Personal Accounts:
a new way to save

Summary of responses to the consultation

June 2007

Department for Work and Pensions

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Summary of responses to the consultation

Presented to Parliament by
the Secretary of State for Work and Pensions
by Command of Her Majesty
June 2007

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Foreword

Our White Paper, *Personal Accounts: a new way to save*, set out our proposals for the next stage of long-term pension reform in Britain. Supported by matching employer contributions, tax relief and automatic enrolment, the new system of Personal Accounts will help many more people to start saving for their retirement.

The consultation has been an invaluable part of the development of these reforms and I am grateful to everyone who has taken the time to respond. There has been a clear consensus on the need for the accounts to be simple, independently run and focused on delivering for the interests of the consumer. This, I believe, will be critical to the success of the scheme and to increasing confidence across the industry as a whole.

As expected, one of the main issues was the question of how to ensure that Personal Accounts are accurately targeted to fill the gap in the existing market, not compete with that market. In designing Personal Accounts as a no-frills occupational pension, I am making clear that this is our objective from the outset. In setting the level of the contribution cap we have again sought to find the right balance between giving the consumer sufficient flexibility to save while protecting existing occupational schemes.

The last year has seen tremendous progress in building a consensus on a new foundation for long-term savings. We must now go further in deepening that consensus around the details of Personal Accounts. The coming year could be the most important in getting this right. There are a number of issues on which further work is required and we must continue to work together in revitalising the workplace pension at the heart of a sustainable, affordable and trusted pensions system for generations to come.

The Rt Hon John Hutton MP

Executive summary

Personal Accounts: a new way to save

1. In December we published the White Paper *Personal Accounts: a new way to save*. It represented a fundamental shift in the approach to private pension saving in the UK. The introduction of automatic enrolment for all eligible employees, with access to a minimum employer contribution, will mean that for the first time employees will have the right to a workplace pension with matching contributions from their employer and government.

2. Our reforms will instigate a change in the savings culture of this country – so that retirement saving becomes the norm. The introduction of a new trust-based occupational scheme, the Personal Accounts scheme, will extend the benefits of an occupational pension to our target group – the millions of people who are currently without access to good quality workplace provision. Personal Accounts will provide employers who do not run their own scheme with a simple way to help their employees to save.

3. In developing Personal Accounts it is essential to maintain the focus on this target group. That means designing a low-cost scheme that will offer people simple choices.

4. But delivering this scheme is not a task for government. We have started to bring in private sector expertise through the creation of the Personal Accounts Delivery Authority. This will continue through to the establishment of an independent Personal Accounts board to run the scheme from 2012.

5. The responses to the White Paper highlighted the consensus behind the need to introduce Personal Accounts. The overwhelming message across the spectrum of stakeholders is that they support both the need for reform and our approach to its delivery.

> *"The Government is right to encourage more people to save more for their retirement, particularly those on low and middle incomes who are currently not saving at all."* (Association of British Insurers)

> *"CBI members strongly support the establishment of a low-cost savings vehicle for lower–moderate earners who are not members of an occupational scheme. The CBI therefore welcomes the Government's decision to take forward the Pensions Commission's recommendation that employees without a pension should be automatically enrolled (with the right to opt out) into a new National Pensions Savings Scheme or an alternative employer scheme."* (Confederation of British Industry)
>
> *"There is widespread support for the principle of automatic enrolment and broad agreement that the proposed levels of contribution to Personal Accounts (4 per cent individual, 3 per cent employer and 1 per cent from tax relief) are reasonable."* (Pensions Policy Institute)
>
> *"The NAPF welcomes the Government's proposed reforms for the introduction of automatic enrolment, mandatory employer contributions and the creation of a Personal Accounts scheme. We share the Government's commitment to pension reform and believe that their proposals will help many more working people save for retirement."* (National Association of Pension Funds)

6. As we progress from discussing policy to focusing on delivery, it is worth reiterating the principles that will continue to drive this work:

   - simplicity: Personal Accounts must simplify the decisions people are asked to make and provide an easy way to save;
   - independence: Personal Accounts will be delivered using private sector expertise independent of outside pressures;
   - working for members: building a Personal Account scheme which commands the confidence of its members and is designed with their needs at its heart;
   - minimising the burden on employers: ensuring that the impact on employers is considered at each stage of development; and
   - supporting good existing provision: focusing Personal Accounts on those without access to workplace schemes.

7. The reforms we are introducing are, by their very nature, long term, so we need to ensure that the decisions we make now will stand the test of time. The Delivery Authority will be able to draw on private sector expertise and experience, to ensure that our reforms are successfully implemented.

8. It is important that we provide the Delivery Authority with the flexibility to deliver a low-cost scheme that meets the needs of its members. This means we do not make decisions now that the Delivery Authority will be better placed to make. But at the same time we need to ensure that the policy framework is well defined, with clear

objectives. We also need to provide certainty for both employers and the pensions industry as they plan for reform. We believe the proposals outlined in this paper balance these requirements.

Simplicity: Personal Accounts must simplify the decisions people are asked to make

9. Pensions are complicated, and too many people find it difficult to save what they need for retirement. Although parts of the pensions market work very well, the market is not working for most people on moderate to low incomes who do not have access to a workplace scheme. It is difficult for this group to find the right kind of pension product for their circumstances and pension providers cannot profitably supply what is needed.

10. Our analysis has shown that people place a high value on simplicity in pension design. It is vital that the Personal Accounts scheme simplifies the decisions people need to take. That is why features such as low cost, simplicity and portability remain fundamental in the scheme design. Personal Accounts must provide an affordable and flexible way to save for employees without access to a workplace pension.

Independence: delivery of reform using private sector expertise

11. In the White Paper we set out our intention to establish a Delivery Authority to design and build the infrastructure needed to implement Personal Accounts. The Delivery Authority will initially be set up as an advisory organisation, its role limited to providing advice to government on the operational and commercial implications of policy. The Government plans to legislate in a second Pensions Bill to extend this role and give the Delivery Authority executive powers.

12. The Authority will, in this executive stage:

- have clear objectives to deliver the infrastructure for the Personal Accounts scheme and automatic enrolment;
- be tasked with delivering a scheme that will meet members' interests with low charges, appropriate investment choices and a panel for prospective members;
- be required to deliver the scheme in a way that minimises the burden on employers and supports existing provision; and
- act in a consultative and open manner – the development of Personal Accounts has been characterised by its emphasis on consultation and this will continue under the Delivery Authority.

13. We anticipate that there will be a period of overlap in delivery responsibility between the Delivery Authority and the Personal Accounts board which will run the scheme from 2012. Personal Accounts will be delivered through a trust-based occupational

scheme, the ultimate strategic management of which will rest with a board of trustees. We propose that a sub-set of these trustees, with responsibility for financial decisions including investment, is appointed during the Delivery Authority's executive stage. This will provide continuity during the transition period and also ensure that trustees are in place to set the strategic direction for the scheme.

14. The degree of independence in delivering Personal Accounts will increase as the Delivery Authority takes on executive powers. While the Department for Work and Pensions will perform a stewardship role throughout the period leading up to the launch of Personal Accounts, its involvement will be closest during the initial stages of the Delivery Authority's work. With the introduction of the Personal Accounts board, that relationship will shift to be one where the trustees are in the lead, whilst continuing to be appointed in accordance with the best practice guidance for public appointments.

Working for members: building a scheme that commands members' confidence

> *"Which? welcomes the White Paper* Personal Accounts: a new way to save *and we see it as an important step forward in the creation of a long-term solution which will empower savers to make additional provision for their retirement."* (Which?)

15. Personal Accounts must be designed to meet the needs of its future members. The scheme is being introduced for the millions of people who have not had the opportunity to save for their retirement in a simple, low-cost, portable scheme – this is the minimum that must be delivered.

16. We will be setting up Personal Accounts as a trust-based occupational scheme. The trustees' legal duty will be to act in the best interests of scheme members. The scheme will be regulated by the Pensions Regulator and therefore subject to the existing proven regulatory framework for all occupational schemes. However, we want to go further and put members' interests right at the heart of Personal Accounts. To that end, we plan to introduce:

- an influential members' panel with a remit to put members' views and concerns to the trustees, and to nominate one third of trustees; and
- a duty to follow best practice in consultation and to develop innovative ways to encourage member engagement and a sense of ownership.

Minimising the burden on employers

"We support the Government's decision to base the model for delivering Personal Accounts on the Pensions Commission's National Pension Savings Scheme (NPSS). We consider that this model will help to minimise the administrative costs and potential risks for employers as well as make it easier for employees to understand Personal Accounts and the automatic enrolment process." (Engineering Employers' Federation)

"Smaller CBI members welcome the Government's decision, following CBI lobbying, to:

- *phase in compulsory employer contributions to Personal Accounts over three years (employers will pay 1 per cent in year one; 2 per cent in year two and 3 per cent in year three); and*
- *place the 3 per cent employer contribution on the face of the bill to try and ensure that the employer contribution is not ratcheted up over time.*

These measures will provide some reassurances that employer costs will not be ratcheted up over time and allow employers to manage the transition." (Confederation of British Industry)

17. Employers will be critical to the success of our reforms. Many employers already offer good pension schemes and understand the need to extend access to that provision to other employees. But for many employers this will be a new responsibility. We are convinced that the right way to tackle this challenge is to design the scheme so that the processes for employers work with existing ones, and do not impose any unnecessary burdens. We outline in this response our approach to minimising the burden on employers, which includes:

- extending to hybrid schemes the simple qualification process for existing defined benefit and defined contribution occupational schemes;
- allowing existing schemes, with benefits or contributions above the Personal Accounts minimum, to run a short waiting period of three months;
- introducing a light-touch but effective compliance regime which works through early intervention, informing employers of their obligations and supporting them in complying, with enforcement as a last resort;
- continuing our engagement with employers and their representative groups in designing and building the scheme; and
- establishing an employers' panel within the Personal Accounts scheme, to ensure that the views of this diverse group can be put to the trustees.

Supporting good existing provision

"The White Paper makes several proposals designed to distinguish Personal Accounts from current private pension provision. These are vital to ensure that a vibrant private pensions and savings sector continues to prosper and grow." (Association of British Insurers)

"Fidelity International still believes that Personal Accounts represent an effective way of encouraging retirement saving in the target market. We are pleased that the Government has taken some heed of warnings of the impact of the new regime on corporate pension provision..." (Fidelity International)

"Taken in conjunction with the enabling reforms of the state pension system, we believe that Personal Accounts represent a significant opportunity to extend private savings levels where, because of structural barriers, current market-based options have fallen short. We also believe that, if carefully implemented, Personal Accounts can deliver increased savings levels and co-exist with existing private sector pension arrangements." (Scottish Widows)

18. Our reforms must also support good existing provision. As our analysis in the White Paper made clear, we estimate that approximately 7 million people are currently not saving enough to give them an income in retirement that they are likely to consider adequate.[1] Personal Accounts are being introduced to tackle this undersaving and we have always been clear that they should complement, rather than compete with, existing provision. While the responses from the pensions industry were supportive of the reform proposals, they also stressed the importance of continuing to support existing good provision alongside the proposed changes.

19. Simply shifting pension saving between groups will not make our reforms a success – success will be characterised by a greater number of people making better provision for their retirement. Personal Accounts are being designed explicitly for the target group of people who are not saving for their retirement now and who, even after the introduction of automatic enrolment, will not have access to a good alternative scheme. This publication outlines a number of proposals that will help to focus Personal Accounts on this group, including:

[1] Estimates of the current level of undersaving for retirement are difficult to construct due to: difficulties identifying appropriate saving targets; uncertainties about which kinds of wealth and asset to take into account; difficulties projecting individuals' future saving and working patterns, particularly around choice of retirement age; reliance on inadequate data; and reliance on a range of other uncertain assumptions, including the impact of future macro-economic developments. Consequently, such estimates should be treated cautiously. The current Department for Work and Pensions estimate draws on analysis by the Institute for Fiscal Studies (Banks J, Emmerson C, Oldfield Z and Tetlow G, 2005, *Prepared for Retirement? The Adequacy and Distribution of Retirement Resources in England*, IFS). The May 2006 White Paper, *Security in retirement: towards a new pensions system*, sets out some of these issues in more detail.

- continuing to work with a range of stakeholders on the role of workplace personal pensions in the context of automatic enrolment; and
- setting the contribution cap at £3,600, to be uprated in line with earnings to 2012 and beyond.

20. The decision on the level of the contribution cap needs to balance giving individuals flexibility for additional saving while focusing the scheme on the target group. The analysis supporting this decision shows that a very large majority of moderate to low earners will be able to reach benchmark replacement rates[2] within a limit of £3,600. This figure will be more effective than a limit of £5,000 (as proposed in the White Paper) at focusing the scheme on the target group, thereby minimising the risk that employers will close existing good schemes and transfer their employees into Personal Accounts.

Next steps

21. This paper sets out a number of further decisions clarifying how our private pension reforms will be delivered. We plan to introduce legislation in a future session of Parliament to extend the remit of the Delivery Authority to include executive powers, and to set the statutory framework for the Personal Accounts scheme.

22. Our broad approach to this legislation will be one that balances two important requirements. We will seek to give certainty to employers and industry on the policy framework for the Personal Accounts scheme. However, decisions on the detail of operational processes will need to take into account the advice of the Delivery Authority.

23. The Chair and Chief Executive of the Delivery Authority will be recruited during the summer, with the intention that they will then be able to engage other Authority members over the coming months. It would be premature for the planned Bill to try to provide certainty about operational processes that can only be decided once the Delivery Authority has been fully established.

24. Therefore, while the intended Bill will ask for primary powers to set up the essential statutory framework for reforms, much of the detail of operational processes will appear at a later stage in secondary legislation, once the advice of the Delivery Authority has been fully taken into account. We believe that this will strike the right balance between providing clarity for industry and employers while giving the Delivery Authority the flexibility it needs to implement our reforms.

[2] The replacement rate measures income in retirement as a percentage of income before retirement.

Chapter 1: Individuals and automatic enrolment

1. Our strategy is to make it both easy and attractive for people on moderate to low incomes to save for retirement. We will do this by introducing a responsibility on employers to automatically enrol eligible workers into occupational pension schemes. Employers with existing good schemes will be encouraged to maintain them, with Personal Accounts available to employers who do not offer a good scheme. The measures we are introducing balance the ability of people to save, the cost to the taxpayer, the impact on employers and the importance of the existing pensions industry.

2. Automatic enrolment into a private pension is an essential component of the wider plan for reform as it creates a presumption in favour of saving. Evidence shows automatic enrolment to be one of the most effective joining techniques for combating the widespread tendency not to act when people are faced with difficult financial decisions.

What *Personal Accounts: a new way to save* proposed

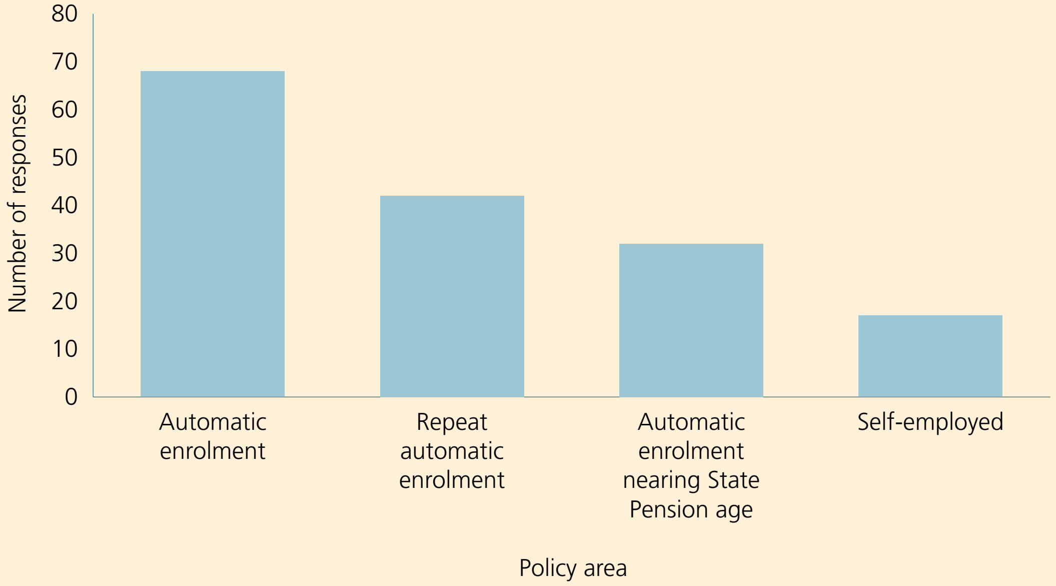
- Individuals will be automatically enrolled into qualifying work-based pension schemes or Personal Accounts if they are workers aged between 22 and State Pension age, and earning above approximately £5,000 a year.

- Contributions will be made on a band of earnings by those earning between around £5,000 and £33,500 a year, the Personal Accounts earnings band, which will be uprated in line with earnings.

- These reforms will provide good incentives to save through the combination of the employer contribution, tax relief and lower costs, building on the stable foundation of a reformed state pension system.

Responses

Figure 1: Number of consultation responses on individuals and automatic enrolment



The White Paper posed two specific questions on automatic enrolment and the treatment of people approaching State Pension age. Respondents also commented more widely on the definition of the target market, which helped to clarify the issues at stake.

Automatic enrolment prior to State Pension age

What the White Paper asked

Whether there should be a cohort of employees approaching State Pension age at the time Personal Accounts are launched who should not be automatically enrolled into Personal Accounts.

"Having a cohort of eligible employees approaching State Pension age when Personal Accounts are introduced, who do not have to be automatically enrolled into Personal Accounts by their employer, would create some unnecessary administrative complexity for employers." (Engineering Employers' Federation)

"The BCC believe there should be a practical cut-off point, for example those approaching State Pension age, who should not automatically be enrolled." (British Chambers of Commerce)

> *"We do not believe it is right to bar those approaching State Pension age from automatic enrolment."* (Legal & General)

Whether, in practical terms, this might adversely affect the interests of this group, because they would be less likely to exercise the positive choice to opt in.

