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Dear Small Pots Policy Team

SPP Response To Ending The Proliferation Of Deferred Small Pension Pots

We welcome the opportunity to respond to this consultation.

Executive Summary

This positive response reflects our feedback to the previous call for evidence. We believe the industry is aligned in viewing small pots as a challenge that needs to be overcome; the issue is the multiple options for achieving this, as all come with positives and negatives. As a body representing a diverse cross section of the pensions industry, we recognise this and welcome the positioning presented as an outcome from previous consultation – i.e. a proposition to take forward but to work collaboratively with the industry to ensure any solution is practical.

We believe that refunds for very small pots should be considered. Whilst refunds may appear contrary to the principle of automatic enrolment, we feel that a pot of £100 is unlikely to make a substantial difference to an individual's retirement income and such sums may assist an individual in managing the present. For note, communications on this matter will need to be carefully considered to avoid member confusion.

We would support clarity from the government around transferring small pots that have existing barriers to consolidation where transferring could detriment a member, such as guarantees or protections (i.e. GMPs, RSTs, protected tax free cash or protected retirement ages). We note that the smallest pots may not be impacted, but the chance of impact will grow as the pot size increases. The industry will require greater clarity on how this will operate in practice, where members may lose such guarantees or protections as a result of transferring their benefits away.

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We note that there is no guarantee that multiple schemes will put themselves forward as consolidators, as this business stream is not necessarily profitable. To attract the desired multiple consolidators, the process needs to be attractive to would-be providers. This includes efficient processes for authorisation (e.g., aligned with what is in place), identifying and transferring pots, and looking to keep pots as large as possible. To this end, refunds would help (e.g., pots consolidated between £100 and £1,000), as would consolidating funds where an individual already has a pot.

Finally, the SPP would like to note that consolidation will not necessarily solve the root cause of the issue around a lack of member engagement with their pension savings. Pensions Dashboards may help to stimulate engagement and make it easier for members to track their savings, but a disengaged scheme member is likely to remain disengaged in the consolidation process and after, until they start to reach their retirement age.

Detailed Response

Q1: Do you agree with this proposal or do you believe a central registry would be more effective approach to support the consolidation of deferred small pots, if so how would you design a central registry?

The SPP would like to note that central registry or clearing house mechanisms would not be required under 'pot follows member' or 'single consolidator' approaches to solving the issue of small pots (albeit it might still be useful under 'pot follows member').

Both proposals will require significant time and cost to build, develop and operate, however, we agree it will be necessary to operate a central platform under a multiple consolidator approach with the two proposed options.

We acknowledge that the most effective and cost-effective approach could (as is suggested) be to use the pensions dashboards framework as a central registry point in the long-term. However, we are not convinced the current initial framework and infrastructure would be sufficient in terms of holding the relevant data to do this effectively, thus, further developments would be required to use the dashboards framework for this purpose. If the timescales are unfavourable, then we would be supportive of a central clearing house, and perhaps they can also act as an independent support function for administrators, providers and members, where there are any issues with data or transfer instructions, which is not uncommon. This will also potentially support the process for members not making active decisions regarding a consolidator scheme, which is covered in our response to Question 2.

We also propose an alternative simplified solution which will remove the need for a central clearing house or central registry under a multi-consolidator model, and this is discussed within our response to Question 2.

Q2. Which, of the options we have set out, do you think is the best approach to allocate a member a default consolidator in cases where a member does not make an active decision? Are there alternatives?

We have concerns that Option A will likely result in members having multiple small pots with multiple providers (one of the existing issues around small pots) and will cause some confusion for members attempting to engage with their pensions, particularly in light of the volume of paperwork they will receive from each provider. Therefore, of the two options, Option B would be preferred, primarily due to member experience but also efficiency from a provider perspective.

We are supportive of Option B as a default for members who have a small pot with an existing consolidator. This will simplify the journey and likely provide a better outcome and experience for members. It will also minimise administration for ceding schemes and better support economies of scale for the consolidators, noting that very small pots are costly to run.

In terms of members who do not hold a deferred pot with an existing consolidator, some further consideration needs to be given to the approach for these members who do not make an active decision. We would not be supportive of members' small pots being allocated to multiple providers in light of our concerns noted above around member experience, as well as the administrative burden to process, dampening of economies of scale and costs to run.

One option for consideration would be for the government to nominate a provider on an annual basis to accept these pots based on overall value for money (aligned to the new framework). Alternatively, the clearing house could allocate and instruct where monies should be received, based on pots being transferred to the various consolidators evenly, in terms of volume, to manage concerns around competition and support all consolidators in building relevant economies of scale. This will further support the government's future proposals around accessing illiquid assets and moving to CDC, all requiring scale for success. A carousel approach could also work based on whoever is within the framework at a given time.

Some members feel there is an argument that these processes are still costly and complex to administer and will be complex for members to understand and follow. Some SPP members feel a simplified approach would be to implement a process which enables the existing scheme's pension provider or trustees to make an informed choice for their scheme(s) to partner with one of the default consolidators. This will allow schemes to select a consolidating scheme which will likely suit their membership needs and better ensure efficient and effective transfer processes and communications. It will also protect members from pension scams. This approach would also allow schemes to communicate and inform members upfront about what will happen to any small pot they hold. It would also remove the need of a clearing house or central registry to be implemented, as discussed under Question 1.

Across all approaches, there is some support to allow members to opt-out of consolidation, and in light of low member engagement, we would not expect this to be a significant number, however giving members the option should help mitigate any complaints. We note that we do not allow members to choose their scheme or provider in respect of their future pension savings under auto-enrolment rules. There is some degree of consideration as to why the industry would subsequently allow members to choose their consolidator scheme, if we know the receiving scheme is suitable and meets various industry standards, however, we accept it could help mitigate harm.

