Supplementary evidence to the House of Commons Work and Pensions Committee's inquiry into pension reform following the White Paper
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PENSIONS POLICY INSTITUTE

PPI

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1. This evidence (supplementary to our memo of March 2006) gives an initial assessment of how well the proposals contained in the White Paper *Security in retirement* relieve the problems in the state pension system. It then raises some concerns with the policy for Personal Accounts. Suggestions to consider in the passage from White Paper to legislation are highlighted in the text and additionally listed at the end of this submission.

State pension reforms

2. Paragraph 4 of the PPI's March 2006 submission to the Committee identified four widely-agreed problems with the current state pension system. The White Paper proposals will relieve these to some extent, but none will be solved.

3. The first problem is that there are ***unequal outcomes***. Higher earners do better from the state pension system than lower earners (who are more likely to be women). The White Paper recognises that an earnings-related state pension is part of the problem, and proposes that State Second Pension (S2P) becomes flat-rate. The reduction of the number of qualifying years for Basic State Pension (BSP) will help to equalise outcomes between men and women.

4. However, unequal outcomes, favouring the better off, will persist for decades[1]. This is because (1) the flattening of S2P is slow (2) earnings-indexing the BSP gives more to pensioners with higher BSP and (3) the White Paper rejects the Pensions Commission's proposals to make the BSP universal for over-75s or any other measure to improve entitlement for current pensioners.

5. Further, proposed improvements to S2P still leave gaps in S2P credits. There will still be a range of outcomes from S2P. Women (who earn less, and are more likely to fall between the gaps) are still unlikely to qualify for full S2P.

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[1] This is shown in Table 5, page 32 of Curry and Steventon (May 2006) *Transition Trade-offs: Options for state pension reform*, PPI. This paper modelled the Pensions Commission's proposed option for reform. More recent modelling by the PPI has confirmed that the White Paper proposal is close enough to the Pensions Commission's proposal for the conclusions from the analysis in the PPI paper to apply to the White Paper proposal. The PPI is undertaking further new modelling.

6. Because S2P is proposed to stay indexed to prices in payment, while BSP is indexed to earnings, the state pension income of older pensioners will be lower than that of comparable younger pensioners[2].

7. The White Paper says that *anyone who has been in employment or caring throughout their working life could receive £135 a week at retirement in state pensions*[3]. For the reasons given above, many people - more than a third[4] - will receive less than £135 a week.

8. The White Paper proposes a tighter squeeze on Savings Credit than the Pensions Commission's proposal. From 2008 (at least 4 years before BSP starts to be earnings indexed) the level above which income becomes eligible for Savings Credit (currently the full BSP level) will be indexed in line with earnings. Less income will become eligible for Savings Credit than in the current system. Low-middle earners currently eligible for Savings Credit will receive less as a result. This will particularly affect older pensioners, who are less likely to have a full BSP and more likely to have low SERPS / S2P pensions; so will find less saving qualifying for Savings Credit. Some pensioners currently receiving Savings Credit will no longer be eligible when entitlement is re-calculated at the end of their assessed income period.

9. The White Paper presents the future indexation of the Guarantee Credit to earnings as a gain. But this indexation was anticipated anyway in all realistic policy analysis and the Government's long-term expenditure projections[5], so has not changed the expected position of those expected to claim Guarantee Credit.

10. Overall, the income distribution of people over state pension age will change very little as a result of the White Paper proposals. The better-off will benefit slightly more than the less well-off[6]. The problem of unequal outcomes will remain.

11. The second problem with the state pension system is its ***complexity***. The White Paper proposes to remove the complexity of contracting-out for Defined Contribution pensions. It also proposes making some of the credits for BSP and S2P the same.

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[2] See PPI Briefing Note Number 31
[3] White Paper page 20
[4] PPI initial estimate
[5] Regulatory Impact Assessment Appendix A
[6] See Table 4 and Chart 8 of Curry and Steventon (2006)

12. But complexity will still be a very significant problem in part due to continuing widespread means-testing. The White Paper suggests that in 2010, 45% of 'pensioner benefit units' are eligible for Pension Credit, but that proportion will reduce to around one-third[7]. The starting-point of this analysis seems low given official estimates that between 44% and 51% were eligible in 2003/4[8].

