Institute and Faculty of Actuaries

7 July 2025

Briefing: Pension Schemes Bill Second Reading

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. Actuaries are big-picture thinkers who use mathematical and risk analysis, behavioural insight and business acumen to draw insight from complexity. Our rigorous approach and expertise help the organisations, communities and governments we work with to make better-informed decisions. In an increasingly uncertain world, it allows them to act in a way that makes sense of the present and plans for the future.

Key points

The Pension Schemes Bill is an **ambitious and significant step in facilitating change to the UK pensions system**. The IFoA is supportive of the Government's efforts to improve outcomes for pensions savers and stimulate growth in the economy. As experts in managing long-term risk and pension scheme management, actuaries will play a vital role in putting the Bill into the practice. Our members are pleased to provide their public interest perspective and analysis on the proposed legislation at Second Reading.

The IFoA believes that **the foremost purpose of pension schemes is - and will always be - to provide good outcomes for members in retirement**. With regards to provisions in the Bill on pension scheme investment, the needs of pension savers should be the driving factor in investment decisions. This means government must balance the need for sufficient investment in growth assets with the associated risks and costs. **We are concerned about the introduction of investment mandation powers, and potential interference of those powers – or their threatened use – with trustees' fiduciary duties.**

Consolidation can help access economies of scale and improve governance but does not come without risk. Compulsory investment in certain sectors may expose schemes and members to higher investment risk, costs, reduced liquidity, and lower diversification.

The Bill has many positive aspects in relation to defined benefit (DB) schemes, including rules that allow surplus funds in DB schemes to be used to help members, employers, and the economy. We look forward to working with the Government and the Pensions Regulator (TPR) to ensure that the requirements are clear, practical and scheme specific, whilst members' benefits are suitably protected and unintended consequences avoided. In addition, **putting DB Superfunds on a formal legislative footing will help provide trustees and sponsors with greater confidence in considering this option for their scheme**.

We are pleased also to see progress through the Bill on numerous other issues in defined contribution (DC) schemes. These include consolidating small DC pots, introducing DC decumulation requirements and requiring DC schemes to deliver value for money. **However, we urge consideration of whether additional powers need to be taken in the Bill to expedite decumulation-only collective DC, noting the guided retirement proposals in the Bill.**

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1. A focus on consolidation and pensions investment (Part 3, Chapter 4 of Pension Schemes Bill)

Key provisions in the Bill: The Pension Schemes Bill builds on the recent Pension Investment Review report, in which the government confirmed plans to double the number of 'megafunds', by requiring all multi-employer defined contribution (DC) pension schemes and Local Government Pension Scheme (LGPS) pools to operate at megafund level, managing at least £25bn in assets by 2030.

The Government expects these schemes to bring economies of scale and to be able to invest more in UK infrastructure and private markets. Similarly, guided retirement, the consolidation of small DC pots, and greater abilities for employers to access surplus are all intended – at least in part – to result in more money staying invested in pension schemes for longer, thereby supporting those investment objectives.

Points to consider:

- **The IFoA has concerns with the proposed design of the asset allocation powers in the Pension Schemes Bill.** The criteria for Master Trust authorisation were intended to produce a safe and reliable savings environment and we do not believe the concept of qualifying assets belongs there. This power introduces a commercial conflict between pension providers and trustees over asset allocation, weakening the fiduciary accountability of the trustees. Providers of the pension are likely to exert pressure to increase holdings of qualifying assets and maintain their authorised Master Trust status, whatever assets they may be forcing into allocations. It is also premature to give the Government a sweeping power it does not expect to make use of (we note the percentage of mandated assets cannot be increased after 2035 but that might encourage a government to "use it or lose it"). We would urge Parliamentarians to consider the implications of a future government – of any configuration – having a power to define qualifying assets as any project that the government of the day can meaningfully define, charging the capital costs to the auto-enrolled pension savings of the nation. Other mechanisms for the Government to achieve its objectives of UK investment would be preferable, in our view, to this open-ended power.

- **Mandating pension investment into specific assets undermines trustees' fiduciary duty to act in the best financial interests of members**, unless legislation removes or changes fiduciary duty for that part of the portfolio where the mandating applies. Should mandating schemes to invest in accordance with Government direction it needs to be made clear what the respective responsibility of Government and trustees are.

- **Mandating pension investment into specific assets would create some additional considerations**. Trustees are legally obligated to prioritise financial returns and manage risk prudently. Investment decisions should be based on scheme-specific needs. Compulsory investment in certain sectors (such as illiquid or unlisted UK assets) may expose schemes and members to higher investment risk, costs, reduced liquidity and lower diversification. This is especially problematic for smaller schemes that may lack the governance capacity or in-house expertise to manage complex or illiquid assets effectively. Mandating investments may also create excess capital supply which could lead to lower returns as schemes compete over the same investment opportunities.

