



Institute
and Faculty
of Actuaries

So What does 'Value for Money' Really Mean in Pensions?

Jenny Sugiarto, KPMG and Sandy Trust, Prudential

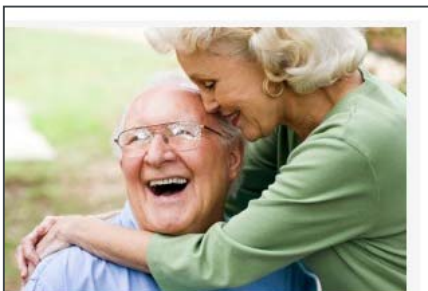
10 November 2014

Outline

- Introduction
 - Defining value for money (VfM)
 - VfM in other sectors
 - Assessing VfM in pensions
 - Practical challenges
-

Introduction

Do old people have enough money?



Happy elderly couples, such as this one, are more likely to lead longer, healthier lives, according to a study.

Source: <http://maryvezzetti.com/blog-mary-vezzetti/>

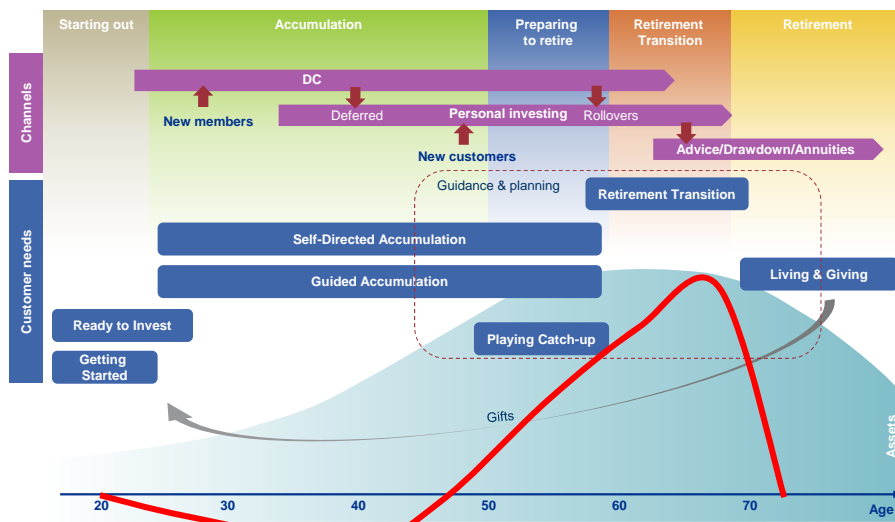


Living on a low income in later life

Living on a low income in later life is very hard work. Every penny has to be watched. Shopping lists have to be kept to. Money has to be saved for bills. There is no room for luxuries.

Source: <http://www.ageuk.org.uk/money-matters/income-and-tax/living-on-a-low-income-in-later-life/>

We think so and so don't save enough



This troubles the powers that be...



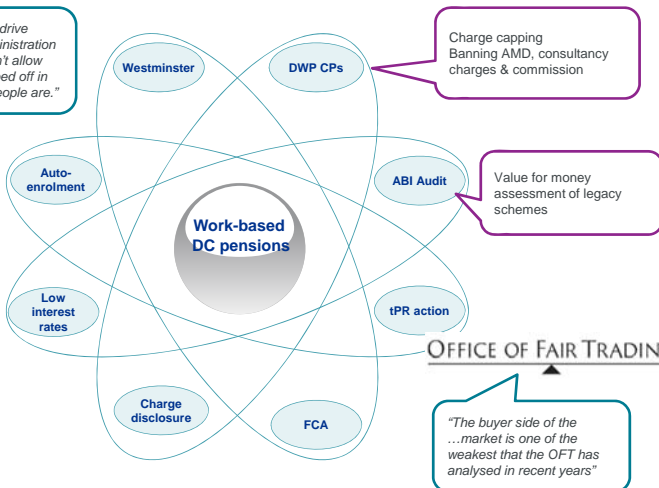
And so the pressure is intense



"We have got to drive down these administration charges. We can't allow people to be ripped off in the way some people are."



