

Introduction

In November and December last year, we consulted on a number of changes to the NEST Rules. The aim of the proposed changes was to align the NEST Rules with some changes to the NEST Order that the Department for Work and Pensions were consulting on, and to improve the effective operation of the scheme for employers and members. The key changes were:

- The ability for employers and members to use contractual enrolment and ‘bulk transfers with consent’ as a means of joining the scheme.
- A proposal to streamline the death benefit rules, and a proposal to allow NEST members to opt in to the exercise of Trustee discretion on death benefits, where those members have concerns about inheritance tax (IHT).
- Giving the Trustee a discretion, on giving notice, to cease the participation of ‘dormant’ employers who have not contributed to NEST for a certain period of time.

The consultation ended on 29 December 2017. This document is our response to that consultation. It:

- provides a summary of the responses received;
- details our response to them; and
- confirms which of the rule changes we intend to proceed with.

We’re very grateful to those who took the time to respond to our consultation.

A list of those who responded is included at **Annex A**.

Responses to the consultation

We received five responses to the consultation, including responses from our members’ and employers’ panels.

Contractual enrolment and joining via a ‘bulk transfer with consent’

Both NEST panels supported these two changes. The employers’ panel commented that NEST ‘must evolve to remove restrictions that inhibit its operation’ and felt that these two changes were an example of this. The members’ panel felt it was ‘crucial that the scheme could function under the same rules as other occupational schemes’ and again felt these changes would meet this aim. The other respondents did not comment on these two changes.

Streamlining the death benefit rule and allowing NEST members to opt in to the exercise of discretion on death benefits

Only one respondent commented on the proposal to streamline the death benefit rules by removing the dependants’ annuity option post age 75. They commented that this change was likely to have a low impact, on the assumption it was rarely taken up, but were concerned that it may be ‘viewed as unreasonable’.

All respondents commented on the proposal to allow NEST members to opt in to the exercise of discretion on death benefits. Both panels, and one other respondent, supported the approach - although the support of the non-panel respondent was qualified by the need for there to be no prejudice to other master trusts. That respondent said they had not identified any such prejudice in the time available.

One respondent did not support the approach and one felt it was surprising and an unusual step which would result in a significant communications challenge and queried whether it would have the desired IHT effect. That respondent felt it would be more straightforward to simply apply discretion across the board.

Those who supported the approach pointed to the fact that it improved the position as compared to the current NEST approach, and that it brought NEST more in line with the market's approach generally. However, they still had concerns around the communication challenge. They felt that members would struggle to distinguish between the two approaches (nominating and completing an expression of wish) and that communicating the difference between the Nomination form and the Expression of Wish form to both members and their employers would be crucial. They also thought communications would be an important means of guarding against scenarios where someone doesn't realise they could benefit from opting in and so fails to do so, resulting in a tax charge. There were also concerns raised about potential costs and about members who would not benefit from this measure cross-subsidising those who would be able to benefit. While the members' panel acknowledged that there is already cross-subsidy within NEST, they suggested that the Trustee monitor the costs and consider charging if appropriate. The members' panel also queried whether the Trustee could automatically apply a narrow exercise of discretion to all pot sizes over a certain size as an alternative.

The respondent who did not support the approach argued that all other registered pension schemes operate trustee discretion for all and NEST would be putting the costs of delivering an IHT product ahead of ensuring good member outcomes. They also suggested that the inertia which keeps automatically enrolled members in NEST, would mean they are unlikely to engage. They suggested that if it's necessary to charge more in order to provide discretion for all, NEST should increase its charge or choose to charge employers.

Dormant employers

The employers' panel said they recognised the need for the Trustee to terminate the participation of an employer in the scheme, in circumstances where they have not contributed for a defined period of time, and do not start contributing by a date notified to them. They felt that the defined period of time should be at least a year.