> *"Which? believes that all people should be automatically enrolled into the scheme unless the DWP can demonstrate that there will be an overriding adverse impact on the scheme as a whole and on an identifiable group of individuals from auto-enrolment."* (Which?)
>
> *"This does not imply that all people between 50 and State Pension age will benefit from a personal account but it does suggest that many people in this age group could potentially benefit from automatic enrolment."* (Pensions Policy Institute)
>
> *"We believe there is an argument for not automatically enrolling those within, say, five years of retirement. This group will likely be unable to save more than a pension of a few pounds a week, which, in the target groupings, is likely to interact adversely with the means-tested benefits system."* (Institute of Directors)

What you said

3. Of those who expressed a view, the majority were not in favour of having a transitional arrangement to exclude those approaching State Pension age from automatic enrolment. Stakeholders from employer organisations as well as consumer groups took this view. There was a range of arguments, including the need for the scheme to be easily understood by the target group and simple for employers to operate. Additionally, it was argued that the scheme should not discriminate against particular groups who might benefit from being automatically enrolled.

4. Those arguing in favour of transitional arrangements were primarily concerned about low rates of return and interaction with means-tested benefits.

5. Some respondents also questioned why those below the age of 22 would not be automatically enrolled. Some called for flexibility on this issue, if this suited their business needs.

How the Government will take this forward

6. We are not planning to automatically enrol people below the age of 22, as to do so would expose employers to the additional administrative burden associated with the frequent job changes made by young people, particularly students. However, people between the ages of 16 and 22 will be able to opt in to Personal Accounts and receive an employer contribution on eligible earnings. There is nothing to prevent an employer enrolling employees under the age of 22, but they will not be required to do so.

7. At the upper end of the age band, we do not intend to require the automatic enrolment of individuals beyond State Pension age. This aligns the upper age limit with the point at which contributions to state provision cease. More important, it avoids forcing a scheme rule change on those employers with schemes that would otherwise qualify. Most of these schemes include a rule that relate to 'normal pension age' (generally between 60 and 65), which means they are not currently open to those over State Pension age. This should also reduce the likelihood that an employer ends up running Personal Accounts in parallel with another qualifying scheme.

8. Given the balance of responses we received, we have decided that we will require employers to automatically enrol all eligible employees between the age of 22 and the State Pension age. There will not be any transitional arrangements for those approaching State Pension age when the scheme is introduced.

9. We recognise that for a transitional period after launch, those close to State Pension age will have less time to build up their pension fund. Last year, we published our analysis[3] which shows that, subject to factors such as employer contributions, tax relief and investment returns, the large majority of people can expect to benefit from saving in Personal Accounts. People who already have some provision for retirement will be able to build on that with whatever they accrue through Personal Accounts. Those reaching retirement with accumulated pension funds of less than 1 per cent of the lifetime limit (£16,000 in 2007/08) would be able to take these savings as a lump sum, 25 per cent of which may be taken tax free.

10. We are aware that those people with high levels of debt, or with an interrupted work record, or who are nearing retirement without an existing pension or any retirement savings, may decide to opt out. We agree with the broad consensus among respondents that people will need good information to help them to make such decisions.

[3]*Financial incentives to save for retirement*, DWP Research Report No. 403, December 2006

Repeat automatic enrolment

What the White Paper asked

Whether three years is the right period for repeat automatic enrolment of employees who have opted out of Personal Accounts.

"We agree that three years is the right period for repeat automatic enrolment of employees who have opted out of Personal Accounts. This strikes the right balance between the needs of the employee, the needs of the employer and keeping the overall costs of the scheme down." (Which?)

"We believe a more practical approach, that will achieve the same results, is for the employer to choose a fixed date in the calendar, every three years, to send out letters to everybody who has opted out of the scheme. This would mean that some people would receive a reminder less than three years after opting out, but nobody would wait more than three years." (Tesco)

"The CBI accepts that re-enrolment should feature as part of NPSS for those employees who initially choose to opt out but subsequently wish to join NPSS, but we would have concerns if employers were compelled to re-enrol employees at frequent intervals. For this reason, we believe the proposed time frame for re-enrolment – three years – is a sensible way to proceed." (Confederation of British Industry)

"The key principle should be that everyone is automatically enrolled." (Trade Union Congress)

How this would affect employers and employees

"Our experience in providing Group Personal Pensions and in running a range of Occupational Pension Schemes leads us to conclude that a single date for all employees to re-enrol would be significantly less complex and therefore, less costly, for employers to administer." (Co-operative)

"Automatic re-enrolment after three years is a huge administration burden, at a time when Government intentions are to aim to reduce the amount of 'red tape' across organisations. For an employer, there would be a negative impact." (Institute of Payroll Professionals)

"EEF considers that it would be easier for employers to administer this repeat automatic enrolment if it had to be undertaken on a fixed date for all employees." (Engineering Employers' Federation)

> *"When employees are opted in after three years, they should be given appropriate information to help them make a decision whether or not to stay enrolled. They should be encouraged to consider how their personal circumstances and expectations about the future have changed."* (Carers UK)
>
> *"A shorter period [than three years] would be more expensive to operate and the impact of supporting communications potentially lessened."* (Scottish Widows)
>
> *"It is also important that it will not create unnecessary burdens for employees, with clear information being given on why the re-enrolment process is being carried out."* (Standard Life)

What you said

11. Most of the respondents who commented on this issue were in favour of re-enrolment, although concern was expressed about the administrative impact on employers. Those who were against automatic re-enrolment primarily cited the additional burden on the employer.

12. There were a number of suggestions from respondents about how to reduce the complexity and overall impact on employers, for example by aligning re-enrolment with the change in tax year, or a salary review or using a fixed re-enrolment date. This approach would enable employers to arrange re-enrolment activity collectively rather than managing a unique re-enrolment date for each employee. There were also suggestions that there should be alternative timescales such as annually or every two years.

13. Some respondents also commented on the information that might be made available at the point of re-enrolment. In particular, they were keen to ensure that workers would be able to assess whether it might be worth making additional contributions to compensate for the fact that they had not been saving up until the point of automatic enrolment.

How the Government will take this forward

14. Re-enrolment is a complicated matter and has implications for individuals, employers and schemes, including Personal Accounts. The basic aim is to set an interval that strikes an appropriate balance between the key needs of maximising participation and minimising the administrative burden to both employers and schemes.

15. We need to ensure that the initial interval fits with the rollout of the overall package of reforms. We also need to look at the impact of job churn and other participation factors on scheme costs, in the form of processing peaks and administrative costs to employers.

16. It is important we get the timing and process of re-enrolment right. We need to work with the Delivery Authority to explore how best to do this and as re-enrolment will not occur until some time after the scheme is introduced we have some time to do this.

17. The Government is aware of the importance of providing greater certainty for employers about its approach to re-enrolment. As we are not yet in a position to confirm the right approach, we will start by establishing a minimum period so that re-enrolment cannot occur more frequently than every three years. In adopting this approach, we aim to provide greater clarity for employers and scheme providers, and enable the Government to take account of further analysis and advice from the Delivery Authority, including any wider consultation, before taking the final decision about both the actual period and the underpinning mechanism for re-enrolment.

Target group

What you said

18. A number of responses suggested that the definition of the target group was too broad. Respondents from the pensions industry wanted to ensure that Personal Accounts remain focused on the core target group to limit the impact on the existing market. Consumer representatives called on Government to design an inclusive, rather than exclusive, scheme.

> *"Personal Accounts have an ill-defined target market and will inevitably compete with existing pension products."* (Norwich Union)
>
> *"A narrower definition of the target group should be adopted – all employees aged between 22 and State Pension age whose employers do not have access to a pension with an employer contribution."* (National Association of Pension Funds)

How the Government will take this forward

19. We will address these concerns by focusing on a defined target group through our decisions on the contribution cap and earnings band.

20. People on earnings below the lower limit of the Personal Accounts earnings band may opt in to Personal Accounts and may receive an employer contribution if offered. However, we will want to avoid automatically enrolling people on very low incomes who will already be receiving a good income replacement rate in retirement through their State Pension.

21. We shall be keeping the impact of this policy under review. However, the Personal Accounts scheme is designed to address the retirement saving needs of workers on moderate to low incomes, who do not already have access to a good workplace pension scheme. In the main, these people are not currently targeted by the pensions industry.

Personal Accounts earnings band

22. In the White Paper we set out our proposal to align the thresholds for the new Personal Accounts earnings band with the Primary Threshold and Upper Earnings Limit for National Insurance contributions (£5,035 and £33,540 in 2006/07),[4] and to up-rate the Personal Accounts earning band annually, in line with average earnings.

23. The upper threshold of the Personal Accounts earning band is needed to ring-fence employer contributions and to maintain the focus of Personal Accounts on people on moderate to low incomes. This will help to differentiate Personal Accounts from existing provision, particularly that aimed at higher earners.

24. In the 2007 Budget, the Chancellor announced an increase in the Upper Earnings Limit, as part of a programme of tax simplification. This change would widen the Personal Accounts earning band if we continued to follow our existing plan.

25. We have, therefore, decided to establish the Personal Accounts earning band in line with the Primary Threshold and Upper Earnings Limit from 2006/07 and to up-rate these thresholds annually in line with average earnings. This means that the Personal Accounts earning band will not increase to the new level of the Upper Earnings Limit. This will help maintain the focus of Personal Accounts on the target group and constrain the extent to which it competes with existing provision. This decision also reduces the cost to employers of doing otherwise.

Job-holder

26. We need a definition of job-holder that provides the best fit with the policy to extend the benefits of low-cost pension saving to people on moderate to low incomes.

27. After careful consideration, we have decided to adopt the definition ‘worker’ to identify eligible job-holders for the purposes of automatic enrolment into private pension saving, including Personal Accounts.

28. Adopting ‘worker’ should align: eligibility for automatic enrolment into private pension saving; the coverage of the Working Time Directive; and the National Minimum Wage Act.

[4] *DWP Regulatory Impact Assessment*, published December 2006, paragraphs 3.2 to 3.20

Scheme Member Contributions – Phasing

35. The phasing of scheme member contributions was covered in the May 2006 White Paper and the December 2006 Regulatory Impact Assessment, but without any commitment to a particular profile.

36. We have carefully considered the profile for phasing worker contributions and concluded that it is important not to disturb the balance between the employer and worker contributions, and to keep it simple.

37. Therefore, we plan to phase in the default scheme member contribution over three years at 1, 3, and then 5 per cent, including tax relief, and will be enhanced by employer contributions of 1, 2, and then 3 per cent.

Chapter 2: Delivering Personal Accounts

What *Personal Accounts: a new way to save* proposed

1. The December 2006 White Paper set out why the Government chose the National Pensions Savings Scheme approach, proposed by the Pensions Commission, over alternatives for delivering Personal Accounts. It was chosen because it:

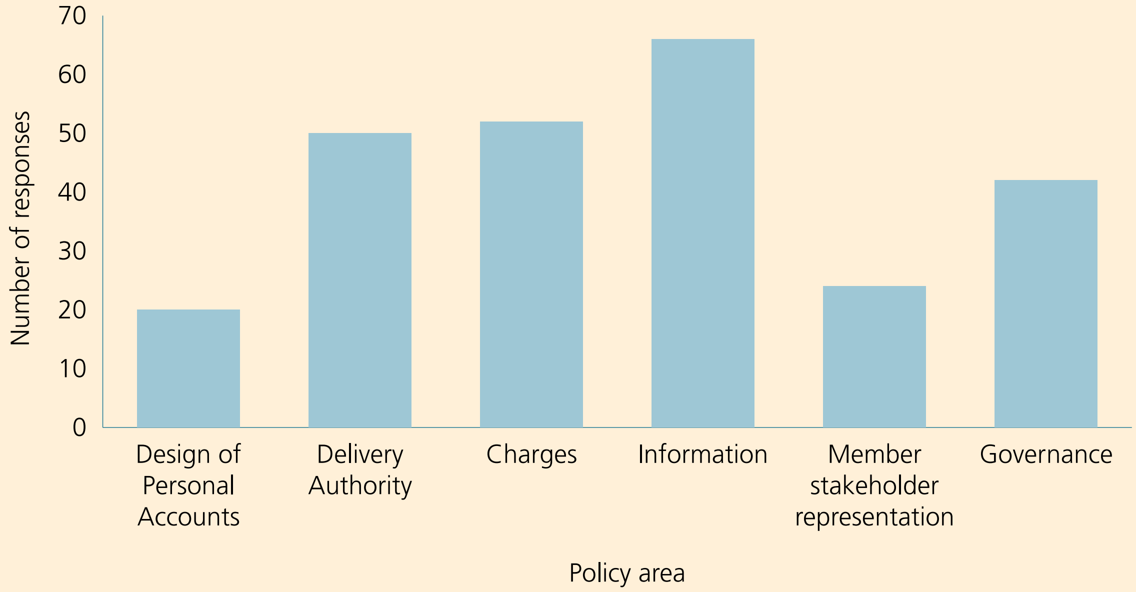
   - offers the simplest model for individuals – balancing simplicity for the majority with choice for the significant minority who want it;
   - delivers low charges – providers do not compete directly for individuals' accounts so there is less marketing expenditure and switching of accounts. Low charges should ensure larger pensions for scheme members; and
   - minimises delivery risk – it is not a government model. Instead, it uses the skills, expertise and capacity of the private sector to develop, build and deliver Personal Accounts.

2. The White Paper set out how this private sector expertise would be deployed through:

   - setting up an advisory Delivery Authority to develop the commercial and procurement strategies;
   - extending the remit of this body to include executive powers to build the infrastructure for delivering private pensions reform, including Personal Accounts; and
   - transition to the Personal Accounts board to run the scheme.

Responses

Figure 2: Number of consultation responses on delivering Personal Accounts



The National Pension Savings Scheme model

What you said

3. We did not pose any specific consultation questions about the delivery model in the White Paper. However, some responses commented positively on the National Pension Savings Scheme approach for delivering Personal Accounts.

> *"The TUC strongly supports the proposals contained in the White Paper – in particular, the adoption of the National Pension Savings Scheme (NPSS) model for Personal Accounts…"* (Trades Union Congress)
>
> *"The Personal Accounts system will have an independent but accountable governance structure through the Delivery Authority and board… Through such governance arrangements, the expertise of the private sector can be harnessed in a competitive fashion throughout the Personal Accounts system in order to deliver an efficient, low-cost, long-term savings vehicle for the target market."* (Investment Management Association)
>
> *"ILAG recognises the issues of pensioner poverty and inadequate long-term saving under provision for retirement, and believes that the proposed National Pension Savings Scheme (NPSS) through a system of Personal Accounts represents a potentially viable way of tackling these issues over time."* (Investment and Life Assurers Group)

4. Other responses did not support the approach. There were concerns that the National Pension Savings Scheme approach may not be able to deliver charges at the levels set out in the White Paper, and some consultation responses suggested that a provider-based approach would offer more effective competition.

> *"Norwich Union continue to believe that a model offering consumers simple choices would deliver a better service for consumers…"* (Norwich Union)
>
> *"We are concerned that the cost and complexity of offering investment choice within the proposed Personal Accounts model will result in less efficient operation of this system than could otherwise have been achieved, a restriction of the choice actually made available by the Personal Accounts board, or both."* (Fidelity)

How the Government will take this forward

5. Since the publication of the White Paper we have done further work on how the National Pension Savings Scheme model will be delivered. The Personal Accounts scheme will be set up independently of government, as a Non-Departmental Public Body operating under the strategic management of a board of trustees – the Personal Accounts board.

6. This chapter provides more detail on the delivery of Personal Accounts including the objectives for the Authority and the Personal Accounts board, the transition between the two organisations, and the responsibilities of the trustees. We focus particularly on effective member representation and the information strategy for Personal Accounts.

7. In addition to the individual responses received on these issues, we would like to acknowledge the contribution of the Pensions Policy Institute in producing a research paper, conducting stakeholder interviews and holding a seminar on the roles of the Delivery Authority and the Personal Accounts board. Their work was very helpful in drawing out the issues for consideration and prompting stakeholder input that has fed into our policy deliberations.

Delivery Authority remit and objectives

What you said

8. Many respondents welcomed the independence of the Delivery Authority from government, and the remit to use industry expertise. Some respondents also advocated giving the Authority flexibility to decide the charging structure, and many stressed the need for transparency. Some saw the Delivery Authority's role as going beyond responsibility to the future members, to include having a duty to take account of the effect of Personal Accounts on the existing pensions market.

9. Responses from the pensions industry largely focused on flexibility for the Authority in deciding charges, a wish to see the duties and objectives in legislation and a general requirement for greater transparency especially with regard to charges and accounting.

"PADA will be focused on the technical aspects of the delivery of the Personal Accounts scheme. Its objectives should be set down in statute at the earliest opportunity – the current Pensions Bill should be used to achieve this objective. These should include a specific duty to minimise any negative impact of the Personal Accounts scheme on today's high-value pensions. To assist PADA in its role the Government should establish a stakeholder advisory group which PADA would be required to consult prior to making recommendations to Ministers." (National Association of Pension Funds)

"We are supportive of the proposal to establish an independent Delivery Authority, involving the existing pensions industry, with responsibility for the design and implementation of the new system. It is imperative that the Delivery Authority has well-defined, measurable objectives around:

- *minimising the impact on existing (and new) employer-sponsored pension provision; and*
- *the financing of the model, and ensuring the reforms are clearly targeted at those on low and moderate incomes who do not have access to a pension." (AXA)*

"Communicating the benefits and features of Personal Accounts should be the responsibility of the PADA and the board." (Watson Wyatt)

"PADA's duties should be set out on the face of the bill, and should include a duty to take account of the impacts of Personal Accounts on the existing market, a duty to focus on the target market, and a requirement to avoid taxpayer subsidy to ensure that all costs are ultimately recovered through charges made to Personal Account holders." (Association of British Insurers)

How the Government will take this forward

Personal Accounts Delivery Authority – advisory stage (2007/08)

10. The Personal Accounts Delivery Authority was introduced in the Pensions Bill 2006 with an initial advisory remit. It is being set up to engage private sector expertise as early as possible to deliver private pension reform, working within a framework set by Government. The Bill currently before Parliament includes provisions to establish the Authority with a remit to 'do anything it thinks appropriate for preparing for the implementation of, or for advising on the modification of, any relevant proposals about Personal Accounts'.

11. This means that the advisory Authority will be:

    - **providing advice and making recommendations** – supporting the Government in understanding the operational and commercial implications of options; and

    - **advising on the design of the commercial strategy** – including the financial, technical and commercial analysis needed for policy development.

12. The Authority will be led by a Chair and Chief Executive with the skills to deliver Personal Accounts and the associated private pension reform. In turn the Authority will be able to recruit those with the appropriate legal, commercial, marketing, operational, business and financial expertise. Clearly the nature of the work undertaken by the Authority will change with time. Successful delivery of the scheme will require continuity, experience and specific expertise. It will be for the Chair and Chief Executive to make sure that they engage the right people at the right time.

