

Personal Accounts Enabling a low risk implementation underpinned by a low cost, scalable administration platform



A Response to PADA's PIN Discussion Note

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Executive Summary

Introduction

aquilaheywood is the leading supplier of pensions administration software solutions in Europe. The pension schemes of over 200 organisations and more than 9 million scheme members are administered using our market leading pensions administration systems.

As such we welcome the opportunity to respond to the PIN Discussion Note.

As suggested by Matt James at the Procurement Information Event, we have answered the questions from the PIN that are most relevant to our experience. Before that, we have summarised our view on the key risks to the success of personal accounts and described our proposition that can help to mitigate the risks related to developing and implementing the administration system.

aquilaheywood's Response

Overall we support the introduction of auto-enrolment and personal accounts as a means to provide individuals with the opportunity to save for their retirement through a straightforward, low-cost product.

However, if personal accounts are going to be seen as a success within the UK, we believe that PADA must focus on some key areas. These are set out below.

Maintain Focus on Simplicity

We believe that it will be important to maintain focus on a straight-forward, simple product in order to contain:

- the cost and risks of systems development;
- the operational costs of running the scheme and associated operational risks; and
- the number of employers levelling-down from their current provision.

Increase Focus on Risks

We noted that at the end of the Procurement Information Event on 2 July, Tim Jones said that his main focus was on mitigation of risks. We believe this is totally appropriate because, at the moment, there are very significant risks and much uncertainty surrounding the introduction of personal accounts.

We believe the main risks relate to the following.

Low Take-up

Much of the initial research was carried out when investment conditions and consumer optimism was much greater than currently – we cannot predict the situation in 2012 but recent significant falls in investment markets may well still be in consumers' minds even if there is a recovery in the meantime. There is a danger that other products such as the Savings Gateway will compete in the same market at the same time with better incentives; moreover in the first year of auto-enrolment the minimum employer contribution is only 1% of the employee's

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earnings over a Primary Threshold of £5,500 (or thereabouts) – this is not necessarily a strong incentive for employees to start investing in a private pension, especially if there is a risk that they may not fully benefit from that investment (see below).

Means-tested Benefits

It has been well documented that individuals may not fully benefit from investing in personal accounts as they may lose out on means-tested benefits. We have consistently said to the Pension Commission and others that this is a significant risk to personal accounts; it significantly impacts the communication/guidance process (and related costs) around auto-enrolment and thereafter; and it will no doubt result in some reputational damage that will impact on volumes and the cost of ongoing administration and complaint handling including any legal costs.

Financial Risks for PADA and Suppliers

How the financing of supplier contracts will operate is still very unclear, not helped by the lack of certainty about volumes and the charging structure. It was explained at the Procurement Information Event that PADA expects to ask the Treasury for significant loans to cover the set-up costs and the shortfall in revenue in the early years, but that it will be up to the Treasury to agree to the level of funding required, which may be difficult in the current economic climate. All this means that the profitability for potential administration suppliers is extremely uncertain and the business case for potential suppliers is challenging.

Political Risks

Clearly there are some short term uncertainties about changes and delays to the current Pension

Bill – it is probably not the highest priority legislation change for the Government in the current political climate. In the longer term there is the impact of a General Election in or before 2010 and a potential change in Government. While this will not necessarily stop the introduction of personal accounts, it would be much easier for a Conservative Government to make changes to or delay the introduction of personal accounts.

Contractual Risk

We understand that suppliers will have to contract with PADA and will then have to novate the contracts through to the Pension Board when appointed. We understand that this should be straightforward but the Pension Board will need to be satisfied about the supplier and contractual arrangements.

Implementation and Operation Risk

For this scale of project the implementation risks and ongoing operational risks are potentially very high; it would be somewhat of an understatement to say that the Government does not have a good record of implementing IT projects and driving out the benefits of new systems.

Against this background, we believe that PADA should have a strong focus on mitigating risks and that it is totally appropriate that Tim Jones should make that his parting comment at the Procurement Information Event.

Increase Focus on Deliverability

Given the above landscape, PADA and potential suppliers need to focus on deliverable solutions that can be implemented at a low cost and with low risk but which are scaleable to meet the anticipated

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volume of members, employers and transactions, and are effective in providing a good quality service at a low on-going operational cost.

aquilaheywood's Solution

Our proposal to PADA, the potential suppliers to PADA and the Pension Board is to rely on an existing, proven, robust, scalable, efficient and flexible pension administration system at the heart of any Scheme Administration solution for personal accounts.

