Institute and Faculty of Actuaries

January 2024

# IFoA submission: Looking to the future: Greater member security and rebalancing risk

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

The Institute and Faculty of Actuaries (IFoA) is pleased to submit feedback on the DWP's Call for Evidence on "Greater member security and rebalancing risk".

Within the actuarial profession we have experts in technical detail, executives in small and large financial institutions, and practitioners working within the financial system itself. Our outlook is rooted in our Royal Charter (dating back to 1884) and in our long history of working with policymakers to effect change. We focus forwards on how we can help individuals and organisations solve financial and risk-related problems in the 21st Century.

If you have any questions on the response, please contact Caolan Ward (caolan.ward@actuaries.org.uk) in the first instance.


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The IFoA has considered the Call for Evidence and on this occasion we have concluded it is more appropriate to respond only at a high level. Therefore we have provided our general views on the proposed "Lifetime Provider" model in this letter, rather than addressing the individual questions in the Call for Evidence. We would be delighted to discuss this further with you.

As we summarise at the end of this letter, although we believe a lifetime provider model may be worthy of consideration at some point in future, it would also have potentially significant unintended consequences, and we do not believe in the short to medium term that it would provide better member outcomes than the Government's current policies; indeed it could undermine them. Hence we believe the concept of a lifetime provider model should be 'parked' for now, whilst current well-established initiatives (and newer ones, such as the default consolidator approach for small pots) continue to be implemented. Once this has been done, a further review of the DC market could take place to determine where the DC savings market can be further improved, for example, whether the remaining deferred "small pots" need a further radical solution to address them, and, whether further changes are needed to encourage efficiencies and consolidation in the DC provider market.

Looking at current priorities, our views are as follows:

***Pensions Dashboards*** – considerable enthusiasm and effort is already being invested by the Government and the pensions industry in bringing Pensions Dashboards to life. Whilst we have some concerns about the current timescales and will welcome further guidance on interim connection deadlines, the IFoA continues to be fully supportive of the aims of Pensions Dashboards. We firmly believe they will:

- significantly increase savers' engagement with their pension savings, leading to better communications, higher contributions and improved outcomes for members and providers
- help improve employer engagement. The IFoA believes it is crucial to retain the employer's link to their employees' pension savings, particularly when the employer's additional and matching contributions are so important for attaining adequate living standards in retirement and while auto-enrolment contributions in isolation are unlikely to be produce adequate retirement savings.
- help to drive consolidation, which we know is a priority for Government and will generally help to improve member outcomes.

Overall, we have strong concerns that a lifetime provider model would bring with it the risk of severing employers' links and engagement with their employees' pension savings. Cutting ties with an active member's employer is likely to reduce employer willingness to contribute above auto-enrolment minimum levels over time, thus reducing contributions and leading to a worsening of member outcomes. It will also remove the Employer from their current role in choosing providers – with many employers having in house resources able to contact robust and meaningful reviews to ensure they are using a suitable provider.

***Value for Money*** – this is another area where much progress has already been made and where the IFoA is fully supportive of the policy intent. The most recent aim is to gradually change the focus from cost to quality, to encourage members to seek a good holistic solution and again to improve outcomes. We believe there is a risk that a lifetime provider model could undermine efforts to ensure members get value for money, and indeed heavy marketing to individuals with a lifetime provider model could lead to 'mis-selling' problems and poorer outcomes, as member apathy sees members 'stuck' with their first provider whilst provider terms deteriorate or, conversely, as poor advice or aggressive marketing leads to members transferring between providers without improving outcomes. Of course, savers with a sufficient degree of engagement and access to good quality advice who do seek to consolidate their funds with their chosen provider "for life" can already do so in respect of any savings other than those from provided by a current Employer.

***Default small pots consolidator model with clearing house*** - The IFoA recognises the need to address deferred small pots to improve member outcomes and in our response to the Mansion House call for evidence on deferred small pots we supported the proposed introduction of a default consolidator model with a clearing house. We believe this, combined with Pensions Dashboards and a Value for Money framework has the potential to largely address the problem of deferred small pots from a member perspective. We accept that it would not immediately stop the flow of new small deferred pots, but over time we would expect the number of small pots to reduce significantly under these proposals. In our view therefore, this issue should be reviewed in a few years' time, once all these initiatives have been introduced and had time to bed down, to see whether more radical changes – such as a lifetime provider model is needed to address this.

