TUC

Meeting future workplace pensions challenges: *improving transfers and dealing with small pension pots*

The TUC response to a DWP consultation

Introduction

1.1 The TUC welcomes the opportunity to respond to this consultation. We represent more than six million members organised in more than 50 unions. We are the leading representative consumer voice on pension policy issues.

1.2 The TUC has been a strong supporter of the recommendations of the Pensions Commission, and has played a full part in constructing the broad consensus for the policies of auto-enrolment.

1.3 We welcome the Government's decision to close the short service refund loophole. While we recognise the burden of small pots within defined benefit pensions, we have always considered pensions as deferred pay. Any system that allows employers to reclaim pension contributions once paid into their employee's pension fund is simply wrong.

1.4 Particularly in an auto-enrolment world, there is a strong case for making sure any pension contributions made – even during a short period of employment – should remain as pension savings.

1.5 The government is therefore right to deal with the small pots issue at the same time as closing the short service refund loophole. However the loophole needs to be closed in a timely manner to deter its use during the staging of auto-enrolment. Dealing with small pots must therefore not be allowed to delay action on short service refunds.

Some context

1.6 Any proposal to deal with small pots is likely to have wider implications for the future development of pensions. It is important that these wider considerations are thought through. Reforms should go with the grain of creating a good pension system based on the architecture set out by the Pensions Commission and endorsed by the Making Auto-enrolment Work Review.

1.7 The introduction of auto-enrolment is welcome. But while many people will be saving for the first time in a pension scheme, and the reform will do much to make pension saving routine, no-one can pretend that the minimum contribution levels required will produce a generous post-retirement income, particularly for anyone who does not have a stable work pattern.

1.8 It is therefore important that every pension pound saved works as hard as possible to provide post-retirement income. There is much research that shows what makes for a good defined contribution pension scheme. These can be summarised as:

- Good governance that aligns the interests of those running the scheme with those of members, which in the UK is normally best provided by trust governance.
- Low charges for both active and deferred members (with no deferred member penalty/active member discount)
- Appropriate default long-term investment strategies

These are all easier to achieve in funds with sufficient scale. Big funds will also find it easier to develop beyond the basic DC model in the direction of what the Pensions Minister has recently described as defined aspiration schemes.

1.9 Perhaps the most important policy innovation of the Pensions Commission Report was its acceptance of a behavioural economics framework. Before the Commission reported, policy for the last few decades was based on the idea that people would act in a 'rational' way. This would mean that they would value future pension income sufficiently to give up current income, assess their investment beliefs and then choose a suitable pensions product carefully weighing up the choices on offer in a functioning competitive market.

1.10 But real people do not act in this way. That is why auto-enrolment is based on a different framework. Of course we want people to take responsibility for their pensions decisions and the system allows them to do this, but public policy now starts by realising that inertia has to serve the majority of people who we know will not take this active interest – at least at that early stage in their lives when they can make the most difference.

1.11 Under the old system the answer to most pension problems was to say that we should provide more education and more information to encourage people to act in their rational self-interest. While we still want to educate people and encourage good communication and information provision, we now recognise that we have to design a system with a good default that will work when people do not engage in an active choice.

1.12 In other words pension education should allow people to make informed choices that may suit them better than relying on the default system. It should not be required to protect them from inertia serving them badly.

1.13 This is why we strongly support the establishment of NEST. It comes as close as any funded pension scheme in the UK to meeting our criteria. Even before auto-enrolment it has already put pressure on pension scheme charges, challenged the investment approach of default funds and provided a model of good pension scheme governance.

1.14 The introduction of auto-enrolment will lead to many more people saving in a pension. In a fairly short period of time the UK private sector workplace pensions system will have gone through three stages:

- Most people building up a defined benefit pension either through an occupational DB scheme or SERPS.
- DB in fast decline in the private sector and only very partially replaced by DC saving, the majority of which through for-profit contract schemes. We are now at the low point of this stage with two out of three private sector workers with no workplace pension contributions.
- The start of auto-enrolment in which we can expect millions more to save into DC pensions, with the introduction of NEST as a major not-for-profit trust governed scheme. DB remains as a significant but minority niche. This phase starts later this year, but will take many years to reach maturity.