- We also note that **there is no universally agreed definition of what investments contribute to "UK growth".** This creates uncertainty for pension schemes when considering asset allocations that align with the Government goal to boost domestic investment. Without a standard definition, trustees may find it difficult to measure or justify how much of a portfolio is supporting the UK economy.

- We understand the Government's desire to increase allocations of pension scheme asset to UK investments. However, we believe that **investment decisions** (particularly in relation to DC default investment strategies) **should, as currently intended, be focussed on achieving the best outcome for**

members. The investment aspects of the VfM framework should focus on longer-term net of all fees/costs returns.

- While we agree that consolidation *can* achieve better outcomes for members, by accessing economies of scale and creating opportunities for better governance and more sophisticated investment strategies, there is **no clear point where scale in of itself is likely to deliver better outcomes** for members. **Size is therefore a somewhat unreliable measure for quality**, when compared to measuring and enforcing good governance standards and investment management.

- **The risks and potential unintended consequences of introducing a minimum asset size include a lack of real choice for members, stifling of innovation, and an increase in systemic risk and herding behaviours** (especially if these providers are also subject to league table-style backward-looking benchmark comparisons as part of the VfM framework). Innovative propositions could also be closed even when functioning well if they fail over time to reach the required scale.

2. The concept of 'guided retirement' (Part 2, Chapter 5)

Key provisions in the Bill: The Pension Schemes Bill introduces 'guided retirement' provisions, requiring defined contribution (DC) pension schemes to offer clear, default retirement income options to members nearing retirement. This aims to simplify retirement choices, particularly for those lacking financial advice, by providing curated selections or a single default solution.

Points to consider:

- As part of the IFoA's 2021 Great Risk Transfer campaign, noting the transfer of financial risk from institutions to individuals, the IFoA recommended that the Government introduce default decumulation pathways for UK pension savers. Default decumulation pathways (referred to in the Bill as 'guided retirement') are an option for all pension savers, and act as a safety net for those who cannot or will not engage with the decumulation process when entering retirement and may need a simpler solution. It is very positive to see the inclusion of 'guided retirement' provisions within the Pension Schemes Bill.

- Since April 2015 individuals have had greater flexibility in how they can access their pension benefits. For example retirees are no longer required to take an annuity and can now access their benefits as cash or transfer them to a drawdown arrangement. Collectively, this group of changes became known as 'pension freedoms'. This change offers individuals much more choice and flexibility. The jury is still out as to whether the reforms were a success, but IFoA research on pension freedoms over the past decade demonstrates worrying trends in terms of UK pension savers' ability to plan for and drawdown on their pension.

- Our most recent 2025 study showed that although more people now perceive the changes as beneficial than at the time of their introduction, many people retire without either taking guidance or seeking advice. Furthermore, **only 1 in 5 access Government guidance and almost 1 in 4 people worry that they will make the wrong decision and run out of money in retirement**. There is also evidence to show that many people have only a limited understanding of the factors that impinge on retirement savings decisions.

- 'The Concerns of Gen Z', a report authored by the Pensions Policy Institute and sponsored by the IFoA, identified challenges facing Gen Z when they are trying to build their retirement savings. It also highlighted their views on Gen Z's attitudes and beliefs about pensions. Of those surveyed, **46% believe the state pension will not exist by the time they reach retirement**. A potential increase in Gen Z's state pension age, currently 68 years of age, could lead to delays in retirement. **Many in Gen Z already expect that they will delay full retirement; 47% say they plan to move to part-time work rather than stop working**

entirely once they reach retirement age. In contrast, 76% of current retirees stopped working completely at retirement.

- Decumulation only collective defined contribution (D-CDC) schemes may be another option that the Government could explore when simplifying retirement choices for UK pension savers. D-CDC schemes are designed specifically for ordinary DC savers to buy with their savings at retirement, to purchase an income for life which is expected to be higher than from an insured annuity. The Pension Schemes Bill requires pension schemes to 'offer retirement products so people have a pension and not just a savings pot', and DC trustees will need to offer their members 'a retirement income solution or range of solutions, including default investment options'. The IFoA believe D-CDC could be a suitable option for many savers and we encourage the Minister to explore this option throughout the passage of the Bill.

- **If the Government needs to take a power in primary legislation to make later amendments to other legislation to facilitate D-CDC, it would be opportune to so as part of the Bill; otherwise, there is a risk that its later facilitation is delayed waiting for a further suitable bill.**

3. Options for defined benefit (DB) schemes (Part 1)

Key provisions in the Bill: Two of the main proposals for defined benefit (DB) schemes in the Bill relate to establishing a legislative framework for DB 'Superfunds' and to modify DB 'surplus release' rules. This will formalise the regulation of Superfunds, which are designed to consolidate and manage DB schemes, allowing sponsors to settle their exposure whilst potentially improving long-term security for members.

The surplus release changes will give trustees of well-funded DB schemes the ability to remove any restrictions on making surplus payments to the scheme sponsor, under specific conditions, potentially unlocking billions of pounds for reinvestment in the UK economy and for the benefit of members.