13. One critical task will be to ensure that the behaviour and preferences of the target group for Personal Accounts remain at the core of the work to design and deliver the scheme. This is a group that is not served by the current pensions market so it is essential that the Delivery Authority adopts an innovative approach and develops a full understanding of the needs of this group by engaging with potential members and the appropriate representative organisations.

14. The development of Personal Accounts has been characterised by a transparent process of consultation, drawing on the views and expertise of stakeholders across industry, employer and consumer groups. We expect this to continue during the Authority's advisory phase and for a strategy to be developed for stakeholder engagement during the executive stage.

15. The Authority will be required to produce an annual report after the end of each financial year. This will be a public document that will include details of the work undertaken, the issues it has advised on and progress made over the year – subject of course to questions of commercial confidentiality.

16. As with any Non-Departmental Public Body, the Department for Work and Pensions will provide support and stewardship to the Authority during this period. A management statement and financial memorandum will be agreed between the two organisations, providing a clear operating framework. These documents will be published and the Authority's progress in implementing Personal Accounts will be monitored.

Pensions Policy Institute seminar and paper – *"What should be the roles and objectives of the Personal Accounts Delivery Authority and board?"*

The Pensions Policy Institute (PPI) were co-sponsored by the Department for Work and Pensions, the Investment Management Association, the National Association of Pension Funds and Which? to explore stakeholders' views on *"What should be the roles and objectives of the Personal Accounts Delivery Authority and Personal Accounts board?"*

The PPI interviewed stakeholders from 20 organisations across industry and consumer groups. Stakeholders were asked about their views on the roles and objectives of the Personal Accounts Delivery Authority and board. A discussion paper was then presented at a PPI seminar.

At the PPI seminar, three options were offered for the remit of the Personal Accounts Delivery Authority and board:

- **narrow remit** to set up and deliver the Personal Accounts scheme only;
- **broad remit** to set up and deliver the Personal Accounts scheme and other elements of pension policy reform, such as designing the test for exempt schemes, registering exempt occupational Pension Schemes and monitoring employer compliance; and
- **hybrid remit** to set up and deliver the Personal Accounts scheme and to provide advice to government on broader pensions policy reform areas.

The key messages from the research and from discussion at the seminar were that:

- stakeholders were broadly in agreement with the Government's aims for setting up and delivering Personal Accounts. In particular:
  - the overriding objective for the Personal Accounts scheme should be that it will be run in the best interests of scheme members.
  - the Personal Accounts scheme should be independent of government to minimise the risk of political interference in investment decisions.
- stakeholders leant towards a hybrid remit for the Delivery Authority and a narrow or hybrid remit for the board. Tasks such as registering exempt schemes and monitoring employer compliance are seen to be the responsibility of government or other public bodies.
- government should continue to take key policy decisions, such as defining the target market and setting the contribution cap. The Delivery Authority and board could provide advice on these decisions but would not have ultimate responsibility for taking them.
- there was no consensus on whether setting the charging structure was a policy decision that should be made by government or an operational decision for the Delivery Authority and board.

- member and other stakeholder representation is essential through all phases of setting up and delivering Personal Accounts. Members' interests were seen to be particularly important. A consumer panel model (as with the Financial Services Authority) was favoured, rather than an independent consumer body.
- the Personal Accounts board could be set up as a trust although the appropriate legal structure will depend on the remit.
- there was strong support for a pre-2012 handover from the Delivery Authority to the board to ensure that the scheme governance is established and stable at launch.
- there was an expectation of continuity of some personnel between the Delivery Authority and board so that experience and know-how were passed on.

Personal Accounts Delivery Authority – executive stage (2008/12)

17. The Government plans to legislate further in a second Pensions Bill, extending the authority's remit and allowing it to take on executive powers. The Authority will have a broad remit, assuming responsibility for delivering the Personal Accounts scheme and wider reforms, within a framework set by government. We propose that the objectives for this executive stage are:

- to design and build the infrastructure that will enable employers to provide automatic enrolment and employer contributions for eligible employees to a qualifying pension scheme; and
- to establish the infrastructure for Personal Accounts within a framework set by legislation and with regard to the interests of future scheme members.

18. The second objective is explicit about the need for decisions relating to Personal Accounts to be made in the interests of future members. This means that any services procured must provide value for money and that the systems built must offer secure administration of contributions.

19. We also propose that in delivering these objectives, the Authority is required to have regard to the following principles:

- minimising the burden on employers;
- minimising the impact on other high-quality pension provision;
- optimising levels of participation and contribution among the target group;
- delivering low charges to members;

- providing an appropriate range of fund choices; and
- acting in an open and consultative manner.

20. The specific tasks to be delivered include designing and implementing a commercial and procurement strategy, delivering the registration function, sourcing finance to deliver the reforms, and setting the charge level and structure for Personal Accounts. During its executive phase the Authority will also have a programme management role, to ensure that the different strands of the programme are designed and delivered in a co-ordinated manner and that systems and infrastructure are suitably integrated.

21. During this period there will be no members, but it will be essential for the Authority to focus on the needs of future members if it is to meet its second objective and deliver a simple scheme to meet the needs of the target group. We expect the Authority to set up 'consumer test panels' to make sure that the products and processes being designed will meet the goal of serving this group. A high proportion of lower earners who are not saving are women and we expect the Authority to take this into account in designing the panels, as well as in its general approach.

22. We envisage that the Authority will operate as a board of executives and non-executives supported by staff and specialist committees. The non-executives will have specific responsibility for audit, nomination and remuneration, as is usual for Non-Departmental Public Bodies.

23. The Authority will be accountable to Parliament through the Secretary of State. It will be required to produce an annual report and accounts, which will be laid before Parliament.

24. The Department for Work and Pensions will continue to perform a stewardship role, supporting the work of the Authority, as it does for its other associated Non-Departmental Public Bodies. Objectives and key targets will be agreed between the Department for Work and Pensions and the Authority with the stewardship team monitoring performance against objectives and targets. These will be published in the Authority's management statement.

Delivering private pension reform

25. Delivering a Personal Accounts scheme is only one part of the reform programme. In addition, the Delivery Authority will be tasked with designing and building the infrastructure that will enable employers to fulfil their requirements to operate automatic enrolment. However, this will not be an appropriate role for the Personal Accounts board. As the trustees of the Personal Accounts scheme can only act in the interest of their members it will not be possible for the trustees, as ultimate managers of the Personal Accounts scheme, to be involved in any of the other activities required

for the private pension reforms to be delivered. There are four key functions that sit outside the Personal Accounts scheme:

- ensuring employers are aware of their new obligations, and employees are aware of their new rights;
- registering how employers intend to fulfil the obligation, whether through Personal Accounts or another scheme;
- ensuring employers automatically enrol eligible employees into a qualifying pension scheme; and
- ensuring compliance with the new obligations.

26. There are a number of existing organisations already involved in either the regulation of pensions, the provision of pensions information or in monitoring employer compliance with statutory requirements, including the Pensions Regulator, Her Majesty's Revenue and Customs and the Financial Services Authority. We have been consulting with these organisations to consider the most cost-effective options for delivering these functions in a way that minimises burdens on employers while ensuring effective compliance with the new pension requirements. The Delivery Authority will be involved in managing this programme of work once it is fully engaged.

27. In doing this work we will consider the following set of key criteria:

- legal frameworks – the current scope of the organisation and any impact of possible legislative changes;
- financial – relative costs for employers and government;
- delivery – possible risks, track record of delivering major functions, expertise in relevant functions, likely impact on timescales;
- commercial – scope for efficiencies, capacity to carry out functions, or to contract out and manage that process;
- strategic fit – impact on pensions landscape, impact on organisation's core business, consistency with Hampton principles of better regulation; and
- customer and stakeholder experience – impact on employers, members and Pension Schemes.

Personal Accounts board: remit and objectives

What *Personal Accounts: a new way to save* proposed

28. The White Paper stated that the Personal Accounts board would be a body corporate, established under statute and self-financing. It would be subject to the normal scrutiny and accounting procedures, accountable to Parliament and would provide an annual report and accounts. The board would be responsible for employing its own staff and it was expected that this would not be a large organisation as most of the functions would be contracted out.

29. It was envisaged that the board would be responsible for three distinct areas:

- setting the strategic direction of the scheme and how the objectives set by the Government will be achieved;
- overall management of the scheme – oversight of scheme delivery; monitoring levels of service to members, setting standards for collection, verification and payment, and information to members; and
- investment strategy – ensuring that contributions are invested in the best interests of members; deciding on the range of funds available to investors; the strategy for investment of the default fund; and appointment and management of fund managers.

What you said

30. There was strong consensus that the Personal Accounts scheme should use the best available expertise and act in the best interests of members. It was suggested that the scheme should monitor and act to reduce opt-out rates among certain groups in the event of problems being identified. There was also the suggestion that the Delivery Authority or Personal Accounts board should introduce a policy similar to the 'treating customers fairly' concept introduced by the Financial Services Authority for the firms it regulates.

31. In its work on the remit of the Personal Accounts board, the Pensions Policy Institute presented stakeholders with three options of a narrow, broad or hybrid remit (see box on page 30):

- **narrow remit** limited to managing the scheme;
- **broad remit** including involvement in work related to exempt schemes and employer compliance alongside the management of the scheme; and
- **hybrid remit** managing the scheme and advising government on broader pensions policy reform areas.

32. The view of most stakeholders questioned was that a narrow or hybrid remit was most appropriate for the Personal Accounts board.

> *"At least one member of the PADA and the Personal Accounts board should have direct experience of running a large, multi-employer, occupational pension scheme."* (National Association of Pension Funds)
>
> *"The individuals appointed must have the knowledge, skills and experience needed to deliver Personal Accounts. These individuals should bring with them extensive expertise from all key groups of stakeholders in the field of pensions: consumers, employers, regulators and pension providers."* (Association of British Insurers)

How the Government will take this forward

33. By contrast with the broader remit of the Delivery Authority, the Personal Accounts board (which will be a trustee board) will have the narrower remit of delivering the Personal Accounts scheme. This will mean that the trustees are responsible for a number of different functions:

- setting the strategic direction of the scheme;
- setting and reviewing the scheme's statement of investment principles;
- ensuring that contributions received from employers are invested in the best interests of members;
- deciding on the choice of funds;
- appointment and management of fund managers;
- reviewing the annual management charge; and
- accountability for the running of the scheme, including:
  - oversight of scheme delivery;
  - monitoring levels of service to members;
  - monitoring levels of service and associated costs to employers;
  - setting standards for collection, verification and payment; and
  - information to members.

34. Trust law requires trustees, in discharging their functions, to carry out their fiduciary duty, to act "prudently, responsibly and honestly"[5] in the best interests of members and beneficiaries. This is a very strong message about the importance of members' interests. It makes clear that the trustees of the Personal Accounts scheme will have a

[5] The Pensions Regulators, http://www.thepensionsregulator.gov.uk/trustees/guidance/fiduciaryDuties/duties-08.aspx

legal duty to manage Personal Accounts in the interests of members. We will make clear that in being tasked with delivery of the Personal Accounts scheme the trustees will be responsible for ensuring that this remains a simple, low-cost pension without any additional features such as life, health insurance or similar.

35. A range of possibly competing objectives can result in a lack of clarity. Additional objectives, such as ensuring security of collection or high levels of customer service, would be covered by this overarching objective to act in the best interests of members and beneficiaries. Given the need to focus on the target market we intend that the trustees meet this objective by having regard to the definition of the target group. Within that target group, the trustees will also need to consider how the needs and requirements of individual groups, for instance women, can best be met.

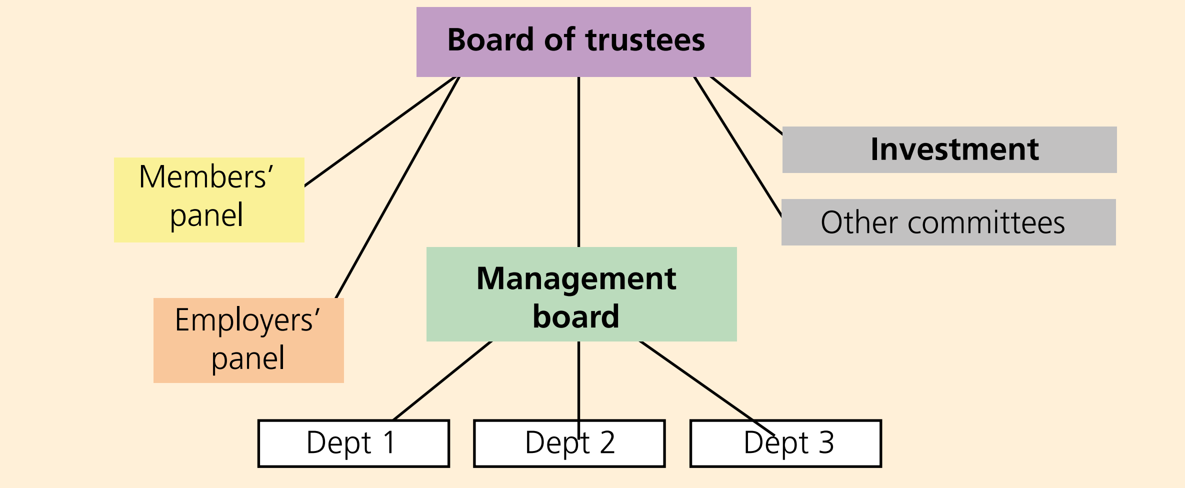
36. We set out in a later section how we think members' interests can most effectively be represented within the governance structure of Personal Accounts. The scheme would benefit from also having arrangements to take on the views of employers. The employers with employees in the Personal Accounts scheme are more likely to be small and micro-employers. Given the very large number of employers involved it is not likely to be cost-effective to use standard methods of pension scheme consultation (see paragraph 57).

37. It is vital that the scheme does not impose unnecessary burdens on employers and we will continue to consider the most effective way to achieve this. We will ask the board to set up an employers' panel charged with providing advice on matters affecting employers, acting as the main channel for consultation with employers and with a specific duty to report on administrative burdens the scheme imposes. It might also be useful if this group could act as a conduit to the board for individual employers – although there will of course be standard complaints arrangements so this will be a matter for the scheme to determine. This would be an advisory panel, but it would have regular meetings with trustees to ensure employers' views are heard.

38. The appointment of the first set of trustees will be a critical task. The trustees will be responsible for ensuring that Personal Accounts are delivered successfully. Between them, the trustees will need to have experience of the pensions market at the highest level and the board should also include trustees with a thorough understanding of the needs of the target group. We expect these individuals to be well qualified experts in their field as they will be required to make the best decisions for millions of members, and to build and retain public confidence.

39. The trustees will take an active role although they are not likely to be involved in the day-to-day management of the scheme. They will take the key strategic decisions but delegate all executive and operational functions to a management board. The trustees, with the Delivery Authority, will be influential in designing the structure of, and their relationship with, the management board. The diagram below demonstrates a probable structure, including member and employer representation.

Figure 3: The Personal Accounts scheme



40. All decisions about how the scheme is delivered and managed will be made by the trustees. When trustees believe that major changes which would affect members should be made to the scheme they will consult with members. There will be no involvement of government in these management decisions. However, unlike standard occupational schemes, the Personal Accounts scheme is being set up within a statutory framework to meet the needs of a particular target group and the trustees will be accountable to Parliament through the Secretary of State.

41. We intend to make the process for appointing the initial board as open and consultative as possible, looking to a wide range of stakeholders to participate in the selection process. We would expect the Authority to be involved in making the final recommendation for Chair to the Secretary of State. Once the board is established, it will make its own subsequent appointments, including a third nominated by the members' panel. It will nominate a Chair, for the approval of the Secretary of State.

42. We are looking at how the introduction of Personal Accounts will affect the existing regulatory landscape. As an occupational pension, the scheme will be regulated by the Pensions Regulator. There will be a robust internal complaints systems and both members and employers will have access to the board via their respective panels. Beyond the scheme's own arrangements, there would also be recourse to the Pensions Ombudsman, which investigates and decides complaints and disputes relating to occupational Pension Schemes.

The transition from the Delivery Authority to the Personal Accounts board

What *Personal Accounts: a new way to save* proposed

43. In the White Paper we anticipated that there might be an overlap period during which the Authority and the Personal Accounts board are both in place, so that any operational problems could be addressed.

What you said

44. Only a small number of responses considered this point and agreed that the transition from Delivery Authority to a live-running board responsible for the scheme from its launch would be a critical time that would need to be managed very carefully.

45. The Pensions Policy Institute's research presented four options for transition from the Delivery Authority to the Personal Accounts board:

- A-day handover, which would mean the board would take over all responsibility for the Personal Accounts scheme from launch;
- pre-2012 handover, the board takes over responsibility before 2012;
- post-2012 handover, the Delivery Authority runs the scheme for some time after launch; and
- parallel operation, in which the two bodies operate in parallel for some period.

The key issues which needed to be considered were identified as clarity of roles, minimising additional costs and maximising continuity and flexibility. Discussion at the Pensions Policy Institute seminar showed strong support for a pre-2012 handover from the Delivery Authority to the board. This would ensure that the scheme governance was established and stable at launch.

> *"There is also a clearer connection between the work of the Delivery Authority and the board than the White Paper acknowledges. In fact, there is likely to be a strong degree of overlap of both tasks and personnel between the Delivery Authority and the board."* (Investment Management Association)

How the Government will take this forward

46. The Delivery Authority will deliver the infrastructure and commercial and procurement strategies necessary for the successful implementation of private pensions reform. This will include setting up Personal Accounts as an occupational pension scheme. The scheme's trustees will be required to take on full responsibility for the scheme once the scheme becomes operational, whether or not this is through a phased approach.

47. Setting up a scheme and managing it over the long term involves different types of expertise, although there will also be areas of overlap. Some degree of continuity between the Authority and the trustees – or the operational management – of the Personal Accounts scheme, would seem appropriate. We expect that some Authority staff will transfer to working for the scheme, although this will be for the trustees to decide. There should be no assumption that staff will automatically move to work for the Personal Accounts scheme.

48. Continuity through the transition period will be provided by the need to bring in a key group of trustees early. The investment strategy will need to be designed considerably in advance of the 'go-live' date. We expect the investment committee to be the first set of trustees appointed. We would expect the Delivery Authority to do much of the groundwork in preparing an investment strategy for discussion with the trustees. Bringing in these trustees before the launch will enable their engagement with other facets of scheme design and so help ensure a successful transition.

What the White Paper asked

The Government is interested in views on how members' interests can best be represented in the governance of Personal Accounts.

