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Work and Pensions Committee

Automatic enrolment in workplace pensions and the National Employment Savings Trust

Eighth Report of Session 2010–12

Volume II

Additional written evidence

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The Work and Pensions Committee

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List of additional written evidence

(published in Volume II on the Committee's website www.parliament.uk/workpencom)

Written evidence

Written evidence submitted by Henry Tapper

1. *Submission Summary*

1.1 NEST (National Employment Savings Trust) is in trouble.

1.2 While it may be a long-stop for the final waves of employers staging auto-enrolment in 2015–16, it is looking increasingly like a “pension of last resort”.

1.3 It is not on the agendas of large and medium sized employers who object to its limitations, are unimpressed by its pricing and wary of its ability to fit in with its auto-enrolment processes either as a main or feeder scheme.

1.4 The Government should not panic, there is time to put things right.

1.5 NEST needs to be better. NEST Corporation has done its work on keeping its charges down, getting its record keeping in order and establishing an appropriate investment strategy.

1.6 But it has failed to tackle the structural issues surrounding decumulation, especially the decumulation of small pension pots.

1.7 This submission argues that the way to improve matters is for the Government to take radical steps to provide Scheme Pensions from NEST (and its sister the Pension Protection Fund (PPF)).

1.8 This could enable those with small defined contribution (DC) pots an opportunity to get equivalent value form their pension pots as the Dutch can from theirs.

1.9 This submission proposes that NEST looks to Australia and its clearance system to encourage employers to run NEST strategies alongside their main workplace strategies.

1.10 The limitations on NEST are a Faustian pact with the ABI (Association of British Insurers) but it’s a pact that cannot be reneged on before 2017. But the Government can make it quite clear that it intends to end these limitations as soon as possible so preventing NEST being strangled at birth. This submission proposes it does just that and does it now.

2. *Submission*

2.1 I am a pensions consultant who has worked for 27 years in financial services. I co-wrote the Eagle Star submission to the Stakeholder Pensions consultations arguing for stakeholder to be set up as a number of large master trusts (along the lines of the Australian “Super” model).

2.2 Since then I have campaigned for collective DC arrangements which deliver better value than personal pensions both in accumulation and decumulation.

2.3 I have argued that people’s fractured pensions history which results from a “new pension each job” creates confusion and disillusionment.

2.4 My hope when NEST was announced was that it would reduce accumulation costs, create opportunities for collective drawdown and encourage a system of contribution clearing where NEST and other such schemes could create a simpler and more popular system for workplace pensions.

2.5 For the most part I was encouraged by the Pensions Act 2008 which created an environment where the improvements I hoped for could happen.

2.6 In this submission, I will make personal comments based on my day to day work with employers in the private sector and my experience of advising individuals both in and out of the workplace.

2.7 I will concentrate my remarks on four issues raised by the inquiry to which I think there are solutions.

3. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

3.1 Employers are unlikely to adopt NEST as their primary auto-enrolment vehicle so long as the contribution cap remains in place. I appreciate the cap protects existing providers but I suspect the Government has previously underestimated the negative impact on NEST take up.

3.2 The requirement for NEST members to repay the loan to NEST Corporation from the contribution levy makes NEST uncompetitive in the accumulation phase relative to private sector alternatives available to medium and large employers. The impact of this charge will render NEST only competitive in provision to SMEs (Small and Medium-size Enterprises). It is worth noting that many large workplace savings have “clean Annual Management Charges (AMC)” of less than 0.3%. I know of two examples—BT and Logica, where the AMC is 0.10% for the default accumulation fund.

3.3 The restriction placed on NEST not to allow employer contribution refunds renders NEST unattractive (relative to other occupational DC structures) to employers with high staff turnover.

3.4 The current ban on transfers into NEST precludes the opportunity for NEST to aggregate small pots and reduces the opportunity for it to drive genuine innovation in the collective decumulation of member's accounts. (see below)

3.5 Taken together the limitations placed on NEST will lead to NEST being the provider of last resort to the recalcitrant employer and the business NEST takes on will be unprofitable meaning that it will become progressively less competitive unless the tax payer is called to bail it out.

4. *NEST's potential market share and the possible effects on other providers*

4.1 I do not know of any employers who have decided to use NEST in future. Nor do I sense any great excitement either from employers, employees or employee representatives about NEST.

4.2 This isn't surprising at a time when most employers are concentrating on managing in the difficult current environment. However it is disappointing.

4.3 Despite a very large amount of money having been spent on NEST, it has come up with little innovation that improves DC outcomes. Assessing NEST against the Pension Regulator's determination on what makes for good DC outcomes, one senses a lost opportunity and to the extent that NEST hasn't boldly gone, it has not encouraged the hoped-for innovation in the private sector.

4.4 As NEST has failed to catch my imagination, the imaginations of others in the pensions industry and certainly the wider population, I think it unlikely that it will capture market share on its merits. Indeed the impact of the limitations discussed in the previous section means that NEST will not be chosen as a pension arrangement.

4.5 Instead it will be imposed on unwilling employers who reluctantly establish pension provision. Such employers would not have chosen to take out a privately run workplace pension. NEST will not take market share from other providers.

4.6 If the limitations were lifted and if NEST were to become genuinely innovative (focussing on decumulation, super efficient administration and low charges) then it's market share would be in line with initial projections. Currently I suspect its market share will be well below that originally anticipated.

5. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

5.1 One of the pleasing side-impacts of NEST has been a revival in interest in Collective DC. In a recent publication the Royal Society of the Arts (RSA) make the claim:

> "If a typical Dutch and a typical British person save the same amount for their pension, the Dutch person can expect a 50% higher income in retirement."

5.2 The savings that the RSA report alert us to occur both in the accumulation and decumulation phases of a pension scheme. While NEST goes some way to providing value for money in the accumulation phase, it is currently offering nothing new on decumulation .

5.3 This is despite it having a default investment strategy that lends itself to collective decumulation (target dated funds).

5.4 Currently the decumulation of DC pensions is provided by insurance companies which offer variants on guaranteed annuities.

5.5 The Government Actuary reckons their individual annuities are 25% more expensive than pensions provided from a collective fund (such as an occupational pension).

5.6 In the reforms introduced in the Pensions Act 2008 and subsequently, the structural weaknesses in UK DC accumulation are simply not addressed.

5.7 If as a result of this inquiry, one new strategy is explored it should be the opportunity presented by the new collective vehicles, NEST (and also the Pension Protection Fund) to provide Scheme Pensions.

5.8 In order for collective pensions to provide the economies the RSA refer to, Scheme Pensions are essential, but Scheme Pensions can only be provided if there is a counterparty prepared to insure the long-tail longevity risk.

5.9 I would argue that as a result of poor pension provision, the State is the insurer of this risk—if only by default.

5.10 If the purpose of NEST is to ensure adequate pensions for those who currently do not have them, it is failing in its approach to decumulation and consequently the longevity risk will remain with the tax-payer. If the State determined it will underwrite the long-tail longevity risk associated with Scheme Pensions then both NEST (in the longer term) and the PPF (now) could provide Scheme Pensions to those with small annuities (say under £50,000 in DC pension savings).

5.11 In short, the taxpayer is not going to get rid of the longevity risk of the target market for NEST and auto-enrolment by continuing with the broken system of individual annuities.

5.12 Until there is genuine reform in the decumulation phase, DC will continue to run at 75% of the efficiency of Dutch pensions

5.13 There is a way forward for the Government in solving this problem and I would be happy to demonstrate it.

6. *Possible measures to reduce the proliferation of small pension pots*

6.1 The underlying reasons why people have small pension pots are:

- 6.1.2 That small amounts of money go into today's DC pensions (relative to previous alternatives).
- 6.1.2 Employers do not offer pension clearing but require employees to start a new pension plan on arrival.
- 6.1.3 People do not aggregate one pension with another when they change jobs.

6.2 To resolve these issues three things need to happen:

- 6.2.1 More money needs to go into DC pensions (and auto-enrolment will mean it does).
- 6.2.2 A system of clearing pensions needs to be established so that people take their pension plan with them.
- 6.2.3 Barriers to transfers within pensions need to be eased.

6.3 As regards clearing, I note with interest the Australian system where the technical issues related to clearing contributions to multiple schemes from a single empoloyer payroll have been resolved. The Government should be talking to the technology providers such as Superchoice which have made this possible.

6.4 As regards the aggregation of DC pension pots I note with dismay that NEST will not be taking transfers in or out until 2017 at the earliest.

6.5 The public are thoroughly fed up with the complexity of pensions, not least the piles of paperwork they build up. While some people never get into the funded pension loop, most people in employment are provided for by a variety of pension plans, some occupational, some personal, some defined benefit (DB), some defined contribution (DC).

6.6 We know it is virtually impossible to aggregate DB pensions into DC schemes (witness pensions mis-selling) but to prevent DC pensions being aggregated with each other seems wilfully obstructive.

6.7 The insurance industry through the ABI, which I understand has lobbied hard to stop NEST taking transfers in and out, is arguing from vested self-interest. However they are also going to bring pensions into and particularly NEST into public disrepute.

6.8 I hope that the Government will reconsider its current stance on NEST's capacity to take transfers in. Were NEST to take transfers in and provide a more efficient means of providing decumulation (see above), I can envisage a model where NEST effectively cleans up the mess that is the "mass" annuity market (eg those with pots less than £50,000)

7. Conclusion

7. 1 NEST is in trouble but it shouldn't be—it is a good project that is currently being strangled at birth by the insurance industry.

7.2 To some extent the restrictions placed on NEST are necessary. It is not right that NEST receives preferential loans from Government without these costs being passé on. However some of the restrictions are "restrictive practices". The imposition of a transfer in and out ban on NEST (at least until 2017) does not make sense to a public fed up with multiple pensions.

7.3 But much more can be done to make NEST more attractive than simply putting it onto a leveller playing field.

7.4 The Government should be urgently looking at ways of improving the clearing system to allow payrolls to clear money to more than one pension arrangement.

7.5 Finally, and most radically, the Government should be looking to decumulate small DC pots through Scheme Pensions, both from NEST and in the short-term from the Pension Protection Fund.

14 July 2011

Written evidence submitted by FairPensions

SUMMARY

- Responsible stewardship of investments will be vital to the achievement of auto-enrolment's policy goals.
- We applaud NEST's (National Employment Savings Trust) thoughtful and forward-looking approach to responsible investment, as well as its efforts to engage members and understand their needs, including with respect to risk appetite and ethical preferences. We hope its leadership will drive up standards across the market.
- We are concerned at the limited attention that has so far been given to ensuring that standards of governance and consumer protection are consistent and comparable across the pensions market. Trust- and contract-based pension arrangements are subject to separate legal and regulatory regimes. While not suggesting that this separation could or should be abolished, we do think that more concerted government action is needed to ensure that both systems act in savers' best interests. Failure to do this could damage trust in the system and thereby discourage people from saving, as well as damaging outcomes for savers.

1. FairPensions is a registered charity that promotes Responsible Investment (RI) by pension schemes and fund managers, and seeks to ensure that savers are well served by their agents in the City. We concentrate below on the following aspects of this inquiry's terms of reference, which are relevant to our area of expertise:

- NEST's potential market share and the possible effects on other providers.
- NEST's investment strategy.
- The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement.

2. With the decline of defined benefit (DB) schemes, the auto-enrolment landscape will be dominated by defined contribution (DC). This means that the five to eight million people predicted to begin saving or save more as a result of the reforms[1] will be largely reliant on the capital markets for their wellbeing in retirement. It is vital that these savers' investments are responsibly stewarded. The impact of this on the success of the policy's ultimate goal—providing for an ageing population—will be two-fold. Firstly and most obviously, it will affect the performance of pension investments. Secondly, it may also impact public trust in the system, which will be a key factor in people's willingness to save in the first place.

(A) NEST—INVESTMENT STRATEGY AND MARKET IMPACT

NEST's investment approach

3. "Responsible investment" approaches reflect the increasingly accepted view that environmental, social and corporate governance (ESG) issues can affect investment performance, and that appropriate consideration of these issues is part of investors' fiduciary duty to their beneficiaries. Responsible investors seek to incorporate ESG issues into their analysis and decision-making, and to be "active owners", exercising their shareholder rights (ie engagement and voting) to improve company performance. In the aftermath of the financial crisis, the need to improve the quality of engagement between investors and companies has been increasingly recognised, most notably with the publication of the UK Stewardship Code for institutional investors.[2]

4. From the outset NEST has taken a thoughtful and forward-looking approach to responsible investment. Its Statement of Investment Principles gives dedicated consideration to responsible investment and confirms that it will become a signatory to both the UK Stewardship Code and the UN Principles for Responsible Investment.[3] Its in-house investment team is well placed to scrutinise their asset managers' responsible investment activity, which will be crucial to ensuring that this commitment is fully implemented.

5. Separately, we also welcome NEST's offering of an ethical fund for members who wish to choose it, following DWP research suggesting that more than a quarter of pension savers were interested in ethical products even if they delivered lower returns.[4] We understand that NEST also conducted detailed research into the particular ethical issues of most concern to their membership demographic. This is particularly laudable, since fiduciary law suggests that any ethical decisions made by a pension fund should be based on the views and priorities of the beneficiaries.[5] However, it also highlights a "supply-side" problem with consumer choice in this area: NEST's ethical fund is an off-the-shelf product, the F&C Stewardship International Fund, which by its nature imperfectly reflects the priorities identified by this research. It is to be

[1] The Pensions Regulator, 2011, *"Enabling good member outcomes in work-based pension provision",* p 5. http://www.thepensionsregulator.gov.uk/docs/dc-discussion-paper-2011.pdf

[2] FRC, UK Stewardship Code 2010, available online at

[3] http://www.NESTpensions.org.uk/schemeweb/NESTWeb/includes/public/docs/statement-of-investment-principles,PDF.pdf

[4] PADA, May 2009, *"Building personal accounts: designing an investment approach",* p 119. See also DWP, 2009, "Individuals' likely reactions to workplace pension reforms", http://research.dwp.gov.uk/asd/asd5/rports2009–2010/rrep669.pdf

[5] See Chapter 4 of our recent report, "Protecting our Best Interests: Rediscovering Fiduciary Obligation", available online at www.fairpensions.org.uk/fiduciaryduty

hoped that if, as anticipated, NEST becomes a significant market participant, it will be in a position to negotiate more bespoke products.

6. We are aware that some have criticised NEST for what they regard as an unduly cautious investment approach which will not deliver adequate returns. Whilst it does not fall within our remit to take a position on the investment strategy itself, we would note that NEST's approach has been developed on the basis of robust and careful research into the needs and priorities of prospective members. In particular, evidence that most people's priority is to avoid loss[6] has led to the decision to take a low-risk approach during the "foundation stage" in order to cultivate the savings habit. We applaud NEST's efforts to discover and act on their members' needs, which can be all too rare in the world of private pensions.

NEST's impact on other providers

7. In a parliamentary debate in December 2010, Pensions Minister Steve Webb expressed the hope that NEST's low charges "will have a downward impact on charges across the market".[7] We hope that NEST's leadership will also drive up standards in relation to responsible investment and member engagement. The publicly available research conducted by NEST, and by the Personal accounts delivery authority (PADA) before it,[8] should also be a useful resource for funds who wish to accommodate members' preferences and priorities but may not have the resources to survey their own members directly. Greater efforts to ascertain member's preferences in the arena of ethical investment, following NEST's lead, could also help drive the market for more bespoke ethical products reflecting members' priorities.

(B) Schemes Eligible for Auto-Enrolment: The "Governance Gap"

8. Moving beyond NEST, we note that the DWP recently conducted a consultation exercise on "regulatory differences between occupational and workplace personal pensions". Our response to this consultation is available on our website.[9] We believe that the issues it raises have significant implications for the likely success of auto-enrolment in achieving its policy objectives of encouraging saving and delivering adequate pensions. Our comments below may also be relevant to this inquiry's question regarding scheme certification.

9. As the recent report of the Workplace Retirement Income Commission noted, "the UK's workplace pensions landscape is highly fragmented."[10] Different forms of pension provision are subject to different laws and regulations which have developed in a more or less *ad hoc* way. The most important distinction is that between trust-based and contract-based providers.

— Trust-based pension schemes are overseen by a board of trustees (both employer- and member-nominated) who have a strict "fiduciary duty" to act in the best interests of scheme members. Trustees are often not investment experts and most delegate day-to-day decisions to external asset managers. These schemes are regulated by The Pensions Regulation (TPR).

— Contract-based pension providers (firms such as Standard Life and Prudential) are subject to a separate legal regime. There is no equivalent of the board of trustees and these providers do not have the same fiduciary duties as trustees: savers are protected only by their contractual relationship with the provider. The employer is not a party to this contract and has no governance responsibilities. However, providers are subject to Financial Seervice Authority (FSA) rules which do not apply to pension fund trustees. They are regulated by both the FSA and TPR, but the FSA is the primary regulator.

10. The body of UK law applying to trust-based schemes is much more developed than that applying to contract-based pension products. In addition, most public policy debates about pensions law and regulation have tended to focus on defined benefit occupational pension schemes. Yet such schemes represent a dwindling proportion of the market: from 1997 to 2010, workplace contract-based pensions rose from 1% to 14% of all private pension saving.[11]

11. Most pension savers will be unaware of the legal differences between different types of pension. Moreover, many will have little or no choice over what type they end up in: under auto-enrolment, the decision is up to the employer. From the consumer point of view, the relationship is the same regardless of the type of pension: they hand over their money to someone whom they entrust to look after it with the goal of providing them a pension in old age. It is therefore logical that the framework in place to ensure consumers' interests are protected should be equally robust for all types of pension provision. This is not to say that the framework should be identical—it would clearly be impossible and probably undesirable to efface the distinction between trust-based and contract-based provision. However, urgent government attention is required to ensure that standards of governance and consumer protection are comparable across the market, albeit that they may be achieved through different mechanisms.

[6] See for example Building personal accounts: Designing an investment approach, p 117–122: http://www.NESTpensions.org.uk/schemeweb/NESTWeb/includes/public/docs/investment-consultation,PDF.pdf

[7] Hansard, 14 Dec 2010: Col 886.

[8] See for example "Building personal accounts: Designing an investment approach": http://www.NESTpensions.org.uk/schemeweb/NESTWeb/includes/public/docs/investment-consultation,PDF.pdf

[9] See www.fairpensions.org.uk/policy

[10] Report of the Workplace Retirement Income Commission, July 2011, p 28.

[11] ONS Annual Survey of Hours and Earnings, 2010, cited in WRIC, July 2011.

The "governance gap"

12. The recent report of the Workplace Retirement Income Commission expressed concern about a "governance vacuum", saying: "In a world where individuals lack the time and expertise to drive a good deal with service providers it must be clear who is standing up for their interests and driving the best deal with suppliers. In trust-based schemes the trustees can play this role but the extent to which they do so seems variable. For contract-based schemes it is usually only the employer who could do this and the extent to which they do so is variable."

13. We agree, except that we believe the implications of the governance gap go beyond the question of agreeing a "good deal" with providers. Standing up for savers' interests also means holding those providers to account on an ongoing basis—including with respect to their exercise of "stewardship", or responsible ownership, to ensure that investee companies are well-governed and deliver sustainable long-term returns. This may be jeopardised by weaknesses in the legal framework on both sides of the pensions market:-

14. Trust-based: Trustees increasingly delegate their powers but cannot delegate their fiduciary responsibilities. As the Myners Report noted 10 years ago, they may not have the expertise to effectively challenge or hold to account those they delegate to. This potentially creates an accountability gap on the part of the asset managers and consultants who make and advise on key decisions affecting members' interests.

15. Contract-based: In contract-based provision there are no trustees at all. In theory, this arguably makes the chain of accountability shorter and therefore more effective. However, many have expressed concern about the absence of anyone charged solely with championing savers' interests. In practice, personal pensions can seem like much more of a "black box", with nobody entrusted to intermediate between the interests of the individual saver and those of the commercial provider.

Government response to date

16. We are disappointed that the Government's response to the consultation on regulatory differences appeared to downplay the significance of the governance issue, apparently accepting arguments that, "many providers of workplace personal pensions had arrangements such as governance committees which meant legislative intervention was unnecessary." However, according to research by TPR, only around half of all relevant employers have such arrangements in place, and in many cases they are informal with little clarity over their role.[12] There remains a danger that employers will see contract-based provision as the "easy option" given the lesser responsibilities it places on them—yet it is far from clear that this serves the interests of beneficiaries.

17. The Government response also points to its guidance on default funds,[13] yet this guidance is extremely broad-brush and effectively states only that roles and accountabilities must be clear, without any elaboration of what governance structures might be desirable or appropriate to ensure that savers' interests are protected. Governance committees are mentioned as one party to whom the guidance might be relevant, but there is no discussion of the circumstances under which it might be appropriate to establish one or of best practice in their operation.

Recommendations

18. *Trust-based*: The Law Commission has stated that asset managers and consultants have the same strict fiduciary duties as trustees under common law.[14] But this is not widely accepted in the industry. We recommend clarification by the regulator to ensure that high standards of protection are applied by those who actually manage savers' money as well as the trustees who appoint them.

19. *Contract-based*: Consideration should be given to the framework governing contract-based providers themselves in two key areas:

- *Duties*: should FSA rules regarding conflicts of interest and obligations towards savers be strengthened, given that contract-based providers fulfil the same role as trust-based schemes in which the legal framework is strong in this regard?
- *Structures*: should measures be taken to ensure that savers in contract-based pension products have an independent champion to defend their interests? If so, should this take the form of a "policyholder committee" within firms themselves (similar to the governance arrangements in jurisdictions which do not have the concept of the trust, such as South Africa), or of employer-led governance committees in individual workplaces, or some combination of the two?

20. If such consideration is delayed until the review of auto-enrolment in 2017, it is possible that the damage will already have been done in the form of suboptimal outcomes for millions of savers and erosion of trust in the system.

[12] TPR, Jan 2008, "DC Research: Data on the occupational DC landscape plus results of independent research", p 27.

[13] Available at www.dwp.gov.uk/docs/def-opt-guid.pdf

[14] Law Commission ref; For further details see "Protecting our Best Interests", 2011, Chapter 2.

About FairPensions

21. FairPensions is a registered charity that promotes Responsible Investment (RI) by pension schemes and fund managers, and seeks to ensure that savers are well served by their agents in the City. RI generally involves shareholder engagement with companies to ensure that environmental, social and corporate governance (ESG) risks with the potential to affect long-term financial returns are monitored and managed.

22. FairPensions publishes research including widely-respected industry benchmarking surveys. Our single-issue campaigns help turn the spotlight onto hitherto neglected areas where there is a strong business case for investor engagement. We also work with policymakers to improve transparency and accountability to savers, and to remove regulatory barriers to RI.

23. We are a member organisation, whose members include representatives of pension savers (such as the National Federation of Occupational Pensioners, UNITE and Unison), a number of leading UK charities (including Oxfam, Amnesty International and WWF), and thousands of individual pension fund members. We are independent of industry and are funded by grants from charitable foundations and trusts.

9 August 2011

Written evidence submitted by Consumer Focus

About Consumer Focus

Consumer Focus is the statutory consumer champion for England, Wales, Scotland and (for postal consumers) Northern Ireland. We operate across the whole of the economy, persuading businesses, public services and policy makers to put consumers at the heart of what they do.

Consumer Focus tackles the issues that matter to consumers, and aims to give people a stronger voice. We don't just draw attention to problems—we work with consumers and with a range of organisations to champion creative solutions that make a difference to consumers' lives.

1. *Introduction*

1.1 Consumer Focus strongly supports the idea of auto-enrolment and the development of NEST (National Employment Savings Trust). NEST has the potential to produce a low-cost savings vehicle for low and medium-paid workers, frequent job-switchers and the low paid self-employed. As we argue in our recent report, *Is it advisable? An investigation into switching and advice in the individual personal pensions market,*[15] these segments of the working population are presently ill-served by the pensions market.

1.2 NEST should be placed on a more equal footing with other employer backed pension schemes. Specifically, the cap on annual contributions and the blanket restriction on transfers in to NEST should be removed. These create disincentives for some employers to use NEST and for some employees to remain opted-in to an employer backed scheme and ultimately work to the detriment of those employees for whom the NEST scheme would provide a better retirement saving option.

2. *Likely impact of the limitations placed on NEST*

2.1 The current ban on transfers into NEST, which is not scheduled to be reviewed until 2017, should be lifted as soon as possible. Savers should be allowed to transfer small pots of money (at least £5,000 and preferably £10,000) from existing pension pots.

2.2 At present 2.4 million people have combined personal and stakeholder pension pots of less than £5,000; four million have less than £10,000 in personal and stakeholder pensions.[16] These savers face on-going detriment as the management and administration costs of these small pots are often large compared to the annual growth. If small savers were allowed to transfer these small pots in to the NEST scheme their savings would be subject to much lower annual management costs. They would also benefit from better visibility and awareness of their savings.

2.3 Concerns have been raised in some quarters of the pensions industry that allowing such transfers could result in the flight of savings and work to the detriment of customers that remain with the pension company. Such concerns should be considered seriously. However, allowing four million savers to transfer a maximum of £10,000 into NEST represents a maximum possible outflow of £40 billion which is relatively small compared to the £470 billion[17] held in insurer administered individual pension plans.

2.4 The cap on annual contributions in to NEST should also be removed. This impedes the ability of NEST to offer an all encompassing and effective pension scheme compliance solution to small and medium sized

[15] Consumer Focus, July 2011; available at www.consumerfocus.org.uk/publications/is-it-advisable-an-investigation-into-switching-and-advice-in-the-individual-personal-pensions-market

[16] HMRC, Personal and Stakeholder Pension Fund Values, May 2010; available at www.hmrc.gov.uk/stats/pensions/table7–13-may10.pdf

[17] Association of British Insurers, Data Bulletin, Oct 2010; available at www.abi.org.uk/Facts_and_Figures/53738.pdf

companies. Employers with higher earning senior staff and a larger number of low paid staff could be put off using NEST as they would have to create a separate scheme for its higher-paid workers.

2.5 Currently, NEST is permitted to accept contributions of up to £3,600 (in 2005–06 prices, equivalent to £4,271 today) per year on behalf of any one employee. The practical impact of this limit, initially designed to ensure NEST was focussed on low and medium-income employees, coupled with the minimum contribution of 8%, is to deny people on modest incomes access to NEST.

2.6 The existence of a hard limit of contributions means that employees whose qualifying earnings fluctuate and might exceed that limit will be auto-enrolled into an alternative, non-NEST, scheme to avoid risk of non-compliance, even if the employee and employer would prefer to use NEST. The only option open, if using NEST, would be to enrol the higher-earning employee into NEST and also into a second top-up scheme for earnings above the NEST cap. This seems a highly bureaucratic approach with no obvious benefit for the employee and additional administrative burdens for the employer.

3. *Possible measures to reduce the proliferation of small pension pots*

3.1 One option available in helping to avoid the proliferation of small pension pots is to require employers to offer new qualifying employees the opportunity to transfer existing pension pots into the new employer's qualifying scheme. Employees should have full disclosure of the annual management costs and any fees associated with the new employer's schemes and be alerted to the need to seek out similar information, if not already known, for any existing scheme.

3.2 As a further measure to reduce the number of small pension pots, and for additional reasons already given above, we believe that NEST should be treated like any other qualifying pension scheme and be allowed to accept transfers in.

16 August 2011

Written evidence submitted by Aviva

1. Executive Summary

1.1 Aviva is one of the world's largest insurance groups with over 53 million customers worldwide and 45,000 employees. In the UK we manage pensions for over two million people as well as over 5,000 company pension schemes. This gives us considerable experience and insight into the important and complex issues associated with the pensions policy world.

1.2 We conduct regular research to better understand the financial concerns of our customers, to ensure our contribution to policy debates is based on real insight. Since 2003, we have conducted a global quantitative study of consumer attitudes to risk, advice, investment and retirement—the Aviva "Consumer Attitudes to Savings" survey; this complements our regular quarterly Real Retirement reports.

1.3 We support the objectives of automatic enrolment and universal pension provision and feel anything which gets more people saving is a good thing. However, we believe the challenge of turning passive investors into actively engaged investors remains.

2. *Auto-enrolment and establishment of the National Employment Savings Trust (NEST)*

2.1 We support many of the changes being introduced through the current Pensions Bill. Many of these changes introduce welcome flexibility to auto-enrolment processes for employers, particularly around waiting periods and certification of contributions. We strongly urge Parliament to pass these reforms and would stress the importance of confirming legislation, and therefore secondary regulations, as quickly as possible to give individuals, employers and the pensions industry reasonable timescales to adapt to the final regulations. As things stand timescales may be tight with final regulations not expected until January 2012 at the earliest.

2.2 We agree that Government needs to encourage more people to make their own retirement provision, due to demographic changes and associated escalating costs of the state pension and other age related welfare costs. We believe broadening access to workplace pensions is a sensible approach which can harness consumer inertia in a positive manner through automatic enrolment.

2.3 It is not yet clear what proportion of the people auto-enrolled into schemes will remain in those schemes and whether there will be any appetite from these joiners to make contributions in excess of the statutory minimum.

3. *Estimated opt-out rates*

3.1 While some commentators are skeptical about auto-enrolment, we[18] have found that the highest percentage of UK families (37%) would be "pleased to be automatically enrolled" and would even "feel valued by their employer" as a result (7%).

[18] Aviva Family Finances Report, Spring 2011.

3.2 Just 15% of UK families said they would choose to opt-out, with the highest percentage of these being single parents (22%) who were also most likely to be concerned about how their "take home" pay might be affected (28%).

3.3 It is interesting to note women—who often have significantly less retirement provision—are more positive about auto-enrolment than men. More (39%) are pleased to be automatically enrolled (men—35%) and just 14% (men—17%) will consider opting-out.

3.4 What was clear from our research was that, while UK families were generally positive about auto-enrolment, there is a significant piece of work needing to be done to inform people of the changes. With not long to go, one in five (20%) have yet to form an opinion on this issue and 12% worry the scheme may not be the best for them.

4. *Communication*

4.1 We very much welcome the £10 million being allocated by the Department for Work and Pensions for a communications campaign to support auto-enrolment and the separate work they are undertaking with employers.

4.2 Our research indicates that, employer communication of the benefits of a workplace pension appears to be crucial to minimising opt-out rates, with 18% of those who are not members of a scheme citing lack of communication as the main reason for not joining.

4.3 Aviva has already launched an auto-enrolment education site for advisers and will be launching a similar site for employers in Q4 2011. Wider and continued communications to all stakeholders to support them through auto-enrolment are being actively considered

5. *Likely impact of auto-enrolment on business*

5.1 There are around a million employers in the UK so the introduction of auto-enrolment in 2012 will cause a significant shift in employers' attitude and behaviour. At present Aviva research indicates just 28% of people have an employer pension which they are actively paying into.

5.2 Creating and administering a pension scheme does lead to immediate and ongoing opportunity and financial costs for employers. Employers will experience two types of cost—one off upfront costs in setting up schemes and responding to the new legislation, and ongoing costs in the form of long-term increases to their pension contributions. We would expect both costs to be a burden to employers, but expect the former cost to decline from 2012 once employers have been phased in and set up appropriate provision although there will be a need to keep this under review.

5.3 The attitudes from employers will be key to the success of greater engagement in pension savings but employer opinions seem to be mixed. Many employers will see auto-enrolment and pension contributions as another burden on business. In addition given that protection for existing schemes is not as complete as we would have liked (eg no "grandfathering" of existing good quality schemes) many existing schemes will need alteration.

5.4 Thousands of employers across the UK currently choose not to provide any employee benefits, beyond the required minimum. Thousands of other employers, however, do invest heavily in developing a rich and varied employee offering.

5.5 Aviva research shows that the offerings vary by size of employer and the range of benefits offered broadly increases in line with the size of employer. Employee appreciation of these benefits is also positively correlated with the size of employer. It should be remembered, however, that only 3.4% of employers in the UK have more than 50 employees (ONS).

5.6 There is a danger any substantial changes to existing schemes may lead to significant administration and compliance costs for employers; consequently employers may seek to mitigate these by levelling down their contributions to the new statutory minimum, to the detriment of existing members. Although certification is welcome—some employers with existing schemes will be able to use an unchanged contribution basis—there remain some issues.

5.7 There are deep seated complications in the use of certification as the rest of the auto-enrolment requirements hinge on the use of banded earnings being the trigger for auto-enrolment itself and liability for contributions. If costs for employers become markedly higher under a certified scheme (than they would under the banded earnings basis) then it is likely employers would level down from existing schemes to a new minimum standard scheme. Grandfathering existing good quality schemes would have been much more effective in preventing such movement.

6. *Self-employed people, part-time, temporary, casual and agency staff*

6.1 Encouraging further savings amongst the self-employed may be more difficult to deliver than amongst employed people.

6.2 A variant of auto-enrolment, will not work as there is no central collection mechanism for the self-employed, unless the Government chooses to act in this capacity or designate a universal provider such as NEST. In addition unless Government wants to make auto-enrolment mandatory for the self-employed on a different basis than the basis applying to employees, there seems no practical way that the current legislation could operate. Certainly efforts to clarify in people's minds the basic level of state pension provision will encourage the self-employed to at least understand where their retirement floor is.

6.3 Given the wide range of possible solutions to retirement saving vehicles that the self-employed may use (including selling the business, working longer, property and equity investment and even reliance on other family members) it is unlikely one solution will appeal to all.

6.4 The legislation does cover part-time, temporary and casual staff and tries to tread a fine line between forcing membership and contributions on a large number of individuals who would not benefit from the experience, and who are more properly provided for under the State system, as opposed to disenfranchising willing savers from participation. Complications inherent in aggregating periods of service and earnings with the same or separate employers mitigate against any further expansion of the legislation's scope and coverage. Some industries may find voluntary solutions to the problem, perhaps by treating employment within a group of otherwise unconnected employers as being continuous. Such initiatives should be supported, but in other respects the current balance—between widening the potential participants and the complications associated with this action—is one that should be supported.

7. *Moderate levels of saving can make a meaningful impact*

7.1 Auto-enrolment mandates a minimum employee/employer contribution of 8% of banded earnings. This minimum will only provide a basic income in retirement and should not be viewed from a policy perspective as a satisfactory outcome. Our challenge is to maximise employee/employer engagement to encourage greater levels of saving.

7.2 Research for Aviva's *Family Finances Report* indicates that when asked how much of their salary they would be prepared to contribute, the most popular response from full-time workers was up to 5% of their salary, if matched by employers.

7.3 For those earning a median UK salary, this would equate to them contributing £1,294 per year and—when combined with matching employer contributions—would represent total pension contributions of £113,872 over a 44-year working life. Using Aviva's pension calculator, a customer might expect a fund of £252,428 (this takes into account inflation and investment growth); this is significantly higher than the current average annuity pot of less than £30,000.

7.4 Our research indicates, 4% of UK families, after living expenses have no additional money, but for 96% of UK families, there is sufficient cash to spend on further expenses. However, just 10% look to put this surplus into some form of retirement savings vehicle. In addition, those who arguably need to take the biggest proactive steps in this arena are least likely to do so—single parents with one or more children (4%).

7.5 Aviva's latest Consumer Attitudes to Savings survey (May 2011) shows the majority of UK adults feel they will need at least half of their regular monthly income to "get by" in retirement and two thirds to be "comfortable". So there is clearly work to be done to meet these expectations.

7.6 It is important for people to realise that even if the entire gap is not plugged, even moderate levels of saving can make a meaningful improvement to their retirement.

8. *Transfer of low value pots*

8.1 A key benefit for NEST over other forms of private sector scheme is that the member's pot can stay in one place, irrespective of changes of employer. This option is not available for savers under the private sector alternative as generally the member would accrue benefits under a different scheme on any change of employer.

