Title: Consolidation of pensions disclosure of information requirements **IA No:** DWP00024 **Lead department or agency:** Department for Work and Pensions (DWP) **Other departments or agencies:**	**Impact Assessment (IA)** **Date:** 24/09/2012 **Stage:** Consultation **Source of intervention:** Domestic **Type of measure:** Secondary legislation **Contact for enquiries:** Paul Needham

Summary: Intervention and Options

RPC Opinion: GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
£149.3m	£83.0m	-£10.0m	Yes	OUT

What is the problem under consideration? Why is government intervention necessary?

The Department is undertaking a critical assessment of the current legislation, with the overall intention of ensuring that the regulations provide clarity and, where possible, consistency in order to enable schemes to meet their legal obligations in this area. The ultimate aim will be to ensure that the information that pension savers receive from their schemes is relevant, clear and fits with the changing pension landscape and overall workplace pension reform agenda. The £83.0 million of savings to business identified comes from allowing pension providers to meet all their disclosure responsibilities through electronic communications instead of paper-based communications or a mixture of electronic and paper-based as now.

What are the policy objectives and the intended effects?

The purpose of the amendments is threefold:
- In response to earlier consultations, consolidate into one Statutory Instrument (SI) the main sets of regulations which require private pension schemes to disclose information to members (and others);
- To re-visit the policy on Statutory Money Purchase Illustrations (SMPIs), following calls to harmonise the pension projections;
- To align the legislation which allows pension schemes to communicate certain information electronically so that all information to members may be communicated in that manner.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Previous consultations have considered consolidation of the disclosure regulations without harmonisation of the requirements. However, gaps and inconsistencies have been identified within the existing DWP legislation and Financial Services Authority requirements, which can best be resolved by reviewing and streamlining existing legislation. There are also ambiguities around the current electronic communications provisions which require clarification.

Non-regulatory methods are not appropriate in this case as the pensions industry needs the disclosure regulations to provide clarity and certainty on the information that is disclosed to members and others (including SMPI's) along with clear timeframes.

Will the policy be reviewed? It will not be reviewed. **If applicable, set review date:** Month/Year

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes	**< 20** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: .... Date: 17/01/2013

Summary: Analysis & Evidence

Policy Option 1

Description:

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2013	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	**High:** Optional	**Best Estimate:** 149.3

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional	1	Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate	478.1		0.047	**478.3**

Description and scale of key monetised costs by 'main affected groups'

The requirement to provide members with information on when their funds are switched to lower risk investments (known as 'lifestyling') imposes on-going costs of £47,000 a year on average. If providers choose to implement electronic communications for fulfilling their disclosure duties, they will incur estimated set-up costs of £478.1 million.

Other key non-monetised costs by 'main affected groups'

Maximum of 5 lines

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate			74.6	**627.8**

Description and scale of key monetised benefits by 'main affected groups'

Providers switching to electronic communications in order to meet their remaining disclosure requirements will realise annual savings of £74.6 million (£627.8 million present value terms over ten years). These savings arise from no longer having to issue-paper based communications to scheme members.

Other key non-monetised benefits by 'main affected groups'

Pension savers will receive clearer, more relevant information about their pension savings. This will ensure that they have all the information they need about their pension saving and will be crucial in their retirement planning. This fits with the changes in the pension landscape from 2012, when millions of people will be saving in a private pension (largely Defined Contribution arrangements) for the first time.

Key assumptions/sensitivities/risks **Discount rate (%)** 3.5

Data has been difficult to come by in this area and the Department has been reliant on informal estimates from industry of the likely costs and benefits of these proposals. The benefits are sensitive to assumptions on take-up of electronic communications and opt-out rates by members who still wish to receive paper communications. Only large schemes are assumed to move to electronic communications; a 10 per cent opt-out rate is assumed for members who still wish to receive paper communications.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
	Benefits: 48.8			OUT

Evidence Base (for summary sheets)

This impact assessment considers three private pensions policy areas:

- consolidation of the disclosure of information regulations;
- a review of SMPIs; and
- extending the current provisions which allow private pension schemes to communicate electronically with their members and other prescribed individuals (e.g. members' spouses and civil partners).

