House of Commons

Work and Pensions Committee

Progress with automatic enrolment and pension reforms: Government and Financial Conduct Authority responses to the Committee's Fourth Report of Session 2014–15

First Special Report of Session 2015–16

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The Work and Pensions Committee

The Work and Pensions Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department for Work and Pensions and its associated public bodies.

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Publications

Committee reports are published on the Committee's website at www.parliament.uk/workpencom and by The Stationery Office by Order of the House.

Committee staff

The current staff of the Committee are Adam Mellows-Facer (Clerk), James Clarke (Committee Specialist), Andrew Wallace (Senior Committee Assistant) and Jessica Bridges-Palmer (Media Officer).

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First Special Report

On 10 March 2015 the previous Work and Pensions Committee published its Fourth Report of Session 2014–15, *Progress with automatic enrolment and pension reforms* (HC 375). On 15 July 2015 we received the Government's Response to the Report. On 6 July 2015 the Committee received a response from the Financial Conduct Authority. The responses are both reproduced as an appendix to this Special Report.

Appendix

Government Response to the Fourth Report of the Work and Pensions Committee, 2014–15

I welcome the fourth report of the Work and Pensions Select Committee (session 2014–2015) on progress with automatic enrolment and pension reforms.

As the Work and Pensions Select Committee will be launching a pension flexibilities inquiry after summer recess, and following the HMT announcement of a consultation on this topic in the autumn, the bulk of the detailed response will be dealt with via this process. The Government is committed to ensuring that individuals have the freedom and choice to access their pension savings in a way that suits them best We understand that some pension providers are still in the process of designing new drawdown products, and we will actively monitor the market as it develops, and hope that a strong and competitive market will emerge.

However, given that these various activities will not begin or report until later this year, we wanted to update you on our progress on automatic enrolment, as well as providing some comment on the Committee's recommendations regarding regulation and the appointment of an independent commission.

We recognise there have been early concerns from consumer and industry groups about the barriers to access. In response to this the Government will launch a consultation later on this month to gather evidence of the issues facing consumers wishing to access their pension savings flexibility. In addition the Financial Conduct Authority and The Pensions Regulator will investigate the issue of exit charges and barriers to transfers, which will inform the Government's thinking on what steps need to be taken to address this.

The scope of the committee's report focussed on the on-going roll out of automatic enrolment, recognising the challenges ahead in supporting 1.3 million small and micro employers. The first small and micro employers met their duties at the beginning of June. Supporting employers to make it as simple as possible to comply is one of my key priorities. I am working closely with DWP officials and staff at The Pensions Regulator, to simplify the language and process for automatic enrolment.

The Regulator is updating the suite of information and tools on its website to make it more straightforward for smaller employers, many of which have little or no experience of pensions, to get automatic enrolment right. Refreshed website content will include information to help employers find a provider including, for the first time, a list of 'master trust' pension schemes open to employers of all sizes, which have been independently audited to prove they are administered to a high standard.

The Pensions Regulator has also carried out extensive research with small employers to create a step-by-step guide to automatic enrolment. Every step of the new guide has been written specifically for smaller employers so that it is easy to follow, making the process as smooth as possible. It covers every task employers will need to carry out, from finding out when their duties come into effect and making initial plans, through to completing a declaration of compliance to confirm that they have met their duties.

The Department and the Regulator continue to receive feedback about the experience of employers. We are learning all the time and we will continue to consider further improvements to support employers, particularly micro employers and those who may need additional help.

We welcome the recommendations made by the committee relating to scheme charges. It is important that schemes used for workplace saving, and particularly for automatic enrolment, deliver good value for money. The coalition Government introduced a cap on charges in the default funds of schemes used for automatic enrolment and introduced new governance requirements for workplace schemes offering money purchase benefits.

These new governance requirements mean that, from April 2015, trustees are required to report on the value delivered by charges and transaction costs in their scheme for the first time. The Government will continue to build on this first phase of transparency. To inform this, in March 2015, DWP and the Financial Conduct Authority published a joint Call for Evidence on 'Transaction Costs Disclosure: Improving Transparency in Workplace Pensions'. This ran until 04 May 2015 and sought views in relation to how transaction costs can be captured and reported in a consistent way and what information should be provided to what audiences.