"ever more inventive ways of extracting money from their clients"



Defining VfM

Value for money is a personal concept

- OED: “The *worth* of something *compared to the price paid* or asked for it”



It is good value for money

I expected more for the price

Having read the reviews, I expected more

- So how to apply the concept to the world of pensions...a long term product with fewer comparatives
-

What is VfM?

OFT: *the scheme charges a member has to pay and the quality of the scheme*

FCA (CP14/16):
...involves **weighing the quality of the scheme against its cost to members.**

NAO: *does not always mean choosing the immediately cheapest option*

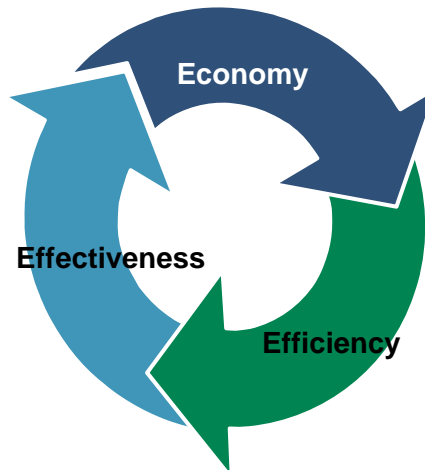
TPR: ... **it does not necessarily have to be low cost, provided higher costs can be justified by higher benefits**

VfM is not....

Only meeting minimum standards	X
Low profitability	X
Equity	X
Good customer outcomes	?

VfM in Other Sectors

VfM Indicators: Example from Higher Education (HE)



VfM Assessment involves judgement

“At the end of the day, all VfM assessments entail some numbers, and some judgement – based on the data provided.”¹

Assessment may involve “working down the value chain”



¹ Indicators and VfM in Governance Programming, DFID, July 2011

VfM Reporting: HEFCE Analysis of HE

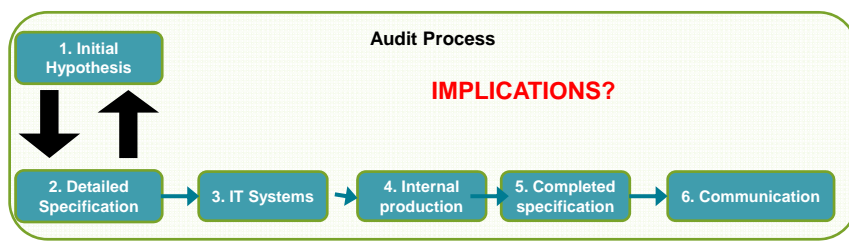
- Significant variation in reports by institution
- Positive aspects include:
 - Mix of qualitative and quantitative information
 - Broad coverage of reports
 - Inclusion of cost and quality information
- Opportunity to improve in areas including:
 - Supporting evidence on what has been achieved
 - Too much focus on one specific type of saving (procurement)
 - Analysis and conclusions of information given

Source: Higher Education Funding Council for England, Analysis of value for money annual reports submitted to HEFCE by English higher education institutions, March 2013

Assessing VfM in Pensions

The ABI/OFT Audit Approach

- Member level calculation, data onerous and not trivial
- Quantitative only approach – calculate RIY based on charges – to identify ‘At Risk’ schemes, 1% level
- No consideration of benefits and implications unclear (report expected in December 2014)

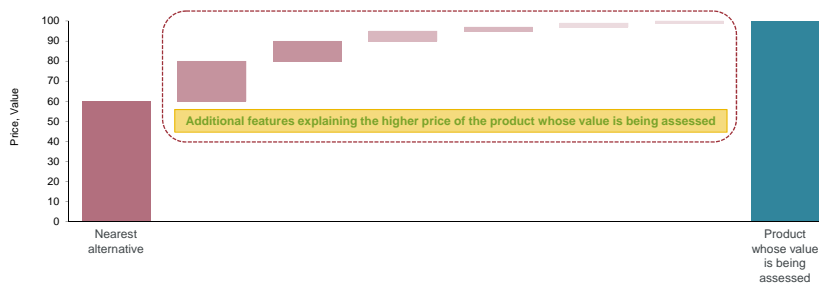


What to take into account?