The majority of the proposed changes are minor and are designed to improve the understanding of the disclosure requirements by private pension schemes. The proposed changes would also improve the communications that members receive as well as allowing the industry to reduce costs with the extension of electronic communications in line with the introduction of automatic enrolment from 2012

The proposed changes are grouped together as they are all aspects of a critical review of legislation rather than separate policy options. The proposed requirement for schemes to notify members when their fund is subject to lifestyling is an essential part of ensuring that members have the information they need.

Disclosure of Information

Issue under consideration

1. Existing DWP legislation requires private pension schemes to disclose prescribed information to members and others (e.g. widows, widowers and civil partners). The main disclosure requirements are contained within three different sets of regulations. These are:
    - The Personal Pension Schemes (Disclosure of Information) Regulations 1987 (SI number 1987 / 1110);
    - The Occupational Pension Schemes (Disclosure of Information) Regulations 1996 (SI number 1996 / 1655); and
    - Regulations 18 – 18E of The Stakeholder Pension Schemes Regulations 2000 (SI number 2000 / 1403).

2. The legislation on disclosure has evolved over a number of years, and there are now numerous discrepancies and gaps between occupational and personal pension schemes. There are sound policy reasons for some of the discrepancies and gaps, but where this is not the case, it is proposed to bring the provisions into line, in order to simplify and streamline the regulations, making it easier for pension schemes and providers to administer.

3. As well as the disclosure of information legislation, the Financial Service Authority (FSA) also provides Conduct of Business rules (COBS) which contain disclosure provisions for personal pension providers. The existing disclosure of information legislation has been mapped against the FSA rules and various areas of inconsistency and duplication have been identified. It is proposed to introduce consistency, where possible, in these areas and remove regulation duplication.

4. The existing disclosure regulations are difficult to negotiate in parts and scheme trustees, administrators and managers may currently need to send different pieces of information at different times, which means that keeping track of the information to be disclosed can be onerous.

5. With the introduction of automatic enrolment, more individuals will be enrolled into a workplace pension than ever before, and many are likely to be a member of more than one scheme throughout their working lives. The discrepancies in the current legislation mean that they may well find the information they receive confusing and unhelpful.

Rationale for Intervention

6. In March 2009, DWP consulted[1] on various amendments to existing disclosure regulations. This included the consolidation of general disclosure provisions into one set of regulations rather than occupational, personal and stakeholder schemes being dealt with separately as in the existing provision.

7. Many respondents to the consultation favoured the proposal to consolidate. It was considered that consolidation would make the regulations clearer and easier to follow and that the regulations should be significantly restructured and simplified, making it clear to schemes exactly what is required to be disclosed and when.

8. The majority of responses called for not only consolidation but also harmonisation of the disclosure regulations in order to remove the disparities. This would ensure that the information provided was, where possible, consistent across the different scheme types and also that the timescales in which the information needs to be provided was aligned. It was also suggested that it would be helpful to consider the FSA's COBS to remove any duplication of requirements.

Policy objectives

9. In light of the consultation responses, DWP have undertaken a critical review of the legislation with the intention of consolidating the existing DWP Disclosure legislation also taking account of the FSA COBS.

10. The overall aims of the consolidation are to ensure that regulations:
    - provide clarity and consistency to schemes;
    - provide for inclusion of information that individuals need in order to understand and manage their pension provision and maximise engagement; and
    - fit with the changing pension landscape and overall workplace pension reform agenda.

Description of amendments

11. The proposed changes to the disclosure of information regulations fall into three broad categories:
    I. Minor changes to ensure that a consolidated set of regulations is clearer and easier to use; this includes ensuring that the terminology used is consistent throughout e.g. existing regulations require schemes to 'give', 'furnish', 'send' or 'provide' information to members which can cause confusion.
    II. Timescales: where possible, the timescales for disclosing information should be harmonised between all schemes. The majority of these proposed changes would not require schemes to provide information sooner or within shorter periods than currently and therefore would not require schemes to make any changes to existing procedures unless they wish to.
    III. Information to be disclosed: where possible, the information required should be harmonised between schemes, and where duplication exists between DWP regulations and FSA requirements, regulations will be revoked. The current requirements have been reviewed to ensure that members are provided with the information that they need; at the time they need it.