We believe that our *administrator* platform meets these requirements and already supports just about all the functionality required for personal accounts. Moreover, it is built on modern technology with all the functionality being web-enabled, allowing suppliers to build employer and individual facing web applications to facilitate communications and straight through processing.

administrator is already in use by many of the UK's largest occupational schemes, Third Party Administrators (TPAs) and Financial Services companies. This is important because, although the NPSS will be an occupational pension scheme, many of the processes and the need for efficiency and customer service quality are consistent with the needs of TPAs and Financial Services companies in supporting large numbers of employers and of scheme members. Therefore we believe that functionality such as Case Management, Document Management, Customer Management, Contact Monitoring, Complaint Handling, SLA Monitoring and Reporting are as important as the comprehensive support that we offer for pension schemes.

Equally important for PADA and potential suppliers will be the ease of integration with other systems, either through web services as part of a Service Oriented Architecture or by using our standard interfaces with Fund Managers, BACS and cheque payments, General Ledgers and Document Production and Despatch systems.

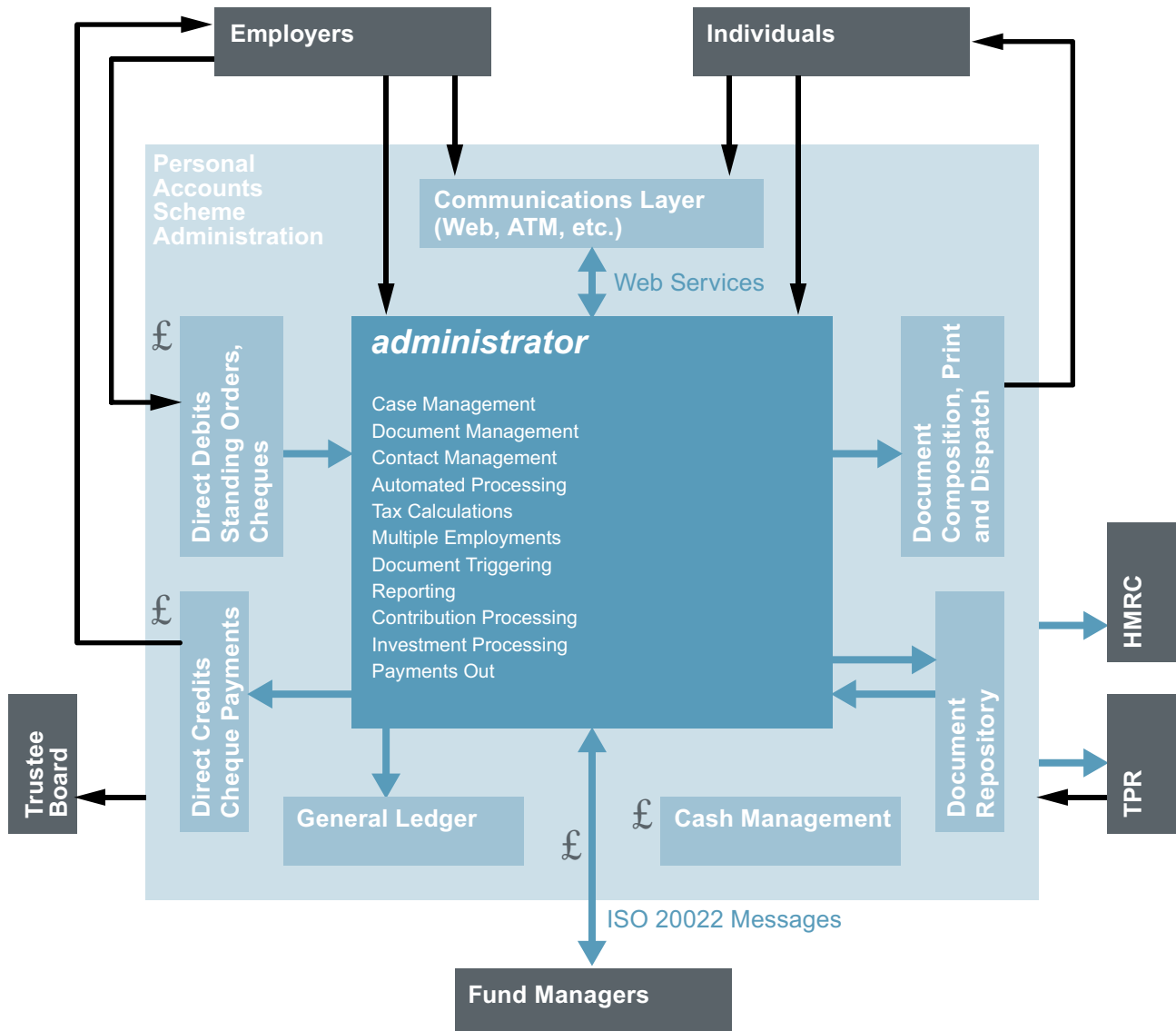
administrator also supports the decumulation stage through the payment of PCLS, pensions and income withdrawal, including flexible retirement and all the related HMRC calculations, monitoring and reporting requirements. While this may not be a day one focus for PADA we believe there will be a case for personal accounts offering a service whereby they pay out pensions/annuities that are effectively costed and reassured by the selected provider rather than passing small amounts of money to the annuity provider to administer a small pension at a potentially uncompetitive rate.