What you said

49. Comments fell broadly into two distinctive areas: those respondents who felt that it was important that the membership of the board should be representative of the financial industry, and that individuals sitting on the board should bring expertise from financial and investment experience; and those respondents for whom it was important that a percentage of the Delivery Authority and board represented the target group for Personal Accounts.

> *"The Government should make the protection of members' interests the key objective for these bodies. While there should be member representation on these bodies, it is more important that those appointed to these bodies have the necessary experience and qualifications to carry out their functions. Lay representation is important but should not be so great as to be able to frustrate the efficient operation of the Personal Accounts system."* (Fidelity)

"We see consumer representation as fundamental if trust and confidence in Personal Accounts is to be upheld.

To maximise consumer interests further, Which? would not only like to see specific Delivery Authority representation but also a standing consumer interest committee to advise the board. We would stress the importance of consumer representation across all Delivery Authority committees." (Which?)

"One way in which the views of … stakeholder groups could be taken into account by the Personal Accounts Delivery Authority and the Personal Accounts board would be to require them to consult a stakeholder advisory body, comprising representatives of all stakeholder groups, on a regular basis as well as before making any significant changes to the structure or method of operation of the Personal Accounts scheme." (Engineering Employers' Federation)

"One means of including member representation would be to appoint representatives of member groups to these bodies. This could include consumer bodies and/or trade unions. The advantage of these organisations is that they have a direct interface with the potential member groups." (Gissing)

"The governance of Personal Accounts should include significant representation of members' interests. We feel that a number of non-executive directors should be appointed who have a background of working for trade union and consumer groups. There should also be lay representation." (First Actuarial)

How the Government will take this forward

Member representation

50. Personal Accounts are for people who do not already have workplace pensions and have not yet engaged with the pension market. For the scheme to succeed, it is essential that the members feel it is their scheme, that their voice is heard and that the scheme is responsive to their needs. The Government is conscious of the importance of getting this right, in a way that is appropriate for Personal Accounts, rather than assuming that the practices of existing occupational schemes will necessarily be the right approach.

51. The work done by the Pensions Policy Institute indicated widespread support for flexibility in creating the best method of engaging with members. Our proposal is to set up a members' panel made up of current scheme members, with an option for the future to include a proportion of retired members, as is normal practice. We have considered whether this panel should also include stakeholder groups representing members but, on balance, think that this would risk the panel becoming politicised and losing its focus on the members.

52. The remit of the panel would be to act as a combination of sounding board and watchdog, ensuring that the trustees fulfil their duty of acting in the members' best interests and communicating member concerns to the trustees. We envisage that this would be achieved through a formal structure, including a prescribed number of meetings, prescribed areas for consultation – for instance on changes to investment strategy – and both prescribed and ad-hoc reports.

53. The legal requirements for occupational schemes include member-nominated trustees but leave scope for schemes to determine their own approach. Some approaches, for example direct election, would be impractical given the potential millions of future members. We think it is more important to design mechanisms that will achieve the aim intended by these requirements, rather than to treat the Personal Accounts scheme as if it faced the same challenges as a conventional occupational scheme.

54. It is essential to meet the spirit of member-nomination of trustees but in a way that will work for Personal Accounts. Our proposal is that the members' panel would nominate one third of trustee board members. Existing regulations and the Pensions Regulator's code of practice allow schemes to decide the best way for members to nominate trustees, and we recommend that in the Personal Accounts scheme this should be a matter for scheme rules.

55. When Personal Accounts are launched there will not be a critical mass of members. We will look to the Delivery Authority to develop a strategy for building the first member panel within the remit set out above. One possibility would be for the first panel to be made up of individuals who have been involved in testing development of the scheme for the Authority.

56. We expect that the Authority will want to consider the model of the Financial Services Authority's consumer panel. In that instance the panel submits its own annual report, to which the Financial Services Authority responds. If this model was thought appropriate, the trustees would have a duty to consider the panel's representations and to give a written response if they disagreed.

Consultation with members

57. Over and above ongoing member representation, from time to time the scheme will want to consult its members (See para 36). Although we do not think that member consultation can be run on the same lines as existing occupational schemes – the costs would probably be disproportionate to any potential member benefits – the need to consult effectively is perhaps even greater for the Personal Accounts scheme.

58. We will task the scheme with developing an imaginative and inclusive approach to how it consults its members about scheme performance, strategy and direction. There is a range of innovative techniques, such as Citizens' Juries, Citizens' Councils and deliberative polls that can be used to engage people in evidence and issues and to enable them to arrive at informed views. A number of examples demonstrate that it is

possible to engage people in serious discussion about what could be thought of as dry subjects. These include:

- the National Pensions Debate – a large-scale UK-wide consultation on proposals to reform the UK pension system. The consultation was deliberative in nature, aiming to engage people in the evidence and policy issues to enable them to arrive at informed views on the issues facing the pensions system in the UK;
- the Department of Health's Your Health, Your Care, Your Say listening exercise. Using a wide range of public participation techniques, this consultation asked the public, patients, service users and staff for their views on how to improve the services provided in the community by the National Health Service and social care;
- the General Medical Council conducted Citizens' Juries to gain views on children's rights when receiving medical care;
- the National Institute for Health and Clinical Excellence has established a Citizens' Council, drawn from the population of England and Wales, to help provide advice about the social values that should underpin the Institute's guidance; and
- the trustees of the BBC Trust keep in close contact with licence fee payers to understand their expectations of the BBC. They do this via research, direct engagement with the public and through the work of the BBC Audience Councils in England, Northern Ireland, Scotland and Wales.

Information

What *Personal Accounts: a new way to save* proposed

59. The White Paper pointed out that all stakeholders agreed that providing good-quality information would be critical to the success of Personal Accounts. At that point it was too early to specify the details of the information products linked with Personal Accounts but the early development work outlined the probable needs of employees, employers, the self-employed and third-party intermediaries.

What the White paper asked

60. The White Paper asked what sort of information should support Personal Accounts, and the responsibilities of different organisations in communicating this information.

What you said

61. Some responses suggested a specific partnership between government and other bodies. Others suggested that information should be made available as soon as possible before Personal Accounts are launched, and that there should be a national

campaign to raise awareness of the new savings system. It was felt that certain groups, particularly women and carers, should be clearly targeted. Some respondents noted that there was a range of high-quality information available, but that availability was not sufficient, as it was having little impact on its target audience.

"The main thrust of this information campaign should probably be undertaken within six to nine months of the introduction of Personal Accounts." (Engineering Employers' Federation)

"Individuals must be put in a position – through education, information and help – where they can make the right choice. The Government must take a leading role in this and ensure the information is clearly targeted." (Association of British Insurers)

"The level and quality of the information will be an essential factor in the success – or otherwise – of Personal Accounts, and of pensions reform in general." (AEGON)

"An important test of the Personal Accounts policy will be whether it is possible to design information and generic advice in a simple and easy-to-understand way to help people decide whether they should opt out of Personal Accounts." (Pensions Policy Institute)

"A number of organisations have a major role to play if all employees are to get access to the necessary information, guidance and advice, including central government, regulators, the Personal Accounts board, trade unions, employers, and consumer groups." (Trades Union Congress)

"We believe the Government should ensure that information provision … is consistent and consumers are able to find information about all forms of pension saving in one place." (Which?)

How the Government will take this forward

62. Clear and high quality information will be critical for individuals to understand the Personal Accounts scheme and the options available to them. The information and communications strategy for Personal Accounts will be a major part of the Delivery Authority's work. We have a wealth of research evidence in place and will continue to build our evidence base to develop customer insight and shape the communication products.

63. The White Paper gave a commitment for the Government to develop an evidence-based information strategy on pensions and Personal Accounts over the course of the year. This will be running alongside the feasibility study examining the provision of a national approach to generic financial advice being led by Otto Thoresen, Chief Executive of AEGON UK, which is to report to Government around the end of 2007. We will continue to engage positively with the review.

64. Generic advice should help individuals understand and engage in the range of options open to them with respect to retirement planning and other financial matters. The wider availability of generic financial advice could be helpful for some individuals who need some help or guidance in understanding their position. This could include those who are automatically enrolled into either a Personal Account or another workplace pension, particularly where an individual may have a range of financial decisions to make.

65. In the period before the Delivery Authority is fully engaged, we are examining the research for key insights and identifying the gaps in our knowledge about an effective information strategy. The objective is to understand what we know already about our target audience and their information needs prior to the authority bringing its expertise to bear on this.

For the longer term we are focusing on:

- creating the right climate for the introduction of Personal Accounts i.e. building understanding and awareness of planning and saving for retirement and what pensions are amongst key groups;

- building confidence in the scheme prior to its introduction. This will require a long term strategy to ensure the correct messages are reaching our target groups and stakeholders to prepare them for the introduction of the new scheme;

- planning the provision of information about the scheme for individuals, employers, industry and the media. This will include messages to aid decision-making around questions such as automatic enrolment, opt-out, investments and decumulation; and

- considering the respective roles of government, the Delivery Authority and other bodies in providing information and communication to support private pension reform and particularly the new requirement to automatically enrol eligible employees.

66. Information will also be critical to support the new compliance regime. The proposed 'educate, enable and enforce' approach will require an integrated programme of information provision to support individuals and employers as the scheme is introduced and delivered.

67. We are aware that the timing of information is critical and are working now with employers to understand the preparations that they will need to make and when information will need to be available. We are also consulting with the public on preferred information products, channels and timing. Information will be inclusive and available in alternative formats, languages and easy read versions, and all information products developed will be thoroughly tested and reviewed by employers and employees.

Chapter 3: Charges and financing

What *Personal Accounts: a new way to save* proposed

- Through Personal Accounts the Government aims to provide people with a simple low-cost way of saving for a pension.
- The Government believes that an annual management charge of 0.3 per cent or equivalent under alternative charge structures, as suggested by the Pensions Commission, is achievable in the long term. In the short term, we expect charges to be comparable with the Commission's estimate when this is adjusted to take account of the likely need to finance the scheme over a shorter timescale.
- In comparison with existing pensions products, we believe that the Personal Accounts scheme will achieve a substantial reduction in charge levels for our target group.

Figure 4: Percentage of consultation responses mentioning charges and financing

Methods of charging

What the White Paper asked

We were interested in hearing views on the appropriate method of charging members for Personal Accounts, and posed a number of specific questions about this.

Which overall charge structure is most appropriate?

What you said

1. Most of the responses suggested that low charges were a key feature for the success of Personal Accounts. Many were in favour of an annual management charge and felt that it would be the most appropriate means of charging members as it was thought to be fair, and was most likely to be the simplest method.

2. Some respondents suggested alternative charging structures: for example, a combination of other charges with the annual management charge, a contribution charge or a joining fee.

"The charge structure should be aimed at groups who do not currently have pension provision. As a result, it should be as low and flat as possible." (Zurich)

"The charging structure must above all be fair and proportionate." (International Financial Data Services)

"The level and structure of the charge should be based on achieving good outcomes for employees; this does not necessarily point to the lowest possible charge." (AXA)

"A flat-rate or tiered Annual Management Charge, as a percentage of the fund under management, would be fair, simple, transparent and easy to understand for the employee." (Co-operative)

"We strongly recommend charging an annual percentage charge on total monies invested in Personal Accounts. Charging a flat fee would disadvantage low earners, a major part of the target group for the Personal Accounts, and therefore not satisfy the requirement that the scheme be fair to all members. Charging a fee on all first-year payments could also discourage this population from saving, as they will initially see a lower return on their contributions. Instead, we believe that an annual charge is the most transparent pricing method available." (JP Morgan)

"A joining fee would be a downright disincentive to some and might act against best efforts to retain entrants." (Re-Connect)

What the White Paper asked

How much flexibility should the Delivery Authority or the Personal Accounts board have in deciding the charging structure?

What you said

3. It was generally agreed that the Delivery Authority should have a certain level of flexibility. Many responses indicated that the Delivery Authority should be able to exercise total flexibility in setting the charge structure. However, some responses argued that there were limitations with all the options.

"It is entirely appropriate for the Delivery Authority to propose, and for the ongoing body to control and maintain, a suitable charging mechanism, as these costs will come directly from employees' Personal Accounts." (British Chambers of Commerce)

"We believe the Delivery Authority should have freedom to levy such charges as they require to cover their costs. However, the existence of such charges should be fully disclosed to ensure transparency and member understanding." (Scottish Widows)

"Either the Personal Accounts Delivery Authority or the Personal Accounts board should have full flexibility in deciding the charging structure." (Pensions Advisory Service)

"The Delivery Authority should have full flexibility in setting charges, within the limits of objectives as expressed in the Paper." (Investment and Life Assurance Group)

"Broadly speaking, the Personal Accounts Delivery Authority must be allowed some autonomy, and should have flexibility in deciding both the charging structure and the level of charges within a framework decided by the Government, following consultation." (B&CE Benefit Schemes)

"If the Delivery Authority and board are to seek to generate significant income, then flexibility in setting charges will be vital to enable charges to be adjusted to reflect actual take-up rates and actual contribution receipts, but that would take away any certainty for members as to what they were being charged." (Gissings)

"Given the interaction with the overall financing of Personal Accounts, we would expect some guidance in legislation for the Delivery Authority and Personal Accounts board. We would advocate that this guidance should be in primary legislation but should leave to the Delivery Authority the exact structure the charge should take." (Prudential)

What the White Paper asked

Are there particular circumstances or activities for which it is appropriate to make an additional charge?

What you said

4. Of those who responded to this question, most felt that there were circumstances where it would be appropriate to make an additional charge. There were very few responses which disagreed with additional charges outright. Most of the respondents felt that any extra charges incurred should be met by those exercising choice, for example by investing in certain funds, or other extra activities such as fund switching.

"In principle, it should be acceptable for additional charges to be levied in specific circumstances, for example on switching funds. No charge should be made for joining and leaving the scheme." (Hargreaves Lansdown)

"To avoid cross-subsidies from the Personal Accounts default and branded funds, it is likely that the board would wish to levy an additional charge for access to third-party branded funds. It may also wish to discourage excessive fund switches by charging beyond a certain number of 'free switches' per year." (Investment Management Association)

"The overall charging structure must recognise that the greatest workload is in establishment of the personal account for any one member, and it would therefore seem to us to be prudent to have some form of initial charge as well as an annual management charge, expressed as a percentage of the fund. A fixed fee would tend to hit smaller funds more than larger funds." (Institute of Directors)

"We recognise that it might be appropriate to make additional charges in a number of circumstances to incentivise members to keep the costs down. We believe that these could include extra charges for active management and branded funds: account holders exercising the choice of branded funds should bear the additional costs of those options … Charges for excessive switching between investment funds: account holders could be allowed a certain number of 'free' switches per year, with all switches above that level prompting an additional charge." (Which?)

"If individuals choose their funds, an additional charge could be incurred as exercise of that choice is likely to increase the fund management costs. However, charging for specific activities may also add complexity and may discourage members from doing what is in their best interests." (Pensions Policy Institute)

> *"We believe that any extra costs that might arise if branded funds are included should be ring-fenced so that there is no cross-subsidy between the default funds and the branded funds. Similarly, if a planholder wishes to switch between funds it may be appropriate that a switching charge is made, provided that it achieves a balance between full cost-recovery and not being so large that it deters switching when appropriate."* (Age Concern)

Additional comments

5. There was also a large number of responses on the level of charges, which were not focused on the specific questions. Some of the responses about the level of charges highlighted the importance of low charges. Others were sceptical that a 0.3 per cent management charge could be achieved.

What you said

> *"We do not believe that a 0.3 per cent annual management charge is possible, at least in the early years, given the wealth of regulation that surrounds schemes."* (SBJ Benefit Consultants Ltd)
>
> *"The Government is raising unreasonable expectations about the costs of the new system."* (Association of British Insurers)
>
> *"We strongly believe Personal Accounts must not be subsidised by the taxpayer to achieve an artificially lower charge. Existing pensions and Personal Accounts will compete against each other, and it is paramount that they do so on an equal footing."* (AEGON UK)
>
> *"Charges and costs of Personal Accounts must not only start low but they must remain at the lowest possible rate throughout an individual's saving experience. The Pensions Commission's estimated aim of no more than 0.3 per cent in the long term should remain the target."* (GMB)
>
> *"Legal & General does not believe that 0.3 per cent will ever be attainable for Personal Accounts, and it certainly offers no prospect of generating later finance to repay the early year strain."* (Legal & General)

Pensions Policy Institute seminar, charging structures for Personal Accounts

"No single charging structure, or combination of structures, has all of the desirable attributes." (Pensions Policy Institute)

The Pensions Policy Institute held a seminar on charging structures for Personal Accounts in March 2007, co-sponsored by the Department for Work and Pensions, AEGON and Standard Life.

The Pensions Policy Institute presented its research findings which evaluated different structures against Government criteria. They looked at a variety of possible charging structures including:

- annual management charges;
- a joining charge and an annual management charge;
- an annual flat fee;
- a contribution charge; and
- a contribution charge and an annual management charge.

The Government's suggested five criteria used to evaluate the different charging structures were:

- fairness to all members, taking into account an individual's ability to pay;
- provides significant revenue in the early years of operation, reducing the amount and length of operating losses, and reducing financing costs;
- simple and easy to understand;
- incentivise members to help keep costs down; and
- incentivise the scheme operator to maximise the fund value.

The research found that, overall, no single charging structure, or combination of charging structures, has all of the desirable attributes. Each charge structure has advantages and disadvantages and there are trade-offs that have to be made.

www.pensionspolicyinstitue.org.uk

How the Government will take this forward

6. The structure and level of charges in the Personal Accounts scheme is extremely important for both scheme members and the wider pensions industry and we are grateful for the responses we have received. There are a number of factors that will influence decisions on this issue, not least the final design of the scheme, the costs incurred in setting up the scheme and the commercial arrangements with any potential suppliers. Many of the decisions relating to these influencing factors will lie with the scheme rather than with government.

7. In light of the responses we have received and in recognition that the relevant knowledge, skills and expertise will lie within the scheme, we have decided the scheme is best placed to make decisions relating to the charging structure, the level of charges and any additional charges for particular services in the Personal Accounts scheme.

8. Trust law requires trustees to act prudently and in the best interests of members. Since members bear the costs of higher charges, there will be a clear incentive for the scheme to set a charge structure that is fair and to keep charges down.

How the scheme will be financed

What you said

9. The White Paper did not specifically ask about funding of either the Delivery Authority or the Personal Accounts scheme; however, a number of responses commented on this.

