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Summary

The proposals of the Pensions Commission offer a great and unique opportunity to reverse the decline in private pension provision and restore confidence in long-term savings. Stakeholder pensions have not been successful in halting the downward trend in non-State pension provision among middle income earners. If significant progress is to be made in encouraging long-term pension savings in this group, it is essential that any new pension savings vehicle is designed so as to minimise the need for financial services regulation about the suitability of the product for its target market. Success in removing the costs of such regulation depends upon a decision about the employer contribution and long-term trends in means-tested State provision for pensioners.

If this opportunity is to be seized there needs to be an integrated approach in which three pre-conditions are met. The first pre-condition is that the correct balance is struck between the role of the State in securing and promoting a new pension savings product and the sense of individual ownership. The second pre-condition is that the new product maintains the simplicity and near-universal suitability proposed by the Pensions Commission to minimise cost and the need for regulation. The third pre-condition is that reform of private pension saving takes place in tandem with a new direction in the State pension system.

1 Introduction

Pensions policy and long-term savings

1. The need to save for the long-term, and for retirement in particular, raises issues of fundamental importance for individuals and for public policy. The capacity to meet that need profoundly affects the welfare of the individuals concerned and their families, as well as the sustainability of the public finances. In 2004 the then Treasury Committee drew attention to the fact that "confidence in savings and the savings industry is at a low ebb".[1] Our predecessors explored factors that would affect prospects for restoring that confidence, including marketing practices and costs in the long-term savings industry, the role of financial services regulation and the impact of tax and benefit policies.

2. Pensions provide the cornerstone of long-term savings. A possible way forward for private and public pension provision has been mapped out in the work of the Pensions Commission chaired by Lord Turner of Ecchinswell.[2] The Commission was an independent body established following the Pensions Green Paper in December 2002 with a remit

> to keep under review the regime for UK private pensions and long-term savings, and to make recommendations to the Secretary of State for Work and Pensions on whether there is a case for moving beyond the current voluntarist approach.[3]

The Commission published its First Report, which set out the challenges society faced and the choices that needed to be made, on 12 October 2004.[4] The Commission's Second, and most substantial, Report, which contained recommendations for new policies relating to private and public pensions, was published on 30 November 2005.[5] On 4 April 2006, the Commission published a third and final Report commenting on specific issues which had arisen in the debate on pension reform since publication of the Commission's Second Report.[6]

Our inquiry

3. At the beginning of March we announced our intention to conduct an inquiry into the design of the National Pension Savings Scheme and the role of financial services regulation. We indicated that we would particularly be concerned with exploring factors affecting the costs of any pension measures arising from the proposals in the Second Report of the Pensions Commission for a National Pension Savings Scheme, the regulation of such

1 Treasury Committee, Eighth Report of Session 2003–04, *Restoring confidence in long-term savings*, HC 71-I, para 1

2 The other members of the Commission were Jeannie Drake and John Hills.

3 *Pensions: Challenges and Choices: The First Report of the Pensions Commission*, October 2004 (hereafter *Pensions: Challenges and Choices*), Executive Summary, p 1

4 *Pensions: Challenges and Choices*

5 *A New Pension Settlement for the Twenty-First Century: The Second Report of the Pensions Commission*, November 2005 (hereafter *A New Pension Settlement*)

6 *Implementing an integrated package of pension reforms: The Final Report of the Pensions Commission*, April 2006 (hereafter *Implementing an integrated package*)

measures, the roles of the Financial Services Authority and the Treasury, and lessons from Stakeholder pensions. We decided to conduct a short, focused inquiry with a view to reporting to the House of Commons prior to the publication of the Pensions White Paper, which is expected by the end of May.[7] We heard oral evidence from Which?, Mr Ned Cazalet of Cazalet Consulting, the Investment Management Association (IMA), the Association of British Insurers (ABI), the National Association of Pension Funds (NAPF), the Financial Services Authority (FSA) and Lord Turner. We also received a range of written evidence which will be published alongside the oral evidence in Volume II of this Report.[8] We are grateful to all those who assisted the Committee in the course of this inquiry.

4. The reports of the Pensions Commission cover a very broad canvas. Many of the issues relating to pensions reform are being examined in a wide-ranging inquiry by the Work and Pensions Committee of the House of Commons.[9] Our own inquiry has concentrated on the issues surrounding the National Pension Savings Scheme and the other models that have been proposed for further private pension provision, including issues of cost and regulation. We have not sought to take evidence on the costs and merits of particular policy measures relating to pensionable age, the level of Basic State Pension and the operation of Pension Credit. We do examine the interaction between the various proposals for further private pension provision and possible future trends in relation to public pension provision.

7 HC Deb, 8 May 2006, col 1

8 For a list of memoranda in Volume II, see p 41

9 For further information on which, see www.parliament.uk/workpencom.

2 Recent trends and future prospects

Private pension provision

Introduction

5. The Pensions Commission's starting point for its proposals is the contention that pensions policies over many years have been founded on a false prospectus. The Commission observed that the State has been planning to play a reduced role in pension provision for the average pensioner, a policy "based on the assumption that private provision will grow to offset this decline".[10] Successive Governments have seen rising voluntary provision as an opportunity to contain public expenditure in the face of the demographic challenge.[11] The reality has been somewhat different, characterised in Lord Turner's words by an increasing number of people on or around middle incomes "not making any provision on top of the State pension, while the State simultaneously is planning to do less for them".[12] Far from growing, voluntary private pension provision "is in serious and probably irreversible decline".[13]

Occupational pensions

6. This decline is most apparent in the occupational pensions sector. Ms Christine Farnish, Chief Executive of the NAPF, told us that, for the last half century, most people in the United Kingdom saving for a pension have saved through a defined benefit (DB) scheme—in which payments in retirement are not directly dependent on individual contributions—sponsored by an employer, where the only decision for the employee has been whether or not to join the scheme. This system, according to Ms Farnish, is "dying around our ears".[14] The Pensions Commission has also referred to a "rapid retreat from DB provision".[15] An estimated 54% of DB occupational schemes closed to new members between the end of 2001 and the end of 2004. By October 2005, only 24% of FTSE 100 companies offered DB schemes to all new employees and 67% did not offer DB schemes to any employees.[16]

7. The causes of this general decline were analysed by the Pensions Commission in their initial Report. That analysis highlighted the reasons for the increased costs of DB final salary pension schemes, costs which were partially disguised by the long bull market in equities of the 1980s and 1990s. The finances of such schemes were also affected by major tax decisions—the removal of tax-exempt status for certain surpluses in 1986 and the dividend tax changes of 1997. The "over-optimistic" assumptions of successive Governments and of employers about the sustainability of long-term returns were then

10 *A New Pension Settlement*, p 2

11 *Ibid*, p 42

12 Q 195

13 *A New Pension Settlement*, p 2

14 Q 66

15 *A New Pension Settlement*, p 54

16 *The Pensions Regulator: Medium Term Strategy*, April 2006, p 13

exposed by the bear market of the period from 2000 to 2003.[17] Lord Turner told us that there has been "a collective fool's paradise", leading to employers' contribution holidays and tax changes "all of which ... with foresight, if you could roll back the clock, you would not have done".[18]

8. The Commission has noted that the rapid decline of DB schemes has "severely exacerbated the gaps that have always existed in Britain's pension system" and increased the inequality in pension provision.[19] Public sector employees account for 18% of all employees, but 36% of all accrued pension rights and funds. There are many high income members of "top hat" defined contribution (DC) schemes in the private sector which pay far higher contribution rates than members of ordinary schemes enjoy.[20] Inequality is often a feature within companies, with an employee in a DB scheme receiving pension promises twice as valuable as those available to another employee doing an identical job but who joined after a DB scheme was closed to new members.[21]

The wider problems of private pensions

9. The weaknesses of private pension provision are by no means confined to those arising from the declining quality and quantity of occupational pension coverage. As the Pensions Commission has observed, "initiatives to stimulate personal pension saving have not worked"; they have also noted that "barriers of inertia and high cost" have deterred voluntary private pension provision.[22] The lack of growth in this market is attributable in considerable measure to three closely linked issues—the weakness of the commission-driven model, the mis-selling scandals of the 1990s and the development of regulation.