The diagram overleaf attempts to capture in one simple picture how an overall personal accounts Scheme Administration platform could operate. The dark blue areas (including the arrows) represent current *administrator* functionality.

Whilst many of the largest occupational schemes, TPAs and Financial Services companies use the *administrator* platform to administer DC pensions schemes we recognise that even the largest of these does not have the number of members or employers that the PIN Discussion Note asks potential suppliers to assume. We do not anticipate this being an issue but we are anticipating carrying out an independent scalability test of *administrator* in advance of the Procurement Process.

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In Summary

We believe that PADA should focus on simplicity, mitigating risk, low cost and scalability, and implement an existing, proven, robust and scalable, efficient and flexible pension administration system at the heart of any Scheme Administration solution for personal accounts.

We believe that *administrator* is the only existing solution that meets those requirements and we look forward to discussing potential IT solutions in more detail with PADA and potential suppliers to PADA.

What is *aquilaheywood*?

aquilaheywood, comprising *aquila* and *heywood*, is the leading supplier of pension administration software solutions in Europe. The pension schemes for over 9 million members in more than 200 major organisations are run using the group's administration software solutions. Our solutions are used by to administer many of the largest trust based occupational schemes, personal pension and stakeholder pension schemes. We have been central to the UK pensions industry for many years and are regularly called upon for our expertise and experience.

The Group provides solutions to the Financial Services, Third Party Administration, Corporate and Public Sector pension scheme markets in the UK, Ireland and the rest of Europe. Its clients include the Scottish Public Pensions Authority, Norwich Union, Fidelity, Aon Consulting, BBC, Asda, BP, British Airways, the UK Atomic Energy Authority, the Northern Ireland DHSS and Public Services Pension Scheme and the European Central Bank. Over 90% of the members of the Local Government Pension Scheme are also administered on the Group's systems.

administrator is *aquila*'s functionally rich pension administration software solution, which addresses the core administration, investment and communication requirements of all significant pension benefit and plan types. Its modern architecture offers a cost effective and low risk solution with proven capability and quality of delivery. *administrator* is fully web enabled, facilitating easy deployment of transactional web access to employers and individual members through a self-service model.

As such we believe that *aquilaheywood* is well placed to put forward objective comments to PADA. We hope that readers value our proposals and recommendations and would appreciate feedback.

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aquilaheywood's Response to Questions

We have encapsulated our response in the Executive Summary as we believe that these are the key issues that PADA need to address.

To assist PADA in this informal consultation we have provided some additional points to answer the questions below that we believe are relevant to our proposition and haven't already been covered above.

Product Development

1. What do you believe are the critical success factors for the acquisition of employers and retention of members into the personal accounts scheme?

2. What are your views on achieving the target participation level considering the scheme is designed to complement and not replace the existing pension market?

aquila Response

From an overall UK Pensions perspective, we believe that it is critical that there is the right balance between employers setting up their own occupational pension schemes or changing existing schemes into which they auto-enrol employees. We have referred to some of the critical success factors to avoid low take-up on page 3; appropriate communication of clear messages to relevant parties at the right time will be very important in this process.

Our proposed solution provides some mitigation to the risk of low take-up by using an existing, tried and tested software solution to reduce cost and risk.

Scheme Design

The requirement to design a scheme which delivers customer satisfaction and a low-cost service for the members and employers within our target market creates a number of design challenges. We are interested in suppliers' views about how the operating model and business processes might be designed in a way that meets these challenges and we are keen to understand the most significant risks to deliverability and how these risks might be mitigated.

