

VFM Framework

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8 March 2026

Dear VFM Policy Team

LCP's response to the Value for Money Framework further consultation, CP26/1

Who we are

LCP is a firm of financial, actuarial, and business consultants, specialising in pensions, investment, insurance, energy, health and business analytics. We have over 1,200 people in the UK, including over 190 partners and around 250 qualified actuaries. The provision of actuarial, investment, covenant, governance, pensions administration and benefits advice, and directly related services, is our core business.

We advise on over £115bn of DC assets covering 10 million members across a variety of DC schemes from Master Trusts to GPPs and Single Employer Trusts. We have therefore provided perspective from all DC arrangements.

About 80% of our work is advising trustees and employers on all aspects of their pension arrangements, including investment strategy. The remaining 20% relates to insurance consulting, energy, health and business analytics. LCP is authorised and regulated by the Financial Conduct Authority for some insurance mediation activities only and is licensed by the Institute and Faculty of Actuaries for a range of investment business activities.

Introduction

We welcome the opportunity to respond to your consultation. We have answered your specific questions below but we have taken the opportunity to summarise our key messages and observations:

- The scope of the Framework should be extended to include decumulation products and non-workplace pensions;
- Some overlapping current legislation should be amended or revoked when the VFM Framework comes into force in order to reduce the compliance burden on schemes;
- We are not convinced that the proposed move from geometric to arithmetic averaging for investment performance metrics offers any additional benefit;
- There is still a risk of "gaming" over the use of FLMS and suggest greater oversight from the regulator or ability for public scrutiny is considered. Specifically, the requirements to obtain and consider advice from an appropriate third party about FLMS should be made stronger;
- The comparator group for assessments must be framed to reflect the objective of the assessment and avoid creating incentives for gaming or homogenisation;
- A four-point RAGG structure is a step forward, but the current design creates material risks unless the framework is tightened, the use of overrides is properly governed, and the regulatory consequences of each rating are reconsidered;
- Insufficient recognition is given to employer-level subsidies and support. Employer support should not be relegated to the narrative part of the process alone. Without meaningful acknowledgment of employers who go further in supporting provision, there is a real risk that businesses will be discouraged from offering anything beyond the bare minimum; and
- Given the significant consequences of the RAGG rating system, a trial period before full implementation would seem sensible.

Chapter 2 – Scope and thresholds

Q1: Do you have any comments on the proposed scope? Do you believe any further exemptions should be considered?

Our views remain largely the same as we set out in our response to CP24/16. In particular, we still believe that decumulation products and non-workplace pensions should be within scope, for the reasons we previously stated, so we do hope that you will keep the Framework's scope under review as you indicate.

Since responses to this consultation are also being read by TPR, we also ask for confirmation that the additional VFM requirements for sub-£100m schemes, as set out in regulation 25(1A) of the Scheme Admin regulations (SI 1996/1715) will be revoked at the same time as the VFM framework comes into force. There can be no merit in both sets of requirements existing in parallel. We also ask for confirmation that schemes which provide no money purchase benefits other than AVCs are not in scope of the VFM framework and that there will be an explicit exemption for them, as there is under the definition of "relevant scheme" in connection with the governance requirements under Part V of the Scheme Admin regulations.

We also ask for confirmation that the intention is still for the Annual Chair's Statement requirements to be phased out once the Framework is fully implemented, as was set out in the consultation outcome paper FS23/3 (11 July 2023) and in which we were quoted as saying that "We strongly believe that introducing the VFM framework without reducing the burden of The Chair Statement will be more than many schemes can cope with". We still stand by this statement and note that you recorded at that time that over a quarter of respondents indicated that the Chair's Statement should be removed on implementation of the VFM Framework, if not sooner.

Q2: Do you have any comments on our proposals in relation to unlinked members? Do you have any preference with regard to the options suggested? Are there alternative options you would like to suggest?

We do not have a strong preference for either option (a) or (b) and therefore would be content if option (a) was adopted as you propose.

Q3: We do not think this situation would arise for trust-based schemes. Do you agree with this understanding?

We think there are situations where this could occur, for example it is possible for historic data where a participating employer has ceased to exist, and member data does not indicate an employer or where there have been bulk transfers in the past into a scheme and employment data has not been carried across. Having said that, we do not think it is a material concern.

Q4: Do you agree with this proposal for transferred members? Why or why not?

We agree with this proposal but note that it could lead to an increase in unintended default options (for example, if members in an annuity targeting fund were mapped into another annuity targeting option which was not currently a default).

Q5: Do you agree with our proposed exemptions for contract-based arrangements? Why or why not?

These seem a pragmatic approach. Your second proposed exemption where schemes will not have to undertake a full VFM assessment when FCA has been notified of a decision to fully close/ transfer all members is especially welcome.

Chapter 3 - Investment performance – backward-looking metrics

Q6: Do you agree with the proposal to use arithmetic averaging instead of geometric averaging? Why or why not?

We understand the rationale for this approach, particularly the desire to reflect the average experience of cohorts of members moving through specific years-to-retirement (YTR) points. However, we have reservations about replacing geometric averaging entirely with arithmetic averaging for investment performance disclosure.