13. PPI modelling suggests a similar shape in the decline of eligibility for Pension Credit after the reforms, but starts at 50% in 2005, more consistent with the current official estimate. The PPI estimate therefore arrives at a higher proportion eligible in 2050 (45%) than the White Paper estimate (33%)[9].

14. The White Paper acknowledges that the number of older people eligible for Pension Credit will be uncertain, but only shows a point estimate calculated as the average of the midpoints of the ranges of outcomes from two different models used[10]. **Government should publish the range of outcomes from the models used to estimate the proportion of pensioner benefit units eligible for Pension Credit in future and the assumptions used**.

15. As well as causing uncertainty about the future value of saving now, Pension Credit complicates the system, and makes it harder for people to understand what they are likely to receive from the state.

16. Complexity also remains as S2P remains. It will become a flat-rate pension like the BSP, but will still have different qualifying criteria.

17. The Government recognised the BSP should be a *near-universal underpin*[11]. It is possible to achieve this with either a residency or a contributory test[12]. Government stresses administrative difficulties with proving past residency (although the PPI believes it would be possible) and prefers to keep the contributory principle[13]. There are also administrative difficulties with the proposed new contributory system. For example, the White Paper leaves for consultation how a system of certification will work to claim new carers' credits for each week that someone cares for 20 hours a week for more[14].

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[7] White Paper Figure 3.v page 123
[8] PQ Lord Oakeshott of Seagrove Bay *Hansard* 25 April 2006 Column WA15
[9] Curry and Steventon (2006)
[10] White Paper Footnote to Figure 3.v page 123
[11] White Paper Paragraph 3.74
[12] Curry and Steventon (2006) pages 20-24
[13] White Paper Paragraph 3.75
[14] White Paper Paragraph 3.94

18. The most effective simplification would have come from adopting a single-tier: merging the two different state pensions BSP and S2P into one. The White Paper consideration of this alternative cited the Pensions Commission's opinion that transition would be difficult to implement – an opinion with which the PPI disagrees having analysed the National Insurance system and other issues carefully[15].

19. The White Paper also cited cost and unfairness as reasons not to go ahead[16]. The cost of a single-tier solution need not be more than that of the White Paper reforms[17].

20. The perceived unfairness in moving to a single-tier is similar to that in suddenly reducing the qualifying years for the contributory system from 44 to 30 – those who have paid 'extra' e.g., because of paying voluntary contributions suddenly get the same as those who did not. This illustrates that despite the Government professing to believe in the contributory principle, it will significantly dilute the principle with this proposal.

21. Further, a single-tier solution would have the benefit (not recognised in the White Paper) of reducing the proportion eligible for Pension Credit further than the White Paper proposals will – down to around 10%[18].

22. How some of the complications of reducing the number of qualifying years to 30 will be managed in practice is not explored in the White Paper. **Legislation will have to address some practical details of the change to 30 years such as how to deal with people who have paid voluntary contributions, or how reciprocal social security agreements with other countries may need to be altered**.

23. The streamlining of some of the qualifying criteria of BSP and S2P means that it would be easier in future to merge the two into a single-tier. The logic of doing this will become clearer once contracting-out has been abolished and S2P has flattened further. **Legislation could set a date, say 2015, for a review to examine the feasibility of merging BSP and S2P**.

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[15] For a project commissioned by the NAPF, *Towards a Citizen's Pension* (2004) and (2005)
[16] White Paper Box 3a and Regulatory Impact Assessment Paragraph 4.17
[17] Curry and Steventon (2006) Table 8 and PPI Briefing Note Number 30
[18] See Curry and Steventon (2006) for the impact and feasibility of different ways of transitioning to a single-tier pension (contributory or residency) and PPI Briefing Note Number 30

24. Overall, there are roughly 100 parameters that define what any individual may receive from state pensions and Pension Credit. After the White Paper reforms, there will still be around 95 parameters[19]. The problem of complexity will remain.

25. The third problem of the current state pension system was that it placed ***too high expectations on private savings***. The White Paper, through the indexation of the BSP to earnings in particular, shows that Government now recognises the state will have to continue to be a significant provider of income in later life.

26. However, the way in which the White Paper phrases the intention to index BSP to earnings still leaves open the possibility that it will not be secured in future. **In order to minimise the political risk in indexation policy, legislation should include not just the start date but the definite commitment to ongoing earnings indexation of the BSP as a minimum** (not contingent on later decisions).