The Government will consult later this year on proposals for improved transaction costs reporting. This work will also inform a decision in 2017 about whether some or all transaction costs should be included within the charge cap.

We acknowledge other key recommendations made by the committee, such as the case for a single regulator and the creation of an independent Commission; however, it is important to me that we first focus on the successful roll out of automatic enrolment, pension flexibilities and charges, placing the consumer at the heart of what we are trying to achieve. I believe that Government resources will be better used focussing on this at this time.

I am very happy to meet with the Committee in the autumn to discuss this further and the Committee's fourth session report.

I am placing a copy of this letter in the House Library.

The Baroness Altmann C.B.E Minister of State for Work and Pensions

Financial Conduct Authority response to the Fourth Report of the Work and Pensions Committee, 2014–15

Introduction

The Financial Conduct Authority (FCA) welcomes the Work and Pensions Committee's Report on progress with automatic enrolment and pension reforms (the Report) which makes a number of recommendations relating to changes to the pensions landscape and expanding the coverage of private pensions.

The Report makes several recommendations which relate specifically to the FCA. We have set out in this document our initial response to these recommendations, and, where appropriate, we describe our next steps in implementation. Our response also includes some comments on several other sections of the Report which touch on issues of relevance to the FCA.

Auto-enrolment governance and charges

We welcome the Report's positive response to the progress made in ensuring value for money and improving governance in workplace pension schemes, and we agree that ensuring value for money remains a priority, particularly as more individuals are saving and the potential complexity of the retirement product market increases. The FCA has been working closely with the Government and The Pensions Regulator (TPR) to introduce a series of measures to ensure the quality of pension schemes remains high.

One of these measures was the introduction of new rules requiring the providers of workplace personal pension schemes to establish and maintain Independent Governance Committees (IGCs), as requested by the Department of Work and Pensions (DWP). In April, the FCA held an inaugural forum for IGC Chairs, in which we set out our expectations. ICGs will act solely in the interests of scheme members in assessing the value of money of schemes. Our rules give IGCs the power to challenge providers on a 'comply or explain' basis and to escalate any concerns to us.

We are monitoring the impact of IGCs ahead of a review of their overall effectiveness in 2017. We continue to take further steps to ensure scheme quality and value for money, and have done a number of pieces of work in this area, such as introducing rules on charge caps for default funds for firms providing workplace pension schemes for auto-enrolment, and publishing a Call for Evidence on reporting and disclosing information about transaction costs in occupational and workplace pension schemes, in advance of rules that we will consult on in the autumn.

The introduction of auto-enrolment has increased the number of individuals who are saving for pensions, and consequently has both expanded the market and the number of consumers relying on it. This intensifies the already important role of institutional investors, as more workers are dependent on capital markets, and the intermediaries in the investment chain who act on their behalf.

We keep the culture and behaviour of firms and individuals at all stages in the investment chain, from asset management through to sales, at the centre of our work, to ensure that they are complying with the spirit as well as the letter of our rules, and working towards good consumer outcomes.

The FCA does not mandate what the best options are for individual consumers, but we are monitoring the development of the market and we will act where appropriate. We frequently review our rules in this area to ensure that they are robust enough to provide effective consumer protection. In particular, we are currently looking at four key areas which include placing the ABI retirement income code of conduct into our rules, consulting on our retirement risk warnings to ensure that they deliver our desired objectives, ensuring our rules are fit for purpose, particularly for drawdown and Uncrystallised Lump Sums and ensuring any technical changes needed are made.

This work also is likely to identify other areas of our rules which will require further analysis in the coming year. One example we have already identified is the need to review our rules on projections to ensure that they continue to meet consumer needs following the introduction of pension flexibilities.

Legacy pension schemes

The Report comments on the challenges of addressing high charges and poor governance in legacy pension schemes. We agree that there are a number of significant challenges in terms of the costs and charges associated with legacy pension schemes.

