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Response to the consultation on the lifetime provider model

Laverock Financial Consultancy welcomes the opportunity to respond to the initial consultation on the lifetime provider model.

At this stage I have not come to a clear conclusion on the benefits of retaining the existing model or moving to a lifetime provider model. In principle the lifetime model appears an attractive one if we were starting a new pensions system from scratch, it may even be better than the one in operation now. However, it is not clear if the considerable cost of transition would be worth it in terms of better financial outcomes for the UK pension saver.

Ultimately I believe that the key criteria on which the proposal should be judged is "Would this lead to better long-term outcomes for members which outweigh the short-term costs of transition?"

This response is based upon finding the right questions to ask in order to answer that question.

I have also considered the specifics of how best to deliver a lifetime provider model in terms of process and technology, should it progress.

1. What are the key considerations to take into account before deciding the process to implement a lifetime provider model and what elements would need to be in place?

Cost v benefits

It will be necessary to understand the costs vs benefits of any move to the lifetime model. In particular in terms of costs:

- The cost of the industry transitioning to the new model, which is likely to be considerable.
- The cost of maintaining the services required for the new model.
- Any indirect costs, for example a potential increase in price due to lack of bulk discounts.

In terms of benefits:

- Will the move lead to better outcomes for members? This must be the key aspect.
- What cost savings can the industry make over time by moving to this model?
- What indirect benefits may there be?

Other options

It should also be considered if these same benefits could be achieved in a different way, for example using a central admin service without moving to a full lifetime provider model or widening the scope of the small pots proposals to include medium-size pots.

Moving to a lifetime provider model will be a large and disruptive project: it is important that cheaper and less disruptive options are also considered.

Regulation

Regulations will need to be laid to parliament, probably after any upcoming general election. We know from previous experience that such regulation takes a long time to pass.

There will need to be changes to the automatic enrolment regulations as they currently are based on employer duties. Moving to a lifetime provider model will mean that duties will not always now apply to the employer.

There will need to be a regulatory framework to approve pensions schemes as appropriate for hosting a lifetime pot. This will need to have stipulated rules on areas such as charges, investments, etc.

Governance / technology

Working groups should be created to look at specific issues, made of representatives from government and industry. For example, a group should specifically look at the technological assumptions and costs.

A governance body and program should be created to facilitate the proposed creation of a clearing house and other technical services such as data standards. This should learn the lessons of the Pensions Dashboard program where possible, in particular around procurement and industry involvement in the solution design. I believe that in the case of Pensions Dashboard, too much technical IT decision-making was internal to the DWP, which led to delays in the delivery.

2. What are the alternative viable mass market vehicles, including CDC, that can provide security for members while spreading risk, and address the transition into a pension income?

No comment, this response is limited to the specifics of the Lifetime Provider model.

3. What are the other considerations and building blocks that need to be in place before moving to a single lifetime provider, including any transitional arrangements?

Clearing house

A central service in the form of a clearing house will be vital in order to efficiently run a model such as single lifetime provider. This will allow employers to easily assign pensions payments to the correct pensions scheme. It should also allow for better compliance with existing rules and new regulations as they can be applied in the system itself.

For example, the clearing house can check if a pension is permissible under the regulations so that an employer does not have to concern itself with whether a pension is suitable. It could also check whether the right contributions have been deducted.

A clearing house should also provide efficiencies, and if implemented correctly, reduce the cost overall of running pensions in the UK.

Build on Pensions Dashboards

The industry and government are already combining to build a pensions dashboards service with find and value functionality. This also provides a baseline of data standards for pensions across the industry. There is the potential to re-use some of the functionality of dashboards, for example, by finding the correct pot. But we could also reuse parts of the infrastructure, as every provider will already be connected to the central service.

In addition, the data standards set out in the pensions dashboard are a good base upon which to build further data standards for any lifetime provider services. Additional data items will have to be added but many will be the same, for example name, address and policy number.

Small pots consolidation

Whilst a single lifetime provider model can help reduce the creation of new small pots, it will not resolve the immediate issue of the millions of small deferred pots that already exist. This is already causing the issues highlighted in part one of the consultation. I therefore suggest that it will be important to deliver the small pots solution of default consolidation first.

Delivering default consolidation first also has the benefit of having a clearing house structure already in place on which to build for the needs of the lifetime provider model.

A strong market of potential providers

Whatever model is chosen for the types of pension allowed to be used there should be a strong market for all customers to choose from. For this to happen there will need to be a good range of providers to choose from, with products suitable for the mass market, including those customers not really targeted for individual personal pensions at the moment.

The regulator should also consider what sort of criteria people will use to choose a pension and to make sure that providers are showing the correct information on comparison engines and other tools people are likely to use to choose a pension. For example, ensuring that charges are shown in the same way and that customers can easily understand the different risks when considering investment options rather than just short term performance.