8.2 People are increasingly contributing to several private pension schemes during their working lives. Aviva research suggests one in three workers (30%) have five jobs or more throughout their lifetime. However, a worrying number of people are failing to keep details of their different pension pots, which could ultimately affect their private pension income in retirement. And nearly two thirds (60%) are unaware they can combine their private pension pots at retirement, potentially increasing their retirement income.

8.3 This means many people retire with a number of small pots—this increases the running costs for pension schemes and places restrictions on who providers can profitably serve. Removing this problem could significantly reduce the running costs of existing schemes and help customers manage their finances more easily.

8.4 We believe legislation should allow automatic transfers of small auto-enrolled pension pots, so savings pots follow members when they move jobs. This could be facilitated through a form of centralised clearing house to match the ceding company with the receiving company and then transfer the funds.

8.5 Much of the current transfer legislation has been built on the basis that members actively take out contracts or agree to scheme membership and thus should actively wish to move values between contracts.

This is not the case for auto-enrolling members. Aviva believes there would be value in changing the requirements for this sub-set of transfers so auto-enrolled members can obtain the benefits of aggregation without an expectation that they become active investors post auto-enrolment.

8.6 Aviva has done further work on this subject which we would be pleased to share with the Committee. We are convinced automatic transfers could improve outcomes for employers, members and providers.

Transfers to and from NEST

8.7 As an extension of the change recommended above, there will be circumstances where a small value pot is created but there is no active scheme willing or able to accept this when the employee ceases employment or becomes self employed.

8.8 To maximise the benefits for scheme members and ensure they can clearly understand their overall pension values, especially if they have an existing NEST pot, non-NEST schemes should be permitted to automatically transfer small pots into NEST. This also has the potential benefits of both reducing the costs of non-NEST schemes and increasing the funds under management for NEST. The restriction on transfers into NEST should be removed to facilitate this.

9. *UK Residency*

9.1 Aviva has one remaining concern with the proposed automatic enrolment legislation, which we believe could be easily amended through the Pensions Bill even at this very late stage.

9.2 Currently legislation compels employers to automatically enrol all UK jobholders into a qualifying scheme, irrespective of where they are permanently resident. For example this includes employees of a Northern Irish company working in Northern Ireland but resident in the Republic of Ireland, or a French national working during the week in London but residing in France. Both of these groups of people are permanently resident in their national "country of origin" rather than the country in which the job is undertaken.

9.3 A partial exemption has been proposed for employers using occupational pension schemes, where the employees are resident in another EU Member state, to prevent the scheme from having to comply with the cross border requirements of the Institutions for Occupational Retirement Provision (IORP). However, there is no such protection for employers using personal pension schemes or if the employees are resident in a country outside the European Union (whether the employer offers a personal pension or any other form of scheme). Although it is doubtless possible for personal pension providers to avoid the complications associated with writing business with non-UK residents by refusing to accept the business entirely, this does not help the employer who retains this liability.

9.4 If their provider refuses to accept a non-UK resident into the scheme, to be compliant the employer would need to try to auto-enrol European resident employees into NEST or an alternative occupational pension scheme. Only then are they regarded as meeting their duty under the legislation although these employees may not end up in a scheme. But why make employers go through this routine, which is ineffective anyway if the employee resides outside the European Union?

9.5 Aviva believes it should be explicitly stated that employers will not be required to automatically enrol UK jobholders who are not UK permanent residents or otherwise fall within the territory of the UK for the purposes of sales and marketing. This will ensure all employers are able to simply and efficiently fulfil their legal duties with regard to automatic enrolment whilst avoiding any conflicts or expensive workarounds to balance the different requirements of local and international law, particularly where this may be impossible. A very minor alteration to the 2008 Pensions Act through the current Pensions Bill will achieve this.

10. *Behavioural change*

10.1 Aviva accepts that auto-enrolment does work with general customer inertia, though this could be a double-edged sword. The challenge of turning passive investors into actively engaged investors remains.

10.2 The worst possible scenario would be for very large numbers of people to spend a number of years in a system they don't engage with and then, when they do realise what has happened, for those same people to turn against the system and pension providers.

10.3 Although the legislation does insulate scheme providers and employers against legal action from members who have been auto-enrolled into a scheme which does not deliver to expectations, auto-enrolment by itself does not lead to the ideal market that we might wish for.

10.4 Only when the retirement market does operate with a more pro-active, engaged and informed customer population will the problem really be solved. Given the complexity of the decisions required from customers, this ideal outcome is still some way off. However, to begin with we would suggest:

Engaging the young

10.5 To get people in the habit early in life, new models should be considered for young people to address their conflicting financial priorities (paying off student debt, saving a deposit on a home or even saving for a holiday). Incentivising workplace ISAs (Individual Savings Account) for young people may be a great bridge to longer-term retirement savings. It would also give them flexibility, with the knowledge that the cash can be used to fund a house purchase or other spending rather than be locked away for up to 40 years.

10.6 Recent Aviva research found such an alternative would be especially attractive to the young (under 25s)—54% felt allowing early access to savings (eg via a workplace ISA) could encourage them to save more, compared to only 30% of the working population in general. We recognise there are a number of significant challenges associated with operating true workplace savings contracts but believe the benefits of providing such a product could be substantial. For the avoidance of doubt, we are not supportive of allowing early access to specific pension savings as we believe this would add considerable further complexity to pensions tax legislation.

Communicating the state pension

10.7 People need to understand their own financial position to make clear plans for retirement saving. Making available simple, accessible information about what the state provides would help create an explicit platform on which individuals can build their own nest eggs. Aviva believes all citizens should receive regular pension statements. This would help them consider the state pension as only part of a mixed strategy for providing for their future, and prompt them to take action as a result of seeing clearly what they stand to get in retirement. Proposals to move to a standard, flat rate pension over time will clearly help people develop this understanding and make it much easier to communicate the mix of state and private provision people should expect or plan for in retirement.

19 August 2011

Written evidence submitted by the Centre for Retirement Reform (CRR)

The CRR

1. The CRR is a think tank and lobbying body set up to help bring about the reform necessary to produce better retirement outcomes for the people of Britain. Although the pensions arena continues to go through change and restructuring, to date this has fallen well short of the root and branch reform required to address the biggest issues affecting retirement now and into the future. The CRR works collaboratively with an extensive range of stakeholders with an interest in retirement savings policy to facilitate a constructive and innovative dialogue to inform the policy debate.

2. The CRR believes three fundamental changes are necessary:

- To facilitate positive public attitudes to longer working lives, flexible retirement concepts and saving for retirement.
- To support the implementation of a policy framework for flexible retirement which is simple, fair, affordable and meaningful.
- To develop a new savings products framework and infrastructure that is attractive to and meets the needs of the public.

These crucial changes are the essential first steps required in a holistic programme of reform; work which will also address the challenges of an older workforce, healthy ageing, long-term care and improving longevity.

Response to Issues

1. *DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees*

We are totally supportive of this initiative from the DWP. We have to communicate with and educate the target market, most of whom will not have been previously saving for their retirement.

2. *Arrangements for phasing and staging the introduction of auto-enrolment*

As employers have already started planning, it is important that these dates are not now changed.

3. *Likely impact of auto-enrolment on business, especially small and micro-businesses*

This will depend on the number of employees that are already in the company pension scheme. A significant number of employers will see a substantial increase in their costs where they have a predominately un-pensioned workforce.

4. *Role of The Pensions Regulator (TPR), including in certification of schemes*

TPR should not be promoting NEST (National Employment Savings Trust). NEST is just another provider and should be competing on level terms with existing providers. Rather than suggest, for example, that certain employers should use NEST, their advice to employers should be that they should select a scheme with the following characteristics (….) so as not to exclude existing providers.

5. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

It is assumed that the reason people aren't currently contributing to a pension scheme is due to the complexities. With inertia, it is hoped that we will see opt-out rates of around 25% however we may be wrong and perhaps people are consciously deciding not to save for their retirement through a pension scheme.

6. *NEST's potential market share and the possible effects on other providers*

7. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

NEST's role is to complement good existing schemes not to compete against them. Historically, the lower-to-moderate earner market has not been attractive to the typical commercial pension provider. However with the likely benefits of scale, we may see new entrants to this market.

8. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

It's correct that transfers should not be allowed until the matter is reviewed in 2017. This would undermine good existing pension schemes that have invested significant money to establish pension schemes without any form of government support.

9. *NEST's investment strategy*

NEST's investment policy for younger new joiners seems ultra conservative. The younger scheme members will be enrolled into their year of retirement target date fund by default and these funds should have a growth objective over the long-term. The investment policy is based on significant research amongst the target market and this research does show that the target group is conservative when it comes to pensions. However, this is where the need for education becomes imperative to enable individual needs and expectations to be met through active individual choice. Anyone can opt to go into a more aggressive growth fund which is available—but that requires active engagement by the member as they have to switch from the default.

Until NEST's set-up costs are recuperated, which could take as long as 15–20 years, their initial charge of 1.8%, plus an AMC (Annual Management Charge) of 0.3% are comparatively high in comparison with the rest of the market. Whilst this may be good news in the short-term for NEST's competitors, in the longer-term it could give pension saving a bad name, with some NEST investors seeing higher returns in a building society account with immediate access.

Again education is key as it is important to factor in the benefit of the employer contribution and the tax relief which would give an overall greater return for most people.

Therefore, the challenge is to decide how to educate, not just respond to research. NEST should have a real and important role in doing this with their principle of being an exemplar of good governance.

While NEST will operate with an AMC of just 0.3%, there is an additional initial charge of 1.8%. Of course, NEST needs to recoup its start-up costs, which will not be insubstantial. But their target market is primarily those new to pension saving.

In many cases, savers may find it difficult to figure out whether they are better off paying an initial charge of 1.8% with a 0.3% AMC or simply going for a scheme with a 0.5% AMC. Clarity of charges should mean the exact opposite. Factor in that people are moving away from retirement at a specific date to flexibility based on the size of their pension fund and their ability to work, perhaps on a part-time basis, and it makes those sums incredibly difficult.

10. *Possible measures to reduce the proliferation of small pension pots*

There are two distinct issues here; small pots that result during working life and small pots at retirement.

For those that develop during working life, we should look at making the transfer process simple for small pots; perhaps even giving consideration to automatic transfers (with an opt-out) when changing jobs.

At retirement, this could be simplified by allowing contract-based schemes to make one lump sum payment per individual per scheme of up to £2,000 based on the triviality rules but irrespective of whether or not the individual had already received a genuine triviality payment.

11. *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications*

12. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

Inertia should mean that the desired behavioural change will happen. In addition, we need to move ahead with the introduction of the universal state pension so that everyone who saves in a pension scheme will be better off at retirement than those who don't save.

23 August 2011

Written evidence submitted by the Society of Pension Consultants (SPC)

Introduction to SPC

1. SPC is the representative body for a wide range of providers of advice and services to work-based pension schemes and to their sponsors. SPC's Members' profile is a key strength and includes accounting firms, solicitors, insurance companies, investment houses, investment performance measurers, consultants and actuaries, independent trustees and external pension administrators. SPC is the only body to focus on the whole range of pension related services across the private pensions sector, and through such a wide spread of providers of advice and services. We do not represent any particular type of provision or any one interest—body or group.

2. Many thousands of individuals and pension funds use the services of one or more of SPC's Members, including the overwhelming majority of the 500 largest UK pension funds. SPC's growing membership collectively employs some 15,000 people providing pension-related advice and services.

Summary and Introduction to our Comments

3. We have prepared these comments on the basis that the short to medium-term operation of auto-enrolment and NEST (National Employment Savings Trust) has already been subject to an independent review, commissioned by the current Government, and, subject to the finalisation of detail in some areas, is now fixed and must remain so, so that the considerable undertaking of preparing for and implementing auto-enrolment can proceed on firm foundations, even if they are not the foundations which everybody might have themselves chosen.

4. This work is now underway, but at this stage it is too early to identify where it has gone well and where it could be improved.

Comments on the Matters Raised by the Select Committee

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

5. DWP has clearly communicated its strategy in meetings, in which we have participated.

6. DWP has now started work on developing templates, which employers may use in communicating with employees on auto-enrolment. The development of the templates is perhaps less advanced than we might have expected, although we understand that this is due to the need for DWP to secure the necessary budgetary clearance within Government for implementing its strategy.

7. In developing its strategy, DWP will need to act in coordination with the Financial Services Authority, The Pensions Regulator and with potential providers of information and advice in the private sector. We have been encouraged by DWP's willingness to inform and consult with SPC.

8. In order to successfully implement its strategy, DWP will need not only to communicate and to provide advice and support, but, in the case of employers, will need to secure their active engagement.

9. DWP will require the resources to actively promote what it has to offer, rather than to simply place the information on its website in a low-key way.

10. Our expectation is that the challenges in successful implementation will be greatest among small and micro employers.

11. In the case of employees, DWP's approach will need to be different. The key aim here is not that employees be engaged, although that is desirable, but that once auto-enrolled they do nothing to change their status.

Arrangements for phasing and staging the introduction of auto-enrolment

12. The briefest consideration of the guidance material, which has now been published by The Pensions Regulator, serves to illustrate that the arrangements for phasing and staging the introduction of auto-enrolment are far from simple. We also consider that they are still not yet fully understood by employers.

13. Specifically, we believe that there is still incomplete understanding of:

— The relatively narrow transitional period for defined benefit schemes.

— The fact that contributions will not be payable at their full rate immediately.

— The arrangements for multi-employer PAYE (Pay As You Earn) schemes.

Likely impact of auto-enrolment on business, especially small and micro-businesses

14. This will not be unique to small and micro-businesses, but we expect that the additional cost arising from employer contributions in respect of auto-enrolled employees and the administration costs of deducting and remitting employer and employee contributions will bear most heavily on small and micro-businesses.

15. We would expect businesses to seek to counteract the costs by restricting their wage bill and/or, if their market will permit it, by increasing their prices.

Role of the pensions regulator, including in certification of schemes

16. As already mentioned, The Pensions Regulator has published guidance material on auto-enrolment, which it intends to update as the detail of the requirements on auto-enrolment are finalised. There is, limited practical experience of using the guidance, but our initial impression is that it is generally helpful and we are confident that the Regulator will be willing to listen to suggestions for improving it in the light of practical experience.

17. The Pensions Regulator faces a very significant challenge in monitoring compliance with the auto-enrolment requirements, bearing in mind that compliance with this new set of requirements will be much more complicated than compliance with the existing Stakeholder requirements.

18. The monitoring will extend beyond certification into processes for auto-enrolment and deduction and remittance of contributions and the scope for the Regulator to actively police certification within its available resources would seem to be limited.

19. It would seem inevitable that the Regulator will need to rely heavily on whistleblowing.

Estimated opt-out rates, including the possible impact on nest if the numbers auto-enrolled are significantly lower than predicted

20. The economic climate is significantly less friendly than when auto-enrolment was conceived and we would therefore expect that opt-out rates will be higher, particularly among the lower paid (ie the target market for NEST) than might have been originally expected, given the immediate pressures on budgets.

21. Perhaps the public and retail sectors are areas where this might be particularly the case.

22. In general, we expect that media comment will play an important part in influencing trends on whether opting-out is perceived to be appropriate or not.

23. For NEST, the main potential impact would appear to be that, if opt-out rates are higher, and this results in it having fewer than planned members, it will have to maintain the temporary charge on contributions for longer, to compensate for a lower yield from the charge.

Nest's potential market share and the possible effects on other providers

24. If the market develops as planned, NEST should have limited impact on other providers, since it is designed to provide a home for contributions from lower paid workers, which are not normally a commercially attractive proposition for other providers.

25. The exception would probably be those providers with a significant presence in the Stakeholder pension scheme market, in which NEST would appear to constitute direct competition.

26. If opt-out rates are so high that NEST is threatened with not being viable if it continues to cater only for its original target market, and moves into areas already catered for by other providers, there could be tensions, given the very substantial State support, which only NEST effectively enjoys.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

27. There is already evidence that auto-enrolment has attracted at least one new potential overseas provider.

28. It has also provoked new interest in the provision of master trusts, which have long been available in the UK, but relatively little used.

29. Another potential development is that providers, whether of master trusts or other types of scheme, will begin to offer employers management of the entire auto-enrolment process as a distinct service.

Likely impact of the limitations placed on nest, including the contributions cap and the ban on transfers

30. The contributions cap and the ban on transfers are due to be reviewed in 2017 and our assumption is that, as a result, both will then be removed. So we assume that any impact of either limitation will be relatively short lived.

31. The contributions cap is a reasonable reflection of the fact that NEST is intended to cater for lower paid workers, whom one would not expect to be in a position to make contributions greater than the capped amount.

32. Whether transfers in are allowed or not, there is an argument that transfers in of small amounts might in some cases be inappropriate, given the contribution charge, which NEST will initially impose.

NEST's investment strategy

33. In the same way that the charges under Stakeholder schemes stimulated considerable discussion and action on charging structures among pension providers generally, NEST's intended investment strategy has stimulated considerable industry debate.

34. It is striking that NEST's approach in the early years of membership is primarily influenced by the aim of persuading members to remain, by minimising the chances of losses, rather than of maximising returns, although it is generally accepted that losses, which can arise from this aim, can most easily be absorbed then.

35. It will be instructive to observe the actual effect on fund growth of the approach to be taken by NEST.

36. The announcement by NEST, that any investment losses will be attributed to employer contributions is sensible, given the aim of avoiding early losses on employee contributions. NEST is constituted as an occupational pension scheme, and is therefore not directly subject to regulation by the Financial Services Authority (FSA), but it would not be surprising if in practice it looked very like a large contract based provider, which would be subject to FSA. We are not sure that FSA would allow the approach which NEST intends to take and we suggest that it should be for consideration whether FSA should permit the same approach.

Possible measures to reduce the proliferation of small pension pots

37. We suggest that the most straightforward way of reducing the proliferation of small pension pots at present would be to liberalise the rules on so called trivial commutation, which allows a small pension to be converted into a lump sum.

38. It is also often suggested that it would be desirable to amalgamate small pension pots, but this is difficult under present rules without the active consent of the individual, particularly in contract based arrangements.

39. It is often suggested that some form of transfer without individual consent to a safe harbour destination should be easier.

40. NEST is sometimes suggested as such a destination, although, as we have previously commented, its planned contribution charge might not, on the face of it, make it a particularly attractive destination for small pots.

41. Another approach, which could be attractive in principle, would be to allow the small pots to be used to buy additional State pension entitlement. This could be worth exploring further, although we suspect that the government might find the idea unattractive, since there would inevitably be administrative implications for the State scheme.

How self-employed people and part-time, temporary, casual and agency staff will be treated under auto-enrolment

42. We would expect one of the largest practical challenges to be to assess whether or not people in these categories are job-holders, which in turn influences how they are treated for auto-enrolment purposes.

43. The rules of NEST and the auto-enrolment regulations generally have not made it particularly straightforward for employers of part-time, temporary, casual and agency staff to voluntarily auto-enrol them, whether or not they are actually required to do so.

44. It would not be surprising if in practice people in these categories, who will often have unpredictable and fluctuating pay, are among the largest categories of opters-out.

45. Also, achieving further savings amongst the self-employed may be more difficult than amongst employed people, since auto-enrolment will not apply to them. It is particularly important that the self-employed understand what the basic level of State Pension provision is, so that they at least understand where their retirement provision floor is.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

46. We expect that auto-enrolment will increase the aggregate amount of pension saving. However, the initial minimum level of contributions will not generate funds which will produce an adequate requirement income.

47. For auto-enrolment to fundamentally change attitudes to retirement saving, employers of all sizes will need to be engaged in the process and be fully compliant.

48. A real strengthening of engagement among individuals will only occur when their pension pots have grown to a reasonable size. It is sometimes suggested that this happens when the amount in the pensions pot is equal to a year's pay.

49. Given current minimum contribution levels, even if individuals do not opt-out, this stage could take a considerable time to reach. However, it is important that individuals understand that even moderate levels of saving can make a worthwhile difference in retirement.

50. Concerns remain that, for the lower paid, auto-enrolment will in effect simply cancel out entitlement to means tested benefits, to which the individual would otherwise have been entitled.

23 August 2011

Written evidence submitted by Chartered Institute of Personnel and Development (CIPD)

Background

1. The CIPD's primary purpose is to improve the standard of people management and development across the economy and help our individual members do a better job for themselves and their organisations. The Public Policy team at CIPD promotes an agenda for productive workplaces to boost economic performance and improve the quality of working life.

2. As Europe's leading professional body for those involved in the management and development of people, we are ideally placed to contribute to the development of public policy across the spectrum of workplace and employment issues.

3. We are able to draw on the experience and knowledge of our 135,000 members and our wide range of research to provide a pragmatic stance on public policy that is based on solid evidence and the real world.

4. Our membership base is wide, with 60% of our members working in private sector services and manufacturing, 33% working in the public sector and 7% in the not-for-profit sector. In addition, 76% of the FTSE 100 companies have CIPD members at director level.

5. In creating our response, we consulted with some of our senior members that have experience of pensions in a professional context.

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees.

6. The DWP is responsible for the provision of advice and support to employees, whereas The Pensions Regulator (TPR) is responsible for the provision of advice and support to employers. The CIPD and some of its members have been in regular contact with both the DWP and TPR commenting on their communication material. We were initially concerned that TPR and the DWP would be working on 2012 communication in isolation from one another, but from our meetings this does not appear to be the case.

7. However, members are still unsure as to what the DWP and TPR communication strategy actually is, pointing out that they have yet to see any "concrete details". **We recommend that both TPR and the DWP need to be clearer in communicating their strategy to employers.**

8. Another CIPD concern is not so much the strategy itself as its execution. There is a fear shared by our members that employers will end up paying for most of the communication process, *as well as* paying for employees to be enrolled and subsequently contributing to their pension schemes. One of our members commented: "*My suspicion is that costs will be cut in the communication area and the Government will rely on employers to do the bulk of the communications required. Pensions is an area that most employees do not understand and there needs to be Government sponsored communication to support what employers are doing*". CIPD Member, travel firm

9. There is also apprehension over whether the eventual employer and employee communication material will be fit for purpose, given the current low level of awareness amongst employees of the upcoming reforms. The CIPD Summer 2011 *Employee Outlook* survey found that just 46% of employees working in the private sector and 42% of those employed in the voluntary sector were aware of the 2012 auto-enrolment plans.

10. Within the private sector, awareness was much higher among those working in the finance (57%) and construction (54%) sectors. The people least cognizant were those working in the hotel and catering sector

(30%), which often employs young workers and who will be among the most affected by auto-enrolment. Among the 18–24 age group working in the non-public sector, just over three in ten (31%) were aware of these pension reforms, increasing to two in five (40%) among the 25–34 age group.

11. By age, the employees most conscious of the changes to pensions are those aged 55 and over (57%) and those aged 45–54 (45%). A similar pattern in the non-public sector can be found by level of seniority, with those in non-managerial roles being less conscious of the change than those in managerial roles.

12. In addition, men (54%) are more aware of the reforms than women (38%). There are also regional differences: those working in Yorkshire and Humberside (51%) and the South West of England (51%), are more aware of the changes than those employed in Wales (35%) and the North West of England (43%).

13. The CIPD's public policy manifesto, *Platform 2011: A blueprint for growth,* called on the Government to support employer efforts to communicate changes brought about by auto-enrolment and the creation of NEST (National Employment Savings Trust). We welcome the Government's commitment to providing advice and support to both employers and employees, as without it, there is a risk that people may opt-out or fail to opt-in when it is in their interests to do so, simply for lack of awareness about what the reforms entail. **However, we recommend that the DWP and TPR adopt a tailored approach to communications that accounts for differences in age, gender and industrial sector.**

14. The communication duty is quite extensive; not only does the employer have to communicate to employees being enrolled in to a pension; they also have to communicate to those who have *not* been enrolled. In many instances, this will be with employees who have not been enrolled because they are already in the company pension scheme, which seems rather a waste of employer resources. We hope that the government will recognise and incorporate this into their communication plans.

Arrangements for phasing and staging the introduction of auto-enrolment

15. From an employer perspective, phasing and staging the introduction of auto-enrolment makes sense. Firstly, it allows employers to prepare their HR and payroll systems for identifying who to enrol and who needs to be communicated with and the message that they should receive.

16. Secondly, it will better allow many employees to deal with the impact of the HMRC's initiative to move PAYE (Pay As You Earn) to real time information (RTI) reporting, which is being brought in between April and October 2013. As a consequence, some of our members will be juggling the implementation of auto-enrolment alongside RTI. There is also the possibility of additional change if Income Tax and National Insurance contributions are merged.

17. Thirdly, phasing will allow employers to better plan for the costs associated with enrolling employees into a pension scheme (such as contribution and communication), especially at a time of uncertain economic growth.

18. From the employee perspective, phasing in their contributions may encourage them not to opt-out of a workplace pension compared with paying the full contribution straight away. Our *Employee Outlook: Focus on pensions* showed that 21% of employees said they would not be able to afford to contribute anything if they were to be enrolled into a pension scheme immediately, whereas this dropped to 18% when asked about contributions being phased in over five years (as per the 2012 reforms). This suggests that phasing in employee contributions may lead to fewer employees opting-out of workplace pensions as they are more able to adapt to a drop in take-home pay.

Likely impact of auto-enrolment on business, especially small and micro-businesses

19. All businesses will see their costs increase, how able they are to absorb these additional costs will depend on the strength of the economy at that time. The CIPD's 2011 *Reward Management* survey found that more employers would increase the value of their pension offering than would reduce it, suggesting that if economic growth is poor then the extra cost may be offset in the future by lower wage growth and a reduction in hiring intentions.

20. With respect to micro and small employers, the ability to absorb the additional costs will depend on how well they are doing financially. For some, they will have to balance increased pay roll costs caused by auto-enrolment and rises in the National Minimum Wage. Hopefully, by the time small and micro employers have to enrol their employees, the economic outlook will have improved.

21. On a more practical note, there is still some confusion among our members about what to do if the company has a number of subsidiaries with their own PAYE references and whether these should be treated as separate entities for staging dates. **We would call on DWP/TPR to ensure clarity in this area as quickly as possible.**

Role of The Pensions Regulator, including in certification of schemes

22. We believe that TPR should be able to cope with the first few years of auto-enrolment, when it will be dealing with a relatively small number of very large employers. However, before long it will be dealing with a very large number of small employers. Members are not sure that TPR will have the resources to be able to

cope during the later period of auto-enrolment, when small and micro employers start to become involved. As one employer commented: *"We need a slick and simple process for certification, otherwise the regulator will get swamped administratively."* CIPD member

Possible measures to reduce the proliferation of small pension pots

23. Options favoured by members include increasing the trivial commutation threshold to allow higher amounts to be paid as a lump sum, making it easier for employees to aggregate small pension pots and allowing the possibility of cashing out *de minimus* account values.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

24. Members thought that part-time staff will not be treated any differently to full-time staff as they already allow part-time staff to join the existing pension scheme. Some members are planning to treat all employees on the payroll the same, but exclude external temps or contractors. Others may exclude some temporary workers if they are paid interns or students on a work placement scheme.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

25. We welcome the introduction of auto-enrolment as a step in the right direction towards encouraging people to save more for their retirement. Our 2011 *Employee outlook: focus on pensions* found that 17% of employees not currently in a pension scheme would prefer to be automatically enrolled by their employer rather than simply being offered the chance to join.

26. The report also showed that the most common employee explanation for not belonging to a company pension was because there was not a pension scheme to join. In most instances there probably was, but it either did not attract an employer contribution, or it was not communicated effectively to employees, with the result that employees were either unaware of its existence or did not value it. There is a strong argument for employers communicating as clearly as possible to workers the implications of auto-enrolment and how it will work on a practical level. Our research shows that 44% of employees would be encouraged to save more if they knew the size of the pension pot they would need to retire comfortably, whilst 19% would be more likely to join their employer's pension scheme if they had a better understanding of it. However, as mentioned previously, the Government must support employer efforts to communicate these changes, so that the burden does not fall solely on employers.

27. The CIPD 2011 *Reward Management* survey found that around 20% of manufacturing and production companies and 16% of private sector firms already automatically enrol employees into their workplace pension scheme. However, we would be reluctant to infer that their experiences of worker take-up would be applicable across the whole private sector. In addition, the figures could be impacted by other factors, such as the level of employer contribution, amount spent of employer communication and education, level of union engagement, *etc*.

28. So, we predict that auto-enrolment will lead to more individuals saving more, but whether they will be saving *enough* will continue to be a concern. As tough economic circumstances, combined with lower pay awards, continue to exert pressure on employees' take-home wages, there is a possibility that people will sacrifice pension saving in order to cope with squeezed living costs. Affordability is a key concern for employees at the moment, and one of the main reasons why many are not currently in pension schemes.

29. Our *Employee Outlook: Focus on pensions* showed that 21% of employees felt they could not afford to join a pension scheme, whilst 13% reported having more pressing financial priorities. As mentioned, we believe that staging employee contributions over five years will ease the financial burden on many employees and facilitate greater take-up of workplace pension schemes. **We also hope that the Government pays close attention to the opt-out rates for auto-enrolment, and considers a suitable strategy for re-engaging employees, if the policy appears not to be increasing saving rates.**

24 August 2011

Written evidence submitted by Forum of Private Business

Introduction

The Forum of Private Business is a proactive, not-for-profit organisation providing comprehensive support, protection and reassurance to over 18,000 small and medium-sized businesses. We add value to businesses through a collective voice for them in local, central and European Government, and the provision of tailored solutions that promote business success.

Research to support this response comes from our Employment Law Panel and Referendum 196, as well as other research publications. Our Employment Law Panel comprises approximately 140 members who have volunteered to provide feedback to us on employment law matters.

Summary of the Forum's Position

The Forum of Private Business understands that, at a time when the public sector is facing significant pension reforms, the Government desires that the private sector also do its bit to encourage employees to save for their future. At present around 36% of people in employment in the private sector are members of workplace pension schemes, as opposed to 84% in the public sector.[ii] We also recognise evidence that points towards a higher percentage of employees saving for their pension if schemes are "opt-out" rather than "opt-in". We recognise that all the significant political parties support the introduction of auto-enrolment for all employers over the next few years.

The majority of respondents to a Forum of Private Business survey opposed the introduction of auto-enrolment.[iii] They believe it would be too costly, add more to already heavy administrative burdens and erode the principle of personal responsibility. However, recognising the political backing of auto-enrolment the Forum has limited its comments in this response to how best the process can be introduced for smaller businesses.

First of all, we believe the timing of the current proposals is an issue. It is clear from surveys that businesses still lack confidence over the economy. This lack of confidence plays a direct role in recruitment and investment decisions. Whilst acknowledging that small businesses will not be liable to enter auto-enrolment schemes until 2014 at the earliest—under current proposals—we feel further flexibility should be given to entering the schemes, so that businesses can enter at a point at which they feel financially and administratively able to cope with the additional demands. In this call, it should not be forgotten that a moratorium exempting micro-businesses from new domestic regulations ends in April 2014. New pension arrangements during this time will be just one of many new regulations micro-businesses will suddenly be faced with, creating a potentially overwhelming flood of regulation at once.

We recognise that this recommendation does not come without its difficulties. Specifically, more flexibility would cause problems with the movement of individuals between businesses and with changes to the size of a business, when that change means the number of employees will trigger a business to become eligible for auto-enrolment.

However, this argument is further supported by a confused and under-funded communications strategy. We hope that NEST will go a long way to resolving this problem and fully support that organisation. In the meantime, there does not exist at present a coordinated and consistent strategy across different government departments and we have fears that the current budget for communicating employers' obligations is insufficient. The Government needs to make a concerted effort to ensure employees know they will be subject to salary deductions for pensions from 2014. This will help defuse potential confrontation between employers and employees when auto-enrolment is imposed. On this final point the Forum will play a role in educating members over the responsibilities of auto-enrolment and support them as much as possible in getting use to the new arrangements.

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

There are three distinct concerns that the Forum would like to highlight in the communication strategy to date; the budget, the consistency of communications and the clarity of responsibilities.

Communications budget

Making Automatic Enrolment Work, the review for the DWP in October 2010, stated:

> *"We believe in addition that there needs to be a well structured and concerted communications exercise to ensure that as many small employers as possible know and understand what is expected of them."* [iv]

The Forum agrees that clarity of the process is absolutely vital to ensuring businesses know what is expected of them. However, the Forum has concerns over the size and scope of the communications budget that the Department for Work and Pensions has to inform small businesses of proposals. The Forum understands that an initially sizeable communications budget was frozen after the 2010 election. We seek assurance that the Treasury will be granting a budget to inform small businesses in particular of their duties and seek to know the scope of that communications campaign. The Forum itself will ensure pensions changes are communicated to all its members.

Consistency

In July the Forum received a press release from the Department of Work and Pensions concerning auto-enrolment. The press release concerned a new language guide meant to simplify administration for employers. However, the release stated:

> *"From October 2012 all employers will have to enrol eligible workers into workplace pension schemes."*

The Government has been at pains to inform businesses of the tiered introduction to auto-enrolment, with the biggest businesses leading the way and smaller employers—in some cases—not due to enter the scheme until April 2016. However, any small employer reading this press release and lacking that wider knowledge will have been a little shocked to learn this liability will hit them in just under a year. Press releases like the one highlighted do much to undo the messaging about the roll-out of auto-enrolment and we urge the Government to ensure there is consistency across departments in this area.

Clarity

The financial impact on businesses that comes with auto-enrolment necessitates clear roles and responsibilities for businesses. At present, the Forum feels there is much scope for improvement. Taking one example—the categories of businesses for rollout times—there are, at present, nearly 50 separate rollout dates for businesses, and 20 for small businesses alone.[v] It will be necessary for all relevant government departments—BIS (Department of Business, Innovation and Skills), HM Treasury and DWP—to ensure businesses know when they are due to become enrolled and make sense of the minefield of categories that exist at present. Guidance specifically aimed at small employers would also be welcomed.

Arrangements for phasing and staging the introduction of auto-enrolment

The Forum believes a phased roll out is the correct way of introducing auto-enrolment pension regulations. The smaller the firm the less likely they are to have a dedicated HR function and therefore the more onerous are the regulations. However, we believe that for small and micro-sized businesses, more leniency needs to be shown as to when businesses auto-enrol their staff.

