

Synopsis of responses to The Pensions Board consultation on the future of defined contribution pensions

Introduction

The Pensions Board published a consultation paper on the future of DC pensions on 13 August 2013 which set out the Board's vision of the future regulation of DC pension provision. The paper set out specific questions to which the Board sought responses by 30 October. The context for the consultation was a review of the regulation and future structure of DC provision with a view to delivering good outcomes for members. While the Board welcomed all comments, specific questions were posed on trusteeship, regulation, investment, disclosure and value for money.

During the consultation period, the Board hosted public meetings in Dublin and Cork to discuss the matters raised in the consultation paper. The format involved presentations by key speakers, followed by breakout sessions on the main issues contained in the consultation document, feedback on the breakout sessions and finally an open forum for attendees to give their views or ask questions. 152 people registered to attend the event in Dublin and 38 in Cork.

The Board received a total of 44 written submissions in response to the consultation, 6 of which came from individuals and 38 came from organisations/schemes. The consultation document posed ten questions and the responses summarised below reflect the main points made and a range of suggestions offered to deal with the questions raised.

This document is a synopsis of the responses the Board received to the consultation phase of this process and does not cover all of the points made. No definitive conclusions have been drawn by the Board at this point and the next stage of the process will involve a detailed consideration of all of the points made in the submissions which will further inform the Board's views on the future direction of DC pensions.

Synopsis of responses

1. Trusteeship

The Board's view is that trustees performance needs to significantly improve in order to best protect members' interests and that trustees should have to self-certify their competency and ability to meet specified knowledge and experience criteria before appointment and annually thereafter.

Do you agree with this?

There was broad agreement that standards of trustee performance should be raised but mixed views as to whether self-certification would actually achieve higher competence levels and could prove to be a 'box -ticking' exercise which still misses key issues. It was remarked

that for self-certification to be meaningful it would need to be policed, for example, through random audits. Some suggested that self-certification could be built into the scheme annual report or by online CPD style annual certification. There was some support for The Pensions Board developing 'hallmarks' or 'kite marks' of quality professional trusteeships that the Board would monitor. Several suggested that any provisions should take account of the size of the scheme with higher standards being required for large schemes with small or one-member schemes being considered separately. It was also suggested that most larger DC schemes are relatively well run and issues are more likely to arise in smaller schemes where the principal employer is the trustee.

What would you suggest as minimum standards for trustee knowledge, understanding and behaviour?

Many positive and constructive suggestions were offered under this heading. Minimum standards proposed for trustee knowledge, understanding and behaviour included QFA Pensions, 15 hours continuous professional development (CPD) per annum with CPD credits being approved by the Board, a level VII in the National Framework of Qualifications in administration/finance, a Pensions Board accredited trustee training programme every 2 years, fitness and probity standards stipulated by the Board, mandatory trustee toolkit modules on governance for all DC trustees and online tests to ensure trustees understand their responsibilities. There was broad agreement that trustees should be sufficiently familiar with strategic management issues, admin functions, investment options and strategies, investment management, scheme administration, reporting obligations, the implications of charges and levies, the need to minimise costs, the concept of trusts, conflicts of interest, the obligation to act in the best interests of all members, the need to challenge advisers, legislative and regulatory requirements and, on a practical level, the day to day workings of their scheme. There were some suggestions that minimum standards should focus on the expertise of the trustee board rather than individual trustees.

It was also suggested that the current training requirements and Trustee Handbook form a reasonable basis for a minimum standard, but that this could be improved with something similar to the codification of good governance for corporate boards, which could be adapted to trustee boards. Similarly, it was suggested that trustee performance could be measured periodically with the standards that apply in the Central Bank's revised Consumer Protection Code for Directors.

Do you agree that the Board should issue a code of governance in order to clarify the standards it expects of DC trustees? If not, what other vehicle could we use to provide further education and guidance for trustees in order to drive up standards of governance and administration?

There was a high level of support for a code of governance to be issued by the Board with views expressed that such a code could greatly assist trustees by clarifying the expected standards and competence required. Some queried whether the code would have a statutory basis and what the consequences of non-compliance would be. It was also suggested that

the code should be short and to the point, be written in plain English, be created in consultation with those schemes proven to be effectively managed, require trustees to certify that they are complying, be tailored in respect of the size and complexity of DC schemes and be supported by a robust supervisory regime.

Other suggestions made were to consider developing a template governance framework and template controls and processes to encourage good practice, e.g. on the Board's website, and to consider holding webinars on particular issues. There were some comments to the effect that the current guidance contained in the trustee handbook and Board's trustee training modules was sufficient and should be more actively promoted by the Board.