10. The problems of the commission-driven life office business model were recently highlighted when Mr Trevor Matthews, Chief Executive of UK Life and Pensions at Standard Life, stated that "our basic business model is flawed".[23] Mr Ned Cazalet of Cazalet Consulting has also cast doubt on the viability of this model.[24] He told us that this model relied on the payment of commission to intermediaries for new sales, which gave those intermediaries an incentive to move business from one provider to another, a process which generated costs to providers without creating new business. He estimated that, in four years, insurance companies had spent about £17 billion trying to obtain pensions business, with little to show for it except business moved from one company to another before it could become profitable. Mr Cazalet thought that "this model is economically defunct ... crazy ... hugely loss-making and ... unsustainable".[25] As our predecessors

17 *Pensions: Challenges and Choices*, pp 121–124

18 Q 221

19 *Pensions; Challenges and Choices*, p 125; *A New Pension Settlement*, p 60

20 *A New Pension Settlement*, pp 60, 62

21 *Ibid*, p 60

22 *Ibid,* pp 2, 4

23 *The Scotsman*, 5 March 2006

24 *Polly Put the Kettle On: Pensions Profitability*, Cazalet Consulting, January 2006

25 Qq 36, 51, 63

observed in 2004, the commission-driven distribution model creates a "negative image ... in the eyes of some potential savers".[26]

11. The commission-driven model contributed to what the Pensions Commission has characterised as "a misguided attempt to extend personal pensions to segments of the market where the economics only appeared to work in periods of exceptional capital return".[27] The private pension market suffered both directly and indirectly from its association with the mis-selling scandals of the 1990s. As Lord Turner observed, "twenty years ago we did not call what [independent financial advisers] do 'advice'. We called it 'sales'." He noted that a sales force remunerated by commission "might tend to sell things which were not in people's interests".[28]

12. The combination of a seemingly flawed business model and advice which had leanings towards a particular outcome led to a rapid growth in regulation of advice. In 2004, our predecessors expressed the view that the FSA had delivered a significant improvement in the regulatory framework and concluded that "the current low level of confidence in the financial savings industry is in large part a reflection of the weak regulatory framework and inappropriate industry practices" that preceded the FSA.[29] However, as Lord Turner noted, regulatory changes in recent years have "added an enormous amount of cost".[30]

13. In 2004, the then Treasury Committee concluded that "the bear market has exposed a catalogue of problems and scandals that has left a large body of savers feeling disillusioned with the long-term savings industry".[31] That view was partially echoed by the Pensions Commission, which has observed that "many do not trust the financial services industry to sell good value products".[32]

14. Recent years have seen a diminution in the willingness or capacity or both of employers to take the lead in the making of adequate pension provision for employees. The leading providers of non-occupational private pensions have been ill-equipped to take up the slack. The combined result has been a dramatic growth in the numbers in the private sector workforce who do not contribute to a non-State pension, from just over 8 million in 1996–97 to nearly 12 million in 2004–05.[33] As Lord Turner concluded, "the private pension system, far from growing to fill the gaps left by the State ... is actually doing less".[34]

26 HC (2003–04) 71-I, para 38

27 *A New Pension Settlement*, p 28

28 Q 211

29 HC (2003–04) 71-I, para 77

30 Q 211

31 HC (2003–04) 71-I, para 110

32 *A New Pension Settlement*, p 27

33 *Implementing an integrated package*, pp 12–13

34 Q 220

The case of Stakeholder pensions

15. The failings of the private pension system in recent years are exemplified by the experience of Stakeholder pensions, which were introduced in 2001. These were foreshadowed in a Pensions Green Paper in 1998 which stated:

> People in middle incomes want to save more for retirement, but current pension arrangements are often unsuitable or expensive. Our new secure, flexible and value-for-money Stakeholder pension schemes will help many middle earners to save for a comfortable retirement.[35]

"Middle earners" were defined as those earning between £9,000 and £18,500 a year.[36]

16. Stakeholder pensions involve a DC scheme with compulsory minimum standards. Employers with five or more staff who do not offer occupational pensions are required to provide access to a Stakeholder scheme if they have one or more relevant employees. Stakeholder pensions are intended to be flexible and portable, with no penalty charges for transfers in and out, freedom to vary contributions and quite small contributions permitted.[37] Stakeholder pensions are sold mainly through financial advisers, either direct to consumers or through the workplace. There is a wide choice of Stakeholder pension product providers with different service and product propositions, and a vast choice in investment funds.[38]

17. Stakeholder pensions have from the outset been faced with uncertainties about the extent to which they can be sold without regulated advice, not least because of the complex interaction between occupational and personal pensions.[39] Following a Government decision in 2004, the FSA has now introduced a Basic Advice regime for the regulation of advice on the sale of Stakeholder products, although there remain several ways in which Stakeholder pensions can be sold, including through a full advice process.[40] Significant concerns persist amongst providers about the limited impact of Basic Advice, the general regulation of sales and the costs such regulation entails.[41]

18. One of the central founding principles of the Stakeholder pension was that there would be a limit on the Annual Management Charge (AMC) that could be levied, alongside prohibitions on certain other charges. The cap on the AMC was initially set at 1%, which providers claimed prevented effective promotion and distribution of Stakeholder pensions.[42] In 2004, the Treasury announced that, for people joining a Stakeholder scheme on or after 6 April 2005, the cap would be 1.5% for the first ten years, reducing to 1% for subsequent years for those remaining in the scheme. The then Financial Secretary to the

35 *A new contract for welfare: Partnership in Pensions*, December 1998, Cm 4179, Department of Social Security, p 47

36 *Ibid*, p 3

37 Ev 128

38 Ev 124

39 *Medium and Long-Term Retail Savings in the UK: A Review*, HM Treasury, July 2002 (hereafter *Sandler Review)*, paras 5.78–5.81

40 HC (2003–04) 71-I, para 65; Ev 124

41 Ev 68, 105, 108

42 HC (2003–04) 71-I, para 68

Treasury told our predecessors in 2004 that the increase of 50 basis points was a "charge explicitly for advice".[43]

19. Mr Cazalet suggested that the increase in the charge cap was actually used to pay more commission to intermediaries.[44] This view appears to be supported by Standard Life, who observed that "providers rationally offered intermediaries as much commission as they could afford within the confines of the charge cap".[45] Standard Life also backed up Mr Cazalet's contention that Stakeholder pensions remain an uneconomic proposition for providers.[46] Mr Mick McAteer, Policy Adviser at Which?, contended that the industry had wished to see the price cap increased to make money at the higher end of the market, not in order to extend reach among those on average earnings or below.[47]

20. In the early stages of the life of the Stakeholder pensions there were some signs of success in reaching the target market of middle earners.[48] However, in 2003 the Department for Work and Pensions provided little evidence of take-up or interest in Stakeholder pensions among middle earners who did not have an existing private pension.[49] Although the number of holders of Stakeholder pensions exceeded 1 million by late-2002, many of these new pension arrangements seem to have arisen from individuals switching from other schemes (notably personal pensions) and from existing Group Personal Pensions being reconstituted as Stakeholder pensions.[50] Since 2002, the number of new contracts has declined year on year.[51] Independent research suggests that private pension coverage has fallen among the target group of middle earners. There has been some increase in use by low or non-earners, but this is probably an attempt to utilise the tax benefits by the spouses of high earners.[52] Analysis by the Pensions Commission suggests that "at income levels below £20,000 it is difficult profitably to sell pensions at the present charge cap".[53]

21. **One of the starting points for consideration of proposals by the Pensions Commission and of rival proposals must be the realisation that Stakeholder pensions have not been successful in halting the decline of non-State pension provision among middle earners. Indeed, a combination of sales approaches, commission incentives, regulatory requirements and decisions about the charge cap have created a position in which Stakeholder pensions are seen as uneconomic to both providers and potential customers among the original target market of middle income earners. The lessons**

43 HC (2003–04) 71-I, para 70; Ev 128

44 Q 36

45 Ev 84

46 *Polly Put the Kettle On*, p 27; Ev 84

47 Q 52

48 *Sandler Review*, para 5.70

49 *Pensions 2002: Public attitudes to pensions and saving for retirement*, Department for Work and Pensions, Research Report No. 193, p 71

50 W Chung, R Disney, C Emmerson and M Wakefield, *Public policy and saving for retirement: Evidence from the introduction of Stakeholder Pensions in the UK*, Centre for Policy Evaluation, The University of Nottingham, Working Paper 5/05, December 2005, p 3

51 Ev 124

52 *Public policy and saving for retirement*, pp 4, 9, 17, 26

53 *A New Pension Settlement*, Appendices, p 228

from this process must be learned in taking forward proposals arising from the work of the Pensions Commission. We have sought to draw out these lessons in our ensuing conclusions and recommendations.

Public pension provision

22. A table in the Second Report of the Pensions Commission indicates that, in the coming years, United Kingdom public expenditure on pensions and assistance for those aged over State Pension Age is likely to be towards the lower end of plans of the European Union fifteen.[54] Lord Turner stressed that there was a "good news" component to this fact, because "we do not face the problems of fiscal sustainability that most of continental Europe faces" and "we have the most developed system of voluntary pension saving in the world".[55] However, he also pointed out that, even were the proposals for State pensions in the Commission's Report to be implemented, the United Kingdom would still be left "with one of the meanest and most basic State pension systems in the OECD".[56]

23. Lord Turner emphasised that this meanness reflected the deliberate policy of British Governments for the last 30 years, following the decision in 1981 to decouple the indexation of the Basic State Pension from earnings and increase it in line with prices.[57] If this policy of the last twenty-five years were to be maintained for the next forty-five years, the value of the Basic State Pension in relation to earnings would be expected to decline markedly.[58]

24. Since the late 1990s the Government has sought to combat pensioner poverty through a Minimum Income Guarantee linked to earnings rather than prices. Since October 2003 the guarantee element has formed part of the Pension Credit, the second component of which is a Savings Credit linked to prices intended to reward pensioner households which saved for their retirement. According to the Government, "concentrating resources on the poorest pensioners has ensured that between 1996–97 and 2004–05 over one million pensioner households were lifted out of relative low-income poverty and 2.1 million pensioner households have been lifted out of absolute low income poverty".[59] At the same time, the effect of these changes, including the operation of the Savings Credit, has been to increase the proportion of pensioner benefit units subject to means-testing. The change also results in high tax credit withdrawal tapers. These may be related to the increase in the number of households facing relatively high marginal tax rates. In our Report on the 2006 Budget, we noted that, since 1998, there has been a reduction in the number of households facing the highest marginal deduction rates of 70% or more, although the number of households facing marginal deduction rates in the region of 60% to 70% has increased.[60]

54 *A New Pension Settlement*, p 119; the table also appears on page 185; no information is published relating to Portugal.