Q3. Do you agree that there is a need for an authorisation regime for a scheme to act as a consolidator? If so, what essential conditions do you think should form part of the authorisation criteria?

SPP members feel strongly that an authorisation regime is needed for a scheme to act as a consolidator, to protect members and industry reputation. SPP members feel that the Master Trust Authorisation approach is robust and provides sufficient protection for the consideration of member outcomes.

We would suggest that additional requirements should be considered in terms of liquidity to protect members and industry reputation.

We feel it is important for consolidator schemes to be able to demonstrate high quality deferred member journeys as well as prove they have effective engagement channels with this group of members. Members with special characteristics such as vulnerability should also be considered.

FCA-regulated firms offering consolidator schemes will be subject to the FCA's Consumer Duty regulations. These firms are required to carry out and evidence a high standard of care for all their members and members can expect to see continuous improvements to products and services as a result. The requirements mean ongoing evidence-based testing against good member outcomes in terms of products and member communications, as well as value for money (which we appreciate will be supported by the proposed new value-for-money framework). These firms are also expected to demonstrate formal internal governance processes focused on evidence-based assessments to achieve good member outcomes and avoid member harm, which should all be challenged by Consumer Duty Champions, likely independent professionals. Thus, we wonder if there is better protection for members for these schemes to be regulated by the FCA, or whether some consideration is given to the requirements for those non-FCA regulated firms to adhere to similar high standards.

Q4. Do you agree with setting the initial maximum limit for consolidation at £1,000, with a regular statutory review?

The question as to what the initial maximum limit for consolidation should be is a tricky one, with different views within SPP evident. This is likely to reflect the different roles of constituent members, and the comment in the consultation response that *the maximum pot limit suitable for automated consolidation may vary depending on the overall consolidation solution chosen* is insightful. Of the options initially presented, we believe the lowest option is the best one, and as per our initial consultation response, a cohort of our members believes that £1,000 is too high (noting the DWP has stated that the average value of a pot smaller than £1,000 is approximately £350), and therefore we would better support a value of c£500 as a starting point, with this being statutory reviewed periodically. It may allow the industry to embed the new model effectively before it increases the threshold and volume of members impacted. Therefore, if the desire is to consolidate a majority of small pots, such an approach seems appropriate. However, now we are commenting on the basis that a multiple-consolidator model is to be used, we accept it is challenging to initiate a low starting point with the acknowledgement that amounts lower than this will unlikely be attractive for consolidator schemes to participate, especially under a multiple-consolidator model. However, in light of the data and statistics provided around 'small pots', it is arguable that £1,000 may be too high to meet this definition. Also, as is noted, this is just a starting point. Over time, if this exercise is successful, the average size of pots will increase (potentially significantly as the DC market matures), and therefore larger pots will be bought into scope with the suggested reviews of the limit.

As per our response to the initial consultation, The SPP, alongside other respondents, favours and would ask the government to reconsider its stance on offering refunds for the smallest pots. This will help manage costs and make the solution more attractive for consolidating schemes. In reality, even if a member had 10 very small pots of up to £100 each at retirement, £1,000 is not going to have a material impact on a member's overall retirement income, and we still feel this should be considered as part of the solution to solving the issue of small pots in the UK.

Q5. Do you agree with this proposal not to mandate schemes to undertake same scheme consolidation at this current time?

The SPP is supportive of this approach at this time for the reasons set out in our initial response, primarily due to complexity and existing legislative and operational barriers, which all need to be considered for this to work effectively.

Q6. As a whole, do you agree with the framework set out above for a default consolidator approach? Are there any areas that you think have not been considered, that need to form part of this framework?

Overall, we are supportive of this approach, and we feel the pensions dashboards framework sits as a key part of the solution to member exchange, albeit the timeframes for the developments that will be needed to the dashboards infrastructure to enable this may not be achievable. In light of this, we think there is merit in allowing existing schemes to choose their consolidator to simplify this process and likely support member engagement and experience and protect around scams.

We would re-iterate that success will require some legislative direction and a marketing campaign to help mitigate concerns around pension scams.

Some thought needs to be given to differentiate between some well-known existing (or future) ‘scheme consolidators’ who have not received the relevant authorisation to be a formal consolidator under the new proposals to ensure members understand the difference and their options as well as the potential risks for choosing a ‘non-authorised’ consolidator.

Further consideration and clarity is required for members with protected benefits or guarantees that currently act as a barrier to consolidation. Whilst we appreciate its unlikely to impact most members with small pots, we have concerns that some will be impacted, and this figure will increase as the size of the pot threshold increases. The industry will need clear understanding and direction for how to manage these benefits in order to avoid member detriment, harm and delays in the process.

FCA-regulated schemes will also need a change to existing legislation which currently acts as a barrier to consolidation, to allow providers to transfer members’ monies without their consent.

Q7. Do you have any comments on the positive or negative impacts of a default consolidator approach on any protected groups, and how any negative effects could be mitigated?

As per our initial response, given that these solutions require (ideally) a degree of understanding, any groups that find it difficult to engage with communications and make decisions would be more impacted.

Small pots are also probably more likely to affect those on lower incomes and those who take periods of leave from employment (similar to the pensions gap and the auto-enrolment qualifying earnings threshold).

Therefore, written communications should be well-tested and relevant signposts for how to get more help via different channels should be clearly stated and available.

As mentioned in our response to Question 6, consideration for any existing barriers for consolidation need to be addressed. This will include legislation (including FCA rules for transferring members' pots away without member consent) or benefits that have guarantees or protections.

Response ends.

Yours sincerely,

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Defined Contribution Committee, SPP

Fred Emden
Chief Executive, SPP

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