Call for evidence Response

Addressing the challenge of deferred small pots: a call for evidence

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Guide and Information

Contents

Executive Summary 3
Responses 4
Broadstone Authors 8

Executive Summary

It is clear to us that the small pots problem should have a solution that satisfies the following principles:

- Simple
- Low level engagement with savers
- Low impact on sponsors
- Best outcome for savers
- Avoid unintended tax consequences

We believe that addressing the small pots issue via an industry, regulator and government led solution.

We also know that many billions of pounds worth of pots have accumulated over many years and auto-enrolment is accelerating this proliferation. This is why we believe that focussing on these lost pots should be the focus and we advocate for the default consolidator approach.

The regulators with government support should be able to build a regulatory framework:

- For 6 default consolidators. This framework should be based off VFM and quality pension provision
- For low level due diligence, fast transfers when pots and destinations are identified
- To ensure panel members are required to ensure contact is kept with members
- To leverage the anticipated successes from Pensions Dashboard at identifying pots and to consolidate them

In addition, we think the government should:

- Provide a minimum pension age override so schemes do not need to amend rules to accept a benefit with a lower normal minimum pension age
- Exempt hybrid schemes where members may benefit from interaction with DB scheme for PCLS purposes.

Broadstone is an independent pensions, investments and employee benefits specialist providing advice, bespoke services and solutions to clients spanning small business through large corporates. We are proud to count the Pension Protection Fund among our many clients, as one of a few select panellists helping members and trustees of pension schemes through the PPF assessment process. We have reviewed this consultation with interest due to our involvement in all different types of valuation covered.

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Responses

Question 1: Do you agree that these are the appropriate key criteria to inform development of a market-wide small pots consolidation solution? Are there additional/different criteria to apply?

Yes these are the appropriate criteria.

Question 2: How do you think we can increase member-initiated consolidation and what are the opportunities, risks, and limitations of member-initiated consolidation?

Pensions Dashboards will be an excellent way to engage with members and advise them of some of the benefits of consolidation.

Care needs to be taken to ensure in appropriate providers with higher charges are not able to convince members to consolidate from good quality schemes appropriate for low and median income workers.

The establishment of the default consolidators will assist in ensuring members go to schemes that provide Value for Money.

Question 3: We would be keen to understand from respondents, how far do you believe market innovations can go in reducing the growth of deferred small pots?

We believe that the policy driven improvements will pave the way for a clearer environment for providers to facilitate simple transfers.

Having a section of FCA authorised consolidators should be accompanied by relaxation to transfer due diligence so that transfers can go to these arrangements smoothly and without further checks.

These consolidator arrangements would be given “white-list” authority for all transferring schemes.

Question 4: Do you consider one of the values below to be the most appropriate starting limit for eligibility for automatic consolidation, and why – or is there an alternative value?

a) £1,000
b) £2,500
c) £5,000
d) £10,000

This is a difficult question and it is possible that the number could change over time.

We think a starting limit should be £2,500.

The limit should probably rise to £5,000 over time and then be subject to regular formal ministerial review as fund sizes change relative to the wider economy and any further proliferation of funds that are seen as too small to sit alone.

Given the current tax rules for taking funds as a lump sum £10,000 should be the upper limit until such time as tax rules change.

Questions 5 to 9

We do not have a response to these questions.

Question 10: Do you think there should be a minimum pot size limit for pots to be eligible for automatic consolidation? If so, what do you think this limit should be, and what should happen to pots below that limit?

This will be better informed as you gather the evidence from the market.

In principle there shouldn't be a minimum pot size.

However, we do question the value of micro pots remaining in the pensions system and further consideration should be given to refunding these tax-free to the contributing member, if they can still be contacted.

If the member cannot be contacted, then it should be consolidated.

Question 11: Do you agree that setting a prescribed period for a pot to be classified as deferred is the most appropriate solution – and what period of time would be appropriate, and why? If not, what would be a more suitable approach?

We agree a period of dormancy should be set before consolidation work commences.

Two years since the last contribution would seem an appropriate period of time.

Question 12: Do you agree with the above summary of potential benefits and implications of the default consolidator/s approach, and if not why?

Yes, we agree.

Question 13: What are the key benefits / risks of a multiple default consolidator and single default consolidator approach, including impacts on the wider pension market, and employers?