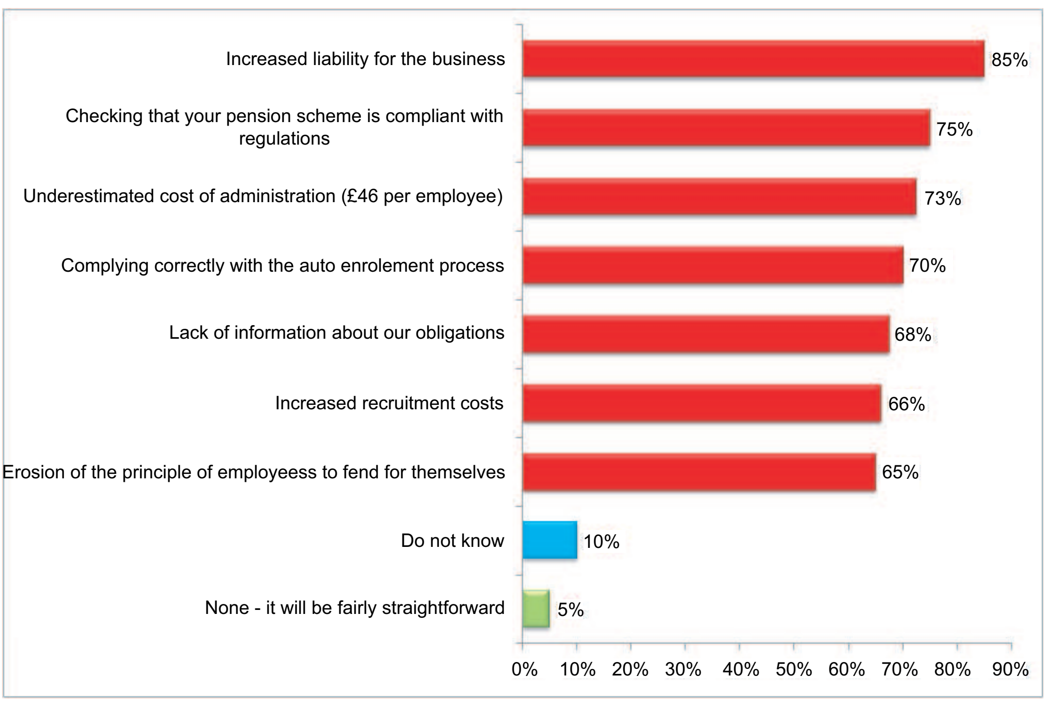
There is already a huge communication challenge for the Government to ensure businesses are aware of their obligations under auto-enrolment. A recent survey suggests 45%[vi] are still unsure of these rules, and whilst awareness is likely to increase over the next couple of years, we believe a more understanding approach to smaller businesses is appropriate. That is why we are suggesting that all micro and small businesses are given more time before being asked to auto-enrol their staff. Businesses must be sure that pension contributions are affordable in an uncertain economic climate.

We welcome the leniency given to new businesses that start-up during the next few years, who will have until the end of the rollout process in order to auto-enrol their staff.

Likely impact of auto-enrolment on business, especially small and micro-businesses

While the Forum recognises the need for the private sector to ensure employees begin to save for their future, there remain a number of concerns about the impact of auto-enrolment on small and micro-businesses.

Figure 1 below shows the main areas of concern from a poll taken in April 2011.[vii]



Increased liability

Cost was the biggest issue, particularly amongst businesses that are still struggling to make significant profits. Almost everyone who had concerns about the pension changes were concerned about the increased liability for the business. Current proposals detail this as 1% of employee salary initially, rising to 3% over time. Further increases may come in the future. It may also be a factor in the recruitment of new staff, though the low liability suggests it will be a minimal consideration. Exporters were particularly concerned about how these costs would impact on their competitiveness with China and other key high growth economies.

A number of questions remain about the affordability of proposals. With the minimum wage due to rise in October 2011 and likely to continue to rise in the future, some businesses will undoubtedly choose to provide pension payments rather than provide an increase in salary to staff. We envisage further problems if employees choose to opt-out of pension arrangements and then ask for an increase in salary instead, creating potential issues over differing levels of salary paid for identical job roles. Whilst common sense would suggest that an individual employee has taken the decision to receive a higher wage instead, we are not sure as to what legally vulnerabilities this may open a business to.

Cost of compliance

The cost of compliance encompasses the costs of understanding the new proposals, the costs of ensuring an existing scheme qualifies and finally the time costs of actually administering the scheme.

Despite the fact that Forum members are twice as likely as other SMEs (Small and Medium-sized Enterprises) to take financial advice, pension schemes are still a big worry for our members as they combine complex financial products with employee rights. Part of this problem stems from the failed initiatives in the past. The scrapping of ACT in 1997, pension scandals in the late 1980s and the creation of a stakeholder pension (which one respondent said that none of their employees took up) has led to scepticism from employers and employees alike.

Over 70% of respondents were concerned about the various administrative aspects of the regulations, with 75% worried about their own scheme's compliance, 73% about the real cost of administration and 70% worried about how to apply the auto-enrolment process. Even for those that feel they do understand the pensions industry, 68% felt that there was a lack of information about the obligations for smaller firms and even the timetable has become confused. One business owner with more than 50 employees, the majority of whom are part-time, argued that his company would need more time to become compliant than a business with 50 full-time staff.

A Forum of Private Business survey found that the cost of compliance has risen to £16.8 billion in total this year.[viii] This is equivalent to £14,200 per small business (£9,300 in internal compliance costs and £4,900 in external costs). However the cost for each business owner feels much higher as the opportunity costs of internal compliance are £29.8 billion or almost three times the actual salaried costs. Employment law accounts for £4.2 billion of that cost and the smaller firms want a more realistic assessment from legislators and enforcers about what they can and should do in terms of compliance. There is a general feeling that although legislation has helped in some areas of management, the time and costs involved in compliance have become excessive. 21% felt that the time and cost spent complying with legislation had meant poorer business performance, 18% felt that it had an impact on the motivation and 5% felt that compliance hindered employment opportunities in the future.

Erosion of the principle of personal responsibility

Although one of the lowest concerns, a majority of respondents to the Forum's survey (65%) were still concerned with the ideological implications of an employer automatically enrolling their staff into pensions. Some business owners were concerned about employees assuming that the pension provided by their business would be sufficient for them in old age. Whilst the Forum recognises the current political appetite for this scheme, this percentage gives some idea of the level of concern amongst businesses that the liability should fall on the individual and not the business.

Furthermore, many employees fail to understand different forms of pensions. The Forum has concerns that, with the current lack of clear communication and understanding, when employees are told about it, their first port of call will be to ask their employer for advice or information. We do not believe that employers should to have to take on an informal advisory role for a policy that is being forced upon them and which is already costing them financially. On that basis, we recommend that Government provide to business owners—or those that will manage the pension pots in larger businesses—guidance on to whom to refer employees for impartial advice.

Solutions

There will of course be a greater awareness of the plans as time progresses—as The Pension Regulator provides further information on duties and the staggered rollout process, and NEST launches through 2011, making information available to all sizes of employer.

However, more information on the basics of pension provision should be available to small and micro-businesses. Business owners would like more support from payroll experts and accountants to understand how they will introduce the scheme and its impact on their business as employees are unlikely to be happy at lower take home pay after a period of austerity and pay freezes.

The Forum feels there is a genuine case for some form of recompense for smaller employers. Many businesses are trading to break even at present and even a small additional liability could be a significant barrier to a business remaining viable. It is of course preferable that an individual remains employed without a pension, than laid off as a result of this set of regulations being over hastily introduced.

Role of The Pensions Regulator, including in certification of schemes

The Government recognises there is a need to keep administrative costs down with this new scheme, including the cost of setting up a pension scheme, automatically enrolling employees, calculating and deducting contributions, and registering with The Pensions Regulator. Further, The Pensions Regulator itself is meant to take a graduated, proportionate and risk-based approach to enforcement.

The Forum asks that the utmost understanding and leniency is given to smaller firms as they negotiate their way around the complex pensions market. The Regulator should work with SMEs towards compliance and not have its first contact with a business through an enforcement role.

NEST's potential market share and the possible effects on other providers

The Forum agrees that a default pension option needs to be available for auto-enrolment and hopes that the presence of NEST in the market will lead to greater competition in this sector.

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers

The Forum agrees that a default pension option needs to be available for auto-enrolment and hopes that the presence of NEST in the market will lead to greater competition in this sector.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

For part-time employees, the Forum supports the principles of auto-enrolment as outlined in previous questions above.

The Forum does not believe that self-employed people should be auto-enrolled into a pension. Many businesses contract in personnel who already operate their own businesses. It is for the self-employed to provide for their own pension, unless a business that contracts them chooses to provide pension arrangements.

For temporary and agency staff, we believe a threshold should apply before pension entitlement is made. Many businesses carry out time specific probation periods before offering permanent employment and pension arrangements should come into force at the point at which permanent employment is offered. Whilst for some businesses that may be after three months, for others it is longer. As current arrangements stand for auto-enrolment, the Forum understands that pension payments are due to be started within the first three months of commencing employment, which means an employer carrying out the administrative function and commencing payments even though he suspects an employee may not be employed at the end of the probation period. This is an unacceptable state of affairs. We recognise that the Agency Workers Directive at present demands equal employment conditions after 12 weeks of continuous work but are keen to learn whether, should a business commence paying permanent employees after a longer time period than 12 weeks, these same conditions could apply to agency workers. If this is not the case, then we will reach a state of affairs where either agency workers are receiving preferential treatment to probationary employees, or a business is making pension payments to employees that may no longer wish to employ.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement.

As shown in other areas of life where an "opt-in" is replaced by an "opt-out" the Forum believes auto-enrolment will have an impact on the number of people saving for their pension. However, we question whether—should current difficult economic conditions continue—employees will choose to lose some of their take home pay and pay into a pension instead. Further, small businesses struggling in those same economic conditions may see this additional cost as one more reason to not take on employees—the proverbial straw on a camel's back. The cost may be small compared to some other overheads faced, but the cumulative burden of government regulation in causing negative behavioural change in employers should not be underestimated.

24 August 2011

References

[i] Note: as figures refer to just over 130 businesses, they should be treated as indicative rather than representative of all small and medium-sized businesses.

[ii] HC Deb 11 August 2011 cc1147-

[iii] Forum of Private Business, Employment Law Panel report, April 2011.

[iv] Making Automatic Enrolment Work, page 5:

[v] http://www.nestpensionadvice.co.uk/site/456/NEST_Pension_Staged_Introduction_Dates.aspx

[vi] BDRC Continental research, November 2010
http://www.bdrc-continental.com/business-sectors/financial/personal-banking/pensions-benefits/

[vii] Forum of Private Business Employment Law Panel report, April 2011.

[viii] Forum of Private Business, Referendum 196, July 2011.

Written evidence submitted by Nick Wood

1.0 Introduction

1.1 I am an Independent Financial Adviser in Cornwall, where I am a Director of Watson French Ltd. I am a Chartered Financial Planner.

1.2 A significant element of my business is with Group Pension Schemes (10–150 members) and I have been taking a keen interest in the proposals for Qualifying Workplace Pension Schemes (QWPS) and the introduction of the National Employment Savings Trust (NEST).

1.3 I am currently engaged on a programme of advising employers of the forthcoming changes, the impact this will have upon their existing schemes and the amendments or revisions that will have to be initiated prior to their specific staging date.

1.4 In addition as I am carrying out scheme reviews and meeting existing members or joining new employees I am, as you would expect, advising them of the changes that will be made to the scheme, from its current guise to that which will be fully effective by 2016.

1.5 This provides me with immediate insight into the reactions of both employers and employees.

1.6 For the purposes of this report to the Committee I will summarise the responses as follows.

2.0 Employers

2.1 None that I have spoken with are fully cognisant of the forthcoming implications, although there is a general awareness of what is involved.

2.2 I believe it is fair to say that at the outset of any dialogue that I have had, the view of the less informed employer has been that this new legislation will be no more involved than the introduction of Stakeholder plans in 2001. Needless to say their interest increases as they learn more of their legal obligations and their attitude changes.

2.3 All the schemes I administer are non-contributory, with employer contributions varying ranging between 3 and 6%.

2.4 I find that Employers who currently operate schemes do so with a contribution level that meets or exceeds their future requirement.

2.5 Employers who have no current arrangements or who are not making any contribution are not excited about having to find a minimum 3% as their contribution.

3.0 Employees

3.1 A large number of the schemes that I work with have a majority of employees who are at the lower end of the pay scale. All the schemes I administer are non-contributory, with employer contributions varying ranging between 3 and 6%.

3.2 Across the schemes I administer approximately 21.40% of the employees make personal contributions to their plan.

3.3 Only a third of these make contributions that, when combined with the employers element, will achieve the minimum overall 8% contribution.

3.4 Of those members that I have spoken with that make personal contributions, approximately half will be willing to accept the small increases necessary in their contribution to meet the overall 8% requirement. However the other half does not feel that they can afford any increase.

3.5 These people recognise that they need to make their own contribution towards their income in retirement, which is why they are currently paying into their plan. Nevertheless they express concern about their ability to meet an increased pension contribution against a background of significant increases in household expenditure with the current rate of inflation. These perceptions are exacerbated by low annual pay increases, or even pay freezes.

3.6 A small number of employee members who are currently not making any payment have expressed a reluctant willingness to meet the required level of contribution, but this is less than 5% of those I have spoken with.

3.7 Therefore in a sample scheme where currently approximately 7% contribute above the QWPS level, this will increase to 18.60% however the residual 81.40% will not be willing to contribute. This represents a very high potential opt-out level.

3.8 Furthermore it reflects the fact that it is the lower paid who are the ones that will feel obliged to opt-out because of affordability. It is the lower paid that are the people who need the greatest level of support and encouragement but they will not receive it.

3.9 These are the people who will look to opt-out of the scheme. In presenting these figures it should be recognised that some people who are currently making some contribution to their pension indicate that they will cease to do so in the future.

3.10 At a recent workplace visit I was approached by a young employee who I enrolled into her company scheme over a year ago. She was very agitated because she'd heard that she was going to have to start paying into her pension plan and wanted to know if this was true. When I explained the forthcoming changes and reiterated the need for self provision she became very distressed and wanted to know who said that this had to happen and: "*why are they taking my money away from me? I can't afford to lose money each month*" She earns £11,000 *per annum* and will opt-out.

4.0 The Employers Dilemma

4.1 Employers will fall into three categories:

(i) Those whose contributions meet or will meet the QWPS minimum in total and employees are not obliged to make any necessary contribution.

(ii) Those who contribute to a current or new scheme and where employees are prepared to make their appropriate minimum contributions. Where an employee elects to opt-out the employer will feel that they have complied with all their requirements and take no further action.

(iii) Those who offer a current scheme, without the necessity of legislation, and who are concerned that those employees who will have to opt-out, on the grounds of affordability, will be denied that employer's contribution which they previously enjoyed. These employees will become disadvantaged under QWPS legislation.

4.2 In this last category there are employers who have expressed a willingness wish to continue to provide the percentage contribution that they currently make and which forms a part of their employee terms and conditions of employment.

4.3 Therefore these employers are looking to offer both a QWPS—for the 18.60% who are able to meet the contribution requirements—and also a Non-Qualifying Workplace Pension Scheme for those employees who have opted-out of the main scheme.

5.0 Summary

5.1 Where no current schemes are provided by employers there will, inevitably, be an uptake by those employees who can afford to make a contribution and have avoided doing so thus far.

5.2 Very small businesses employing 10 or less employees will look to NEST as providing a simple solution.

5.3 Nest will particularly suit employers whose work force is transient, seasonal or part-time. The ease of portability will suit those employees who recognise the importance of self provision and make contributions.

5.4 More discerning employers will look to offer a qualifying alternative to NEST or as an overarching scheme that provides enhanced benefits for staff recruitment and retention purposes.

5.5 Opting-out will be very high amongst the very low and low paid employees as well as households with high outgoings comprising debt burdens and increasing living costs. Where they fail to immediately opt-out due to their own inaction there will be antagonism of the employee towards the employer.

5.6 Alternative, non-qualifying schemes will exist alongside formal QWPS for those employers who wish to continue to provide ongoing employee provision for those who opt-out.

24 August 2011

Written evidence submitted by Age UK

INTRODUCTION

1. Age UK has strongly supported the introduction of pensions auto-enrolment and believes that the priority at this stage should be to make auto-enrolment work rather than radical reform. In this context, we welcome the Committee's decision to inquire into various matters which will affect the success of auto-enrolment.

2. However, in order to keep pension reform on track in future we recommend that the Government should consider an ongoing or regularly convened independent Commission on pensions. The current direction of pension reform was set up with broad consensus following work by the independent Pensions Commission. A major reason why this was successful was that it obtained broad agreement on the evidence base before making any recommendations. We believe that a permanent commission or regular reviews could help ensure that future governments make decisions based on agreed evidence and maintain a consistent direction of travel in terms of retirement provision.

DWP's communications strategy

3. Both the DWP and the National Employment Savings Trust (NEST) have carried out a great deal of valuable consumer research and both have produced useful language guides. Work has gone on behind the scenes on an individual communications strategy, but it is disappointing that only recently has a clear statement been made on funding for this. We appreciate that spending is constrained. However, this is the biggest reform of workplace pensions for a generation and it must be given a chance to work. We believe that it is now a priority to start to roll out communications and adequate funding must be made available for this task. If it is not, the gap will be filled by potentially poor quality communications from other bodies and misleading media messages.

4. The following are all required:

— A published communications strategy with a clear lead responsible for coordinating the work of the DWP, NEST, Money Advice Service, The Pensions Advisory Service (TPAS) and The Pensions Regulator (TPR) to ensure that best value is achieved from what funding is available.

— Clear messaging and support for employers, starting as soon as possible, to ensure that the messages they put out are accurate and direct employees to the right place for further information. Small employers will need particular support.

— Enough advertising and media work to ensure people have a clear first point of contact for questions and problems.

— Telephone support. While we appreciate the need to keep costs low by the use of online material where possible, the people who most need support may not be online and many people will need more detailed individual information and guidance from staff with pensions knowledge—not just general call centre staff working to a script. The role of TPAS is essential.

— Clear and consistent messaging from providers of workplace pensions, particularly around the language they use. We hope that they will change their terminology to reflect the research carried out by DWP and NEST.

5. The success of auto-enrolment will also be affected by communications at retirement. Any problems that people have in drawing their pension or buying a retirement income will damage confidence in the pensions system as a whole. It is essential that the DWP communications strategy, and the bodies listed above, also cover the needs of those who are retiring. The number of people affected is substantial, as around half a million pension annuities are currently bought each year.

Arrangements for phasing and staging the introduction of auto-enrolment

6. Age UK would like to see auto-enrolment introduced as soon as possible for all employees but we recognise that the arrangements for phasing and staging were the subject of extensive consultation and should not be changed now. We are aware that the Government's three-year exemption from new regulation for small businesses will introduce a minor delay to staging for some small firms. We would be extremely concerned if any further delay were introduced: the burdens on smaller firms should be reduced by targeted support, rather than by unfairly excluding their employees from auto-enrolment.

NEST's potential market share and the possible effects on other providers

7. We are not in a position to predict the effects of introducing auto-enrolment and NEST, but we strongly believe that a step-change is necessary to improve quality and reduce costs in the workplace pensions industry. However, even though firms have been given valuable protection from competition through the NEST contribution cap and transfer ban, and from European distance selling requirements, the only quality requirement is a minimum contribution. There is guidance on investment options but no requirement to keep charges low, although The Pensions Regulator's recent paper on workplace pensions reveals a wide range of costs. For example, 45% of contract-based schemes had charges over 1% but only 15% had charges below 0.6%. Significant increases in pension income could be gained by reducing charges: a median earner with a

full savings history who pays an Annual Management Charge at the stakeholder level of 1.5% for 10 years and 1% thereafter would see a reduction in their total fund value of 20%, compared to a reduction of 9% for a 0.5% charge. We urge the Government to consider ways to limit charges.

8. We are particularly concerned about the practice of having a high charge which is discounted while the member is contributing and then increases when they leave the employer and stop paying in—so-called "Active member discounts". Members have virtually no negotiating power in such situations—their only option is to transfer their money to a different scheme, yet it is often very difficult to do this.

Limitations on NEST

9. The limitations on NEST are potentially damaging, both because they protect the existing pensions industry from competition and because they increase costs for employers and employees in the target market for reform.

10. Although few people in the target market will be a position to exceed the contributions cap, its existence creates the following problems:

- Employees who receive a windfall that they might want to save for their retirement, such as a lump sum from an inheritance, cannot pay it into NEST if it would take them above the £3,600 cap for the year. They are unlikely to set up a separate pension for a one-off payment so a valuable opportunity to increase pension savings could be lost.
- Administering the limit increases the costs for NEST.
- Employers who want to use NEST for all their employees will not be able to do so if they have a few higher-paid staff whose contributions would be above the cap. They will have to set up two schemes; in practice they may be deterred from using NEST even for lower-paid employees who would benefit from its low charges and specially designed systems.

11. The ban on transfers into NEST is also creating unnecessary cost and difficulties. It means that people cannot use NEST to consolidate pension savings built up elsewhere. Although people can transfer money out of NEST to consolidate in another pension scheme, it is unlikely that another pension scheme will want to accept small amounts of savings as the administration costs of doing so are high.

12. The issue is urgent because, unless every employer uses NEST, auto-enrolment will increase the incidence of small pensions as employees move from employer to employer. As people find it difficult to consolidate their savings, they risk losing track of their pension rights. In Australia, an estimated 5.8 million "super" accounts, or one in five, are lost—an average of one lost account for every two working Australians.[i] In the UK, the lack of any transfer market for defined contribution pensions reduces competition and increases costs.

13. Allowing transfers into NEST would also provide a simple solution to regulatory arbitrage that arises because of the differing tax treatment of trust-based and contract-based pension schemes. Whereas a trust-based scheme can refund members (and employers') contributions if the member leaves within the first two years, a contract-based scheme cannot. This has led to some pension providers setting up master trusts with the aim of encouraging such refunds for early leavers, meaning that employees build up no pension savings and lose their employer's contributions**.** Age UK believes that the simplest way to avoid this regulatory arbitrage would be to allow the contributions of early leavers in trust-based pension schemes (including the employer's contribution) to be transferred to NEST**.**

14. Age UK and its predecessor charities, Age Concern and Help the Aged, campaigned against the limitations on NEST and we would like to see them removed as soon as possible. Even if they are removed following the proposed 2017 review, damage will already have been done as by then employers will have chosen their pension scheme.

15. We note that the "Making Auto-enrolment Work" review commissioned by the Government in 2010 recommended that legislation should make it clear that the contributions cap would be removed in 2017. The Making Auto-enrolment Work review also concluded that facilitating transfers into NEST was "critical to the success of the reforms".

16. Age UK would like to see amendments to the Pension Bill currently before Parliament which would:

- remove the £3,600 contribution cap; and
- permit transfers into NEST.

Possible measures to reduce the proliferation of small pension pots

17. On average, someone will have 11 different jobs with different employers during their lifetime.[ii] Under the current regime, they could end up with a different pension with each employer, greatly increasing the cost and complexity. The following steps could help to reduce the proliferation of small pension pots:

- Allow them to be transferred into NEST, as recommended above.
- Remove existing barriers to transfers into other (non-NEST) schemes during working life.

— Encourage consolidation on retirement.

— Reduce the need to consolidate by improving the "trivial commutation" rules, which allow people with total pension savings of under £18,000 to be drawn in cash.

18. Transfers into NEST would facilitate consolidation because a NEST member has one lifetime account, allowing them to stop and start saving with minimum administrative cost.

19. In principle there is nothing to stop people transferring pension savings to other (non-NEST) schemes. In practice there are many barriers, including:

— restrictive terms and conditions on some pension schemes such as penalties for transfers out or in;

— favourable terms and conditions on some pension schemes (such as guaranteed annuity rates) that make transfers undesirable;

— the need to establish a transfer value with defined benefit schemes;

— the legacy of pension mis-selling, which introduced a special regulatory regime for pension transfers;

— a resulting lack of advice and a tendency by providers to discourage transfers on an execution-only basis; and

— if an adviser is willing to act, they may charge a fee which makes small transfers uneconomic.

20. The regulatory regime for pension transfers was introduced for good reasons, following the mis-selling of pension transfers which encouraged people to transfer savings from good defined benefit schemes to expensive personal pensions. We would not suggest removing this regulatory regime, but it should be reviewed. We also recommend that providers are required to set out in their transfer documentation any favourable terms and conditions (such as guaranteed annuity rates) that could be lost on transfer.

21. Particular lessons may be learnt from Australia, which we understand has set up special consolidation funds. We note that the National Association of Pension Funds has previously proposed the development of "super trusts" to aid consolidation. We are supportive of these proposals in principle, as long as they simplify matters for small employers and lead to larger more cost-effective schemes. However, in the short-term we see NEST as being the appropriate choice for smaller employers. In addition, we are concerned that The Pensions Regulator has found some examples of multi-employer occupational pension schemes with non-associated employers where conflicts of interest have the potential for member detriment. Any new "consolidation" vehicles should meet similar standards of governance and administration to NEST.

22. The ABI (Association of British Insurers) has worked to make transfers easier through its "Options" scheme, which can also be used for transfers before retirement. However, membership is voluntary. We recommend that all pension providers should be required to join this scheme or meet minimum service standards.

23. However, even if transfers are made easier, many people will still end up with a number of pension pots on retirement. It is essential that people are helped to consolidate at this stage because larger pension pots qualify for better annuity rates than smaller ones. The open market option which allows people to shop around for an annuity, rather than buying from their existing provider, is also still not working adequately. Age UK recommends that a process is developed where people are automatically referred to either specialist advice or NEST. NEST has developed a specialist system to facilitate annuitisation for people with small funds.

24. In addition, to stop people losing track of their pensions, the Government and pensions industry should consider encouraging and facilitating people to "log" their pension membership with a scheme such as the Pensions Tracing Service at the time of joining. This might also make it possible to provide combined pension forecasts, bringing together information from all of an individual's pension savings. Although it has not yet proved possible to do this, technological change should make it easier in future.

25. Finally, the barriers to trivial commutation should be removed. There is evidence that many people are annuitising sums below the commutation limit of £18,000. This may be because they have other pension savings that take them above the limit, or it may be because people do not know about trivial commutation or are caught by rules that require them to commute all pension savings within a 12-month period.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

26. Many people in these groups will still remain under-pensioned because:

— There is an earnings threshold of £7,475 below which auto-enrolment will not be required.

— The earnings threshold applies per job so someone with more than one part-time job could be excluded even though their total earnings are above £7,475.

— Employers can apply a waiting period of three months before auto-enrolling staff. This will exclude people who work in a succession of short-term jobs.

— The self-employed can opt-in but not will be encouraged to do so.

27. These exemptions impact particularly heavily on part-timers, women and black and ethnic minority groups with low earnings. We urge the Government not to increase the £7,475 threshold, even if the personal tax allowance (its comparator) is increased. For example, an increase to £10,000 would exclude the 25% of women who earn below £10,000, and nearly 60% of part-timers.[iii]

28. While we understand the desire to simplify the system to ensure that the introduction of auto-enrolment is manageable for employers, the impact of these exemptions on pension coverage must be monitored, and action taken to improve coverage if it appears that significant numbers of people are likely to remain outside the net.

29. The Government should also look at ways to encourage voluntary pension contributions from groups that might benefit from saving. For example, self-employed people may be encouraged to save by setting up a system whereby people can contribute to NEST through their tax return or self-assessment statement, rather as it is currently possible to donate to charity this way. Linking the contributions to the tax system in this way would be a good opportunity to explain the tax advantages of contributions (particularly if people are filing online where it would be possible to personalise the saving).

Achieving behavioural change

30. We are hopeful that the introduction of auto-enrolment will improve pension provision through the combined impact of the wider access to workplace pensions, compulsory employer contributions and the effect of inertia so that employees will have to do something in order not to save, rather than having to proactively join a scheme. It is important that the impact is closely monitored including looking at: levels of contracting out, rates of saving, and characteristics of savers to ensure that policy goals are being achieved. We are especially keen to see an improvement in private saving outcomes from groups who are currently underpensioned such as women, and people from black and ethnic minorities. However the impact of auto-enrolment needs to be looked in the context of retirement pension provision more widely which is why Age UK believes the Government should consider setting up an independent commission to review the evidence and provide independent analysis and advice to the Government.

References

[i] http://www.thegovmonitor.com/economy/australia-makes-it-easy-to-find-lost-superannuation-accounts-45941.html

[ii] *Making auto-enrolment work,* Department for Work and Pensions, October 2010

[iii] *Annual Survey of Hours and Earnings 2009,* Office for National Statistics

25 August 2011

Written evidence submitted by Building and Civil Engineering Benefit Schemes

Introduction

B&CE (Building and Civil Engineering) Benefit Schemes was set up almost 70 years ago for the construction industry by the construction industry. As a not-for-profit organisation, it has no shareholders and returns any surpluses to the industry.

B&CE has been operating the EasyBuild stakeholder personal pension scheme for the past 10 years. It is the construction industry's largest pension scheme and the UK's largest stakeholder pension scheme with over 500,000 members. Launched in 2001, EasyBuild is predominantly aimed at low to moderate earners and has been successfully servicing a highly transient workforce ever since. We believe we are one of the only schemes to have achieved any success in attracting low to moderate earners to save.

We believe everyone who saves for retirement should be demonstrably better off as a result of doing so. We are fully supportive of the principles leading to automatic enrolment.

Our Response to the Terms of Reference

1. *DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees*

We are encouraged by DWP's strategy and in particular their willingness to work with pension providers and to engage with as many media streams as possible. It is also pleasing that there is a budget to do so. Our greatest concern is that all stakeholders including the Government have a duty to educate the public about the reasons for and the need to save for their retirement.

We have had the opportunity to meet with DWP officials to add our comments and are in ongoing dialogue with officials.

2. *Arrangements for phasing and staging the introduction of auto-enrolment*

We understand the reasons behind these arrangements, although the staging dates themselves are still subject to secondary legislation. There should be no further changes as movements dilute the message and may lead employers to think/assume "it will not happen".

3. *Likely impact of auto-enrolment on business, especially small and micro-businesses*

The regulations will undoubtedly increase costs for business not only in contribution terms but also in administrative and compliance costs eg processing opt-outs.

For small and micro-businesses, whilst the staging dates do not commence until mid 2014, the contribution phasing in period will be a lot shorter and so these businesses will see a more rapid escalation in their costs.

As the economy remains fragile, it could be that the media blame the increased costs under automatic enrolment, however unfairly, as a reason for future business failures.

There are clear signs of specialist companies moving towards the provision of services to smaller employers to help with automatic enrolment duties and these schemes should be encouraged.

4. *Role of The Pensions Regulator, including in certification of schemes*

As several recent surveys have demonstrated, awareness amongst employers of the auto-enrolment regulations and the impact of them is very low and we would strongly recommend that The Pensions Regulator (TPR) focuses on this massive task.

The employer guidance issued by the Regulator is extremely helpful to employers, providers and trustees in getting ready for automatic enrolment. B&CE has fostered good working relationships with TPR over the years and particularly with issues around automatic enrolment.

The certification rules as set out by DWP are we feel far too complicated and in view of our "low to moderate earner" population has little application for our corporate customers. However, it is essential these rules are finalised as rapidly as possible.

It seems logical that TPR have clear responsibilities in policing certification, although it seems odd that there is no requirement for employers to provide evidence of certification.

As an independent regulator, TPR should not be promoting NEST (National Employment Savings Trust). NEST is just another provider and should be competing on level terms with existing providers. Rather than suggest, for example, that certain employers should use NEST, their advice to employers should be that they should select a qualifying scheme with the characteristics as outlined in their consultation and response on enabling good member outcomes in defined contribution schemes.

The involvement of TPR in auto-enrolment is essential especially as the regulatory complexity surrounding pension provision it is not an easy matter for a lay employer or employee to understand.

Defined contribution pension provision (as it will be the major auto-enrolment option) would benefit from a simple common regulatory framework, regardless of whether it is a trust based or contract based scheme.

We have as a provider always maintained a constructive dialogue with TPR and this certainly applies with automatic enrolment.

5. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

The success of automatic enrolment is important not just the success of NEST. Pension providers have invested considerable resources already in readiness for automatic enrolment. This investment will continue over the coming year.

The estimations of opt-out vary widely and there is a lot of speculation. Inertia will be very likely and the first time workers really see an impact will be when they receive their first pay packet after the employer has started to deduct contributions.

There is a view that when the employee contribution increases from 1% to 3% and then to 5%, then there could be an increase in employees ceasing contributions or reducing them.

For automatic enrolment to be a success, the opt-out rate needs to be as low as possible and for there to be an overall increase in pension scheme membership and not simply a churning between schemes.

A high opt-out rate could well provide a political spur to compulsion as we believe has happened in other countries.

The potential impact on NEST and pension providers of a low take up will be huge as there has been major investment of money and time. We all have an obligation and shared responsibility to make auto-enrolment work. The Government can assist this with national awareness of the issues.

6. *NEST's potential market share and the possible effects on other providers*
Whether auto-enrolment is likely to attract new providers and encourage new models of provision

These two issues are very interlinked.

NEST was introduced to complement existing pension arrangements and this purpose must be maintained. There are concerns that NEST maybe being treated more favourably to the detriment of other providers.

We would not want to see NEST being used by employers as a way of levelling down benefits by closing good existing quality schemes.

The Government and the regulators must make it totally clear to employers that automatic enrolment does not equate to NEST.

B&CE are an established pension provider in the low to moderate earner market which is very much the NEST target market. Our experience is that there are very few other providers geared up to handle the administration surrounding transient workforces and handling small pots and so it is unlikely that many have the desire to target this market with a proven track record of investment and administration expertise.

In terms of membership, current estimates suggest that NEST could end up with around two million members and this will make it one of the largest schemes in the UK by membership, NEST will have to accept that these members will be low paid and may not build up significant funds under management.

There will undoubtedly be new models of pension provision coming into the market over the coming months particularly non UK players. However, these models will probably not differ too much from what is in place already due to the prescriptive nature of UK pension legislation.

7. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

As it has been proposed that these are reviewed in 2017, we believe this should remain the case. It's correct that transfers should not be allowed until the matter is reviewed in 2017. This would undermine good existing providers who have invested significant money to establish pension schemes without any form of government support.

8. *NEST's investment strategy*

NEST's investment policy for younger new joiners seems ultra conservative. The investment policy is apparently based on significant research amongst the target market which shows that the target group is conservative when it comes to pensions. However, this is where the need for education becomes imperative to enable individual needs and expectations to be met through active individual choice. Any member can opt to go into a more aggressive growth fund which is available, but that requires active engagement by the member as they have to switch from the default.

9. *Possible measures to reduce the proliferation of small pension pots*

Job mobility and job uncertainty means many workers have and will build up a number of small pension pots and this has meant that the funds are difficult to manage and transfer without complicated processes.

We are encouraged that the DWP are looking into this issue following the recent consultation, but do not believe that setting up NEST as the default receiving scheme for all small pot transfers is right—this gives NEST a totally unfair advantage.

If there is a decision that there should be automatic aggregation then more than one provider should be able to act in this way. Aggregation of pots at retirement already happens through the Open Market Option at retirement.

The transfer process must be made easier and quicker, as set out in the auto-enrolment review, as if no action is taken it will become increasingly difficult to annuitise at retirement because of members holding a large number of small pots.

The employee is also much more likely to engage with pensions if they can see the total worth of their funds rather than being in lots of separate small pots. A simple suggestion would be to allow lighter touch regulation and a simpler transfer process where schemes met set certain standards on charges, default investment funds and governance.

Unlike many providers we do not have a minimum pot size for the purchase of an annuity. The lack of market choice for a worker therefore needs addressing. Equally setting up such small annuities produces not only a meaningless annuity payment but also creates considerable confusion in the public's eyes.

The issue of small pots and transfers is all linked into the DWP review of the short service refund. We think that the time period for the short service refund rule is somewhat out of date in the current economic climate in the light of changing work patterns and increased job mobility. A period of two years used to be short service many years ago but is probably not far off the average employment time period now! The Government has to resolve the regulatory arbitrage issues so that the differences between trust based and contract based schemes are resolved.

Perhaps drawing some consistency between the rules and time periods allowed for auto-enrolment commencement/opt-out and that for short service refunds would be sensible.

If it is decided to keep short service refunds, and to avoid going against the principles of auto-enrolment, we would strongly recommend that any short service refund should be made only if the member requests it. The refund option should not be the default option as it is in many trusts.

Other suggestions we have to reduce the proliferation of small pots are:

— Offer the same £2,000 *de minimis* limit for contract based schemes as offered to trust based arrangements.
— The trivial commutation rules should apply from age 55 as for annuitisation.
— The triviality limit of £2,000 could be imposed on a "per provider" rather than "per scheme" basis. This would limit the ability of a contract based arrangement to segment funds and encourage providers to investigate internal transfers.