2. Regulation

The Board proposes the introduction of legislation requiring new schemes to satisfy the Board that scheme design and the trustees are fit for purpose before being granted approval. Older schemes could be given a time frame in which to comply with the provisions.

Do you agree with this suggestion?

The vast majority of responses under this heading related to the issue of scheme design being fit for purpose with only a handful of comments made concerning trustees in the same vein. There was general support for the proposal concerning the pre-approval of scheme design with some caveats expressed about possible unintended consequences e.g. delays in approval, the need to be consistent with Revenue requirements, the lead-in time being sufficient, the approval process not becoming too complicated or creating barriers that might discourage employers from setting up schemes. However, questions were raised regarding how it could be determined whether a scheme design was in fact appropriate and it was commented that it was hard to envisage a 'one size fits all' design. Suggestions to deal with such issues included only allowing schemes of a certain size with smaller schemes having to be either a contract based arrangement or to join a master trust arrangement. Another proposal suggested independent certification be required on whether a scheme is fit for purpose with the Board maintaining a register of those qualified to give certification.

The need to address the number of single member and very small schemes was also mentioned. There were some views to the effect that that all of the Regulators (the Board, Central Bank and Revenue) could agree a common template for the approval, design and operational aspects of new schemes that would ensure compliance with each one's statutory requirements and codes of practice in the members' best interests. Those who dissented with the pre-approval of scheme design commented that this task is already carried out by Revenue and that perhaps a quality symbol for schemes of a certain design could be introduced.

In relation to trustees being fit for purpose, those who commented said that certain positions, e.g. chair of trustees, could be pre-approved and modelled on a framework such as the

Central Bank's 'fit and proper' regime, with other trustees required to demonstrate compliance. Other suggestions were that trustees could be required to produce a certification of advice they have received in areas in which they have no particular expertise or be subject to regular independent competency certification. It was also suggested that the more critical issue is to ensure that trustees engage professional advisers who are 'fit for purpose'.

3. Investment

While it is important for defined contribution members to have investment choice, the options offered can be complex and default strategies not always suitable for the needs of members.

Do you have suggestions as to how we can ensure that defaults offered are appropriate and do not expose members to unnecessary and unexpected amounts of risk?

There were a number of suggestions offered on how to create appropriate default strategies. It was generally agreed that default strategies need to be carefully designed and suitably structured to assist members in making the best decisions. It was proposed that the Board should provide templates and best practice guides which encourage the use of plain language, clearly explain risks, use graphics and give practical examples. It was also proposed that the Board could produce a leaflet setting out the different categories of investment choice and the details that members should consider, pitched at a very basic level. Some thought that benefit statements should set out the details of the funds the member is invested in, its investment performance, how that performance came about and any investment risks in the year ahead. Others felt that default funds should be lower risk with typical annual growth of 4%+, the bond to equity mix needs to be more balanced, 50:50 being a better mix than the current 75%+ equities seen in many Irish funds, and more diversification to other regions.

Other suggestions were that lifestyling options should be mandatory for defaults and tailored to suit different retirement options with a max of 8 to 10 funds offered covering different risk levels, with a risk rating for funds. Another proposal was that trustees should be required to appoint a Scheme Advisor or Actuary to construct the default investment strategy, akin to the PRSA regime. There was also broad support for the adoption of a standardised risk rating system.

There were some comments to the effect that efforts should be on engagement with members rather than relying on default strategies and that 'white labelling', which refers to a type of investment strategy rather than a specific pension fund works better for members in understanding investment principles. Others suggestions were that providers should offer a standardised DIS which has to have actuarial input and include lifestyling approved by The

Pensions Board, particularly for one member schemes. Where trustees want a different approach, this could be approved by the Board on a scheme specific basis.

Would it be helpful if the Board produced practical guidance on the design and governance of default strategies?

It was generally considered that practical guidance on the design, governance, review, monitoring and communication of default strategies would be helpful. Numerous suggestions were offered on the form this guidance might take to include ideas such as the Board engaging with schemes by having a 'star rating system', whereby the provider could submit documentation to the Board and be scored on factors such as openness about risk, plain English and clear visual presentation. This could increase standards and provide trustees with a benchmark. It was also suggested that the Board could consider maintaining a register of default strategies as operated by the larger schemes that would be available on request to schemes. Another view indicated the Board should include in legislation that all schemes must include a default investment strategy from establishment and issue guidance to provide that such a strategy adopts an investment profile consistent with fulfilling the reasonable expectation of a typical member with respect to the outcome of saving for retirement. There were some views that the Key Investor Information Document (KIID) as set out in the PRIPs proposal would be a useful way to ensure information on funds are disclosed to trustees in a clear and consistent manner. A number of comments also indicated that the investment guidance produced by the Board last year was sufficient and with a suggestion that guidance could contain a risk questionnaire for members which could help them choose the risk category they fall into.

