

PENSIONS

THE USE OF DEFAULT OPTIONS IN WORKPLACE PERSONAL PENSIONS AND THE USE OF GROUP SELF INVESTED PERSONAL PENSIONS FOR AUTOMATIC ENROLMENT

GOVERNMENT RESPONSE TO THE CONSULTATION

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DWP Department for
Work and Pensions

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SECTION 1: INTRODUCTION

1. On 24th September 2009 we published draft guidance on 'The use of Default Options in Workplace Personal Pensions and the use of Group Self Invested Personal Pensions for Automatic Enrolment'. This consultation closed on 17th December 2009.
2. The draft guidance covers the use of default options in workplace personal pensions (WPPs) used for automatic enrolment and the use of group self invested personal pensions (SIPPs) for automatic enrolment.
3. We received 32 formal written responses to this consultation and we are grateful to everyone who replied. We also met with pension providers and consumer groups and we are grateful to all those who gave so generously of their time to discuss the issues and to share ideas and suggestions. A list of organisations that responded to the consultation is at Annex A.
4. This document is available on the DWP website at:

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SECTION 2: CONTEXT

5. The Pensions Act 2008 introduces a duty on employers to automatically enrol all eligible jobholders into qualifying workplace pension provision from 2012. Employers are able to choose the qualifying workplace pension scheme they adopt to discharge this duty.
6. Given that individuals cannot be required to make an active choice when being automatically enrolled, qualifying schemes used for automatic enrolment need to have a default option¹ in place.
7. The draft guidance set out minimum standards for default options in workplace personal pensions.
8. Stakeholders broadly supported the aims of the 2012 reforms and, in general, understood the necessity of guidance. A few stakeholders questioned the need for guidance. The majority of stakeholders also advocated a broadening of the guidance to also support employers and advisers, as well as an extension of the guidance to apply to the default option in occupational schemes. However, there were reservations about the guidance being over-prescriptive.

Future plans for guidance

9. As a result of the consultation we plan to extend the scope of the guidance to employers and advisers and to incorporate occupational schemes. To do this we will undertake further research and consultation, with publication of combined guidance intended for spring 2011.
10. A later publication date allows us to continue to work with stakeholders on areas that were raised in the consultation responses. In particular we will address the key areas of: responsibilities, charges, and common industry benchmarks.
11. There are also some straightforward changes to make to the draft guidance following stakeholder responses and this document incorporates our proposals for these areas.
12. This document contains a summary of the responses to key areas of the guidance and the consultation questions.

¹ The default option is the investment option used when an individual pension member does not indicate an investment choice.

SECTION 3: RESPONSES TO THE CONSULTATION

13. **Responsibilities - The guidance gave underlying responsibility of the default option to the operator. This requires the operator to have ongoing responsibility for the design, implementation, governance and communication of the default option.**

Stakeholder response to consultation

14. Many respondents commented that the emphasis on operator responsibility did not reflect how the market currently operates. It was suggested that the role of the employer and adviser needed to be given more consideration.
15. Some stakeholders questioned how the emphasis on responsibilities in this guidance would fit in with the Investment Governance Group's (IGG) draft guidance on DC schemes.

Government response

16. Underlying responsibility was originally given to the operator to ensure a strong chain of accountability to safeguard members' interests. However we agree that this does not accurately reflect the way in which the pensions market currently works.
17. We propose to continue working with stakeholders and the IGG to amend this area to take better account of the responsibilities of employers and providers.

18. **Affordability - We set out the design principle that, "The default option should be appropriately and competitively priced. Total charges should be below the stakeholder price cap".**

Stakeholder response to consultation

19. Many stakeholders, particularly providers, were critical of this design principle. Four main concerns were raised:
- a price cap is unnecessary;
 - potential for innovation to be stifled, e.g. guaranteed scheme with higher charges;
 - how the price cap and the FSA's Retail Distribution Review (RDR) would interact;
 - how compatible the stakeholder pensions price cap would be with a variety of charging structures.

Government response

20. In line with stakeholder responses, we propose to remove the reference to the stakeholder pension price cap. We intend to continue working with all stakeholders on rewording the affordability principle so that consumers are protected whilst not stifling innovation within the industry nor being overly prescriptive.

Q2.1 - We asked whether the term ‘operator’ provides enough clarity on who falls under the remit of the guidance.

Stakeholder response to consultation

21. The majority of stakeholders felt that the term operator was adequate but that some further explanation would aid clarity.
22. Many stakeholders questioned whether the guidance should be aimed solely at the operator.

Government response

23. The draft guidance states that, “by operator we mean the person who is, for the purposes of regulation, the operator of the pension scheme with the relevant FSA permission (Regulated Activities Order article 52)”.
24. We propose to enhance the clarity of the term operator by including the FSA definition in the guidance and making reference to the commonly used term provider.
25. We also propose broadening the scope of the guidance to support employers and advisers as well as operators.

Q.2.2 - We asked whether the Department should issue separate guidance on the design of default options in occupational schemes as well as workplace personal pensions.

