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Comparison of the regulatory frameworks for DC pensions

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Comparison of the regulatory frameworks for DC pensions

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- Overview of the research approach
- The regulatory frameworks
- Approach to recent developments
- Differences between the regimes

Overview of the research approach

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- Desk research
- Interviews with 13 representatives from different organisations including:
  - Pension providers
  - Legal experts
  - Advisers
  - Employers' organisations

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Regulation of pension schemes

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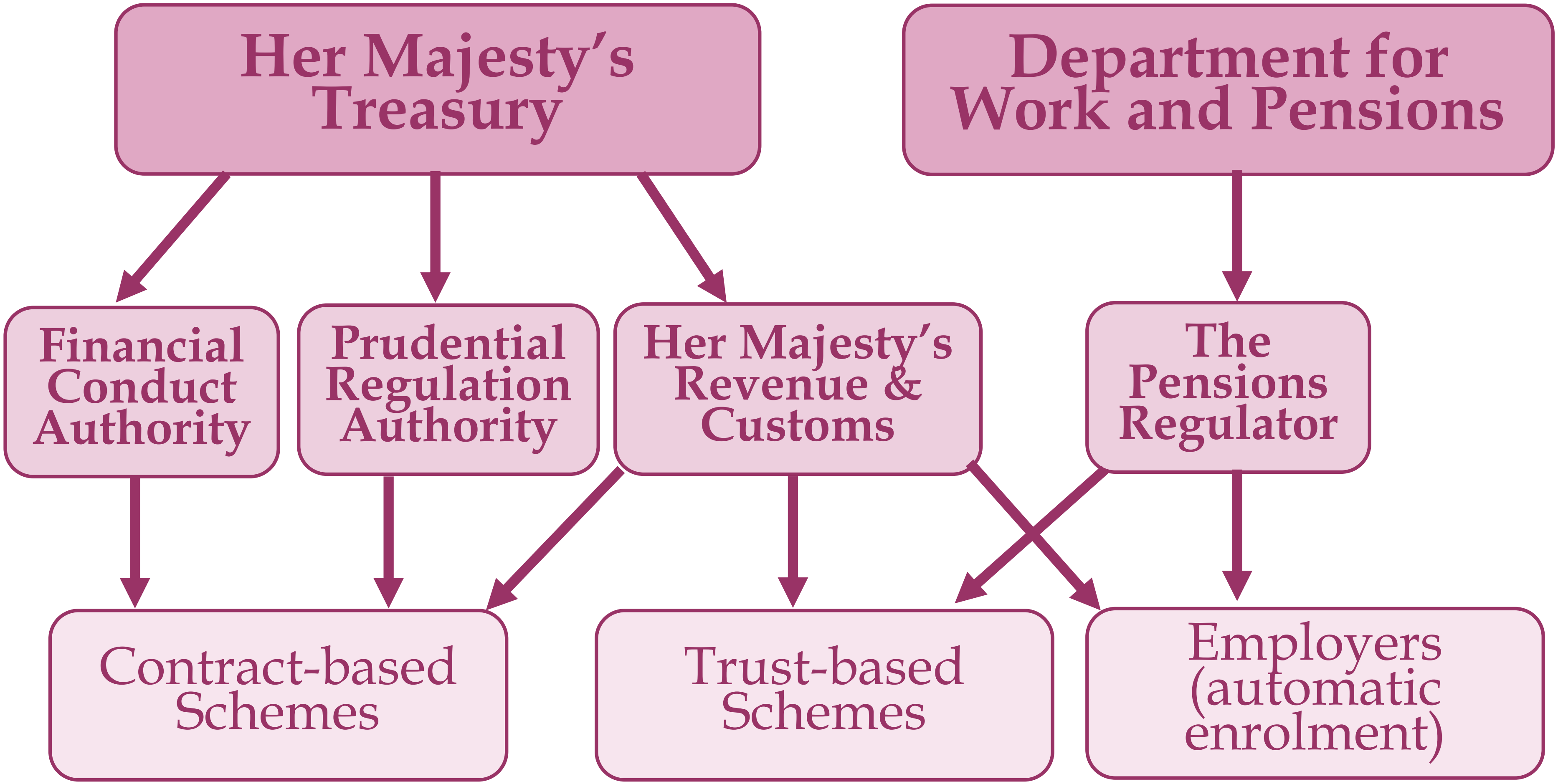

Under contract-based schemes, the employer may select the pension provider but the contract is with the employee

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The employer

- May select the pension scheme
- Makes contributions on behalf of the individual

The contract is between the employee and the pension scheme provider and is subject to contract law

The pension scheme provider

- Administers the pension scheme
- Invests the scheme assets
- Completes the tax return