55 Q 220

56 Q 194. See Q 223 for a qualification in relation to medium income countries within the OECD.

57 Q 218

58 *A New Pension Settlement*, pp 28–29

59 *Budget 2006: A strong and strengthening economy: Investing in Britain's future*, HM Treasury, March 2006, HC (2005–06) 968, p 109

60 Treasury Committee, Fourth Report of Session 2005–06, *The 2006 Budget*, HC 994-I, para 85

The trends relating to means-testing and tapers are expected to continue were the policies on indexation of recent years to be maintained.[61]

61 *A New Pension Settlement*, pp 142, 294

3 The Commission's proposals and other options

The National Pension Savings Scheme

25. Having identified the main weaknesses of State and private pension provision in the United Kingdom, the Pensions Commission makes proposals to remedy those weaknesses. The Commission seeks to remedy the failings of the private pension savings market by the establishment of a new long-term savings vehicle. The Commission builds on the insight of the Sandler Review that "the inherent tendencies toward complexity in the savings market, and the consequent need to regulate the sales process, have made it uneconomic for the industry adequately to serve lower-income consumers",[62] an insight which remains valid today, in part because of the experience of Stakeholder pensions. The Commission's proposals are not intended for the lowest earners, who are protected to some extent by current State provision.[63] Equally, those proposals are designed to exclude those with employers that offer better provision than that proposed.[64] Lord Turner told us:

> The key concern is not the public sector nor the very largest companies, which will tend to provide pensions, but the broad swathe of people of average earnings working for small and medium enterprises where it is very costly to get them on an individual basis and where employers on the whole are retreating from their historic role in pension provision. If I had to have one archetype that we are thinking about, it is the person on average earnings, £22,000 a year, working for a 20- to 50-man firm. It is about how to get saving opportunities to that person. That is the middle of the range we are most worried about ... It will be targeted at those on average earnings, a bit above and a bit below. I think it will be targeted at the broad swathe of middle Britain.[65]

26. The Commission proposes to target these people through a new National Pension Savings Scheme (NPSS), which is intended to be a low cost, national DC pension saving scheme into which employees aged 21 and over without better occupational schemes would be automatically enrolled, with a right to opt out. The minimum contribution in respect of individuals in the scheme would be 8% of gross earnings between the Primary Threshold (currently £5,035) and the Upper Earnings Limit (currently £33,540). This would be composed of an employee payment of 4% of post-tax pay, effective tax relief or tax credit at around 1% and a matching employer contribution of 3%. The employer contribution would be compulsory where the employee remained auto-enrolled and made individual contributions, and it is estimated by the Commission that the compulsory contribution would add about 2% to the cost of employing the median earner.[66] Both

62 *Sandler Review*, p iv

63 *A New Pension Settlement*, p 62

64 *Ibid*, pp 36, 362–364

65 Qq 194–195

66 *A New Pension Settlement*, pp 7, 36, 355–356. The figures for the Primary Threshold and the Upper Earnings Limit are those for 2006–07, not those for 2005–06 given in the Second Report of the Pensions Commission: see www.hmrc.gov.uk/rates/nic.htm and www.hmrc.gov.uk/rates/it.htm.

employees and employers would be able to make additional, voluntary contributions up to a cash limit of twice the minimum contribution in respect of eligible employees, about 16% of relevant earnings.[67] The individual accounts created by contributions in respect of each participant would be managed by a single national body, probably established by statute for that purpose.[68] There would be a range of investment options available, but these would be limited in number and there would be a default fund available.[69] The rules on decumulation, including the broad requirement to convert amounts saved into an annuity, would be the same as for other pension schemes.[70]

27. The costs of the Scheme are intended to be kept markedly below the overall costs of existing market alternatives by three main factors. First, the national organiser of the Scheme would be the "bulk buyer" of administrative services and fund management in existing, competitive markets.[71] Second, the competitive sales process, with associated commissions, would be removed from the exercise. Third, it is intended that participation in the Scheme could be promoted and secured without the regulated advice which is required for many products in the competitive savings market. Lord Turner told us that this last approach built on the fact that individual decisions were already taken in the occupational pension scheme environment without regulated advice:

> What we have essentially designed in the NPSS is a very large, multi-employer defined contribution occupational scheme; we have simply taken a set of existing procedures that work in many companies in the occupational scheme arena and designed the system where they can also work for small companies.[72]

State provision

28. The Pensions Commission also makes proposals for reforms to the State pension system to underpin private saving. The Commission analyses the two-tier system as it has developed over the last twenty-five years, with various changes to the State Second Pension and its precursors and a Basic State Pension linked to prices, and concluded, in Lord Turner's words, that "British pension policy ... has been doing two things badly rather than one thing well. We have been doing a Basic State Pension which is getting more and more mean, and an earnings-related pension which has been salami-sliced so many times that nobody understands it."[73] The Commission's aim is to return over time to "focusing on doing one thing well, which is flat-rate pension provision".[74] There are five main components to the Commission's proposed reforms of State pensions:

67 *A New Pension Settlement*, pp 358, 360

68 *Ibid*, pp 37, 402–403

69 *Ibid*, pp 372–378

70 *Ibid*, p 37

71 *Implementing an integrated package*, p 10

72 Q 211

73 Q 223

74 *Ibid*

- to build on the current two-tier system and recent reforms by accelerating the evolution of the State Second Pension to a flat-rate pension by freezing the Upper Earnings Limit for accruals to that Pension in nominal terms;
- to index the Basic State Pension to average earnings growth in the long-term, "ideally starting in 2010 or 2011 as the public expenditure benefit of the rise in women's State Pension Age begins to flow through";
- to raise the State Pension Age gradually, broadly in proportion to the increase in life expectancy, for instance to 66 by 2030, 67 by 2040 and 68 by 2050;
- to maintain the reductions in pensioner poverty achieved by Pension Credit, but limit the spread of means-testing by freezing the maximum level of Savings Credit payments in real terms (which implies that the lower Savings Credit threshold increases faster than in line with average earnings); and
- to base future accruals to the Basic State Pension on an individual and universal basis—linked to residency—and improve carer benefits within the State Second Pension.[75]

The Commission forecasts that public expenditure on State pensions and pensioner benefits would rise from 6.2% of GDP in 2005 to between 7.5% and 8.0% by 2045 if its proposals were implemented.[76]

The rival options

29. Following the publication of the Second Report of the Pensions Commission, responses have focused particularly on the desirability and deliverability of the NPSS. Several rival options to that Scheme have emerged. There has been less extensive debate on the proposed reforms to the State system. Alternative proposals in this area "have come almost entirely from interest groups and experts who believe that the Commission should have argued for more radical and more rapid action to improve the generosity of the State pension, to simplify it, and to make it less means-tested, even if this implied a much more significant increase in the percentage of national income devoted to State pension expenditure".[77] For example, the Pensions Reform Group, led by the Rt Hon Frank Field MP, has proposed a Universal Protected Pension which would involve a higher Basic State Pension than proposed by the Pensions Commission and entail compulsory contributions for all in work. Lord Turner told us of some of his concerns about these proposals.[78] We have not considered the merits of these proposals by the Pension Reform Group, which go beyond the remit of our inquiry.

30. The first main option proposed as an alternative to the NPSS has been presented by the NAPF. Their proposal would involve the establishment of a number of Super Trusts run to protect the interests of members and with individual accounts for each member. The contribution levels and auto-enrolment arrangements of the NPSS would be reflected in

75 *A New Pension Settlement*, p 21

76 *Ibid*

77 *Implementing an integrated package*, p 14

78 Ev 127; Q 222

the provisions for the Super Trusts. Employers who did not offer a superior scheme would be obliged to join a Super Trust, but the choice of Trust would be for the employer not the employee, who would also be constrained in choices relating to asset allocation. The NAPF is not wedded to a particular number of Super Trusts, although management charges would be expected to rise with a greater number of such Trusts.[79] Ms Farnish told us that the NAPF's approach would "be a more evolutionary one ... to build on more of what we already have".[80]

31. The second model proposed as an alternative to the NPSS is the ABI's concept of "Partnership Pensions". This seeks to build on the existing retail market model, but with many of the costs associated with the competitive market, including commission, marketing expenditure and the costs of regulated advice, removed.[81] The levels of minimum contributions in respect of employers and the arrangements for auto-enrolment would be carried forward from the NPSS proposals, but there would be a range of competing, licensed providers. The choice of insurance company provider would be primarily driven by employers, but with the possibility of individual choice override. Where the employer or employee did not choose a provider, one would automatically be allocated on the basis of a "carousel" similar to that already operating in respect of Child Trust Funds. There would be a wide range of asset choices. The ABI envisages a new economic regulator—the Retirement Income Commission—to monitor and promote the new system, and license providers.[82] As with the NAPF proposals, those of the ABI seek to build on the experience and expertise of current market participants.