27. The potential over-optimism in expectations of Personal Accounts is considered later in this submission.

28. The fourth problem with state pensions is that ***policy was widely seen as unsustainable***. This was largely because of the future growth in eligibility for Pension Credit. It is therefore helpful that the Government has clarified it never intended that a significant majority of people should be entitled to Pension Credit[20]. The White Paper proposals should stop the future spread of Pension Credit.

29. However, the White Paper does not allay uncertainty in the future extent of Pension Credit. It provides no mechanism by which the intention of earnings uprating Guarantee Credit, or the uprating of the Savings Credit threshold, will be assured. Both these parameters have a significant impact on the proportion of people eligible for Pension Credit[21]. The uncertainty in what these parameters will be in future means the future value of saving now is made more uncertain than it otherwise would be. **The uncertainty could be minimised by setting the uprating of all Pension Credit parameters in legislation in the same way as BSP earnings indexation**.

[19] PPI analysis. Excludes Personal Accounts.
[20] White Paper Paragraph 31
[21] PPI Briefing Note Number 31

30. The White Paper reforms suggest more people than now will have a 100% withdrawal rate on their savings (because of being eligible for Guarantee Credit but not Savings Credit) although fewer will have a 40% withdrawal rate (because of Savings Credit) than would have been the case if current policy continued[22]. This trade-off has the advantage of fewer people eligible for Pension Credit, but the disadvantage of penalising some lower income savers more heavily than currently; where to strike the balance is a difficult policy question.

31. The long-term growth in the share of GDP now planned to be spent on pensions as a result of the White Paper proposals is more realistic than in previous projections, given the growth in the number of people over state pension age[23].

32. The proposed abolition of contracting-out for Defined Contribution (DC) arrangements will result in an increase in Government revenue of more than £4 billion in 2012. This has not been factored into Government projections of spending on pensions[24], even though the resulting higher future spending on S2P has been counted. If the increased revenue is also allowed for, there is very little immediate change in the Government's overall net fiscal position. The increased revenue from abolishing contracting-out for DC arrangements will almost exactly offset the short-term costs of state pension reform[25].

33. However, whether the revenue gain will be 'hypothecated' in this way is not addressed in the White Paper. **Government should account for how the revenue gains from abolishing contracting-out on DC will be spent, in particular confirming that they will be spent on improving pensions rather than on other areas of Government spending or debt reduction.**

34. The planned increase in State Pension Age (SPA) also adds to the sustainability of state pensions by reflecting life expectancy improvements. The increases proposed by the Pensions Commission appeared modest[26] and the White Paper proposals, although to be made earlier, appear reasonable.

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[22] As illustrated by White Paper Figure 3.v page 123
[23] PPI Briefing Note Number 27
[24] See page 24 of the White Paper
[25] White Paper Figure 9, page 24
[26] PPI evidence to House of Commons Work and Pensions Committee March 2006, Paragraph 11

35. The PPI suggested that the age for Guarantee Credit remain lower than SPA to help mitigate the impact of different life expectancies for different socio-economic groups[27]. The White Paper suggests that increasing the Guarantee Credit age from its then level of 65 be considered nearer the time of proposed SPA increases (from 2024), based on updated evidence of life expectancy trends at that time. This seems sensible. **The commitment to hold a review on the eligibility age for Guarantee Credit, say in 2020, could be written into legislation.**

36. The intention of holding periodic reviews of life expectancy trends and other issues as set out in Paragraph 3.40 of the White Paper[28] also seems sensible. However, to make sure these reviews actually happen, **legislation could lay down time spans within which the Government of the day has to commission a formal, evidence-based independent review of specified pensions policy issues or general reviews of the effectiveness of pensions policy[29].**

37. **Regular reviews to confirm or otherwise the rationale for planned increases in SPA would be especially helpful because of the uncertainty in future trends in longevity**. For example, the intention to raise SPA on the schedule in the White Paper could be made to depend on the outcome of reviews on certain dates. To illustrate, each of the planned SPA increases would be subject to review and able to be revised upwards no less than 15 years before the planned change and down no less than 5 years before the planned change; both movements needing to be justified by life expectancy changes being better or worse than that projected in the justification of the planned schedule. **The first SPA review could be coincident with the review of the default retirement age in 2011[30].**