1.15 It is right to ask whether the workplace pension system that we have today is right for this new stage. The contract based occupational pension system developed to serve something of a niche market in what was a predominantly DB world. Even the name Group Personal Pension betrays it origin as a rebadged product developed originally to serve individual savers, most likely to be self-employed or company owners.

1.16 The questions posed by the Kay Review of UK Equity Markets and Long-Term Decision Making are as relevant for the even long term framework of pension saving as they are the capital needs of business. We therefore quote from John Kay's foreword:

> 'Equity markets are a principal means by which savers can contribute to, and share in, the success of British business. Many people who know nothing of the stock exchange participate in equity markets through their pension funds and other vehicles of long term investment.
>
> Most of the respondents to our consultation – including many from within the financial services sector – felt that these fundamental objectives of rewarding savers through the activities of high performing companies could be more effectively achieved. While the growth of financial intermediation has many positive aspects, intermediation is not an end in itself, and the rewards of intermediation can ultimately be justified only by the contribution such activity makes to economic activity outside the financial sector. Markets exist to serve customers'.[1]

1.17 Current market pressures in workplace pensions do not serve savers. Under auto-enrolment employers choose pension providers. Most will no doubt wish to do well by their current employees, but we cannot rely on this. Competitive pressure led the pensions industry to explore exploiting short-service refunds by setting up trust-based commercial vehicles. The effect of these was to take employer contributions away from the worker and return them to the employer. Similarly the development of active member discounts/short-service refunds are driven by market forces acting directly against the interests of the saver.

1.18 We make these preliminary points to help establish a framework to judge the proposals in the consultation paper. We would suggest the following tests based on this approach:

- Will a new small pots system provide the best possible outcome for consumers who do not make active choices?
- Will it provide appropriate choices for consumers who wish to be engaged?
- Will it help develop a better pensions system in the long-term?

Of course we recognise there are other criteria. The system should be as straightforward and simple for employers to operate as possible. But that should not be traded off against consumer outcome, but dealt with in the detailed design of a new system that deals with small pots. And given the non-alignment between the interests of savers, employers and commercial pension providers, we should not be frightened of radical proposals that disrupt current arrangements and help a transition towards a better pensions system based on the scale and good governance aligned with the interests of savers that would provide the launching pad for the defined aspiration of collective DC.

1.19 As we will argue later, we have a key concern that restricting the consultation to small pots is a mistake. Small pots are an undoubted problem for employers and pension providers, but for consumers similar issues arise when they cease employment with any size of pot. Indeed damage to a big pot will have a bigger proportionate impact on post-retirement income than a similar effect on a small pot.

1.20 We respond to the consultation in detail by responding to the specific questions set out in the consultation document, but thought it would be useful to provide an overview of our approach.

The TUC's approach in summary

1.21 We do not believe that improvements to the current system can solve the small pots problem as they will not meet our test that a new system should work without active engagement by savers. However many improvements can be made to help members who wish to make active choices. We strongly believe that what is good for savers with small pots is also likely to be good for savers with medium and large pots too. If we do not end up with a default system for savers with bigger pots, some of the changes outlined in this section would help them get the best from their pension savings. As we recognise the difficulties of dealing with the stock of legacy pots through a new system, and can see that this may be better dealt with on a longer time-scale, a better tracing and transfer voluntary system could play an important role.

1.22 While we can see the theoretical attraction of 'one big pot' following a worker from job to job we do not think this can work. We have two main difficulties:

- We cannot support a default transfer system that could see money taken from a good scheme and passed on to a bad scheme, for example one with much higher charges. To be made to work, there would therefore need to be a guarantee that all auto-enrolment pension schemes met tough quality standards.
- The practical difficulties are immense. Not everyone moves in an orderly manner from job to job every few years, choosing to save in a pension in each. The difficulties of dealing with people who move jobs frequently, hold multiple jobs, take career breaks, face unemployment and/or drop in and out of pensions saving are severe. An auto-transfer system that only covers small pots is likely to cover a high proportion of workers with irregular work patterns.