> *"An important principle to observe will be that those people that join Personal Accounts from the start should not bear an unreasonable burden of the start-up costs of the scheme."* (Which?)
>
> *"The flat annual management charge means big losses for the administrator and the fund manager in the early years, with profits only in the later years. Therefore support is necessary from government in those early years and a guarantee that there will be sufficient time for the costs to be recovered before any new tendering process, e.g. for a change of administrator, is allowed."* (International Financial Data Services)
>
> *"We strongly believe that there should be no taxpayer subsidy of the operation of Personal Accounts, including building the infrastructure needed for delivery. Any taxpayer subsidy would imbalance the market for workplace pensions in an unacceptable way. It would also be important that any financing required was on a commercial basis to avoid being anti-competitive."* (Prudential)

How the Government will take this forward

10. In taking forward our private pension reforms, some costs will arise in relation to the set up of the Personal Accounts scheme, for example the development of the collection process, and there will be other costs which relate to other aspects of the reforms such as the requirement to automatically enrol all eligible employees into a workplace pension. These will be distinct strands of work.

11. It would not be correct for members to bear costs unrelated to the scheme. Equally, the Government has no intention of unfairly subsidising the Personal Accounts scheme with taxpayers' money. We will continue to develop our funding strategy further over the coming months.

12. Funding for the Delivery Authority in its initial advisory stage will come from government, and paid as grant-in-aid. This will be the Authority's only source of funding and it will not need an additional external source of finance.

13. The Government's intention is that the Personal Accounts scheme will, in the long term, be self-financing through member charges. We are still developing the funding requirements of the scheme and there are a number of sources to consider from which finance can be obtained. We are assessing a wide range of potential financing arrangements and their implications for members, government and potential suppliers.

14. In the short term, there will be costs associated with the scheme and the Delivery Authority in its executive stage. These will inevitably arise before significant revenues from member charges are available. There will, therefore, be a requirement for financing to meet these initial costs.

15. The White Paper advised that there were a number of possible sources which could provide finance for the scheme, for example government, suppliers such as pension providers or administrators, and third parties such as banks.

16. A number of responses have raised the issue of the impact that any state financial support for the Personal Accounts scheme might have on its competitiveness in relation to other pension products. The responses comment that state support of this nature would artificially reduce the costs faced by the scheme, thereby subsidising scheme members at the expense of the general taxpayer and giving an advantage to the Personal Accounts scheme over provision currently available to individuals.

17. We recognise that the Personal Accounts scheme should not receive state support that gives it an unfair competitive advantage over other pension providers. It is the Government's intention that costs related to the set up and operation of the Personal Accounts scheme will not be subsidised by taxpayers.

18. Any funding solution for Personal Accounts will take into account the need for low charges for members, value for money for taxpayers, commercial viability and the impact on industry, and will comply with European Union public procurement and legislation on competition.

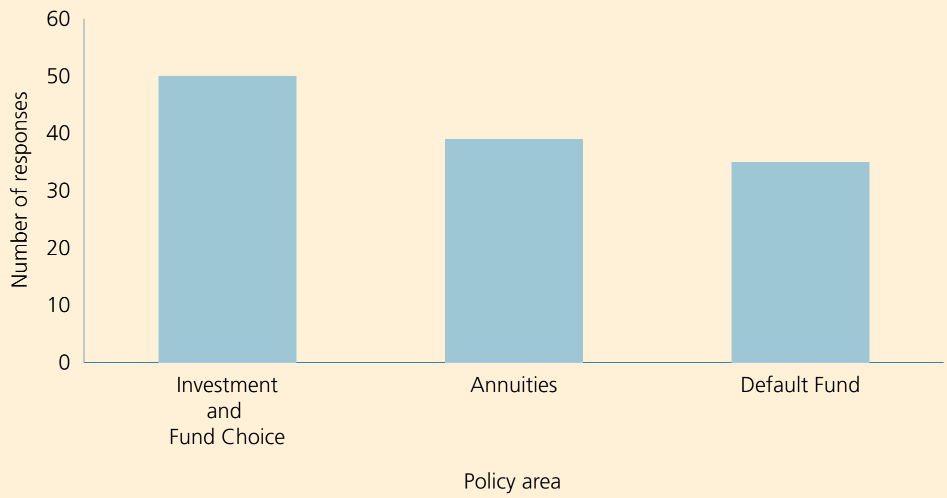
Chapter 4: Investment and accessing savings

What *Personal Accounts: a new way to save* proposed

- Personal Accounts will offer a default fund into which members will be enrolled if they do not exercise choice.
- The executive Delivery Authority will design the investment strategy within a general framework set by the Government.
- Personal Accounts will work within the current tax framework: most people will annuitise.

Responses

Figure 5: Number of consultation responses on investment and accessing savings



Investment

What you said

1. There were no specific consultation questions about investment. Of those responses which mentioned investment or funds, the majority agreed that the design of the default fund would be very important.

> *"We welcome the commitment that the Delivery Authority and Personal Accounts board will design the fund options based on consultation with people in the target group."* (Carers UK)
>
> *"We welcome the commitment in the White Paper to design the default fund to deliver an appropriate trade-off between risk and return. Ensuring the default option is* (relatively) low risk will facilitate generic advice provision and ensure personal account holders with low levels of financial literacy are not disadvantaged." (Fawcett Society)
>
> *"Which? has argued that consumers would be confused by unlimited choice, and … what is needed is managed choice with a limited number of funds."* (Which?)

How the Government will take this forward

2. We have been considering this issue further since publication of the White Paper. Personal Accounts will be a trust-based occupational pension scheme, with the legislative foundation of trust law. As such, the scheme trustees will be ultimately responsible for investment decisions. This mirrors practice in other defined contribution occupational pension schemes and will utilise the knowledge, skills and experience of the scheme trustees.

3. We anticipate that the Personal Accounts Delivery Authority will do much of the preparatory work on drawing up a proposed investment strategy. The trustees responsible for investment decisions will be appointed in advance of the scheme launch so that they can review this proposed strategy and make the final investment decisions.

4. We expect Personal Accounts to offer a default fund for members who do not wish to exercise choice and a wider range of funds, which we expect to include social, environmental and ethical investments, and branded funds.

Accessing savings

What you said

5. There were no specific consultation questions about accessing savings but there was broad agreement that the process of buying an annuity was important, that it must be fully explained to scheme members, and that it should be subject to the same rules as for any defined contribution scheme.

> *"Exercise of an open market option is important, but there are many developments occurring in this area which may make a conventional annuity choice simplistic."* (Investment and Life Assurance Group)
>
> *"The fact that an annuity guarantees an income for life, however long, and the impossibility of doing that for yourself on a non-pooled basis, must be communicated."* (Legal & General)
>
> *"We welcome and share the Government's belief that annuities are the best way for consumers to protect themselves from the risk of outliving their retirement savings. We are keen on developing and advocating decumulation solutions for both the Personal Accounts and non-Personal Accounts markets, and believe that, in principle, those solutions should be the same."* (Prudential)

How the Government will take this forward

6. We announced in the White Paper that Personal Accounts would be subject to the same tax rules as other tax-favoured pension schemes. Tax relief will be provided on contributions to Personal Accounts under the simplified tax regime introduced in April 2006 to encourage individuals to save for an income in retirement. In return, the same rules will apply to how the accumulated pension fund will be converted into a regular of income in retirement:

- income from Personal Accounts cannot be accessed until the scheme member reaches 55 years of age and income must be secured by the time that person reaches 75 years of age;
- a quarter of an individual's total pension fund will be available as a tax-free lump sum;
- an individual with a total pension accumulation of less than 1 per cent of the lifetime limit (£16,000 in 2007/08) will not be required to secure their income by purchasing an annuity and can take their pension as a taxable lump sum; and
- if an individual dies before age 75 without accessing their pension savings a pension or lump sum will be payable to dependants.

7. It will be the responsibility of the Delivery Authority, in consultation with the scheme trustees, to develop detailed processes by which individuals will access their savings. These processes will be developed in the light of the review of the 'open market option' announced by the Government in the 2006 Pre-Budget Report. Working with key stakeholders, the review will look to improve the outcomes for people buying annuities by improving the operation of the open market option to ensure more people get a better deal. We expect final conclusions to be reached on this review by the end of the year.

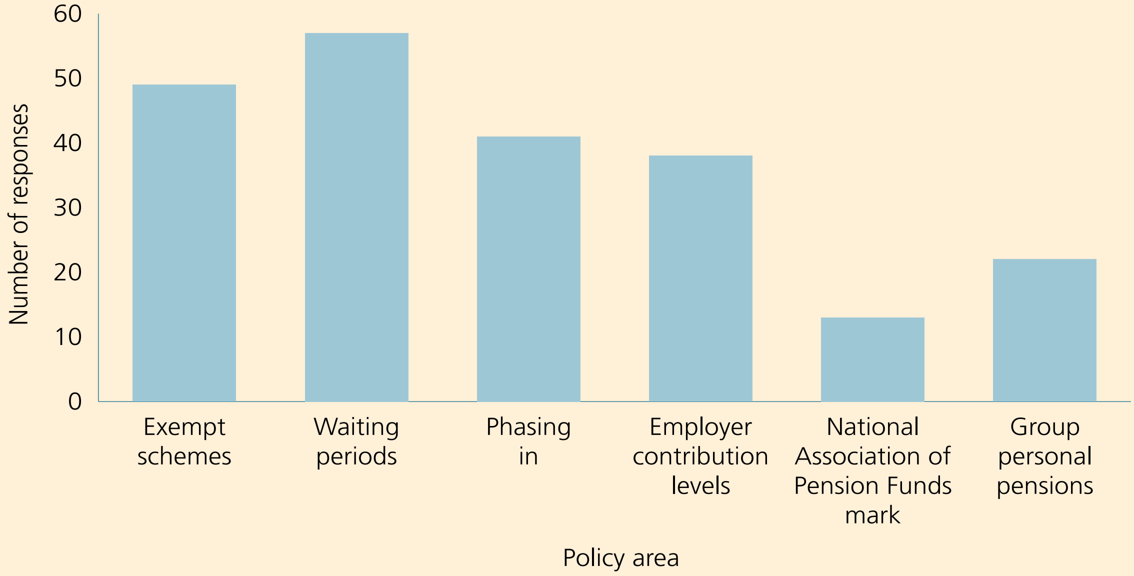
Chapter 5: Employers and private pension reform

What *Personal Accounts: a new way to save* proposed

- The Government's aim is to support existing good quality pension provision.
- The Government is committed to designing Personal Accounts so that employers already providing good pension schemes for their staff can manage the potential costs of automatic enrolment and re-enrolment. This should allow them to avoid any sudden and unexpected increases in costs that could lead to them to withdraw from their current pension provision.
- The Government will consult on how the reform might be phased in for employers with qualifying schemes to help them manage costs and on whether more generous schemes should be able to operate waiting periods.
- To help support existing provision, there will be simple tests of scheme quality that will enable employers to offer existing schemes instead of or alongside Personal Accounts. The tests will be based on those already in existence, and where possible qualification will be through self-certification.

Responses

Figure 6: Number of consultation responses on employers and private pension reform



Employer policy: looking forward

1. The Government recognises that employers will be affected both by the policy framework, set out in this response and previous White Papers, and by the business operations designed for the reforms. We believe the policy framework is based soundly on the available evidence and strikes a balance between minimising burdens on employers and enabling individuals to build up meaningful savings. We will continue to ensure the design is such that burdens on employers are minimised. The Government and the Personal Accounts Delivery Authority will take forward work to deliver on this. At this stage, rightly, the business process for employers is not yet decided. As with all large reforms, the Government will continue to keep the policy framework in this chapter under review in the light of cumulative burdens on employers, new evidence, and changing market contexts as we move closer to delivery. This should ensure that our reforms remain coherent and meet our objectives whilst minimising the impact on employers.

Waiting periods within Personal Accounts

What *Personal Accounts: a new way to save* proposed

2. In the December White Paper, the Government stated that it was not proposing a formal waiting period in Personal Accounts, although it recognised there would be a short administrative period before the automatic enrolment process was completed. It sought views on this approach.

What you said

3. The majority of responses were in agreement that there should be no waiting period for Personal Accounts and often cited that those who change job frequently might not be able to save if there was a waiting period. Those who supported a waiting period cited the administrative burden caused for employers by individuals who leave employment after a short period of time.

"The EEF supports the Government's view that there should not be a waiting period for personal accounts" (Engineering Employers' Federation)

"EOC is pleased that the Government is not proposing a formal waiting period. Auto-enrolment is a key benefit and for it to work Government needs to minimise the potential for opt outs." (Equal Opportunities Commission)

"The FSB strongly believes that there should be a waiting period of at least six months before an employee is auto-enrolled. There must be the correct balance between burdens and reaching the target group of the reform." (Federation of Small Businesses)

"The BCC wishes to see enrolment into Personal Accounts once an employee has completed their probationary period." (British Chambers of Commerce)

"A waiting period would result in many people, particularly vulnerable people and those on low incomes, missing out on the benefits that the Personal Accounts system will bring." (B&CE Benefit Schemes)

"Given that the employer's contribution effectively forms part of the employee's remuneration, we believe that employees should be entitled to the contribution regardless of their length of service." (Mercer Human Resources Consulting)

How the Government will take this forward

4. The Government remains of the view that there should be no formal waiting period for Personal Accounts. This view is supported by a wide range of commentators including consumer interest groups, the pensions industry and some employers. It is important for our target group to begin saving as soon as they are employed. The introduction of a waiting period would have a significant impact on the target group in that it would:

- adversely affect individual outcomes;
- disadvantage short-term and seasonal workers;
- affect participation rates; and
- create perverse labour market incentives.

5. We recognise that some employers are concerned about automatically enrolling short-term employees. Many of these employees are a key part of our target group of people who could reasonably save for a better income in retirement. The expectation therefore will be for employers to automatically enrol eligible workers into Personal Accounts from the first day of employment. We will however continue to keep this approach under review. It is recognised that there may also need to be a short period before contributions are made to allow individuals the opportunity to opt out.

Waiting periods and other qualifying schemes

What the White Paper asked

Whether employers with exempt schemes, with contributions or benefits that are higher than the minimum level, could operate a short waiting period, of perhaps three or six months, to encourage them to continue to offer high-quality schemes?

What should be the minimum level of scheme contributions above which a waiting period is acceptable should be?

What you said

6. Consultation responses broadly supported a waiting period for employers offering higher contributions or benefits. A few responses felt that a tiered system was too complicated and that qualifying schemes other than Personal Accounts should not have a waiting period so that there was complete alignment. Most other responses supported the proposition of allowing high quality qualifying schemes to operate with

a waiting period. There was no preference on the duration of this period, but most suggested that between three and six months would be appropriate.

> *"The Government should allow exempt schemes offering high-value contributions to operate short waiting periods of three to six months."* (National Association of Pension Funds)
>
> *"Employers with an occupational pension scheme that meets the criteria for exempting them from having to automatically enrol their employees into Personal Accounts should be able to have a short waiting period of between three and six months."* (Engineering Employers' Federation)
>
> *"We agree that employers with exempt schemes that are higher than the minimum should be allowed to operate a short waiting period. This would be particularly helpful to those employers with high turnover rates of staff."* (AEGON UK)
>
> *"A waiting period would only be acceptable where scheme contributions were superior to those of the Personal Accounts scheme. If not, an employee would (1) miss out on contributions for several months of service and (2) obtain lower contributions once access was finally granted to the employer's pension scheme."* (JP Morgan)
>
> *"We would therefore strongly urge the Government to allow occupational schemes to be able to set a waiting period of 6-12 months more than that for Personal Accounts, provided the scheme is good enough to meet the Government's definition of a good scheme."* (Tesco)
>
> *"Allowing a short waiting period for exempt schemes with contributions that are higher than the minimum level could encourage employers to continue to offer good-quality schemes."* (Which?)

How the Government will take this forward

7. The Government has explored the options in the light of employer costs, individual savings and equal treatment legislation and has decided that an appropriate balance between supporting employers and ensuring employees can accrue savings quickly would be to allow employers who offer higher contributions or benefits to operate a three month waiting period. The intention is to support those employers who already provide or intend to provide higher value contributions or benefits by allowing them to manage their costs over a period of time rather than incurring an immediate increase in costs.

8. We recognise that a waiting period may make it more difficult for those target group employees who frequently change jobs to accrue a pension fund. We have aimed to limit the impact of this by restricting this to employers who provide significantly higher contributions or benefits to their workers.

9. We will continue to engage with stakeholders on how to apply this policy effectively and minimise any administrative burden. We will also need to establish a method for setting the higher contribution (and equivalent benefit) level. An important principle we are considering is that members should be able to accrue a pension of equal or better value to Personal Accounts within the first year of saving.

The National Association of Pension Funds' Quality Mark

10. The National Association of Pension Funds, in the period before the White Paper last December, raised the idea of linking a waiting period for high quality schemes to a proposal for its Good Pensions Quality Mark.

What you said

11. A number of responses mentioned the National Association of Pension Funds idea of a Quality Mark for good occupational schemes.

> *"The Government is also consulting on an appropriate benchmark 'test' for permitting a waiting period … CBI members have not expressed strong opinions as to what this figure should be, although members said such a benchmark test should not be linked to the National Association of Pension Funds' proposed quality mark."* (Confederation of British Industry)
>
> *"For the employer it would enable them to demonstrate that they are offering a pension of better value than the Personal Accounts minimum and for the employee it would allow them to identify employers offering a good pension."* (National Association of Pension Funds)

How the Government will take this forward

We welcome the efforts of the National Association of Pension Funds to lead the industry in developing a Quality Mark and believe that it could help members to appreciate the value of their employers' pension schemes. We want to reassure employers that a quality mark would not be used to raise minimum standards. That is why we want the mark to be owned and supported by the industry and employers themselves.

Qualifying schemes and phasing in

What the White Paper asked:

How to ensure that employers with exempt schemes have the flexibility to manage the implementation of these reforms in the same way as employers who will operate Personal Accounts, for example by:

- ***phasing in the minimum employer contribution or levels of accrual for exempt schemes over three years or an appropriate period;***
- ***phasing in by groups of employees; or***
- ***some other approach?***

What you said

12. Responses were divided on this issue. Some suggested that phasing in for other qualifying schemes should replicate the arrangements for Personal Accounts to avoid complexity and confusion. Others recommended that employers should have the flexibility to choose which framework is appropriate to their operations rather than have the Government fix one standard for all qualifying schemes.