The Committee will be aware that, last year, an Independent Project Board (IPB), chaired by Carol Sergeant, conducted an audit of older DC workplace pension schemes where members were deemed at risk of high charges. The IPB recommended that providers take actions to improve outcomes for pension savers, with oversight by IGCs and trustee boards. This is a priority area for IGCs, and the DWP and the FCA are conducting a joint review of industry-wide progress which will report by the end of 2016.

Earlier this year the FCA published a Call for Evidence jointly with the DWP to explore issues including transparency in reporting of information about transaction costs and charges, the role of IGCS and trustees in receiving transaction costs information and how and to whom information should be provided. We are now analysing the evidence and expect to consult on any rule changes later this year.

Protecting savers

We agree with the Committee that the new flexibility in retirement choices will likely have a positive impact on broader attitudes to saving. We also agree that these flexibilities create new risks for savers in making poor decisions.

As part of the Government’s wider pension reforms, the FCA has an ongoing responsibility for maintaining and developing the standards that Designated Guidance Providers (those delivering the Pension Wise service) must meet. Our initial focus has been on readiness, usage and performance. All services were fully available on 6 April. So far, consumer feedback has been positive and there have been no availability issues.

Telephone demand has been close to the Government's original estimates, but face-to-face demand has been much lower; only 10-15 per cent of Citizens Advice capacity has been used. Citizens Advice have developed marketing plans to seek to increase usage and we will monitor the impact following the implementation of these plans. Promotion of these services was restricted during the pre-election period, and now that this is over, we do expect further uptake. However, as part of these estimates we and the Government also expect that a number of people waiting to exercise their pension freedoms will have already decided what to do, and do not wish to take any guidance.

Recognising some of the risks created by the new freedoms, we have introduced rules on retirement risk warnings – referred to in the Report as the "second line of defence" – which require firms involved in the sale of retirement income products to give additional warnings tailored to their customers and to alert them to the availability of Pension Wise. Our initial monitoring of the retirement risks warnings appears to suggest they are working as intended, albeit with a small numbers of customers frustrated by that they are required to listen to them.

The Report recommends that the new Government, and proposed new independent pension commission, **'assess whether the protections for savers that have been put in place so far are adequate, including those aimed at protecting savers from poor treatment by pension providers, as well as from scams and fraud'** (Paragraph 94).

We are aware that the new flexible pension regime increases the risk of investment scam activity, in particular scams that target the over-55 age group by encouraging them to withdraw money from their pension savings. Recently published research from Which?[1] found that a third of over 55s have been contacted about their pensions by companies that could be frauds. Over half said that they thought they would be able to identify a legitimate pension investment and 37% thought they could be tricked into a scam.

We take this risk very seriously, and in April the FCA launched the second phase of our ScamSmart campaign. This is a national media campaign which focuses on alerting consumers to the risk, and to the steps they should take to protect themselves from investment scams. This campaign worked in collaboration with Pension Wise and we have signposted consumers to ScamSmart and Pension Wise advice where appropriate.

The first phase of ScamSmart launched in October 2014, and since then, 100,000 people have visited the dedicated website, with 20% of visitors checking an investment through the Warning List. Evaluation shows our targeting approach is working, with a 67% increase in visits from the retired with resources segment to our scams web content since the campaign started. One particular strength has been our radio advertising which has cut through and resonated with at-risk consumers. One consumer was compelled to write and tell us our adverts had "A simple message without creating over anxiety … I think I am

1 Over third of over 55s hassled by dodgy pensions sales' (Which?, May 2015)

investment savvy but even I benefit from the reminder that these plausible thieves are out there."

We also adapted our "warning list" tool to capture audience experience of pension related scams specifically. According to this intelligence, around 30% of warning list users had been approached by scammers to invest their pension pots .

We also work closely with other organisations, including ActionFraud and The Pension Regulator, to share intelligence on pension liberation and investment scams.