12. The proposed changes mentioned in item I above are designed to reduce the burden on schemes by making the regulations clearer and easier to understand. It is anticipated that this would reduce the time and effort scheme administrators and lawyers spend on interpreting the regulations. It would also improve member outcomes by providing them with the information that they need at the right time.

13. Item II, which includes harmonisation of timescales for personal and occupational schemes where possible, would improve member outcomes by providing them with the information that they need at the right time. Where it is proposed that the timescales should be extended, it would be for schemes to choose whether, and if so when, to make the changes.

[1] Review of Disclosure of Information Requirements applying to Occupational, Personal & Stakeholder Pension Schemes. Public Consultation March 2009 - http://www.dwp.gov.uk/docs/pen-scheme-disclosure-reqts-consultation.pdf

14. Under item III, a gap has been identified in the current disclosure regulations where members would benefit from additional information. Where members of stakeholder pension schemes have not made a choice about how their pension savings are invested, the scheme is required not only to subject members' rights to lifestyling, but also to notify members of this. (Schemes which operate lifestyling usually begin to move members' investments to less risky funds such as bonds or cash at around 5 – 10 years before retirement, to ensure that any large fluctuations in the investment markets have less impact on older members – as they have less time to recoup any large reductions in investment returns. "Target date funds", would also be included under this provision – they are similar to traditional lifestyling, but instead of switching an *individual's* savings to lower risk funds, the switch occurs at the level of the fund that corresponds to the individual's expected retirement date).

15. Although the existing regulatory requirements apply only to stakeholder pension schemes, other money purchase schemes *may* use lifestyling on a voluntary basis and notify members of this. The draft regulations include a *requirement* for pension schemes which use lifestyling to notify members that their pension savings will become subjected to lifestyling, in advance of the lifestyling taking effect. The impact of lifestyling on members' savings can be considerable. It will be important for individuals to be aware that their funds are being managed in this way, particularly as there is no longer an accepted standard retirement age. Although this is an additional requirement on schemes, there is flexibility around the timing and methods for informing members. This information could be sent with other communications which schemes already send – such as the SMPIs within the year preceding the lifestyling arrangement being commenced. See paragraph 53 for further details.

16. Under item III, there are also discrepancies between the information that must be disclosed to members of personal and occupational schemes. For example, schemes are currently required to provide detailed information on transfers out as part of the information which is given to members when they join a scheme, but the exact requirements differ according to scheme type. In order to streamline, harmonise and simplify the regulations, it is proposed that the basic scheme information should notify members when they join a scheme that transfers out of the scheme are available, and that detailed information is available on request. Additionally, the intention is to remove duplication between DWP regulations on disclosure of information for Personal Pension Schemes and FSA disclosure requirements for Personal Pensions.

Statutory Money Purchase Illustrations (SMPIs)

Issue under consideration

17. In 2003, SMPIs were introduced for all money purchase pension schemes. The policy intention was to provide members with a projection of the value of their pension savings at retirement on a broadly consistent basis across all schemes and members.

18. The SMPI is part of an annual statement which provides personalised information to members about their pension fund, for example, the contributions made in the past year. Figures are given in today's prices so that members can make effective decisions about the spending power of their projected pension and whether they need to save more for their retirement. Schemes are required to use standardised assumptions for the SMPI, e.g. that a member will purchase a joint life, index-linked annuity.

19. SMPI legislation is supported by actuarial guidance - Technical Memorandum 1 (TM1), owned and published by the Financial Reporting Council Limited (FRC) (Formerly the Board for Actuarial Standards (BAS)). This provides schemes with a detailed methodology for calculating the future value of the pension fund. TM1 is used by all money purchase schemes to ensure a standardised and consistent approach to pension projections. TM1 also includes appropriate rates on assumptions used in the calculation.

20. Responses to the latest consultation by the FRC on product projections indicated that in principle there is an overarching desire to keep point of sale and annual projections consistent where appropriate.