"A 'big bang' approach would be fair across all employees, but could result in difficulties for the employer, particularly in small and/or family-owned businesses. As such, a gradual phasing in of minimum employer contribution for all employees would seem to be the fairest approach for all concerned parties." (JP Morgan)

"We welcome the phasing in of the contribution, but believe that it does not go far enough to counterbalance the negative impact this is going to have on small employers. We urge Government to reconsider a five-year phasing in period." (Federation of Small Businesses)

"EOC supports the Government's proposal that alternative schemes should not have a longer phasing period than Personal Accounts." (Equal Opportunities Commission)

"Consumers should not be unreasonably disadvantaged by any phasing in of minimum employer contributions." (Which?)

"We are not convinced that phasing in accruals, for example, would add any real benefit, since this implies a change in scheme design to provide lower accruals for certain groups." (Gissings)

How the Government will take this forward

13. In the December White Paper the Government proposed to phase in the minimum employer contribution for Personal Accounts over three years. We welcomed views on whether this was the appropriate period. In the consultation smaller businesses favoured a five year phasing in period. While we recognise that a longer period reduces total costs to employers, a balance has to be struck with the need for individuals to accrue savings and with the desirability (both for employers and administrators) of reaching steady state of delivery in a reasonable time scale. It remains therefore the Government's intention to provide for a three year, rather than a five year, phasing in period for the employers' contribution for Personal Accounts.

14. On balance, the concept of phasing by contributions received the greatest support but responses were mixed. We have therefore explored a full range of options in terms of employer costs, delivery costs and individual outcomes and decided that qualifying defined contribution schemes should phase in by contributions (along the same lines as Personal Accounts); and qualifying defined benefit schemes should phase in by employee group.

15. Phasing in contributions for defined contribution schemes will be relatively easy for employers to implement and is aligned with Personal Accounts. All employees will be enrolled immediately when automatic enrolment commences and will therefore build up pension benefits from that point. Employers running defined contribution schemes will be able to smooth their costs under this option, as the contributions will gradually increase during the phasing period.

16. For defined benefit schemes, phasing in by contributions or accruals would make it difficult to meet the funding requirements, or the Reference Scheme Test in the case of contracted-out schemes; and would be disproportionately complex to administer. The option of phasing in by employee group is simpler. The intention would be for employers to automatically enrol all new and previously ineligible employees at the start of the phasing in period and to have automatically enrolled all previously eligible non-joiners by the end of the period.

17. We will continue to engage with stakeholders on how to make the phasing period and method work best for all employers. We will keep the approach to the phasing period under review. We will also ensure that we apply the appropriate phasing-in framework for employers with hybrid pension schemes (schemes that provide a mix of defined benefit and defined contribution pensions).

Hybrid schemes

What the White Paper said

18. The White Paper stated that we would look at how the qualifying tests could be adapted for employers who have chosen to provide hybrid schemes.

How the Government will take this forward

19. In the White Paper we committed to consult with pensions professionals and employers about how hybrid schemes would be able to meet the qualification criteria. Employers sponsoring hybrid pension schemes will be able to choose as to whether to apply the qualifying test for defined benefit schemes or the test for defined contribution schemes or an appropriate combination depending on the nature of their scheme. To provide both employers and individuals with assurance that the more complex schemes pass the test, we are considering how we might establish a set of key factors that must be taken into account in identifying which test to apply; how the tests might be applied; and also when it may be essential to seek professional advice before certifying the scheme.

20. The Government is committed to minimising burdens on business and believes that in most cases employers, supported by their advisers, will be best placed to decide on the appropriate test to apply to their scheme. This approach avoids prescriptive legislation and builds on the proposed defined benefit and defined contribution qualifying tests which have been broadly welcomed by stakeholders.

More information on the scheme qualification tests

Refining the scheme qualification tests

21. Automatic enrolment is the most effective way of increasing participation while still preserving choice for those who do not wish to save. In the White Paper we said that in order to qualify, schemes would be required to automatically enrol eligible workers. In practice this would have required schemes themselves to identify eligible workers and undertake automatic enrolment activity. This might have placed a requirement on schemes at odds with their duty to existing members, for example by requiring a scheme with restricted eligibility to grant access to a much wider group of workers. It would also have separated the requirement to automatically enrol from the requirement placed on employers to provide a minimum contribution or equivalent benefit for eligible workers.

22. We have therefore decided to clarify that there will be an overarching requirement on the employer to automatically enrol eligible workers into a qualifying occupational pension scheme. By placing the requirement to automatically enrol on the employer

rather than the scheme, the employer retains control of the pension arrangements on offer to the workforce. It also helps with monitoring compliance because the employer is responsible for ensuring that all of the eligible workers are accounted for.

23. The White Paper stated that, in order to be a qualifying scheme, a defined contribution scheme would need to provide equal or better benefits than Personal Accounts. We have decided that a scheme will have to be certified as providing minimum contributions of 8 per cent (with a minimum 3 per cent employer contribution) on band earnings for each individual rather than compared with the average contribution going into the scheme. This will ensure that all workers receive the minimum level and the test is not distorted by members with high contributions cross-subsidising those with contributions below the minimum. The defined contribution qualifying test will therefore change from a scheme average test to a scheme minimum test. We believe this is a technical clarification and does not diverge significantly from the understanding and consensus among employer stakeholders. We do not expect this change to place any additional administrative burden on employers in certifying their schemes.

Non-occupational workplace pension provision

What the White Paper asked

How can the Government treat non-occupational workplace pension arrangements as schemes for the purposes of exemption from Personal Accounts requirements?

How can the Government ensure that, in the absence of automatic enrolment, these vehicles can offer similar levels of coverage and saving similar to those estimated for automatic enrolment?

What you said

24. Most of the responses came from pension providers who currently provide workplace personal pension arrangements for employers, and most suggested that there was no straightforward solution to these questions.

"Full automatic enrolment should apply to all workplace pension arrangements. The Government should either redefine GPPs and stakeholder pensions as occupational Pension Schemes or require employers to amend employment contracts." (National Association of Pension Funds)

"The Government should therefore, as its primary objective, ensure that the provisions of the Distance Marketing Directive (DMD) do not apply to GPPs or group stakeholder schemes where there is an employer contribution of at least 3 per cent of earnings." (Association of British Insurers)

"In the absence of automatic enrolment under Group Personal Pensions (GPP), the BCC would suggest that GPP providers obtain an opt-out statement from the prospective member on entry to the GPP." (British Chambers of Commerce)

"The Government should ensure the provisions of the Distance Marketing Directive (DMD) should be interpreted to not apply to any contract-based pension arrangement where there is an employer contribution of at least 3 per cent of band earnings. This will allow contract-based arrangements to employ automatic enrolment." (AEGON UK)

"The June 2005 the Department for Work and Pensions guidance on automatic enrolment does suggest that some form of automatic enrolment could be used for contract-based schemes and we would recommend that this approach be investigated further." (The Co-operative)

"There is a particular concern with the variable quality of 'non-occupational' workplace pension provision such as group personal pensions." (Trades Union Congress)

"Continue to see a role for these schemes (GPPs and Group SIPPs) in the aftermath of 2012, although they will need to meet a number of tests to ensure that they deliver appropriate pension provision for consumers." (Which?)

How the Government will take this forward

25. The Government recognises that workplace personal pension arrangements, such as Group Personal Pensions and Group Stakeholder Pensions, form a significant and valuable part of the existing pensions market and is keen to see these arrangements continue in the run-up to 2012 and beyond. However, we want to ensure that any decision regarding exemption for employers operating such arrangements from Personal Accounts requirements balances the twin aims of supporting the continuation of high-quality existing pension arrangements and ensuring sufficient coverage and savings levels for employees.

26. Since the publication of the White Paper, we have engaged in detailed discussions with a range of interested parties to better understand the issues involved. We have received a variety of suggestions and analysis from our stakeholders. There were two broad themes to the suggestions we have received:

- firstly that we should seek to pass domestic legislation to enable automatic enrolment into personal pension arrangements; and
- secondly that we should allow workplace personal pension arrangements to gain exemption from Personal Account and automatic enrolment requirements based on alternative joining mechanisms that would be acceptable under European law.

European law requirements

27. European law prohibits inertia selling of financial products,[6] including personal pensions. This means that it is not possible to automatically enrol individuals into work place personal pension arrangements.

28. We have received suggestions relating to altering domestic law as a means of overcoming the need to comply with European law:

- amend domestic legislation to reclassify workplace personal pension arrangements as occupational pensions in order to enable employers to use automatic enrolment in such arrangements; or
- pass an overriding domestic law that permits any employer to automatically enrol their employees into a workplace personal pension arrangement as part of the general terms of employment, thereby removing the need to obtain written consent from individual employees.

29. We do not think that these are viable solutions because legally no amendments to domestic law will nullify the application of European law. The domestic definition of a pension arrangement or employment process will not prevent analysis under European law as to the nature of the arrangement. We think that such an analysis would result in the arrangement in question being considered a personal pension and the suggested enrolment process being inertia selling. Therefore, we do not think that the suggested solutions resolve the issue.

Alternative joining mechanisms

30. The Government is considering the effectiveness of alternative joining mechanisms for workplace personal pension arrangements that are compliant with European law to see whether this could provide a workable solution. While this option looks promising, there are a number of aspects which we are keen to better understand:

[6] Inertia selling is the provision of unsolicited services with a demand for payment

- What is the best enrolment mechanism for ensuring that participation and contribution levels in workplace personal pensions are comparable to what they would be under pure automatic enrolment?

- How can we frame such a requirement in legislation in a way that encourages employers to maximise pension participation among their workforce whilst allowing sufficient flexibility for such employers to choose the most suitable processes for operating their pension arrangements?

31. Additionally, the Government is keen to explore how existing products and services within the current pensions market could be utilised further in order to complement workplace personal pension arrangements both in the run-up to 2012 and beyond. We are interested in views on:

- What potential there is for the development of corporate trust services and multi-employer master trust schemes in order for occupational pension arrangements to complement workplace personal pension arrangements?

32. The Government will continue to work closely with stakeholders on these challenging and important issues in the run-up to the second Pensions Bill and thereafter in the years leading up to implementation in 2012. We are keen to find a pragmatic solution to this issue.

Other issues which were not specific questions

Support for employers

What you said

33. Most responses were supportive of the proposals that had been put forward to help employers adjust to the new requirement and increased costs. A number of responses called for the Government to provide small employers with some direct financial assistance.

34. The Confederation of British Industry and the Federation of Small Businesses suggested that the Government should reimburse smaller employers for a proportion of their pension contributions to Personal Accounts.

"BCC urge the Government to realise the financial impact such a scheme would have on small businesses …" (British Chambers of Commerce)

"Funds must be set aside by the Government to educate and train employers of their responsibility." (British Chambers of Commerce)

"To achieve the necessary buy-in from employers there needs to be assurance from Government that some form of financial assistance will be available." (Federation of Small Businesses)

"EEF considers that the provision of [this] initial financial assistance would demonstrate that the Government has recognised that many smaller employers will have to cope with the additional cost of making and administering pension contributions." (Engineering Employers' Federation)

How the Government will take this forward

35. The Government's priority is to ensure that Personal Accounts are designed in a way that minimises employer burdens. The question of any direct fiscal support must be a decision for future governments based on the fiscal position at the time.

36. The Work and Pensions Select Committee recognised that the costs of support packages suggested by several employer representative bodies were prohibitive and has recommended that the Government invest in making the scheme as simple and cheap for businesses to administer as possible, rather than subsidising employer contributions.

37. Minimising the overall burden on employers remains a guiding principle in the development of Personal Accounts policy. Therefore our proposals include:

- not requiring employers to choose the fund or give advice;
- setting out the level of the minimum employer contribution in primary legislation;
- phasing in the minimum employer contribution over three years;
- introducing simple and straightforward qualifying tests for schemes that can be used for automatic enrolment;
- enabling employers offering qualifying schemes with higher levels of contribution or benefits to enjoy a three-month waiting period before they are required to automatically enrol their workers; and
- developing a light touch but effective compliance regime.

Minimising the burden on employers

We have undertaken an extensive series of consultation events with employers and representatives of small businesses to understand the impact of these reforms and help inform the design of Personal Accounts; this process will continue. We have also undertaken, and published, research into employers' attitudes to Personal Accounts and will continue to develop our understanding of how employers will engage with Personal Accounts in the period before implementation.

The Government has also set up the analytical group mentioned in paragraph 1.23 of the Regulatory Impact Assessment to *Personal Accounts: a new way to save.* The group has the remit of examining estimates of the compliance and other administrative burdens associated with Personal Accounts proposals.

38. The administrative cost of Personal Accounts will, of course, depend on the processes for employers. The Government will continue to ensure that the design of Personal Accounts minimises the burdens on employers. This is one of the principles that the Personal Accounts Delivery Authority must have regard to in meeting its objectives. At this stage, rightly, the business process for employers is not yet decided. The findings of the group will feed into policy design and the work of the Delivery Authority. Estimates of the administrative burden on employers that take into account the work of the expert group will be reported in full later this year. For the longer term, the establishment of the employer panel (see Chapter 2), which will represent the views of employers to the Personal Accounts scheme trustees, will ensure that minimising employer burdens remains a key principle for the scheme.

Collection of contributions

What you said

39. Most responses wanted the Government to explore using existing Her Majesty's Revenue & Customs' Pay As You Earn systems to facilitate the collection of Personal Accounts contributions. This was because the Pay As You Earn system used for tax and National Insurance collection is one employers are already familiar with and avoids the need to deal with a new collections process.

"There is a strong case for HMRC involvement in the collection of contributions." (Age Concern)

"It is essential that for employers the interaction with Personal Accounts is simple and uncomplicated. A close alignment to existing National Insurance/tax collection would be desirable so that it is possible for all employers to engage with Personal Accounts even if they offer schemes that are exempt." (Equal Opportunities Commission)

"In our view therefore, the involvement of HMRC should not be ruled out at this point even though it may be a longer-term ambition than full introduction in 2012." (Investment Management Association)

"The FSB feels very strongly that to minimise duplication and to make the administration burden as simple as possible PAYE should be the vehicle used for administration and collection of pension contributions." (Federation of Small Businesses)

How the Government will take this forward

40. We recognise that in making payments to the Personal Accounts scheme, employers will want to use existing infrastructure and processes which they are familiar with, and that Her Majesty's Revenue & Customs systems have been identified by many stakeholders as an obvious choice. The Government is continuing to explore options. However, at this stage we believe there are significant obstacles to using Her Majesty's Revenue & Customs systems as the collection mechanism for Personal Accounts.

41. Although, Her Majesty's Revenue & Customs intends to modernise the Pay As You Earn system, the inherent time lag in the exisiting system means that is unlikely to be suitable for Personal Accounts. The Pay As You Earn system requires employers to pay over the money they have deducted every month, but does not require any information about that money to be reported until after the end of the financial year to which it relates.

42. Using this system, contributions to Personal Accounts could not be allocated to the individual's choice of fund until the information identifying their individual contributions was provided to the Personal Accounts scheme up to 18 months after it had been deducted. It would also be impossible, without adding significant information requirements, to identify when in the year any particular contribution had been made, and the precise return on each individual's funds in the period prior to investment.

43. This delay would also mean that there was no validation of who the payment related to when made. For Personal Accounts, there would need to be extra processes for handling contributions where the payment cannot be matched to an individual. The planned modernisation of the PAYE system will not, on its own, result in it meeting the needs of Personal Accounts.

44. One of the core principles driving work on the delivery of Personal Accounts is that burdens on employers are minimised. The Government will therefore continue to review all the options and will work with the Personal Accounts Delivery Authority to design a collection process that minimises costs to employers. The objective will be to align with employer processes as far as possible and be compatible with exisiting payroll processes and systems, best practice and IT functionality.

45. In conclusion, the Government's current view is that Pay As You Earn is unlikely to meet the core requirements for Personal Accounts. However, the final decision on this issue will be made on the basis of an appraisal of the risks, costs and benefits of the options available, as part of wider impact assessment work.

Chapter 6: Compliance

What *Personal Accounts: a new way to save* proposed

1. From 2012, employers with workers based in the United Kingdom will be responsible for automatically enrolling all eligible employees into an occupational pension, either the proposed new Personal Accounts scheme or a qualifying alternative workplace scheme. In the case of defined contribution schemes, such as Personal Accounts, there will be a minimum employer contribution of 3 per cent in addition to the contributions made by participating employees.

2. In last December's White Paper, the Government noted that these reforms introduce important new rights for employees and requirements for employers. While we recognise that the majority of employers will comply with their new obligations, there is a risk that a significant minority might not do so.

3. There will need to be a compliance regime capable of effectively safeguarding those rights while at the same time imposing no unnecessary burdens on employers. The Government therefore proposed a three-stage compliance strategy of educating employers and employees about the new requirements and rights, enabling employers to comply with them and where necessary taking proportionate enforcement action. The regime will be developed with full regard to the principles of good regulation as detailed in the Legislative and Regulatory Reform Act 2006 and Hampton Principles.[7]

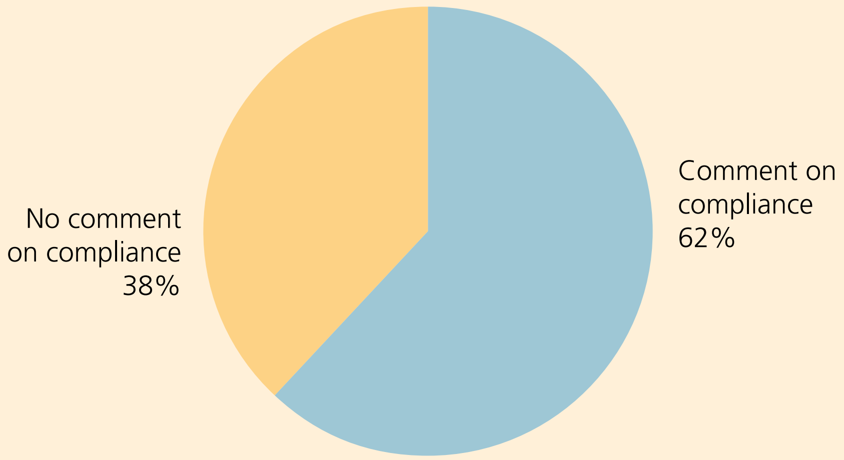
> *"The compliance regime should be light-touch, based on education, enablement and enforcement, and include proportionate penalties."* (National Association of Pension Funds)
>
> *"EEF is pleased that the Government has confirmed in the White Paper that it will be adopting 'a light-touch, risk-based and proportionate' compliance regime."* (Engineering Employers' Federation)
>
> *"On the whole the FSB is generally supportive of the proposed compliance regime. The FSB believes that a light-touch compliance regime, with appropriate penalties for non-compliance is the right approach."* (Federation of Small Businesses)
>
> *"The BCC welcome the proposed 'light-touch' compliance approach to establishing Personal Accounts."* (British Chambers of Commerce)

[7] The Hampton Report *Reducing Administrative Burdens: Effective Inspection and Enforcement*, March 2005 set out seven principles of good regulation

> *"We support the Government's approach of using light-touch compliance and of only using enforcement after 'education' and 'enablement' have been tried, on the basis that most companies will want to do the right thing for their members."* (Tesco)

4. The White Paper posed a number of specific questions about the design of the compliance regime; this chapter sets out how people responded and how the Government intends to take this work forward.