Geometric averaging remains the most appropriate measure of long-term investment performance where returns compound over time, as it reflects the actual growth rate experienced by members. Arithmetic averaging can overstate expected long-term outcomes where returns are volatile and may therefore give an unintentionally optimistic impression of performance, particularly over longer horizons.

Given that DC member outcomes are ultimately driven by compounded returns, this distinction is important when assessing value for members. This point is particularly relevant for the 30 year to retirement longer term returns, where most strategies would have a consistent “growth phase” allocation for many years.

We recognise that the consultation is seeking to capture the experience of different member cohorts as they pass through YTR points, and arithmetic averaging may provide a pragmatic approximation of average observed annual outcomes across cohorts. Nevertheless, we do not believe this fully substitutes for the insight provided by geometric averages, especially when assessing the effectiveness of long-term investment strategy design. And therefore, our preference is geometric, outcome based. We question whether an additional set of data adds any further value to the performance assessment.

Separately, but still relevant to this proposal, a note on gross performance: the industry standard is that gross performance is before the deduction of the fund managers fee (the fund AMC) but is still net of the fund additional expenses (such as for custody and administration). The proposal is for returns on three methods – but performance gross of both the fund AMC (investment management charges) and additional expenses is not an industry standard approach. We suggest there is little value added from reporting performance on three different methods and propose this is simplified to the two commonly reported methods used in the investment industry:

- Performance gross of investment management charges (but net of additional expenses and transaction costs).
- Performance net of all costs and charges.

We believe there may be confusion and erroneous reporting of figures unless clear guidance is provided. In particular, how performance fees are to be reflected should be clarified as they tend to be captured in additional expenses, but also cost information for schemes that are structured on an unbundled basis and for hybrid arrangements where costs are shared between sections. We are also aware of examples of cross-subsidy between investment and administration related costs, which could affect the reliability of this assessment.

For contract-based schemes and some provider trust-based offerings, it may not be possible to split between investment and administration costs. We would welcome further clarity about what costs should be included and state explicitly what is needed for contract-based vs unbundled trust-based schemes.

Q7: Do you agree with our proposed disclosures to facilitate comparisons between multi-employer arrangements with variable charges? Why or why not?

We broadly agree, since improving comparability between multi-employer arrangements with variable charging structures is important for supporting trustee oversight and the transparency may lead to lower fees being negotiated for the benefit of members.

Requiring disclosure of the maximum, minimum and median values for key metrics (such as performance net of charges) should help illustrate the range of member outcomes within arrangements where charges vary by employer, legacy section, or pricing tier. This is preferable to relying solely on a single average figure, which can mask dispersion and potentially obscure poorer value cohorts.

Q8: Do you agree with our suggested approach for mapping the performance of TDFs with multi-year cohorts for the purposes of deriving the relevant performance data?

The proposed approach to mapping TDF performance where funds are structured around multi-year retirement cohorts rather than single-year vintages does represent member experience for the cohorts that are 30, 5 or 0 years to retirement. In practice, many TDF arrangements group members targeting retirement within a range of years and requiring performance reporting strictly aligned to exact years-to-retirement (YTR) points would not reflect how these strategies are implemented.

However, this approach creates inconsistencies when comparing to lifestyle strategies. All else equal in terms of glidepath and assuming upward trending markets, the TDF returns will be higher than the equivalent lifestyle, due to the issue of step changing between one TDF and another and effectively moving back in the glidepath to a more risky / higher expected return point.

For example, to calculate the 5-year return to end of 2023 for the 5 years to retirement cohort, for TDFs with 5-year vintages the calculation would be:

- In 2023 the calendar year return of the 2026-2030 TDF (since 2028 is the target retirement year for members that are 5 years to retirement).
- In 2022 the 2026-2030 TDF (since 2027 is target retirement year now, being 5 years away from 2022).
- In 2021 the 2026-2030 TDF (2026 target retirement year).
- In 2020 the 2021-2025 TDF (2025 target retirement year).
- In 2019 the 2021-2025 TDF (2024 target retirement year).

The problem with this approach is that there is a step change as we move from one TDF to another in the calculation. In this example the performance reported in 2020 would be for a more de-risked asset allocation than in 2021. It is effectively jumping 5 years back in the equivalent lifestyle glidepath.

This results in performance that does not reflect either a consistent 5-year-to-retirement allocation or the actual experience of a member cohort. It risks distorting comparisons between TDF providers with different bucket structures and is expected to favour TDF approaches over lifestyles (which are fixed to reporting at a particular YTR part of the glidepath each calendar year). The impact is larger the wider the buckets are and the steeper the de-risking of the glidepath underlying the TDFs.

We suggest interpolating between adjacent TDFs to derive a smoother glidepath return and avoid the issues around step change from one TDF to another. For example, in 2021 the 2021–2025 TDF is centred around ~2023 retirement, which is 2 YTR in 2021, and the 2026–2030 TDF is centred around ~2028 retirement, which is 7 YTR in 2021. The 5YTR point sits between the two TDFs. The weights would be calculated based on the years; in this example to calculate the 2021 figure for 5YTR we'd take 40% of the 2021-2025 TDF return and 60% of the 2026-2030 TDF return (ie $5 = 40\% \times 2 + 60\% \times 7$).

