Taking the leap in delivering value

Jack Gray discusses the DWP's proposed value for money framework and the key role employers will play in driving VFM for members

Summary
- The DWP and regulators are seeking to drive consolidation and value for money in DC pensions with their new VFM framework.
- There is disagreement in the industry as to whether the proposals in the framework go far enough.
- Concerns about legacy schemes and data points have been raised, with some warning it may be overly complex.
- Employers seem set to play an important role in driving VFM for their workers.

As more people reitre with a solely DC workplace pension, the importance of providing members with value for money (VFM) continues to grow. The Department for Work and Pensions' (DWP) consultation on a VFM framework, which was developed in partnership with The Pensions Regulator (TPR) and Financial Conduct Authority, has proposed key metrics, standards and data disclosures for DC schemes, as well as proposals for the use of this data in comparisons and assessments of VFM. Its aim is to give providers, schemes and employers an extra nudge to take the leap in delivering better value for members.

It will provide a standardised understanding of value through metrics, allowing transparent comparisons between pension schemes and potentially driving competition.

In turn, the government and regulators expect this to increase consolidation in the marketplace, improve DC outcomes and increase employer engagement with pension provider selection. One of the key messages within the proposal is to deliver a more holistic VFM assessment, rather than focusing on cost alone, as

TPT Retirement Solutions DC director, Philip Smith, explains: "At the moment, the assessment process for a lot of employers is quite crude and there is a

bit of a race to the bottom on fees in the market.

"Judgements can be made on a matter of basis points, which may not necessarily be the best decision in the long term. A more holistic approach is to be welcomed."

The framework is expected to be enacted in two stages. Its initial focus will be on defaults in workplace and legacy pension schemes, before extending to self-select options, non-workplace pensions and DC pension in decumulation. "Retail products are out of scope as normally the client is more engaged," notes Vidett director of business development and client director, Kevin Clark.

Meeting expectations

The proposals for the framework have been broadly welcomed by the industry, with a seemingly universal agreement that VFM is an important measure in ensuring that those retiring with a DC pension get good outcomes in retirement. However, there has been some disagreements as to whether the proposals go far enough.

"Our view is that this is thorough enough," states Pensions Management Institute director of policy and external affairs, Tim Middleton. "It doesn't need to go into much more detail than it is. It's got quite a detailed framework. The disclosure procedures are very comprehensive, and we think that it goes far enough. We also agree with the idea that it doesn't make a lot of sense for it to go into some of the more specialist DC schemes."

Clark agrees, commenting that the proposals go far enough and the question now is how they can be implemented in a cost-effective manner, as trustees will then be able to quantify the outcomes of their good governance because they will become more measurable.

However, Standard Life head of workplace proposition, Neil Hugh, argues that the proposals need adjusting in respect of investment performance and costs and charges to make sure they are more meaningful and comparable. "We would also like to see more specifics around how measurement of service metrics will be standardised – currently, different providers measure the time taken over tasks in different ways," he adds.

Working through the details

While the proposed framework has broadly been welcomed, the devil will be in the detail, warns Smith. He notes that there are challenges in the consultation that the industry will have to deal with. One of the key issues raised is the large number of data points that schemes will have to consider: "There are potentially 3,000 data points that schemes might have to wrestle with, which is a lot," he says. "Working through all of that will take some time. Given the level of detail, I think it will be a challenge to get it through before the election."

Hugh echoes this concern, stating that the proposals currently generate too many data points due to the different age cohorts, defaults and employers, and warns that this will result in VFM being harder to analyse and compare across the industry.

"We need to think about how we engage employers in this process, because they are likely to be the people who use these VFM assessments"

"On quality of service, the proposals are aimed at a basic level of service and need to go much further by bringing in engagement activity and digital tools," he continues. "We would also like to see more specifics around how measurement of service metrics will be standardised – currently, different providers measure the time taken over tasks in different ways."

One of the notable absences from the DWP's consultation was integrating ESG and responsible investment practices into the VFM framework. While this is an initial consultation and changes could be made before the implementation of the framework, several industry figures noted that trustees have to abide by responsible investment requirements and it will be interesting to see how this is balanced with the requirements set out in the VFM consultation.

"There had been discussions relating to the defined benefit (DB) sector about pressure for DB schemes to invest in the UK economy in order to help it grow," says Middleton.

"I wonder if that principle may

filter into DC saving at some point. If it does, it is going to be interesting to see how that can be aligned with existing commitments regarding ESG, for example, as well as the more general common-law principle about trustees investing in assets that will best serve their members."

Hugh states that Standard Life would welcome the introduction of ESG and financial wellbeing metrics, as the relationship between responsible investing and good outcomes is becoming more obvious, as is people's ability to determine what they want to achieve with their pensions.

"A forward-looking element will focus on investment design encompassing ESG/Task Force on Climate-related Financial Disclosures," adds Clark.

"Communication services will need further enhancing to provide more access to information as well as access to retirement solutions."

Impact on trustees

One of the commonly occurring topics for discussion whenever a new consultation or policy is unveiled is the potential burden it will place on pension trustees. Trustees have seen swathes of new regulations over the past few years, and any new requirements usually add to their already heavy workload.

"This is something that *[trustees]* will do some initial work on to get the whole thing set up," notes Middleton. "They'll be working closely with their advisers and is one of those things that will be subject to periodic review."

He adds that the new framework calls into question whether the Chair's Statement is needed, if there is a formal commitment for a board to review VFM on a regular basis. If VFM is properly disclosed, and members understand what they are looking at, it will help improve public confidence in the DC sector, according to Middleton.

"If you think about the newer master trusts, a lot of this material will have been done, driven by commercial factors as much as anything else, when the master trusts were established," he continues. "So, there is probably not quite so much work that they have to do."

While the proposals may add some work to trustees' schedules, especially for smaller schemes, Hugh states that trustees and independent governance committees will be empowered to have more challenging conversations about VFM, which will ultimately lead to better outcomes.

Furthermore, if the data provided through VFM assessments identifies poor performers, enhances competition and assists advisers in achieving improved outcomes, trustees and employers will be able to provide bespoke solutions for each client and not herd to one preferred option, according to Clark.

The role of employers

Speaking to *Pensions Age* in last month's magazine, then-TPR CEO, Charles Counsell, expressed the regulator's hope that employers, especially larger ones, would look at the VFM framework and help drive value for their workers' pensions.

Smith argues that the main benefits for members are going to come via the employer.

"One of the things that seems to be missing from the consultation is the role of the employer," he says. "We need to think about how we engage employers in this process, because they are likely to be the people who use these VFM assessments by comparing providers and potentially changing providers if they feel their workplace pension is not providing VFM."

While there are cohorts of employers that spend a lot of time and effort managing their workplace pensions, and have layers of governance over and above the trustee board, there are also employers at the other end of the spectrum who are not interested or do not have the resources, Smith adds.

Hughes agrees on the importance of employers in driving VFM, noting that, in the first phase, the audience will be pension professionals and employers: "The extent to which schemes can demonstrate VFM against the framework will help employers decide on who runs their workplace scheme," he continues. "If their existing provider is not competitive, the employer will have better tools to assess them against and they could choose to move their scheme."

Written by Jack Gray