21. The FSA requires providers to provide personal pension projections at the point of sale. These projections differ from SMPIs in that they:
    - allow schemes to customise the assumptions to members' individual circumstances.
    - specify three growth rates (whereas the SMPI uses a single rate),
    - allow for schemes to provide a projection which includes a pension commencement lump sum (currently not included within TM1)
    - are not calculated using today's prices.

Rationale for Intervention

22. The differences between the FSA point of sale projections and SMPIs mean that a person taking out a personal pension is likely to receive conflicting information in the point of sale projection compared to the SMPI they will receive within the following year. This can cause confusion to members receiving their first statement and seeing a vastly different outline of what their pension might be at retirement. Although the FSA have consulted on a move to inflation adjusted projections, this will still leave a number of inconsistencies between FSA requirements and the TM1 which DWP would like to address.

23. In 2010, the BAS consulted on the effectiveness of SMPIs. Responses suggested that the aim of providing consistent illustrations had been met but that scheme members don't engage with the SMPI or use the information it contains to make decisions about saving for their retirement. It was suggested that SMPIs are too long, contains too many caveats and that members don't understand them.

24. Additionally, with the introduction of automatic enrolment, there are many people who will be saving in a pension for the first time. It is important to ensure that the SMPI is appropriate for this new cohort of savers as well as existing scheme members and provides them with information that they need to make appropriate retirement provision.

25. Current regulations are prescriptive in the information that must be provided to pension scheme members. This is because the original policy intent was to ensure consistency for members in the type of illustration they received, regardless of the scheme type to allow comparison between schemes. However, due to the BAS consultation responses, informal stakeholder engagement and consumer research findings, along with the FSA offering more customised pension projections, it is believed that this level of prescription is no longer in the best interest of members.

26. One reason for the assumptions specified in the regulations (that members would purchase an index-linked, joint life annuity at retirement) was due to contracted out schemes being required to provide survivors' benefits. With the removal of contracting out for money purchase schemes from April 2012, this is no longer necessary. Most individuals currently take a single life, flat rate annuity with a tax free lump sum, and therefore the current illustrations are not meaningful to many members and in some cases can be unhelpful and off-putting.

Policy objectives;

27. The policy objectives are the same as those mentioned in paragraph 10 above, with the additional aims of:

    - ensuring that legislation for SMPIs is fit for purpose for both the current members of pension schemes and also new members of pension schemes post 2012;
    - harmonisation with FSA point of sale projections;
    - ultimately improving member engagement and understanding of the annual information.

Description of Amendments

28. The proposed changes to SMPI legislation are designed to move away from standardised projections, towards more meaningful projections that relate to what the member can actually receive at the point of retirement and which can be tailored to the individual member. It is expected this would increase member engagement by giving a better indication of what their retirement benefits might be. It is also consistent with the FRC's approach for providers to use justifiable assumptions that take account of the nature of their members' investments rather than using standard numbers.

29. It is therefore proposed to remove the specific requirements for annuity assumptions from legislation. This deregulatory approach would allow schemes to choose the most appropriate assumptions for members based on their knowledge of members' individual situations or for schemes to encourage members to choose their own assumptions should they wish to do so. Whilst it would be preferable for members themselves to make this choice, it is recognised that due to current low levels of engagement, many members are unlikely to do so, at least in the short term.

30. These proposed amendments would mean that whilst schemes can continue with current illustration structures if they choose to do so, they would also have more choice in the assumptions that are used and can change these should they wish. TM1 would continue to supply the rates and guidance needed by schemes to provide these illustrations. This approach would also have the added benefit of bringing regulations closer into line with the requirements set out by the FSA for point of sale projections.

31. This would give schemes more flexibility in designing SMPIs and whilst there would be costs involved in making these changes, for example with updating computer systems, in the longer term greater member engagement may lead to increased pension saving, which ultimately benefits pension providers as well.

32. Should schemes choose to make changes to SMPI assumptions, they would be required to communicate these changes to members. This could be included as part of the new statement and therefore shouldn't incur any significant costs on top of the changes they have already decided to make.

33. Schemes also have the option of providing real-time statements (i.e. a statement that is updated more than once a year). Current regulations require that schemes provide a notification each time the statement is updated. This is not the policy intention with real-time statements and therefore this will be amended so that a notification is only required once in a 12 month period.