Q9: Do you agree with our proposed risk metrics? Why or why not?

We consider the proposed volatility metrics to be straightforward to calculate and intuitive. The approach of calculating annualised standard deviation (ASD) using monthly gross returns, and averaging variances over multi-year periods before taking the square root, is statistically sensible. Whilst a simple arithmetic average could be considered here, this approach would understate risk and not recognise that high volatility years contribute disproportionately more risk than lower volatility years.

We welcome the removal of the requirement to report maximum drawdown. Whilst maximum drawdown can be a useful risk metric in some contexts, it measures the largest peak-to-trough fall over a period and is therefore highly sensitive to the precise sequence and timing of returns within that period; two funds with identical annual returns over a year could report materially different maximum drawdowns depending on whether losses occurred early or late in the year, or whether there were interim recoveries. As a result, maximum drawdown can reflect short-term market timing effects rather than underlying volatility or long-term risk characteristics. This adds complexity without materially improving understanding of value.

We would encourage consideration of whether the gross investment performance dispersion metric is necessary alongside the proposed volatility measures. Dispersion (defined as the range between the highest and lowest annual gross return in the period) is straightforward to calculate but is driven by single outlier years and does not provide insight into the consistency of returns within the period. Both average and maximum ASD are already required and provide more statistically robust measures of variability. The incremental benefit of also reporting dispersion appears limited. In the interests of proportionality and clarity, we suggest that the framework could be streamlined by removing this metric.

Q10: In light of the role that total costs and charges play in the calculation of net performance, we would be interested in views on whether chain-linking should be applied to costs and charges or if there are alternative suggestions that achieve more accurate reporting of net performance?

We suggest applying AUM-weighting to net performance as for gross returns. For total costs and charges, we do not see value in including figures from arrangements that no longer exist. Instead, reporting the costs and charges of the continuing arrangement alone provides a clearer reflection of what charges are likely to be applied to members going forward.

We support the objective of presenting investment performance on a comparable basis across all arrangements. However, for single-employer trust schemes, the definitions of “investment charges” and “net of all costs and charges” require greater clarity. In our view, performance figures presented net of costs should reflect only those charges borne by members, as these determine the returns members receive in practice.

In some schemes, members meet only additional fund expenses already reflected in gross performance, while the annual management charge (AMC) is paid in full by the sponsoring employer. This results in a materially lower effective member charge than under a typical member-borne structure.

It is unclear whether an employer-funded AMC should nevertheless be treated as an “investment charge” and deducted when producing “investment performance net of investment charges”. If deducted, this would understate the return members receive and distort comparisons with arrangements where charges are member-borne. If such a deduction is required, any employer subsidy should be clearly disclosed and appropriately reflected in comparisons.

Similarly, the scope of “net of all costs and charges” is unclear. In some schemes, members do not fund day-to-day DC administration. Requiring estimated administration costs to be deducted from performance would introduce subjectivity and inconsistency unless detailed and prescriptive guidance is provided on what should be included and how it should be calculated.

Greater consideration should therefore be given to the diversity of charging structures within single-employer trusts, particularly where employers subsidise member costs. The reporting framework should ensure that genuine value delivered to members through such arrangements is not obscured in the pursuit of standardised comparisons.

Q11: Do you agree with our proposals for chain-linking? Why or why not?

We agree that a clear methodology is required where members are moved between default arrangements to preserve continuity of performance reporting and avoid artificial breaks in track records and “survivorship bias” as underperforming strategies are quietly shelved and better performing ones are promoted as the “flagship” defaults. The proposed chain-linking approach provides a logical framework for achieving this.

Use of weighted average monthly returns based on assets under management (AuM) at the point of merger (or on a rolling basis where transfers occur in stages) makes sense to account for the relative importance of each strategy in the merger.

This reflects the experience of members and avoids overstating or understating volatility or returns during transition periods. The distinction between single-step and phased transfers is also sensible and reflects operational reality in large schemes. Greater clarity is needed in the definition to ensure that chain-linking is required for all bulk transfers into a new arrangement, irrespective of whether they are trustee, provider or employer-initiated.

We agree that chain-linking should not apply where arrangements from different firms merge, as the metrics are designed to assess whether a particular firm’s offering demonstrates value, and having a good track record “watered down” by a worse performing strategy of a firm acquired would act to discourage firms from acquiring struggling competitors (and hence discourage consolidation).

We support the exemption from chain-linking where members are moved to an existing receiving arrangement within the same firm that meets the stated criteria (minimum three-year history, ability to accept contributions, and minimum 5% active contribution participation). These conditions are proportionate safeguards to prevent the creation of artificial or dormant arrangements solely to facilitate transfers.

We would suggest consideration to requiring reporting of a provider default return figure in aggregate where all default strategy returns are amalgamated, weighting each figure by the value of asset in that default at the year end. For returns to be compared like for like we’d suggest only drawdown targeting strategies are amalgamated in this way, and to reduce the burden of compliance to exclude any default that has less than 5% of the overall assets of the provider in default strategies.