32. In their written evidence to us, the Treasury and the Department for Work and Pensions stated that they were also considering a further model, which would use a national clearing house to manage and deliver the enrolment, reconciliation and collection functions, but with a competing market of pension providers.[83] Lord Turner told us that he had not discussed this model in detail with the Department for Work and Pensions, but he viewed it as closer to the retail model with competing insurance companies advocated by the ABI than to the wholesale model that he was advocating.[84]

Towards a consensus on auto-enrolment

33. Endeavours to promote long-term saving up to and including Stakeholder pensions have relied on a voluntary approach. Both the NPSS and the rival options proposed by the ABI and the NAPF involve a substantial move away from voluntarism towards automatic enrolment, but stopping short of compulsion, so that an individual employee stands to be included in a national system, but has the freedom to opt out.[85] The Pensions Commission, in their final Report, noted that

79 Ev 50; *Implementing an integrated package*, pp 28–31

80 Q 100

81 Qq 64, 189, 191

82 Ev 106; *Implementing an integrated package*, p 29; Q 73

83 Ev 127

84 Q 189

85 Q 210

> there is general agreement that without automatic enrolment it will be impossible to increase pension participation rates significantly or to reduce the costs of pension saving via the elimination of regulated advice costs.[86]

Lord Turner told us that he was generally satisfied with the response to the Commission's proposals, and particularly with the "very considerable across-the-board support for … the principle of automatic enrolment rather than going with either full compulsion or leaving it to entire voluntarism … as the appropriate way forward".[87] **The Pensions Commission is to be congratulated for bringing about a broad consensus in favour of auto-enrolment as the basis for securing a major advance in the level of private pension saving among middle earners. A move to auto-enrolment is an essential precondition if the NPSS or any rival option is to be implemented.**

86 *Implementing an integrated package*, p 16

87 Q 186

4 The suitability hurdle

An integrated package

34. The Pensions Commission has stressed that the main proposals in its Second Report represented an integrated package. In that Report, the Commission described its proposals for reform of the State system and for the creation of the NPSS as "complementary".[88] In its final Report, the Commission goes further. It notes that the policies implemented must form "a coherent and integrated whole" and clearly recognise "the interconnections between State system design and private pension policy".[89] Having identified the four key dimensions of the proposed integrated approach—State system reform to deliver more generous, more universal, less means-tested and simpler State provision, auto-enrolment, matching employer contributions and a public role as the bulk buyer of fund management—the Commission remarks that "parallel progress on all four [is] essential for success".[90] The reasons why the Commission calls for an integrated approach become particularly apparent when consideration is given to the regulatory requirements relating to the process of enrolment.

The regulatory context

35. Responding in part to past problems of mis-selling in the retail financial services market, including the provision of advice relating to the move from occupational to personal pensions, the FSA has created a considerable regulatory framework surrounding the sale of financial services products. Sales advice is regulated in various ways, and different sales regimes are available, as is demonstrated by the experience of Stakeholder pensions considered earlier.[91] The costs of regulated advice are one of the main reasons why products have proved unsuitable to those on middle or low earnings, and one of the key aims of the Pensions Commission in the design of the NPSS is to establish arrangements where auto-enrolment is appropriate without the need for individual, regulated advice because such advice entails costs which reduce the effective value of contributions significantly.

36. Some evidence we received called into question whether it would be possible and appropriate to "sell" the NPSS or a rival option via auto-enrolment without individual advice. Royal London highlighted circumstances, including those of persons moving towards retirement and of persons with sporadic patterns of earnings, where individuals might not benefit from enrolment in the NPSS.[92] It was noted by Lord Turner and the FSA that some people, particularly those with high levels of credit card debt, might be better off opting out of the NPSS or any rival scheme introduced, but it was suggested that these

88 *A New Pension Settlement*, p 133

89 *Implementing an integrated package*, p 40

90 *Ibid*, pp 10, 12

91 Para 17

92 Ev 79

considerations could be taken forward within a framework of generic rather than individual advice.[93]

37. Lord Turner told us that, "in order for the Government safely to automatically enrol people in [the NPSS or a rival proposal] and to use the power of inertia for that, we need to have a high confidence that for the vast majority of people this will clearly be a high value investment opportunity".[94] The Rt Hon John Hutton MP, the Secretary of State for Work and Pensions, made a remark in similar terms to the House on 8 May 2006:

> If we are to establish a new National Pension Savings Scheme along the lines suggested, we have to be absolutely sure that it will be safe automatically to enrol people in it, so that they will always be better off inside it than remaining outside it and relying on means-tested support from the State.[95]

38. The FSA's memorandum acknowledged the centrality of removing the requirement for individual suitability advice, and therefore regulation of such advice, to the proposals of the Pensions Commission and of the ABI and NAPF.[96] The FSA and Lord Turner agreed that two elements were of crucial importance in determining whether the high hurdle of "near universal" suitability can be jumped—the employer contribution and the reform of the means-tested supplements to the State Pension.[97]

The employer contribution

39. A crucial component of the NPSS proposal is a requirement for the employee contribution of at least 4% of post-tax earnings to be complemented by a contribution by the employer of at least 3%. This is also a feature of the NAPF and ABI models. The merits of this contribution have been keenly discussed. The CBI and the British Chambers of Commerce oppose the proposal, citing the costs which might result to business and the fact that these costs constitute a higher percentage of total labour costs for smaller employers.[98] Some employer groups, including the Engineering Employers Federation (EEF), are supportive of the concept.[99] The Secretary of State for Work and Pensions said recently:

> The judgment that we have to make in deciding whether to proceed with employer contributions is a fine one, and we must be mindful of the impact on the labour market, and particularly on small companies.[100]

40. The evidence we received reinforced the importance of that judgment. The Pensions Commission has made clear that the employer contribution is "essential" in ensuring that all participants can be certain of achieving attractive returns on their contributions, even if

93 Qq 135, 209

94 Q 188

95 HC Deb, 8 May 2006, col 7

96 Ev 122

97 *Ibid*; Qq 114, 116, 188

98 *Implementing an integrated package*, p 18

99 Ev 114; Qq 186, 187

100 HC Deb, 8 May 2006, col 7

some of them continue to be subject to means-testing in retirement.[101] The FSA confirmed to us that "provided employers are required to make compulsory matching contributions, the wisdom of not opting out of the scheme is readily apparent as consumers will gain financially from the employer contribution". The near universal suitability was partly "contingent" on employer contributions.[102] Lord Turner also told us that "the employer compulsion element is a key part of the overall architecture … We believe that is crucial to the success and to high participation rates, so we would be wary of dropping that contingent compulsion on employers".[103] **The compulsory matching employer contribution is an integral element of the NPSS and of the rival options. If there were to be no such contributions, the FSA's evidence indicates that it is unlikely that participation in the proposed scheme or schemes could be provided for without some regulated advice. With the increased costs consequent upon the need for such advice and diminishing contributions overall, it appears open to question whether a new scheme or schemes without such contributions would represent a step-change from Stakeholder pensions.**

The trend in means-testing

41. Without the reforms of the State pension system which the Pensions Commission propose and which we have summarised above,[104] the Commission estimates that the continuation of current policies would lead to over 70% of pensioner households being covered by Pension Credit by 2050.[105] Implementation of the Commission's own proposed reforms of the State system, coupled with the NPSS, is forecast by the Commission to lead to the proportion of pensioner benefit units on Pension Credit peaking at around 40% in 2015 and falling by 2050 to around 33%.[106] The Pensions Policy Institute, in written evidence to the Work and Pensions Committee, has argued that the Commission understates the current number of pensioner benefit units currently entitled to Pension Credit and therefore, "even after the Pensions Commission proposals (for State pension reform and the NPSS) have almost worked through, in 2050, the proportion [on Pension Credit] would remain in the order of 45%", rather than 33% as forecast by the Commission.[107] In response, Lord Turner expressed confidence in the Commission's figures, while acknowledging that various assumptions about the future dynamism of private pension income played a role in modelling in this area.[108]

42. The Second Report of the Pensions Commission stated that "a clear policy to prevent the future **spread** of means-testing is essential to the success and credibility of the NPSS".[109] In evidence to us, Lord Turner went slightly further, referring to the importance of

101 *A New Pension Settlement*, p 134; *Implementing an integrated package*, p 20

102 Ev 123, 122; Q 134

103 Q 188

104 See para 28

105 *A New Pension Settlement*, p 240

106 *Ibid*, p 294

107 Pensions Policy Institute, Memorandum to the Work and Pensions Committee, paras 23–26 (made available to the Treasury Committee in accordance with SO No. 137A by order of the Work and Pensions Committee, 29 March 2006)

108 Q 212

109 *A New Pension Settlement*, p 134; emphasis in original

"reducing the degree of means-testing in the State system".[110] Commenting on the apparent difference of emphasis in these statements, Lord Turner attached importance to

> a trajectory where it is going down rather than going up … The first step is to make sure that it does not grow, but ideally it should go down further than that.[111]

43. The Savings Credit component of the Pension Credit is designed to reward the savings habit amongst current pensioners and encourage it in future pensioners.[112] However, much of the evidence we received indicated that the prevalence of means-testing was vital to determining whether investment in the NPSS or a rival scheme would be worthwhile. Lord Turner told us:

> We believe that a set of changes to the trajectory of the State pension system is … important, that if we did the NPSS and did nothing on the State pension side the success of the NPSS would be undermined by people saying, 'We are being encouraged to save in a form where a lot of the money is coming out of means-testing at the other end'.[113]

44. Ms Farnish of the NAPF thought that, if there was a failure to carry through reforms to the State pension system, "then any system into which the vast majority of working people are auto-enrolled is doomed to fail".[114] Mr Dick Saunders, Chief Executive of the IMA, similarly thought that such a scheme would be a "non-runner" with means-testing at the levels currently envisaged.[115]

45. Mr Saunders noted that the NPSS was unlikely to be launched for five years and that it would be a further five to ten years before people with substantial savings as a result came to retire, giving "quite a long window in which to sort out the State pension scheme".[116] The Pensions Commission envisaged the link between the Basic State Pension and average earnings growth "ideally starting in 2010 or 2011", but acknowledged that there was "a trade-off" to be struck in deciding the starting date:

> Early implementation would be more costly at a time when public expenditure constraints are tight: later implementation makes it more important that private savings increase to compensate but, by delaying the date from which the spread of means-testing can be halted, may make that increase less likely.[117]

46. Lord Turner did not view as ideal the suggestion that the earnings link might be restored initially only for pensioners aged 75 and over, not least because of the complexity it would add to the system, but stressed the importance of clearly communicating the future policy trend and creating a continuity in policy with a cross-party consensus so that

110 Q 188

111 Q 199

112 HC (2005–06) 968, p 109

113 Q 207

114 Q 107

115 Q 108

116 *Ibid*

117 *A New Pension Settlement*, pp 21, 31

all concerned could have confidence that a framework for the future would "stick over time".[118] He considered that the NPSS could be delivered on the basis of suitability to the vast majority of people with compulsory employer contributions and "as long as we are making progress against means-testing on the State side".[119]

47. The FSA noted that "the proposed NPSS's near universal suitability is contingent on employer contributions and the reform of means-tested State pensions and without these it would be more difficult to demonstrate".[120] The FSA observed that "the fewer people affected by means-tested benefits, the more likely that saving for a pension through any NPSS that may be introduced will provide the consumer with a benefit".[121] In oral evidence, Mr Clive Briault, Managing Director, Retail Markets in the FSA, said of the reduction of means-testing:

> We are saying that we would regard that as an important element. I do not think one should over-exaggerate the impact. I think it is probably true to say that, even with a degree of means-testing, for the vast majority of employees it would still make sense to save through something akin to the [NPSS] … but clearly the greater the impact of means-testing, the greater the possibility that saving in that way would not be suitable for that individual because they may find at the end of it that they are not well off because they have lost the means-tested element because they have saved through the pension scheme, so the greater the potential impact of that, the more concerned we would be about whether or not saving in that way was likely to be suitable for all individuals.[122]

Conclusions

48. We are not concerned in this inquiry with questions about the fiscal sustainability and impact on overall pensioner welfare of particular changes to the State pension system, but with the narrower question of the impact of such changes—or the absence of such changes—on measures arising from the work of the Pensions Commission that are designed to boost pension saving among middle income earners and those just above or below average earnings. There are two dimensions to, and two timetables for, the impact of the extent of means-testing in the State system on private pension saving. As the Pensions Commission notes, there is both an actual disincentive and a "perceived disincentive" arising from the prevalence of means-testing.[123] One timetable relates to the actual impact of means-testing on the effective value of the retirement income of an NPSS account holder. The second timetable relates to the decisions by the FSA about the necessity or otherwise for an advice regime entailing detailed examination of an individual's circumstances before a decision can be reached about participation in the NPSS. This may depend in part on the FSA's assessment of public policy on means-testing.

118 Qq 214–215, 224

119 Q 211

120 Ev 122

121 Ev 123

122 Q 132

123 *Implementing an integrated package*, p 16

49. **The successful delivery of a new pension saving vehicle suitable for the vast majority of those eligible to contribute and thus not requiring regulated sales advice is contingent upon expectations about the extent and future course of means-testing for pensioners. These expectations are dependent not only on announcements expected in the Pensions White Paper, but also on the ability of present and future Governments to establish a policy framework based on a broad political consensus, together with accompanying forecasts on those eligible for means-testing, which deserve and attract the confidence of the public.**

50. One of the lessons of the development of Stakeholder pensions is that the regulatory decision-making framework is far from static. The FSA will not make a single irrevocable decision about suitability regulation: its statutory duties are likely to require it to keep a watching brief to ensure that any framework for decisions relating to suitability remains appropriate. **It is of vital importance not only that the Government establishes a long-term coherent approach to policy on private and public pension provision and communicates effectively with the FSA in relation to the FSA's regulatory requirements, but also that the Government continues to provide leadership and support to ensure that a regulatory position on suitability in relation to the NPSS or a rival option, once arrived at by the FSA, proves sustainable in the long-term.**

51. The evidence that we received on suitability, and our consideration of it so far, has concentrated on whether and how the need for individual, regulated suitability advice can be prevented. Success in this regard appears pivotal to the economics of the NPSS and the rival models. It is nevertheless also important to ensure that, in designing out such advice, the needs of potential participants in any scheme that is adopted are not neglected. Advice of a generic kind must be carefully designed to enable individuals to ensure that their circumstances are such as not to warrant opting out. Employers will provide an important avenue for, or source of, advice in many cases, but some employers will be aware of the cost implications for them of participation, and thus the cost advantages of an employee opting out. The Resolution Foundation has highlighted the importance of generic, non-regulated advice being available to assist those entering the pensions system and at other crucial stages in their pensions lifecycle.[124] **We recommend that the Government give consideration at an early stage in implementation of an NPSS or any comparable measure to the design and availability of generic advice to those considering participation in the scheme as well as to scheme members. It may well be that the requirement for generic advice in this context will need to be met as part of wider endeavours to improve the quality of generic financial advice that we are considering during our current inquiry into financial inclusion.**

124 Ev 76

5 The challenges of implementation

Provider choice and its regulation

52. The question of whether regulated advice on suitability proves necessary depends on factors which the NPSS and the rival options have in common—proposals for auto-enrolment, contingent compulsion in relation to employer contributions and linkage to reforms of the State system. However, there are a number of other factors affecting the design of a new scheme, some with regulatory implications, that depend upon the way in which such a new scheme is designed and implemented. The first which we consider is that of consumer choice.

53. Under the NPSS proposed by the Pensions Commission, there would be a single, monopoly provider of the Scheme and thus no provider choice. This approach is arguably inherent in the Commission's views on the benefits of a public sector role as an organiser of pension savings and bulk buyer of fund management.[125] Which? supported the single provider model, arguing that it would cut out unnecessary marketing and distribution costs and remove "the 'negative' competition costs associated with the open market model".[126]

54. The NAPF proposal for Super Trusts would allow for some competition in provision, and Ms Farnish thought that differentiation on the grounds of the quality of consumer service and administrative systems would be helpful.[127] However, the choice of provider would be for the employer, not for the individual account holder. The EEF expressed concern about the potential costs and risks for employers in making this choice.[128] The FSA told us that a choice that resided with employers rather than individual consumers would not lead to the creation of regulatory requirements arising from the FSA's concern for the appropriate degree of consumer protection; employers, even small employers, were not viewed as consumers; regulation would be a matter for The Pensions Regulator in the same way as for existing occupational pension schemes.[129]

55. The ABI model of Partnership Pensions is designed to offer choice to the individual consumer. An employer would be expected to propose a pension provider, but the individual would have a right to choose. Where neither employer nor employee made a selection, the provider would be chosen essentially at random, by a "carousel" system similar to that used for the allocation of Child Trust Funds where no parental choice is exercised. The ABI consider that their proposals "would harness competition to increase participation rates and saving levels, improve service and exert downward pressure on charges".[130] There would be some elements of the current competitive market under the ABI model, but to reduce costs there would be a standard contract between the provider

125 *Implementing an integrated package*, p 10

126 Ev 94

127 Q 97

128 Ev 116

129 Qq 125–131

130 Ev 106

and the employer, direct selling without commission and regulated marketing expenditure.[131] Mr Stephen Haddrill, Director General of the ABI, emphasised these contrasts with the current market:

> We are proposing to take out a long distribution chain and take out commission and sell direct and move into a new world … This is an opportunity for the industry as well as an opportunity for savers.[132]

56. Some evidence we received was avowedly sceptical about the novelty of this "new world" and whether the insurance opportunity merited another opportunity. Which? contended that "the ABI proposals would not have the trust and confidence of consumers, and without that confidence and trust you will not have a sustainable pension system".[133] Both Which? and the NAPF argued that the providers were bound to spend money on marketing or advertising to attract consumers, thus pushing up costs, a concern also shared by the Pensions Commission in their final Report.[134] The Resolution Foundation pointed to the findings of a recent FSA survey indicating that product choice was more often based on promotional literature than product features.[135] Lord Turner was concerned at the additional costs arising from competition when account holders switched providers. He also saw a risk in the automatic allocation of individual accounts to different providers where no choice was made, because of possible complaints by those allocated to "the less successful companies".[136]

57. The ABI's evidence implied that the benefits of limited regulation with its consequent cost savings would apply to their model as they applied to the NPSS and to the NAPF model.[137] This was directly challenged by the NAPF and Which? Ms Farnish said:

> Clearly, if we ended up with a system whereby commercial providers, whether they were insurers or anyone else, were designated as people into whom the funds were auto-enrolled, then we would need a much stricter regulatory regime than the sort of model perhaps that we have put forward, or the Turner model.[138]

Mr McAteer contended that "an open market model ... means you definitely need regulated financial advice".[139] He thought that a role for the FSA was essential to prevent mis-selling in an open market; he considered what he saw as the ABI's vision of an unregulated sales process with an open market as "an appalling vista".[140]

131 Q 92

132 Q 95

133 Q 2

134 Q 34; Ev 98; *Implementing an integrated package*, p 32

135 Ev 76

136 Q 189

137 Q 107

138 *Ibid*

139 Q 23

140 Qq 31, 42, 44

58. The FSA's written evidence appeared to lend weight to the notion that the ABI model has significant regulatory implications. The FSA's list of "features which would increase the likely requirement for regulatory interventions" included:

> The introduction of a sales process at either employer or employee level. As soon as joining any NPSS that may be introduced becomes intermediated, there is likely to be an information asymmetry and the chance of mis-selling increases. The introduction of multiple products and providers will complicate the decision-making process for consumers. In addition the product providers may need greater levels of supervision from a prudential and administrative perspective.[141]

In oral evidence Mr Briault confirmed that, although much depended on the final design, the ABI model seemed likely to require "some degree of conduct of business regulation", particularly if consumers felt the need for independent advice on the choice of provider. He suggested that complexity and an element of greater choice could "have the effect of leading us more into something akin to some form of regulated advice".[142]

59. **One of the keys to the success of the NPSS or an alternative that is implemented is the minimisation of the need for regulation, because regulation entails additional costs. The NPSS and the NAPF model remove the element of employee choice about a provider, and thus the possibility that such a choice may have regulatory implications. The ABI model introduces consumer choice. From the evidence we received, not least from the FSA, it seems likely that such choice will create additional regulatory requirements which may in turn affect the overall costs of any scheme based on that model. This places an additional onus on the ABI to provide convincing evidence that provider competition will serve to drive down costs.**

Asset allocation and choice

60. In 2004 Mr Ron Sandler, author of the Treasury-commissioned review of medium and long-term retail savings, told our predecessors:

> There is no question that the ultimate outcome for consumers in their savings process is governed in the overwhelming majority by the asset allocation decision. Some analysts would attribute 90% of the outcome to asset allocation and the balance to security selection and stock selection thereafter ... There is almost universally no attention given to asset allocation by advisers in this country. Their focus is on product purchase.[143]

The NPSS and its rivals vary in their approach to asset choice and allocation.

61. The NAPF's proposals are based on the premise that all members of a Super Trust would be entered into a single, pooled fund, so precluding consumer choice about funds.[144] Ms Farnish argued that choice of investments was not a desirable objective in building a

141 Ev 123

142 Qq 114–115, 117–124, 138

143 HC (2003–04) 71-I, para 39

144 Ev 54

new pension system for the mass market.[145] The NAPF pointed to findings of the Pensions Commission and the FSA about limited consumer knowledge of asset options and risk, and concluded that "all the evidence shows that the vast majority of consumers are not able to make those sorts of asset allocation decisions".[146] The ABI's proposals envisage an open competitive market in relation to asset management, considering that "a bit of competition around the return on the assets ... is beneficial".[147]

62. The Pensions Commission effectively proposes a middle path somewhere between these two approaches. Lord Turner told us "we believe that we can get the best of both worlds by having a core range of funds but also an open access system".[148] The Commission envisaged that the NPSS would "bulk negotiate a range of 6–10 funds". There would also be a "default fund" for those not wishing to come to a decision on asset allocation. This would be "a 'lifestyle' smoothing fund, which automatically shifts members from high equity allocations at earlier ages to index bond allocations as they approach retirement".[149] Lord Turner viewed the design of the default fund as "the most important discretionary decision" for the NPSS Board.[150] Mr Saunders thought it likely that a high proportion of consumers would choose the default fund and also saw it as important for those responsible for running the NPSS to establish "a really good default model".[151] It seems likely that the 6–10 core funds would be subject to passive management in relation to equities, not least because of the weight of evidence to suggest that active management cannot be relied upon to produce higher returns and entails additional costs.[152] However, under the proposed open access system, members could opt for other funds responding to individual preferences, such as investment in "alternative asset classes", such as private equity funds or hedge funds, or in funds designed to be ethically or environmentally responsible or that comply with Islamic investment requirements.[153]

63. Lord Turner considered that the combination of a default fund and a right to choose from other investment options "mitigates the political risk" because politicians would not be held to account for investment performance in the same way as they might be under a model in which investment choice was not always made by consumers.[154] **The availability of investment choices which are clearly signposted and accompanied by appropriate information about risk and reward is highly desirable and catered for under the proposed design of the NPSS. Nevertheless, much evidence suggests that most members would remain in the default fund. The design of the range of funds, especially the default fund, and the quality of asset management of the funds would be crucial to the success of the NPSS. We expect the case for independent scrutiny of the funds, and**

145 Q 84

146 Ev 54; Q 84

147 Q 91

148 Q 237

149 *A New Pension Settlement*, pp 37, 372–378

150 Q 234

151 Q 86

152 Qq 29, 30, 147–154

153 *A New Pension Settlement*, p 376; Q 237

154 Q 235

especially of the default fund, to be one of the issues to be considered during parliamentary scrutiny of the measures arising from the White Paper.

Prudential regulation

64. The FSA is responsible for the prudential regulation of the firms which provide personal, including Stakeholder, pensions and annuities. The FSA seeks to ensure that firms have sufficient resources, adequate senior management arrangements, and systems and controls in place to manage their business properly, both in normal and adverse circumstances, including sufficient capital to absorb losses from risks inherent in the business where necessary.[155] The FSA has noted that the principles of prudential regulation may be applicable depending on how a scheme is established: "The more the risk is carried by the private sector, the more likely there is to be a need for prudential supervision with powers of intervention where necessary".[156] The Pensions Commission and the IMA envisage that governance of the NPSS will be in the public sector, albeit with significant independence from Government.[157] **If the Government sets out the detail of governance arrangements for a single provider of pensions and funds within a single scheme, based on the proposals of the Pensions Commission, it will be important for the Government to clarify at an early stage the likely responsibilities of the FSA for prudential regulation in relation to the provider and funds within a single scheme. The Committee endorses the recommendation of the Pensions Commission that the governance should secure an institution which is clearly separate from direct government influence and which is also, in the words of the Commission, "clearly public and non profit-making".**[158]

Establishment and infrastructure

65. The Pensions Commission concluded that "it will be difficult to get the NPSS fully up and running before about 2010".[159] The Commission also acknowledged that "a major implementation planning exercise, with consultation, will be needed before final details are decided and the scheme is launched".[160]

66. One of the perceived strengths of the rival options proposed by the NAPF and the ABI is that they build on existing systems and infrastructure, including IT support. Ms Farnish stressed that Super Trusts would build on the practical experience of the occupational pensions sector, noting for example that account transfers between Trusts could be accomplished at a very low cost.[161] The ABI similarly stressed the capacity of Partnership Pensions to utilise the infrastructure currently being operated within the existing market.[162] Both Which? and the IMA questioned the advantages of the ABI model. Mr McAteer

155 Ev 121

156 Ev 123

157 *A New Pension Settlement*, p 37; Ev 44

158 *A New Pension Settlement*, p 402

159 *Ibid,* p 31

160 *Ibid*, p x

161 Q 101

162 Q 78

argued that insurance company systems did not offer advantages in verifying and reconciling contributions.[163] Mr Saunders felt that the ABI's approach entailed additional problems relating to the transfer of accounts between companies.[164]

67. The NPSS proposals envisage a unified infrastructure for handling individual accounts. The ABI argued that this approach would "simply expose the taxpayer to high set-up costs, uncertain future liabilities, and the financial risks associated with major Government IT projects".[165] The NAPF also argued that the NPSS would "require people to put their faith in a new public sector IT project".[166] Which? and the IMA rejected these suggestions. Mr McAteer saw the characterisation of the NPSS administration as a quango as a "straw man". In reality, Mr McAteer and Mr Saunders contended, the NPSS board would act as a clearing house, contracting out its work within a competitive market with many existing suppliers, and benefiting from its role as a bulk purchaser.[167]

68. Encouragingly, Mr Haddrill acknowledged that "the debate has moved on" from initial concerns expressed by the ABI about centralised administration of the NPSS: "Certainly, I think we are all agreed, on this table anyway, that the administration bit should be done by the private sector because that is where the systems are".[168] In a similar mood of compromise, Lord Turner conceded that there was an operational risk involved in the establishment of the administrative systems needed to support a single national scheme.[169] **There is a possibility of effective public sector purchase of relevant administrative services from the private sector, provided that the purchasers on behalf of the NPSS or any similar national scheme have the relevant skills, whether acquired in the public or private sectors. It is important that overall administrative costs are minimised and that an appropriate balance of risk between public and private sector is achieved.**

Collection systems

69. The NPSS and the rival schemes proposed by the NAPF and the ABI depend upon the effective and efficient collection of contributions from employers and employees. The NAPF and the ABI both contended that such contributions in relation to their proposed schemes could be collected through existing arrangements.[170] The NPSS would require new collection arrangements and the Pensions Commission canvassed two options. The first would be to use the PAYE system that is already used for employer national insurance contributions. This suffers from the disadvantage that there is a time delay between aggregate payments by employers and the provision of information relating those payments to specific individuals, thus delaying investment and reducing the precision of individual account information. The second option would be a dedicated Pension Payment System, which would be more up-to-date, but would be, at least minimally, more

163 Q 9

164 Q 74

165 Ev 105

166 Ev 63

167 Qq 11, 13, 16, 67, 69, 83

168 Q 72

169 Q 228

170 Qq 70, 71, 82

burdensome on business. The Commission favoured the second option, while calling for further investigation.[171] The IMA and Which? thought it was possible that the PAYE option could be made workable, using a "smoothing" mechanism to prevent any investment loss to individuals from the time delay inherent in the system.[172] Lord Turner admitted that collections systems were "not an issue that we bottomed out fully".[173] **In the event that the Government proposes a model for private pension provision based on the NPSS, we recommend that the Government, in its response to this Report, set out the matters that will need to be considered before a final decision is reached on collection systems.**