1.23 We therefore support an aggregator scheme approach with one or more aggregator funds. To make such a system work there would need to be one aggregator that has a public service obligation to accept pots, however small. NEST is the obvious choice, as long as its role as an aggregator does not create costs that have to be borne by its other members.

1.24 The most difficult issue is whether, and if so how many, other schemes should be allowed to be aggregators that can receive transfers without the active consent of savers. Many would argue against a monopoly aggregator, while a large number of aggregators would be self-defeating as people could end up with small pots scattered across a number of aggregators – not much better than the current system.

1.25 We therefore favour a regulated system that would allow other schemes to become aggregators - but only if they meet high standards and are likely to serve a sectoral market which would mean that people would be likely to move between employers using the same aggregator.

1.26 This would be likely to leave NEST with the majority of auto-transfers, but with sufficient diversity in the system to ensure that its performance can be bench-marked against other providers.

1.27 This consultation flows from industry and employer concern for the difficulties of dealing with small pots. But it is not obvious from the consumer perspective that a better system for consolidating pots should be confined to small pots. If we develop a system where the risks of detriment from auto-transfer are marginal, we see no objection to the system applying to all pots. This may appear to be radical, but we think it likely that the bigger the pot and the older the worker the more likely it is that that they will want to actively engaged. We therefore set out in outline a system that could auto-transfer all pots.

1.28 We also recognise that the proposals that flow from this consultation will not bring about the big shake-up in the management of workplace pension savings that we want to see in one go. So while we make no apologies for wishing to locate our suggested changes within a longer term strategy, we also suggest some interim moves that will be both easier to achieve and provoke less opposition from vested interests.

1.29 We now deal with the detail of our response, following the structure of the consultation document as closely as possible.

Chapter 2 – small pension pots: the case for change

2.1 *Do you have evidence on the scale of the current problem of small pension pots?*

We do not have any extra evidence to add.

2.2 *Do you agree that the barriers listed on page 17 are the current barriers to transfers?*

Yes – and we would emphasise that the failure of many members to initiate transfers even when it is clearly in their interests to do so underlines our view that we need a new system where inertia delivers good outcomes, whatever the size of the pot.

Chapter 3 – Improvements to the current regulatory framework

3.1 Would any or all of the proposals listed on pages 24 and 25 under this option be an effective way to facilitate more transfers and reduce the number of small pension pots?

We do not think that improving the current system will deal with the small pots problem. This is because inertia will lead many to leave pots with their previous employer.

However that does not mean we should not consider such improvements. While we need a new auto-transfer system that mirrors auto-enrolment, we should also help those who want to make active choices whatever the size of their pot.

We would therefore support some of the proposals outlined in this chapter as part of a wider reform package – they are a necessary but far from sufficient reform.

We therefore support proposals to make it easier to transfer pensions by simplifying the process and requiring all pension schemes to accept transfers in. Promoting the work of the Pensions Tracing Service will be uncontroversial. If either auto-transfer or encouragement of voluntary consolidation is applied to past pension pots, then the PTS has an important role. Routinely linking all pension records to NI numbers is the best way to enable past and future pot consolidation.

We would reserve judgement on proposals to reduce the costs of administration – while we do not wish to see unnecessary administrative burdens on schemes we would not want to see scheme members with small pots treated differently from those with bigger savings.

3.2 Are there other ways to reduce costs further and make it easier for people to find any small, dormant pension pots – during the accumulation phase and at the point of retirement?

Under the new system – whatever approach is adopted – the old employer will have to provide information about their employee's pension pot when they leave their job. This would be a good opportunity to encourage them to use the Pensions Tracing Service or trigger transfers from previous schemes that they know about. If there is a simple and uniform approach to pension transfers it should be possible for an employee to trigger a consolidation of their pension pots even if we do not end up with auto-transfers for all existing pension pots.