We propose the chain-linked is applied for all cases where member assets are moved from one default to another. This would cover employer driven movements and provider driven movements. One approach could be to consider assets at the end of the year of the receiving default and then the % of assets at the year end that came from transfers in from other defaults – the weight of those previous defaults and the performance of those over the year could be factored in to create an aggregate performance.

Q12: Do you agree with our proposals relating to legacy arrangements? Why or why not?

We agree with the proposals relating to legacy arrangements. The approach to with-profits and smoothed-return funds, including the look-through to underlying investment returns and reversing deductions when calculating gross performance, provides transparency and ensures consistency with the treatment of in-scope arrangements.

We also support the guidance on guarantees, highlighting them in the features table without adjusting past performance or risk metrics avoids distortion of historical metrics (in particular risk metrics, which may be understated with a guarantee applying) and ensures investment approaches across providers are compared on a consistent basis.

Finally, we note and agree with your proposal that any additional features not specifically covered in the requirements should be included as part of the rationalisation step of the VFM assessment.

Chapter 4 - Investment performance – forward-looking metrics

Q13: Do you agree with the proposed FLM disclosures and the use of own assumptions? Why or why not?

While we are supportive of the use of own assumptions, giving providers discretion over the assumptions used for FLM disclosures creates a clear risk of a “race to the top” within what is considered plausible. While the requirement for external input on these assumptions is helpful, we do not believe this goes far enough and believe further controls are required.

The forward-looking metrics example illustrates expected returns over a 10-year period for members who are five years from retirement and for those already at retirement age. This does not make sense. These members are not expected to remain invested for a further 10 years in the same strategy, and asset allocations at this stage are designed to be appropriate for retirement and taking benefits, not to maximise growth over a subsequent decade. As a result, their 10-year performance figures may appear comparatively weak relative to younger cohorts, which could be misleading and distort assessments of value.

Q14: Do you agree with the proposed requirement to obtain and consider external advice? Why or why not?

Yes, we agree with the proposed requirement. However, it should be made clear that such advice must constitute regulated investment advice provided by an appropriately authorised firm. This would provide an important safeguard around quality, professional standards and accountability.

In addition, we believe there should be greater transparency around the assumptions adopted. Requiring schemes (or providers) to disclose their key assumptions either publicly or to TPR and or FCA, would enhance accountability and allow for effective regulatory oversight. Such disclosure would help identify outliers, reduce the risk of optimistic bias, and discourage a “race to the top” in expected return assumptions.

Without regulatory visibility, the requirement to obtain external advice alone may not be sufficient to mitigate gaming risk. Combining regulated advice with transparent disclosure would materially strengthen the robustness and comparability of FLMs across the market.

There should also be the expectation that trustees and firms do follow the regulated investment advice about the assumptions and explicit disclosure if any assumption is used that deviates from the advice.

Q15: Are the proposed guardrails sufficient to reduce the risk of gaming and ensure the FLMs disclosed are credible for use in the assessment process? If not, what alternatives/ additions would you propose?

As noted above in the response to the previous question, we favour regulatory oversight around the assumptions that are used in the FLMs and note that external advice should be in the form of regulated advice.

Chapter 5 - Asset allocation disclosures

Q16: Do you foresee any difficulties in reporting this data? If yes, what specifically?

We recognise the objective of improving transparency around asset allocation, particularly in relation to UK and illiquid investments. However, we are concerned that the level of granularity proposed is disproportionate to the stated purpose and will be materially burdensome to implement.

The combined requirements of asset class and sub-asset class splits, UK and non-UK, listed and unlisted – for three separate cohorts – represent a significant expansion of reporting obligations.

The requirement to express synthetic exposures in physical asset terms adds further complexity and may result in disclosures that are misleading – for example it is unclear how an investment in a leveraged fund would be reported when the total must be 100%.

We suggest the reporting requirements are made consistent with the asset allocation requirements already applying to Chair's Statements (notwithstanding our previous comments that Chair Statements should be abolished in due course). This would avoid trustees having to report asset allocations in two different ways.

Chapter 6 - Costs and charges

Q17: Do you agree with our proposals for disclosing employer subsidies? Why or why not?

In our view, it is important that the framework recognises the wide range of cost structures across schemes, particularly where employers subsidise charges that would otherwise be paid by members. Many of our clients have all administration and governance related costs covered by the sponsoring employer, which delivers a clear financial benefit to members by reducing their overall cost of saving (this applies to some employers within master trusts as well as single employer trusts). We also have at least one client where **both the Annual Management Charge (AMC) and administration costs are met entirely by the employer**, with members paying only limited additional expenses of up to "x%". This creates a significantly lower member charge than would be seen under a standard charging structure.

However, under the proposed VFM approach, it is not clear whether these employer-paid costs would be visible in member-level comparisons. Reporting total charges in the VFM assessment outcome without apportioning between the members and employer misrepresents the value of the arrangement to the member and this risks schemes that provide meaningful employer subsidies appearing more expensive or less competitive than they actually are, leading to misleading conclusions. Further, in our experience a move from single trust to master trust is often accompanied by employers stepping away from providing any subsidy on charges. The risk we see potentially playing out here is if the proposals are implemented then trust schemes with members paying subsidised charges will get wound up as the VFM report shows total charges without subsidy to be higher than master trusts. Members will then be moved to a master trust but will actually receive worse value with higher charges paid as the employers takes the opportunity to save money by removing existing subsidisation.