10. *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications*

We established our industry wide scheme as a stakeholder personal pension scheme in 2001 rather than a defined contribution (DC) occupational trust based scheme, so that we could accept self employed members. It is vital as an industry wide scheme for transient workers that their scheme is fully portable as they move employers and employment status.

There are a substantial proportion of construction workers within the industry, many of whom are working with individuals who are "caught" within the automatic enrolment regulations. There is anecdotal evidence that smaller construction employers could look at changing the status of their workforce from employed to self employed to avoid their employer duties under automatic enrolment.

The self employed are excluded from the automatic enrolment regulations. The way NEST rules have been drafted, gives them an unfair advantage in being able to accept the self employed.

It is likely that employers will use the three month waiting period as a way of reducing costs and so therefore, casual and agency workers could be excluded from building up meaningful pots during their working career.

11. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

Automatic enrolment on its own is not necessarily going to change behaviour—it has to be a constant and consistent approach by the Government, the pension industry as well as employers and trustees to ensure the desired behavioural changes occur.

There are three key steps:

— The first is education and awareness. We believe that it is necessary for all workers to understand the concept of retirement, and the benefits of saving for retirement by keeping it as simple as possible (and by knowing that they will just have a flat rate state pension they will know what they will have to live on if they do not save) and how to fund the lifestyle they want.
— The second characteristic is simplicity. Pension legislation and product differentiation by providers has caused a confusion of options for members. We believe that the vast majority of members appreciate a small number of funds to choose from, a transparent and consistent charging structure and the information they need that is not hidden behind jargon.
— The final characteristic is responsibility. Defined contribution pension schemes impose various responsibilities on the member, sponsor and provider of the scheme. It is important that each party understands their own responsibilities and what they should expect from the other parties. The Pensions Regulator can play a role in ensuring the Employer is complying with their responsibilities and that schemes are well governed, and meet certain standards.

Summary

As we have said, we firmly believe everyone who saves for retirement should be demonstrably better off as a result of doing so.

We are fully supportive of the principles leading to automatic enrolment and for it to be successful; the content of pension communications needs to be kept as simple as possible with all stakeholders having vital parts to play.

It must be emphasised that NEST and automatic enrolment are not the same—NEST is a complementary pension provider. The different rules for contract and trust based schemes must be resolved along with the issues surrounding small pots and the need to make transfers of pension (in particular defined contribution) arrangements less complicated.

26 August 2011

Written evidence submitted by Investment and Life Assurance Group

1. *Introduction*

1.1 It is very difficult to predict with any certainty the impact the reforms will have due to three direct drivers that will affect behaviours. These are the decisions made by:

— employers;

— existing providers; and

— employees.

1.2 The outcome will be also be influenced by indirect drivers, for example in these tough economic times the decisions made by employers to control costs, and employees to balance their long term savings with their immediate cash flow needs.

2. *NEST's potential market share and possible effects on other providers*

2.1 The outcome is not predictable. From an employer's point of view, the key challenge will be how much better NEST (National Employment Savings Trust) dovetails into HR and payroll processes/systems than other provider offerings. If the solution, including existing arrangements, is costly, employers will seek other solutions.

2.2 Providers will be selective, preferring to deal with those employers with the correct employee staff turnover profile. Employees effectively volunteer to join existing workplace schemes, thereby opt-out rates are minimal. After the introduction of auto-enrolment opt-out rates of 10–20% could add significantly to acquisition costs that will make competing with NEST uncompetitive in many situations.

2.3 Consideration should be given to the existing individual voluntary sector ie personal pension and voluntary contributions:

— If there is no employer scheme available, will they continue once the employer introduces such a scheme?

— If an employer improves its scheme, what are consequences?

— If an employer chooses to level down contributions, what are the consequences?

— Will current providers and existing distribution channels be able to reach the employees affected and reduce the consequent reduction in retirement savings?

3. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

3.1 There are indications that new providers might be considering entering the market. However, a new provider obtains sufficient scale quickly in order to overcome cost constraints. This will only be possible if they have the requisite technology and distribution capabilities.

4. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

4.1 Where these remain, NEST is unlikely to appeal to employers with more affluent employees. However if the cap on contributions and a ban on transfers is removed it becomes a different proposition. NEST will then be a low cost basic pension with no bells and whistles which could be attractive across a wide spectrum of employees.

5. *Possible measures to reduce the proliferation of small pension pots*

The reforms will result in many smaller pension pots as well as even smaller value pots. The simple solution is to empower schemes to transfer these to NEST. Those who accrue small pots are likely to have had more jobs than others so it is probable they will be accruing other pots within NEST and will gain from the efficiency of consolidation.

6. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

6.1 Auto-enrolment is based on the premise that saving for a retirement must be through a pension. There is no doubt that the reforms will lead to more people saving through pensions but it will be interesting to see by how much the aggregate savings amount will increase. (Please also see Section 1 above—influences and drivers).

6.2 Evidence suggests that a benchmark employer contribution of 6% and a requirement for an employee contribution may translate into a 60% employee take up rate. Other demands on employee's income will influence by how much auto-enrolment will improve that take up rate.

6.3 Those with more short-term demands on their income might be more likely to participate if a proportion of their savings were put in more accessible savings vehicles, eg a work place ISA (Individual Savings Account) where up to £10,000 could be held before contributions had to go into a pension.

As well as encouraging a savings culture, individuals would have the reassurance of accessibility to some of their savings for emergencies and other immediate needs.

26 August 2011

Written evidence submitted by Aon Hewitt Ltd

SUMMARY

1. Aon Hewitt is pleased to submit its response to the Work and Pension Committee's inquiry into automatic enrolment in workplace pensions and the National Employment Savings Trust (NEST).

2. By way of background, Aon Hewitt is a global company providing human resource consulting and outsourcing solutions with more than 29,000 professionals in 90 countries. We are currently working with our clients on the steps they will need to take in order to be compliant with the automatic enrolment legislation.

3. We have set out below our comments on the specific questions you raised. In general, we are surprised by the timing of the inquiry, given that at this late stage it is likely to be too late to change the policy framework on which the automatic enrolment obligations will be introduced and it is too early to be able to comment on whether automatic enrolment will work from an administrative perspective and how it is fulfilling its aims. Specifically:

(a) We think more will need to be done to communicate with employers than is budgeted for.

(b) Uncertainty in rules and late changes are making it difficult for employers to plan for staging.

(c) There will be a negative impact on some employers' profitability and an administrative burden on all employers.

(d) Opt-out rates are difficult to predict.

(e) NEST and other providers will have challenges to face to be able to deal with the large member volumes.

(f) Auto-enrolment will not be a trigger for new providers in the UK market.

(g) The cap on contributions for NEST could eventually erode good quality employer pension provision back to minimum levels.

(h) We are extremely concerned that investment losses on accounts with NEST will be reported to members as a reduction in employer contributions.

(i) There will, no doubt, be a proliferation of small pension accounts.

(j) Auto-enrolment may mean an increase in pensions savings but it will be due to inertia and it may not be associated with behavioural changes of the need to save for retirement without a much more extensive universal communication campaign.

1. *DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees*

4. The majority of Aon Hewitt clients will not be relying on communications directly from DWP or TPR (The Pensions Regulator). Instead, their information will come from us as their advisors. We understand there is a very limited budget available to DWP, TPR and NEST and therefore the impact of their communications campaigns is likely to be very limited. The resulting lack of awareness of material issued by these bodies may cause a problem for smaller employers who do not have the resources or the advisors to help them and brief them on the requirements.

2. *Arrangements for phasing and staging the introduction of auto-enrolment*

5. The main difficulty around the staging dates is the lack of certainty that still exists. Draft regulations which establish staging dates have only just been released for consultation. Once these staging dates are finalised, there will be more certainty and companies will know their timescales. Once again, late changes to the rules are unhelpful and are discouraging organisations from pushing forward with the changes needed in order to comply.

6. What is complicating this (especially for those with early staging dates) is the fact that the rules are not yet fixed. This uncertainty is blighting companies' abilitities to start implementing the new processes required in order to comply with the new requirements.

7. Indeed, some of the rules that will enable employers to decide which of their schemes are qualifying schemes are still not available even in draft versions. This includes guidance on certifying defined benefit schemes and the rules around hybrid schemes.

3. *Likely impact of auto-enrolment on business, especially small and micro-businesses*

8. We believe that for some of Aon Hewitt's clients, particularly those with high staff turnover, low current pension scheme membership take-up rates and/or low profitability margins, the impact of auto-enrolment on their business profitability will be substantial. For other employers, certain aspects of the new rules will be onerous in terms of broad administration and this will add to operating costs.

9. There is no denying that there is significant complexity in the new requirements. We are particularly concerned because employers will have to operate a different joining process for different categories of workers. That is, where an employer wishes to reduce the complexity at their own expense by simply auto-enrolling all their workers irrespective of earnings level or age into the employer's good quality pension arrangements, an employer must continue to identify different groups of workers and treat them differently. The issue revolves around the different definitions of a jobholder. What this means in practice is that employers cannot give non-eligible jobholders and entitled workers the one month to opt-out following auto-enrolment—they would need to be treated as a normal leaver. This is likely to be a barrier to broadening the coverage of pension savings and may even mean that employers stop automatically pensioning those outside the eligible jobholders definition (where they would currently). This would therefore lead to a reduction of those covered compared to the current state.

4. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

10. Given the limitations of "public" budgets for awareness building and education of employees and employers as discussed under heading one, above, opt-out rates will largely be dependent on the information and education provided by employers themselves. It is likely that employee inertia will lead to perhaps a majority of workers who have been automatically enrolled, continuing to be members. However, lower than expected membership numbers and assets may lead to higher charges being levied for a longer period of time.

5. *NEST's potential market share and the possible effects on other providers*

11. We have reservations about the capacity impacts for both NEST and other providers. Whilst bundled providers appear to be able to fairly easily scale up their computer systems to deal with the greater volume of members and transactions, we query the number of trained people they will need to be able to operate help facilities for members and employers.

6. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

12. We do not think auto-enrolment will encourage many new providers into the UK pensions market place.

7. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

13. Allowing transfers into NEST (subject to some criteria, either monetary or service related) may help members to consolidate their pension savings, particularly if their work patterns are transient in nature.

14. The cap on contributions to NEST will mean that most employers, if they wish to carry on pensioning earnings above the cap, will still have to operate another pension scheme in addition to NEST in order to continue with this higher level of provision. Most organisations we advise want to limit the impact of the new requirements and so are unlikely to want to contribute to more than one pension arrangement. Most companies have been working towards simplification and so are not keen to increase complexity further. (At the same time, we recognise the concerns of pensions providers that any removal of the cap may distort the market and may, in fact, mean that the number of providers in the UK may eventually reduce.)

15. From NEST's point of view, these limitations which make NEST less attractive to employers who want to pension higher earners, may mean NEST has a large proportion of small account balances building up from lower paid workers as some employers will utilise their own arrangements to cover their workforce.

8. *NEST's investment strategy*

16. NEST have announced that any investment losses will be shown against employer contributions rather than being properly attributed to all contributions. This is something that would not be allowed outside NEST and, in fact, may be a barrier to contributing individuals properly understanding investment in a defined contribution (DC) environment which has got to be a fundamental part of building awareness of the need to save for retirement and the impact of members' decisions on their eventual level of pension. We feel strongly that NEST should be subject to the same legal requirements on information and disclosure as other pension scheme providers. If so, the proposed approach for NEST would be prohibited because it is misleading.

17. We do not expect to see many schemes other than NEST adopting Target Date Funds (TDF) as they are not readily available and most schemes are not big enough to build and administer their own. We do not know, for the few that may use TDF whether they will also include a Foundation Stage similar to the NEST strategy.

9. *Possible measures to reduce the proliferation of small pension pots*

18. If the vesting rules remain as they currently are, then this is likely to be less of an issue for trust based schemes which can pay a refund of contributions on leaving with less than two years of service, coupled with the ability to transfer deferred members away to individual policies. For contract based schemes with immediate vesting, this may mean pricing increases and these costs are typically paid by members of a pension arrangement. As mentioned above in point seven, if transfers are allowed to NEST, this may reduce the administrative burden and therefore overall cost on employers and employees (depending on who is paying administration costs).

19. We have already seen evidence that bundled pension providers are looking to increase pricing for organisations who have a high level of staff turnover and who already operate pension schemes because of the larger number of small (dormant) accounts which will remain. The charging structure of NEST, however, would be unlikely to encourage transfers because of the initial charge that will be taken for the foreseeable future.

20. It is interesting to note that in some other countries which have extended pension coverage to cover all workers, specific campaigns have been launched to get members to consolidate their accounts or look for "lost" small accounts.

10. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

21. Auto-enrolment will mean more people save for retirement but mainly due to inertia. It will not contribute to people's understanding of the need to save for retirement and elements such as not properly attributing investment losses may actually hamper some people's understanding.

22. An emphasis on the charges to members for the investment options available under NEST (and some DC schemes) is also likely to lead to behaviours whereby members regard the cheapest investments as the best. This could lead to excessive volatility in growth assets (as it will cause a preference for equities over more stable growth assets such as property) and excessive demand for government stock (which will appear cheaper than corporate bonds).

23. Without awareness building and education of those who will be auto-enrolled, any deduction of pension contributions may just be viewed as another tax by those who auto-enrol.

26 August 2011

Written evidence submitted by Compass Group PLC

Compass Group PLC is a contract foodservice and support services company that provides a range of consumer-facing foodservice solutions to its clients in over 50 countries.

In the UK, Compass employs approximately 90,000 people (many of them part-time, casual or seasonal) across 5,000 plus sites and has a reasonable level of employee turnover, in line with the sector.

Summary

Compass Group PLC is committed to complying fully with the auto-enrolment requirements. However, the arrangements as they stand are likely to cause a significant and costly administrative impact on our business if the requirements remain as they currently are. We believe that a large part of this impact is avoidable if urgent attention is given to three areas in particular:

1. The administrative burden of auto-enrolment should not be under-estimated for a business such as ours that has a highly transient workforce with variable earnings patterns and many employees on the cusp of earnings limits. We ask the Government to consider simplifying the arrangements wherever possible so that the compliance burden is minimised within the overall policy objectives.

2. Early confirmation of key outstanding issues (for example the treatment of employer contributions for early leavers) and practical reassurance regarding the risks of using NEST will enable us to make informed business decisions in a timely manner. Currently the lack of clarity prevents us from doing this.

3. Separate requirements regarding Real Time Information are causing conflicting requirements for changes to our payroll system at a similar time to those needed for auto-enrolment. We request that the Government consider delaying the implementation of Real Time Information until April 2013.

Terms of Reference for the Inquiry Followed by Compass Comments

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

1. The staging date for pension auto-enrolment for Compass Group is November 2012 and the implementation date of Real Time Information is April 2013. Both of these initiatives will involve considerable development of Compass's HR system (SAP). This will create excessive workload within the payroll and IT team. Development and testing of the SAP system will be more difficult with two major projects at the same time. Our request is that the Real Time Information launch is delayed until April 2013.

Arrangements for phasing and staging the introduction of auto-enrolment

2. We have a concern over the phasing of staging dates for auto-enrolment, in terms of fairness and UK competition laws. Those employers who have early staging dates are disadvantaged compared to those with later ones, having to fund both direct and indirect costs. In practice, these means that for any business that we bid for between November 2013 and 2016 we will be more expensive than our smaller competitors. This disadvantage extends past the first re-enrolment period after three years as smaller competitors and newly formed companies will only just be getting ready to initiate auto-enrolment. We would ask the Government to reconsider the first re-enrolment date for large employers so that it does not start until after 2016 when all employers are live under the new regulations.

Likely impact of auto-enrolment on business, especially small and micro-businesses

3. It should not be assumed that small businesses are the only ones facing severe business disruption. Being a very large company with a reasonable turnover of employees means that auto-enrolment will be a huge administrative burden for Compass. Even with a three month waiting period we will still have to enrol a very large number of employees who will leave the Company within the first six months. We would ask the Government to consider alternative solutions for employers like Compass, such as a longer waiting period of six months.

4. We would like clarity on the issue of TUPE and opting-out. Our preferred solution is for any opt-out request to TUPE across until our next re-enrolment period so that we do not need to auto-enrol all TUPE transfees at the point of transfer. TUPE transfers in our sector often happen at short notice and involve a high degree of communication already.

Role of The Pensions Regulator, including in certification of schemes

5. We believe the principle of self certification is good but would request clarification of the final details as soon as possible. It is difficult for a company to commit to one of the three self certification routes, knowing it is still possible for these to be changed.

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

6. It seems possible that the ability to opt-out will be removed at some future date. If so, this should be clarified now. In that case, a sense of proportionality is needed as to the complexity and administrative burden of the opt-out arrangements bearing in mind that they may be only temporary.

7. We understand that an individual who has already opted-out of pensions in the UK because their benefits are already, or are expected to be, above the Lifetime Allowance will still have to be auto-enrolled and then they must again opt-out. If they fail to do so then they would lose their (enhanced or fixed) protection. We understand the employer can advise them of this situation but must word this carefully so as not to be seen to be inducing them to opt-out. We ask the Government to consider allowing us to contact the individuals concerned with more detail and provide them with an opt-out form.

NEST's potential market share and the possible effects on other providers

8. We have not yet decided whether NEST (National Employment Savings Trust) is a viable option for Compass and we are spending a significant amount of time getting to know NEST and meeting the team. We are very aware that NEST has no track record in terms of pension provision and we have some concerns that we will be one of the first companies to utilise NEST if we choose that option. We are extremely concerned that it works, as any failures in processes could leave the Company exposed to non-compliance with auto-enrolment. We want to understand the Government's and Regulator's position in relation to any potential failures with NEST (or any other provider) to protect employers who become non-compliant due to matters outside of their control (ie a system failure of NEST or providers).

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers

9. If NEST is used by larger employers to provide pensions for their more transient employees then NEST should be as flexible as possible on transfers. So we are seeking clarification that NEST will allow individuals to transfer in to their NEST account.

NEST's investment strategy

10. We would like to understand whether the Government supports NEST's approach to investments, in particular the "Foundation phase" as a lower risk start for younger members. This does not conform to the industry norm and we ask the Government to indicate its support for this approach.

Possible measures to reduce the proliferation of small pension pots

11. We note that the position on short service refunds remains under question.

This clearly has a major impact for employers who are likely to have many people leaving within the current two year window. The decision as to whether short service refunds will continue in any shape or form at all is key to our decision on which provider to use. We ask the Government to confirm their position on this issue as soon as practically possible, ideally when their full report to the call for evidence is issued in the autumn. Otherwise, it will impact on our ability to be ready for the November 2012 staging date.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

12. We employ a large number of casual workers who have non regular working patterns. It is difficult to estimate their earnings at the beginning of the tax year and earnings from the previous year are no indication to earnings in the following tax year. We ask the Government to consider changing the regulations so that we have to auto-enrol workers once they meet the lower earnings limit in the tax year. This population will of course have the right to join the pension scheme before they reach the lower earning limit or indeed if they did not meet it.

26 August 2011

Written evidence submitted by Mercer

Summary

1. Mercer fully supports the aims and intentions behind the new auto-enrolment legislation, although there are certain areas where we feel amendments could and should be made, for example in relation to individuals with enhanced or fixed protection and in relation to employers who have pensioners in the same PAYE (Pay As You Earn) scheme as the rest of their current employees.

2. We believe that NEST (National Employment Savings Trust) fills a gap that has existed in the market to date and that due to its scale it is likely to have an influence on both pension providers and occupational pension schemes. However the degree and direction of that influence are difficult to predict.

3. It would help if both the DWP and The Pensions Regulator could be more open and alert to some of the complex issues that are facing employers in working through the implications.

Terms of Reference for the Inquiry

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

4. It is important that the liaison between DWP and stakeholders (providers, employers, representative industry bodies such as SPC and NAPF, *etc*) continues to be close, to ensure that further process and policy developments address the needs of current and future members of occupational schemes, both defined benefit (DB) and defined contribution (DC). There are distinct differences between trust-based and contract-based provision. We are not aware that a specific published strategy in relation to private pension provision exists, so do not know what to expect from DWP over the next 12 months or so. It would be useful if DWP could publish a list of templates or other material they intend to draft to help with communication.

This approach needs to be backed up by broader, basic educational communications from the Government about the principles of saving for income in retirement (the Pensions Bill debate indicates something is planned but more detail/information at an early stage would be useful).

5. The early drafts of communication templates that the DWP has shared, and meetings to discuss them, indicate that the DWP needs to gather knowledge from a wide range of other parties to ensure that the communication is fit for purpose.

6. Something should also be done urgently to help employers deal with their higher earners and members who have fixed or enhanced protection, who must be auto-enrolled but who will face a significant tax cost if they fail to opt-out. Employers are struggling to understand what they can tell such members without it being considered an inducement and are receiving mixed messages from different Government departments. For example, HM Revenue and Customs is suggesting a cash alternative to a pension contribution although this is potentially incompatible with auto-enrolment. In our view, the simplest route would be to exclude members with protection from the eligibility requirements.

Arrangements for phasing and staging the introduction of auto-enrolment

7. At the expense of ending up with a more complex structure, the DWP has done well to listen to the concerns of businesses and put together a plan that will work for most employers. It is also welcome that the phasing has been extended to schemes that will use certification. We do think however that some employers are likely to need help with the process—see also paragraph 12 below.

8. There is an issue for schemes that pay pensioners through their main payroll that has been recognised in the recent consultation and which could bring forward a scheme's staging date significantly. Currently the DWP has said that it can do nothing about this as The Pensions Regulator has no way of identifying who is an employee and who a pensioner; however a more helpful approach would be to allow employers to provide evidence to the Regulator about the respective numbers as at 1 April 2012; then they should have the option of deferring their staging date to the one implied by the number of employees only.

Likely impact of auto-enrolment on business, especially small and micro-businesses

9. The impact on all businesses will be to increase costs, directly and indirectly.

Role of The Pensions Regulator, including in certification of schemes

10. It would be useful for employers, trustees and service providers to understand what the Regulator's priorities are: what precisely will they be looking for and at what frequency? This will in turn help the Regulator. Presumably this will be clarified in the Regulator's compliance and enforcement strategy expected later this year.

11. The Regulator states that it is not its role to interpret the legislation; that can only be done by the courts. Whilst this is the correct legal position, on a day to day basis the Regulator will in practice have to take a view on areas of the legislation which remain unclear, because to do otherwise would mean it could not successfully regulate. It is therefore reasonable to expect the Regulator to share its view with those it regulates.

One area of uncertainty, for example, is how the Regulator would determine where the main administration of a pension scheme is located, if the day-to-day administration of a UK pension scheme, with UK trustees, was outsourced to another country. Also, in the area of salary sacrifice, although the Regulator has provided some comments in its detailed guidance, it is still far from clear as to what it means in practice. It would therefore be extremely helpful if the Regulator could be more proactive and open in its views on areas of uncertainty and be willing to say how it will regulate in these areas.

12. The Regulator could also consider running "training seminars" for employers on a few key activities, to walk them through their processes and promote a higher probability of success. Options could include delivery via organisations such as Business Link.

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

13. There have been various independent research reports and press comments around estimated opt-out rates and we have nothing specific to add.

14. The possible impact is quite serious and likely to result in the loss of any remaining credibility for the whole pensions industry if, after years of preparation and at a significant cost to the tax-payer of setting up NEST, auto-enrolment is considered to be a failure due to high opt-out rates.

15. This goes back to the previous comment about the importance of having a targeted education campaign in the run up to auto-enrolment.

NEST's potential market share and the possible effects on other providers

16. The degree of legislative and regulatory change that is affecting occupational schemes (eg tax reforms, the abolition of contracting-out on a protected rights basis, to name two) currently is high, so it will be hard to isolate the effect of NEST on decisions made by employers in relation to how they comply with their auto-enrolment responsibilities.

17. Major change with financial implications invariably prompts employers to carry out a serious review of their pension provision strategy, which these days, usually means finding ways to improve cost efficiencies and remove unnecessary costs. NEST itself may appear to be an attractive alternative to the complexity of running

an occupational pension scheme, or the level of benefits available from NEST may be perceived as an acceptable benchmark to level down to. This could lead to an increased rate of closure of occupational pension schemes.

18. Other providers are taking the opportunity to create new products (such as master trust arrangements) that compete with NEST, but these compete with occupational pension schemes as well. Employers might adopt these new products for the future, making them, rather than their existing occupational pension provision, available to new employees.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

19. Linked to paragraphs 16 to 18 above. New models of provision are a good outcome if they do provide new and better retirement savings options for employees, but new ones at the expense of better ones are less desirable.

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers

20. For individuals, the cap limits true savings potential, although it is likely to be high enough that the limit has no material effect for target members.

21. The ban on transfers does need to be removed sooner rather than later in order to allow individuals more choice and opportunity eg access to NEST's retirement panel for pots built up in other funds.

NEST's investment strategy

22. No comment.

Possible measures to reduce the proliferation of small pension pots

23. No single step can address this but a number of different options used in combination could reduce the anticipated proliferation. Some examples:

(i) Increase trivial commutation limit.

(ii) Make it easier for members to transfer their pension savings at retirement to enable individuals to amalgamate their savings.

(iii) Allow pots up to a certain size to be amalgamated with those of a spouse or partner.

(iv) Allow pots up to a certain size to be passed on to a dependant's pension fund.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

24. We do not believe auto-enrolment will have much impact on the self-employed. Although NEST allows the self-employed to participate, this is no different to other contract-based arrangements, although stopping and starting contributions may be less problematic.

25. It is likely that many more temporary, casual and agency staff will now have access to an occupational pension scheme, so there is likely to be more saving amongst this group. However, the levels of opt-out within this group are a big uncertainty.

26. The introduction of the waiting period introduces some potential inequality issues as temporary and casual staff will be affected more than long-term employees; however the ability to opt-in during the waiting period mitigates this issue.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

27. By itself, it is possible that it will achieve some behavioural change, since behavioural inertia means many people will not opt-out. However, unless individuals have already made the decision or accept that they need to save for retirement, the result could be that that, whilst more people save, the overall level of saving does not increase since, as a result, some employers are likely to reduce their current level of provision. Government education and increased confidence in financial products, alongside legislation, is needed before material changes in behaviour can be expected.

26 August 2011

Written evidence submitted by Dean Wetton Advisory (DWA)

This response covers the following issues:

- — Likely impact of auto-enrolment on business, especially small and micro-businesses.
- — Role of The Pensions Regulator, including in certification of schemes.
- — NEST's potential market share and the possible effects on other providers.
- — Whether auto-enrolment is likely to attract new providers and encourage new models of provision.
- — NEST's investment strategy.

Summary

1. As NEST is ultimately funded by the taxpayer we believe it will have an unfair advantage in terms of implicit Government guarantee to cover operational risks and possibly even investment risk. We propose a system of similar implicit guarantee for pension funds that meet very high governance standards. This will improve the competitive environment and therefore choices available for smaller businesses with less resource to evaluate competing solutions for auto-enrolment.

2. Dean Wetton Advisory (DWA) was founded to provide conviction-led proactive investment advice to small and large clients. Our primary focus is on defined contribution pension plans, which we believe are the future of pensions, and we offer these underlying members access to large scale solutions by working with large providers to scale down solutions. Prior to founding DWA, Dean Wetton was Head of the Manager Evaluation Function at P-Solve, the investment consulting arm of the Punter-Southall Group. Before joining P-Solve, Dean was a senior member of Hewitt's Manager Research Team, leading the Hewitt global practice in usage and development of third party risk models.

3. DWA have in place and already operational a competitor to NEST, Pensions Umbrella Trust (PUT). We believe it is as robust from both an investment point of view and from a scheme governance point of view and it is probably cheaper (although the way NEST has priced itself makes direct comparisons difficult). PUT is aimed at smaller employers and is easy to join. It is designed to be a cooperative of employers when there are enough employers to make it self-sufficient. See further notes on PUT at paragraph 11.

4. We also have another two defined contribution master trust clients that we advise on investment issues that could be regarded as competitors to NEST.

5. We note that these organisations will be competing with NEST (National Employment Savings Trust) which has been funded by the taxpayer by a £120 million loan (at 31 March 2011, NEST 2011 Annual Report) which will peak at £665.7 million in March 2019 (DWP—NEST Loan agreement 11 November 2010). The loan interest rate has not been disclosed.

6. In addition we think that in employers' and members' minds there could well be an expectation that NEST will be backed by the Government. For example:

(a) even if NEST is unable to repay the loan, the Government is unlikely to foreclose NEST;

(b) if an operational error occurs, it will be rectified by NEST;

(c) if fraud occurs it will be made good by NEST (backed by the Government); and

(d) there may even be an expectation that if investment performance is extremely poor it may be augmented by a subsidy.

7. We believe that small businesses who have little resource to devote to a full evaluation of the options for auto-enrolment will therefore see NEST as the only low risk option.

8. We would like a level playing field in term of implicit Government guarantees. We think that the high standards of governance we have in place should provide sufficient confidence in the product and our suggestion is that if other schemes meet a high standard, as determined by the Pensions Regulator or other body then this certification could carry a similar guarantee as the one enjoyed by NEST. The National Association of Pension Funds (NAPF) already has a certification scheme which may be able to be used directly or with little modification.[19] The Pensions Quality Mark (PQM) rates defined contribution schemes in terms of contribution rates, governance and communications.

9. This would help level the playing field and give smaller businesses without the resource to conduct fullest due diligence the opportunity to use alternative providers with confidence.

10. This may result in a knock on effect if NEST deflects small funds away from embryonic master trusts and inhibits them achieving the scale that NEST is guaranteed. It will lay open the path for tied insurance company master trusts which are simply distribution channels for their investment products and offer no better a level of governance than contract based schemes tied to an investment platform. This will ultimately supress competition and reduce choice available for consumers.

[19] www.pensionsqualitymark.org.uk

Notes on Pensions Umbrella Trust

11. Pensions Umbrella Trust is a multi employer master trust which has only defined contribution members and no guarantees. It therefore cannot have a deficit by definition. The scheme uses independent providers, carefully sourced for all activities, including the trustees. Within the scheme these are all accountable to the trustees and can be replaced should they not perform to requirements and the trustees are accountable to an elected Governance Committee and can be replaced should the need arise. As the Governance Committee is elected by the employers it effectively makes it a cooperative of employers.

12. Its investment philosophy, similar to NEST, is to allow choice for those that want it and choose for those that don't. PUT actively manages what it believes to be the best default and allows governed choices for those who want it. This contrasts to the market norm which is to offer choice and assist members to make those difficult choices. It is however different in the level of risk it targets for members over their life in that it will take slightly more in order to achieve higher returns. It offers a more diversified Sharia fund lifestyle offering. PUT is operational and holds members funds.

26 August 2011

Written evidence submitted by the Tax Incentivised Savings Association

Introduction

The Tax Incentivised Savings Association (TISA) has a growing membership of over 120 organisations interested in the UK market for retail financial services products, from Child Trust Funds, through Individual Savings Accounts to Pensions. We have Advisory Councils in Retirement Saving, Wraps and Distribution, whose observations and thinking have contributed to this response. We are distinguished by the very wide scope of our membership, from Banks, though Investment Houses and Life and Pension providers, to distribution organisations and IFAs (Independent Financial Advisor). We are not, therefore, restricted to representing a sector approach, but rather the views of a very broad church indeed. We also, as an organisation, start from the principle that what is good for the consumer must, in the long-term, be good for the business of our membership.

TISA is pleased to submit the following comments within the terms of reference for the inquiry.

1. *DWP's communication strategy for introducing automatic enrolment and provision of advice to employers and employees*

More communication is required with the general public and employers to ensure that timely and accurate information is available concerning the automatic enrolment duties of employers, the rights and responsibilities of workers within the new regime and the implementation timeline.

Better informed consumers will be in a position to make informed decisions about their retirement needs and saving opportunities. Clear information for consumers, including the importance of saving for retirement and the value of the employer contribution should help to minimise the level of opt-outs and increase awareness of the need for saving.

The Pension Regulator website provides clear and very useful information to the adviser, employer and employee. As an industry it is imperative that the pension industry including the media work together as a whole to make auto-enrolment a success. Much is needed to educate the industry, advisers, employers and employees for all to understand the implications of auto-enrolment and what each party will need to do in order to comply. Looking at the economic growth forecasted for the next few years it is important that the employers cost to comply with auto-enrolment is kept to a minimum. As such guidance and help to reduce the administration and setup cost will be needed.

2. *Arrangements for phasing and staging the introduction of auto-enrolment*

The arrangements for phasing and staging are complex and take too long to achieve full enrolment of all workers. Minimum contributions are too low for too long a period. There is a risk of confusion over employee entitlements in businesses of different sizes.

3. *Likely impact of auto-enrolment on business, especially small and micro-businesses*

Most small businesses are still unaware of auto-enrolment and the implications that it will have for their businesses. The impact will be felt on a number of different levels:

— education in the rules and responsibilities;
— the selection of a compliant scheme and the setting up process of both the scheme and automatic enrolment;
— the on-going administrative overhead of enrolling and removing staff; and
— the financial overhead of contributions.

Phasing and staging both in terms of introducing small enterprises and increasing the contribution limits over a period of time should help to reduce the financial impact of contributions, however it is an additional burden and in the slow growth economic environment predicted over the next few years means that it could have an impact on the economy. Whilst the employer can predict and budget for pension contributions, the on-going administrative overhead could be an unknown if automated solutions are not introduced.

There is evidence that small employers will find the current auto-enrolment phasing and staging processes extremely confusing. The effect correlates directly with employee numbers ie becomes greater the fewer employees. This may have effects for opt-out rates, or indeed basic compliance, for small and micro employers.

4. *The role of the Pensions Regulator, including certification of schemes*

The change to introduce new employer duties requires a significant effort in implementing the new compliance regime for The Pensions Regulator (TPR). Greater clarity on the compliance regime and TPR expectations of pension providers would be welcome.

The proposed certification process will help enable the 200,000 employers who already have existing pension schemes to maintain those schemes for the benefit of both current and future members.

It could be useful if information on providers which operate qualifying schemes is accessible and published on TPR's website so that employers and advisers can easily identify sources of schemes which qualify.

5. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

Opt-out rates will be influenced by the public and media's perception of how auto-enrolment is introduced and rolled out. Good collaboration across the industry is important to make auto-enrolment and therefore take-up a success.

NEST will require a critical mass of members to remain viable without tax payer support and to repay the loan from HM Treasury required for its set up. The numbers automatically enrolled should be as predicted but the level of opt-outs will be the factor which impacts NEST's success. Theoretically, the policy reform objective could be met without NEST being successful should other providers decide to operate within the NEST target market.

6. *NEST's potential market share and the possible effects on other providers*

TISA believes that since NEST is targeted at those parts of the market which are not commercially attractive other providers; there should be little impact on other pension providers. It is likely that some large providers will work in collaboration with NEST to provide solutions for some employers.

The greatest concern is that NEST might not attract the level of business required to achieve the planned break even profile. Commercial providers are concerned to achieve a level playing field with the NEST scheme, to the extent possible, and would not wish to see any extension of taxpayer funded loans to the scheme. Neither would commercial providers wish to see NEST actively competing by seeking business from those market segments already well provided for by the private sector.

However, NEST's success will be important in shaping the general public's perception of automatic enrolment and the wider pension industry.

7. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

TISA notes that long-term savings for retirement are not currently confined to workplace pension products. Automatic enrolment should increase the numbers of workers participating in employer schemes, however it is likely that other forms of retirement saving will continue.

TISA is of the view that the current complexity of some pension product structures makes pension products unattractive to many savers, particularly those in the low to medium earnings bands, despite the fact that the tax benefits are more attractive than other savings products. It remains to be seen whether the availability of an employer contribution will increase the attractiveness of workplace pension saving to the general public.

