may want to consider this point as well.

Question 33: Do you agree with our proposed actions and timings for firms with arrangements rated amber or red? If not, what alternative approach would you suggest?

We are content with the proposed actions and timings for firms with Red rated arrangements, but again, see our previous comments for suggested changes for Amber arrangements.

The timings proposed are tight but, realistically, we expect most providers will be able to anticipate when an arrangement is going to be rated Amber or Red and therefore should be able to start preparing to take action ahead of formal notification from the IGC.

Question 34: Do you think that we should require firms to transfer savers out of red-rated arrangements, subject to enabling legislative changes? What are the costs associated with the proposed actions and are they proportionate? If you don't agree with our proposed actions, what would you suggest?

We believe that *requiring* firms to transfer savers out of Red arrangements is a step too far. But we strongly support enabling legislative changes that would *permit* providers to do so where it is in the best interests of savers and subject to appropriate safeguards.

The costs and timescales involved with a transfer without consent exercise should not be underestimated. These exercises are significant projects, may not always be appropriate (eg where there are guarantees or tax protections and/ or savers are near to retirement age) and will probably be seen as an option of last resort.

Question 35: Do you think that requiring transfer from arrangements could benefit one group of savers to the potential detriment of others? If so, please explain and can you suggest an approach that doesn't risk detriment to some savers?

There are two ways of interpreting this question:

- **Could a bulk transfer be detrimental to *some* of the group of savers who are being transferred?** The answer to this is yes where, as noted above, savers may have tax protections or guarantees that could be lost on transfer, or are already too close to retirement to effectively benefit from the transfer.

- **Could a bulk transfer be detrimental to a group of savers in the same arrangement who are *not* being transferred?** If the transfer were carried out on a fair and value-driven basis then we do not see this being a real concern. If transfers out of an arrangement reduced that arrangement to such a degree that it can no longer operate at scale then that would itself indicate that the arrangement should be fully closed.

LCP powering possibility

Disclosure requirements

Question 36: Do you agree with our proposals for how the Chair's annual reports should be expanded to include the results of VFM assessments? Are there any proposed elements that in practice would not be useful?

Yes, this seems sensible. However, we note that the last bullet point of paragraph 10.8 requires that reports include how ESG considerations have been taken into account "whilst not mandatory". If something is not mandatory then it should not have to be included in the report. As stated earlier, we believe ESG considerations should be included in the assessment.

We want to record our very strong view that the requirements for DC Chair's Statements should be removed since the VFM framework is likely to be more useful and lead to better saver outcomes. We strongly oppose the continuation of DC Chair's Statements in parallel with the VFM framework on the basis that this would be an unbearable compliance burden.

Question 37: Do you agree with requiring a narrative explanation for the RAG rating for all firm-designed in-scope arrangements including those rated green? Do you think this requirement should be limited to amber and red ratings?

We agree with this as long as a narrative explanation is proportional and kept fairly short (for example within a particular word count). For Red and Amber ratings a narrative would be helpful in explaining why VFM has not been achieved and, for a Green rating, a short narrative might be helpful in explaining any areas where judgement calls have been made in matters of materiality, for example.

Question 38: Should IGC Chairs be required to produce a plain-language summary of their reports?

In theory, a plain-language summary is to be welcomed. However, in practice disengagement amongst pension savers is extremely high, as you note several times throughout the consultation. Therefore it is not clear whether the additional cost of this would be justified. However, this may be a "chicken and egg" situation, whereby plain-language summaries would increase engagement. On balance, we believe that IGCs are themselves best placed to decide if a plain-language summary would be useful and therefore the current status quo of voluntary production of these should continue.

Question 39: Do you agree with the need for a features table and the contents we are proposing? Are there changes we should consider? Do you think that the disclosure requirements for bespoke arrangements should be different and if so, in what way?

We see the attraction of such a features table but do wonder if providers will be happy to disclose all of the proposed components of it since some of it is bordering on commercially sensitive information.

Question 40: Do you agree with our proposed approach to publication including requiring publication of a flat file? What other solutions would best support the aims of the Framework in due course?

We support the idea of a machine-readable flat file being produced that will enable automated comparisons between schemes, alongside more readable reports intended for human consumption.

However, we do note that your example template has more than 1,100 rows on it which shows the potential quantum of data that schemes are required to produce for each in-scope arrangement.

Question 41: Do you think we should require machine-readable RAG ratings and potentially other information from the IGC Chair's annual report? What do you think are the benefits and costs or possible negative effects of this?

The ability of AI tools to parse and interpret prose and technical text has increased exponentially over the last few years. We expect that the rapidly increasing capabilities of these tools will mean that no special machine-readable versions of the annual report will be required.