4. Disclosure

Many members do not understand enough about their pension schemes to make informed decisions. Information given often has a legal purpose, with sometimes too much information given, and is not necessarily structured so that members are clear how it should be used to make decisions.

How can member information be improved to ensure that it is accurate, clear and understandable and enable members to make informed decisions about their retirement savings?

There was universal agreement that the quality of member information generally needs to be improved, made more user-friendly and that current regulatory requisites are inadequate. Many submissions stated that information needs to be clear, concise, written in plain English, layered, easy to understand, focused on key information, designed with the member reading it in mind and to enable them to make decisions. Many said the volume of information required is too high and language is too legalistic, with several suggestions that

disclosure regulations need to be completely reviewed and simplified, with input from stakeholders. The need to distinguish between communication and information was considered to be necessary as key messages in benefit statements, such as funding adequacy, investment suitability and value for money are getting lost in the detail. A simplified statement with opening and closing balances and any changes in between, broken down by contributions, investment performance, tax, levies, benefit payments and charges, which is set out in an uncluttered, simple and personalised manner was considered to be essential. Some suggested that member benefit statements should be one page only and summarise key information at the start. Other information could then be provided if necessary. Other suggestions were the use of templates, more visual information and the ability to provide information electronically.

There were views that the statement of reasonable projection (SRP) should be discontinued and replaced with a simple forecasting tool which members could utilise or a SRP that links to a specific target benefit each year and highlights steps that might be taken to keep on track. It was also commented that disclosure requirements for DC often appear to be a modification of what was required for DB and DC merits its own disclosure approach.

How can costs and charges borne by members be more clearly and transparently communicated to them?

There was much support for having a standard means of disclosing costs to allow comparisons - suggestions were RIY, TER or monetary amounts and percentage of fund. There was a suggestion that The Central Bank and the Board should work together to ensure a consistent approach to communication of charges from provider to trustee. It was also suggested that there could be a publically available register of charges, which could be broken down by administration, investment, advice and compliance, and colour coded against an average.

Proposals for benefit statements indicated that these should be like bank statements with opening/closing balances, contributions and transfers in, the total annual fees charged as a percentage of the fund each year and investment returns. Some submissions emphasised that any new disclosure requirements around charges should be written in plain English with a recommendation for worked examples to be displayed in documents. There were suggestions for the need for Board involvement in the area of charges, to include issuing a standard leaflet setting out clearly what charges members need to be aware of, together with a simple explanation of these charges, and that the Board should consider setting a standard definition for total expense charge and provide clear guidelines on the disclosure of any entry /exit charges.

Another proposal was that the Board and Revenue could create a universal 'retirement benefit calculator', like DSP's redundancy calculator, which could be updated if and when legislative changes occur. It was also suggested that schemes be encouraged to undertake an analysis of their costs, alongside a statement showing what service/value is expected to be provided for that cost, who is meeting this cost and how that cost might vary in the future.

5. Value for Money

Trustees need to be demanding consumers on behalf of their members especially where smaller schemes, which do not benefit from economies of scale, are concerned.

How can trustees be supported/educated to ask the right questions about the different costs and charges incurred by their scheme in order to enable value of money comparisons to be made and to assess the fairness to members of the costs and charges?

Many commented that value for money cannot only be about costs but must take account of services provided and overall benefits for members. Other suggestions said that having a standard measure would allow comparison and that the Board could produce a template set of questions for trustees to ask when analysing costs and publish a benchmark for typical costs. It was also suggested that costs should be displayed in monetary amounts on benefit statements as well as percentages, particularly for investment services, and that all costs should be displayed separately. It was also suggested that part of trustees' qualifications criteria should be to demonstrate a knowledge of charges.

Plain English guidance in the form of Q&As and checklists of points to consider when making comparisons on charges were also proposed and that trustees should seek an independent review of their schemes to ensure they are receiving reasonable value for money. It was also suggested that trustees should adopt tendering processes when engaging providers/advisers and that non-professional trustees engage independent experts to make comparisons and develop strategies for assessing value for money. There were some views concerning the role of providers, suggesting that these entities should be required to annually provide trustees with a statement outlining the amount of fees earned in connection with their scheme, split by source of payment, the services provided to the scheme in respect of the fees received, the options not taken which would have resulted in lower fees for the members and an explanation as to why the lower cost option was not availed of.

6. Other

Are there any additional points you would like to suggest on how the governance of defined contribution pensions could be improved?