Pricing in the group pensions market is already competitive and margins are low for commercial providers. Therefore, TISA is of the view that it is unlikely that there will be many new entrants into the market, particularly that which serves the low to medium earnings segment.

8. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

The contribution cap and the ban on transfers have succeeded in ensuring that NEST has remained focussed on its target market, where the public service obligation scheme is essential for the successful implementation of automatic enrolment.

The contribution cap may make NEST unattractive to some parts of the market and make it likely that some employers will opt to run more than one pension scheme. TISA and most pension product providers take the view that this limitation on the NEST scheme is unnecessary and adds complexity and therefore cost for NEST scheme members.

TISA supports the Government's position of reviewing the restrictions on the NEST scheme in 2017. Once every employer is operating automatic enrolment it may be possible to lift these restrictions without breaching the EU rules on State Aid. The issue of transfers is a difficult one where there are arguments for administrative benefits in the consolidation of small dormant accounts. However, commercial providers are keen to ensure that the NEST scheme does not become acquisitive, thereby distorting the market.

9. *NEST's investment strategy*

TISA recognises the efforts made in the effective consultation exercise on the NEST investment strategy. NEST has a major challenge to balance a lower risk strategy versus producing a good long-term investment return. However care should be taken that the NEST default strategy does not become the benchmark for other pension funds' default strategy.

10. *Possible measures to reduce the proliferation of small pension pots*

TISA believes that the pension industry could collaborate more effectively to facilitate transfers and in particular the transferability of small pension pots. Allowing transfers in and out of the NEST scheme could help to increase the average pension pot size. An improvement in the administrative processes and the speed of execution of pension transfers would provide better clarity and simplicity for employees to understand their pensions, hence increasing interest and hopefully saving behaviour.

11. *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment and the equality implications*

Part-time, temporary, casual and agency workers will only acquire employer contribution rights under automatic enrolment where they earn above the enrolment threshold. In addition, the self-employed have access to NEST and must decide whether to participate in this or alternative retirement saving products.

For the employer of this group of workers, there may be challenges in determining whether a particular worker should be automatically enrolled. There is complexity for employers in determining whether an employee who would not normally earn over the threshold over the long pay period might experience a short pay reference period with higher earnings, on a one off basis, thereby requiring automatic enrolment.

TISA notes that for low earners the State Pension should provide an adequate replacement rate. With the aim of ensuring that those on low incomes and those with an interrupted working life are lifted above the poverty line, TISA strongly supports the Government's proposals to pay a single State Pension at a level above the Minimum Income Guarantee level.

12. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

TISA is of the view that auto-enrolment will go some way to encouraging personal responsibility for retirement saving. However, whilst pension products remain complex and the general public lack an understanding of what they may receive in retirement from state provision, there is a risk that levels of saving will remain too low. TISA believes that policy development should include state provision above the minimum pension guarantee level so that the general public have a clear understanding of the total level of state retirement and other benefits which they will receive in retirement. This would allow people to determine the level of retirement income they wish to have and therefore the level of saving which they need to put in place.

In addition, automatic enrolment could be a stepping stone in looking at how personal debt levels can be reduced and further saving encouraged to really address general personal financial health of the nation and to help with the demographical aging issues with which we are faced. However, the debate remains as to whether saving is appropriate for those with debt.

26 August 2011

Written evidence submitted by the Financial Services Authority's Financial Services Consumer Panel

The Financial Services Consumer Panel welcomes the opportunity to provide input into the Work and Pensions Committee inquiry into automatic enrolment in workplace pensions and the National Employment Savings Trust (NEST).

The Panel has taken a close interest in pension reform and the development of NEST which, although outside the remit of the FSA (Financial Services Authority), is likely to have a significant impact on consumers and how they interact with the areas of the industry regulated by the FSA and its successors. It has in the past responded to a number of consultations and provided other input to the DWP. Copies of these responses are available on the Panel website.[20]

In drafting this reply, we have chosen to focus on the first of the points raised, specifically the DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees.

The Panel is broadly supportive of an initiative such as pension reform which has the objective of improving access to retirement saving for those who do not currently have a pension. However, it believes there are specific issues that must be addressed if the communication of the auto-enrolment process is to be effective and appropriate.

Individual Circumstances

We believe that communications from NEST, or other qualifying schemes into which they may be auto-enrolled, must actively alert consumers to the issues they should be taking into account when making the decision to stay in or opt-out, signposting to regulated advice or the Money Advice Service, where appropriate. These should explicitly include:

- The advantages of long-term saving.
- The impact of employer contributions and tax relief on pension saving.
- Proximity to retirement.
- Other commitments including existing debt.
- Likely interaction with the benefits system.

There tends to be an assumption that it is in the best interests of most people to stay in (or join) a workplace pension where employers contribute and that it will generally be impossible to identify in advance the small number of people who are at risk of not benefiting from saving. We have some reservations about that assessment. There are groups of individuals who are likely to be better off saving in a cash ISA (Individual Savings Account), or reducing their debts, than enrolling in a pension scheme.

On the other hand, there are those who would benefit from being in a pension scheme, but who choose to disproportionately prioritise current spending over saving for the future (the behaviour known as "hyperbolic discounting"), and choose to opt-out. This is, and should remain, their choice, but the consequences of the decision must be clearly communicated to them.

Additionally, those on low incomes and with no previous savings currently in their 40s and 50s who are likely to be living in rented accommodation after retirement are at high risk of being worse off unless the current benefit system changes. We believe that further work is needed to identify the probable size of these groups and consideration given of how to reflect their circumstances in the programme of education and publicity.

Therefore it is important that information encourages people to think about their personal situation, rather than assuming that one outcome will work for all.

Incentives to Opt-out

The Panel agrees with the authority given to The Pensions Regulator to take action against any employer encouraging employees to opt-out through inducements or coercion (including penalties of up to £50,000 or imprisonment of up to two years) and would encourage this policy to be robustly applied.

Employer Advice

We are conscious that advising employers on their choice of pension scheme is not an activity regulated by the FSA or indeed The Pensions Regulator. We are concerned that this might become a significant regulatory gap in future and a source of indirect consumer detriment.

Managing Expectations

The Panel has advised NEST that it needs to manage the expectations of the level of the ultimate pension income that contributors will receive from their NEST pension. People must be warned that they should not rely on a minimum contribution to NEST, or minimum contributions to other workplace schemes into which they may be auto-enrolled, to provide a good income in retirement. They should be advised to consider additional measures including additional contributions to NEST or another qualifying scheme.

[20] http://www.fs-cp.org.uk/publications/responses/2011.shtml

In conclusion, the Panel believes that the relevant authorities need to strike a careful balance to ensure that the appropriate people, and only the appropriate people, are automatically enrolled into pension schemes, and that they have access to the relevant information at the decision-making point.

26 August 2011

Written evidence submitted by the Pensions Management Institute

Introduction

The Pensions Management Institute (PMI) is the professional body for people working in the pensions sector. The PMI's members (currently over 4,200) work as pensions managers, consultants and technical specialists in consultancies and insurance companies. Many are also actuaries, pensions lawyers or company secretaries. Their experience is therefore wide ranging and has contributed to the thinking expressed in this response.

PMI's Response

Summary

We are broadly supportive of the auto-enrolment programme, which we note still enjoys widespread cross party support.

The communication programmes of DWP and TPR (The Pensions Regulator) will be crucial to the successful launch of auto-enrolment.

Progressing the Government's idea of a universal State Pension of around £140 per week will help to reduce opt-outs from auto-enrolment.

We support the removal of the restrictions on NEST (National Employment Savings Trust) in 2017 when they are due for review. By then they will have served their purpose of restricting NEST's ability to compete with existing private sector pension providers in line with the EU requirements on the State Aid given to NEST.

We have some potential concerns that NEST has adopted a cautious investment approach, which may undermine the macro-economic argument for funded pension provision although we do understand that the target audience for NEST is proven to react negatively to market volatility.

We are concerned that there may be unintended consequences following auto-enrolment, with either employees cutting back other savings plans or employers cutting back the generosity of pension provision.

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

The DWP has been confronted with a massive communications challenge in that it must successfully explain a technically complicated subject to a huge audience but has extremely limited resources. It has responded by seeking to work closely with industry professionals in order to explore the effective use of a range of communication channels, including social media and SmartPhone Apps.

The Pensions Advisory Service (TPAS) will have a pivotal role in providing information and guidance to the general public, and it is important to ensure that it has adequate resources to ensure that it is able to carry out this role effectively.

The Pensions Regulator has already developed a suite of online tools to help advise employers of their new responsibilities. Again, it is important to ensure that the Regulator remains adequately resourced, but the communication strategy is already highly developed and there are no grounds for supposing that it will not be successful.

Arrangements for phasing and staging the introduction of auto-enrolment

We are satisfied that phasing and staging have been appropriately arranged. There is however some danger of complacency. The first tranche of employers, being the UK's largest employers, will consist of organisations with extensive experience of workplace pension provision. These employers will therefore experience relatively little difficulty in understanding and meeting their new statutory responsibilities.

The appearance of initial success of automatic enrolment should not lead to an assumption that the project as a whole will proceed smoothly. The critical phase will concern the involvement of smaller employers. Smaller organisations are less likely to have previous experience of workplace pensions (and will have less access to professional help), and these employers are far more at risk of failing to comply with the new regime.

Likely impact of auto-enrolment on business, especially small and micro-businesses

Many employers will perceive auto-enrolment as a form of taxation, and it is to be expected that media coverage—particularly in the popular press—will be emotive and misleading. Some will seek to demonstrate a direct link between auto-enrolment and increased insolvencies.

It is likely that many smaller employers will seek to evade their responsibilities. Many may seek to offer illegal incentives to persuade employees to opt-out. Others may attempt to renegotiate employment contracts so that current employees become self-employed contractors.

It is important that the Regulator is adequately resourced in order to identify abuses of the new regime. The Regulator must not assume that pension administrators can identify these cases on its behalf, as pension administrators are not privy to what is going on inside the workplace.

Role of the Pensions Regulator, including the certification of schemes

The Regulator will have the principal role in enforcing the Employer Compliance Regime. However, it must be remembered that many Qualifying Schemes will be contract-based and so will be subject to regulation by the Financial Services Authority (FSA). It is imperative that there is close co-operation between FSA and TPR to ensure that consistent and effective regulation applies to all workplace pension arrangements.

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

Feedback from employers and employees suggests that take up rates will be towards the low end of the Government's 50% to 80% assumption. Perhaps as many as 45% of employees will opt-out.

The numbers opting-out will be lower if the Government's ideas for a universal State Pension of around £140 per week, as aired in the recent Green Paper, have gained traction by the time employees start being auto-enrolled, as this will significantly reduce the fear that people will lose means tested benefits as a result of saving in a pension.

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers; and possible measures to reduce the proliferation of small pension pots

We would like to see the constraints on NEST removed in 2017 when they become due for review. Whilst we recognise that these restrictions were a key part of obtaining EU approval for the State Aid given to NEST, we believe that by 2017, when all employers will have chosen an auto-enrolment scheme, it would be appropriate to relax the constraints. The contributions cap in particular will frustrate the overall objective of promoting adequate levels of retirement saving.

NEST is designed to operate as a low-cost scheme, and is committed to holding small pots. We believe that the current policy of banning transfers is a missed opportunity. NEST is one scheme that could be used as a default vehicle for accepting all leavers' pots which fall below a set monetary value. This would ensure both that other pension providers would not accumulate a proliferation of commercially unviable pots and also that members would have a relatively simple task in tracing past pension rights.

However, we believe that consolidation could also be commercially viable for other consolidation vehicles, and we would not wish to see NEST being given a further tax payer subsidy to fund its acceptance of small pots.

NEST's potential market share and the possible effects on other providers

We observe that despite NEST's protestations that its target market is largely made up of small employers unfamiliar with pensions NEST has now recruited a salesforce and is actively marketing to large employers with good existing pension schemes. The auto-enrol project could fail if NEST concentrates on trying to replace good existing schemes rather than trying to make itself available for the small employer that may be poorly serviced, or even not serviced at all, by the existing pensions market.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

We expect auto-enrolment to drive new innovation in the pension market.

Already we are seeing signs of master-trusts emerging, which will enable employers to come together and enjoy the benefits of trust based governance with economies of scale and lighter touch stewardship. Furthermore, it will be essential for existing providers to up their game in order to execute profitably those new entrants to existing plans that have previously been unengaged and commercially unattractive.

NEST's investment strategy

We note that NEST is adopting a cautious investment strategy, following research amongst it's prospective members. For young employees in particular, the target of matching CPI (Consumer Price Index) during the foundation phase may generate very low returns, particularly if CPI returns to the Government's intended level of 2%.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

Part-time, casual and agency employees will be adequately served by the new regime, although auto-enrolment will introduce significant administrative difficulties in many cases.

We do not believe that it is practical to extend auto-enrolment to the self-employed. The use of Personal Service Companies, where income is derived principally through dividends rather than salaries, will mean that many self-employed will not comply with the definition of an Eligible Jobholder.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

There is still much to be done if auto-enrolment is to achieve the desired behavioural change. The DWP and TPR communication programmes will be major determinants in ensuring that auto-enrolment is welcomed by employees and employers and does change behaviour.

It is important that we guard against unintended consequences following the launch of auto-enrolment. These unintended consequences could include:

- Employees stopping other forms of savings, like ISAs (Individual Savings Account), to pay for pension contributions.
- Employees mistaking the low level of auto-enrolment contributions for adequacy. In many cases their employers will be prepared to pay higher matching contributions if employees also pay more than the minimum.
- Employers "dumbing down" or "levelling down" the generosity of their pension schemes. There is a clear danger that some employers will react to greater levels of pension scheme participation amongst their workers by reducing the generosity of pension schemes, to try and keep their total costs unchanged.

26 August 2011

Written evidence submitted by the GMB

1. This evidence is submitted on behalf of GMB, Britain's general trade union with more than 600,000 members working across the economy in both the public and private sectors.

2. GMB welcomes the Select Committee's inquiry into of the introduction of these key policies, instigated by the last Government and following the comprehensive review of the UK's pensions system led by Lord Turner.

3. We have consistently welcomed the concept of automatic enrolment and a suitable means of accruing retirement provision for employees who have previously been denied access to workplace based pension arrangements and employer backed contributions towards retirement savings. We have continued to work with DWP officials with a view to making these policies the success so vital to the future of the UK's ageing population.

4. Despite this we have some concerns with the current policy direction that we believe will diminish its likelihood of success and would wish the Committee to consider these as part of their inquiry.

Restrictions on Automatic Enrolment

5. GMB remains concerned that by extending the restrictions that apply to who should be automatically enrolled, as recommended in the 2010 review of this policy; the solution that automatic enrolment was designed to provide can never be fully attained.

6. Firstly the extension of the minimum earnings threshold to the planned £7,475 *per annum*, is likely to impact on a large number of workers, particularly part-time workers. Estimates put the additional number of people excluded form automatic enrolment through this extension at 600,000.

7. Secondly the retention of a minimum age applicable to who can be automatically enrolled is age discriminatory in principle, if not in practice. By denying those aged under 22 the right to employer backed retirement provision, the Government is sending out the wrong message in trying to instil a culture of saving and self-provision. As we look to a future where more people are obliged to enter the workplace earlier, as they are priced out of higher education, GMB believes that implementing a policy that encourages saving from an early age will be beneficial. Not only will this mean that savings will accrue investment income for longer, but it will also make opting-out of retirement saving in the future less likely as a saving mentality has been adopted right from the beginning of a person's working life.

8. We have similar concerns around the proposed facility that will allow employers to delay automatic enrolment by up to three months. This is estimated to exclude a further 500,000 people from benefiting from this policy. This is particularly true of transient and seasonal workers who already have serious obstacles to making retirement provision in the current framework. Aside from the unfair treatment of this group, the danger

of this policy is that by offering employees a number of months before pension contributions are deducted from pay, the later introduction of these deductions would surely lead to a greater level of opt-out as individuals notice the impact of pension deductions more.

Enforcement of Automatic Enrolment

9. GMB has previously provided the Committee with details of our analysis of participation rate in the Local Government Pension Scheme (LGPS), following information obtained through Freedom of Information requests from more than 100 Local Authorities in England. We would reiterate the findings of that analysis which show that, in for a pension arrangement that has operated on an automatic enrolment basis for 20 years. These show that the range of participation amongst employees is vast, from 46% to 99% between employers.

10. It is imperative that Government introduces a robust enforcement mechanism for NEST (National Employment Savings Trust) and the auto-enrolment process. Local authorities are not bad employers and, it is to be hoped, they do not actively dissuade employees from remaining in the pension scheme however, take up rates vary significantly. The introduction of NEST will encounter an indeterminate number of employers who actively want employees to opt-out. Their capacity to do so must be limited.

11. Similarly employers must be assisted in implementation, if confusion continues in local government where the policy has been in place for 20 years, Government must be prepared for far more significant issues when auto-enrolment is introduced throughout the economy.

12. There must be a robust checking procedure to ensure employers are fulfilling their obligations. Relying on workers alone to report failures to comply will not be sufficient. Firstly, the communication of employer obligations in this regard does not appear to have had sufficient attention from NEST, DWP or The Pensions Regulator (TPR), meaning that employees are unlikely to be aware that their employer is breaching the requirements. Secondly, the quality of the data available to those tasked with enforcing and measuring the effectiveness of NEST is unlikely to be universally sufficient without some degree of verification.

13. Auto-enrolment itself is not a panacea for inadequate pension saving in the UK and there is a danger in holding the view that merely by stating a policy and legislating for it, the desired result will instantly occur. GMB appreciates that penalties for non-compliance are part of the package and supports this principle even though the quantum of penalty that is likely to be levied is comparatively low. Our concern is that the penalties will rarely be an issue because breaches are not uncovered.

14. GMB recognises that an effective enforcement approach will require greater resource; however, we believe this is essential if a lot more money is not to be wasted on a lacklustre implementation plan that ultimately will fail to deliver on the objectives set out.

Restrictions on NEST

15. GMB recognises that a review of the operation of NEST is due to take place in 2017, particularly focussed on the limitations designed to minimise its impact on the market.

16. However, GMB strongly believes that for NEST to be a sustainable success the review needs to closely examine the policies that restrict the inward and outward transfer of pension savings and the level of contributions that NEST can receive. The justification for these is ill founded as these reforms were built in response on failure of existing providers to deliver competitive savings vehicles for the majority of the workforce. The planned review should be brought forward and these restrictions lifted.

Summary

17. Although we remain supportive of this policy set as a whole GMB has numerous reservations as outlined about the direction of travel for the introduction of automatic enrolment and NEST. We will continue to put these concerns to DWP and work with Government to make this a success story.

18. However, the limitation of access to pension provision, the scope for poor enforcement of automatic enrolment and the restrictions being placed on NEST mean that we envisage that the problems that are hoped to be addressed will persist into the future.

26 August 2011

Written evidence submitted by AEGON

AEGON welcomes the opportunity to make a submission to Work and Pensions Committee inquiry into Automatic Enrolment/NEST (National Employment Savings Trust). We have been long-term supporters of the Government's workplace pension reform agenda, particularly automatic enrolment and we believe the policy must be kept on track from October 2012.

About AEGON

We've been helping people get ready for their financial futures since Scottish Equitable was formed in 1831. We're now one of the UK's leading providers of pensions, life insurance, investments and annuities. With headquarters in Edinburgh, AEGON in the UK helps over two million customers to secure their long-term financial futures.

In 1994, we joined the AEGON Group, one of the world's largest financial services organisations, with a presence in over 20 countries. Its main markets are the UK, the USA and the Netherlands.

AEGON:

— employs approximately 26,500 people worldwide;

— has around 40 million policyholders; and

— has revenue-generating investments of EUR 413 Billion (£355 billion).

Specific Points

DWP's communication strategy

The introduction of automatic enrolment presents a significant opportunity to communicate to a wide cross-section of the working population the need to make greater provision for future financial needs.

We're pleased that the Government is committed to an auto-enrolment communications strategy and wants to work in partnership with the pensions industry and consumer groups. It's vitally important that the DWP shows leadership here. The success of its policy will depend on how well long-term savings messages are communicated and received. Inertia is not enough—simply being automatically enrolled into an employer's scheme and contributing at the minimum rate will not be sufficient for many people to generate an adequate income in retirement. It will continue to be important that people are persuaded of the benefits of staying in their employer's pension scheme and of contributing more than the statutory minimum.

The campaign shouldn't just focus on the first year of automatic enrolment, despite this being the time when the largest firms and the majority of employees are automatically enrolled. The communication plan also needs to reach the thousands of employers and their employees who will go through this process at later dates up to September 2016. If the DWP's communication momentum is lost, there is a risk that take-up and contribution rates will suffer and the very people the policy is designed for will lose out. The DWP also needs to remember that the largest employer's reenrolment dates will take place in 2015–16, before some of the smallest employers have started to "staging".

The industry, Government and regulators need to have consistent messages about the value of pension saving and what good outcomes in retirement looks like. People will need to be encouraged to keep on saving—even during difficult times.

At the end of last year we carried out some research[21] looking at what incentivises people to save. Although we discovered that the current incentives are not working effectively, we found that the "matching" concept of getting £X elsewhere for every £Y you personally put in would be a more resonant way of communicating the tax benefits and has the potential to increase pension saving. We therefore suggested that positioning tax relief on pension savings as Government "matching" in all communications (including NEST) could make existing tax incentives more effective.

Phasing/staging

All employers will be given their staging dates by The Pensions Regulator and these are now published on their website. The DWP is currently consulting on draft regulations which changes some of the staging dates due to the moratorium on small business. Generally this has put back the staging dates for the smaller employers, although in cases where a small employer uses a multi-employer PAYE (Pay As You Earn) scheme it has added more complexity.

As an administrator of numerous employer pension schemes we are planning for automatic enrolment and this will mean identifying the staging dates of all of our employer schemes. Many of the employers we work with have potentially less than 50 lives and will be staged in by PAYE reference number. This isn't information held by providers. We understand that The Pensions Regulator will be obtaining PAYE references numbers

[21] Towards more effective savings incentives: AEGON 2011 http://www.aegon.co.uk/About-AEGON/Industry-insights/Shaping-our-industry/Research/Effective-incentives-for-savings/index.htm

from the HM Revenue and Customs (HMRC) to help them to identify staging dates. We would like to see The Pensions Regulator and HMRC share information with pension providers to help providers plan for staging.

We have previously raised concerns that the phasing in of the 8% statutory minimum contribution is too slow. We continue to believe this.

Role of The Pensions Regulator

We believe that The Pensions Regulator will have a challenging role over the next five years in making sure all employers are aware of their new responsibilities and that they comply with the automatic enrolment regulation. It faces particular challenges with micro employers, those with les than five employees, of which it has no regulatory experience.

Opt-out rates

Although various attempts have been made to gauge the likely level of opting-out, these are necessarily based either on surveys which cannot replicate precisely the decisions people will face, or on extrapolation from other markets where circumstances differ.

We expect take-up into existing schemes to be higher, but it is more difficult to predict what will happen with employers where there is little or no existing provision. In addition, it seems likely that opt-out rates will vary significantly between employers, across socio-economic groups and geographical regions.

The industry's focus will move from encouraging people to join pension schemes to encouraging people to stay in and contribute more than the minimum. Successful communication could affect the opt-out rates—that's why it's so important that the government does its bit to get the message across.

New providers/new models of provision

Automatic enrolment is a major innovation in workplace pension provision. It would be surprising if this did not give rise to different patterns of market behaviour and this may include both new providers and new models of distribution and provision. It also give rise to innovative scheme designs. To some extent, there are already signs of this in the market such as the increase in master trust arrangements.

This should ultimately be to the benefit of both employers and individual savers as the market adapts and provides solutions more closely matched to their needs. However, we would note that these will require significant upfront investment. A cap on charges of the sort proposed by various commentators would be likely to hinder innovation.

Impact of limitations on NEST

The limitations imposed on NEST were aimed at ensuring that existing good provision would not be undermined. Our understanding has always been that the impact of the contribution cap and the ban on transfers would form part of the review of automatic enrolment scheduled for 2017. We believe the reforms should be given the time to "bed in" and that a review in 2017 will enable analysis to be informed by practical experience and evidence.

NEST is designed as a low cost scheme with no in-built advice costs. Employers using NEST and wishing to appoint a professional financial adviser will therefore have to pay fees for their services. We expect most employers who choose to select NEST will do so on a non-advised basis.

Measures to reduce proliferation of small pots

The Government moved quickly after the 2010 general election to raise the lower earnings threshold at which employees became eligible for automatic enrolment and while they did not go as far as we had suggested, this was nonetheless a welcome step which will go some way to obviate this problem. However, a lower contribution threshold will give rise to a *de-minimis* contribution for those people who are automatically enrolled into their employer's pension scheme.

There remain, nonetheless, various categories of workers who, by the nature of their employment, will accumulate small pots "by default" within one employer scheme and then move on. In some cases, such workers could accumulate a large number of "small pots". These are inefficient to administer and currently difficult for the individual consumer to track and consolidate.

The industry is currently considering various approaches to alleviate this problem, including a mechanism to allow the automatic transfer of employees' small pensions pots from to their new employer's pension scheme. We are also expecting the DWP to issue a Green Paper in the autumn, which will consider options to address the issue.

Behavioural change

In many ways, it is the acid test of the reforms whether they induce behavioural change. It is important to know what we mean by this.

Some will view it as successful behavioural change, if lots more people are saving a little bit more. This may not be full success, but it will be an improvement. Indeed, there is a risk that the message people will hear, is that they are going to be automatically enrolled into a pension, and if they do nothing they will have a decent income in retirement. While in the vast majority of cases, they will have a better income than without automatic enrolment, for a large number such an approach is liable to lead to disappointment, as the statutory minimum contribution levels are unlikely to produce the level of income most people desire.

The behavioural change we need to effect is to persuade people of the benefits of long-term saving and the desirability of deferring and spreading consumption. We need to find a way not just to harness inertia to get people started, but also to build on that and generate a culture of saving. Employers will have an important role to harness the power of saving.

26 August 2011

Written evidence submitted by Jardine Lloyd Thompson

Jardine Lloyd Thompson (JLT) provides consulting, actuarial and administration services to trustees and employers in relation to 1,500 or so work-based pension arrangements with assets ranging from a few thousand pounds to over £1,000 million, and to individuals with regard to individual pensions. Following the acquisition of HSBC Actuaries and Consultants Limited in December 2009, we are one of the "big four" employee benefit consultancies in the UK. In preparing these comments, we have taken into account the fact that auto-enrolment and NEST (National Employment Savings Trust) have already been subject to an independent review and numerous consultations. Also, our submission is confined to areas that are of particular interest to JLT and our clients.

DWP's communication strategy

Our only observation, here, is that the communication strategy will involve a number of different government departments and other bodies, and it is important that DWP works with the Financial Services Authority, The Pensions Regulator and other stakeholders. Early indications are, however, that the strategy is "joined up". We hope that, despite budget cuts, DWP will be given the necessary resources to promote the workplace pension reforms properly; the success of the reforms is dependent upon employer engagement.

Phasing and Staging

We remain very concerned about the transitional arrangements for defined benefit (DB) pension schemes and the "levelling down risk" posed by the workplace pension reforms in this respect.

For DB schemes, phasing of contributions is obviously not possible, and there is therefore the option of deferring auto-enrolment for up to four years for "prescribed" jobholders. Such jobholders are, however, essentially only those in the employ of a company at its staging date, assuming this is the company's first enrolment date.

There is no DB "transitional/deferral period" for eligible jobholders entering employment after the staging date. We consider this to be anomalous because:

(1) jobholders can always opt-in at any time during the transitional period and must be notified in writing of this right; and

(2) there is no equivalent limitation in respect of phasing in of contributions for defined contributions (DC) (ie phasing can be used for DC schemes whether or not the jobholder was in the company's employ on its staging date).

To add some context, we advise a large employer in the retail sector which has a 2012 staging date. It currently operates a CARE (Career Average Revalued Earnings) scheme.

The employer is considering their options in terms of the auto-enrolment of tens of thousands of currently unpensioned employees.

Two of many options under consideration are extending the CARE scheme or a new section in it, or simply minimum contributions to a DC plan.

The transitional provisions for auto-enrolment are very much a factor in the decision making process/cost projections, and the ambit of the DB transition could well determine whether or not jobholders are offered a DB scheme that significantly exceeds the qualifying conditions and, unlike DC, does not pass all the risks of pension saving on to employees.

We understand that a number of factors were considered at the time that the DB transition policy was being developed:

— Recognition that high quality DB provision is in long-term decline.

— Recognition that existing "prescribed" jobholders had made a conscious decision not to enter into their employer's DB provision.

— The need to provide a balance between allowing employers to adjust to the reforms. (by benefiting from the contribution savings from the prescribed jobholders), whilst ensuring that new employees are automatically enrolled as soon as possible.

Our view is that, if there truly is a commitment to maintain high quality workplace pension provision then, for the reasons explained above, the DB transitional period should be reconsidered.

In any event, our experience is that the current narrow transitional period for defined benefit schemes is not understood by many employers.

Auto-enrolling jobholders and other workers

Our only other major concern is that the auto-enrolment provisions are not flexible enough to cater for employers that want to rely on them in order to automatically enrol all their workers, whether or not there is a requirement to do so. A number of large employers have expressed an interest in this, as a practical way of meeting their obligation, but it is not clear that this is possible especially if a contract based scheme is being used as the qualifying pension scheme.

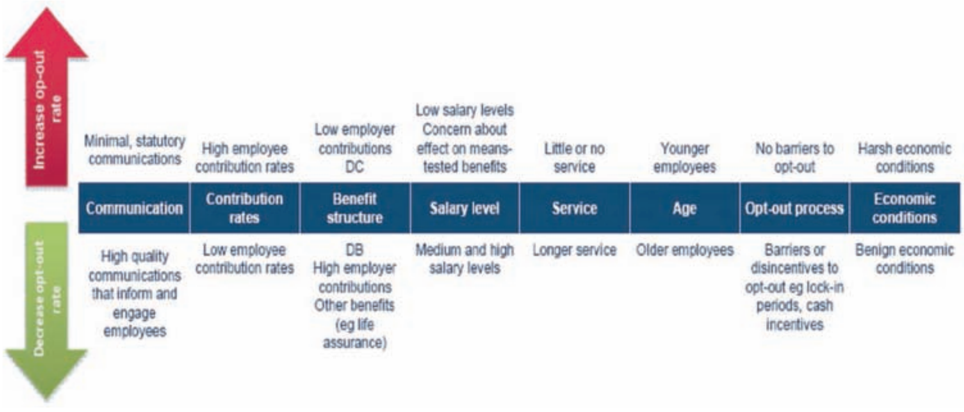
Role of The Pensions Regulator

We have reviewed the guidance and other materials on the Regulator's website and, overall, find them very helpful, especially the flowcharts covering different auto-enrolment processes. Nevertheless, our view is that many employers will only be able to comply with all the requirements (enrolment, opt-out, contribution reconciliation, *etc*) through an automated process. The Regulator seems to be of the view that payroll providers are already well progressed in their development of new software. This, however, is not our experience. Rather, the development of software that is capable of fully automating the auto-enrolment duties is at an early stage and many payroll providers will not be offering complete solutions.

Estimated opt-out rates

There has been a tremendous amount of research into this, both by government and the pensions industry. Whilst, there appears to be some consensus over an overall opt-out rate of between one-quarter and one-third, there could be huge "swings" in respect of particular groups. Importantly, given the economic climate opt-out rates could be much higher among the lower paid (ie the target market for NEST) than might have been originally envisaged when DWP surveys were first conducted.

Many other factors will affect opt-outs too, either positively or negatively, as illustrated below.



In addition, media portrayal of auto-enrolment (and pensions in general) will play an important role and, to date, there has been some notable negative commentary.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

Auto-enrolment has already created renewed interest in master trust schemes. Further, pension providers and advisers are starting to develop new products to help employers with the management of auto-enrolment processes.

If innovation is to be encouraged then it is important that regulations do not unnecessarily prevent new models of provision. The main auto-enrolment regulations (SI 2010/772) are, for example, already causing confusion in terms of opt-out processes and the ability of members to opt-out of a scheme over the phone.

Clarity is also needed in respect of the government's intentions on refunds of contributions for early leavers and simplification of disclosure requirements.

Limitations on NEST

The contributions cap and the ban on transfers are due to be reviewed in 2017. It seems highly likely that both will then be removed. So, we assume their impact, if any, will be temporary.

Our view is that the limitations were imposed for a reason and that there is no need for them to be reconsidered in advance of the official review five years after the reforms take effect.

Measures to reduce the proliferation of small pension pots

An extension of the trivial commutation rules is already under consideration and, if implemented, this would be a straightforward way of reducing the "small pot issue".

The extent to which auto-enrolment is likely to change behaviour

It has already been widely observed that auto-enrolment will not, on its own, deliver adequate retirement incomes for most people.

If the reforms are to succeed in changing behaviour and encouraging people to build on the minimum contributions then it is imperative that employers of all sizes are fully engaged with auto-enrolment and encouraged to do more than simply comply with their minimum statutory obligations.

In this regard, I would refer, again, to our comments on transitional periods for DB schemes, above.

26 August 2011

Written evidence submitted by KPMG LLP

Before responding to specific consultation questions, we would like to make some general points.

Firstly, we are supportive of the automatic enrolment legislation in principle. We believe there needs to be a concerted effort to improve pension savings and this is a good first step in doing so. We have some concerns that the regulations do not go far enough, in terms of default contribution levels in particular, however, we are at least going in the right direction.

Secondly, the approach to the legislation—and hence the body of procedures it has engendered—has become extremely complicated. This complexity adds greatly to implementation costs, decreases certainty and is likely to be off-putting to smaller employers in particular. We note that The Pensions Regulator has issued, alongside further resource documents and a specific guide for software developers, over 190 pages of detailed procedural guidance which, whilst very helpful, still leaves many questions unanswered.

We would hope and expect that the Regulator will not apply an overly pedantic approach to enforcement. But, this being the case, why have such detailed, pedantic legislation in the first place? A principles-based approach may have been more prudent.

Thirdly, automatic enrolment is synonymous with NEST (National Employment Savings Trust) in the eyes of many of those otherwise unfamiliar with pension provision. A lot is therefore riding on NEST's success. It is vital that its systems are robust, as any high profile failure could have massive reputational repercussions for the pensions industry as a whole—perhaps even on a par with the mis-selling scandal of the 1990s. The same goes to some extent for its investment performance—where publicity given to poor outcomes would be seen as a reflection on the worth of pension provision generally.

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

The DWP's communication strategy is aimed at raising awareness of the changes and was apparently due to start in 2010. The fact that we have struggled to work out what the strategy actually is, or to find any examples of its implementation, suggests that it may not be wholly effective. The Pensions Regulator's direct employer communications appear to be appropriate and timely.

Arrangements for phasing and staging the introduction of auto-enrolment

Our view is that the phasing and staging arrangements are generally sensible and workable. Basing staging dates on the size of an employer's largest PAYE (Pay As You Earn) scheme may result in some anomalous outcomes, as there will be many cases where the size of the PAYE scheme does not closely reflect the number of workers who will be subject to auto-enrolment. However, this may be an acceptable price to pay for having a clear, objective basis for establishing the staging date.

Likely impact of auto-enrolment on business, especially small and micro-businesses

The automatic enrolment process is procedurally very complex, especially as regards workers on low and fluctuating earnings. Given the concentration of such earners working for small and micro-businesses, we believe there will be a disproportionate burden on such employers. These employers are likely to be those least well equipped to deal with that complexity.

