

## Mansion House 2024: Reforms to the DC pension market

### What you need to know

- On 14 November 2024 in her first Mansion House speech, the Chancellor set out plans for consolidation of DC pensions. Concurrently, the government's Pension Investment Review interim report was published, alongside a new DC focused consultation 'Pensions Investment Review: Unlocking the UK pensions market for growth'.
- Overall, the government is of the opinion that larger pension schemes have the power to increase saver returns, and boost investment in UK 'productive assets'. The interim report therefore sets out the government's 'long-term vision for a defined contribution pension system with fewer, larger and less fragmented schemes'.
- The consultation includes the following proposals:
  - For multi-employer schemes including Master Trusts, Group Personal Pension and contract-based arrangements, there should be a minimum size of perhaps £25bn-£50bn and maximum number of default funds per provider, which would apply from no earlier than 2030.
  - Increased powers to be granted for contract-based pension providers to consolidate their arrangements, without the existing need to seek member consent.
  - A greater focus on value rather than cost, to be taken by stakeholders including employers, consultants and advisors.
  - Greater investment in UK productive asset classes such as infrastructure and private equity, with the inspiration being arrangements in Australia and Canada where this is commonplace.
- The consultation closes on 16 January 2025, with a new Pensions Bill still expected in the spring covering material elements of the frameworks raised at Mansion House.
- Interestingly, the focus was on multi-employer DC arrangements rather than single employer trust-based schemes. The implication is that the forthcoming Value for Money requirements, previously consulted on, are seen by government to adequately prompt these schemes to provide good value or consolidate.

### Actions you can take

- **Employers:** The consultation suggests employers take a more active and ongoing role in ensuring their pension arrangement delivers value to their employees. Whether or not it becomes a legal duty, we recommend that employers review and assess their current and legacy pension arrangements.
- **Trustees of single employer trust-based schemes:** With the increasing focus on value and consolidation, trustees should revisit their latest Value for Members assessment and explore actions to improve value in any underperforming areas ahead of the new requirements, or commence consolidation if good value is not expected.
- **Governance committees:** Those overseeing an employer's pension arrangements such as a master trust or Group Personal Pension should consider value, not just costs. This involves asking would members, including those in legacy arrangements, receive better value in more modern products or in a different arrangement or provider.
- **Trustees of master trusts and Independent Governance Committees (IGCs):** With the government's focus on fewer, larger multi-employer DC schemes, trustees and IGCs should engage with their scheme strategist and funder on commercial activities and future growth plans.

## The finer detail: Who the reforms will affect

### Members of DC pension schemes

The potential reforms to the DC pension market aim to drive better outcomes for members and support the UK growth agenda.

### Multi-employer schemes (Master Trusts and GPPs)

The government suggests that a greater number of benefits can start to arise when a scheme size gets to £25bn-£50bn. This leads to the proposal to restrict the number of default funds available and set a minimum size of the arrangement. The minimum size restriction would likely not apply before 2030 and there could be incremental stages that need to be reached.

The government is also interested in the role pricing has on the DC pensions market. It is exploring whether it would be appropriate to remove the ability for providers to set different pricing for different investors in the same product.

### GPP / contract-based schemes

Bulk transfers without member consent can currently be made from trust-based schemes under certain situations. The reforms explore whether bulk transfers from GPPs can be made without consent to either a contract- or trust-based arrangement and, what safeguards should apply to ensure terms and conditions are in the interests of members. This would open the path for Master Trusts to accept bulk transfers of members from GPPs without individual member consent being needed.

### Trust-based schemes

The announcements do not impact single employer trust-based schemes or those with associated employers. The focus for these schemes will be via the forthcoming Value for Money requirements.

### Employers

Along with all stakeholders, employers will be encouraged to focus on overall value during provider selection exercises and not just on cost. The proposals include a potential requirement for employers to review the provider selected for their employees every 3-5 years. The consultation also questions whether this potential employer duty to monitor the selected provider should fall to a named executive within the company.

### Advisers

Again, the focus on value (rather than scheme cost) is raised, and whether the existing regulatory regime achieves this. For example, there is currently no regulatory supervision of pension scheme selection advice. The consultation poses questions on the benefits to regulate this advice and what type of regulation would be effective.



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## XPS viewpoint

The proposals outlined in the Chancellor's speech represent a generational change to the UK pensions market. Our high-level views on the overall policy are outlined below.

### Helpful that there are no plans for mandatory exposures to private market assets

We think it's right that the Chancellor stayed away from mandating allocations to specific asset classes as we believed this could be a slippery slope. DC schemes should have one clear goal: maximising members' retirement incomes through strong, risk-adjusted returns. Pensions exist to support members' retirements, not to serve economic objectives. Mandating specific allocations risks distorting the market and undermining members' trust in the government's priorities for the industry.

### Tapping into economies of scale is easier said than done

Economies of scale will only be realised if a merger results in one arrangement, rather than multiple sections due to decision makers looking to minimise merger costs. There are also diseconomies of scale that start to appear when an asset owner becomes too large. For example, investments in the smaller end of the publicly traded stock market become a challenge because a meaningful position size would involve holding a significant proportion of the equity, thereby introducing illiquidity challenges. We suggest that the government focuses on creating an environment where beneficial consolidation can take place as its goal, and scale is not the goal in itself.

### Focus needs to shift towards performance and away from cost

We believe that scale alone is not sufficient to improve outcomes. Using Australia as an example, one reason their DC schemes have such large allocations to these assets is because there is clear evidence that achieving strong, risk-adjusted returns will win them new business. As noted in the consultation, there isn't the same focus on long term value in the UK currently, but we think the introduction of some type of performance-based league tables would help change the mindset. Performance league tables are not included in the current proposals.

### Investment model for accessing private markets

There are various ways DC schemes might access private markets, including pooled funds, segregated portfolios, co-investments and even direct investments. Scale is not required to unlock the immediate benefits of investing in private markets. We believe it is already feasible for schemes of £30m and above to invest up to 20% in illiquid markets through the use of an investment platform and pooled funds. Scale alone is not sufficient to guarantee that private market investments accessed via more complex investment models will be successful. The recent high profile losses experienced by international pension schemes with large undiversified stakes is a prominent example. More generally the dispersion in performance outcomes for private market assets means maintaining adequate diversification is more important than with other asset classes.

## Find out more

For further information, please get in touch with **Christopher Barnes** or **Mark Searle** or speak to your usual XPS Group contact.



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