Figure 7: Percentage of consultation responses mentioning compliance



Designing the compliance regime

What the White Paper asked

How can employees who choose to save in Personal Accounts best be protected from suffering detrimental treatment by their employers compared with those who opt out?

What you said

5. Many highlighted the importance of an effective regime that does not place undue burdens on employers, but some employee and consumer representatives drew attention to specific risks around the opt-out decision.

"The Government must also make provisions to ensure that employers do not evade their responsibilities to employees by … putting pressure on staff to opt out of the pension scheme." (Trades Union Congress)

"The Government should take steps ... to ensure that employees are not being put under undue pressure or given incentives to opt out inappropriately." (Age Concern)

"Which? supports a proportionate and effective compliance regime to ensure that consumer rights are safeguarded." (Which?)

How the Government will take this forward

6. It is vital that individuals are free to make the choice as to whether or not to become a member of Personal Accounts or an alternative qualifying scheme without interference.

7. We have therefore been exploring how employees can best be protected against the possibility of being treated unfairly because of their wish to save in a pension and we are considering the introduction of new statutory rights. One option would be to build on the existing framework of employment rights so that individuals who wish to save in a pension scheme would be protected from being unfairly dismissed or being subject to detrimental treatment, such as being passed over for promotion. Some of these rights may be enforceable through the Employment Tribunal system, but we continue to look at alternatives.

What type of information and support would encourage compliance?

What you said

8. Respondents emphasised the need for clear and simple information delivered to employers and employees at the right time through different media and appropriate channels, for example Business Link or Her Majesty's Revenue & Customs employer packs. The importance of communicating messages via advisers as well as directly was stressed, especially for small employers. Support in the form of a dedicated telephone helpline was also regarded as a necessity.

9. Several examples of good practice in relation to the provision of good quality information to support a compliance regime were cited by respondents including communications around the National Minimum Wage and the Pensions Regulator's e-learning programme for trustees.

"It will be important for the Government, working in conjunction with the Personal Accounts Delivery Authority, to provide employers and employees, as well as the self-employed and third-party/intermediary organisations, with comprehensive information about Personal Accounts." (Engineering Employers' Federation)

"Good information and communication is at the heart of compliance with Personal Accounts legislation. This starts with a vibrant and effective marketing campaign by Government to ensure employers and employees are aware of their rights and obligations." (AEGON UK)

"Employers need to understand their requirements … be able to access information readily and easily … this will be down to effective communication channels and material." (British Chambers of Commerce)

How the Government will take this forward

10. The information strategy for employers will be designed to provide them with everything they need in order to comply with the new obligations, and the strategy for employees will be designed to create a sense of entitlement to a pension contribution from their employer. The development of these strategies will be taken forward through further consultation with interested stakeholders and with advice from the Personal Accounts Delivery Authority.

How can processes be designed to encourage compliance?

What you said

11. Some respondents felt that the focus of the compliance regime should be on safeguarding and protecting employees, while others thought that the National Minimum Wage was a good model on which to base the Personal Accounts compliance regime.

"Maximum compliance will be encouraged by simplicity, clarification of what is required by employers and assistance from the Personal Accounts Delivery Authority or the Personal Accounts board as appropriate." (ACA)

"The processes need to be as simple, and impose as little additional cost over and above the contributions, as possible." (Gissings)

"We would also support the ABI's proposal for a risk-based approach targeting those employers who have high rates of opt-out." (Co-operative)

How the Government will take this forward

12. Since December 2006, the Government has continued to build on its understanding of compliance regimes, the effectiveness of different approaches and the likely impact of the three following compliance approaches:

    - Employee enforcement through an Employment Tribunal: enforcement would be left to the employee. The awareness campaign about the changes coming in from 2012 would encourage employers to meet their requirements to automatically enrol employees into qualifying schemes. If an employer did not meet this requirement, the employee could seek redress by pursuing a case through the Employment Tribunal.

    - Employee enforcement with third-party support: enforcement would be driven by the employee, but with third-party support from an organisation able to investigate matters on their behalf. If an employer did not meet the requirements, the employee could contact a whistleblowing helpline to obtain help with taking their case further.

    - Automated processes to support enforcement: administrative processes would be designed to support compliance from the start, with a smaller role for the individual employee. Compliance activity would take place behind the scenes, with the details of compliant employers being matched against a database to check whether employers had complied with the obligation to automatically enrol their employees into a pension scheme. If an employer was identified as non-compliant, reminder letters would be sent, followed ultimately by proportionate penalties.

13. Under the first two options, a high level of compliance would be achieved through an effective information campaign though substantial pockets of non-compliance might remain. Further compliance would be reliant on employees being proactive in enforcing their rights by either taking their case to an employment tribunal or whistleblowing.

14. The Government does not think it would be realistic to expect large numbers of employees to do this, and even if they did, the costs involved in taking and defending a case at an Employment Tribunal for both employees and their employers would be extremely high.

15. The third option focuses on using data that the Government already holds on employers to contact them and inform them of their obligations. It then identifies which employers have not responded and issues follow-up letters and penalty notices. Evidence from other compliance regimes, such as that used by Her Majesty's Revenue & Customs for Pay As You Earn and National Insurance Contributions, suggests that this could be an effective way of delivering compliance. At the same time it would be the most light-touch option for compliant employers because it identifies the potentially non-compliant and enables subsequent enforcement action to be targeted at them.

16. We believe that this approach is likely to generate a significantly higher level of compliance for the least cost to all, including business, and seems most likely to lead to a high level of participation in Personal Accounts – while remaining light-touch and proportionate.

17. We are continuing to work with employers, together with organisations with expertise both in regulating pensions and in employer compliance, to explore the details of our compliance strategy.

How could the proposed penalty regime be structured?

What you said

18. There was strong support for a compliance regime that included a proportionate financial penalty system linked to the severity of the failure to comply.

> *"Any financial penalties imposed should be used to improve the pensions of employees."* (Association of British Insurers)
>
> *"On the whole the FSB is generally supportive of the proposed compliance regime. The FSB believes that a light-touch compliance regime, with appropriate penalties for non-compliance, is the right approach."* (Federation of Small Businesses)
>
> *"The TUC is very keen to ensure that any regime is truly effective at identifying and penalising wayward employers."* (Trades Union Congress)
>
> *"The compliance regime should … include proportionate penalties."* (National Association of Pension Funds)

How the Government will take this forward

19. We are using a framework of guiding principles (based on the penalties principles recommended by the Macrory review[8]) as well as analysis of existing systems to develop the sanction options. These principles include that there should be no financial benefit gained by the non-compliant and that the sanctions should be proportionate to the nature of the regulatory offence.

[8] The Cabinet Office commissioned Professor Richard Macrory to review the system of regulatory sanctions in 2005. His final report, *Regulatory Justice: Making Sanctions Effective,* November 2006, outlined a number of principles regulators should have regard to when designing a sanctioning regime

20. We are considering the following options for a graduated approach to enforcement where employers have failed to register or failed to make payments on time:

- Letters: where automated checks generate a possible case of non-compliance, a letter informing the employer and providing an opportunity to comply or explain would be issued. If there was no response to this letter by the deadline, then further communications would follow.
- Financial penalties: after opportunities to comply or explain, the next stage of the process would be a financial penalty, probably on a sliding scale.
- Appeals: if penalties are imposed, then employers must have the right of appeal. The Government would envisage using the new First Tier Tribunal, which it is intended to set up under the Tribunals, Courts and Enforcement Bill currently going through Parliament.
- Criminal prosecution: while the Government envisages using financial penalties for the majority of cases, it is considering whether or not to retain the option of criminal prosecution in the most serious cases.

How valuable would a whistleblowing helpline for employees be?

What you said

21. Some respondents believed a whistleblowing helpline for employees would be useful as part of the compliance regime. Other responses highlighted that this alone would not be sufficient.

> *"The most suitable compliance regime for Personal Accounts will be one based on whistleblowing by the employee(s) affected."* (Co-operative)
>
> *"A whistle-blowing helpline would seem to be a good idea."* (Investment and Life Assurance Group)
>
> *"A whistle-blowing helpline could be useful for employees of medium-sized or large firms."* (Zurich)

How the Government will take this forward

22. The Government believes a whistleblowing helpline could provide an important communications channel for employees and will be exploring its role further as part of its overall information and communication strategy. It is vital that employees who are concerned about their rights under these new reforms have a clear route available to them for registering a complaint and for receiving information and advice about it.

26. The National Minimum Wage whistleblowing helpline provides such a route for all complaints. One indication of the success of this helpline is that only a very small number of cases raised through it ever need to be settled at an Employment Tribunal. Over 90 per cent of cases are successfully resolved before going to Tribunal.

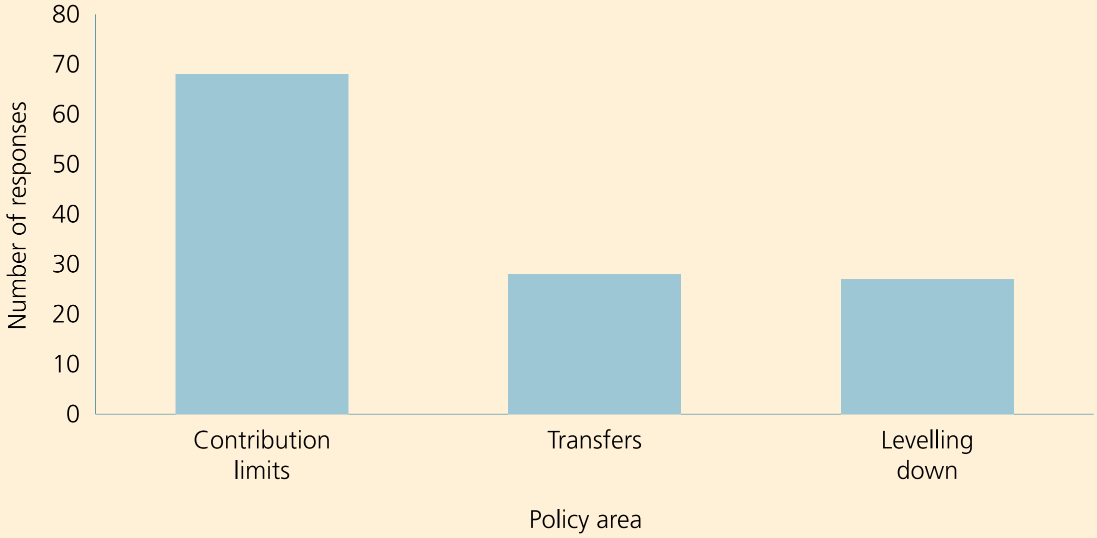
Chapter 7: Personal Accounts and existing pension provision

What *Personal Accounts: a new way to save* proposed

1. Our private pension reform aims to complement, rather than compete with, existing good-quality pension provision. To help achieve this there will be:

- a simple and straightforward exemption process for existing good quality employer pension schemes;
- a prohibition on transfers to and from Personal Accounts, at least until 2020;
- an annual contribution limit for the Personal Accounts scheme; and
- a higher annual contribution limit in the first year of the scheme to enable non-pension saving before implementation.

Figure 8: Number of consultation responses on contribution limits, transfers and levelling down



2. It was clear from the responses that the Government's objectives of minimising the impact on existing good schemes and avoiding the 'levelling down' of contributions were widely supported. From the Trades Union Congress to 'Which?' to individual insurance companies, it was agreed that our policy objectives would not be achieved if Personal Accounts merely replaced existing good schemes.

3. A number of respondents encouraged the Government to remain vigilant about the risk of employers levelling down their contributions in 2012 as a result of higher participation and the requirement for a minimum employer contribution. In particular, the Association of British Insurers and the National Association of Pension Funds made it clear that the reforms should not suffer from 'mission creep'.

> *"The challenge is to stimulate people to take a greater interest in their financial affairs in a cost-effective way which avoids distorting existing markets."* (Association of British Insurers)
>
> *"We support the proposals to enhance public understanding of the value of occupational schemes and hope that pension provision by employers will become more significant in the future as a tool for recruitment and retention."* (Which?)
>
> *"CBI members remain concerned about the likely impact of the reforms on employers who already provide good-quality schemes. In particular, there is continuing concern that automatic enrolment will – in many instances – significantly increase costs for such employers. The consequence is that employers will be forced to re-examine the pension benefits they provide. Such 'levelling down' could take a number of forms and over the longer-term there is a danger that many may choose to move to Personal Accounts if the defined contribution regime becomes over-regulated and restrictive."* (Confederation of British Industry)
>
> *"We believe that the risk of levelling down can be avoided if the Government adopts a narrower definition of the target group and aims Personal Accounts only at those people who do not have access to a good pension at work, rather than those who have the opportunity to join a pension at work but have not yet done so. To ensure that Personal Accounts are properly targeted and designed around the needs of the target group, we recommend that the Delivery Authority is given a specific objective of optimising participation and saving among those in workplaces without a good pension."* (National Association of Pension Funds)

The annual contribution limit

What the White Paper said

4. The White Paper set out a series of measures designed to focus Personal Accounts on the target market of moderate to low earners without access to good pension provision. One such measure was an annual contribution limit. This measure was first proposed by the Pensions Commission:

The contribution cap would limit *"the extent to which higher earners could use the NPSS as a low-cost alternative for pension saving that is already in many places occurring."*[9]

5. The limit was intended to influence the decision-making of employers with higher-paid employees, discouraging them from offering Personal Accounts as their workplace scheme.

6. The Pensions Commission proposed that the annual limit should be set at £3,000. The Department for Work and Pensions undertook further analysis, and concluded that a higher limit, of £5,000, would be preferable, in order to provide individuals with greater flexibility to save. We asked for views on the level of the limit in our consultation.

What you said

7. The White Paper consultation responses revealed a wider variety of views on this issue, in terms both of the level of the limit and how it is designed. The Engineering Employers' Federation opposed any limit. Consumer groups and trade unions such as the Trades Union Congress, AMICUS, Equal Opportunities Commission and Which?, while not comfortable with a limit in principle, argued that if a limit was necessary it should remain at £5,000.

8. Representatives from the financial services industry, such as the Association of British Insurers, National Association of Pension Funds and Investment Management Association, and some of their members expressed opposition to a £5,000 limit, and argued that a £3,000 limit was necessary in order to focus the scheme on the target market.

9. Other stakeholders, such as the Equal Opportunities Commission, Age Concern and Help the Aged, have suggested different ways of designing the limit, such as a lifetime limit, or allowing exceptions to the limit for specific payments, such as inherited sums.

10. The Work and Pensions Select Committee stated that: "We do not believe that the contribution cap should exist purely to protect existing pensions industry providers from extra competition. The interests of pension savers should be paramount, and we expect many occupational or group personal pension schemes to offer a high-quality and competitive alternative to Personal Accounts for large numbers of employees without special protection. We take the view that a better justification for the contributions cap is to reduce the risk of levelling down by making it harder for employers to cut their contributions."[10]

[9] Pensions Commission, *A New Pension Settlement for the Twenty-First Century: The Second Report of the Pensions Commission*, 2005

[10] House of Commons Work and Pensions Select Committee, Personal Accounts, Fifth Report of Session 2006-07 (HC220-1)

"There should be an annual contribution ceiling to Personal Accounts of £3,000 per year." (National Association of Pension Funds)

"The ABI believes that a cap of £5,000 would capture 93 per cent of the current market for employer-sponsored money-purchase schemes. The cap should be £3,000 or less." (Association of British Insurers)

"We think £5,000 would be a reasonable limit in the circumstances." (Association of Chartered Certified Accountants)

"For most people in the target market, a £5,000 limit on overall contributions to Personal Accounts will be easily sufficient." (Family Investments)

"Imposing a cap on contributions enables the government to meet its aim of supporting existing occupational pension provision – if there were no cap then many more employers might choose to replace their occupational or group personal provision with Personal Accounts." (Mercer Human Resources Consulting)

"The BCC believe ultimately there should be no limits, but for the initial launch fully support the White Paper proposal." (British Chambers of Commerce)

"There is currently no such limit on employer or employee contributions into other forms of pension saving; not putting Personal Accounts on the same footing would put them at a disadvantage." (Ford)

"GMB is concerned that £5,000 may be too low and can see no reason for reducing this still further to £3,000 as some groups seem to be advocating. Personal Accounts should be about enabling and encouraging pension saving, not restricting it and deterring otherwise prudent savers." (GMB)

"We support an annual contribution limit of £5,000 in today's earnings and up-rated in the run-up to 2012. Any less would risk placing a cap on people's aspirations for a comfortable retirement. The Government should also examine the feasibility of establishing a lifetime limit, instead of strict annual limits." (Which?)

The level of the limit

11. We received many responses on the appropriate level for an annual contribution limit. The responses were based on an analysis of a range of different factors, but mainly focused on the potential impact on existing schemes and products of different contribution levels, and also the impact on the ability of individuals to save flexibly for their retirement. Different stakeholders had different views on how that balance should be reflected in the limit – some argued that the limit should be £3,000, others that it should be £5,000.

12. Since the White Paper was published we have undertaken further analysis of both the £3,000 and £5,000 limits and we have looked at a full range of options in between. In discussion in this document we use £3,600 (the gross amount that non-earners are able to contribute into a registered pension scheme and receive tax relief on their contributions in any given tax year) and £4,000 to illustrate the effects of the limit at different levels.

13. Before considering further the appropriate level of the limit, it is worth noting that in the December White Paper we proposed that the Personal Accounts board would review the contribution limit. However, as we have developed more detailed proposals for the governance arrangements of the scheme we have concluded that this would not be appropriate. We believe that government would be in a better position than the Personal Accounts trustees to review the contribution limit, as part of its responsibility to ensure that the scheme is targeted and complements existing provision.