Role of the Pensions Regulator, including in certification of schemes

We believe it is vital that the Regulator operates a risk-based approach and refrains from enforcing an overly pedantic interpretation of the requirements, particularly in the early years. Many, particularly smaller employers will be struggling to do their best to fulfil the spirit of the legislation; they should not be penalised for occasional transgressions of detailed requirements.

The Regulator needs to be adequately resourced to carry out its enforcement role. If it fails to do so from the start, there is a risk that the system will fall into disrepute (as was the case to a considerable extent with the stakeholder pensions access requirements).

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

The system relies heavily on inertia; individuals' statements of their intentions as regards opting-out may not match their actions. However, we would expect a lower opt-out rate for new joiners than for existing workers who are auto-enrolled. We would also expect the opt-out rate to decline steadily over the years, as auto-enrolment and pension scheme membership become more firmly embedded in the culture.

NEST's potential market share and the possible effects on other providers

Early success is likely to engender lasting success. If, on the other hand, NEST struggles in the early years, its large fixed cost base will mean that its charges will have to remain higher for longer, discouraging take-up by employers.

In the course of our involvement in a number of client auto-enrolment projects and discussions we are not aware of any employers looking to use NEST as their main pension scheme offer to employees. That said, we do believe NEST has a place in the UK market—in particular, to support those employers looking to offer a compliance minimum outside their existing pension arrangements. Pension providers are likely to be supportive of this approach to scheme design.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

We are aware of renewed interest in master trust arrangements and the launch of new providers offering this pension structure. We are aware that many leading providers are not interested in low value contributions; others are keeping an open mind and waiting to see how the market develops.

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers

These will put some employers off using NEST. The contribution cap in particular will be an obstacle for those employers whose workers' incomes cover a wide range. Many will not wish to have to deal with different schemes for different sections of the workforce (and so will shun NEST).

The ban on transfers is less of an issue, though it may discourage the use of NEST as a feeder scheme.

NEST's investment strategy

We applaud the level of research and analysis that has gone into the design of NEST's investment strategy and the focus on risk is a strong message to its members and to the market in general. We understand the rationale used in the creation of the default and design of the fund range options, and while we may not agree fully with the approach, can understand the route taken to meet the objectives set.

We are concerned somewhat that the message around the Growth Phase of the default investment strategy may be seen as too prudent by members, as their annual illustrations may only see long term projection returns of just over 5%. (We assume NEST will communicate with members using statutory money purchase illustrations (SMPI) assumptions of inflation of 2.5% plus the investment objective of the growth phase of 3% over inflation. Schemes using standard SMPI assumptions would increase the projected members' income by over 40%—equivalent to an additional £100,000 pension fund value at retirement for someone on a starting salary of £20,000, even with a similar investment strategy.)

We also question the level of involvement in the management of the default strategy as we understand the phasing and investment strategy can be adjusted from a risk perspective. Again, we understand the rationale behind the approach, however, are concerned about the potentially negative effect of making a decision which impacts on a member. It is unlikely that a change in phasing or investment strategy will impact positively on all members all of the time, hence, as mentioned already, any negative messages around NEST could inadvertently impact on the rest of the industry. We question whether this potential involvement is justified and a more strategic approach adopted.

Possible measures to reduce the proliferation of small pension pots

Schemes should not be faced with having to administer numerous small pension pots. If the refund option is withdrawn or curtailed (as appears likely) then schemes should be given the option to transfer the rights without the member's consent. This would require a receiving scheme of last resort, so to speak; NEST would be the obvious candidate. However, the NEST charging structure is not designed to cater for transfers and would be disadvantageous for transferring members, compared to other available products.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

The auto-enrolment processes are disproportionately burdensome for these groups. We are likely to see an increased use of short-term (less than three month) contracts in order to avoid having to auto-enrol. Alignment of the auto-enrolment earnings bands and triggers to National Insurance contribution requirements would have made far more sense in dealing with these groups in particular.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

If it achieves reasonable early success then the automatic enrolment regime can go on to deliver a steady cultural change in retirement savings over a period of years. Conversely, it will be difficult to recover from a weak or controversy-laden start. The attitude of the popular press is likely to do much to shape public attitudes in the early period of implementation.

Also, as noted at the outset, there is massive reputational risk to the pensions industry as a whole, if NEST fails to perform as well as expected—either in terms of its systems or its investment outcomes.

About KPMG

KPMG LLP, a UK limited liability partnership, is a subsidiary of KPMG Europe LLP and operates from 22 offices across the UK with nearly 11,000 partners and staff. The UK firm recorded a turnover of £1.6 billion in the year ended September 2010. KPMG is a global network of professional firms providing Audit, Tax, and Advisory services. We operate in 150 countries and have more than 138,000 professionals working in member firms around the world. The independent member firms of the KPMG network are affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. KPMG International provides no client services.

The UK Pensions practice at KPMG currently advises many of the UK's largest businesses on pensions, with over £200 billion of total pensions liabilities. By KPMG's estimates, these latest revenues and its headcount of 450 people mean its UK pensions practice is now the fourth largest pensions advisory business in the UK.

26 August 2011

Written evidence submitted by the Universities and Colleges Employers Association (UCEA)

Executive Summary

1.1 Higher education (HE) employers participate in a number of pension schemes, the largest of which are the Universities Superannuation Scheme, the Teachers' Pension Scheme (TPS) and the Local Government Pension Scheme (LGPS).

1.2 Due to the rules or regulations of these schemes it is compulsory for eligible members to be entered into the relevant scheme and in most cases this already happens automatically. Despite this there is still a relatively high level of opt-out across the HE sector. UCEA surveys suggest that affordability is an issue, especially for lower paid support staff.

1.3 This suggests that the schemes being offered are not meeting the needs of some HE employees but there is no flexibility to allow HE employers to offer a more appropriate pension vehicle. It also prevents the employers from effectively managing the cost of auto-enrolment.

1.4 There is a further potential issue as to the ability for the defined benefit schemes on offer to meet the needs of employees who are on variable or flexible contract terms.

1.5 The inability for employers, such as those in the HE sector, to take advantage of alternative pension saving vehicles like NEST (National Employment Savings Trust) to fulfil their duties under the auto-enrolment legislation should be taken into account when assessing possible future levels of opt-out and the potential population of prospective members for NEST.

1. Background Information

2.1 The Universities and Colleges Employers Association (UCEA) represents 164 Higher Education employers across the UK and welcomes this opportunity to present evidence to the Work and Pensions Select Committee. Universities and Colleges of HE present together as employers of over half a million people (250,000 full-time staff, 130,000 part-time and a further 195,000 "atypical" staff on variable contracts). Each HEI (Higher Education Institute) is a separate independent employer and our individual employing institutions often present as the major employer in their locality.

2.2 Over 100 HEIs in the UK have employees enrolled in at least one of the public service pension schemes which are currently in consultation on increases to employee contributions from April 2012 and potential changes to the benefits provided by the schemes from 2015, particularly the Teachers' Pension Scheme, the Local Government Pension Scheme and their Scottish and Northern Ireland equivalents. A significant number of employers, particularly institutions with medical schools, also make contributions on behalf of employees to the NHS Pension Scheme (NHSPS). Although precise figures are unavailable, the configuration of public service schemes affects around 200,000 eligible employees in the HE sector. This mainly refers to "post 92" institutions.

2.3 Because of their former association with local authorities, or as a result of a merger, 58% of HEIs contribute to TPS or STSS and 68% contribute to LGPS/S. They are required by Regulation to offer eligible employees the relevant statutory pension schemes (ie TPS for academics and LGPS for support staff). A small number are members of the LGPS through voluntary admission agreements. A further 16% contribute to the NHSPS as a result of their association with the NHS.

2.4 The HEIs, not covered by the Regulations (which usually refers to the "pre 92" institutions), have grouped together to provide the Universities Superannuation Scheme (USS) for academic and senior administrative employees and most institutions have a Self Administered Trust scheme (SAT) for their support employees. The largest example of a SAT is the Superannuation Arrangements of the University of London (SAUL) which provides pensions for 50 institutions in the London area.

2.5 As a result of the pension challenges faced by the sector the Employers Pensions Forum (EPF) was established by Guild HE, the Universities and Colleges Employers Association and Universities UK (UUK) in 2007 as a broad based forum for HEIs to discuss current and longer term pensions issues and to develop a strategy that will enable the HE sector to continue to offer staff access to high quality pensions schemes as an important part of the total remuneration package.

2.6 Membership of the Forum consists of representatives drawn from Vice-Chancellors, Principals, Finance Directors, HR Directors, Registrars and Chairs of Governing bodies, all with considerable experience in this area. The current EPF Chair is Professor Brian Cantor, (Vice-Chancellor of the University of York).

2.7 The EPF has two sub committees: the USS Group which focuses on the Universities Superannuation Scheme (USS) of which the majority of individual members can be found working in pre-92 HEIs, and the Local Government and Teachers' Schemes Group which focuses on the Teachers' Pensions Scheme and the Local Government Pension Schemes in the UK which are mainly offered to staff working in post-92 HEIs and HE colleges/university colleges.

2.8 Further information on the EPF and the pension provision in the HE sector can be found here: http://www.employerspensionsforum.co.uk

2. Comments on the Subject of the Inquiry

3.1 UCEA would comment on the following topics being reviewed by the Select Committee.

3.2 *Likely impact of auto-enrolment on business, especially small and micro-businesses*

3.2.1 The pension provision in the HE sector can be expressed as follows:

Category of staff	*Pre 92 institutions*	*Post 92 institutions*
Academic staff	Universities Superannuation Scheme	Teachers' Pension Scheme
Non academic/"support" staff	Usually a locally administered scheme. Often a Self Administered Trust (SAT) eg SAUL.	Local Government Pension Scheme
Medical lecturers	National Health Service Pension Scheme	National Health Service Pension Scheme

3.2.2 In pre 92 institutions membership of the USS must be provided to those employees in USS pensionable posts as a result of the exclusivity rule found in the Trust Deed that governs the scheme. This means that an institution cannot choose to offer an alternative pension to those employees.

3.2.3 There is greater flexibility in the benefits that can be provided through local schemes for the support staff in pre 92 institutions, but most of these schemes are still on a defined benefit basis.

3.2.4 In post 92 institutions providing membership of TPS or LGPS is required under statute or in some cases under an admission agreement. Again no alternative can be offered except in a very few cases where the higher education institution (HEI) has been able to negotiate an alternative approach with the administering authority under the terms of the admission agreement. This will usually cover new members only.

3.2.5 Despite the requirement for these schemes to be offered and an existing process of auto-enrolment for new joiners, some institutions already have high opt-out rates as shown below from our 2010 remuneration survey:

Percentage of employees opting-out of the scheme	*Scheme* *LGPS/S*	*TPS*
Mean	24.9%	19.4%
Maximum	70%	72%

3.2.6 Therefore the main impact of auto-enrolment will be to increase the employer contribution costs, should all these members choose to join the relevant scheme. Employer contributions to the USS are 16% of pensionable payroll, for TPS this is 14% and LGPS varies but the average is 19%. While this cost can be delayed until the end of the staging period for existing staff who have opted-out they will all have to be auto enrolled eventually. For most HEIs staff costs make up between 50 and 60% of expenditure so managing this element of the cost base is vital.

3.2.7 The additional impacts are expected to be:

- Cost of increased administration—as has been the case for many years, HEIs are trying to increase efficiency and reduce costs especially in light of the new funding regime to be introduced from 2012.
- Cost of understanding the impact of auto-enrolment on the HEI, communication with members *etc*—not all HEIs have internal pensions expertise and may need to involve specialist external support.
- Cost of ensuring that the correct functions are being undertaken by the scheme on behalf of the employer—this is complicated by the fact that most HEIs participate in more than one pension scheme.

3.3 *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

3.3.1 UCEA does not currently have any data on expected future opt-outs however examples of comments from HEIs in the 2010 remuneration survey are shown below:

Comment
We have seen a handful of members opt-out of the USS on the basis of affordability.
We are seeing some members opting-out but not significant numbers.
More members opting-out are stating they cannot currently afford the contributions.
3.5% increase in TPS. 5% increase in LGPS [opt-outs].
LGPS declining but USS static.
New staff on low salaries opting-out.

3.3.2 It is expected that for some employees the issue of pensions affordability will continue to drive up the level of opt-outs. Especially in light of the proposed increase in employee contributions to the public sector pension schemes and the uncertainty surrounding the future benefits that will be provided by these schemes.

3.3.3 The HE sector has repeatedly stated that it is committed to high quality, affordable and sustainable pensions for all employees. It is with this in mind that the moderate reforms to the USS were recently agreed. However it is clear that for an increasing number of HE employees the current schemes that are offered may not be appropriate and that this may at least in part be due to affordability issues.

3.4 *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications*

3.4.1 HE employers take on employees on a variety of different contracts, often working simultaneously for more than one HE provider. UCEA has already had a number of questions raised with regard to auto-enrolment, for example:

- How to deal with zero hours contracts. These employees work extremely variable hours and are paid on a timesheet claims basis by the HEI.
- How to treat casual workers who do not meet the entry retirements for the appropriate HE sector scheme but would meet the auto-enrolment criteria.
- How to treat employees who have already drawn their pension through a flexible retirement scheme but continue to work.

3.4.2 These questions are perhaps easier to resolve when the pension scheme that is to be provided is a defined contribution arrangement, such as NEST. However as the HE sector is, for the main part, unable to provide any alternative to the defined benefit arrangements that are currently offered, the question of dealing with employees on flexible or casual contracts in the HE environment is much more difficult. For example, it is impossible to enrol an employee in LGPS and for only the employer to contribute.

3.4.3 UCEA will continue to work with HEIs to resolve these issues but any further Government guidance would be welcomed.

3.5 *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

3.5.1 In order to succeed auto-enrolment must have full buy in from both employers and employees. The only way this can be achieved is by providing a pension scheme which is appropriate and affordable to both parties.

3.5.2 Currently across much of HE there is no flexibility in the pension scheme that can be offered to eligible employees. In many cases employees have already opted-out and therefore it must be surmised that the scheme on offer was not appropriate for them. This could be for a number of reasons, such as an inability to afford the contributions, being on a fixed term contract, not being permanently based in the UK, working for multiple employers offering different pension schemes *etc*. Unfortunately in most cases in HE the scheme that is offered is out of the employers' control.

3.5.3 Many HEIs have enquired about the possibility of using NEST as an alternative for employees who opt-out of the defined benefit scheme. While this is currently not an option, UCEA is engaging with BIS (Department for Business Innovation and Skills) to investigate the possibility of greater flexibility regarding the public sector pension schemes offered by HE. The USS is also undertaking a review of the exclusivity rule to see if a rule change to allow greater flexibility could be possible.

3.5.4 Until such time as these changes are made there will continue to be a substantial number of HE employees who opt-out of the pension schemes on offer because they are not the appropriate vehicle for them to use to save for their future. If opt-out rates increase this will leave HE employers with no option than to have a proportion of their staff with no pension at all and, perhaps worse, no ancillary benefits such as life cover or ill health cover.

3.5.5 This also has an impact on NEST as it could substantially decrease the pool of prospective members that it can expect to draw from.

26 August 2011

Written evidence submitted by Scottish Life/Royal London Group

Introduction

Royal London Group is pleased to contribute to the inquiry on automatic enrolment in workplace pensions. Our pensions division, Scottish Life, has considerable practical experience of setting up and administering workplace pension schemes. This submission is based on our practical experience.

Summary

The task of communicating automatic enrolment to employers and their workforces is complex and should not be underestimated. Micro-business are a particularly hard to reach group and the impact of automatic enrolment will fall disproportionately on them.

New staging dates should be communicated to all employers as a matter of urgency and there should be no further revisions to the timetable.

It is extremely difficult to predict the level of opt-outs. The rate of opt-out may be influenced by the state of the wider economy and factors such as higher levels of student debt as university fees increase.

It is likely that NEST (National Employment Savings Trust) may experience a higher rate of opt-out than private sector schemes. If this is the case, policymakers must avoid measures that would improve NEST's already favoured terms.

NEST's low risk investment approach will not produce the optimal investment growth for longer term savers. Investments may fail to keep pace with inflation.

Automatic enrolment will increase the proliferation of small pots. Government and industry should find ways to significantly simplify transfers and pension consolidation.

Workers in some sectors will find themselves in a cycle of being auto enrolled and then falling below the thresholds. A waiting period would help mitigate this.

Responses to the Issues Raised in the Terms of Reference

DWP's communication strategy for introducing auto-enrolment (AE) and provision of advice and support to employers and employees

1. We are pleased that budget has been secured to ensure that AE is communicated effectively. AE is a significant change to the way pensions are operated in the UK and quality communication will be central to ensuring success.

2. We understand that NEST is a required part of the pensions reforms, not least to service parts of the market that commercial providers will not reach. It is essential however that any communications do not give undue weight to NEST or in any way imply that NEST is any more appropriate than other providers.

3. We are currently reviewing our communications in light of the DWP language guide to ensure consistency of messages where this is appropriate to our target market.

4. Professional financial advisers will, and should, play a significant role in assisting employers and their staff. The communications work by DWP should recognise this.

5. It is also important that intermediaries have clarity on the advice process given the close proximity of the implementation timeframe for both AE and the Retail Distribution Review (RDR). DWP and FSA (Financial Services Authority) must continue to work together to ensure clarity for advisers and others.

Arrangements for phasing and staging the introduction of auto-enrolment

6. Given the Government's commitment to small business we understand the need to change the staging dates to keep this promise, but the new arrangements must be signposted to those they affect.

7. DWP have said: "they (employers) will not be required to contact the regulator for a new staging date" but will be ascribed a new one. However, DWP have also stated they cannot separately identify employers in a multi employer PAYE (Pay As You Earn). This seems to imply that only the larger PAYE (the one over 239 lives) will receive a notification of staging and that any micro employers within that PAYE will have to recognise that they could have a later staging date. New communications on staging dates will be required to bring this to the attention of this category of employer.

8. It is essential that no further changes are made to the schedule to ensure providers, employers and their advisers have certainty around the timing of the obligations.

9. In the interests of clarity, all those involved in communicating information should act in concert. For example, The Pensions Regulator (TPR) have updated their website to take account of the proposed staging changes but DWP have not.

10. We understand the need for phasing to allow employers and employees who are currently not contributing to pensions to plan and budget appropriately. We believe however that it is essential that employers and employees are not left with the impression that saving at these levels (even the steady state) will be sufficient to provide a reasonable level of income in retirement. The government and industry must continue to work together to encourage savings above the minimum requirements.

Likely impact of auto-enrolment on business, especially small and micro-businesses

11. The burden on small and micro-businesses is disproportionate, especially in terms of administration.

- These employers are most likely to have little or no knowledge of pensions and therefore will be most worried about satisfying their obligations. It is therefore essential that this group can get appropriate advice on how to deal with their obligations. Consideration needs to be given as to how this will be provided given the inability of the advice market to supply services to this sector.
- We anticipate that some employers will change their relationship with their workforce to self employed (rather than employed) to save the costs of pension contributions and administration.
- In small businesses, where the firm typically will not employ someone to look after pension matters, the introduction of AE could well divert the owner's attention away from running the business.

Role of The Pensions Regulator, including in certification of schemes

12. We appreciate the work TPR has done in laying out their regulatory principles and compliance approach. It is good to note that the Regulator intends to concentrate on education, advice and instruction to comply with the new regime (at least in the first instance) rather than statutory enforcement.

13. TPR must continue to explain clearly to employers how and why AE is different to Stakeholder Pensions, where there was significant non compliance and few sanctions for transgression.

14. The stance that TPR may be taking with regard to certification could cause some employers to take their eye off the ball. We believe that TPR will not take a proactive role in asking how employers are ensuring compliance. For example, an employer certifies on the 7% basis in September 2014, but makes no declaration the following year. It would appear that TPR will assume they are complying in another way. This may mean

that the certification, and the discipline needed to ensure that the regulations are being met, are not properly embedded. We recognise that TPR will have a great deal of work to do and will have to find ways to target their resources.

15. The regulations allow any employer to bring their staging date forward to as early as October 2012 and there may be a presumption that this will be very uncommon. This may not be the case as any employer making changes to their scheme around October 2012 may look to comply with the new arrangements and bring forward their staging date. TPR should be ready to accommodate more early adopters than may currently be planned for.

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

16. The Institute of Directors research found that half of employers believe fewer than 20% of employees will opt-out whereas a quarter feel more than 50% will opt-out. We believe that the rate of opt-out will vary widely, dependent on such factors as:

(a) Size of firm.

(b) Industry sector (eg prevalence of short-term and part-time workers).

(c) Economic conditions/debt levels.

17. Understanding these factors and selecting businesses with the appropriate characteristics are likely to enable providers to identify firms with a relatively low opt-out rates. One consequence of this is that NEST will inevitably end up a higher proportion of firms with high opt-out rates. The cost implications for NEST are obvious.

18. One example of how on economics and debt levels may be a factor is the effect that higher university tuition fees could have on opt-out rates. In future those with loans will pay 9% on earnings over £21,000 and there is no “opt-out” of these payments. The overall result could be higher levels of opt-out from AE until loans are repaid.

NEST’s potential market share and the possible effects on other providers/Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers/NEST’s investment strategy

19. We have grouped our answers with regard to NEST together as we believe this helps demonstrate the issues that may arise.

20. The effect on the industry depends on the nature of the business it attracts. NEST has had the benefit of a significant “set up” loan and its charging structure would give a price to every employer which only the largest could hope to obtain currently. NEST may therefore attract not only many small and micro-businesses that the private sector cannot economically serve, but also a section of the SME market which the private sector can serve.

21. The limitations on NEST with regard to contributions and transfers were designed to ensure that, at least initially, NEST remained focused on its target market. This is necessary while AE is being phased in. We understand the need for this position to be reviewed in 2017.

22. If and when any restrictions placed on NEST are removed, it is even more important that loans and any other state support provided do not give NEST an unfair commercial advantage.

23. The whole area of transfers needs to be reviewed and not just the question of whether NEST should be able to accept transfers in and make transfers out. (See paragraph 28 with reference to small pots.)

24. We understand NEST’s investment approach is based on research of their target market. We do not believe that this is the right approach to long-term investment to help people maximise their retirement income.

25. NEST’s decision to deliberately keep volatility low in the foundation stage may therefore be seen as controversial. Traditionally the early accumulation stage is the one phase where members can afford higher volatility. If you’re a 20 or 30 years old, with plenty of time to save, you should typically be aiming to maximise investment growth for an appropriate level of risk. In this context volatility is not necessarily a bad thing. The long-term nature of the investment means the impact of higher volatility in the early years can easily be absorbed.

26. The practical effect of NEST’s investment approach is that the asset allocation is likely to have a significant weighting towards cash and gilts. Neither of these assets will offer much protection against inflation so investors could see the value of their savings fall in real terms.

Whether auto-enrolment is likely to attract new providers and encourage new models of provision

27. We expect automatic enrolment to attract new providers to the market but are unconvinced of their likely success given the pressure NEST could bring to bear on the shape and commercial viability of the market. Providers in this market will need to innovate and look for new models to compete.

Possible measures to reduce the proliferation of small pension pots

28. Small pots arise due to the fact that people change jobs more frequently than in the past (perhaps 10–15 times). Having lots of small pots is uneconomic for providers to administer. It also makes it difficult for the employee to see a proper picture of their retirement provision. One answer to this is to bring all an employee's pots together. However advising on consolidation can be uneconomic for intermediaries and there is a reluctance on the part of providers to accept transfers without advice. Possible solutions are:

(a) Automatically transfer all pots under a certain size to NEST unless the individual elects otherwise. However this may not consolidate all pots as the worker could have some larger pots above the threshold and/or be in new employment which offers pension provision.

(b) Automatically transfer pots under a certain size to the next provider (unless the individual elects otherwise) regardless of whether this is NEST or a commercial provider. Here the member would have one consolidated pot (unless they chose otherwise or had pots over the threshold). There would have to be a mechanism put in place to match paid up funds and values with a new provider and efficiently move the funds.

(c) Make accepting transfers from qualifying workplace pension schemes (DC schemes only) compulsory without the need for advice to have been provided. So if someone wanted to bring their pot with them, the new provider would have to accept it.

29. Although the simplicity of automatic transfer (in its various forms) is superficially attractive we strongly favour a greatly simplified transfer process as being crucial in reducing the number of small pots.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

30. Self-employed people are not required to be automatically enrolled under the legislation. They can however use NEST if they wish to do so.

31. Part-time, temporary, casual and agency staff are affected in the same say as all other employees. If their earnings in a pay reference period exceed the threshold they will be automatically enrolled. This does cause an issue when earnings spike for a short period of time.

32. Take as an example a part-time worker in retail who earns a relatively low wage say £5,500 *per annum*. Where there is a seasonal upturn in hours worked, as might happen in the Christmas and January sales periods, earnings in a Pay Reference Period may exceed the weekly or monthly AE trigger and the worker would then be eligible for automatic enrolment. In the absence of a waiting period the member would be automatically enrolled only to find that when their hours returned to normal the contributions paid were very small (if the basis was qualifying earnings). This will impose administration on the employer for little employee benefit; the employee is unlikely to see any real value from the pot; and the provider will have to administer very small contributions and pots, probably at a loss.

33. The use of "waiting periods" prior to automatic enrolment could help mitigate the impact of the example above. But this may create some other problems. For example, if a three month waiting period were used, the person that tipped over the AE threshold due to increased hours could be given a generic notice to say they may be automatically enrolled at the end of the waiting period if their earnings still exceeded the AE threshold. If their wages had decreased by the new assessment date, the member would not be automatically enrolled but would have to be told (in the interests of good communications) that their earnings were not sufficient to warrant automatic enrolment. This could mean a lot of work and cost for the employer and confusion for the employee. This issue could be especially acute where there are multiple earnings spikes in the year.

34. It is difficult to see how this can be made easier unless:

(a) Employers have the right to only offer automatic enrolment once per year.

(b) "Super No"—where an employee can indicate that they are opting-out for a year, even if they reach the hurdle again.

About Scottish Life and Royal London Group

Scottish Life

Scottish Life was founded in 1881 in Edinburgh as a proprietary company, becoming a mutual company in 1968.

On 1 July 2001, Scottish Life demutualised and transferred its business to The Royal London Mutual Insurance Society Limited. Scottish Life is a division of Royal London and is the specialist pensions business within the Group, providing individual and group pensions to the market via intermediaries.

Scottish Life and Royal London's other intermediary businesses are based mainly in Edinburgh where 1,020 staff are employed, with 740 working in other parts of the UK and overseas.

Royal London Group

Royal London Group is a specialist financial service provider. Its businesses focus on those sectors of the market which value quality propositions, operating through a number of brands:

— Scottish Life—UK pensions market.

— Bright Grey—UK protection market.

— Scottish Provident—UK protection market.

— Caledonian Life—RoI protection market.

— Royal London 360°—offshore investment markets.

— RLAM—fund management.

— Royal London Plus—life and pensions administration.

— Ascentric/IFDL—Wrap Platform.

Royal London is the largest mutual life and pensions company in the UK with Group funds under management of £43.7 billion. Group businesses serve around 3 million customers and employ 2,630 people. Figures quoted are as at 30 June 2011.

26 August 2011

Written evidence by Supertrust UK Master Trust

BACKGROUND

Supertrust UK Master Trust was established in 2005 (then known as the 21cp Retirement Trust) in order to give non-associated employers the opportunity to offer an occupational scheme model to employees as an alternative to contract based schemes.

The model is based on a traditional employer sponsored occupational scheme and was designed specifically to meet the needs of employers and employees as an alternative to the then proposed Personal Accounts. It is intended to combine the benefits of occupational schemes and contract based schemes.

The directors' work backgrounds have been entirely occupational scheme based, both as consultants and in–house pension managers of large corporates. We have had direct experience of managing both contract based and trust based schemes, both defined benefit and defined contribution.

EXECUTIVE SUMMARY

1. It is unrealistic to assume that all potential conflicts of interest in a commercial environment can be pre-determined. Therefore The Pensions Regulator should have wide powers to determine whether the governance structure and processes of a scheme warrants continued certification for opt-out.

2. NEST (National Employment Savings Trust) should not be in an unfairly competitive position, but should be seen as the benchmark for good governance of workplace schemes. By providing a measure of competition it might serve to inhibit adoption of terms which would render commercial plans uncompetitive.

3. New providers and innovation in the interest of employees can develop in a healthy competitive environment. Government should be alert to the attempts by vested interests to weaken differentiation between different systems on the grounds that employers should not be influenced by what serves their interests.

4. Defined Contribution (DC) investment will over time develop techniques for managing a wider range of risks than just asset volatility. Objectives define what risks need to be managed, regulations should not assume that they can second guess the objectives employees may in future be able to seek.

1. *Role of The Pension Regulator*

1.1 The challenges we perceive are:

1.1.1 Managing the risks employees are exposed to under different DC scheme models.

1.1.2 Identifying the risks which new pension models will carry.

1.1.3 Maintaining a proportionate and appropriate level of regulation.

1.1.4 Delivering guidance which does not reflect transient views which become out-dated and inhibit innovation.

1.2 Our particular interest is the trust model for non-associated employers (commonly called master trusts). This is essentially the same model utilised by NEST.

1.3 The essential problem is how the conflict of interests are managed where a pension plan is a commercial enterprise required to make a return for shareholders. Our view is that NEST provides a counterbalance to limit the potential for possible excesses in the free market.

1.4 Without NEST there would not be a benchmark against which good practice and fair pricing could be judged. Our view is that if the private sector cannot compete with NEST then the private sector has failed.

1.5 Having said that, NEST must operate as a self-financing plan, and should not enjoy any tax paid financial subsidy, or enjoy privileges which are not accessible within a free market.

1.6 We do not believe that a private sector master trust which has shareholders to repay, rather than government, for start-up costs, is currently facing any different a conflict of interest. NEST has increased its charges to pay for its start-up costs, it is clearly in the nation's interests for NEST to exist than not exist. Similarly, it is in the nation's interests for the private sector to be able to develop new systems which better meet the needs of workplace pension provision.

1.7 We do not believe the contract based system, already commanding significant control of the market place, has demonstrated any potential to manage the conflicts between distributing retail products and protecting employees' interests.

1.8. In our master trust plan we have sought to address the broader conflicts issues by appointing a co-trustee, an independent professional trustee, part of a national law practice. This, combined with transparency of charges, is intended to give a measure of comfort that inequitable and unfair treatment of employees is less likely to arise.

1.9 If the master trust provider has an interest in the products or services being utilised, there is a greater need to supervise the governance arrangements. Trust law allows the terms of the trust document to determine what is, and is not permitted to be done, so some master trusts are able to be established as simply the distributor of a managers investment products. There needs to be a clear distinction made between trusts which restrict trustees to offering a single provider's pension products, and those giving traditional unfettered powers of investment.

1.10 We are also in discussion with the Association of Member Nominated Trustees to debate how their Association could help us develop a simple structure which would allow the Association, or elected representatives, to oversee the trust's activities.

1.11 We suggest that the initial certification of schemes need be a simple process based on self-certification that auto-enrolment rules would be adhered to. We believe one of the ways in which the Pension Regulator could retain the ability to regulate proportionately, would be to have wide powers of investigation, and the ability to cancel a certificate on reasonable grounds of governance failures. That would preclude the need to try and identify governance weaknesses and create regulations, in advance of them becoming apparent.

1.12 For this reason we do not believe it would be helpful to try and develop comprehensive new regulations to cover new trust models. We would acknowledge that a fit and proper person test should be applied to commercially run trustee businesses such as ours.

2. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

2.1 The purpose in setting up Supertrust UK was a strongly held belief that the existing models of delivering workplace pensions would not deliver the objectives of low cost, wide ranging pension savings managed in the interests of employees.

2.2 The drift away from trust based schemes was not to enhance outcomes for employees, it was so that employers could distance themselves from the greater obligations being placed on them, as legislation to protect employees' interests under occupational schemes took effect.

2.3 Employers will engage in pension scheme matters primarily because they have an interest to enhance or protect. Our experience working within large corporates is that their level of engagement is in direct proportion to their desire to manage corporate reputational and financial risk. Good pension outcomes may result, (as they might from incentivising employees to take transfers), but the paternalistic motivation has been lost as today's more transient working patterns take hold.

2.4 In an ideal world, employers would want to ensure a well governed scheme operated in the interests of their employees, which enhances HR relations. In the real world, we see little evidence of that sentiment and little evidence that employers have any interest in shaping development of effective workplace pension solutions.

2.5 The market and competition has been allowed to dominate supply and employers do not take initiatives to shape supply from the demand side. This might partly be explained by the fact that the employer is only the gatekeeper, the end consumer, the employees is not able to have any influence.

2.6 The authorities have shown concern over employers taking action to select schemes which may reduce the employer's overheads egreleasing employer contributions if an employee chooses a refund. This has been presented by those with a vested interest in supressing competition as employers making choices not in the interests of employees.

2.7 We would ask the Committee to be wary of reacting to demands from existing interest to eliminate differences between trust based and contract based schemes. The danger is a dumbing down of governance standards and inhibiting innovation to meet employee needs. This dumbing down effect has already been shown by the lowering of the original opt-out standards which contract based schemes were unable to meet.

2.8 We believe that new models will not rely on employer engagement to succeed. The employer's wish to disengage from any governance role must be recognised. This view led us to our initial model of establishing an occupational scheme in the image of a traditional trust based scheme, but on a self-financing basis.

2.9 For this reason we believe that any views on future development of workplace pensions which rely on greater employer engagement are flawed. The only reason we see for supporting that view is to justify the continued validity of contract based schemes which can have no governance if it is not initiated by the employer.

3. *NEST's Investment Strategy*

3.1 The domination of the market by insurance companies selling investment products has determined the conventional view of DC investing.

3.2 Products are sold on a supermarket basis or within a "Wrapper" offering wide choice as a marketing feature. We see this as analogous to car makers selling car components out of a warehouse for individuals to build a car. It would be very easy to end up with non-complementary components which didn't fit together and a vehicle not for purpose.

3.3 This system suits the industry, and forces reliance on intermediary support. Choice is not a pre-requisite to good outcomes; in fact research has shown that it is more likely to lead to inaction rather than greater engagement.

3.4 NEST follows the path of the conventional informed view that investors must have access to investment strategies which allow investment risk to be managed effectively. Target dated funds are an appropriate offering, and have the same objective as lifestyling in reducing volatility towards retirement.

3.5 We would not suggest that this is wrong, but the inherent weakness of any target dated or lifestyling arrangement should be acknowledged. It would be dangerous to assume that there is no other risk management strategy apart from constraining volatility of investment return.