We note the current provision to state these costs in the table shown in 10.12. Our concern with this approach is that external parties are likely to use data points to make decisions rather than considering additional context. This could lead to a solution appearing to offer better value before considering the benefits of employer subsidy which would not reflect reality. In the case of two identical strategies, one of which benefits from employer subsidy, in our view the metrics should reflect this difference to avoid suboptimal decision-making.

We also believe that a clearer definition of employer subsidy is required to ensure consistency. For example, are employer subsidies only intended to refer to explicit costs and charges met by the employer, or do they also include "value added" factors such as in-house pension departments, trustee oversight costs and or communication exercises funded by employers.

Q18: We are aware that profit share and with-profits distribution can follow some time after the performance to which they relate. We have considered whether there would be benefit in apportionment, linking the share/ distribution to the period to which it relates. We would be interested in views on this.

As distributions may be declared or paid in a different period from the performance to which they relate, recognising them solely in the period of payment could materially distort year-on-year cost disclosures. This would reduce comparability across firms and over time, particularly where distributions are irregular or reflect smoothing. Therefore, we support the proposal.

Chapter 7 - Quality of services

As consultants, we are unable to comment specifically on how the data can be managed and obtained as it is held within provider or third party systems, however we have provided views on the questions from our perspective.

Q19: We would like to include 'Payments out as retirement income' as a key transaction. We are aware that some individuals approaching retirement may request payment at a future date, hence our request for data based on requests for immediate payment. We would be interested in views on whether our proposed measure above would provide a reasonable measure.

We support the inclusion of payments made to provide retirement income within the definition of a core financial transaction, provided the term is more tightly defined.

- If the definition is intended to capture all income-drawdown withdrawals (rather than only the member's first payment request), the metrics and tolerances must make that explicit.
- Drawdown amounts and frequencies are variable and so that data will therefore move over time. From a pure "promptness and accuracy" standpoint this variability is less of an issue, so long as the measure is confined to the efficiency of processing, not the member's chosen pattern of withdrawals.

It is important to note that providers/trustees will only have control over the payments going out of their scheme and not whether it has arrived at its correct destination.

We welcome the updated drafting. As noted, trustees and providers can only influence the arrangements they administer and the effectiveness of their own processes and the proposed wording reflects that practical reality.

Q20: We would be interested in views on whether the payment of Pension Commencement Lump Sum should be a transaction included in this section.

It seems sensible to include this metric as it may help ascertain how members are behaving, as well as if they are paid in a timely manner.

Q21: Do you have any comments about our proposal to collect complaints data at the level at which the same service is experienced? Do you agree with our proposed definition of a platform?

Your proposal seems sensible. You may want to consider separating between active and deferred members for further granularity and understanding.

Q22: We would be interested in views on whether our proposed approach to negative perception metrics will provide relevant data to indicate saver concerns.

From our experience, negative feedback generally comes from individuals who are dissatisfied and therefore more inclined to respond. Individuals who are happy or neutral generally don't provide feedback. Therefore, there is a danger that this data will be skewed.

Within workplace pensions, this effect may be magnified as member engagement is generally low across the industry. Also, it is possible different arrangements may attract different volumes of complaints and due to member understanding, may not accurately reflect the position of the scheme. It is also important to define exactly what a complaint is eg is it any expression of dissatisfaction.

It may be more helpful to focus on the outcome rather than the individual numbers, for example how many were upheld or escalated internally, as well as the Ombudsman related data.

Q23: Does our revised approach to engagement metrics seem appropriate? Additionally, we would be grateful if you could provide us with an explanation of what surveys/data gathering exercises you currently undertake for member engagement. If you would be willing to share a copy of your member engagement survey(s) with us, please tell us.

Distinct market segments attract markedly different member and employer profiles, which in turn drive contrasting patterns of engagement. Some metrics will therefore produce systematically lower (or higher) scores for certain schemes irrespective of their underlying quality or scale.

While schemes continue to set specific engagement objectives, it is still being developed. Many schemes are starting from quite a low engagement base and therefore some of the metrics will not provide the insight that is expected. In addition, whilst the metrics may increase and change over time, they are not necessarily an indication of value for money.

Q24: We welcome feedback on our revised proposals for engagement metrics and how that engagement generates specific outcomes.

We fully support the decision to allow additional time for the development of engagement metrics. Developing clear, consistent and comparable metrics with broad agreement across participants will take time and careful consideration.

Areas to potentially investigate further to include in future assessments could be:

- **Member profiles:** age, earnings, industry sector and pot size materially influence both the need for, and likelihood of, engagement.
- **Inertia as a positive outcome:** for many members, remaining enrolled and benefiting from a well-governed default fund is paramount. Metrics should recognise circumstances where "no action" equates to a good result.
- **Channel and content:** communications need to be tailored to the target audience; one approach will not suit every scheme type.