Again we see no real point in treating small pots differently from medium or larger pots. While it is probably more likely that the bigger the pot the more likely it is that savers will actively manage it, this cannot be taken for granted. A cliff-edge would inevitably be arbitrary, and those with savings just over any limit will not be well served by a new system.

We have heard suggestions that instead of a transfer system, a database could be built that would allow individuals to trace all their pension pots without consolidating them in a single fund. This does not seem to us to be an adequate response. The advantage of consolidating pots is that it will reduce costs. If the cost of administering a pot is largely fixed, it makes sense to minimise the number of pots in the system. A virtual system would work in the other direction.

Chapter 4 – Automatic transfers

4.1 Taking account of our principles for reform, which of the two models in Chapters 5 and 6 do you think has the most merit?

We favour the aggregator approach. While we recognise that there are some attractions in the 'pot follows member' approach, we think there are two substantial problems with this approach:

- Members may suffer detriment if their funds are transferred to a poorer scheme.
- We have grave doubts about its practicality and cost.

In contrast we think an aggregator approach based on NEST is practical, in the best interest of consumers and meets the criteria we set out above.

4.2 Do you have any other suggestions for a process to overcome problems associated with small pots and improve transfers?

Any successful system in our view will be a variant of the aggregator approach.

4.3 Although the solutions in this paper deal with small pots in defined contribution (DC) schemes, we would be grateful for views on how defined benefit (DB) schemes should be treated and whether we should also consider applying any transfer solution to DB rights?

We recognise that it is unrealistic to expect DB schemes to hold on to micro pots, or to accept transfers in of small amounts. The aggregator system we advocate could ensure that all of a short service refund within a DB scheme was kept within the pensions system for the benefit of the member. The current short service refund trigger of two years service was developed with the needs of DB schemes in mind, and it would make sense to maintain the same limit.

Other transfers from DB schemes should not be subject to any auto-transfer system. There is a severe risk of member detriment in giving up DB rights, and should only be taken after careful consideration and proper advice.

There will also be a significant number of people with some degree of hybridity in past pension contributions, such as guaranteed access to favourable annuity rates. It is important that members do not give these up without informed advised consent in any auto-transfer system.

4.4 Do you agree that under an automatic transfer system, members should have the right to opt out?

Yes. Our approach is based on a straightforward principle. Inertia should deliver a good result, but members should always be free to make a different choice if they wish.

4.5 Do you agree that individuals should not be required to take advice in an automatic transfer system, provided sufficient safeguards are put in place?

If a "pot follows member" system is introduced and there is a possibility that a member should suffer detriment from an auto-transfer then members need to be alerted to this and have access to advice (paid for by the employer).

If an aggregator approach along the lines we suggest is adopted than we see no need for advice, as long as aggregators meet the quality tests needed to protect against member detriment.

In any auto-transfer system there would need to be protection for any rights in past schemes that go beyond a simple DC member, such as enhanced annuity rights.

4.6 Do you agree that solutions to address the expected rise in small pots after automatic enrolment should also be designed to take account of the existing stock of small and dormant pension pots?

We strongly support the principle of consolidating small and dormant DC pension pots, unless there are clear reasons not to do so such as a guarantee of particular annuity rates. But our concerns about the "pot follow members" approach apply as much to past small pots as ones built up in current or future employment.

However, while we support consolidation of past pots in principle, we recognise that this is not a simple process. It may therefore be more practical to introduce a new auto-transfer for future pension scheme leavers as a first step, with further consideration of the consolidation of previous pots.

Chapter 5 – An aggregator scheme for small pots

5.1 What are the particular challenges and benefits created by introducing one or several aggregator schemes?

5.2 Do you agree with the aggregator scheme characteristics set out?

5.3 Could the pensions industry offer an aggregator scheme with these characteristics?

5.4 Have we correctly understood the implications of there being one or several aggregator scheme(s)?

5.5 Should there be several aggregator schemes or one?

5.6 What are the advantages of NEST acting as the aggregator scheme?

We answer these questions together in the following section.