38. Working longer is of immense significance as a response to demographic trends. The White Paper focuses on enabling and informing individuals and employers about their choices. As part of this, **Government should try harder to explode the myth that *we all have to work to state pension age* that continues in reporting of policy on later working. And including likely life expectancy in state pension forecasts would give useful information in context[31].**

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27 PPI evidence to House of Commons Work and Pensions Committee March 2006, Paragraph 11
28 And also referred to in Paragraph 2.52 of the White Paper
29 New Zealand and Ireland are examples of countries with legislation requiring general policy reviews at specific times. See PPI Briefing Note Number 29.
30 White Paper Paragraph 4.13. See PPI memo to the Pensions Commission March 2005 for more detail on how to make SPA increases contingent on a rolling review.
31 The PPI suggested this in a letter to the then Pensions Minister in September 2004

The NPSS, renamed in the White Paper as Personal Accounts

39. The PPI has previously raised concerns about the risks in the policy and design of the NPSS, while appreciating the potential value of an auto-enrolment scheme[32]. The White Paper does not take the discussion on the NPSS or Personal Accounts very much further than the Pensions Commission proposal and leaves many issues for consultation. The PPI's concerns about both policy and design of the proposal therefore still remain. Comments follow on some of the most critical policy issues.

40. The White Paper accepts that the state should provide a flat-rate pension and leave earnings-related provision to the private sector. This is in line with what the majority of pensions experts would view as the best roles of each sector[33].

41. But the White Paper goes further than many pension experts suggest by a very significant Government intervention in the private sector with Personal Accounts. This intervention aims at fairly high earnings-related retirement income (around 45% NAE for an average earner). The alternative view of many experts is that the Government should focus on delivering good flat-rate basic provision (minimum 21-25% NAE) and encourage/facilitate further provision without getting involved in its delivery[34].

42. The White Paper justification for the significant intervention in private saving through Personal Accounts is selective. No targets for success are defined. Expectations may be over-optimistic and potential reasons why the proposed intervention may not be effective are not fully addressed. The policy choice is inherently risky, yet policy alternatives are not fully explored.

43. The White Paper suggests that adequacy of retirement income against an income target is a better measure of policy success than the proportion of state vs. private income (it is proposed to drop the so-called 60:40 aspiration)[35]. The number of people 'undersaving' to reach the target is the key measure used by Government to illustrate current problems.

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[32] See PPI evidence to House of Commons Work and Pensions Committee March 2006, O'Connell (2006) *NPSS policy and design choices*, PPI and *Initial analysis of the Pensions Commission's Second report* (PPI, February 2006) Paragraphs 15 et. seq.
[33] PPI (2006) *Shaping a Stable Pensions Solution*
[34] See PPI (2006) *Shaping a Stable Pensions Solution* and O'Connell (2006)
[35] White Paper Annex C

44. The Government does not set a target for the reduction in the number of people 'undersaving' as a result of the proposed reforms. Such a target would be very difficult to set, given the inherent shortcomings of any analysis to measure the extent of undersaving[36] (which are not discussed in the White Paper). This means that whether the policy is a success or not will be to a large extent subjective.

45. The White Paper illustrates a median earner with a full life of NI contributions and saving in Personal Accounts who should reach a replacement rate of 45%[37]. Despite stating that a 45% replacement rate is not a target (let alone a guarantee)[38] it may become an expectation in the absence of any other measure.

46. As earlier sections of this note discussed, basic state provision will not be certain or adequate enough to form a secure base for Personal Accounts. Means-testing through Pension Credit is likely to remain at high levels, up to 45% of pensioner households. Personal Accounts will therefore have to both make up for inadequacies in state provision as well as get to a higher replacement rate.

47. The success of Personal Accounts is therefore very likely to become a continuing tough test for future Governments. **Government should address what it believes should be the target outcome of Personal Accounts, and how that can be measured.**

48. The White Paper may set unrealistically optimistic expectations for what Personal Accounts can achieve. In particular, remaining complexity and uncertainty in the extent of means-testing through Pension Credit will continue to make the value of private saving (in Personal Accounts or otherwise) uncertain. Especially if that means the Financial Services Authority cannot give clear generic advice on the definite value of staying opted in to Personal Accounts, then opt-outs may be higher than expected[39].