Chapter 8 - Assessment process

Q25: Do you agree with our proposal for comparisons against a commercial market comparator group and the criteria for it? Why or why not?

Your proposal seems broadly sensible as clear criteria for selecting comparators improves transparency and reduces subjectivity.

However, we would encourage consideration be given to the at-retirement cohort as different at-retirement targets are not directly comparable. Cash-targeted strategies and drawdown-targeted strategies for example, have

fundamentally different risk/return profiles, so simple comparisons could distort the results. The risk for the at-retirement cohort is that this benchmarking could create incentives for all strategies to increase risk at-retirement to aim for higher returns despite the overall retirement objective. The performance metrics are more likely to be heavily focussed on than the risk metrics. For example it could lead to behaviour that finds it easier to increase equities and explain a bad year of performance than to manage risk but consistently underperform riskier strategies.

There are a number of areas where caution is needed:

- Assuming MTs are the best-value benchmark risks baking in a conclusion before the assessment begins. The framework needs to be explicit about whether it is comparing schemes against the *best in market* or assessing whether members would be better off consolidating into a different scheme.
- Avoiding a league-table dynamic is essential. Australia shows that when comparators are known in advance, schemes can game the metrics, herd into similar strategies and reduce innovation.
- Comparator breadth matters. Too narrow (only MTs) risks benchmark hugging; too broad risks turning the exercise into a performance table. The set should reflect scale, complexity and risk profile, and be reviewed periodically.

Overall the proposal is workable, but only if the comparator group is framed to reflect the objective of the assessment and avoids creating incentives for gaming or homogenisation.

Q26: Do you agree with our proposed approach to comparisons for different types of arrangements? Why or why not?

Using different comparison approaches for different arrangement types makes sense, but the framework needs to avoid narrow, self-referential peer groups and must recognise where cross-type comparisons remain necessary.

- Different models operate differently. Master trusts, Single Employer Trusts and bundled/unbundled schemes vary in scale, governance, investment autonomy, member/customer demographics and cost structures, so a single comparison method would distort results. A tailored comparison reduces the risk of unfairly marking up or down a certain model. This approach allows schemes to understand what “good” looks like within their peer group without forcing inappropriate like-for-unlike comparisons.
- However, we believe further thought needs to be given to avoid narrow comparator sets. Comparing only within a tight master trust universe risks benchmark hugging, herding and reduced innovation. This is also especially acute for very large schemes, Single Employer Trusts who are to compare total costs and charges with the average of the comparable cohort of employers (based on size and AUM) in the MT comparator group. For larger schemes, the peer group of comparable employers could be very low and make the results distorted / reliant on a small number of arrangements and associated terms limiting the usefulness of the comparison.
- Recognising when best-in-class comparisons still matter. If the policy aim includes testing whether members could receive better value through consolidation, the framework must allow cross-type comparisons where they reflect realistic alternatives.

The differentiated approach is directionally right, but its effectiveness depends on calibrating comparator groups so they are neither too narrow nor too broad, and on acknowledging that very large schemes may have limited true peers. A balanced framework that still allows meaningful cross-type comparisons will better support genuine improvements in value without creating distortions.

Q27: Do you agree with the approach for weighting of BLMs and FLMs? Why or why not?

We have commented on 27-31 together below.

Q28: Do you have any feedback on the proposed approach in option 1? What improvements or changes would you suggest?

We have commented on 27-31 together below.

Q29: Do you agree with the proposal for the composite metric in option 2? Why or why not? Is it helpful for considering value? If so, is equal weighting appropriate for the composite metric or what alternatives would you suggest?

We have commented on 27-31 together below.

Q30: Do you agree with the proposed composite comparison figure in option 2? If not, what do you think the composite metric or the FLMs should be compared against?

We have commented on 27-31 together below.

Q31: Do you have any feedback on the proposed approach in option 2? What improvements or changes would you suggest?

This answer covers 27-31 together.

The rationale for including FLMs to allow for recent strategic changes is sensible.

However, allowing FLMs to compensate for and justify poor performance could create further misuse and make the data less comparable or useful. For example, if equity markets are down and therefore not in line with long term expectations for the asset class then this should be reflected in BLMs and will be reflected across all comparator schemes. This should not, in our view, allow for an increase in the weight to FLMs.

If different weightings are to be used then there should be set weightings (eg 50%, 30%, 10%) to make weighted figures comparable. However we encourage thought to be given to set parameters over how much weight can be given to the FLM based on how large the changes were and or the period since the changes were made.

If there is flexibility in the weightings between BLM and FLM then the timeline for providing the data would need to be extended. Trustees would need to gather the data and assess its performance against long term expectations and then agree which weight to give. The current timescales would not allow for that to happen.

If equal weightings are used across the board as per option 2 then this defeats the purpose of including FLMs to allow for strategic changes. This purely dilutes the results of the BLMs.

Q32: Do you agree with the proposed guardrails? Do you believe other guardrails would be appropriate?

We agree that the use of FLMs should reduce over time as the BLM should start to allow for the changes in strategic allocations.