Stakeholder response to consultation

26. Stakeholder views were mixed on whether additional guidance was necessary, however the majority welcomed some sort of guidance on occupational schemes.
27. A common theme among stakeholders was that there should be a ‘level playing field’ between all defined contribution (DC) schemes.

Government response

28. The draft guidance only relates to WPPs as it was originally felt that occupational schemes provided more protection for members. However, during research carried out by PricewaterhouseCooper (PwC) in summer 2009, many participants questioned why guidance was solely directed at WPPs.
29. In line with the majority of stakeholder views, we propose to incorporate guidance for occupational schemes into the current guidance document. This will require further research and consultation.

Q. 2.3 - We asked whether it would be helpful to set out in guidance how many default options we feel should be offered to the employer, and if so, what a manageable number of options would be.

Stakeholder response to consultation

- 30. In general stakeholders felt that setting out how many default options should be offered would be unnecessary and/or unhelpful.
- 31. Some stakeholders said that it was fair for operators to only offer one default fund if they wished.

Government response

- 32. We originally recommended to operators that when offering a default option, a manageable and targeted set of options should be presented to the employer.
- 33. Taking stakeholder views into consideration, we propose to reword the recommendation so that operators should offer at least one default option to the employer.

Q.2.4 - We asked whether it would be useful to define ‘common industry benchmarks’ more closely.

Stakeholder response to consultation

- 34. Many stakeholders felt it was unnecessary or unhelpful to define common industry benchmarks more closely as they were likely to change over time. However there were a small number of respondents that said defining common industry benchmarks would promote clarity and understanding.
- 35. Some concerns were raised that certain benchmarks may promote riskier default options, which only perform better in the short-term.

Government response

- 36. The guidance states that the default option should be reviewed by operators when certain events occur, e.g. when there is consistent underperformance of the underlying funds used in the strategy against common industry benchmarks.
- 37. Although many stakeholders felt that it was unnecessary to define common industry benchmarks more closely we propose to continue stakeholder dialogue in this area to ensure there are sufficient safeguards in place for members in response to the potential use of benchmarks with excessive risk.

Q2.5 & Q2.6 - We asked if there were any other cases which should trigger a review, and what else the review should look at.

Stakeholder response to consultation

38. Stakeholders responded with some good suggestions of other cases that should trigger a review, as well as some examples of cases that were not appropriate to trigger to a review.

Government response

39. The guidance advises operators on review aspects of the default option. It gives examples of when it should be reviewed along with what the review should look at.
40. We propose to incorporate some stakeholder suggestions into examples of when and how to trigger a review, e.g. when legislative changes occur.

Q2.7 - We asked how feasible it would be for operators to make information on the review of their default option available on their website.

Stakeholder response to consultation

41. The majority of stakeholders felt that this was feasible as long as the information provided was generic. However it was also highlighted that members without internet access should be taken into consideration.
42. Some stakeholders warned against giving members too much information in case it had a negative effect, and questioned whether the benefits would outweigh the costs for operators.

Government response

43. PwC research highlighted that participants saw the promotion of communication as an important role of the guidance. Therefore the guidance set out recommendations for operators on their communication with members.
44. On further consideration of the cost and benefits to operators, we intend to relax the guidance recommendations on communications. We propose that operators need only to provide information on request however members will need to be initially informed that they are entitled to request this information.

Q.3.1, 3.2 & 3.3

We asked whether the definitions of SIPPs and group SIPPs provided were helpful and for suggestions of alternative definitions.

We asked whether it would be helpful to provide separate sections on the use of insured and non-insured group SIPPs given their different structures.

We asked whether stakeholders viewed non-insured group SIPPs as a suitable product for auto-enrolment, given their non-tiered structure.

Stakeholder response to consultation

45. Not all stakeholders responded to the questions on SIPPs and group SIPPs. Of those that did respond, a majority felt that these products (insured and non-insured) did not require a separate section in the guidance as long as they are subject to the same minimum standards as any other WPP.

Government response

46. A separate section was originally included in the guidance for SIPPs and group SIPPs due to their different structure.

47. Taking into account the majority of stakeholder views, we propose to remove the separate section on SIPPs and group SIPPs as they are already subject to the overall guidance, which sets out minimum standards for default options in WPPs.

SECTION 4: NEXT STEPS

48. We plan to carry out further research in order to inform the extension of the guidance to include occupational schemes. During the additional research phase, we will continue to engage with stakeholders on redrafting key areas of the WPP guidance. We intend to consult on the amended guidance in late 2010, with a revised publication date of spring 2011.

Annex A: List of respondents

ABI
Aegon
Alliance Bernstein
AMPs
APL
Aviva
Capita Hartshead
CBI
Fidelity
Friends Provident
Hargreaves Lansdown
Hewitt
ICAS Pensions Working Party
IMA
Investment & Life Assurance Group
IoD
Legal & General
MetLife
Mercer
NAPF
PADA
PensionsDCisions
PMI
Prudential
Scottish Life & Royal London
Scottish Widows
Society of Pension Consultants
Standard Life
TISA
TPAS
TUC
Wakefield Council