3.6 It is necessary to be alert to the future development of DC investing which strives to mirror the liability matching techniques employed by many defined benefit (DB) schemes. The problem is highlighted in a Working Paper produced by the International Organisation of Pension Supervisors[22] where the difficulty of employees managing the risk of annuity outcome is touched on:

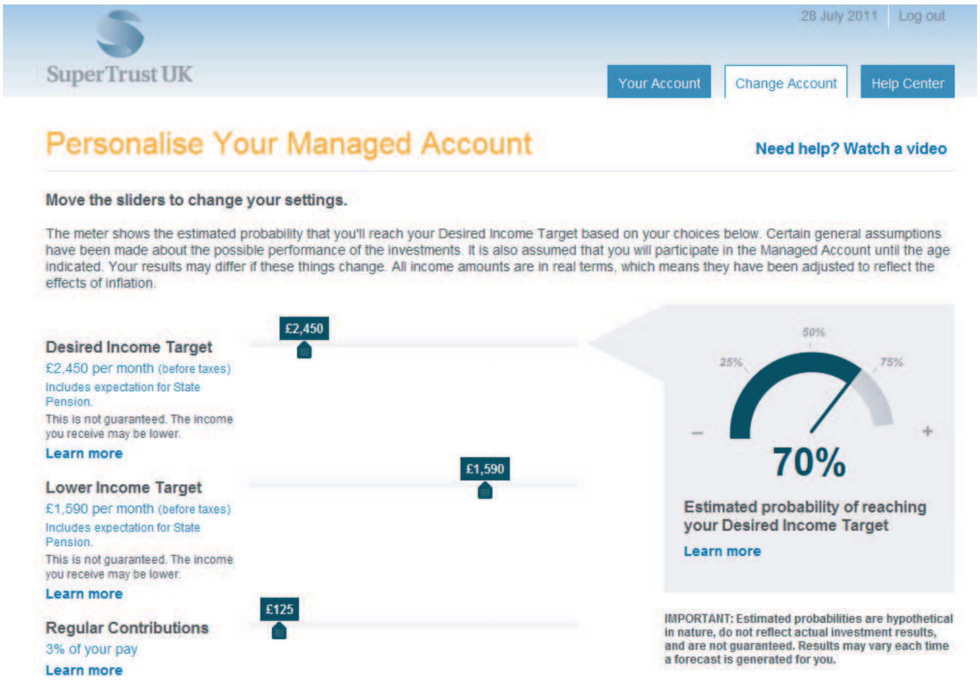
> "..with DB pension funds, supervisors primarily focus on investment risk via underfunding levels and mismatches between assets and liabilities. However, within DC funds investment risk is harder to measure as probability distributions need to be considered, not the probability of achieving a specified outcome (unless such an outcome is targeted, which is rarely the case and difficult to measure for DC plans).[23]

3.7 The conclusion is that "…with DC systems the focus has to be on processes rather than outcomes as benefits are not guaranteed."

3.8 These statements made in a paper produced in October 2010 are already proving to be out-dated. The assumption that asset volatility is the only risk that can be managed is no longer the case. Professor Robert Merton has developed financial modelling tools using algorithms which not only factor in asset volatility but also model volatility of interest rates, inflation and longevity drift, just as DB schemes do in projecting liabilities. All that has to be done to allow DB techniques of risk management to be employed is to set DC annuity targets and treat them as if they are a "liability". The target is clearly not "guaranteed" but that does not preclude treating it as a target, it simply means the probability has to be shown alongside the goal.

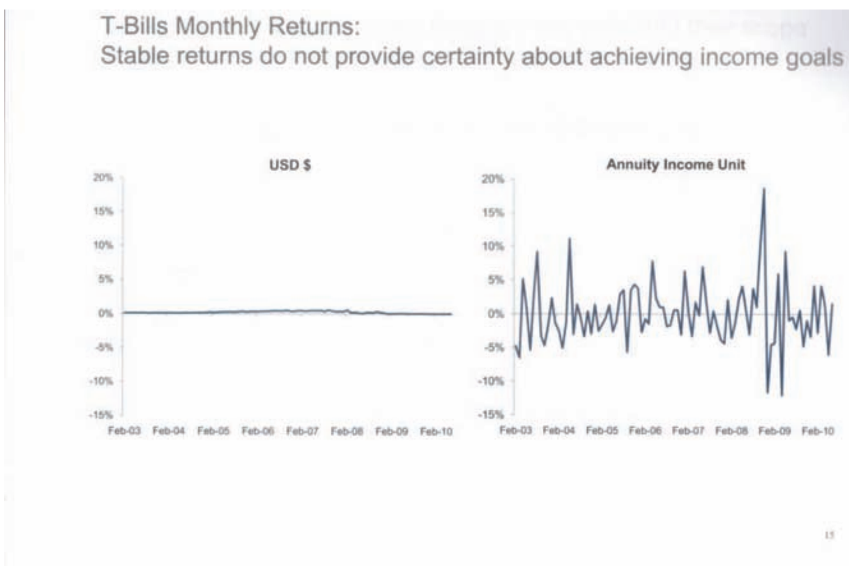
3.9 Below is what the user interface looks like. The employee has no involvement with investment decisions, it is exactly the same principle as the fiduciary management service which trustees are able to use for DB funding where the trustees set the goal and the fiduciary manager optimizes portfolio construction and asset allocation. Employees determine the goal and the risk budget, the rest is managed for them.

[22] Working Paper No. 12 2010 *Managing and supervising risks in defined contribution schemes*.
[23] The International Organisation of Pension Supervisors John Ashcroft, Fiona Stewart.



3.10 The important point to be drawn is that fiduciary management does not seek to constrain volatility, it factors in expected volatility and harnesses volatility to optimise potential outcomes. Any regulatory control which takes asset volatility as the measure of good governance is assuming it is the only measure, not because it is the most important risk to be managed, but because it is the only one which can be measured.

3.11 Professor Robert Merton who developed thinking in this area illustrates the flaw of constraining volatility by showing annuity outcomes when you invest in a low volatile investment (US Treasury Bills (T-Bills)), the result is a wide range of random annuity outcomes.



3.12 Investing in more volatile investments would show a similar picture, there is little difference in the distribution of annuity outcomes whether investments are exposed to high or low levels of volatility.

3.13 More information on this topic can be found at this site http://www.dfaus.com/managed_dc/

4. *Possible measures to reduce the proliferation of small pension pots*

4.1 Small pots will proliferate if funds do not move with an employee when he changes employer. However, the problem is that commission based pension products will likely incur transfer penalties employees which may make some transfers unattractive. Our response to this would be to explain that a transfer penalty is not a charge which is avoided if funds are left alone, it is simply taking charges out of the account which were due to be recovered throughout the future lifetime of the policy.

4.2 Small pots may, or may not be a problem, from the administration perspective. Whether it is a problem or not for the provider depends on how the cost of administration is structured.

4.3 Taking an insurance company, their charges are set when a contract is taken out and the impact on the insurer in terms of profitability should it become a small pot, is not an issue which needs to be addressed.

4.4 If an employer is operating an occupational scheme and bears the administration costs, the employer will seek to reduce any perceived unnecessary expenditure. Paying the overhead for administering a closed account for an ex-employee, whatever size, will be seen as non-productive expenditure.

4.5 The prime concern should be with the impact on employees rather than providers and employers. Providers will organise their own affairs to suit themselves, employers have the choice of operating a scheme where they finance the overheads directly, or they can use a vehicle which is self-financing and resolves direct cost issues.

4.6 Resolution of the problem would occur with greater collectivisation of schemes. Reducing proliferation of schemes themselves will reduce proliferation of small pots.

4.7 Much proliferation is created when employers change investment provider under contract based schemes. Since there is not a common investment pool, and each contract is controlled by the employee himself, changing investment provider means a new contract is created and an orphaned pension account is created. Lesser usage of contract based schemes and greater usage of master trusts will reduce this problem.

4.8 The master trust is able to take a bulk transfer from other occupational schemes and a number of employers have sought this option. The existing scheme trustees need to satisfy themselves that a transfer is in the interests of the members but existing regulations are a barrier to transfers proceeding. The transfer regulations were drawn up specifically to allow bulk transfers between occupational pension schemes but made no distinction between DC schemes and DB schemes. Consequently actuaries and trustees find it difficult to interpret, with clarity, how they should certify equivalence of value of "benefits" when funds are being transferred out of one fund to another with no change in immediate value but with an inevitable different unquantifiable future value.

4.9 Our recommendation would be to lower the barriers to inter-scheme bulk transfers where the transfer is DC to DC. Specifically:

4.9.1 It should not be necessary that the transferring scheme is being wound up.

4.9.2 Bulk transfers should be possible for a specified category of membership.

4.9.3 An actuarial certificate is irrelevant.

4.9.4 The employer should be able to request a bulk transfer for non-active employees without trustee consent where the scheme is certified for auto-enrolment.

4.10 Anecdotally, the least well run occupational schemes are considered to be small schemes of small employers run as a bundled package by insurance companies. Trustees are least likely to understand their role or responsibilities and insurers are not responsible for ensuring trustee duties are exercised.

4.11 The Federation of Small Businesses could be engaged to educate members on the responsibilities of operating an occupational scheme. Our experience to date is that intermediaries will only earn commission by setting up alternative contract based schemes, ignoring the fact that future governance responsibilities may be just as onerous and incur additional costs. This is a message the retail industry has no incentive to give and there is a responsibility on government to give factual practical advice to counter inadequate information from product distributors.

4.12 In terms of small pots, what is not being recognised when small contract based schemes are set up is the cross subsidy borne by small employers. Insurers price their units according to volume of potential business. Employees of small companies pay higher charges than large corporations by a significant amount. Under a collective trust arrangement, such as ours, the investments are pooled and every member bears the same charges, so sharing the benefits of economies of scale equitably.

5. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

5.1 We have spent considerable time working on strategies to enhance employee engagement. The main driver for us adopting the Managed DC approach (paragraph 3.9) was its potential to engage employees.

5.2 The main negatives to employee engagement we would argue is:

5.2.1 We pose questions to employees when they join they do not understand—"Would you like to choose your funds, if not there is a default fund where you do not have to choose".

5.2.2 We cannot easily address the question "How much pension will I get?".

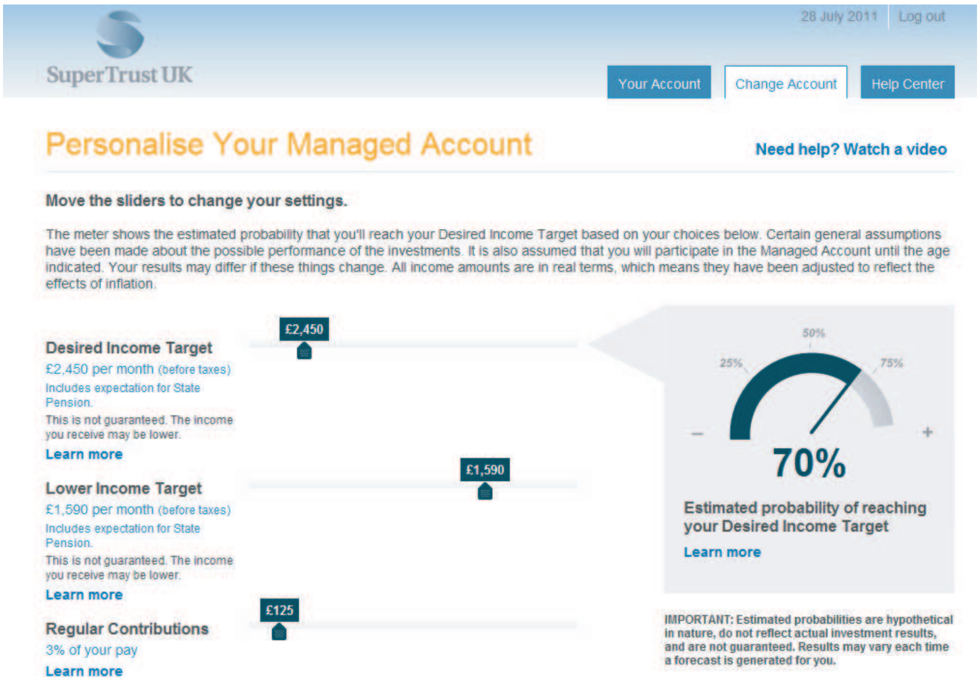
5.2.3 We present an investment plan not a pension plan.

5.2.4 Employees do not trust financial institutions, they may not even trust the employer.

5.2.5 They would rather have money to pay household bills than save for a pension.

5.3 Our attempt at addressing these points is as follows:

5.3.1 Managed DC does not ask these questions, employees are invited to choose income targets as a first step and can see immediately how much they need to pay and when they can retire.



5.3.2 There is the possibility that an independent structure under the governance of trustees may give a degree of comfort to employees who distrust familiar pension arrangements.

5.3.3 There is a greater chance of employees being willing to save if they have a clear picture of what they can expect in return. Current systems give the impression that money disappears in a black hole and when the market falls they have lost money.

5.3.4 The recent market turmoil has proven the value of focussing on annuity outcomes and distracting attention from current fund values. The projections of annuity move very little when markets fall. The technical reasons are that the modeller is anticipating future flows of contributions, has already factored in expected volatility of equities and is re-balancing asset allocations to optimise hitting the target.

26 August 2011

Written evidence submitted by Recruitment and Employment Confederation (REC)

In our written evidence we seek to highlight the concerns of the recruitment industry with specific reference to:

— The arrangements for phasing and staging the introduction of auto-enrolment.

— The likely impact of auto-enrolment on our members' businesses and how auto-enrolment applies to temporary agency workers.

— The role of The Pensions Regulator (TPR).

— DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees.

By way of introduction, we have included a short paragraph on the REC. We have also provided a few notes on the recruitment industry with particular reference to temporary agency workers; most of whom will be affected by auto-enrolment.

The REC

The REC is the trade body for the UK's £20 billion private recruitment and staffing industry. We represent over 8,000 recruitment company branches, estimated to constitute half of all UK recruitment branches by number but a higher proportion by turnover. All REC members sign up to our Code of Professional Practice and we investigate complaints against the Code through our Professional Standards Committee, which is made up of industry experts and representatives from the TUC and CBI. As a result, by using an REC member, clients and candidates are assured that the agency meets a robust set of standards.

With regard to the UK recruitment industry itself, it is estimated that agency workers make up around 4% of the total UK workforce. REC research has shown that temporary work is a vital source of flexibility within the labour market, as well as a stepping stone for those seeking permanent work. The flexibility of temporary working is an attractive option to both employers and individuals and our research indicates that it is set to increase in coming years. It is therefore imperative that the auto-enrolment of temporary workers into pensions schemes does not adversely affect the UK's successful model of flexible work.

The REC has been making representations to the Department of Work and Pensions on behalf of the recruitment industry regarding pensions auto-enrolment since 2007. Although several of our concerns were addressed in the drafting of the 2011 Pensions Bill, we remain apprehensive about the impact of the legislation on the recruitment industry. We therefore welcome the Committee's inquiry and we have focussed our comments on the areas the Committee is looking into.

The arrangements for phasing and staging the introduction of auto-enrolment

The REC has alerted policymakers that the decision to automatically enrol workers by payroll size over four years will create significant distortions in the recruitment market, as agencies join at different times. This is because the wage and wage costs associated with an agency worker are the basis of the overall cost of supplying of staff. Even the initial 1% employer contribution will impact on rate negotiations with clients, and added to this will be the costs associated with setting up automatic enrolment processes.

Fundamentally, this means that agencies coming in at later staging dates have lower costs than earlier entrants, creating market advantage. Furthermore, the decision to determine staging date by size of a company's payroll can actually penalise successful smaller firms. Whilst a small recruiter may have very few of it own employees, the more temp workers it has out on assignment at the payroll "snapshot" date, the earlier the business has to begin auto-enrolment.

This distortive effect is particularly pronounced in the agency work market as the wage costs of a worker is the basis for the service provided. So a system in which agencies were staged in at the same time would simplifiy the regulations for both businesses and the agency worker, as the latter may work through several recruitment agencies at the same time and experience varying automatic enrolment dates.

The likely impact of auto-enrolment on our members' businesses and how auto-enrolment applies to temporary agency staff

Our principal concerns relate to the mechanisms of auto-enrolment and so getting sufficient detail in the guidance accompanying the legislation will be crucial for our members.

Firstly, whilst the REC supports the aims of encouraging more workers to save for a pension, the reality is that for many temporary workers, saving for a pension is unlikely to be a high priority. This is because many undertake temporary work for a short time to help bridge gaps in their working lives for a variety of reasons—whether it is earning extra money whilst studying or taking temporary work whilst seeking a permanent position.

Many temporary workers are also very sensitive to even small changes in the wages they take home. We therefore think it is likely that the number of temporary workers choosing to opt-out of the scheme will be considerable.

Meanwhile, for those workers who remain in a pension scheme, it is important to recall that that the turnover of agency workers is typically far greater than other types of workers. We are therefore concerned about the amount of administration this will cause for our membership. Fundamentally, high opt-out levels among temporary workers will mean added bureaucracy and cost for recruiters. For instance, employers (a category which our members are legally referred to in the legislation) will have to refund even small contributions made to pension schemes in the opt-out period. Whilst refunds are relatively straightforward if a worker remains on the payroll, in cases where workers are no longer being paid or have moved on to another role, the cost of processing the refund may far outweigh the value of it. So if processing many transactions of small sums of money, the cost will be significant to the agency concerned.

We would also ask the Committee to bear in mind that for some sectors, including agriculture and industrial work, there will be a high level of foreign temporary workers. As it stands, we do not think the provision for these workers to access their pension savings when they return to their home countries has been sufficiently thought through.

Any regulations that are passed to implement auto-enrolment must recognise the distinctions between the arrangements under which an employee and a temporary worker are engaged. So in some sectors it is common for agency workers to register for work with a number of different agencies. In some instances the agency worker may not be offered work (if the agency is unable to secure a suitable assignment). Alternatively there could be significant periods of time that elapse between assignments. In the interim the agency worker may be engaged by and supplied by one or a number of different agencies.

Waiting period

The obligation to enrol a job holder into a qualifying pension scheme will be subject to an optional three month waiting period (subject to the 2011 Pension Bill being passed in its current form). While it will be straightforward to determine how this will apply to an employee engaged in permanent employment, this will not necessarily be the case for agency workers and other casual workers.

For example, our members are concerned with how the waiting period would apply if an agency worker has carried out one assignment for an agency followed by a lengthy period in which no assignments are undertaken? Other queries include what counts as a week, and what type of pause in work will break continuity. It is worth recalling that the recruitment industry is about to implement the Agency Worker Regulations (AWR), which also include a 12 week qualifying period, which is calculated in a different way. So whilst the concept of a qualifying period is familiar, and indeed welcome, to recruiters, much thought needs to be given to the way in which this waiting period will apply to agency and other casual workers.

Determining whether a worker meets the earning threshold for auto-enrolment

The rates of pay that an agency worker may receive can fluctuate from assignment to assignment. While a minimum rate of pay will be agreed with the agency worker at the point at which the agency agrees to provide its services to an agency worker, the actual rate of pay that applies in respect of each assignment is very much determined by what a given hirer is prepared to pay or what the agency is able to negotiate. Typically there is no guarantee of work for agency workers and therefore the earnings over any given period cannot clearly be determined. In contrast to employees in permanent employment, it will be more difficult to determine whether an individual will meet the annual earnings threshold to either qualify for compulsory or voluntary enrolment into a pension scheme.

The role of The Pensions Regulator

The Pensions Regulator (TPR) has never regulated employers before, let alone recruitment firms. We need sensible, risk-based enforcement that understands the recruitment industry and the particular challenges it faces, but does not allow rogue agencies to flout the rules and undercut competition. Recruitment agencies will be under pressure from clients to ensure that they put forward the most cost-effective worker and as there is no obligation for a recruitment agency to provide work, we remain concerned that workers who have opted-out of the scheme may have an advantage. We therefore think that TPR should tailor its regulation to the sector appropriately and in order to be able to do this it is vital that TPR has a comprehensive knowledge of the recruitment industry. We would be pleased to act as a conduit in this instance and our initial discussions with TPR have been encouraging.

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees

Coming just one year after the recruitment industry adapts to its most significant piece of legislation in 20 years—the Agency Workers Regulations—automatic enrolment in workplace pensions will cause more consternation within the recruitment industry. We therefore need to do everything possible to inform recruiters about the legislation. Our initial discussions with TPR have been encouraging and we will be working with them on joint campaigns in the coming months using various communications channels. This communications project will be a two way process as, fundamentally, TPR needs to understand the recruitment industry in order to regulate it effectively.

The REC is committed to working with TPR, DWP and pension providers such as NEST (National Employment Savings Trust) to ensure that the proposed changes to pensions savings result in real benefits to temporary agency workers with minimal bureaucratic costs on the agency work sector that plays such a crucial role in the UK economy.

25 August 2011

Written evidence submitted by Prudential

DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees.

1. Effective communication will be essential for auto-enrolment to be a success. It is important that the budget is suitable to the task and that a clear central, co-ordinated message is given. A diluted or confusing message could be more detrimental than beneficial.

2. As auto-enrolment draws closer it is vital that communication to employers commence as soon as possible. Many employers will need to take action and this will take time.

3. In order to ensure that employers select the most suitable auto-enrolment scheme for their employees they are likely to need further information and guidance, again this takes time to achieve and it is important that suitable sources of information are available.

4. Face to face provision of information is often most suitable for complex issues, it is therefore regrettable that such provision is unlikely to be universally available, especially for smaller employers who may not be willing, or able, to pay for advice.

5. There is a possibility that the communication strategy could push employers towards using NEST (National Employment Savings Trust) for their provision (either replacing existing provision or as a new pension for employees) when this may not be a suitable vehicle for all. It is therefore important that communication is clear, accurate and balanced.

6. Communication aimed at employees needs to avoid treating them as a homogeneous group. For example, research by Prudential and the International Longevity Centre has identified particular challenges for communicating auto-enrolment to young people. There are also challenges in communicating auto-enrolment to employees closer to retirement who may urgently need to start saving significantly more than the minimum contribution to secure a comfortable retirement.

7. *Arrangements for phasing and staging the introduction of auto-enrolment*

8. We believe that the phasing and staging proposals while adding a degree of complexity will be beneficial and will allow all parties time to introduce auto-enrolment, thus increasing its chances of success.

9. Smaller employers will be given a little longer to prepare and seek additional information. If all employers had to implement auto-enrolment at the same time there may be issues around the availability of advisors/information. Any issues in the process can be dealt with by the time small employers have to implement the changes and streamlining (from lessons learnt) is likely to have occurred thus reducing the burden.

10. For both employees and employers the gradual increase in contributions will mean that the financial impact of auto-enrolment is not felt in one single hit. This is likely to increase the chances of employees staying auto-enrolled. Hopefully the employees wages will rise each year by more than 1% meaning that there is no absolute reduction in take home pay from the increase in contribution.

11. For The Pensions Regulator a gradual introduction will allow for education and enforcement; auto-enrolment is unlikely to be a success if there is no form of enforcement (either guiding or punitive) from the Regulator.

12. *Role of The Pensions Regulator, including in certification of schemes*

13. The auto-enrolment regime is unlikely to be successful unless there is an appropriate combination of information, guidance and enforcement. Enforcement could be "soft" in the form of reminders and encouragement but ultimately sanction enforcement will be required. Without this form of enforcement auto-enrolment is unlikely to work as some employers will feel no pressing need to comply with the requirements. Enforcement will be required both in the initial duty of an employer to provide access to a scheme and in ensuring that schemes are (and remain) qualifying.

14. The Pensions Regulator will require resources to provide the communication and guidance needed and to carry out monitoring and enforcement. Without appropriate resources the Regulator will be unable to carry out these important duties effectively and this may present a risk to the long-term success of auto-enrolment.

15. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

16. We have no additional information on opt-out rates however NEST's charging structure and expectations would suggest that higher than expected opt-out rates would reduce the financial viability of the proposition and increase the time taken to repay initial costs.

17. While the NEST charging structure could be adjusted to reflect changes to initial expectations, the larger financial impact on higher than expected opt-out rates is likely to be the future cost of inadequate private pension provision for those who opt-out.

18. It is therefore essential that opt-out rates are minimised by providing clear, reliable and timely information to those for whom auto-enrolment will be the first entry into pension saving.

19. *NEST's potential market share and the possible effects on other providers*

20. NEST has been designed to cater to a section of the market traditionally under provided for by the current market. If NEST is successful in targeting this market then the impact on other providers should be minimal, indeed the best case scenario would be that NEST operates as a partner to existing providers enabling pension provision to be tailored to the needs of the particular employee's rather than taking a one size fits all approach.

21. NEST should be primarily concerned with opening up new markets (those who currently have no pension provision) rather than taking market share from existing providers who would, in all likelihood, be competing for different parts of the market than that for which NEST is designed.

22. It is important that NEST is not thrown into direct competition with the rest of the market (at least in the early years). In addition to the fact that NEST has been designed with a specific target market in mind it needs time to build its credentials and reputation and it needs to be able to work with a clear message aimed at its target market. For this is it likely to need to assistance and support of existing providers and direct competition would confuse and dilute that message.

23. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

24. The introduction of auto-enrolment is a fundamental change in pension provision in the UK. Where such a change takes place it is possible, perhaps even likely, that new providers and models of provision would be developed.

25. The likelihood of new providers and models of provision will be partially dependent on the degree of success of auto-enrolment. If opt-outs are high the likelihood of significant changes in the market are reduced.

26. In addition to wider market changes new propositions, such as auto-enrolment and NEST, are likely to lead to innovations in processes and administration and possibly to changes in the regulatory environment.

27. Changes in the regulatory environment may lead to reduced costs for all pension provision (as the costs of complying with regulation fall). It is important that relaxations in regulatory requirements apply equally to all appropriate schemes and are not limited to NEST.

28. Whilst NEST may be a suitable proposition for a large number of individuals it may not be the "most suitable" and people may be better off elsewhere. It is important that the regulatory playing field is kept level.

29. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

30. The contributions cap and transfer ban were implemented for good reason and those reasons remain.

31. It is important that NEST is able to concentrate on establishing itself in the market and showing that pension saving is worthwhile. In order to do this it must be able to focus on its primary objective which is encouraging pension saving amongst low and middle earners who currently do not save. With 8% contributions an individual would need to be earning a fairly significant amount to breach the current contribution cap.

32. In respect to transfers, the NEST model is based on there being a moratorium on transfers at the beginning. If NEST were expected to receive transfers it would need to review its charging structure—an initial charge may have limit impact on regular savings but on a lump sum (or a transfer) the loss of funds incurred due to the initial charge (especially at dates closer to retirement) could be difficult to make up.

33. It would not be possible to waive this charge for transfers because this would upset the costing of NEST. It would also mean regular savers were paying more than those who transfer-in, and delay the repayment of the loan given to establish NEST.

34. It has also been suggested that NEST should be a safe-harbour scheme for those with small pots. Again consideration would need to be given as to whether NEST was structured to deal with such pots of money. These small pots can be comparatively expensive to administer and a large number of them could make NESTs current charging structure unviable. Therefore it is important to fully consider the potential consequences of such proposals.

35. Costs could be reduced by reducing the regulatory burden on NEST but it would be unfair to the existing industry to create an uneven playing field based on the assumption that NEST would be the best, and safest, place for such funds. NEST must work within the same regulatory structure as existing schemes and, if any changes are made they should apply to all pension schemes equally.

36. *NEST's investment strategy*

37. NEST appears to be utilising a sensible investment strategy in relation to its expected membership. This strategy would not be suitable to all (and is another reason the limitations on NEST should remain).

38. NEST will be using an unusual form of lifestyling in that in early years and late years funds will be invested in low risk, low growth vehicles but in middle years more risk will be taken.

39. The reason for this unusual strategy is the feeling that people would be put off saving if they showed a loss in early years (which can happen more readily with high risk funds). However, with reduced risk comes reduced potential for growth, a loss of potential growth in early years, when it has time to benefit from compound effects, could have a significant impact on final pot size.

40. *Possible measures to reduce the proliferation of small pension pots*

41. As mentioned above small pension pots are comparatively expensive to administer—there are fixed costs involved and charges on small pension pots are unlikely to cover these.

42. The suggestion that NEST should act as a safe-harbour for small pots would potentially endanger the financial viability of NEST as its charging structure is not geared up to operate large numbers of small pots (which would be even smaller once they transferred to NEST due to the impact of initial charges).

43. One way to reduce the impact of small pots on the financial viability of NEST would be to reduce the regulatory burden associated with such pots. However in order to maintain a level playing field and not unfairly advantage NEST at the cost of other providers the reduced burden would need to apply to all schemes (or as a minimum to all appropriate schemes). This in turn would enable other providers to reduce the costs of administering small pots, eliminating some of the problems which have been identified.

44. Any reduction in burden would, of course, need to be done in such a way as to not unduly reduce the protections provided to individual savers.

45. *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications*

46. There are still some issues relating to those who are self-employed or have work patterns other than that of full-time employed. While most of these individuals will not be caught by the auto-enrolment requirements all will be able to choose to make pension provision. If auto-enrolment is a success it should drive the acceptance of private retirement provision as a social norm.

47. The current proposals cover those employed by an agency and those working part-time who earn over the threshold but there are some who would not be covered. To include all such individuals would be extremely difficult to achieve and would add significant cost and complexity to the auto-enrolment model. For example how could an employer contribution for the self employed by arranged?

48. The main aim should be to encourage those not covered to either make their own provision or to opt-in (where this is available).

49. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

50. A large factor in the success of auto-enrolment (in relation to behaviours) will be the portrayal of auto-enrolment in the media. This will be a significant factor in influencing popular opinion of the reforms.

51. If the initial (and early) stages of auto-enrolment are successful it is likely that it will begin to change behaviours in relation to pensions. However, in order to have a marked effect (and, importantly, to encourage people to save more than the minimum) pension saving will have to be seen as something which is desirable and achievable. One of the downsides of auto-enrolment focussing on the power of inertia may be that it does not have the impact on behaviour that choosing to contribute would have.

52. To counter this possible effect it is vital that communication to those auto-enrolled is well thought-out and timely. Most people will need to be able to recognise the advantages of saving for retirement a long time before those benefits are actually realised.

31 August 2011

Written evidence submitted by Scottish Widows

Scottish Widows welcomes the Committee's inquiry into automatic enrolment into workplace pensions and NEST (National Employment Savings Trust).

We believe the introduction of automatic enrolment and the establishment of NEST is a crucial step in improving the level of retirement provision across the UK population.

We do believe however, that even after the 2012 pension reforms are introduced, further coordinated work will be required to embed a stronger savings culture in the UK.

While not within the remit of this specific inquiry, we would draw the Committee's attention to other initiatives towards improving the savings culture in the UK that we think the Committee would benefit from considering further. In particular, the Retail Distribution Review and the creation of the money advice service are two significant issues that could help. We believe the Committee could carry out further inquiries to assess the success of these, and other initiatives, to deliver a stronger savings landscape alongside the 2012 pensions reform.

The inter-relationships between all these initiatives needs careful consideration to ensure we develop the stronger savings culture required in the UK.

To form our response to this specific inquiry, we have pulled statistics from our annual Scottish Widows UK Pensions Report, a 5000 person survey of attitudes towards pensions, which provides a solid foundation to consider what more can be done to help consumers prepare for a comfortable retirement.

Response to Points Raised under the Terms of Reference of the Inquiry

1. The terms of reference of the inquiry outline a number of issues which the Committee wishes to have further information about. Our response on each of the points is outlined as below.

2. *DWP's communication strategy for introducing auto-enrolment and provision of advice and support to employers and employees*

3. We support the DWP communications strategy for introducing auto-enrolment, as without communications support, there is a very real risk that people will not engage with auto-enrolment at all, and there is a risk that of consumers rejecting the changes when they are introduced.

4. There is uncertainty in many people's minds about whether they should remain in a pension scheme when they are automatically enrolled, and what the cost to them will be. Clear communications explaining the benefits are needed over the next 18 months and beyond, with consistent messages from DWP, The Pensions Regulator, NEST and other pension providers.

5. The success of NEST is integral to pensions reform, and consumers must see it as a high quality, good value, well managed pension scheme and not just as a Government initiative. How it is presented by all stakeholders, but in particular the media, will remain very important. Consumer rejection is something we would not like to see as it would be bad not only for NEST and auto-enrolment, but also the broader industry.

6. *Arrangements for phasing and staging the introduction of auto-enrolment*

7. Over the years we have conducted research into consumer attitudes towards pensions covering a wide range of issues. Over this time we have asked a number of questions about attitudes towards NEST and PADA (Personal Accounts Delivery Authority) before that. We sought to find out what people anticipated doing when they would be automatically enrolled and what amount of money they would be happy to save.

8. Over this time we have consistently found that consumers underestimate how much they will have to contribute following automatic enrolment. The average anticipated contribution this year has risen from £33.90 to £37.50, but is still a significant underestimate of the amount likely to be required, which we believe for an average earner will be around £60 to £70 a month.

9. In light of this, the phasing in period should help ensure those automatically enrolled are more likely to stay enrolled as the contribution they need to make will be closer to their expectations.

10. Education on the level of their contributions required under automatic enrolment will be important to avoid possible withdrawals when consumers see the amounts being deducted from their pay both in the immediate term, but also over the longer term as their contributions will rise.

11. *Likely impact of auto-enrolment on business, especially small and micro-businesses*

12. The effect on small businesses will be proportionally greater than for large companies, but is deferred by the staging and phasing process. Scottish Widows will be launching our workplace pensions report in September 2011, where we analyse the likely outcomes of automatic enrolment for different sizes of company. We will submit a copy of the report to the Committee.[24]

13. What our report shows is that there are differences in attitudes towards pensions provision between small and micro-business community as opposed to medium or large enterprises. However, the vast majority of workers in small and micro employers would like some form of advice or information from their employer as well as the provision of a pension.

14. *Role of The Pensions Regulator, including in certification of schemes*

15. The Pensions Regulator has a key role to play in supporting employers who are implementing automatic enrolment and in monitoring employer activity, particularly where there is any attempt to evade the employer responsibilities. We believe this should be the focus, with self-certification by employers that they are meeting the contribution requirements where pensionable earnings are different from qualifying earnings.

16. *Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted*

17. At this point we can only say that the opt-out rate is uncertain. From our surveys, support for automatic enrolment appears reasonably strong, with only 11% expecting to opt-out, the same as in our survey last year, though a further 21% remain undecided.

18. We understand NEST have carried out similar research, and their figures are not overly dissimilar to what we found.

[24] Information provided, not printed.

19. *NEST's potential market share and the possible effects on other providers*

20. In terms of NESTs market share, NEST is being created to fix an acknowledged market failure of the industry to reach what are generally smaller businesses that the industry currently finds harder to serve. This should lead to a growth in the overall size of the market.

21. While there is no agreed upper limit for the size and scale of a scheme NEST could aim for, the task for the private sector is ultimately to differentiate our proposition from NEST, showing where we can add value to employers through other services.

22. *Whether auto-enrolment is likely to attract new providers and encourage new models of provision*

23. We are encouraged by the clear focus of NEST on those it was set up for and don't see any need for artificial restrictions.

24. That said, we are naturally concerned that one way NEST could try to build scale is by targeting existing provision. This is something we would oppose, and from our discussions with NEST Corporation we regard it as unlikely.

25. *Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers*

26. Our position on contribution caps is that we're happy for these measures to be discontinued in 2017 as is currently planned. The original reasons for establishing the cap largely remain, and we do not support its removal in the short term. Its presence should not inhibit NEST in serving its target market.

27. If the contribution cap were lifted, there is a danger that NEST could destabilise the existing market and that a pension scheme set up with a Government loan could prove detrimental to the commercial market.

28. We believe the best solution concerning transfers is to have complete freedom of movement of pensions money (i.e. into NEST from GPP (Group Personal Pension) and also out of NEST to GPP). In particular, when an individual changes job it is beneficial if their pension can follow them.

29. This means that the consumer can always have the proposition that is best for them through time and they get to see all of their benefits in one place.

30. *NEST's investment strategy*

31. NEST's strategy has been designed to be appropriate for its target group. A similar strategy may not be optimal for the different target groups serviced by the current industry.

32. *Possible measures to reduce the proliferation of small pension pots*

33. We support industry initiatives to improve transfer processes and allow individuals to move their pensions easily when they change employer.

34. *How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications*

35. No comments.

36. *The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement*

37. From our findings we would expect that many people will remain enrolled in pension schemes but will continue to pay the minimum required. The challenge is to achieve a level of consumer engagement where auto-enrolment is seen only as a start, with contributions increasing over time.

20 September 2011

Written evidence submitted by Which?