The key benefit is that members will see one larger pot. Pot follows member works for current savers and their most recent fund. Consolidating old lost pots provides an opportunity for the member to be able to have one point of contact for their legacy pension savings. Engagement in pensions remains a major issue and the pensions dashboard will allow members to see their pensions in one place but if spread across multiple providers and in small sums the inconvenience of contacting multiple providers (multiple phone calls, emails, app, different investment choices charges etc) is a barrier to that engagement.

Having one larger pot will also psychologically be more attractive to engage with.

Question 14: Who should be able to be a consolidator; should there be a limited number, and, if so, how many, and why?

We think this should be limited to half-a dozen or so providers.

Providers would need to be able to demonstrate to regulatory standard their VFM credentials. We note that there is ongoing work on the VFM and while this is an open question in that consultation. Whatever the outcome the government/regulator could set industry product standard on VFM that default consolidators should be able to satisfy.

This needs to be simple, open and transparent to those applying to ensure the regulation of these providers and the arrangement being used.

Similar to previous authorisations, schemes acting as default consolidators should be able to demonstrate a track record in the pensions industry as well as strategies to manage these funds for the long term into decumulation and indeed prescribed steps to wind-up and transfer to an alternate consolidator should business models change.

Question 15: What would be the appropriate approach to giving members choice in terms of choosing their consolidator, and what approach should be taken if the member did not make an active choice?

This would be a three stage process:

1. Member led decision would be the option to transfer to one of the 6 default consolidators.
2. If no member option then consolidation should be with the fund (or largest fund) with one of the default consolidators
3. Failing that a consolidator would be chosen for all small pots the member may have on a carousel basis

We can foresee some issues with creating the technology to be able to share this information and move this and how this is built and operated should be consideration for a future consultation.

Question 16: Do you agree with the above summary of potential benefits and implications of the pot follows member approach, and if not why?

Question 17: What are the key benefits / risks of a pot follows member, including impacts on the wider pension market, and employers?

The simplicity and lack of member action being required has advantages for the member and resolves the concerns of inertia/member inaction.

We are concerned about the possible outcome of members being moved from a scheme with better VFM credentials to a poorer scheme. Most importantly this could be higher charges but could also be reduced flexibility on retirement options and/or poorer governance standards. We're also concerned about the potential for transaction charges and sequencing impact of transferring the whole pot in one go.

Question 18: Of the two solutions set out above what is your preferred approach, and why?

The automatic consolidator should be the only approach.

Question 19: Are there any further / fresh or hybrid solutions that are worthy of consideration?

No.

Question 20: Should there be an initial focus on managing the flow of new pots or removal of the existing stock, and where does the balance of impact lie for each of the solutions presented?

We should be dealing with existing small pots.

Perhaps this could be addressed by looking in year 1 at pots that have been dormant for 5 years+, then year 2 3 years+ before year 3 "years+ as business-as-usual state.

Question 21: What could be done to incentivise, build momentum, and help build market and member confidence in member exchanges, either now or in future? Would this be best taken forward by industry or government?

Public information campaign to advise that the government and industry are going to work together to work for your better retirement by:

- Launching/ed the dashboard to reconnect you to your pension pots
- Taking action in your best interest to consolidate your lost small pots in one quality scheme

Question 22: Could a member exchange form part of a hybrid model alongside one of the large-scale consolidation solutions discussed in Section 5, or with a large-scale consolidation solution acting as a backstop?

No. We agree that this method should be dropped.

Question 23: Do you agree that same scheme consolidation has a key role to play in the wider consolidation of deferred small pots, and can act as a foundational measure to larger market-wide solutions? If not, why?

Yes – we are convinced that this is the preferred solution.

Question 24: If your scheme currently does not undertake same scheme consolidation, what are the reasons behind this and what would be required to overcome this?

N/A

Question 25: As part of this call for evidence we would therefore welcome views on how protected groups are currently impacted by the deferred small pots issue;

(a) whether the impact differs between groups and in comparison, with non-protected groups
(b) what mitigations providers are putting in place and the impact of each of the options on protected groups, and
(c) and how any negative effects arising from them may be mitigated.

We would anticipate that small pots would most likely impact ethnic minority groups and women who are more likely to be in and out of work for various societal and family reasons and so accumulating a number of small pots due to their working patterns. These people would benefit from a default consolidator solution.

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