Why we support an aggregator model

An aggregator model can be constructed that meets both the practicality and principled objections raised by a 'pot follows member' model.

There is more than one way an aggregator system could be built, with the number of aggregators a critical design factor. However while we set out how we think such an approach might best work, we would still be likely to support a practical aggregator approach even if it made different design choices, subject to its meeting our overall criteria.

Any aggregator system would need to have at least one fund with a public service obligation to receive transfers from any source. While it would be possible to create a new fund to do this, it makes sense to use NEST. This is the right choice because NEST:

- already has a public service duty to accept pension contributions
- has low charges and is available to anyone
- is a not-for-profit organisation with trust-based governance that puts the interests of its members first
- has a default investment strategy designed to serve the interests and preferences of low to medium earners – the most likely people to have small pots
- does not distinguish between active and deferred members (so that all members are charged the same AMC)
- already has arrangements for annuitising small pots
- is leading the way in developing jargon-free communications based on a deep understanding of low and medium earners.

These would all need to be design features of any aggregator with a public service obligation. As NEST already has them, it makes sense to use it for this purpose.

Auto-transfers must not move people into a scheme that is substantially worse than the one they leave. Few schemes beat NEST's charges or rival its emphasis on low to medium earners.

But it would be wrong to expect NEST to take up this role if it resulted in extra costs imposed on its other members. The government would need to discuss with NEST the financial obligations of assuming this role.

In particular it would be wrong to make the criteria for small pots so restrictive that NEST only ended up with tiny pots that would not interest any commercial provider. As we consistently argue, there is a strong case for treating all pots the same when someone leaves an existing pension arrangement, but if the government does not accept this argument it must not go to the other extreme and limit the size of pots to those it would be uneconomic for NEST or anyone else to administer.

We know that some parts of the pensions industry oppose the aggregator approach, but if they lose that argument it would not be a sensible compromise to define small pots in a way that means NEST or other aggregators only end up with uneconomic micro-pots.

There are two possible alternatives to using NEST as a default aggregator:

- *establish a new trust based NEST-like aggregator independent from government but sponsored by it*. We see no point in duplicating many of NEST's functions within a new body. Transfers can help NEST achieve scale on a more rapid timetable, which will no doubt be helpful given the slow build up of contributions caused by delays in staging and phasing.
- *Award the role through competitive tender to a commercial pension provider.* We do not see this as providing the right guarantees for consumers. Funds should only be auto-transferred to a scheme that can

guarantee good governance, and this cannot be guaranteed through a contract. Auto-transferred funds must be managed under a fiduciary regime in which the interests of those running the scheme are fully aligned with those of savers.

The argument against NEST as a sole aggregator is that it may be wrong for NEST to have a monopoly role. Some argue that competition will improve outcomes. Others suggest that it may make NEST too big. A more subtle argument would be that if NEST is given the sole aggregator role, the practical trade-offs may involve severely limiting the size, and thus the number of pots, transferred which would neither benefit NEST nor the savers who miss out on auto-transfer.

The argument for a sole aggregator is that it if there are multiple aggregators there is a risk that the system fails to achieve its prime function as some people's pots may end up split between different funds. This may be limited if there is a limited number of aggregators. But that would require a potentially complex system to license aggregators.

We do not take a principled position on this issue. We do not accept the arguments against NEST as the sole aggregator. Auto-enrolment will already lead to it becoming over time a pension fund of global significance. Even significant sums aggregated through auto-transfer will do no more than speed this process up.

Nor do we see an argument for multiple aggregators based on an economics text book model of competition. It is unclear how aggregators would be chosen in any kind of worthwhile market that would ensure the efficient outcome for savers that markets are meant to achieve.

But we recognise that there are some stronger arguments against NEST having a sole aggregator role. While we do not see classic competition arguments, there may be a case for diversity so that it is easier to benchmark and compare aggregator funds.

We also recognise that in some sectors such as construction, there are already multi-employer schemes that play a de-facto aggregator role for workers who stay within that sector.