Executive Summary

Which? supports automatic enrolment to combat the inertia that mitigates against pension saving. We also strongly support the NEST (National Employment Savings Trust) scheme which will be a low-charging scheme and run by trustees with a clear fiduciary duty to act in the best interests of members. NEST will help ensure that competition is used to deliver low charges to its members. Trust in the organisation running the pension scheme was the most important factor for consumers.

It is vital that all schemes used for auto-enrolment are high quality, free from conflicts of interest, offer protection for consumers' assets, have low charges and provide value for money. The level of charges in the pension scheme used for auto-enrolment will have a substantial impact on the final pension received by the employee.

With regard to workplace personal pensions offered by insurance companies we see substantial risk of a regulatory black hole. No regulator or Government department appears to be taking responsibility for ensuring that workplace personal pension schemes provide value for money. There are no requirements for workplace pension schemes used for auto-enrolment to have low charges and deductions. This represents a reduction in consumer protection compared to the current requirements for employers to designate a stakeholder scheme or a group personal pension (GPP) with no transfer penalties. The FSA (Finanical Services Authority) insists that it is not a "price regulator" and has not acted on our concerns about charging structures and levels. There is too much reliance on "disclosure" of information, even though the majority of consumers will struggle to process and act on any information provided.

We are particularly concerned about the increase in charges levied by some insurance companies, for people who change jobs. Which? research has found that some companies are charging 0.5%–0.7% Annual Management Charge (AMC) for active members but once the person leaves then the charges could double to 1.2%–1.5% AMC. As we know that around 60% of people who start contributing to group personal pensions have stopped contributing after four years (mainly due to job changes) a substantial proportion of people will end up paying the higher charges, far exceeding the charges they would be paying in NEST. Such high charges could have a big impact on the pension received by the consumer, potentially seeing their pension reduced by around 25%.

The insurance companies which operate this practice call it an "active member discount" but we believe that a more appropriate name is a "deferred member penalty". Varying annual management charges through the introduction of extra charges for deferred members are basically transfer penalties by the back door, penalising people who regularly switch employers.

We are also concerned by the FSA's proposals to allow employers to negotiate "consultancy charges" with their advisers and for these to be deducted from their employees' pension pots. There is a clear risk that excessive deductions could be negotiated with the employer. The FSA has confirmed that it has no problem with deductions being made which are up to 35% of the first year's group personal pension contributions.

Which? believes that there should either be more highly specified quality requirements, or employers must receive better advice where advisers are required to benchmark the charges against those in NEST to ensure that the workplace personal pension provides good value for money.

During the House of Lords Committee Stage, Lord Freud stated that: "if the research shows that charging levels are creeping up, we have the power under the Pensions Act 2008 to regulate to set a cap for qualifying schemes and auto-enrolment schemes". Our research demonstrates that charges are already high in comparison to NEST so we want to know precisely at what point government will step in?

Which? would like to see a commitment from the minister to clarify the governance and regulation around these issues, and find a solution that is best for employees and supports employers. It is worth noting that the Pensions Commission's Second Report recommended that auto-enrolment into a defined contribution scheme should only be permitted if: "the combined employer and employee contribution exceeds the combined level in the [NEST scheme] taking into account the level of charges".

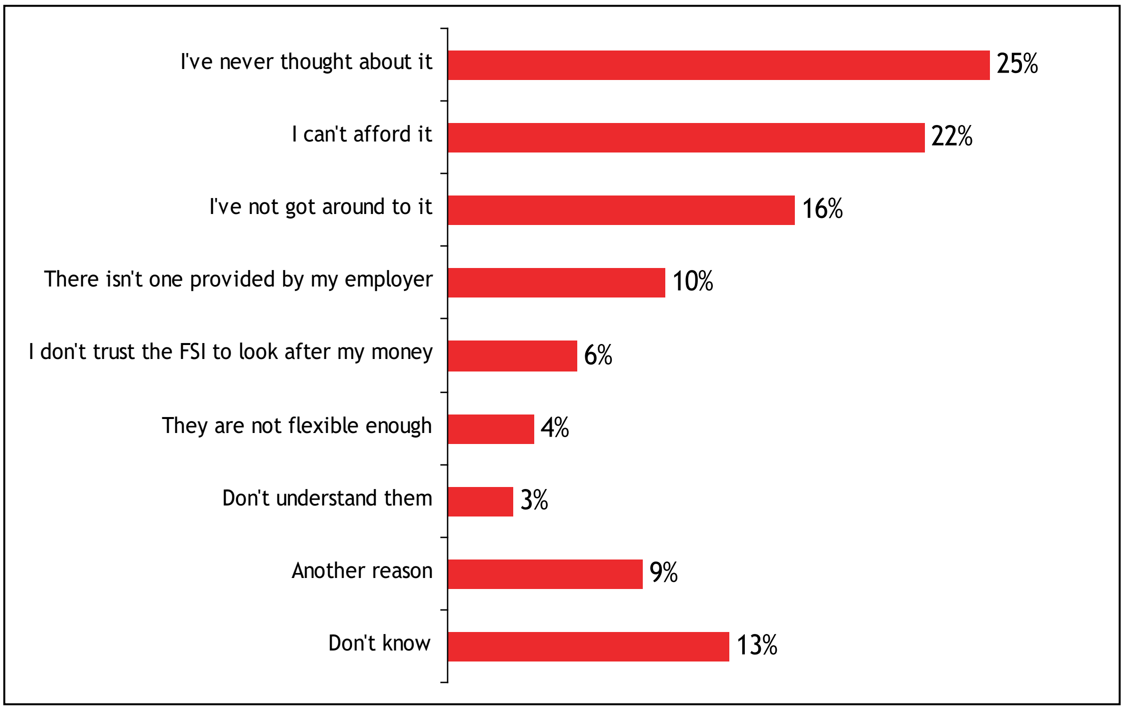
The NEST contribution limit and transfer ban have negative implications for consumers and cap their aspirations for a comfortable retirement. In particular the contribution cap introduces additional hassle for consumers and employers. There are no effective alternatives for consumers who wish to contribute more than the cap and the hassle of finding an alternative pension plan will put people off making proper provision. Consumers and employers need certainty that these restrictions will be lifted in 2017.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

Which? remains committed to the widest possible auto-enrolment system and one in which NEST is a central player. Our research has found that there continues to be a low level of pension saving and retirement planning in the UK. This is particularly the case amongst young and lower socio-economic groups who are the main target of auto-enrolment and are the main likely beneficiaries from joining NEST. Our research also continues to find evidence of significant inertia with regard to saving for retirement. Inertia was the most common reason (39%) for not having a pension in our survey: 25% said they "have never thought about it" (with this increasing to 33% amongst younger respondents: aged 16–44); while 16% said they "haven't got round to it". Affordability is also a barrier, with 22% reporting that they "can't afford it".

Figure 1

MAIN REASON(S) WHY PEOPLE DON'T HAVE A PENSION

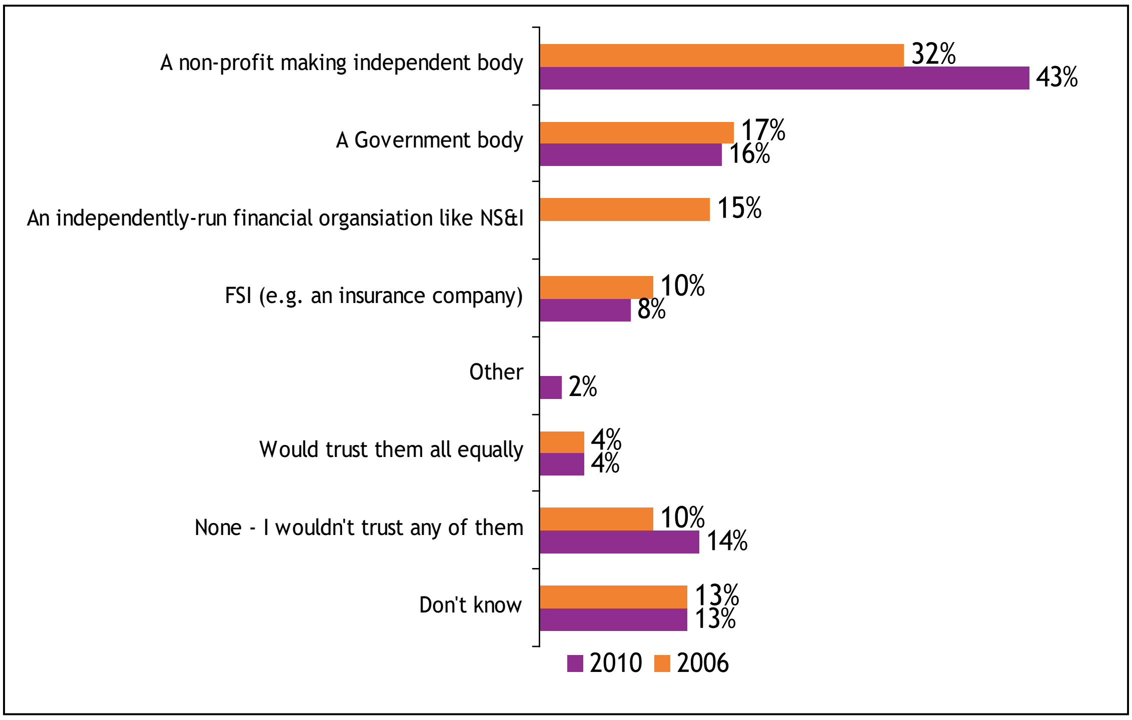


Source: Which? Pensions research July 2010 *Q.4 Below are some reasons other people have given for not having a pension. Which of the following best explains why you do not have a pension? BASE—all adults UK currently working or seeking work without a pension (275)*

Consumers continue to strongly prefer an independent, not-for-profit body to manage any new pension scheme. A non-profit making independent body is most (43%) trusted by consumers to manage a new pension scheme. Only 8% would prefer the financial services industry to manage such a scheme.

Figure 2

ORGANISATIONS MOST TRUSTED TO MANAGE A PERSONAL PENSION ACCOUNT IN MEMBERS' BEST INTERESTS



Source: Which? Pensions research July 2010 and September 2006. *Q.8 And who would you trust the most to manage a Personal Pension Account in your best interests? BASE 2010—all adults UK currently working or seeking work (555) BASE 2006—all UK respondents working/seeking work (528)*

These findings provide strong support for the principle of auto-enrolment to combat the inertia that mitigates against pension saving and for a scheme like NEST to meet the needs of those who are under-provisioned or do not have access to an employer scheme. They also echo the well established concerns about private pension provision and the intuitive preference for a scheme that is managed solely for the benefits of members.

The quality and charges of workplace personal pension schemes

Which? wants to ensure that the scheme into which an employee is automatically enrolled is fit for purpose and high quality. Employers can choose a range of schemes including NEST but there is nothing stopping a disengaged employer choosing an inappropriate pension scheme that is unsuitable for their employees or has excessive charges.

In trust-based occupational schemes such as NEST, trustees have a fiduciary duty to act in their members' best interests and should monitor investment managers, funds and charges as a function of this duty. They would also have a clear duty to prevent any excessive charges or deductions being made from members' investments. However, providers of workplace personal pension schemes such as group personal pensions do not have the same responsibility to their customers. GPPs and other forms of contract-based workplace pension provision such as Group-SIPPs therefore represent a greater risk of consumer detriment. In assessing the risk of consumer detriment we would examine:

— The possible consumer outcome.

— The scope for any conflict of interest/market failure.

— Whether we can rely on competition and market forces alone to deliver good outcomes for consumers.

We have suggested a number of tests that workplace personal pensions including GPPs would need to meet some of which could be incorporated into the "qualifying scheme" test. These include good standards of governance to protect members' interests; appropriate levels of investment choice and a suitable default option; low charges; and no penalties for consumers that stop contributing or transfer their pension.

The objective of the Government's pension reforms are to improve access to affordable, low-cost pension saving. We would be very concerned if weaknesses relating to the structure of GPPs or other contract-based workplace schemes resulted in high charges. Pension charges can have a dramatic effect on the final amount received by the consumer. An increase in the Annual Management Charge from 0.5% a year to 1.5% a year can reduce the final pension received by 20–25%. A male median earner's pension pot would be worth £63,000 if the Annual Management Charge is 1.5% a year, meaning that £24,000 is lost in charges. Under an AMC of 0.5% his pension pot would be worth £78,000 and just £9,000 would be lost in charges.

Which? does not believe that the existing FSA principles or the DWP's default options guidance provide the appropriate degree of consumer protection. It is unrealistic to expect that the FSA principles or the aspirations expressed in the default options guidance alone will provide the proper degree of discipline on providers of GPPs to be "mindful of ensuring that the products they design for this market treat"[25] consumers fairly.

The FSA and the DWP have failed to conduct a proper analysis of the factors which will be driving the market in the run-up to 2012, identify where conflicts of interest are likely to arise, identify how these will be tackled or how regulators will need to respond to the market changes to ensure good outcomes for consumers. The FSA and the DWP are also ignoring the lessons from previous mis-selling scandals. Namely, that one of the best ways to prevent consumer detriment is to set high standards through product regulation.

Default options

We agree that it is likely that the vast majority of individuals being automatically enrolled will end up in the default option and that therefore the charges, design, governance and communication of the default option will be critical in ensuring a good outcome for consumers.

However, we are concerned that the current draft of the DWP's guidance does not contain strong enough protections for consumers. It is also not clear what the status of the guidance is, how compliance will be monitored and what regulatory steps will be taken if providers, advisers and employers fail to comply. For example, we note that the guidance says that the default option should be "competitively priced", but that the FSA's position has consistently been that it is not a price regulator so it is not clear when the FSA would take action to ensure that schemes complied with this requirement. Furthermore, as providing advice to employers is not a regulated activity it is clear that some advisers will not even be regulated by the FSA.

[25] FSA, CP 10/26.

We have several concerns regarding the operation of the market for GPPs and other workplace personal pension schemes:

1. The regulatory black hole which seems to exist between the DWP, FSA and TPR (The Pensions Regulator) for ensuring that workplace personal pension schemes are high quality and low charging.
2. The level and structure of charges made by GPPs and other workplace personal pensions
3. The practice of applying "deferred member penalties"—penalising consumers who switch jobs.
4. The advice/recommendations provided to employers to establish a GPP or other workplace scheme into which consumer's are automatically enrolled.
5. The prevention of excessive or unnecessary deductions made under the pretence of "consultancy charging".
6. The treatment of consumers who are placed in the default option.
7. The degree of investment choice within a GPP or other workplace pension scheme.

In the following paragraphs we have briefly summarised some of the conflicts of interest facing product designers, advisers and employers which could lead to poor outcomes. We also summarise the demand side pressures which could be exerted by employers and employees/consumers.

Product design: Product providers will continue to face incentives to design products which appeal to advisers and employers rather than those which are most appropriate for their employees. This may involve limited market pressure to keep charges low for employees, particularly for ex-employees. It may also involve pressure from employers to design schemes which favour current employees whilst imposing penalties on ex-employees and deferred members.

Before the end of 2012 they will face pressure to increase their share of the market by paying more commission to financial advisers. After 2012 they will face pressure to facilitate the payment of "consultancy charges" from pension schemes. The FSA has stated that these could be up to 35% of the first year's contribution into a pension. As part of the RDR (Retail Distribution Review) the FSA has not placed any regulatory responsibility on product providers to monitor the level of deductions or to determine whether they are reasonable.

Advisers: In the lead up to the end of 2012 and the implementation of the Retail Distribution Review advisers will face incentives to sell schemes paying high and ongoing commission rates so that post the introduction of automatic enrolment enhanced participation rates within these schemes will lead to commission payments to the adviser. They will also face pressure to recycle or churn existing schemes. Following the implementation of the FSA's flawed concept of "consultancy charging", advisers will face commercial pressure to maximise the amount of charges which they are able to deduct from employees pension pots. The system of "consultancy charges" could also bias the recommendations of advisers away from the NEST scheme.

We have previously questioned the validity of the FSA's example that a recommendation to employers to establish a GPP as a qualifying alternative to NEST could be justified merely on the basis that an employer wishes to contribute more than the maximum proposed for NEST. We have concerns that an adviser may justify a recommendation to establish a more expensive GPP than NEST on the grounds that the employer will need to contribute more than the maximum for a small group of employees.

However, a recommendation to an employer to establish a GPP or other workplace personal pension may be given by an adviser not authorised under FSMA (Financial Services and Markets Act). We question what tools the FSA may have at its disposal to ensure high standards of advice or to take action against the adviser. The adviser would not need to have any individual contact with employees, who from 2012 would be automatically enrolled into the GPP. No personal recommendation to employees would be provided and it is difficult to see how the FSA's existing rules or powers provide an appropriate degree of protection for consumers.

Employers: The introduction of automatic enrolment will require a large number of previously unengaged employers to choose a pension scheme for their employees. Unless clearly defined quality requirements are in place then this increases the risk for their employees. The FSA should also recognise that conflicts of interest exist in that employers may place more weight on the interests of their existing employees within the scheme over and above the interests of ex-employees. This means that even where employers are engaged in the choice of scheme this could lead to market pressure on product providers to deliver schemes which penalise ex-employees through the application of additional charges, "deferred member penalties" or other forms of transfer penalty.

Employers will also face little pressure from their employees to limit the scale of "consultancy charges" which they permit advisers to charge to their employees. They will face little financial incentive to pay the advice fees themselves rather than passing them on to their employees through "consultancy charging".

Employees/Consumers: As acknowledged by the Government and the FSA the demand side pressures in the market are weak. Our research suggests that consumers do not understand pensions or pension charges and find it very difficult to identify whether they are getting a good deal. This means that they do not exert meaningful market pressure for improvements. As the DWP has noted: "Consumers on moderate incomes typically do not understand pension products well, find it hard to make comparisons, and rarely switch providers."

Disclosure of charges to GPP members alongside or included in the usual "Key Facts" documents would not be effective in securing good outcomes for consumers. This material would be unlikely to be read or understood by the target market for pension reform. Indeed, automatic enrolment means that once the scheme has been chosen by their employer, consumers will be automatically enrolled in the scheme and if they choose to opt-out they will lose the employer contribution. Therefore the only route available to dissatisfied consumers is to lobby their employer to change the scheme. We believe that in the overwhelming majority of cases this is extremely unlikely to happen. There is a clear risk that if "consultancy charging" is automatically applied to all members of a GPP then consumers risk paying excessive charges.

The persistency of group personal pensions has declined in recent years with almost 40% of consumers having stopped contributing within two years and 60% of consumers having stopped contributing within four years.[26] Due to the frequency of job changes persistency of GPPs is unlikely to increase beyond current levels.

Policy solutions

When Which? and a number of other consumer and industry groups wrote to the European Commission in relation to the application of the Distance Marketing Directive to workplace personal pension schemes the letter said:

> "It is important to ensure savers get a fair deal. The legislation currently being discussed by the UK Parliament gives the UK Government wide powers to establish a quality threshold that can effectively protect consumers. The Government has committed to consult and seek consensus from all the stakeholders, including the Financial Services Authority, about this."

The actions taken so far by the Department for Work and Pensions and the FSA have not, as yet, provided us with the appropriate degree of reassurance. Indeed, the FSA's proposals for "consultancy charging" have arguably made the situation worse for consumers.

Which? believes that the approach of the Government and the FSA will not ensure that contract-based workplace provision delivers appropriate pension provision for consumers.

We believe the following policy solutions should be considered:

— Specified quality requirements for qualifying pension schemes: This should include charging structures and levels, a prohibition on transfer penalties, protection of assets and a requirement to specify an appropriate default fund. We would favour further discussion of the requirements imposed on the product provider/product designer of the GPP or other workplace personal pension schemes. In particular, the FSA should examine applying some of the analysis and policy options from its discussion paper on product intervention to GPPs.

— Making the sale of workplace pension schemes to employers and any advice provided a regulated activity.

— RU64 style rule for employers/advisers. Advisers would have to certify that the workplace personal pension they recommend to an employer would provide at least as good an outcome as NEST. We would welcome discussion with the FSA and the DWP as to what they consider the existing requirements impose on those providing advice to employers about the type of pension scheme to establish to fulfil their employer duty post 2012.

— Required contributions to contract-based schemes to take account of the level of charges: This was a recommendation of the Pensions Commission and would help align the interests of employees and employers for good value pension provision. It would increase the incentives for employers to choose low-charging schemes.

— FSA/DWP and TPR to conduct regular surveys into the level and structures of charges in workplace pensions: This would ensure regular monitoring of the market in the run-up to auto-enrolment and highlight any schemes being sold with high charges.

Role of The Pensions Regulator, including in certification of schemes

The role of The Pensions Regulator in relation to the certification of schemes mainly covers the arrangements for the payment and level of contributions.[27] Providers of contract-based schemes are required to be authorised by the FSA. There are absolutely no requirements imposed by The Pensions Regulator with regard to the charges levied or the deductions made from consumers' pension pots.

We are also concerned about the conflicts of interest which may exist in multi-employer master trust schemes if the trustee is close to or appointed by the provider. The Pensions Regulator and the DWP should also ensure that there is sufficient protection of consumers assets invested in trust-based schemes.

[26] FSA persistency survey 2010, page 27.
[27] http://www.thepensionsregulator.gov.uk/docs/pensions-reform-pension-schemes-v2.pdf

Estimated opt-out rates, including the possible impact on NEST if the numbers auto-enrolled are significantly lower than predicted

Which? research conducted in 2010 shows that inertia is the main barrier to pension saving. Overall, 39% reported an inertia-related reason. One quarter said they "have never thought about it", followed by a further 16% who said "they've never got round to it". We expect that these groups are unlikely to opt-out of NEST or any other pension scheme. A further 10% said that there wasn't an existing pension scheme provided by their employer.

Opt-outs from pension saving are most likely to emerge from the group which gave lack of affordability (22%) as a reason for not saving for a pension. However, the phasing in of contribution rates over several years may lead to a proportion of this group not opting-out.

NEST's potential market share and the possible effects on other providers

It is difficult to estimate the precise share of the market which will be taken by NEST. This will depend on decisions made by other product providers, advisers and employers. The contribution limit placed on NEST means that some employers may need to operate two schemes. They may use NEST for the low-middle income group of employees and a different pension scheme for higher earners who will definitely contribute more than the contribution cap.

We have seen no evidence that the current pensions market has or will meet the needs of the target market, primarily low-middle income groups (other than by levying charges which destroy incentives to save). The evidence points to very few truly new schemes in the Group Personal Pensions market. ABI (Association of British Insurers) statistics demonstrate that the total amount of contributions to GPPs has not increased despite the reported levels of new business. Instead, the reported levels of new business are the result of existing schemes being switched between providers.[28]

Ideally, NEST should act as a spur to other providers to improve their product offerings and reduce their charges. However, unless the Government tackles the regulatory blackhole and the conflicts of interest identified this is unlikely to happen.

Likely impact of the limitations placed on NEST, including the contributions cap and the ban on transfers

We are concerned that the limitations placed on NEST with regard to contribution caps and the ban on transfers will have negative implications for consumers.

The Contribution cap

The auto-enrolment review[29] made a recommendation that the Government should legislate now to remove the annual contribution limit for NEST from 2017. Which? is concerned that this recommendation was not reflected in the Pensions Bill. Contributions to NEST are currently limited to around £4,300 per year (in today's prices), and we believe this cap will provide a disincentive for some people to save for their pension. Which? believes it would be a mistake to restrict people's ability to save or cap their aspirations for a comfortable retirement.

Which? would like to see the cap on contributions to NEST removed. We believe this is necessary for the following reasons:

— *It means people will save more money for their pension*: The NEST Board has a duty to encourage saving above the minimum level of contributions so the cap should be removed to help them achieve this. 70% of people agreed that there should be flexibility about how much can be paid into the NEST scheme.[30]

— *Anyone wanting to make contributions slightly above the annual limit may struggle to find an appropriate pensions vehicle outside of NEST*: One of the reasons for the Pensions Commission's recommendation to establish the scheme was that the pensions industry did not offer cost effective alternatives. Which? research found that 52% of people would be put off saving more by the hassle of finding and opening a separate secondary pension plan.[31]

— *The cap introduces additional complexity for consumers, employers and the NEST scheme*: Significant changes in earnings or one-off additional contributions from consumers could mean that they breach the limit and are required to halt regular contributions for the rest of the year. This creates extra administrative hassle for employers and the NEST scheme.

[28] FSA, CP 09/31, Delivering the Retail distribution review: Professionalism; corporate pensions and applicability of RDR proposals to pure protection advice, page 72–73.

[29] DWP, Making Automatic Enrolment Work, October 2010, page 131.

[30] Which? market research 2007.

[31] Which? market research 2007.

The ban on transfers

Transfers into NEST are currently heavily restricted, and we think that there needs to be consideration of how this can be changed. Employees are changing jobs more frequently than ever before which has led to an increase in multiple small pension's pots. Allowing an employee to transfer pension pots into NEST, especially small pensions pots, encourages better pension savings and takes the burden of administering small pension pots away from the employer and the pension scheme.

Which? would like to see employees allowed to transfer their pension's pots into NEST. We think this will provide a solution to the nations growing collection of small and orphaned pension's pots. Enabling people to consolidate their pension savings into one place would also make it much easier for them to calculate their potential retirement income.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

The Pensions Bill introduces an optional three month waiting period, so an employer can delay an employee's auto-enrolment into a qualifying pension scheme by up to three months. If they do this the employer is required to give the employee a notice. Which? is concerned that situations could arise where an employee has their auto-enrolment deferred more than once. Which? believes that it is important that if an employee reaches the auto-enrolment threshold for two months, but then doesn't for the third month, the next month that they reach the earning threshold they should be automatically enrolled, rather than re-triggering the three month wait. If this change is not made, workers with fluctuating earnings could find that their auto-enrolment is deferred for several separate three-month periods, reducing the provision which they are making for their retirement.

Which? would like to see a limit on the number of deferral notices which may be given to an employee. This would also help prevent consumers who fulfil a number of short-term contracts with the same employer from having their automatic enrolment deferred multiple times.

We are also concerned about the ability of some schemes to offer "short service refunds", returning an employees contributions if they leave the scheme in the first two years. We welcome statements from the Minister that employers should not make "their decision about scheme type on the assumption that short service rules will continue to exist in their current form going forward".[32]

Annex A

Charging Structures and Levels

In relation to the charging structure there will be clear market pressure from product providers to increase the level of charges. Below, we explain in more detail our concerns around the practice of what we believe should be called "deferred member penalties". We believe that these pressures are indicative of a market where even when employers are engaged in the choice of pension scheme the interests of past employees might not be properly considered or protected. We believe that the default options guidance should explicitly prohibit transfer penalties and penalties for members who change employer. It would be perverse if pension providers were able to get around any requirements by euphemistically describing these penalty charges as the withdrawal of an "active member discount".

Active Member Discounts/Deferred Member Penalties

One of the current practices concerning us in workplace personal pensions run by some insurance companies is the practice of increasing charges when people change jobs. This is where, for example, current employees (or "active members") pay an Annual Management Charge (AMC) of 0.5% but past employees (or "deferred members") pay a higher Annual Management Charge of up to 1.5%.

Research commissioned by the DWP found that market pressures were being exerted on pension providers to put forward schemes which penalised employees who moved jobs. For example, one provider said:

> "It is interesting that the market has changed on this. If you want to go back five to 10 years ago, the desire amongst employers was to say, 'We want you to have a good low scheme charge, and if you leave us, you can maintain that.' But increasingly the employers have turned that 180 degrees and they want to be able to say, 'You have a really good deal on your pension plan here, but if you leave, the charges will be higher.' It is acting as a retention rather than a recruitment tool."

As the research noted: "Some providers did allow employers to choose the option of active member discounts to new employees, but pointed out that they adopted the model only as a result of competitive pressure. The providers that offered active member discounts were seen by the reluctant adopters as offering members an even lower, more competitive AMC, meaning that they had to follow suit to remain competitive."

A provider which had been a reluctant adopter of a charging model which penalised deferred members told the researchers that:

[32] http://www.dwp.gov.uk/newsroom/press-releases/2011/jun-2011/dwp071–11.shtml

> "We were pressurised into this, because it was the only way that we could compete in the market. That's the way the market has gone."

It is worth noting that persistency figures for group business indicate that 60%–64% of regular premium group personal pensions sold in recent years ceased to have contributions made to them within four years.[33] For those sold in 2006, around 50% had lapsed within three years. We cannot see any reason to believe that the persistency of group business will increase dramatically in the future. This means that it is highly likely that the majority of employees within a scheme will end up paying the higher "deferred member" charge.

Which? research has found that some companies are charging 0.5–0.7% Annual Management Charge for active members but once the person changes job then the charges could double to a maximum of 1.2%–1.5% AMC. As we know that around 60% of people who start contributing to Group Personal Pensions have stopped contributing after four years (mainly due to job changes) a substantial proportion of people will end up paying the higher charges, far exceeding the charges they would be paying in NEST. Such high charges could have a big impact on the pension received by the consumer, potentially seeing their pension reduced by around 25%.

Company	*Typical Annual Management Charge for Active Members*	*Maximum AMC for Deferred Members*
AEGON	0.75%	Average of 1.35%
Aviva	0.6%	Up to 0.99%
Friends Life	Not disclosed	Up to 1.19%
Scottish Widows	Up to 0.45%	0.9%
Zurich	Up to 0.69%	Up to 1.19%

"Consultancy charges"

We oppose the concept of "consultancy charging" for GPPs. This would reintroduce a conflict of interest between the intermediary and the consumer/employee. We cannot see any justification for consumers to pay what is essentially "commission" to an adviser chosen by their employer. There is no guarantee that an employer would seek to minimise the extent of these charges on employees. This may particularly be the case for those employers who have not previously arranged a pension scheme for their employees and are entering the market for the first time because of the introduction of the employer duty to automatically enrol employees into a qualifying pension scheme from 2012.

It is reasonable to conclude that the use of commission has led to upward pressure on overall costs. The concept of "consultancy charging" would be likely to have a similar effect. DWP research found that GPPs where the intermediary is paid commission are significantly more expensive than where no commission is charged. Annual Management Charges: "typically ranged from 0.4% to 0.6% where the intermediary charged no commission; and from 0.8% to 1.0% where commission was charged."[34] A consumer contributing to a GPP where commission was charged will therefore receive a pension around 10–11% smaller than if they contributed the same amount to NEST or a GPP where no commission is charged. There can be no justification that a rise in charges is necessary to improve access. Indeed, it would be perverse to sanction an increase in charges when affordability is of such a concern to consumers.

We were concerned by the statements made by the FSA in Policy Statement 10/10 which stated that the FSA saw no reason why consultancy charges at levels in the range of 10% to 35% of the first year's GPP contributions could not be deducted.[35] We believe the DWP should explicitly state whether it considers this level of deduction in "consultancy charges" to be reasonable.

6 October 2011

Written evidence submitted by Randstad UK Holding Limited

1. Introduction

We seek to highlight our concerns with specific reference to:

- Arrangements for phasing and staging the introduction of auto-enrolment.
- Likely impact of auto-enrolment on business, especially small and micro-businesses.
- How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications.
- The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement.

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[33] FSA, 2010 Survey of the persistency of Life and Pensions policies.

[34] DWP, Current practices in the workplace personal pension market: Qualitative research with pension providers and intermediaries, July 2009, page 56.

[35] Policy Statement 10/10, Delivering the Retail Distribution Review—corporate pensions, page 12.

By way of introduction, we have included a short paragraph on Randstad and also the UK recruitment industry.

2. Randstad

Randstad is a leading recruitment and HR solutions company in the UK, and part of the world's second largest HR services organisation. In the UK, Randstad has the recruitment industry's most diverse portfolio of specialist companies. Randstad's 12 sectors are: Accounting, Banking and Finance; Construction, Property and Engineering; Education; Interim Management and Search; Health, Social and Domiciliary Care; Human Resources; IT; Legal; Retail; Sales, Marketing and Creative; Staffing; and Managed Services.

Randstad is a trusted adviser to organisations across the private and public sectors, matching their full-time, part-time and temporary talent requirements, and to candidates, providing them with long-term career counsel.

Ninety five per cent of Randstad's business by sales in the UK is fully Randstad branded or co-branded. At the end of 2010, Randstad had 2,040 corporate employees in the UK, working in 289 locations and supplied approximately 25,000 agency workers every week. UK revenue in 2010 was €802.3million.

3. UK Recruitment Industry

With regard to the UK recruitment industry itself, it is estimated that agency workers make up around 4% of the total UK workforce. Randstad is one of the main sponsors of REC (Recruitment and Employment Confederation) research, which has shown that temporary work is a vital source of flexibility within our labour market as well as a valuable stepping-stone for those seeking permanent work. The flexibility of temporary working is an attractive option to both employers and individuals and our research indicates that it is set to increase in coming years. It is therefore imperative that the auto-enrolment of temporary workers into pension schemes does not adversely affect the creation of temporary jobs, especially at this crucial time for the UK economy. This is also particularly important in our industry given the real challenges faced by the recent introduction of the Agency Workers Regulations (AWR).

4. Expected Impact of Automatic Enrolment

Arrangements for phasing and staging the introduction of auto-enrolment

Randstad is very concerned as to the phasing arrangements whereby agency workers will be enrolled by the payroll size of the recruitment business. This will create a significant advantage for smaller recruitment businesses as they are likely to join at a later date. However, the system could also penalise these smaller companies as they are likely to join at an earlier date than other SMEs (Small and Medium-sized Enterprises) given that agency workers will be counted as part of the payroll along with permanent employees.

The position is complicated by the fact that Randstad operates different businesses in the UK and each of these has different legal entities. We have been striving for some time to obtain clear guidance on whether all of our UK entities should join phasing at the same time and we still are receiving different views on this from advisers.

Likely impact of auto-enrolment on business, especially small and micro-businesses

Given the very high turnover of agency workers (the average length of assignment across all our UK businesses is approximately 14 weeks), we do have significant concerns as to the administrative impact of auto-enrolment. Although some of these issues have been alleviated by the introduction of the 12 week qualifying period, many of our concerns still exist.

We would expect many agency workers to view saving for a pension as a low priority, given that many agency workers undertake temporary work as a means of getting back into the workforce or to bridge gaps in their working lives. As such, we would expect to see high opt-out levels amongst agency workers. This, coupled with the high turnover and average length of assignments, is likely to cause high levels of administration with no real benefit for individuals.

How self-employed people, and part-time, temporary, casual and agency staff, will be treated under auto-enrolment; and the equality implications

We are concerned that agency workers, temporary and casual staff could be treated less favourably than permanent workers under auto-enrolment. We believe it possible that some end-users will be far more willing to engage with workers that have opted-out of auto-enrolment, because this will lead to lower costs being passed on to them. This risk is heightened by the fact that the recent introduction of AWR is likely already to be increasing end-user costs. We expect the combined effect of AWR and pensions legislation will be (possibly considerably) detrimental to the UK recruitment industry.

The extent to which auto-enrolment is likely to achieve the desired behavioural change in terms of encouraging people to make provision for retirement

As indicated above, whilst we recognise the need for more workers to save for a pension, this is unlikely to be a high priority for many of our temporary workers. As mentioned, we believe that saving for a pension will be less of a priority for many temporary workers, as they often choose temporary work to help bridge gaps in their working lives for a variety of reasons—whether it is earning extra money whilst studying, or taking temporary work whilst seeking a permanent position. Soundings that we have taken suggest that it is likely that the number of temporary workers choosing to opt-out of the scheme will be considerable. We would suggest that it would have been better, and may be desirable in the future, to abolish any opting-out from auto-enrolment and to force all workers to save for their retirement.

Randstad is committed to working with DWP, NEST (National Employment Savings Trust) and other bodies such as the REC and providers to ensure that the proposed changes to pensions savings result in real benefits to agency workers, and minimal bureaucratic costs on the agency work/recruitment sector.

24 October 2011

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