Q33: What is your preferred proposed approach to step 1: option 1 or 2? Why?

On balance our preference is for option 1 as it allows for the FLM to reflect changes in strategic asset allocation that may not be captured in recent BLM. However, parameters should be put in place to reduce the overreliance and misuse of FLMs.

In addition to the parameters mentioned in Q31, thought should be given to the extent to which non-value for a cohort can be overridden. For example, an arrangement that appears not to deliver value for the at-retirement YTR cohort can conclude that overall value is delivered if there is a negligible number of members in the non-value cohort. While there may not be a significant proportion of these members, they are still an important group to consider given they are those close to accessing their savings and crystallising the returns and perceived value of the arrangement.

Q34: Do you agree with the proposed use of FLMs in step 1, alongside BLMs? Or should FLMs be considered in a different way in the assessment process?

As above.

Q35: Do you agree with the proposed approach to considering service value in step 2? Why or why not?

Now that the 'value delivered from services' metrics have been reduced significantly, the approach is reasonable. The metrics are so limited that it would be hard to justify increasing the value rating on these alone. However, this does mean that the whole assessment is largely a performance test as opposed to an overall value assessment.

We would like to see this position change and for more services to be assessed and included in the assessment over time. If the current proposed process continues then this could disincentivise spending on services in a bid to reduce costs.

Q36: Do you agree with the proposed approach to considering overall value in step 3 and rationalisation? Why or why not?

The proposed process appears sensible. We are pleased that consideration of special features and characteristics can be given and that wider context can be given to the overall rating.

However, thought should be given as to how far the rationalisation step can improve the assessment and what oversight will be in place. The framework allows for judgement-based overrides, but it is unclear who will scrutinise whether these are justified, consistent and evidence-based. Without a formal check, ratings could drift, become politicised, or vary materially between assessors.

Q37: Do you agree with the proposed updated RAGG ratings? Why or why not?

A four-point RAGG structure is a step forward, but the current design creates material risks unless the framework is tightened, the use of overrides is properly governed, and the regulatory consequences of each rating are reconsidered.

Where the proposal improves on the current system

- The extra category gives a clearer separation between schemes that are genuinely strong and those that are simply adequate.
- It should help highlight where intervention is needed without forcing everything into a binary pass/fail outcome.

Where the proposal creates significant risks

- **No clear oversight of overrides.** The framework allows for judgement-based overrides, but it is unclear who will scrutinise whether these are justified, consistent and evidence-based. Without a formal check, ratings could drift, become politicised, or vary materially between assessors.
- **Amber as drafted would make master trusts commercially unviable.** An amber rating would effectively stop new business and trigger outflows as employers and advisers avoid the reputational and regulatory risk. For master trusts, which rely on scale, this would rapidly undermine financial sustainability.

- **Green currently functions like an interim amber.** As drafted in the Bill, a green rating is not a stable “good” outcome but a temporary status pending further assessment. In practice, this would have similar commercial consequences to amber, again risking destabilisation of otherwise well-run master trusts.
- **Compression of outcomes remains likely.** Even with four categories, most schemes will cluster in the middle unless thresholds are objective and transparent.
- **Oversimplification risk.** A single domain rating can mask important differences (eg, strong investment outcomes but high risk or high charges).
- **Borderline volatility.** Small data movements could push a scheme across a threshold, triggering disproportionate regulatory and commercial consequences.
- **Inconsistent interpretation.** Without prescriptive guidance, schemes may apply criteria and rationalisation differently, undermining comparability.

The direction is positive, but the framework needs stronger guardrails: clear governance around overrides, transparent thresholds, and a rethink of the commercial consequences of amber and green. Without this, the system risks destabilising master trusts and creating outcomes that do not reflect underlying member value.

Q38: Overall, do you agree with the assessment process we have outlined above? Why or why not? What changes would you propose?

We agree it is important for schemes to be able to provide context and further information to support the overall rating given. We welcome the rationalisation step. However it is not clear how far the rationalisation could improve the rating given from steps 1 and 2. It is also not clear how the rationalisation / override will be assessed and monitored. This could lead to misuse of the self-assessment and in extremity undermine the whole process.

Further clarity is needed on what will be disclosed to participants and also to the market on the assessment and if the rationalisation context will also be visible.

Chapter 9 - Actions for arrangements offering poor value

Q39: Do you agree with the proposed transfer requirements for red rated arrangements? Why or why not?

We understand the rationale for introducing strengthened transfer requirements for red-rated arrangements, and we agree that members in persistently underperforming schemes should be protected and supported to achieve better outcomes. The principle of encouraging movement away from arrangements that consistently fail the VFM standards is sound and aligns with the broader objective of improving member outcomes.

However, we have some concerns about the proposed transfer requirements as currently drafted:

- **Risk of forced transfers without member-level nuance:** A red rating may arise from issues in a specific domain (e.g. governance or charges) rather than poor investment performance. Requiring transfers in all cases could disrupt members unnecessarily, particularly where the arrangement still delivers good outcomes in key areas or where the issues are already being addressed.
- **Practical challenges for schemes with complex benefits:** Certain arrangements (such as those with bespoke charging structures, employer-funded subsidies, or legacy investment guarantees) may struggle to transfer members on a like-for-like basis. Mandatory transfers could risk loss of valuable features or unintended detriment.
- **Timing and capacity pressures:** If multiple schemes receive red ratings simultaneously, the receiving providers may not have capacity to accept large volumes of transfers within the required timelines. This could create operational risk and lead to sub-optimal decisions driven by deadline pressures.