The FCA has committed to undertake a thorough review of the rules in the pension and retirement area starting in summer this year, to ensure that consumer protection is appropriate. We have already begun early work on this including hosting round tables with industry and consumer groups.

Decumulation

We agree with the Committee's view that pension schemes will need to adapt the investment strategies of their default funds to take account of the changes. We also agree that the changes will need time to bed in, and for the broader impact to become apparent.

The Report **'urge[s] the FCA and TPR to monitor the behaviour of schemes closely to ensure action (or inaction) in this area is appropriate and not to the detriment of savers'** (Paragraph 103). We agree with the Committee on the need to remain vigilant, and we continue to use the full range of our available tools – including research, thematic reviews and policy statements – to identify and quantify emerging risks, alongside our powers of supervision and enforcement to mitigate any risks that we identify.

The FCA also monitors the market to track product development, consumer behaviour and outcomes, as well as the take-up of the Pension Wise service. We will take action in relation to this information where we feel that it is necessary to provide further support to consumers, or to remove barriers to competition and value in the market.

With co-operation from four major firms, we are currently undertaking behavioural trials of redesigns of the wake-up packs that consumers receive from pension providers in the run-up to retirement. This builds on our previous work and that undertaken by the Government and industry and will inform any rule changes we think are necessary. We will consult on these within a wider review of rules in this area in summer 2015.

Pensions Dashboard

The Committee agrees with the FCA on the benefits for a service to enable individuals to access consolidated information about their pension saving in one place. The Report recommends that **'the next Government ensures that the regulators prioritise the introduction of a "pensions dashboard", which would ideally include both private and state entitlement, and make its use by providers a mandatory requirement'** (Paragraph 108).

As referenced by the Report, we are continuing to work towards the Pensions Dashboard, which would allow consumers to view all of their lifetime pension savings, including accumulated defined contribution savings and state pension entitlements, in one place. This has had the broad support of a number of stakeholders, including the former Pensions Minister, Steve Webb, as well as industry and consumer representatives. The findings of the FCA's Retirement Income Market Study also support the introduction of a dashboard, although costs and benefits must be clear[2].

Together with DWP, we are currently looking at the various options for infrastructure, models and testing, as well as how best to work with industry to create the dashboard service. We are also now in discussions with the Government on the most effective and efficient way to develop the service.

Regulatory framework

The Report recommends that **'the next Government consider the merits of establishing a single regulator covering the whole remit of pension saving, drawing on detailed analysis of the current regulatory framework carried out by the new independent pension commission which we propose'** (Paragraph 125).

The question of whether or not there should be a single pensions regulator is a matter for government, not the regulators. Nonetheless, the FCA does not accept the Report's description of the FCA's approach to the regulation of pension products, which the Committee suggests lacks focus and expertise. We undertake a wide range of activity including market studies, thematic work and policy, and work with HM Treasury, the DWP, TPR and bodies such as the Pensions Advisory Service and the Money Advice Service. Any attempt to separate the regulation of financial services products will inevitably result in distinctions being drawn at some point in the regulatory landscape and potentially substituting one boundary for another. The FCA continues to regulate broader areas such as investments, and the trend towards increasing use of contract based defined contribution schemes, and other developments such as the lowering of the value of the lifetime allowance, means that increasing numbers of consumers will be looking to a range of long-term savings, not just those in a pensions tax wrapper.

Customers cannot always be expected to have a full understanding or sufficient knowledge of complex products, including pensions, and the associated risks. In such circumstances firms must treat customers fairly and the regulatory framework needs to include safeguards. Nonetheless, consumers must be expected to take some responsibility for their decisions appropriate to their level of financial knowledge and understanding. Our interventions in the pensions space have been targeted to achieve this balance of outcomes – combining better information for consumers (improved wake-up packs, the pensions dashboard), ex-ante protections (the retirement risk warnings), protections designed to improve governance in the interests of consumers (IGCs) and thematic or other supervisory work targeted at potential breaches of our requirements

2 https://www.fca.org.uk/static/documents/market-studies/ms14-03-3.pdf