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[36] For a review of the problems with undersaving analysis see O'Connell (2006) pages 12-13
[37] White Paper Paragraphs 1.100-1.102, Regulatory Impact Assessment Paragraph 1.64
[38] Regulatory Impact Assessment Paragraph 2.45
[39] House of Commons Treasury Committee, *The design of the National Pensions Savings Scheme and the role of financial services regulation* Fifth Report of Session 2005-6, Paragraphs 48-49

49. The White Paper suggests a central estimate of 6.7m employees out of 10.8m eligible to be automatically enrolled into Personal Accounts will stay opted in: an implied opt-in rate of 62%[40]. This is slightly more modest than the Pensions Commission's assumption.

50. As the White Paper recognises, the only evidence of the impact of auto-enrolment on take-up rates is in employer-based schemes where the employer has voluntarily decided to introduce auto-enrolment. But many employees will not receive any encouragement to stay in Personal Accounts from their employer. The opt-in rate could therefore be lower than 60%. The White Paper suggests a lower bound of 50%, but this may still turn out to be optimistic. There is no evidence from any other national auto-enrolment scheme in operation, but the New Zealand Government suggests 25% of eligible employees will stay in the planned KiwiSaver[41].

51. The White Paper examples of saving in Personal Accounts also assume that having started, people stay contributing continuously throughout a working life with a full National Insurance record[42]. This may well be over-optimistic, given the diversity of working lives. Women in particular would be expected to opt in and out of Personal Accounts.

52. The White Paper gives the reasons why people do not save as they 'should' as the complexity of incentives to save, inertia and the cost of providing pensions, and the reforms are designed to combat these problems[43]. But it ignores other reasons why people do not save, for example: lack of money, preference for spending more or paying down debt, lack of trust in pensions or investments, preference for non-pension savings vehicles. For example, one survey showed 54% of non-savers do not save because they have *no spare money*; the next reason was the *risk of poor returns* at 18%[44]. Given the multiplicity of reasons, auto-enrolment is likely to help, but it may not be the 'silver bullet' that solves the perceived problem.

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[40] Regulatory Impact Assessment Figure 2.i page 49
[41] O'Connell (2006). Note that KiwiSaver will operate auto-enrolment similarly to the NPSS, but there is no compulsory employer contribution and less tax incentive than in the NPSS. But the value from saving is more certain, as there is no risk of being caught in means-testing.
[42] White Paper page 61, Annex E; Regulatory Impact Assessment page 53
[43] White Paper 1.32-1.45
[44] ABI (2005) *The State of the Nation's Saving* 2005 pages 12 to 16. See also Mayhew (2003) *Pensions 2002: Public attitudes to pensions and saving for retirement*, DWP Research Report no. 193, Tables 2.25 and 2.26 which also suggests there are numerous reasons why individuals do not save.

53. Any intervention by Government into the savings, capital and labour markets risks distorting those markets. Previous interventions (by previous and current Governments) either did not meet expectations (stakeholder pensions) or had to be wound back (SERPS). Parts of the White Paper focus on rolling back regulation from previous interventions (contracting-out, GMPs) while a chapter is dedicated to introducing a state/private vehicle which will necessitate new complicated and restrictive regulation.

54. The risk of future practical difficulties is compounded by the requirement, in either of the two proposed Personal Account models, for new large-scale system development[45].

55. These risks should be set in the context that Personal Accounts are expected to be a small part of the overall retirement savings sector. Government estimates are that even at maturity, the stock of assets in Personal Accounts will be less than 1/10th of the total sector assets[46].

56. This is because Personal Accounts are aimed at one group – those without current private pension provision. But necessarily, the introduction of Personal Accounts means additional regulation and other consequences across the whole sector.