Whether or not such schemes need to be part of an auto-enrolment system is a matter for debate. Given such schemes are already strongly established, it may be possible to construct some other approach in which it is made very easy for job leavers to stay in their existing scheme. This may be simply a matter of exempting employers in such schemes – as long as they meet minimum quality standards – from the need to auto-transfer leavers.

We would therefore favour either

- a simple system with NEST as the sole fund used for auto-transfers, with perhaps exemptions for some employers in sectors with good multi-employer schemes.
- a system with a limited number of aggregators with funds that wished to serve this purpose needing approval from a regulator. To get such approval

funds would need to demonstrate good governance, low charges, appropriate default investment strategies and other tests to ensure a minimal likelihood of member detriment in an auto-transfer.

5.7 What is the best approach to defining a small pot for this option? Would it be preferable for:

- *Default transfers to be compulsory if the pot is under a certain size.*
- *Default transfers to be voluntary for schemes.*
- *Default transfers to become compulsory under a certain size, but voluntary within a band.*
- *Should there be a transfer limit on pots below a certain size and if so, what should happen to the pot?*

The only way to approach this set of questions is to start with the simple test – what will be best for the consumer?

In an aggregator scheme, a member would only be better off keeping their funds in a scheme of which they were no longer an active member if it had lower charges, better governance or a better default investment strategy than the aggregator.

We would therefore favour automatic transfer into an aggregator unless the previous scheme was able to demonstrate to a regulator that they were at least as good as the default aggregator.

While the consultation document only asks about small pots, we do not see any consumer advantage in not applying this test to all transfers however big or small. The starting point for these questions appears to be what is best for pension schemes, not what is best for pension savers.

Of course we recognise that the bigger the pot, the more likely the member is to engage with this process, seek advice and/or make an active choice. But this does not mean that there is an easy to determine cliff-edge pension pot size, with auto-transfer working for people with savings less than this but suffering detriment through inertia if the saver keeps their money there.

There is a further issue with a cut off. From the point of view of a scheme a small pot is best described by its absolute size. But from the point of view of a member, age makes a big difference. What would look like a small pot at age 60, would look like a substantial start for a 25 year old.

However we recognise that going from a system where transfers can be difficult and are unusual straight to a system where all pots are auto-transferred may be seen as a radical step too far.

A possible transitional phase may therefore give pension schemes a choice about whether they transfer pots. This would allow each scheme to either decide that that they wish to transfer all pots or only those that they choose to define as small.

Of course the individual ex-employee should also have the choice of transferring their funds to their new employer's scheme or an aggregator.

This would need to be accompanied by a ban on active member discounts to protect consumers from the consequences of inertia.

This would allow the transfer system to develop in stages.

We would prefer to give the option to choose whether to transfer to an aggregator rather than setting an arbitrary and uniform pot size below which auto-transfer happens, and above which it doesn't. We do not think any of the suggested cut-off figures are rational. Figures based on trivial commutation limits make sense for people approaching retirement, but make no sense for younger workers. An arbitrary small figure serves neither schemes nor members, and only has a rationale for the pensions industry in allowing them to load uneconomic pots elsewhere.

If a new system does include an specified cut-off point for small pots, we would favour this being substantial. If an aggregator system is going to work, then the aggregator needs to be able to administer the funds in an economic way. Confining auto-transfers to micro-pots will not lead to an economically efficient system.

We would also want to allow voluntary transfer of bigger pots above any small pot limit.

If auto-transfer is only permitted for pots below a threshold there is a danger that pots left with the previous scheme attract a deferred member penalty (even though deferred pots may be cheaper to administer than active ones). The government would need to use its powers to outlaw active member discounts.

We are instinctively against a de minimis provision. We believe pensions savings should be retained as pension savings. Many of those contributing to NEST – particularly during the lengthy staging and phasing process - will be contributing very small amounts to NEST. If there is to be a de minimis system then we would favour a tough test such as the sum being transferred being less than the cost of a pension transfer. Both employee and employer contributions should be returned to the worker.

5.8 Given the default nature of the transfer, which of the member, the transferring scheme or the aggregator scheme should pay the default transfer costs?