- | | |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • FCA – “Weighing the quality of the scheme against the cost to members” • Quality <ul style="list-style-type: none"> – design and execution of the investment strategy – administration of the scheme including communication with members, and – governance of the scheme, including regular assessment of its value for money. • Costs <ul style="list-style-type: none"> – costs and charges for scheme and investment administration, and transaction costs | <ul style="list-style-type: none"> • TPR – 6 DC Principles (underpinned by 31 quality features) <ol style="list-style-type: none"> 1. Essential Characteristics “Schemes designed to be durable, fair and deliver good outcomes” 2. Establishing Governance “Comprehensive scheme governance” 3. People “fit and proper people” 4. Ongoing governance and monitoring 5. Administration 6. Comms to members “Communication is designed to ensure members are able to make informed decisions about their retirement savings” |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

Value-based pricing

- The value of a product to consumers is typically positively related to the benefit to the consumer and negatively related to its price
- Value-based pricing is one pricing strategy available to firms
- It consists of (i) identifying the 'nearest alternative' and of (ii) explaining how the product's features may justify any price gap



Practical challenges with use of nearest alternative

Numerous options

- Identify products with similar characteristics sold by other firms
- Consider other products sold by the same firm

Nearest alternative may not provide VfM

- Provider may face limited competitive constraints
- May require framework to be adapted
- Possibility is to look instead for a "competitive benchmark"

Need to include all relevant variables

- Product features may not capture all variables that drive choice and value
- e.g. investment strategies

Evaluating VfM using surveys

Firms (e.g. groceries) use a number of tools carry out peer comparison, including:

- Customer surveys, trial promotions, focus groups and monitoring competitors' prices

What could life offices do?

- Consider existing surveys evidence (e.g. DWP 2012) and run their own customer surveys (of both employers and employees)
 - Compare survey results to actual data and consider conjoint analysis
-

Evaluating VfM: Do products meet customer needs?



Hang on a minute...TCF!

- Culture of Treating Customers Fairly
 - Products & services designed to meet customer needs & targeted accordingly
 - Clear information before, during & after point of sale
 - Any advice given is suitable
 - Performance & service meet expectations and are of an acceptable standard
 - No unreasonable post sale barriers to change, switching, claiming or complaining
-

Practical challenges

Challenges - Embedding Vfm reporting

- Policy and framework
 - Risk appetite, MI, KRIs
 - Ownership in the business (part of conduct risk?)
 - Recruiting for governance structure
 - Meets regulatory (TPR, IGC, DWP – others?) requirements
 - Data – quantitative and qualitative
 - Building efficient data and reporting architecture
 - Appropriate qualitative data and metrics for assessment – whether to include customer outcomes?
 - How to blend company, scheme and member level information
-

Challenges - Whole-life costing

Certain products are consumed over a long time span

➤ Benefits and costs (including charges) may vary over the lifetime of the product

Consider mortgages:

➤ Long term product but with frequent switching (as some look every 2-3 years for the best deal at that point in time)

➤ Borrowers who do not regularly shop around may lose out

➤ BUT - if all borrowers regularly switched, it may be difficult for providers to keep offering good introductory rates to everyone

Applicable to pensions?

➤ Inappropriate to compare short term investment returns

➤ Switching is challenging for members in workplace schemes

Challenges - Level of granularity

Level	What
Provider	Governance framework, capital, servicing levels, IT infrastructure, digital capability
Product	Provides for member needs (guarantees, pension flexibility) appropriately, appropriate for scheme
Scheme	Investment strategy design and execution, member communications, member engagement, conflicts (employer vs employee)
Member	Charges levied, contributions, customer outcomes pre and post retirement

Conclusion

Regulatory cost OR customer and commercial opportunity?

- Vfm reporting is here to stay
 - But it is complex and there is a lack of clarity on approach
 - Embedding this quickly is challenging (and expensive)
 - BUT creates a rich stream of member level data
 - Allowing us to drive communication and hence engagement with our customers in an unprecedented way
 - Can we adapt and seize the opportunity to help our customers and in doing so help ourselves?
-



Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.