57. The White Paper briefly refers to the investment risk a saver will run from Personal Accounts[47]. The fact that the Government is planning to organise, regulate and encourage Personal Accounts has been confused with a Government guarantee of outcomes in some reporting of the proposals. Future Governments may face calls for compensation if there is a major problem with the outcomes from Personal Accounts. **Government will have to make unambiguously clear in all literature what the nature of Government guarantee is in Personal Accounts and consider how acceptable it will be if people do not fully appreciate their investment risks.**

[45] White Paper Paragraphs 1.55-1.56; Figures 1.vi and 1.vii
[46] Regulatory Impact Assessment Paragraph 2.111
[47] White Paper Paragraph 1.75

58. The White Paper addresses quite briefly why it is Government's role to address 'undersaving' by imposing auto-enrolment.
    - The Government takes from the Pensions Commission's research that *very few median earners want* [a replacement rate] *less than 45%*[48].
    - It takes as a given that the Government should intervene in the private savings market to help individuals reach that level of income through a Government-sponsored savings scheme, because individuals are not likely to make the decision to start saving if left alone, even with improved information[49].
    - It proposes that auto-enrolment would tackle some reasons why people do not save (as outlined in Paragraph 52 of this note)[50].
    - It proposes two different delivery options for Personal Accounts.

59. The White Paper did not explore any alternatives for different balances between state and private provision, any different types of intervention into private savings markets (other than to rule out compulsion) or different policies in which auto-enrolment could be effective with less risk. The options considered for Personal Accounts were different delivery methods

60. One alternative policy, not mentioned in the White Paper but considered by the PPI[51], is a model where:
    - Basic income is better assured through the state pension, with much less means-testing, and,
    - Less prescriptive auto-enrolment is introduced into existing savings products to help people save flexibly rather than implicitly impose a target of a specific replacement rate for pension income in retirement.

61. There are many ways this could work. As one example, if NI rates were increased by 1% for employer and employee and state pensions improved commensurately, then a sound base would be better secured. Minimum contribution rates to an auto-enrolment savings vehicle could be set at 6% rather than 8%, with no need for contingent compulsion on employers. This would give a similar overall result to the White Paper reforms at less risk. It could be a better balanced policy, especially beneficial for low earners.

[48] White Paper Paragraph 1.100
[49] White Paper Paragraph E.20 Annex E, Regulatory Impact Assessment Paragraphs 2.22-2.28
[50] White Paper 1.32-1.45
[51] This alternative is suggested from the work done in New Zealand to plan for KiwiSaver, see O'Connell (2006) and PPI evidence to House of Commons Work and Pensions Committee March 2006

62. Given the risks and uncertainties inherent in the policy choice underpinning both models of Personal Accounts in the White Paper, **more policy analysis of the rationale for and alternative models of an auto-enrolment savings scheme seems necessary before detailed product design is undertaken**.

63. Many of the remaining Personal Accounts design questions depend on practical details that only someone working as an employer or a provider day-to-day will understand, for example the practical issues of transferring current pension saving into Personal Accounts or how to deal with people with more than one job. **There would be significant advantages to Government in bringing people with practical experience of working in industry into the Personal Accounts development team as early as possible.**

64. One of the criteria suggested for analysing the options for Personal Accounts design is *value for money for the taxpayer*[52]. There are two aspects to this: (1) the cost of tax foregone in reliefs on corporation tax, employee income tax and NI contributions as a result of additional saving, expected to amount to £1.2 - 3billion a year[53]; and, (2) the IT, administration, marketing and regulatory costs that are paid by the taxpayer rather than recouped through Personal Account fees.

65. Whether there is value for money from tax reliefs is a significant issue not addressed in the White Paper, which assumed the current pension saving tax relief policy would follow through into Personal Accounts (it would not be desirable to have two different tax relief systems running alongside each other). The Pensions Commission suggested that reforming the current system is too difficult, although recognised the widely-held view that it is highly regressive, costly and ineffective.

66. Discussions between the PPI and practitioners suggest that reform would be possible. **A review of value for money to the taxpayer of current and alternative systems of tax incentives for pensions and other forms of savings would help address a remaining significant policy issue**.

[52] White Paper paragraph 1.71
[53] Regulatory Impact Assessment Appendix E page 169

67. The White Paper quotes the Pensions Commission's estimate of £500m set-up cost, but offered no further analysis. It gave no details on how the cost would be split between the taxpayer and Personal Account fees[54]. Given this large uncertain cost to the taxpayer, and previous bad experiences with Government-run IT projects, **the plans for the design and build of Personal Accounts would have to be very carefully scrutinised, costed and compared to alternatives**. As a base-line comparator, there would be no set-up or additional on-going administration cost to the taxpayer from providing better pensions through the state.