Points to consider:

- The IFoA believe that there are several challenges and opportunities currently for DB schemes. For schemes closed to new entrants, most (but by no means all) DB schemes have become better funded, and nearly all are becoming more mature with shorter time horizons. Many are now reassessing their journey plans, with an increasing number looking to secure their benefits in full with an insurer.

- Some schemes would like to be able to run on and continue to take modest levels of risk and are looking for the regulatory framework in which they operate to be supportive. Small schemes have fewer options, whether in terms of investment, settlement, or governance and there are still some stressed schemes and sponsors with material deficits to address.

- For open schemes, most currently have a greater proportion of assets invested in higher growth asset classes. They would like a regulatory framework which does not create disincentives or place hurdles in the way of continuing to invest in this manner, which aims to balance security and ongoing affordability.

- Proposals on a formal regulatory framework for DB Superfunds, as opposed to the Pension Regulator's informal 'interim' regime, should provide clarity on the above and is a welcome development within the Bill.

- There are many positive elements in the Bill for DB schemes including provisions to facilitate the use of surplus funds to benefit employers, members, and the economy. This includes a confirmation that member security is important and that trustees are best placed to make decisions on the use of any surplus. The devil will be in the detail, and we look forward to working with government and the Pensions Regulator to ensure that the requirements are clear, practical and scheme-specific, but avoid unintended consequences.

4. Small pots (Part 2, Chapter 2)

Key provisions in the Bill: The Bill includes proposals for automatically consolidating small DC pension pots into larger, better-value schemes. This aims to address the issue of people building up multiple small pots as they change jobs, making it easier to manage and track retirement savings. Specifically, the Bill outlines a plan to consolidate "dormant" deferred small pots (those with no contributions for at least 12 months and where the member has not made an active investment decision) valued at £1,000 or less, moving them to "automatic consolidator" schemes, likely large Master Trusts.

Points to consider:

- The IFoA recognises the need to address deferred small pots to improve member outcomes and in previous responses on this issue we supported the proposed introduction of a default consolidator model like the one proposed in the Pension Schemes Bill.

- We believe that proposals on small pots like those contained in the Bill, 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.

5. Value for Money (Part 2, Chapter 1)

Key provisions in the Bill: The Pension Schemes Bill introduces a "value for money" framework to ensure Defined Contribution (DC) pension schemes deliver good outcomes for savers. This involves requiring schemes to publicly disclose data, assess performance against benchmarks, and take action if they fall short. The framework aims to drive improvements in investment performance, charges, and customer service.

Points to consider

- Whether a scheme is delivering value for money ultimately depends on member outcomes at retirement. All schemes should seek to maximise member outcomes at retirement, and this will not be achieved by minimising cost alone. There must be a step change away from the focus on low cost to net investment performance. For example, it is likely that investment in illiquid assets will improve member outcomes at retirement, but this cannot be achieved in a low-cost environment.

- While lower investment costs should result in members building up greater retirement savings, this has been at the expense of other important areas, such as the quality of member administration, communications and more innovative/complex investment strategies (which usually come with higher costs).The aim of the VfM requirements aim to bring these wider factors into play when trustees/providers assess the performance of their schemes.

- A long-term and consistent approach must be adopted when promoting metric data, particularly in relation to net fund performance. In Australia, the *YourSuper* comparison tool in Australia shows performance over three, five and 10-year periods. Short-term performance can be misleading and should not be published. Where schemes make changes to their investment strategies over time, performance should be chainlinked to retain sufficient historic data. A consistent comparison date, i.e. 31 December should be adopted. Finally, it should be made clear past performance is not a guide to future performance.

- There is a risk that publicising metric data could result in schemes "chasing historic returns". This has, to some extent, already occurred in the past few years across the Master Trust market where those with heavy equity market allocations have benefitted from the concentrated returns seen from the mega-cap US tech stocks. This has resulted in some providers moving away from more multi-asset growth portfolios to higher equity allocations to minimise the risk of lagging other providers. It remains to be seen which approach will ultimately deliver the best member outcomes at retirement but certainly raises the potential risk of herding and increases trustees' regret aversion which could in turn stifle innovation in investment design.

- The choice of "relevant benchmarks" and "comparator schemes/arrangements" is crucial to ensure that schemes that do not provide good value are required to conclude "intermediate" or "not delivering ratings". Prescribed benchmarks and prescribed comparator schemes/arrangements would ensure a consistent approach.

- There are also risks with implementing VfM metrics if they result in cliff-edges ratings, where two similar performing schemes can end up in different sides of the line. For example, if small differences result in ratings move a scheme from 'fully delivering' to 'intermediate' this could have significant (and disproportionate) commercial impacts. We have concerns that rather than the VfM framework encouraging the raising of standards it drives herding and becomes a constraint to innovation.

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