While the members' panel also recognized the need for NEST to terminate dormant employer accounts, they suggested that communications should clearly set out all the key dates to the employer. They also suggested that NEST consider the scenario of an employer who enrolls some employees, all of whom opt out so that the employer is correctly not making any contributions. That employer would then want to be able to re-enrol those employees at the three-year re-enrolment period but their participation may have been ceased by NEST in the meantime. While they did not

think this was a reason not to make the Rule change, they urged NEST to consider this scenario when implementing employer cessation. The employers' panel raised a very similar example involving a member on maternity leave who stops contributing but will need to be re-enrolled.

One other respondent commented on this proposal. They suggested either writing to employers after about one year but giving them the option to say they wish to continue participating, or if that's not possible, having a longer dormancy period of, say, 3 years.

Length of consultation

One respondent felt the consultation was too short and did not give them enough time to fully consult their members on the death benefits and IHT proposal. They said this was exacerbated by the fact that the consultation also took place during the Christmas period.

NEST Corporation's response

Contractual enrolment and joining via a 'bulk transfer with consent'

We agree with the panels that these two changes align NEST with other occupational pension schemes and will allow the scheme to operate more effectively for employers and members.

Streamlining the death benefit rule and allowing NEST members to opt in to the exercise of discretion on death benefits

As we explained in the consultation, we believe the key reason for offering a dependants' annuity option post age 75 disappeared when the freedom and choice changes came into effect. Our understanding of the market is that we would not be out of line were we to offer a lump sum only and therefore we do not think removing this option is likely to be viewed as unreasonable. We agree it's likely to be low impact as no-one has chosen this option from NEST to date.

As regards our proposals on exercising discretion on death benefits, we are continuing to consider the points made by respondents that other pension schemes operate discretion for all their members without the need to opt in and the fact that the inertia which keeps many automatically enrolled members in NEST could mean they won't engage with the option to opt in. We need to weigh these up against:

- the fact that NEST already operates a different approach to other schemes on death benefits (for reasons related to cost and to the volumes of members likely to be affected by the issue, and the impact on them in a (previous) world where the annual contribution limit and restrictions on transfers into NEST existed); and
- the cost of exercising discretion for all, together with the proportion of our membership likely to benefit from it.

We also need to take account of the fact NEST currently allows members to nominate beneficiaries and have certainty that their pots will be paid to their nominees (if still alive and traceable at time of death) and that it could be unfair to take this right away from members.

We agree with respondents - as acknowledged in our consultation - that our proposed approach brings with it a communications challenge. Were we to go down this route, our plan would be to develop a thoughtful communications strategy taking account of employers as well as members (as advised by the employers' panel).

Taking all these points into account, our preference is to continue exploring the feasibility of both our proposed approach and the other options suggested by respondents including applying discretion for everyone.

On the question of whether the opt in approach works from an IHT perspective, our legal advice is that given the approach still involves the exercise of discretion by the Trustee and the member is not able to direct who the benefit is paid to, this should usually mean IHT would not apply to the death benefits of those who opt in.

Dormant employers

The question of whether the dormancy period should be e.g. one year (as suggested by the employers' panel) or the three years suggested by two other respondents, is not an issue that needs to be agreed at this stage. This is because the proposed rule does not specify a timescale, but leaves this to the Trustee to determine. We do not have any plans to implement this in the short term but are very grateful for the helpful points respondents raised and will take these into account when we do come to determine the timeframe.

Length of consultation

We unfortunately had little control over the start date of our consultation because we couldn't consult in advance of DWP's consultation on the Order changes. This led to our consultation running over the Christmas period. We'll try to avoid this in future where we can. We've considered the consultation timelines of previous analogous consultations (such as by DWP for NEST Order changes) and do not feel this one - just short of seven weeks - is out of line with those.

The Rule changes we intend to proceed with

We intend to proceed with all of the Rule changes consulted on, with the exception of the changes concerning opting in to discretion on death benefits, with effect 6 April 2018. This aligns with the date the Order changes are due to come into effect.

We'll continue to explore the feasibility of our proposed approach on death benefits and discretion, along with other options that have been suggested during this consultation, including applying discretion to all, with a view to making an appropriate rule change early next year.

Annex A

Respondents to the consultation

The Society of Pension Professionals

Salvus Master Trust

The Institute of Chartered Accountants in England and Wales

The NEST members' panel

The NEST employers' panel