Electronic Communications

Issue under consideration

34. In December 2010, DWP amended the three main sets of disclosure regulations to allow pension schemes to communicate electronically[2] with their members and others (e.g. spouses and civil partners). The provisions enabled schemes to provide information on a website and provided clarity about the use of e-mail, including safeguards for those receiving communications in this way. These changes applied to some, but not all, matters disclosed by occupational, personal and stakeholder pension schemes.

35. The 2010 amendments allow schemes to communicate electronically with recipients of the information unless they have opted not to receive information in this manner. So paper based communications are still available to those who prefer this method. The changes are permissive, in that schemes do not have to send information electronically, but can do so should they wish subject to member agreement.

36. Since introducing the December 2010 amendments, the Department has identified 12 additional statutory instruments (SIs) which include requirements to disclose information to members and others. Together the 12 SIs require schemes to disclose around 44 pieces of information. The information covers very diverse situations, which may occur at different times over the course of a member's lifetime and will vary in frequency. For example the information may need to be disclosed:

- *To specific members, as and when required.* For example, different sets of regulations require differing information to be disclosed when a member leaves a scheme before retirement age - depending on whether members opt to preserve their rights in the existing scheme or transfer them to another scheme. The information is disclosed at different times - information about rights

[2] The Occupational, Personal and Stakeholder Pension Schemes (Disclosure of Information) (Amendment) Regulations 2010 (SI 2010 / 2659)

and options is disclosed initially, and additional information is disclosed at various stages, depending on whether the member chooses to preserve or transfer their rights. With the introduction of automatic enrolment and increased mobility of workers, the need to provide information regarding preservation and transfers is likely to increase.
- *To all members, at a specific time of the scheme's lifecycle.* When schemes are wound up, information is disclosed to members (and beneficiaries too, on occasions) at prescribed times during that process. When this occurs, information will need to be disclosed to all members. Depending on the size of the scheme, large numbers of people may be involved.
- *To a small number of members, infrequently, but with a high volume of information.* Information needs to be disclosed on various occasions the member's pension is being shared on divorce. This includes information relating to the pension's value, details of the transfer process and details of charges to be deducted. In these circumstances, although the disclosure relates only to one person, the volume of information to be disclosed may be high.

37. The additional 12 SIs identified specify that the prescribed information can be disclosed:
    - by post i.e. to the recipients last known postal address; or
    - 'in writing' (to include information sent through emails and not via a website).

    This would mean that schemes wishing to adopt electronic communications could send some, but not all information, electronically.

<u>Rationale for Intervention</u>

38. Responses to a DWP consultation in March 2010 supported the December 2010 amendments which allow schemes to disclose information electronically. Many responses also called for the widening of this provision to include additional regulations on specific issues which also contain a disclosure element.

39. Extending the existing electronic communications provisions to cover instances where pension schemes are required to disclose particular information to members and others which can currently only be sent by post, and to remove doubt about whether email or websites may be used, is likely to increase the take up of electronic communications by pension schemes – this is because they will be able to send all information to members and others electronically, rather than having to send some items by post.

<u>Description of proposed amendments</u>

40. The proposed amendments to these regulations provide clarity about how schemes may communicate electronically and are permissive. Schemes would have the option to send information electronically, e.g. via email, or through a website, should they choose. Whilst some schemes may have this technology already in place, other schemes will not have the functionality. Set-up costs may be incurred for schemes choosing to take up this communication method but as there is no requirement for schemes to do so, it is entirely at the discretion of the scheme.

41. For those schemes which currently don't use electronic communications, these amendments would allow them to reduce the amount of paper based communication and any costs involved with this as well as increasing efficiency in communicating with their members.