There was a diverse range of additional comments and suggestions on how the governance of DC pensions could be improved. Issues that were mentioned frequently were:

- a. The need for a level playing field from a regulatory and tax perspective for all types of pensions

It was observed that taxation legislation can lead to anomalies between arrangements, e.g. USC liability on employer contributions to PRSAs, thus encouraging the establishment of single member schemes over RACs and PRSAs. The main alternative to small DCs is PRSAs which are not suitable in all circumstances, e.g. death benefits can be provided under DC but not PRSAs and there are differing costs and tax treatments between these categories of arrangements. One solution proposed for these regulatory challenges was to regulate providers instead of the scheme, as is the case with PRSAs. Another suggestion involved the introduction of legislation to encourage the use of master trusts and industry wide schemes large enough to facilitate good governance, reduced costs and efficiencies of scale, with the Board possibly preparing data to illustrate that members of smaller schemes would benefit from joining master trusts /industry wide schemes. A converse view was that the assumption that large schemes are more cost effective needs to be challenged, the example given was NEST in the UK and other multi-employer schemes, which it is alleged have not reduced costs for members.

There was strong support expressed for changes to the regulatory environment and significant changes to tax legislation but with the caveat that we do not end up with multiple layers of regulation that make pensions overly complex.

b. Simplification of system

In order to develop a clear over-arching vision for DC, it was proposed that simplification of the system is needed, as complexity is seen as a key impediment to member and employer engagement and is a significant driver of costs. Suggestions made were for simplification of the choice of products - one type of retirement savings account only, set up under trust or contract and one post-retirement account i.e. an ARF. Another suggestion was to simplify taxation by having a yearly contributions cap linked to taxable earnings subject to an annual maximum and an overall lifetime limit. For benefits, suggestions included allowing access after 50, a tax free lump sum with the remainder for annuity purpose or an ARF. ARFs should be subject to a lower minimum drawdown from age 60 and a higher maximum until 75. Amounts should be indexed and ages tied to changes in SPA.

c. Frozen schemes

There were some suggestions made concerning frozen schemes to the effect that if a scheme is frozen for 3 years and trustees do not elect to continue, administration should be given to the provider and members notified of how the scheme is to be administered and with whom they should engage. Frozen AVCs could be treated in the same way. It was also suggested that the Board could consider a project with the providers to wind-up these schemes and that legislation be introduced so that where a professional trustee takes on the role of trusteeship of a frozen scheme, with no other person available to accept the role of trustee, that they cannot be held liable for any issues/errors that arose before they took on the trustee role for the purpose of winding up the scheme. It was also suggested that single member frozen schemes should be capable of auto-conversion to BOBs/PRSA status.

d. Single member schemes

There were a number of comments made about single member schemes. It was suggested that one member schemes should be considered separately with reduced legislative requirements and that where member and trustee are the same person, these schemes should be regulated like contract based pensions and be exempted from trustee minimum standards. It was further suggested that if single member schemes are removed into a separate category then the number of active and frozen schemes remaining is reduced by 90%. Master trusts were recommended as a way of dealing with the volume of single member schemes, though some views were expressed that the drive for efficiency with larger schemes would be at the expense of individual consumers getting tailored advice.

e. Auto-Enrolment

It was noted that it is very important that any decisions taken in relation to DC are consistent with and supportive of any future auto-enrolment environment. Whilst clarity is needed on what exactly the model will be in this regard, it was suggested that it is hard to dispute from data available that a soft mandatory system is required. It was also suggested that such a system should be technology friendly, so that all regulatory and legislative requirements can be satisfied online. Views were expressed that the introduction of auto-enrolment may cure many of the issues around frozen or dormant schemes, in that such schemes could possibly be subsumed into an overall State scheme. Economies of scale would mean that benefits are not eroded by charges and having records held centrally would increase the chances of tracing members.

f. Issues of concern

Concerns were expressed that the cost of regulatory and tax complexity were not addressed in the consultation paper and that further regulation, greater governance requirements and the possibility of more professional trustees will add to costs. It was especially queried whether such costs were appropriate for smaller schemes. It was stipulated that changes to the existing regime needs to take account of the realities of trusteeship and the establishment of schemes and should involve the minimum amount of regulation. It was suggested that the Board should consider using its existing powers and enforcing current requirements before introducing new legislation - this may reduce the number of trustees, and in particular directors of sponsoring employers, who are not aware they are also a trustee.

Deferred members are another cause of concern and their unconstrained growth in DC trusts is creating an escalating cost and governance burden. Schemes have to expend money searching for such members. Another concern was that the consultation process makes no attempt to assess if DC constitutes good value for money or is capable of providing adequate and sustainable pensions. The scope of the DC consultation was considered to be very narrow and that rather than tackle issues piecemeal, a clear overarching vision for DC is needed.