14. Several stakeholders have noted that the Pensions Commission recommended an annual limit of £3,000 in 2005, but by the time Personal Accounts come into being, the value of such a limit would have fallen as a proportion of individuals' earnings. In order to keep Personal Accounts focused on the target market whilst ensuring that members' savings will reflect earnings growth, we propose that the contribution limit be uprated in line with average earnings growth from 2005. Our analysis will use 2005 as a baseline to allow for a direct comparison with the Pensions Commission's Second Report which was published in 2005.

Impact on existing pension provision and on individuals

15. Setting the contribution limit involves a delicate trade-off between targeting the Personal Accounts scheme and enabling individuals to achieve their benchmark replacement rate. In setting a contribution limit for Personal Accounts we are constraining the amount that individuals are allowed to save. However, a guiding principle of Personal Accounts is that the scheme should be targeted at moderate to low earners currently without access to employer-sponsored pension provision. In order to keep this focus, a contribution limit is appropriate to reduce the suitability of Personal Accounts for people who are currently well served by the existing market.

16. The annual contribution limit will be one of the ways in which Personal Accounts will differ from other pension schemes. Other differences include that there will be no transfers in the early years of implementation and no additional features such as life insurance. These factors should ensure that the scheme remains focused on its target market.

17. Our analysis of the contribution limit has looked at the impact on existing schemes and products, and the impact on individuals. Many of the responses to the consultation argued that a contribution limit of £5,000 was too high to target Personal Accounts effectively at the sections of the market that are currently under-served.

18. The table below shows the percentage of people contributing to a defined contribution pension who would be constrained by a particular annual contribution limit. Personal Accounts would compete with that proportion of existing provision if the contribution limit were the only determining factor. On this basis, if the contribution limit was set at £5,000, Personal Accounts would then be attractive to around half of all individuals with earnings above £30,000, whereas it would only be attractive to a quarter of these with a contribution limit of £3,000.

Table 1: Percentage of people currently contributing to a pension scheme by income group

Annual Income	**Percentage of people saving below thresholds**			
	less than £3,000	less than £3,600	less than £4,000	less than £5,000
less than £15,000	96 per cent	98 per cent	98 per cent	99 per cent
£15,000-£30,000	81 per cent	87 per cent	90 per cent	95 per cent
Over £30,000	24 per cent	34 per cent	40 per cent	53 per cent

Source: Office for National Statistics, 2005, *Annual Survey of Hours and Earnings*, workplace-based Pension Schemes excluding defined benefit schemes

19. Several stakeholders, including representatives from the pensions industry, have expressed concern that despite the basic nature of the Personal Accounts scheme, unless the contribution limit is set below £5,000, and preferably at £3,000, then existing schemes and products could be subject to excessive competition. They also make the point that it would be better to start with a lower level and then increase it later if circumstances allow, than to start off with a higher limit which could cause irreversible damage to existing schemes and products.

20. Looking at the impact on individuals, the Pensions Commission's proposal for a contribution limit was designed on the basis of allowing a median earner to reach their 67 per cent benchmark replacement rate if they contributed at the maximum from age 21, a relatively early age to be saving. Table 1 shows how different contribution limit levels affect the point at which people with different levels of earnings would need to start saving to reach their benchmark replacement rate. The figures demonstrate that a higher limit would allow individuals to start saving later, but any contribution limit between £3,000 and £5,000 would enable continuously employed moderate earners to save enough for an adequate pension income. Having a contribution limit higher than £3,000 gives individuals some flexibility about when to save, or to increase contributions from the default level.

Table 2: PPI estimates of required contributions to achieve benchmark replacement rates			
Annual contribution limit (in 2005 terms)	**Male, earning median earnings benchmark replacement rate 67% Start saving at:**	**Female, earning £20,000 per year – benchmark replacement rate 67% Start saving at:**	**Male, low earner, earning £15,000 per year benchmark replacement rate 70% Start saving at:**
£3,000	21	30	44
£3,600	26	35	46
£4,000	30	36	48
£5,000	35	41	51

Source: DWP modeling.
Notes: assumes 3.5 per cent average real return and retirement age of 68 and individual earns median earnings each year. Earnings increase in line with average earnings each year.

21. The Pensions Policy Institute has presented its own analysis of the required contribution rates for different individuals.[11] This analysis uses different assumptions from the DWP analysis. However, it does draw similar conclusions, that a contribution limit of £3,000 would be too low, but a contribution limit slightly higher than this would enable most low to moderate earners to save at a sufficient level to reach benchmark replacement rates. They conclude that a contribution limit of £5,000 would be higher than necessary and would risk undermining existing provision.

[11] PPI *Response to Government's White Paper* March 2007

Table 3: PPI estimates of required contributions to achieve benchmark replacement rates

	1st decile	2nd decile	median
Man – full NI history – age 25 in 2012	£700 (7.7%)	£1,400 (9.9%)	£1,800 (9.5%)
Woman with caring breaks – age 25 in 2012	£200 (4.5%)	£1,600 (17.5%)	£2,900* (23.1%)
Woman with caring breaks – age 40 in 2012 – no prior saving	£600 (12.4%)	£2,500 (26.9%)	£4,000** (31.9%)
Self-employed man – age 25 in 2012	£1,700 (19.6%)	£2,400 (17.6%)	£2,900* (15.3%)

Source: PPI briefing note 38, *What should be the contribution cap for Personal Accounts*, June 2007.
Notes: * indicates contribution rate that exceed £3,000 in some (*) or all (**) years.
Figures in brackets denotes savings rates as a percentage of band earnings.

The design of the limit

22. During the consultation period, the Government also received a number of stakeholder proposals outlining alternative ways to design the contribution limit. The main suggestions are discussed below.

A lifetime limit

23. A number of stakeholders, in particular the Equal Opportunities Commission, suggested setting a lifetime, rather than an annual limit. This would allow individuals with irregular working patterns to contribute more when they are in paid employment. However, this has a number of drawbacks:

- it risks diluting the main objective of a contribution limit, which is to keep the Personal Accounts scheme focused on serving the target market of moderate to low earners;
- it would create significantly increased flexibility which could shift that focus by making Personal Accounts a more attractive proposition for employers with existing schemes and higher income employees; and
- it would require employers and employees to plan their savings patterns over an unrealistic time horizon. For example, an individual may make regular additional contributions early in their working life, but may find they had hit their lifetime limit by middle age. They would then face the prospect, if still with an employer offering Personal Accounts, of being forced to stop saving and losing access to their minimum employer contribution.

A rolling limit

24. Other stakeholders have suggested a 'rolling limit', possibly over three years, to allow more flexibility for individuals who wish to make additional contributions. While this added flexibility is attractive in principle, it would add complexity to the Personal Accounts scheme, increasing costs for members, which would be at odds with the objectives of low cost and simplicity. In addition, it would only benefit those in the target group with frequent and large fluctuations in income.

Lump sum contributions

25. Some stakeholders suggested allowing individuals to contribute lump sums from specific sources into Personal Accounts, such as from a bonus or inheritance. Under these proposals, these lump sum contributions would not be subject to the contribution limit in Personal Accounts.

26. Providing greater flexibility, through a lifetime lump sum limit, would enable individuals with breaks from the labour market to save more and get closer to their benchmark replacement rate. However, it could be very difficult to identify the source of lump sums and thus treat certain sources of money differently. Any lump sum limit would probably therefore have to allow individuals to contribute lump sums from any income sources.

How the Government will take this forward

27. A wealth of analysis has been undertaken on the level of the Personal Accounts contribution limit, both by the Department for Work and Pensions and by a range of stakeholders. The White Paper made it clear that any decision on the contribution limit would have to balance the twin aims of focusing the scheme on the target market and providing individuals with sufficient flexibility to save for their retirement.

28. After further analysis, the Government believes that a limit of £5,000 would not be the most appropriate reflection of this balance. We have decided that a limit of £3,600, based on 2005 earnings, to compare directly with the Pensions Commission's proposal, would be a more appropriate level. Analysis shows that most moderate to low earners will still be able to reach benchmark replacement rates within a limit of £3,600. This means that the level of the limit will not fall below the gross amount on which non-earners can receive tax relief on their contributions in any given tax year. This provides greater simplicity and a level playing field with other savings options for economically inactive members who wish to continue to contribute to Personal Accounts. We believe this figure will be more effective than a limit of £5,000 at focusing the scheme on the target market, minimising the risk that Personal Accounts will compete with existing schemes and products. The Delivery Authority will advise the Government on the most effective way to implement this limit.

29. Individuals may wish to pay one-off lump sum contributions into their Personal Account. We will therefore ask the Personal Accounts Delivery Authority to explore the possibility of an additional lump sum contribution limit, targeted at individuals

with irregular working patterns, which would run alongside the annual limit. This limit would operate on a lifetime basis.

30. Any lifetime lump sum contribution limit would have to be designed in a way that targeted it at helping those who have taken a break from contributing, to enable them to catch up on their contributions. This would minimise the risk of Personal Accounts competing with existing pension products. The Delivery Authority will advise on the operational cost and feasibility of this option, and also what an appropriate level might be. The Delivery Authority would need to be satisfied that the benefits of this added flexibility were not outweighed by the costs of designing and administering this addition.

31. As discussed above, the £3,600 limit will be based on 2005 earnings levels, and will be uprated with earnings from that point to implementation from 2012.

Transfers

What the *Personal Accounts: a new way to save* proposed

32. The White Paper announced that the Government was planning to prohibit transfers between Personal Accounts and alternative schemes in order to:

- focus Personal Accounts on moderate to low earners who do not currently have access to a good employer-sponsored pension scheme;
- make the scheme simpler to operate – much existing pensions provision offers a range of features that would not easily translate into the straightforward Personal Accounts scheme; and
- minimise market disturbance during the transitional period after the introduction of the new scheme.

33. The December White Paper also proposed that the policy on transfers be reviewed in 2020, once the market impact of the reforms can be assessed and the scheme has become established.

What you said

"We support the Government's proposal for a prohibition on transfers into and out of Personal Accounts." (Association of British Insurers)

"We welcome the proposal to prohibit transfers as this will help to stabilise the pensions environment during the first years of Personal Accounts and avoid savers having to make complex decisions which rightly would require professional advice and guidance." (National Association of Pension Funds)

"The CBI supports the Government's intention not to allow transfers in or out of Personal Accounts as part of the drive to ensure focus is kept on the target market. Prohibiting inward transfers would remove the administrative cost and complexity associated with transfers for the Personal Accounts scheme and existing providers, as well as minimising the impact on the existing market and existing provision." (Confederation of British Industry)

"We welcome the ring-fencing of Personal Accounts through a ban on transfers into or out of Personal Accounts, with a review in 2020." (Prudential)

34. The White Paper consultation responses show broad agreement among stakeholders, particularly those from the financial services industry, that a ban on transfers was necessary. Several stakeholders also noted that prohibiting transfers should act as a disincentive to employers looking to level down into Personal Accounts.

35. GMB was less enthusiastic and the Trades Union Congress sounded a note of caution when they suggested that the prohibition could lead to mis-selling in the run-up to 2012. However, they did accept that the policy was understandable considering the need to avoid damaging existing provision.

How the Government will take this forward

Prohibition on transfers

36. The Government maintains its view that prohibiting transfers between Personal Accounts and other schemes, at least in the short term, remains a sensible idea. This view was widely supported in the White Paper, subject to a review in 2020.

The review of the contribution limit and transfers

37. The White Paper proposed that the contribution limit and its level, and the prohibition of transfers, be reviewed in 2020 to assess their effectiveness in helping to focus the reforms on the target market. This date was based on a five-year period following the full implementation of the Personal Accounts scheme in 2015, as contributions will be phased in over a three-year period from 2012.

38. The Work and Pensions Select Committee suggested that this period of phasing in should be disregarded, and the review take place in 2017, five years after the introduction of the scheme, regardless of the phasing in of contributions. The Government agrees with this proposal, and the review will take place in 2017.

Further suggestions to minimise the impact of pension reform on existing schemes and products

39. Most respondents agreed that the most effective way of minimising this risk would be to design the scheme according to the needs of the target market. The prohibition of transfers and the annual contribution limit are two such mechanisms, and other suggestions are discussed below.

40. The National Association of Pension Funds proposed a further idea to reduce the risk of 'levelling down' – the 'Good Pension Quality Mark', whereby employer schemes could achieve accreditation based on contribution levels, in order to promote the continuation of existing schemes (see Chapter 5).

41. The Government welcomes the efforts of the National Association of Pension Funds to lead the industry in developing a quality mark and believes that it may help members to appreciate better the value of their employer's pension scheme. It is the employer who ultimately bears the cost of higher contributions or benefits and enabling them to operate with a short waiting period is a way of recognising their generosity.

42. In addition, the Government has proposed a series of measures designed to focus the Personal Accounts scheme on the target market and minimise the risk of adversely impacting existing workplace pension schemes. These measures received widespread support, and the Government remains open to further proposals to achieve this objective.

Saving to 2012

What the *Personal Accounts: a new way to save* proposed

43. The White Paper acknowledged that because Personal Accounts would be available from 2012 it was important that individuals continued to make the most of opportunities to save in the interim. The White Paper drew attention to the efforts of the Government, the Financial Services Authority and the financial services industry to encourage saving in the years before the introduction of Personal Accounts. These included:

- simplification of the tax regime, which has made it easier for individuals to make lump sum contributions;

- Financial Services Authority's seminars on 'Managing your money' in workplaces across the country; and
- the 'Save More Now' campaign launched by the Association of British Insurers.

44. In addition, the Government also proposed that the contribution limit be set at £10,000 in the first year of the scheme, in order to enable individuals to move any savings accumulated prior to 2012 into the Personal Accounts scheme.

45. The December White Paper also envisaged a role for employers building on an existing relationship with their employees and starting automatic enrolment before 2012.

What you said

"We are also concerned about setting the limit in the first year at £10,000, and believe this is unnecessary. Although we accept setting a higher limit will give people the opportunity to notionally 'earmark' regular savings for Personal Accounts in the run-up to 2012, we believe that in reality very few of the target market for Personal Accounts will be able to afford to save anything approaching the £10,000 limit." (AEGON UK)

"Our view is that the cap should be set at £3,000 p.a., including the first year of launch. Although a higher cap in the first year would not discourage existing savers from saving in other vehicles, it is unlikely to encourage the target group to start saving, and it would also add another layer of complexity to the new system." (AXA)

"While believing that a £5,000 ceiling on contributions is too high to have the desired effects, we endorse the Government's recommendation that the ceiling should be £10,000 in the first year. This would allow people to save significant amounts between now and 2012 and deposit this as a lump sum in Personal Accounts." (National Association of Pension Funds)

"We support the provision for increased contributions in the first year of Personal Accounts. Given that people will be unable to transfer accumulated pension savings into Personal Accounts, a contribution limit of £10,000 in the first year seems appropriate. We believe the Government should clarify the tax treatment of any initial contributions. Our preferred option would be that the £10,000 limit should apply to individual contributions and any tax relief would be applied on top of this figure." (Which?)

[12] Clery E, McKay S, Phillips M and Robinson C, 2007, *Attitudes to pensions: The 2006 survey,* DWP Research Report No. 434

[13] Pettigrew N, Taylor J, Simpson C, Lancaster J and Madden R, 2007, *Live now, save later? Young people, saving and pensions,* DWP Research Report No. 438

46. Many pension providers opposed the £10,000 limit and questioned whether there was a real desire in the target market for such a high cap in the first year. The National Association of Pension Funds, however, acknowledged the importance of allowing people to deposit lump sums in the new scheme and supported an initial limit of £10,000.

47. The consumer group Which? also supported the idea of allowing employees without existing employer-sponsored provision to prepare for the introduction of Personal Accounts in 2012.

How the Government will take this forward

48. The proposal of a higher limit of £10,000 in the first year is designed to encourage saving in the years before 2012. We recognise the concerns of various stakeholders which must be balanced against the needs of savers and will continue to discuss this with our stakeholders.

49. We have an ongoing programme of research on attitudes to pensions and savings for retirement and on how we can encourage people both to start saving and to save more for retirement. Our latest research looks at attitudes to saving, and the findings from *Attitudes to pensions: The 2006 survey*[12] and *Live now, save later? Young people, saving and pensions*[13] will inform the policy development process.

50. We will continue to work with others across government, in industry and consumer representatives to explore how we can encourage people to start saving or to save more. This will allow us to share expertise and market knowledge, and to consider how existing savings products might be used more effectively.

Annex A: List of organisations that responded to the White Paper consultation

Association of British Insurers (ABI)

Association of Consulting Actuaries (ACA)

The Association of Chartered Certified Accountants (ACCA)

Actuarial Profession

AEGON

Age Concern

Amicus

Aquilaheywood

ASDA

Association of Convenience Stores

AXA

Building & Civil Engineering Benefit Schemes (B&CE)

British Chambers of Commerce (BCC)

Buck Consultants

Carers UK

Confederation of British Industries (CBI)

Connect

Financial Services Consumer Panel

Co-Operative

The Depositary and Trustee Association (DATA)

Disability Action

Engineering Employers' Federation (EEF)

Equal Opportunities Commission (EOC)

Fair Pensions

Family Investments

Fawcett Society

Fidelity

First Actuarial

Ford Motors

Friends Provident

Federation of Small Businesses (FSB)

GMB - Britain’s General Union

Gissings

Hargreaves Lansdown

Help the Aged

HBOS

Investment Management Association (IMA)

International Financial Data Services (IFDS)

Investment and Life Assurance Group (ILAG)

Institute of Directors (IoD)

Jaguar Cars Ltd

JP Morgan Asset Management

Land Rover

Legal and General

Mercer Human Resource Consulting Group

National Association of Pension Funds (NAPF)

Norwich Union

Occupational Pensioners Alliance

Payroll Professional

Pensions Investments Research Consultants Ltd (PIRC)

Pensions Policy Institute (PPI)

Policy Research Institute on Ageing and Ethnicity (PRIAE)

Professional Contractors Group

Prudential

Re-connect Retired Members Association

Resolution Foundation

Royal National Institute of Blind People (RNIB)

Royal London Group

Runnymede Trust

SBJ Benefit Consultants

Scottish Widows

Society of Pension Consultants (SBC)

Standard Life

Tesco

The Newspaper Society

The Pensions Trust

Tor Financial Consulting

The Pensions Advisory Service (TPAS)

Transport for London (TFL)

Trades Union Congress (TUC)

UK Social Investment Forum (UKSIF)

Watson Wyatt

West Norfolk Womens and Carers’ Pensions Network

Which?

Xafinity Paymaster

Zurich

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