<u>Costs and benefits of the proposals</u>

42. Although a number of changes are being proposed, not all of them will involve any monetised costs or benefits. In particular, it is expected that the following changes will not yield any monetised costs or benefits:

    - Reducing the volume of information that must be sent to new members.
    - Removal of prescription over assumptions used in SMPI calculations.
    - Removal of duplication between DWP and FSA disclosure requirements

43. The pensions industry has confirmed that the removal of the requirement to provide scheme members with information relating to transfers out and additional voluntary contributions (AVCs) will not yield any financial benefit. Member communications are created on IT platforms. Changing the parameters in an IT system already in place is straightforward – typically it is simply a matter of going into a computer screen and adjusting one or several parameters at the same time. It is therefore trivial to remove generic pieces of information and the monetary benefits to the provider of no longer providing this information are therefore nil. Members benefit from this to the extent that the information they receive is simpler and more relevant to them.

44. Nor does the proposal to remove prescription on assumptions used in SMPIs impose any costs or provide any benefits to providers, who are free to continue with the existing assumptions or change them as they see fit. If they do wish to change assumptions then some actuarial costs will be incurred. Any benefit in terms of different assumptions will be for members, who may receive illustrations that could be better suited to their specific circumstances. This could result in increased member engagement and possibly greater levels of pension saving.

45. With regards to the proposal to restrict notifications of real-time statement updates, there may be additional benefits in terms of savings on notifications, however at this stage the value of any benefits and likely take-up of such an option is not known. It is also worth emphasising the voluntary nature of real-time statements – these are not being imposed.

46. In addition to the changes that do not have quantifiable costs and benefits, there are two changes being proposed which yield monetary costs and benefits. These relate to:

    - requiring schemes to inform members when their funds are about to be lifestyled; and
    - extending the ability of providers to use electronic communications to discharge their disclosure responsibilities.

    These are discussed in more detail below.

Additional information requirements relating to lifestyling

47. The benefits of the additional information requirements accrue to members. Disclosure of these pieces of information will help individuals to engage with their pension saving and will be crucial in aiding individuals with their retirement planning.

48. Although there is no specific evidence to show that provision of additional information on the timing of lifestyling will increase member engagement, DWP research[3] does indicate that supplementary information requirements can increase confidence on the part of individuals in the decisions they make with regard to their pension saving. Even if this information is not always read, individuals feel that its provision can demonstrate a transparent and trustworthy process. So it is clear that individuals ascribe some positive benefit to this kind of information.

49. Information on the timing of lifestyling will allow individuals to assess whether lifestyling is indeed the best option for them at that point in time; or whether they should either continue to have their pension savings invested in the same way as previously or switch to another investment strategy at that point, given their circumstances and retirement objectives. It will also allow individuals to take account of prevailing conditions in the financial markets just prior to lifestyling – this could help avoid the problem of members who see a fall in the value of their fund just prior to lifestyling, which then gets 'locked-in' as funds are shifted into less volatile, but lower-returning asset classes.

50. The costs of providing this information fall on the pension scheme. The actual information requirements themselves are straightforward and generic and require no complex communications on the part of the scheme. As such, the industry has informed the Department that the costs of the information itself are minimal; and that the costs, such as they are, of providing this information arise

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[3] 'The information people may require to support their decision to remain in, or opt out of, a workplace pension' DWP research report 540, 2008. Available to download from http://statistics.dwp.gov.uk/asd/asd5/rports2007-2008/rrep540.pdf

through having to send a paper-based communication to members informing them that they are about to be lifestyled.

51. Pension providers state that there would be a £1 per member cost of informing members they are about to be lifestyled. In this impact assessment, this is simply multiplied by the affected membership in order to generate the annual costs of providing these communications. In future years, this £1 per member cost has been adjusted for inflation.

52. Since members lifestyle only once, this piece of information need be communicated only once. So in any given year, the cost needs to be applied only in respect of those members who will begin lifestyling in that year.

53. Not all scheme members are in lifestyled funds and an adjustment has been made for this. The 2010 National Association of Pension Funds annual survey found that 91 per cent of defined contribution schemes offered a default fund and 79 per cent of these funds were lifestyled. Membership figures have been adjusted for this.