The employee

Makes pension contributions

Independent Governance Committee

- Assesses value for money of pension schemes
- Challenges the scheme to make changes where necessary

Trustees are in place to provide impartial oversight of the pension scheme – and have extensive responsibilities

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The employer
- Sets up a pension scheme
- Makes contributions on behalf of the individual

Trustees' role is
- To protect the scheme assets from employers' intervention
- To provide oversight (including expertise, where appropriate)

The employee
- Makes contributions

Trust-based pension

The trustees' responsibilities include:
- Reviewing whether the administration provider or fund manager are delivering the best outcomes
- Keeping records
- Completing tax returns

Activities related to a single pension scheme can be regulated by both the TPR and the FCA

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Regulated by The Pensions Regulator

Employer
Activity: Makes contribution on behalf of employee

Trust-based occupational pension scheme: Activities: Employer and trustee administer the pension, and communicate with employees

Regulated by the Financial Conduct Authority

Insurance company manages pension
Activity: manages investments in the pension schemes, and other elements such as the ‘death-in-service-schemes

The member
Activity:
Builds up a Defined Contribution pension pot as a member of a trust-based pension scheme

While the regulators' responsibilities are similar, the FCA has additional responsibilities around integrity and competition

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FCA	TPR
Protection for consumers	**Protection** of benefits of members of occupational pension schemes and members of personal pensions with direct payment schemes
Enhancing **integrity** of the UK financial system	Improving **understanding** of good administration of work-based pension schemes
Promoting effective **competition** in the interests of consumer	

Regulators' approaches reflect different underpinnings of the law and different expectations of trustees and providers

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- TPR regulates the body of law that relates to trustees who are responsible for overseeing assets on a collective basis, and optimising outcomes at the collective rather than at an individual level
- The FCA expects providers to optimise each individual's outcomes

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The regulators have identified some shared priorities in terms of risks to pension savers

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FCA **TPR**

Lower value of DC pots at retirement due to sub-optimal investment decisions or high charges

Risks related to pension flexibilities

- Individual using savings in a way not suited to their needs
- Pension scams

Consumer behaviours including information asymmetries, inertia

Employers, under automatic enrolment, accessing poor quality schemes and advice

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TPR plays an important role in ensuring that employers make contributions under automatic enrolment

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- From April 2014 to March 2015 around 35,000 employers completed their declaration of compliance
- In the same period TPR only issued 22 unpaid contribution notices

Both regimes have strengths that could helpfully inform approaches taken by the other regulator

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Activity	Contract-based (FCA)	Trust-based (TPR)
Rigour	Threshold conditions Ongoing monitoring, including supervision and thematic reviews	Reliance on trustees and whistle-blowers
Communication	Reflects where member is on retirement journey Prescriptive around information provided to members	Can tailor communications to members May not reflect an individual's position on their retirement journey
Compatibility with workplace pensions	Requirement to promote consumer choice less relevant under automatic enrolment	Schemes have the leeway to provide information relevant to the members' situation
Cost of managing pension schemes	Higher volume of work and cost	Lower volume of work and cost

Concerns around lack of conditions to entry centre on the possibility of winding up of some Master Trusts

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- Concerns relate to some Master Trusts only
- Lack of threshold conditions such as solvency requirements
- Concern that Master Trusts without sufficient scale will enter the market and subsequently wind up:
  - Implications for employers (burden of moving employees into a new scheme)
  - Implications for employees (administration costs may be covered by pension scheme funds)
- Master Trust assurance framework is optional but may address this if it becomes mandatory

There is a concern that a lack of transparency may lead to worse outcomes for some pension savers

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- Move towards services being bundled with concerns around conflicts of interest and difficulty of assessing value for money
- Specific concerns for trust-based pensions noted include:
  - Boards of trustees may not feel able to appoint investment managers other than those linked to the Master Trust sponsor
  - Concerns around commercial interests being prioritised over members' outcomes
  - TPR has no remit to promote competition and protect the integrity of the market
- Issue of bundling has been noted for both contract and trust-based schemes

Competing views exist around whether there should be a single regulator

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- Concerns around regulatory arbitrage in current system
- Concerns around any change include:
  - Increasing the burden on employers at a time when they are experiencing a high regulatory burden
  - Volume of law needing to be changed to accommodate move to a single regulator
  - Not clear where a regulator should sit

Conclusions

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- Both regulators have strengths
- FCA has a rigorous framework
- TPR plays an important role in ensuring employers' contributions are paid
- Concerns around the winding up of some Master Trusts. However, new regulations and the Master Trust assurance framework represent a move towards a more stringent approach
- There is a concern that a lack of transparency under both regimes may lead to worse outcomes for some pension savers
- There is a consensus that combining the regulators would not be straightforward