***Auto-enrolment improvements*** – as noted above, whilst auto-enrolment has been a resounding success in terms of encouraging new pension savers to the market, it is now generally accepted that minimum auto-enrolment contributions are not yet at a level expected to provide savers with an adequate standard of living in retirement. Further pursuit of this aim, through further gradual improvements to auto-enrolment minimum contributions and widening of the eligibility criteria when circumstances permit, alongside further Value for Money improvements, would be beneficial for member outcomes. Any changes that might cause employers to cut back their contributions from those above minimum auto-enrolment levels, for example if the link is broken between employers and their employees' active pension savings, would be counter-productive.

***DC decumulation service requirement which could feature Collective defined contribution (CDC) –*** The Government will be aware from previous IFoA submissions that the IFoA is supportive of the introduction of CDC schemes, and supportive of the role they could play for decumulation solutions in particular within the suite of decumulation services. Whilst CDC needs a degree of scale to work well, and some overseas designs rely on a continuing flow of new members, it can undoubtedly work without a lifetime provider model. We therefore remain supportive and would resist linking the Government's policy on CDC to a lifetime provider policy intent.

The longer the time horizon of the scheme, the better CDC works, and for this reason whole-of-life CDC is easier to manage than in-decumulation CDC. In principle, whole-of-life CDC is a viable model for "lifetime provider" pension provision. An important merit of CDC is how much more is done for the member by the CDC scheme by default, without needing the member choices involved in DC.

However, the UK market is still a significant way away from this being ready to implement. The next step for CDC in the UK is to make available multi-employer CDC and allow time for whole-of-life multi-employer CDC schemes to come to market. Some employers may choose CDC as their auto-enrolment qualifying scheme.

As noted previously, decumulation CDC could work well even without a "lifetime provider" model, if it is one of the decumulation options offered to members at retirement.

Before CDC has developed much in the UK, it is too early to say what forms of CDC might work best.  Its merits could make it a good default, in time.  As noted in the consultation para 156, to require auto-enrolment to be into CDC would be a major change and something to be considered much later once CDC is well established.

**What problem needs to be solved?**

Whilst recognising the Government's desire for consolidation as a route to increasing "productive" investment in the UK economy, the IFoA does not believe the Government needs to stop the flow of new deferred small pots to achieve this, nor risk the success of auto-enrolment or the success of further established initiatives to improve member outcomes. A default consolidator model is a practical way of addressing small pots and we do not believe a lifetime provider model would bring sufficient advantages to justify it supplanting the good work in progress. If, in due course, a further solution is needed to stop the flow of new small pots, a lifetime provider model might be revisited, along with any other relevant solutions.

If the aim of a lifetime provider model is to give more members more "choice" it should only be done if it is very clear members want and value this choice, will be able to withstand aggressive marketing and will understand products sufficiently to make the right choice for them. Unfortunately, the UK experience to date is that this is seldom the case other than with high earners. We note that the vast majority of members in DC schemes remain in the "default" strategy provided, despite usually having extensive other choices available to them. The pensions miss-selling experience of the early 1990s (when many members of high quality DB schemes were enticed to opt out of their employer scheme, take a transfer and invest in personal pensions instead) is worth noting as a very good example of the potential unintended consequences of placing too much importance on choice when it comes to complex financial products.

In summary, the IFoA does not believe moving to a lifetime provider model addresses a current problem or that it should be the Government's immediate priority. This would risk undermining the current priorities that focus on:

- improving member outcomes across the board by improving the visibility of pension savings through Pensions Dashboards;
- increasing member and employer engagement with pension savings through Pensions Dashboards and by retaining an employer link with members' active pension saving;
- improving the quality of pension savings with an enhanced Value For Money framework;
- improving member and provider outcomes by consolidating deferred small pots using a default consolidator model
- introducing a requirement for DC schemes to provide decumulation options which could feature CDC; and
- improving outcomes for individuals, and especially those whose employers do not seek contribute above minimum levels, by gradually improving auto-enrolment contributions and widening eligibility.

Once these priorities have been addressed and changes have bedded down, we are supportive of a further review, to identify whether a lifetime provider model would enhance outcomes for members, for example by addressing further the small pots problem, or meeting member demands for more autonomy and choice in their DC provision.

The IFoA would be delighted to discuss this further with you. Please contact Caolan Ward (caolan.ward@actuaries.org.uk) if this would be of interest.