54. Multiplying affected membership (based on DWP estimates of future pension membership) by the per-member cost of this information requirement yields the following annual profile of costs, whose annual average is £47,000 (2012/13 prices) and present value over a ten year period is -£431,000:

Table 1: Annual costs of disclosing information on lifestyling, £ thousands, 2012/13 prices

2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
210	30	30	30	30	30	30	30	30	30

Source: DWP estimates

55. Note that in 2013, when these proposed regulations are proposed for introduction, it is assumed that all affected members will receive such a communication; in future years, once schemes have the option of using electronic communications to discharge their disclosure requirements (see below) it is assumed that only those schemes with less than 10,000 members will continue to use paper-based communications (on the grounds that the fixed set-up costs of electronic communications outweigh the benefits for smaller schemes – again, see below). This leads to a significant reduction in costs from 2014 onwards.

Electronic Communications

56. Under this proposal, pension providers will have the option of discharging their additional disclosure requirements to members through electronic, rather than paper-based, methods of communications. This would yield a monetary benefit for the scheme in terms of the saving made on no longer having to print and post multiple paper-based communications to scheme members. As indicated in paragraph 36 not all communications are sent each year, and not all members necessarily receive each communication, industry sources estimate the annual per member saving (i.e. benefit) as being in the range £0.50 - £4. For the purposes of calculating an estimate of the benefits of moving to electronic communications, this impact assessment takes the mid-point of this range – £2.25 – as the annual per-member saving realised by the pension provider. In future years this per member saving has been adjusted for inflation.

57. Any providers wishing to use electronic communications will incur one-off set-up costs in creating a secure electronic communications system. Industry sources have informed the Department that the estimated cost of this could be in the range £600,000 - £800,000 per scheme and is invariant to the size of the scheme. For the purposes of calculating an estimate of the costs of electronic communications, this impact assessment takes the mid-point of this range – £700,000 – as the per scheme cost.

58. Given the size of this one-off implementation cost, and the fact that it is invariant to scheme size, since the decision to move to electronic communications is a voluntary one, it is reasonable to assume that only large schemes would take advantage of the ability to move to electronic communications for disclosure. For smaller schemes, the benefits will be outweighed by the costs. Schemes/providers in both the public and private sectors will be able to take advantage. This impact assessment assumes that only those schemes with 10,000 or more members will make the move to

electronic communications. The Department believes that this may be a conservative estimate of take-up by pension schemes - many smaller schemes are administered by providers who achieve economies of scale by providing a similar service for a number of schemes. Excluding all schemes with less than 10,000 members might therefore underestimate the number of schemes that would use this provision – however, in the absence of firm data the Department feels it is better to simply note this point and err on the side of caution in the estimates.

59. Multiplying the number of providers/schemes by the estimated per scheme set-up cost and multiplying the affected membership (based on DWP estimates of future pension membership) by the estimated per member saving from electronic communications yields the following annual profile of costs and benefits:

Table 2: Annual costs and benefits of moving to e-communications, £ million, 2012/13 prices

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Costs	478.1	0	0	0	0	0	0	0	0	0
Benefits	0	73.6	77.1	81.5	85.1	85.1	85.1	86.1	86.1	86.1

Source: DWP estimates

60. The annual average of these benefits is £74.6 million (2012/13 prices) while the present value over a ten-year period is £627.8 million; the net present value (benefits net of costs) is £149.7 million.

61. Members will be no worse-off as a result of this change because they will have the right to request continued use of paper-based communications if they so choose; so any scheme members who are unable to access electronically provided information will not be adversely affected by the change.

Risks and assumptions

62. There is no published data on costs and benefits in the areas dealt with by these proposals. In developing the evidence base for these proposals, the Department has been reliant upon informal discussions with the industry on the likely costs and benefits and it is acknowledged that some of the estimates and assumptions will not be as robust as if other sources of data, such as comprehensive industry surveys were available. As there is a strong reliance on information obtained from informal consultation, the Department welcomes any consultation responses about whether any or all of its assumptions and estimates are reasonable and accurately reflect the costs and benefits of the proposals.

63. As described above, using information provided directly by the industry, the IA makes different assumptions about the per-member costs of providing information on lifestyling and the per-member benefits of moving to electronic communications – in particular that the per-member cost (£1) of the lifestyling requirement is less than the per-member benefit (£2.25) from moving to electronic communications. This difference would be expected as a single disclosure (for lifestyling – see paragraph 51), should cost less than multiple paper-based disclosures. Since electronic communications allow for multiple disclosures to be made electronically, assuming that the per-member benefit is greater than the per-member cost of a single disclosure is justified – and this is confirmed by the pensions industry through the estimates on per-member costs and benefits that it has provided.