Assuming that the personal accounts scheme will have up to 7 million active savers, suppliers are asked to provide their views about:

- 3. How the process of setting up new employers and automatically enrolling new members can be most effectively designed and implemented, including how to handle such issues as:*
- a. Identity validation and 'know your customer' checks;*
 - b. Members opting out of automatic enrolment and requiring a refund of contributions;*
 - c. The occurrence of members with multiple employers;*
 - d. The automatic enrolment of new members very close to retirement.*

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4. How the process of collecting contributions from up to around 1 million employers each month can be most effectively designed and implemented, including how to handle such issues as:

- a. Minimising the occurrence of errors and exceptions;*
- b. Operating an annual cap on contributions and handling refunds;*
- c. Handling tax relief on different types of contributions;*
- d. Monitoring and dealing with late/missed payments including nil contributions;*
- e. Accepting additional 'lump sum' contributions;*
- f. Complying with anti-money laundering regulations.*

5. How the processes for maintaining accounts can be most effectively designed and implemented, taking into accounts such issues as:

- a. The potential for 'small pots' to accumulate over time;*
- b. Minimising administrative errors and exceptions;*
- c. Ensuring data quality;*
- d. Controlling security and access;*
- e. Handling dormant accounts;*
- f. Managing archiving requirements.*

6. How customer contact should be effectively designed for:

- a. Inbound and outbound activities including regular transactions and life events; and*
- b. Characteristics of the target market such as accessibility, language needs and financial literacy.*

7. Whether any additional complexity in all of the above may arise from the requirement to enrol and collect contributions from self-employed members.

aquila Response

Most of these issues will occur and it will be important to deal with them in a robust and scalable way with as much automation as possible. Many of the transactions are capable of being handled by 'self-service' website applications for employers and employees but we recognise that such technology will not be universally available. Our solution already supports most if not all such transactions. In particular, it already supports:

- a simplified and easy to use auto-enrolment process that has been tried and tested, helping to minimise operational and take up risk;
- automated handling of errors and exceptions, tax relief and other contribution processes.

Again, communications and 'money guidance' prior to auto-enrolment and on-going communications will be key to the success of personal accounts. This is particularly true for any members who may only contribute for a short period, such as those close to retirement or seasonal migrant workers, and who may get little or no benefit from contributions.

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A few additional specific comments:

- We do not anticipate any additional complexity of dealing with self-employed members or dealing with members with multiple employments/self-employments over and above the complexity of communicating the rationale of having Net Pay (NPA) and Relief at Source (RAS) tax relief mechanisms at the same time for different employments. PADA should give consideration to only allowing RAS on all contributions automatically grossed up at the point of payment.
- An annual cap of contributions will need to be monitored every time there is a payment; we believe that it would be inappropriate to only check after the year end, by which time excess contributions will have been invested, significantly complicating the refund process.

Information Systems and Information Technology

Personal accounts must be delivered at low cost in order to provide a viable pensions saving product for low to medium earners. At the heart of personal accounts is a simple low-cost pension product, which receives new customers via an auto-enrolment process.

It is expected that the suppliers for Scheme Administration will make use of existing products and systems that can meet the majority of capabilities for personal accounts with minimal configuration. Further information is required to

understand the extent to which this is possible and to understand the major drivers of risk, cost and time associated with the IS and IT architecture to support personal accounts.

At this stage we would emphasise that we are not evaluating any individual suppliers or product vendor but simply seeking to understand the current capabilities of the product market place to meet the likely requirements of the Authority.

The Authority would value input from suppliers and product vendors on the following topics:

8. What is the functional coverage of your existing solutions and products with respect to the capabilities described in this paper?

9. Which of your existing solutions or products are best suited to supporting personal accounts, and how would they be integrated?

10. What are the constraints of these solutions or products? Specifically, to what extent could those products or platforms accommodate:

a. The functional aspects that differentiate personal accounts from existing defined contribution pension schemes.

b. The volumes anticipated for personal accounts.

11. What will be the most significant cost drivers associated with providing the IS and IT required to support personal accounts?

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12. What set up and ongoing costs can be anticipated with regard to:

- a. Implementing your existing solutions or commercially available products (for example software licences, maintenance, set-up and configuration costs).
- b. Integrating those products to provide the IS and IT required to support personal accounts.
- c. Enhancing those products to meet the functional aspects that differentiate personal accounts from your existing defined contribution pension solution.
- d. Scaling those products to meet the volumes anticipated for personal accounts.
- e. Development effort where the purchase of commercially available products or the re-use of existing platforms is either not possible or is undesirable.