- **Employer and trustee engagement:** In many cases, red ratings will be symptoms of broader issues (such as employer decisions around subsidising costs or changing scheme design). A mandatory transfer requirement could reduce flexibility for trustees and employers to implement remediation plans that might resolve the issues without member disruption.

Overall, while we support the intention to protect members in persistently failing arrangements, we believe the transfer requirement should include **greater proportionality and flexibility**, allowing for remediation where appropriate and ensuring that transfers occur only where they are genuinely in members' interests.

Q40: Do you agree with the actions proposed for not value arrangements? Why or why not?

We agree with the principle that arrangements identified as “not value” should be required to take clear, timely action to address the issues highlighted through the VFM assessment. Strong, consistent follow-up is essential if the framework is to drive improvements and ensure members are protected. The proposed actions (diagnosing the underlying causes, producing a remediation plan, and reporting progress) are sensible and aligned with that objective.

However, we have some reservations about the proposals in their current form:

- **One-size-fits-all action requirements may be inappropriate.** Not all “not value” outcomes carry the same degree of risk or urgency. Issues relating to governance or service quality, for example, may require a different approach than those arising from persistent underperformance or high charges. A more proportionate framework would avoid unnecessary burden and support more targeted remediation.
- **Insufficient flexibility for legitimate employer- or scheme-specific circumstances.** Some arrangements have structural features (such as employer-funded administration, bespoke investment options, or legacy benefits) that may influence their VFM assessment but do not necessarily indicate poor outcomes for members. A rigid action plan could unintentionally disadvantage these arrangements or require steps that are not in members' long-term interests.
- **Risk of premature escalation to wind-up or transfer.** If the expectations for improvement are too tightly defined, schemes may feel compelled to consider wind-up or transfers before having had sufficient time to implement appropriate remediation. This could lead to unnecessary disruption, capacity constraints in the market, or sub-optimal decisions driven by regulatory timelines rather than member outcomes.

Overall, we support the direction of travel but believe the proposed actions would benefit from **greater proportionality, clearer guidance on acceptable remediation pathways, and flexibility where unique scheme features mean the standard approach may not be appropriate**. This would ensure that action requirements are robust while still allowing trustees and employers to respond in a way that genuinely improves member outcomes.

Chapter 10 - Disclosure requirements

Q41: How should firms and trustees provide data to the central VFM database? E.g machine-readable flat file, file transfer, webform, direct API etc.

The priority here must be for a fast, efficient, standardised and reliable method of data provision. Beyond that, we are neutral as to what IT solution is adopted.

However, we would ask that the system is designed to enable more than one person from a scheme to access the database, possibly with different permission levels (eg data input, sign-off, submission etc), and that the data can be loaded in stages prior to being submitted. Both of these are to improve ease of access and also to assist checking of data prior to submission.

Q42: Do you agree with our proposals for the central VFM database? Why or why not?

We believe that a central VFM database could have significant advantages over the previous proposals of VFM data being housed on diverse individual websites potentially in different layouts and formats. In comparison, a

central database could lead to more standardisation in presentation and make comparisons easier since there would only be a single location to search. These advantages could make the process more efficient.

Balancing this, it is difficult to be more optimistic about this proposal given that it is clear that your thinking on this is still at a very early stage and that in recent years, governments and other national bodies generally have a fairly poor track record when it comes to implementing large-scale IT projects.

Significant questions about the details of this proposal need to be answered including how it will be run and how schemes will interact with it.

Finally, clarity is needed about whom would be funding the proposed database: would it be central government, users of the database, an industry-wide levy, or will it come out of current FCA/ TPR funding?

Q43: When in the VFM cycle should VFM data be made publicly available and why? For example, should data be made publicly available in March or in October alongside assessments?

We agree with you that both viewpoints have merit. However, on balance we favour earlier publication in the interests of full transparency and also agree with your comment that if there is only limited access then selected elements of that data could enter the public domain, perhaps in an attempt to influence commercial decisions.

Q44: Do you have any comments on the suggestion that firm/ IGC or trustees should also add a link to the final VFM assessment report on to the proposed central VFM database?

If this can be implemented in a straightforward, low-cost and efficient manner with little additional overhead then we believe this would be beneficial.

Chapter 11 - Amendments to current FCA Handbook requirements

Q45: We would welcome further comments on our proposals relating to the FCA Handbook.

We have no comments to make here.

Q46: Do you have any comments on our updated cost benefit analysis? A new CBA will be produced in the next consultation phase, incorporating further feedback and any substantive market or policy changes.

We have no comments to make here.

Conclusion

We hope our comments are useful. We would of course be very happy to discuss further any of our comments in detail with you.

Yours sincerely

{By email only 8 March 2026}

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