Summary
- The DWP, TPR and FCA continue to work towards creation of a new value for money (VFM) framework, based on real value for members and savers, rather than costs borne by them and by sponsoring employers.
- The existing value for members regulatory guidance is only partially effective. A new framework will focus on investment performance and quality of service as well as costs and charges. Schemes and vehicles offering poor VFM will be expected to consolidate into larger schemes or master trusts.
- Further work is needed to finalise framework details, particularly around areas including data requirements, evaluating assessment outcomes, investment strategies and whether consolidation will definitely deliver better VFM for members.
- A timetable for implementation is set for 2027, but this depends on the passage of new legislation.
- Whatever the final form of the framework, its most important result must be a focus on value for members and savers, not just on meeting new compliance requirements.

Defining 'value'

David Adams reports on the efforts of regulators and the industry to create a new framework to measure and report on value for money

Value in pension provision is about much more than the bottom line. Following a joint consultation, in July 2023 the Department for Work and Pensions (DWP), The Pensions Regulator (TPR) and the Financial Conduct Authority (FCA) published a joint response document outlining revised proposals for a new value for money (VFM) framework. At its heart is the need for employers, scheme trustees, the Independent Governance Committees (IGCs) and pension providers to focus not on short-term costs but on longer-term value.

Current value for members assessment rules mean DC scheme trustees must assess whether a scheme's costs and services provide good value for members, and publish this assessment in the annual Chair's Statement. Smaller schemes (sub £100 million) must complete and publish an enhanced version. But not all schemes or providers are in scope, or follow this guidance. In 2022, only about 24 per cent of all DC schemes were meeting TPR requirements, according to its own research.

The DWP, TPR and FCA propose a phased introduction of a new VFM framework, focusing first on default arrangements in workplace pensions, with work on more complex issues, including the decumulation phase, collective DC provision and non-workplace pensions, to follow.

The proposed framework will require trustees and IGCs to consider value through investment performance, service, and costs and charges and report assessment outcomes every year.

"It will provide a transparent, standardised means by which schemes can holistically assess these factors, evidence VFM outcomes and the actions they are taking to improve value provided to savers," says a TPR spokesperson. "This will help … the industry to focus upon value and ensure consolidation occurs where in the best interests of savers."

Assessment of investment performance will be based on gross performance by age cohort and years to retirement. Reporting periods of one, three and five years are proposed, plus 10 and/or 15 years if data is available. More controversially, a forward-looking metric is also proposed; as are quantifiable metrics for quality of service. Overall VFM must be compared against at least three other schemes, including two large schemes (over £10 billion). A red/amber/green (RAG) system will denote assessment outcomes, with red-rated schemes expected to consolidate if possible.

The introduction of a VFM framework for trust-based schemes will require primary legislation. The FCA could introduce new rules for contract-based schemes more quickly, but both regulators and government have said they want consistency in approaches to all DC schemes or vehicles. The FCA will consult on how the VFM framework

"Employers *[must]* continue to ensure value for money is delivered for members following consolidation"

will be used by contract-based schemes in 'spring 2024'. (A date had not been announced at the time of writing, but the consultation is widely expected in May or June.) Papers published by the government following the March 2024 Budget suggest it wants the new framework up and running in 2027.

A good start

The industry has given these revised proposals a cautious welcome.

"We welcome the overall ambition around data transparency, standardisation and a more objective process for evaluating value for money overall, not just cost," says Hymans Robertson head of DC trustee governance consulting, Claire Kapitan.

"I think the proposals are good, but the sense I'm getting from the industry is that more development is needed," says Pensions Policy Institute (PPI) head of policy research, Daniela Silcock. "There needs to be more clarity on quite a few things."

There are concerns over the proposed metrics for investment performance, including use of a forward metric. "If you're looking at a growth phase for a default option, *[investing in]* equities may drive performance, but what is the risk attached to that?" asks Zedra client director, Sam Burden.

"It looks like a lot of investment performance data to gather," says LCP principal, Tim Box. "I can see we might have a whole new cottage industry of VFM consultants."

There are concerns that the RAG scoring system will be too simple: Schemes will need to justify and contextualise their judgement, but headline verdicts could be misleading and damaging. There are also concerns about creating genuinely meaningful and consistent qualitative metrics for quality of service.

Some insights into the practical impact of these sorts of disclosure requirements can be gleaned from work that pensions law firm Sackers has been doing with prominent IGCs running contract-based schemes, coordinating an anonymised value for money initiative that has effectively created a VFM group study for those schemes.

Sackers partner, Jacqui Reid, who leads the project, says one insight is that when attempting to measure value qualitatively, "people answer questions in different ways … so how do you know you're comparing apples with apples?"

Another drawback of the proposed framework is the lack of focus (at present) on the decumulation phase. The joint consultation response document suggests that as the VFM framework evolves it will "complement work on decumulation by enabling pension savers to better understand the value of different services and products in the decumulation market".

Reservations have also been expressed about how use of the VFM framework will interact with the government's desire for pension schemes to invest in illiquid assets such as infrastructure. Certainly, larger schemes or vehicles will find it easier to make such investments.

"The proposed *[VFM]* framework will require trustees and IGCs to consider value through investment performance, service, and costs and charges and report assessment outcomes every year"

Aegon head of pensions, Kate Smith, highlights the diversity of available illiquid investments and the fact that they may not produce a return very quickly. "A one-year return is not an adequate timeframe to … *[determine]* good value," she says. "It needs to be at least five years."

In addition, while moving away from a narrow focus on costs should enable a greater degree of investment diversification and sophistication, some schemes may feel they should copy the strategies of those schemes or vehicles deemed to be offering greater value for money. "Will that be the right thing to do for members?" asks Mercer principal, Ken Anderson.

Unresolved issues

Anticipated consolidation within the DC market is supposed to help improve member and saver outcomes – but there will be a need to ensure that this actually is the case.

"We are pro consolidation when it's in members' best interests … *[but]* we're concerned that some value assessment measures are very burdensome on some schemes," says Pensions and Lifetime Savings Association (PLSA) head of DC, master trusts and lifetime savings, Alyshia Harrington-Clark. "We might see consolidation not because it's in the interests of the member, but because schemes are regulated out of the market."

TPR is already running a small pilot for a VFM framework with a small group of schemes. Sixteen per cent of sub-£100 million schemes participating in the pilot have concluded that they are not offering good value for money, so will wind up.

Kapitan stresses the need for employers to continue to ensure value for money is delivered for members following consolidation of a scheme into a larger master trust or another vehicle. "Smaller employers are less likely to monitor arrangements on an ongoing basis," she says. "There's a risk … that they don't hold the provider to account and demand that they're delivering value for staff."

Finally, there is the question of how long it will take to implement the new framework. New regulation for trust-based schemes will require new legislation, but we are now within months of a General Election. There is cross-party consensus on VFM, but we cannot be certain momentum will be maintained by whoever forms the next government.

Whenever it is implemented, TPR summarises its ambition for the new VFM framework to be "to ensure all trustees approach the assessment of value in a consistent way, so all savers can feel assured they are receiving value for money"; and for "consideration of saver value to be integrated into every decision trustees make".

"It's going to be a good step forward," says Burden. "It brings that public disclosure and transparency. It also focuses the minds of trustee boards and governance committees, so they're really thinking about value for money."

But that focus must be led above all by what real value means for members and savers, says Anderson. "If you've got metrics upon which a scheme is being assessed in the public domain … you are going to end up with some schemes focusing on those metrics, rather than thinking about what is most important for their members," he warns. Whatever else value means, it must be tied to that purpose.

Written by David Adams, a freelance journalist