Transfers in and out

70. The Pensions Commission proposed that transfers between the NPSS and other pension schemes "should be allowed, but perhaps subject to a maximum transfer allowed into the NPSS".[174] Ms Farnish thought that there would be a strong case for permitting existing DC pension accruals to be transferred into "whatever new system finally materialised that is well-run, well-governed, low charge and in the interests of consumers".[175] The FSA did not expect to see large scale transfers into or out of the NPSS, but, asked to reflect on a possible comparison with past mis-selling, Mr Briault said:

> There is always the possibility of mis-selling of that type. We are ... acutely aware of that possibility and not least because of previous episodes of that sort, so we would be keeping a very close eye on that and, if we saw—and I hope we would be quicker off the mark—large-scale shifts out of the national pension scheme into other schemes, we would want to reassure ourselves very quickly that that was being done on the basis that it was suitable for those employees.[176]

71. There may be circumstances in which it is appropriate for individuals to transfer out of the NPSS or any comparable scheme that is established. Nevertheless, there is a potential risk that transfers in and out might be encouraged in inappropriate circumstances. **We welcome the early indications from the FSA that it will be alert to the possibility of mis-selling within the context of transfers in and out of the NPSS. It is essential that information provided to members and potential member of any new scheme includes clear guidance on circumstances where it might and might not be appropriate to transfer in or out of the scheme.**

171 *A New Pension Settlement*, pp 364–368

172 Qq 18, 70, 82; Ev 93

173 Q 233

174 *A New Pension Settlement*, p 36

175 Q 103

176 Qq 163, 167

The overall costs of a new national scheme

72. In an era of low inflation, the charges that are removed from a person's fund in the form of an AMC have a profound effect on the overall returns from a managed fund.[177] This was emphasised by Lord Turner:

> We have to be clear that we have got to do that [remove suitability advice] to get the costs out of the system. The difference between 1.3% and 0.3% means that by the time the person retires their pension, if we can get it to 0.3%, it is going to be something like 20% higher for the whole of their retirement.[178]

The figures used in the illustration were not chosen at random. The first—1.3%—is the current average AMC of Stakeholder pensions, while the second—0.3%—is the target AMC for the NPSS.[179] The NAPF model would be expected to operate at an AMC around 0.4%, although the charge would vary depending on the number of Super Trusts because of the costs of transfer between them.[180] It would be for The Pensions Regulator to monitor and regulate such charges.[181] The ABI model of Partnership Pensions would be expected to operate at an AMC in a range between 0.6% to 0.75%. The ABI would wish to see the operator of the new market overseen by a new economic regulator, with a power to recommend the setting of a price cap as a safeguard measure.[182]

73. The level of the AMC depends in part on the costs of aspects of implementation that we have already examined, such as administrations costs and collection systems. All of the costings just quoted also depend on a shared assumption that individual suitability advice, and the associated conduct of business regulation, will not be required, although we have already pointed to evidence indicating the likelihood that the ABI model would bring additional regulatory costs.[183] Some evidence suggested that the costs of the NPSS might be significantly higher than those foreshadowed in a target AMC of 0.3% or below. Mr Cazalet believed that the Pensions Commission had very significantly over-estimated the likely levels of "persistency" in the NPSS, in other words the likelihood of members of the Scheme consistently remaining within it. Although he accepted that there would be less switching with a single provider that in a competitive market of many providers, he thought that the Commission had significantly under-estimated the likely levels of people moving in and out of the Scheme, because of factors such as indebtedness, and fluctuations in free disposable income.[184] Mr Cazalet did not believe that the NPSS administration would be sustainable with an AMC of 0.3%.[185] Standard Life made a similar point.[186] The

177 Q 51

178 Q 211

179 Q 191; *A New Pension Settlement*, p 20

180 Ev 52; *Implementing an integrated package*, p 31; Q 85

181 Q 97

182 Ev 106, 109

183 Paras 58–59

184 *Polly Put the Kettle On*, p 33; Qq 3, 5, 6

185 Qq 3, 6

186 Ev 82

ABI pointed to analysis which it had commissioned from Deloittes suggesting that the AMC under the NPSS was more likely to be around 0.45% than 0.3%.[187]

74. Lord Turner pointed to the fact that the proposals in the Second Report of the Pensions Commission had had a significant effect in driving down the range of proposed AMCs under discussion so that almost all proposals were in the range of 0.3% to 0.6%.[188] He also said that "we are more confident about the relative ranking of the different proposals in terms of cost than we are about any precise figure". Although the NPSS might not initially meet the 0.3% target for its AMC, it would be the lowest cost option of the three options.[189] The IMA thought that a target range of 0.3% to 0.5% was realistic in the early stages of the NPSS, but that costs would fall to around 0.3% over a longer period.[190] Mr McAteer also attached importance to the likely downward trend.[191]

75. In the last Parliament our predecessors expressed the view that it would be preferable for price caps for regulated products to be set "by an independent body after clear and transparent analysis".[192] However, the then Committee was considering an existing competitive market. What the ABI is now proposing is the creation of a new competitive market with its own economic regulator. As the Pensions Commission has pointed out, there is evidence to indicate that competition will not drive down costs, and that segments of the market may go unserved if they cannot be served at a profit.[193] **Experience of Stakeholder pensions indicates that market operators may exert pressure for any charge cap to be increased and may tend to serve the most profitable parts of a market, not those most in need.**

76. **It is of crucial importance to the success of the NPSS and the overall trend of private pension savings that the Annual Management Charge is as low as possible and moves in a downward direction. An independent Board of the NPSS would have every incentive to see charges low and falling, as would the trustees of a Super Trust.**

Market impact

77. The Pensions Commission's Second Report did not contain a detailed analysis of the likely market impact of the establishment of the NPSS. The ABI was concerned that, if the debate on the NPSS and any rival option continues too long, "potentially it overhangs the existing savings market".[194] Equally, the experiences of Stakeholder pensions suggests that, once a model with lower costs is established, it has the beneficial effect of encouraging lower levels of charges across the wider market.[195]

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187 Ev 107

188 Qq 186, 191

189 Q 193

190 Qq 105, 98

191 Q 7

192 HC (2003–04) 71-I, para 73

193 *Implementing an integrate package*, p 32

194 Q 108

195 *Sandler Review*, para 5.71

78. The most significant concern about the market impact of the NPSS relates to the occupational pensions sector. It has been suggested that it might lead to “levelling down”, with employers seeing the NPSS as a Government-blessed standard for employer contributions and withdrawing from current schemes with higher contributions.[196] Lord Turner argued that employers retained an incentive to offer a better package to their employees than a prescribed minimum in order to compete in a competitive labour market. He also saw protecting those without adequate pensions as a higher social priority, and pointed out that the occupational pensions market would have to be very “fragile” to be profoundly affected by the introduction of the NPSS.[197] He supported the proposition that one way to prevent “levelling down” was to promote measures to enhance understanding of the value of occupational pension provision.[198]

79. The possible market impact of the NPSS or any rival option does not greatly affect choice between the options, because that impact will be similar for any option. All would entail a minimum employer contribution, and the possibility of additional, voluntary employee contributions. **We agree with Lord Turner that the higher social priority in this area is to promote additional pension provision for those who currently lack it. Nevertheless, we consider that the market impact of a new scheme, both prior to implementation and following implementation, merits further study and we recommend that the Government give further consideration to these issues at an early stage. We also recommend that the Government consider further measures to enhance public understanding of the long-term financial value of occupational pension schemes.**

196 *Implementing an integrated package*, p 37; Q 111

197 Q 222

198 Q 225

6 Conclusion: the potential of a new savings model

80. Much attention has been paid to the role that might be played by the public sector or public appointees in the governance and management of the NPSS. However, it is of paramount importance to the Scheme that money within the Scheme will remain that of the individual account holders. Lord Turner said "we are trying to get the idea that this is a property right, that what you have in you put in and that if you die before retirement it belongs to you".[199] He concluded:

> I think the key thing is that the primary legislation has to make it plain that this is not a National Pensions Savings Fund; it is a system which creates individual property rights in those accounts where the role of government in relation to fund manager is as a bulk buyer to get value for money; it is not an asset allocation, it is not making an asset allocation choice.[200]

Several witnesses referred to the value of individual accounts as a possible savings and investment vehicle for the target groups even when they are not employed.[201]

81. **There is a great and unique opportunity to reverse the decline in private pension provision and restore confidence in long-term savings. For this opportunity to be seized, there needs to be an integrated approach in which three pre-conditions are met. The first pre-condition is that the correct balance is struck between the role of the State in securing and promoting a new pension savings product and the sense of individual ownership. The second pre-condition is that the new product maintains the simplicity and near-universal suitability proposed by the Pensions Commission to minimise cost and the need for regulation. The third pre-condition is that reform of private pension saving takes place in tandem with a new direction in the State pension system.**

199 Q 198

200 Q 237

201 Qq 50, 197

Conclusions and recommendations

Recent trends and future proposals

1. One of the starting points for consideration of proposals by the Pensions Commission and of rival proposals must be the realisation that Stakeholder pensions have not been successful in halting the decline of non-State pension provision among middle earners. Indeed, a combination of sales approaches, commission incentives, regulatory requirements and decisions about the charge cap have created a position in which Stakeholder pensions are seen as uneconomic to both providers and potential customers among the original target market of middle income earners. The lessons from this process must be learned in taking forward proposals arising from the work of the Pensions Commission. We have sought to draw out these lessons in our ensuing conclusions and recommendations. (Paragraph 21)