64. One further issue relates to opt-outs from receiving electronic communications. As discussed above, members will retain the option to request paper-based communications from their pension provider. This is designed to protect those members without the ability to access electronic communications. No data exists on the numbers likely to opt-out in such a fashion, so as a central assumption the estimates assume a 10 per cent opt-out rate from electronic communications i.e. 10 per cent of the affected membership chooses to receive paper-based communications instead. The Department will seek data on possible opt-out rates during the consultation on the proposals, such that the estimates can be refined.

Direct costs and benefits to business (One-in, Two-out impact)

65. The present value of the costs to *private sector*[4] pension providers from this proposal is calculated to be £323.2 million for the purposes of One-In-Two-Out calculations; the present value of the benefits is calculated as being £406.2 million. The net present value is simply the difference between the benefits and costs, so £83.0 million. In line with the One-In-Two-Out methodology, these figures are derived by taking the private sector cash costs and benefits which underlie the figures in tables 1 and 2 above, deflating them to 2009 price terms using the GDP deflator series[5] calculated by HM Treasury, and then calculating the present value – using 2010 as the base year – of this deflated series of cash flows using a real discount rate of 3.5%.

66. On a One-In-Two-Out methodology the Equivalent Annual Net Cost to Business (EACNB) is calculated to be -£10.0 million (i.e. an annual net benefit of £10.0 million). This is calculated over a 10 year period**.**

67. Note that of the £323.2 million present value cost to business, only £0.36 million is directly imposed as a result of the requirement to inform members that they are about to start lifestyling. The remainder of the costs (£322.84 million) arise from the setting up of electronic communications – this is an entirely voluntary endeavour and providers will only incur this cost if it is felt that the cost is outweighed by the benefit of doing so.

<u>Micro-businesses not exempted</u>

68. These proposals apply to all sizes of business and micro-businesses are not exempted. However, in practice, micro-businesses will not be involved in the administration of pension schemes. For occupational schemes, pension scheme administration (which includes the provision of communications) will be contracted out to large third-party providers upon whom the impacts of these proposals would fall.

<u>Wider impacts</u>

69. This review is intended to allow schemes to provide simpler communications and information to their members. They will have more flexibility around sending the information as well determining which information should be sent. Clearer and more consistent information for members is likely to remove barriers to member engagement with pensions.

70. Consistency with the FSA point of sale projections should make SMPI communications easier and clearer for both industry and pension scheme members.

71. The simplifications outlined in this Impact Assessment form part of the Red Tape Challenge (RTC) agenda and take into account responses from stakeholders to the RTC spotlight on pensions.

<u>Summary and preferred option with description of implementation plan.</u>

72. The consolidation of the disclosure of information requirements would provide schemes with a clearer, more consistent set of regulations which would make communicating with their members easier. The main changes are:
    - Reducing the volume of information that must be sent to new members, and;
    - Introducing a requirement for schemes to disclose information on lifestyling.

73. The SMPI changes are ultimately designed to help improve member engagement with their annual information and help with retirement planning, these include:
    - Removing the current prescription around the specific annuity assumptions schemes must use when calculating an annual projection;
    - Where schemes choose to make a change to their annuity assumptions, the new SMPI would include notification to the member of the change in assumptions since their last SMPI; and

[4] Public sector pension schemes are out of scope for one-in, one-out purposes and have therefore been stripped out of the present value calculations.
[5] GDP Deflator series. Available from HM Treasury at http://www.hm-treasury.gov.uk/data_gdp_fig.htm

- Where schemes provide for real-time statements they will not need to provide a notification to the member each time the statement is updated. Only one notification will be required each year.

74. Following the 2010 amendments to allow schemes to communicate electronically with their members, additional disclosure requirements contained within specific pension regulations have been identified. The current electronic communication provisions would be extended to clarify that schemes can fulfil their disclosure requirements electronically, including by providing information on a website should they wish to do so, subject to members being able to opt out.

75. The proposed changes would be introduced by secondary legislation by October 2013.