Sackers

Mansion House 2024: Government proposes pensions "megafunds"

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Introduction

The Chancellor, Rachel Reeves, delivered her first Mansion House speech on 14 November 2024. Following the avalanche of pensions reforms announced by former Chancellor Jeremy Hunt in 2023, this year's speech confirmed plans to "go further" and create pension "megafunds" to "power growth in our economy".

Key points

- The Government is "clear" that the future of workplace DC schemes is in "fewer, bigger, better run schemes" that can "deliver better returns" and "boost investment in the UK".
- Two key measures are proposed which are designed to accelerate and help enable scale and consolidation in the DC market: introduce minimum size requirements for DC default arrangements in multi-employer schemes used for automatic enrolment ("AE") as well as limits on the number of such arrangements, and override individual contracts to allow the bulk transfer of assets from contract-based schemes without individual savers' consent.
- Single-employer schemes are excluded from the proposals, as the new VFM framework should ensure those schemes achieve value. Views are sought on whether there are other schemes with specific characteristics, such as sharia-compliant funds, which it would be in the public interest to exclude.
- In addition, the Government is consulting on proposals "to put the LGPS on a clearer, firmer long-term trajectory to scale and consolidation…as well as measures to improve LGPS fund and pool governance and drive local investment".
- The Chancellor also announced that, as part of the Government's climate commitments, pension funds will be required to develop and implement credible transition plans that align with the goal of the Paris Agreement to limit the rise in global warming to 1.5 degrees Celsius.

Background

In its election manifesto, the Government committed to undertake a review of the pensions landscape to consider what steps were needed to improve pension outcomes and increase investment in UK markets. Launched in July 2024, the first phase of this review considered four main areas:

- scale and consolidation in the DC workplace market
- the LGPS
- cost vs value in the DC workplace market, and
- UK investment.

To inform the review, a call for evidence on pension investment was run during September. Our response can be viewed here.

With the aim of allowing a "full and thorough consultation process" ahead of next year's Pension Schemes Bill, the Mansion House speech introduced an interim report with the initial findings of the review's first phase and two new consultations:

- Pensions Investment Review: Unlocking the UK pensions market for growth, which proposes measures designed to accelerate and help enable scale and consolidation in the DC market
- LGPS (England and Wales): Fit for the future, which contains a package of proposed reforms to the structure, investments and governance of the LGPS, intended to tackle "fragmentation and inefficiency".

Unlocking the UK pensions market for growth

Achieving scale in the DC market

To achieve the scale the Government considers necessary to "remove complexity and fragmentation" from the pensions market, it is seeking views on proposals to introduce minimum size requirements for default funds in multi-employer DC schemes which are used for AE as well as limits on the number of such arrangements.

The consultation explores:

- whether the maximum number and size of defaults should be applied at arrangement or fund level
- whether schemes should be able to provide different pricing structures within the same default or between multiple defaults
- what the maximum number of defaults should be
- the correct minimum size of assets under management that should apply, and
- when such scale should be achieved by.

Since these measures are "significant market changes" which would require sufficient lead in time, the requirements would not apply before 2030 at the earliest. Options to allow schemes to "staircase up" their value and reduce the number of default funds they operate are being considered.

Bulk transfers without consent from contract-based schemes

Seeking to address the "significant barrier to consolidation" posed by the requirement for contract-based pension providers to get individual consents before transferring members to another arrangement, the consultation proposes measures to enable contractual overrides for contract-based schemes, subject to the appropriate protections. This would support the forthcoming VFM framework and small pot default consolidators, but the Government envisages bulk transfers without consent also being used in wider circumstances where it is in members' best interests. Detailed rules on the use of transfers without consent will be developed by the FCA and subject to further consultation.

Costs vs value: The role of employers and advisers

The Government has been clear that the DC market is operating with an excessive focus on costs which comes at the expense of considering a broader range of metrics of scheme quality and limits budgets to enable investment in a broader set of asset classes. Respondents to the call for evidence suggested that to drive a shift in culture, all participants in the pensions ecosystem should be focused on value. As a result, the Government is also using this consultation to explore the role of employers and advisers and seek further views on the relative merits of proposals to encourage these groups to make this shift in focus.

Next steps

The consultation on unlocking the UK pensions market for growth closes on 16 January 2025. Many of the proposals "could lead to fundamental changes which will require primary legislation", and a decision on whether to include these measures in next year's Pension Schemes Bill will be made in light of the consultation outcome.

A final report on phase one of the pensions review is due in the spring. It will further consider investment by pension funds in the UK. The scope of phase two "will be published in due course", but it is expected to consider additional steps to improve pension outcomes, including assessing retirement adequacy.

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