

BBS briefing note

The National Employment Savings Trust – the new name for Personal Accounts

BBS briefing note 47 introduced Auto-Enrolment and the proposed Personal Accounts scheme. We now know a great deal more about the latter, including the new name: the National Employment Savings Trust is the full title but NEST, and the associated logo, will be how it becomes to be known.



This *BBS briefing note* provides further background on NEST.

ESTABLISHMENT AND GOVERNANCE

NEST is established as an occupational pension scheme under trust, and a not-for-profit organization, NEST Corporation, will act as Trustee. Lawrence Churchill (currently Chair of the Pension Protection Fund) will be the Chairman of NEST Corporation and the others on the eight member board have backgrounds in insurance, investment, and public service. The Personal Accounts Delivery Authority, which was established to set up the Personal Accounts scheme, will be wound up from 5 July 2010.

THE PURPOSE AND DESIGN OF NEST

NEST will be open to all employers of any size or sector that wish to use it to fulfill their duty to auto-enrol employees into a pension scheme (see *BBS briefing note 58* on the auto-enrolment requirements).

It is aimed in particular at low to moderate earners who currently don't participate in workplace pensions. The intention is that NEST will complement, not replace, existing provision but whether this will prove true remains to be seen.

NEST will operate as a defined contribution pension scheme with member-earmarked accounts. Members of NEST will have one NEST account throughout their working life into which contributions (including member contributions) will be paid direct by employers.

The minimum contributions required to join NEST are those defined under the auto-enrolment rules, but members and employers can pay more. However, there will be a maximum annual contribution, which has been set initially at £3,600. This feature has been included to discourage employers from using NEST as an alternative to high quality company schemes. Another feature designed to protect company schemes from competition from NEST is a general ban on transfers in or out. The exception to this is at retirement age when a transfer out will be permitted. The maximum contributions and ban on transfers are to be reviewed in 2017.

INVESTMENT APPROACH

A consultation process, based on the discussion paper "Building Personal Accounts: Designing an investment approach", has been undertaken to establish arrangements for the investment of NEST earmarked accounts that are suitable for its target membership of low to moderate earners.

The details of how NEST funds will be invested are not yet known but the expected approach is that NEST will use funds that are largely passive (i.e. index tracking) and are based on a target retirement date. Over the years leading up to that date, the fund will reduce risk, probably by switching into cash and bonds. The intention is similar to the lifestyling approach used by many defined contribution schemes, but the reduction of risk as retirement approaches is made within the



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fund, rather than by switching between funds at member level.

Target date funds have advantages over lifestyling in that fund managers can time moves from high to lower risk investments taking market conditions into account and it is easier to incorporate a wider range of investment classes.

There are likely to be a limited range of options as alternatives to the target date funds, which are expected to include Shariah law compliant funds.

NEST ADMINISTRATION

NEST has been designed as an online business with the aim that member administration "will be delivered largely through e-channels – which could include the internet, email, text messages and future digital platforms". There will be alternative approaches for members who can't access digital channels but these will be discouraged. The contract for the administration of NEST has been awarded to Tata Consultancy Services.

NEST's costs will be met out of the contributions it receives, but with a government loan to cover initial costs. The intention is that NEST should be delivered at no cost to the taxpayer.

The Department for Work and Pensions have announced an anticipated 0.3 per cent annual management charge on accumulated funds with an initial additional charge on contributions of some 2 per cent.

At retirement, NEST members will have the options usually associated with a defined contribution scheme - a lump sum can be taken (currently free of tax) of up to 25% of the fund and conversion of the balance into an income will be by purchasing an annuity. It will be possible to take small funds entirely in cash under the usual HMRC rules.

BBS VIEW

NEST will be the immediate solution to the problem of auto-enrolment for smaller employers. Whether it will appeal to medium to larger employers, who typically will already have pension arrangements in place, remains to be seen. NEST has many limitations and it offers little scope to employers to add value in their pension offering to employees.

Generally, our view is that those responsible have made sensible decisions in establishing NEST as the means of delivering the Personal Accounts agenda of the Pensions Act 2008. However, this will be a huge undertaking with many risks, and the initial 2% charge on contributions looks heavy. NEST will therefore continue to be subject to political risk and could be altered, or even abandoned, if there is a change of government.