68. One crucial policy difference between the two models of Personal Accounts presented in the White Paper is how much choice the individual should be offered. **It would be helpful if Government confirmed its policy intentions on promoting personal responsibility**. Does it want to achieve both more pension saving <u>and</u> a better understanding of how to approach investment (more consistent with the 'brand choice' model) or does it just want more people putting money into pension savings without necessarily engaging with the process (more consistent with the Pensions Commission model)?

69. The White Paper is light on plans for giving information about Personal Accounts to individuals and helping them make their choices in Personal Accounts – initial and ongoing - and other related financial decisions. If Government introduced a national auto-enrolment savings scheme without providing a good free source of independent generic advice on a wide range of lifetime financial decisions[55], the impact of Personal Accounts may be limited and/or the risk of mis-buying increased.

70. **Government plans for providing a good, free source of independent guidance in making the financial decisions required by the introduction of auto-enrolment need to be more detailed and costed**.

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[54] Regulatory Impact Assessment Paragraphs 2.123-2.127. In addition, it estimates costs to employers (excluding contributions) could be £230m set up and £90m p.a., White Paper Paragraph 1.125

[55] 'Advice' probably describes it best but can be confused with regulated 'best advice' which is not what most commentators envisage for an independent source of generic advice. It should be more than just information, and help people make their own decisions, stopping short of telling people what to do.

Summary of suggested issues to consider

a. Government should publish the range of outcomes from the models used to estimate the proportion of pensioner benefit units eligible for Pension Credit in future and the assumptions used (Paragraph 14).

b. Legislation will have to address some practical details of the change to 30 years qualification period for full BSP such as how to deal with people who have paid voluntary contributions, or how reciprocal social security agreements with other countries may need to be altered (Paragraph 22).

c. Legislation could set a date, say 2015, for a review to examine the feasibility of merging BSP and S2P (Paragraph 23).

d. In order to minimise the political risk in indexation policy, legislation should include not just the start date but the definite commitment to ongoing earnings indexation of the BSP as a minimum (not contingent on later decisions) (Paragraph 26).

e. Further uncertainty could be minimised by setting the uprating of all Pension Credit parameters in legislation in the same way as BSP earnings indexation (Paragraph 29).

f. Government should account for how the revenue gains from abolishing contracting-out on DC will be spent, in particular confirming that they will be spent on improving pensions rather than on other areas of Government spending or debt reduction (Paragraph 33).

g. The commitment to hold a review on the eligibility age for Guarantee Credit, say in 2020, could be written into legislation (Paragraph 35).

h. Legislation could lay down time spans within which the Government of the day has to commission a formal, evidence-based independent review of specified pensions policy issues or general reviews of the effectiveness of pensions policy (Paragraph 36).

i. Regular reviews to confirm or otherwise the rationale for planned increases in SPA would be especially helpful because of the uncertainty in future trends in longevity. The first SPA review could be coincident with the review of the default retirement age in 2011 (Paragraph 37).

j. Government should try harder to explode the myth that *we all have to work to state pension age* that continues in reporting of policy on later working. And including likely life expectancy in state pension forecasts would give useful information in context (Paragraph 38).

k. Government should address what it believes should be the target outcome of Personal Accounts, and how that can be measured (Paragraph 47).

l. Government will have to make unambiguously clear in all literature what the nature of Government guarantee is in Personal Accounts and consider how acceptable it will be if people do not fully appreciate their investment risks (Paragraph 57).

m. More policy analysis of the rationale for and alternative models of an auto-enrolment savings scheme seems necessary before detailed product design is undertaken (Paragraph 62).

n. There would be significant advantages to Government in bringing people with practical experience of working in industry into the Personal Accounts development team as early as possible (Paragraph 63).

o. A review of value for money to the taxpayer of current and alternative systems of tax incentives for pensions and other forms of savings would help address a remaining significant policy issue (Paragraph 66).

p. The plans for the design and build of Personal Accounts would have to be very carefully scrutinised, costed and compared to alternatives (Paragraph 67).

q. It would be helpful if Government confirmed its policy intentions on promoting personal responsibility (Paragraph 68).

r. Government plans for providing a good, free source of independent guidance in making the financial decisions required by the introduction of auto-enrolment need to be more detailed and costed (Paragraph 70).