Amendments to current Handbook requirements

Question 42: Do you agree that the proposed new rules should be under existing requirements for IGCs, with carve outs as appropriate? If not, what alternative approach would you suggest?

Question 43: Do you have suggestions for further amendments to existing requirements for IGCs and if so, why do you think these are needed?

Question 44: Do you agree that we should exempt "accidental workplace SIPPs" from COBS 19.5 and the requirement for an IGC or GAA? If not, what would you propose?

Other organisations are probably better placed to answer these questions about amendments required to COBS but from our reading your proposals in this section seem sensible to us.

Future development

Question 45: How do you think the use of data will evolve and what other measures may be needed?

Question 46: We invite views on the roll out, evolution and future phases of the framework, over what time periods, and on the correct sequencing of these developments.

We will answer these questions together by giving our thoughts in this area.

Overall, we request that sufficiently long notice of the framework implementation is given so that affected providers and schemes can properly resource for it. You have noted that Pensions Dashboards are currently under development and with this, and many other regulatory initiatives, providers are struggling to manage it all.

We also ask that FCA (and TPR) react nimbly and quickly should it become apparent that there are post-implementation issues with the framework that need adjustment. In asking this, we are mindful that this may be a particular issue for TPR that does not have the same direct power to make rules as FCA does.

We have mentioned above that we are in favour of rolling out the framework more broadly to sub-1,000 member arrangements, non-workplace arrangements and also being applied to the decumulation phase. We have also said that we believe that inclusion of forward-looking metrics should be considered.

The idea of incorporating VFM information into Dashboards sounds appealing in principle, but as you allude to, it will be critical to get the balance right regarding member comprehension and behaviour to avoid negative impacts. We are also mindful of what lessons can be learnt from DC chair's statements.

Cost benefit analysis

Question 47: Do you have any comments on our cost benefit analysis?

Most of our views about the CBA can be derived from our answers to the previous 46 questions.

However, we would make the following additional points.

The framework will require collation of a huge amount of data and for providers with many default arrangements this will be multiplied many times over. We request that where data collation can be cut back that it is done so – as we have suggested in a couple of places in our response.

We are concerned that an annual VFM assessment is too onerous and could hamper actual improvements to VFM if providers and schemes get caught up in a resource-intensive annual cycle of these assessments, as we have seen with DC Chair Statements. We do not believe that VFM needs to be assessed every year, and we draw comparisons with, for example, the requirement to normally only review a Statement of Investment Principles every three years.

We have already expressed concern about the simplicity and bluntness of the proposed RAG rating system and in particular the commercial impact that an Amber rating will have on a provider. If this is not altered then we believe that IGCs (and trustee boards) will go to quite some length to avoid giving Red or Amber ratings resulting in the majority of arrangements being rated Green. This does risk defeating the entire purpose of the VFM framework.

We also believe that very few employers will have the appetite to investigate beyond whether their arrangement is rated Green or not. We do not believe that the majority of employers will push their providers to deliver further VFM improvements to a Green rated arrangement. It will be competition between providers that improves VFM beyond this point.

We also noted your assertion that the framework could close the gap in performance by 1%-3% each year. We would, of course, welcome this improvement if it could be delivered by the framework but we would be interested to see more of your analysis backing this expectation since this seems quite a large enhancement to achieve, particularly on a cumulative basis.

Conclusion

As we said in our introduction, we welcome this consultation and support the introduction of the VFM framework and we trust that our comments are read in that context. We would, of course, be very happy to discuss any of our comments in detail with you and we look forward to the next stage of implementing a VFM framework for the benefit of savers.

Yours sincerely

{By email only 17 October 2024}

Laura Myers
Partner
Head of DC

+44 (0)20 7432 6639
laura.myers@lcp.uk.com

Lydia Fearn
Partner

+44 (0)20 7432 3060
lydia.fearn@lcp.uk.com

Tim Box
Principal

+44 (0)1962 872739
tim.box@lcp.uk.com

About Lane Clark & Peacock LLP

We are a limited liability partnership registered in England and Wales with registered number OC301436. LCP is a registered trademark in the UK and in the EU. All partners are members of Lane Clark & Peacock LLP. A list of members' names is available for inspection at 95 Wigmore Street, London, W1U 1DQ, the firm's principal place of business and registered office.

Lane Clark & Peacock LLP is authorised and regulated by the Financial Conduct Authority and is licensed by the Institute and Faculty of Actuaries for a range of investment business activities.

© Lane Clark & Peacock LLP 2024

https://www.lcp.com/third-party-privacy-notice/emails-important-information/ contains important information about this communication from LCP, including limitations as to its use.