The Commission's proposals and other options

2. The Pensions Commission is to be congratulated for bringing about a broad consensus in favour of auto-enrolment as the basis for securing a major advance in the level of private pension saving among middle earners. A move to auto-enrolment is an essential precondition if the NPSS or any rival option is to be implemented. (Paragraph 33)

The suitability hurdle

3. The compulsory matching employer contribution is an integral element of the NPSS and of the rival options. If there were to be no such contributions, the FSA's evidence indicates that it is unlikely that participation in the proposed scheme or schemes could be provided for without some regulated advice. With the increased costs consequent upon the need for such advice and diminishing contributions overall, it appears open to question whether a new scheme or schemes without such contributions would represent a step-change from Stakeholder pensions. (Paragraph 40)

4. The successful delivery of a new pension saving vehicle suitable for the vast majority of those eligible to contribute and thus not requiring regulated sales advice is contingent upon expectations about the extent and future course of means-testing for pensioners. These expectations are dependent not only on announcements expected in the Pensions White Paper, but also on the ability of present and future Governments to establish a policy framework based on a broad political consensus, together with accompanying forecasts on those eligible for means-testing, which deserve and attract the confidence of the public. (Paragraph 49)

5. It is of vital importance not only that the Government establishes a long-term coherent approach to policy on private and public pension provision and communicates effectively with the FSA in relation to the FSA's regulatory requirements, but also that the Government continues to provide leadership and support to ensure that a regulatory position on suitability in relation to the NPSS or a

rival option, once arrived at by the FSA, proves sustainable in the long-term. (Paragraph 50)

6. We recommend that the Government give consideration at an early stage in implementation of an NPSS or any comparable measure to the design and availability of generic advice to those considering participation in the scheme as well as to scheme members. It may well be that the requirement for generic advice in this context will need to be met as part of wider endeavours to improve the quality of generic financial advice that we are considering during our current inquiry into financial inclusion. (Paragraph 51)

The challenges of implementation

7. One of the keys to the success of the NPSS or an alternative that is implemented is the minimisation of the need for regulation, because regulation entails additional costs. The NPSS and the NAPF model remove the element of employee choice about a provider, and thus the possibility that such a choice may have regulatory implications. The ABI model introduces consumer choice. From the evidence we received, not least from the FSA, it seems likely that such choice will create additional regulatory requirements which may in turn affect the overall costs of any scheme based on that model. This places an additional onus on the ABI to provide convincing evidence that provider competition will serve to drive down costs. (Paragraph 59)

8. The availability of investment choices which are clearly signposted and accompanied by appropriate information about risk and reward is highly desirable and catered for under the proposed design of the NPSS. Nevertheless, much evidence suggests that most members will remain in the default fund. The design of the range of funds, especially the default fund, and the quality of asset management of the funds, would be crucial to the success of the NPSS. We expect the case for independent scrutiny, especially of the default fund, to be one of the issues to be considered during parliamentary scrutiny of the measures arising from the White Paper. (Paragraph 63)

9. If the Government sets out the detail of governance arrangements for a single provider of pensions and funds within a single scheme, based on the proposals of the Pensions Commission, it will be important for the Government to clarify at an early stage the likely responsibilities of the FSA for prudential regulation in relation to the provider and funds within a single scheme. The Committee endorses the recommendation of the Pensions Commission that the governance should secure an institution which is clearly separate from direct government influence and which is also, in the words of the Commission "clearly public and non profit-making". (Paragraph 64)

10. There is a possibility of effective public sector purchase of relevant administrative services from the private sector, provided that the purchasers on behalf of the NPSS or any similar national scheme have the relevant skills, whether acquired in the public or private sectors. It is important that overall administrative costs are minimised and that an appropriate balance of risk between public and private sector is achieved. (Paragraph 68)

11. In the event that the Government proposes a model for private pension provision based on the NPSS, we recommend that the Government, in its response to this Report, set out the matters that will need to be considered before a final decision is reached on collection systems. (Paragraph 69)

12. We welcome the early indications from the FSA that it will be alert to the possibility of mis-selling within the context of transfers in and out of the NPSS. It is essential that information provided to members and potential member of any new scheme includes clear guidance on circumstances where it might and might not be appropriate to transfer in or out of the scheme. (Paragraph 71)

13. Experience of Stakeholder pensions indicates that market operators may exert pressure for any charge cap to be increased and may tend to serve the most profitable parts of a market, not those most in need. (Paragraph 75)

14. It is of crucial importance to the success of the NPSS and the overall trend of private pension savings that the Annual Management Charge is as low as possible and moves in a downward direction. An independent Board of the NPSS would have every incentive to see charges low and falling, as would the trustees of a Super Trust. (Paragraph 76)

15. We agree with Lord Turner that the higher social priority in this area is to promote additional pension provision for those who currently lack it. Nevertheless, we consider that the market impact of a new scheme, both prior to implementation and following implementation, merits further study and we recommend that the Government give further consideration to these issues at an early stage. We also recommend that the Government consider further measures to enhance public understanding of the long-term financial value of occupational pension schemes. (Paragraph 79)

Conclusion: the potential of a new savings model

16. There is a great and unique opportunity to reverse the decline in private pension provision and restore confidence in long-term savings. For this opportunity to be seized, there needs to be an integrated approach in which three preconditions are met. The first precondition is that the correct balance is struck between the role of the State in securing and promoting a new pension savings product and the sense of individual ownership. The second precondition is that the new product maintains the simplicity and near-universal suitability proposed by the Pensions Commission to minimise cost and the need for regulation. The third precondition is that reform of private pension saving takes place in tandem with a new direction in the State pension system. (Paragraph 81)

Formal minutes

Thursday 18 May 2006

Members present

Mr John McFall, in the Chair

Jim Cousins
Angela Eagle
Mr Michael Fallon
Ms Sally Keeble
Mr Andrew Love
Kerry McCarthy
Peter Viggers

The design of a National Pension Savings Scheme and the role of financial services regulation

The Committee considered this matter.

Draft Report (The design of a National Pension Savings Scheme and the role of financial services regulation), proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 3 read and agreed to.

Paragraph 4 read, amended and agreed to.

Paragraphs 5 to 11 read and agreed to.

Paragraph 12 read, amended and agreed to.

Paragraphs 13 to 16 read and agreed to.

Paragraph 17 read, amended and agreed to.

Paragraphs 18 to 23 read and agreed to.

Paragraphs 24 to 26 read, amended and agreed to.

Paragraphs 27 to 37 read and agreed to.

Paragraph 38 read, amended and agreed to.

Paragraph 39 read and agreed to.

Paragraph 40 read, amended and agreed to.

Paragraphs 41 to 48 read and agreed to.

Paragraph 49 read, amended and agreed to.

Paragraphs 50 to 62 read and agreed to.

Paragraphs 63 and 64 read, amended and agreed to.

Paragraphs 65 to 70 read and agreed to.

Paragraph 71 read, amended and agreed to.

Paragraphs 72 to 80 read and agreed to.

Paragraph 81 read, amended and agreed to.

Summary read, amended and agreed to.

Resolved, That the Report, as amended, be the Fifth Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134 (Select committees (reports)).

Several papers were ordered to be appended to the Minutes of Evidence.

Ordered, That the Appendices to the Minutes of Evidence taken before the Committee be reported to the House.

Several Memoranda were ordered to be reported to the House.

[Adjourned till Monday 22 May at 4.45 pm

List of witnesses

Tuesday 25 April 2006

Mr Mick McAteer, Policy Advisor, Which? and **Mr Edward Cazalet**, Cazalet Consulting Ev 1

Mr Richard Saunders, Chief Executive, Investment Management Association, **Mr Stephen Haddrill**, Director General, Association of British Insurers, and **Ms Christine Farnish,** Chief Executive, National Association of Pension Funds Ev 13

Wednesday 3 May 2006

Mr Clive Briault, Managing Director, Retail Markets, and **Mr Dan Waters,** Director, Retail Policy, Financial Services Authority Ev 23

Lord Turner of Ecchinswell, Chairman, Pensions Commission Ev 31

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3	London Stock Exchange	Ev 48
4	National Association of Pension Funds (NAPF)	Ev 49
5	Norwich Union	Ev 66
6	The Professional Insurance Marketing Association (PIMA)	Ev 69
7	The Public and Commercial Services Union	Ev 73
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9	Royal London	Ev 78
10	The Standard Life Assurance Company	Ev 80
11	Trades Union Congress (TUC)	Ev 87
12	UNITE (The National Federation of Royal Mail & BT Pensioners)	Ev 89
13	Which?	Ev 91
14	Association of British Insurers (ABI)	Ev 104
15	Association of British Insurers (ABI) (supplementary)	Ev 110
16	British Bankers Association (BBA)	Ev 111
17	Engineering Employers Federation (EEF)	Ev 113
18	Fidelity International	Ev 118
19	Financial Services Authority (FSA)	Ev 120
20	HM Treasury and Department for Work and Pensions	Ev 125

List of Reports from the Treasury Committee during the current Parliament

Session 2005–06

		Report
First Report	The Monetary Policy Committee of the Bank of England: appointment hearing	HC 525
Second Report	The 2005 Pre-Budget Report	HC 739
Third Report	The Monetary Policy Committee of the Bank of England: appointment hearing for Sir John Gieve	HC 861
Fourth Report	The 2006 Budget	HC 994