We believe the transferring scheme should meet the cost. It is of benefit to schemes not to have small pots. It is not unreasonable to expect them to meet the cost. It would not be unreasonable for this to be a flat cost per transfer, rather than a percentage fee.

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Chapter 6 – Pensions move with people from job to job

6.1 Are the existing protections for individuals sufficient for this option where pensions follow people from job to job?

6.2 Should a pot size maximum be applied to pension pots that are automatically transferred? If so, what should the maximum be?

6.3 How could a central database successfully match members with their pension pots?

6.4 To what extent could the pensions industry deliver a suitable electronic platform/database?

6.5 What should happen to pots when an individual does not join an employer for a long time?

6.6 What should happen to an individual's older dormant pension pots in this proposed process (those pots in DC schemes), where pensions follow people from job to job?

As we do not support a pot follows member model we set out here our objections – they are both principled and practical.

Why we oppose a pot follows member model

We could not support a system that meant that savers could be "auto-transferred" from a good scheme to a less good scheme. For example an employee could work for a large employer providing a well-governed, low-charge scheme with a sensible default investment strategy but change job to a smaller employer with a scheme that has higher charges, poor governance and a default investment strategy designed for well paid managers with a high risk appetite. If such a transfer took place at the top of a stock market bubble, which then burst, the employee would be understandably aggrieved if their pension pot fell in value.

Even if the schemes were otherwise similar but the new scheme had significantly higher charges it would be hard to justify.

A particular concern is the position of any extra voluntary contributions paid by the member. Could it be right in any circumstances for these to suffer detriment from an unsuitable auto-transfer?

While we can see the potential advantage of building "one big pot" to both the member and the pensions industry, unless we can ensure that this pot is built for the benefit of the member rather than the convenience of pension providers we cannot support this approach. The danger of "one big pot" is that it will attract rent seekers.

The previous government had concerns that allowing contract-based schemes to be used for auto-enrolment would breach EU rules on distance selling. To overcome these fears they sought "a letter of comfort" using the widespread support for this move among stakeholders – including consumer groups and unions.

There must be a similar concern that an auto-transfer system would breach the same rules – particularly when an alternative route to the same policy objective is available. It is unlikely that there would be such a wide consensus among stakeholders for allowing auto-transfer to contract based schemes without tough regulation that protects against consumer detriment.

To do this we would need to regulate every pension scheme to ensure consistent low charges, good governance and sensible default investment strategies. In our ideal DC+ world of a limited number of large scale trust governed schemes this would become an attractive option, but we are a long way from that.

Even with tougher regulation of receiving schemes, we have severe doubts on the practicalities of a pot follows member model when there are so many different schemes and pension providers.

It is easy to see how this might work for people with regular employment patterns who change job infrequently and move between large employers in the same sector. Such savers may even make up the majority of current occupational and contract pension scheme members, but the start of auto-enrolment will quickly alter this balance.

The new system from the start will need to be able to deal with people with much less ordered career patterns including those with breaks in their employment. There is no simple answer to what to do with the pot for someone who moves into unemployment.

Some people move jobs frequently. How would the transferring employer keep up with this? Is there not a risk that the costs of many transfers get placed on the saver?

Making transfers easy for employers should not be the prime concern of the new system, but it still has to be practical.

We understand that some are advocating a central database of employees and employer pension provision that can be used to match small pots with future employers. This would be a challenging and brave IT project, not just in establishing the infrastructure but securing future accurate and timely data.

- What would happen if a pension scheme did not wish to participate in a centralised IT project?
- Who would pay to run a central register? Would costs not end up being borne by members?
- How long would it take to establish this system? Would it delay the end of short service refunds?

We do not believe it is possible to provide answers to these, and other questions, with sufficient certainty therefore making the "pot follows member" model a very high risk proposal.

We cannot therefore give a pot follows member system our support unless there are very substantial changes in the pensions landscape that will radically reduce the quantity and improve the quality of the pension schemes into which pots would be transferred.

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[1] http://www.bis.gov.uk/kayreview