Fully automated and digital from outset

In order to achieve the benefits in terms of efficiency that are expected any process and system design must be automated from the outset. If employers, members or pensions schemes are required to use paper processes it will be a major barrier to take up and create additional friction and cost in the system.

For example, when a new member of staff joins a company the employer should be able to send the contributions to that employee’s lifetime provider without having to complete any paperwork. And the pot for life should be able to accept the monies and apply them to the pension without needing additional information - it should all be passed electronically by the clearing house.

The place of Advice?

In considering a lifetime provider model there will have to be an understanding of how the move will affect advice. At the moment the vast majority of workplace pensions are non-advised. However, with members now expected to make an active choice, and with the potential that existing pots could be used, this will likely change.   Some people may choose to use the services of an adviser and some may choose to use a pension that already receives advice as their pot of choice.

In particular, consideration will have to be given to how any ongoing charges for advice may impact on the overall charges and whether these should they be included in any charge cap.

It will also be important to understand what impact the FCA consultation on the advice boundary may have. For instance, would an online comparison tool be considered Targeted Support or Simplified Advice?

Money laundering

Checks currently take place in order to prevent pensions from being used for money laundering. These are based upon the existing model and will have to be changed in order to facilitate the lifetime provider model.

The risk is that these processes could run counter to the desire to make the process automated and reduce the impact on employers.   For example, a pensions firm will need to check that the employer is a legitimate company, and this could lead to a request for evidence from the employer, leading to delays in processing a pension and placing burden on the employer.

I would suggest that wherever possible checks like this should be covered by the clearing house, or otherwise automated.

Minimising impact on employers

As a point of principle the change to a lifetime provider model should minimise the administrative work for employers.   It should be as easy to send pensions contributions to an employee's pension pot as it is to send their pay to their chosen bank account.

To facilitate this I would suggest that a model similar to the account number and branch code system in banking be considered in pensions, so that it is easy for the new employee to inform their employer of which pensions pot to send the payments to.

I would also suggest that obligations for employers be limited to ensuring that they deduct the right contributions and pay them to the clearing system. It should not be the responsibility of the employer to check the suitability of a pension scheme that the customer has chosen. That should be the role of the regulator and the central clearing system.

Engaging with payroll

Automatic enrolment showed that payroll organisations are a key factor in facilitating an efficient workplace pensions system.   It is important therefore to engage with payroll organistions from the outset, especially when it comes to considering how any clearing house model may work.

4. What are the advantages and disadvantages of moving to a member-led lifetime provider model prior to considering introducing a default lifetime provider model?

It will allow for a trial

By having a period where a smaller number of individuals use a lifetime pot, there is the potential to trial certain processes. It will also allow regulators to see how the market and members will behave before a full scale move to a new model.

It could allow for realising benefits earlier.

If starting with a member-led model allows for the delivery of certain services and systems earlier it could also allow for the realisation of some benefits earlier.

Staging may have additional costs

Having a multi-phase delivery may mean increased overall costs and potentially lead to a delay in the final desired solution.

Will it create extra work for employers?

A concern with a member-led model is that it may prove to be a "worse of both worlds" situation for employers. They will still have to undertake all the activities they do now for running employer-chosen schemes, with the additional burden of facilitating member choice. This could be exacerbated if the member-choice service was not fully automated in the early stages.

Will it only benefit the already engaged?

There is a danger that an interim member-led stage will only benefit certain parts of the workforce. For commercial reasons, pensions firms are likely to target the highest paid staff.

5. What is the right timing and sequencing of these potential changes? Which part would best be implemented first and why, or should any be implemented concurrently?

It is vital that Pensions Dashboards and the existing proposals for small pots be delivered as per the current timetable. This will allow any lifetime provider model to build on these.

Given the time needed to deliver the regulatory changes and create a technical infrastructure for lifetime provider, it is also important that Pensions Dashboards and small pots are not delayed to wait for lifetime provider.

Technical and policy decisions can be made for lifetime provider over the next year or two and then delivery started once Pensions Dashboards and small pots are live.

Realistically this would probably lead to a schedule along these lines:

Pensions Dashboard – delivery 2024-26
Small pots – solution design 2024-25, delivery 2026-27
Lifetime provider – policy decision 2024-25, solution design 2025-27, delivery 2027-28

This is based upon the experience of similar projects such as Pensions Dashboards and Automatic Enrolment.

Laverock Financial Consultancy Ltd / Ian Macintyre

Laverock FC is a business run by Ian Macintyre, an independent consultant specialising in pensions regulations and technology. In particular bridging the gap between policy conversations and the reality of implementation on the technology used by the pensions industry. He also provides support to firms that need to implement the proposed changes.

Ian has been a member of working groups on Pensions Dashboards, Small Pots and Lifetime Provider Model.