13. What will be the major risks, issues and challenges associated with the IS and IT development to support personal accounts?

14. What technology innovations and emerging standards may provide opportunities for personal accounts?

15. What case studies or reference sites do you have for previous projects with similar scale and complexity attributes to personal accounts?

aquila Response

We have set out how the existing functionality supports the requirements for personal accounts and the scalability issues on pages 3–6. We already support all the key processes that would need to be done within the main administration platform for the Scheme Administration function.

We acknowledge that there are some differences between the requirements for personal accounts and those for a standard occupational DC Scheme. However, the *administrator* platform also supports Financial Services pension products for group schemes and individuals. This allows us to support the broader range of functionality requirements for dealing with self-employed members for example. We believe that *administrator* is the only existing administration platform that supports occupational pensions and group and individual personal pensions. Accordingly, we are not aware of any constraints at this stage.

The significant cost drivers associated with providing the IS and IT required to support personal accounts will be:

- the cost of developing and testing new functionality (but this is not a significant cost for us because of the good fit with our existing functionality);
- systems integration (but this is not a significant cost for us because of the limited number of additional systems required and the range of standard interfaces that we support);

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- development to deal with scalability issues (where we are already identifying if there are any issues that need addressing);
- implementation project costs (we have a strong record of delivering within timescales and budget but this is mainly configuration work which will be an issue to be addressed by potential suppliers rather than ourselves).

There will typically be licence costs but from our point of view these are not “cost drivers associated with supporting personal accounts” as *administrator* is an existing, tried and tested administration platform.

Question 12 about set up and on-going costs has largely been answered in that these will be significantly reduced by using an existing platform that supports the functionality required for personal accounts. Quantifying costs is a matter to be addressed by potential suppliers rather than ourselves.

As regards 12(e), we would suggest that using an existing platform is very possible and highly desirable to achieve a low-cost, low-risk solution for personal accounts administration.

We constantly update our product to take advantage of technology innovations and emerging standards within IT development and in the pension market. Technology innovations include the rapid extension to self-service web applications facilitated by web services, and the extension into wider service oriented architecture facilitating easier and more

robust integration. The gradual adoption of standard messaging between pension administrators and Fund Managers using the ISO 20022 standard messages is enabling straight through processing in a robust and scalable fashion. We would suggest that PADA and the Pension Board should only deal with Fund Managers that support ISO 20022 standard messaging for funds available through personal accounts.

We believe there is an opportunity, if not a necessity, to agree and mandate a similar set of standard messages between payroll providers and the personal accounts Scheme Administration platform from the outset.

Most of our implementation projects are large scale and complex; in this situation implementation issues are probably best addressed by potential suppliers.

Implementation

Given the number of employers and employees expected to engage with the new pension reforms and personal accounts, we expect that the introduction of the employer duties for all schemes, including personal accounts, will be staged over a period of time. This includes the requirement to register with the Pensions Regulator and enrol appropriate employees into a qualifying pension scheme and begin paying contributions.

There are several options that could be used to structure the roll out. A number have already been rejected due to legal and practical difficulties. The current preferred option, subject to formal

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consultation by DWP later in the year, is that the introduction of the employer duties will be staged by means of PAYE scheme size. Within such a framework, there remain several options for a sequencing of the introduction of the employer duties.

Latest estimates suggest anticipated volumes of between 1 million and 1.5 million PAYE schemes and between 4 million and 7 million employees.

Based on these estimates, we would be interested in hearing views on:

16. The risks associated with the implementation and how PADA should mitigate them, in particular scaleability.

17. Which approach, within the overall framework of business size, minimises which of these risks and why.

18. What is the most practical means of staging the implementation and are there any associated legal concerns.

19. The minimum and preferred time period(s) within which the introduction of personal accounts could be safely rolled out, from collections from the first employer to the last in the roll out.

20. How these estimates of time periods vary depending on whether, and if so to what extent, piloting has previously taken place.

21. Which of the risks identified above can be

mitigated with a pilot and which would remain?

22. How should PADA provide appropriate support to employers during the implementation phase so that they are ready and able to engage with personal accounts?

The approach agreed after consultation will be set out in regulations by DWP.

aquila Response

As identified above, implementation aspects are largely issues to be addressed by potential suppliers rather than ourselves.

We have suggested ways to limit risk on pages 3–4 by using an existing, tried and tested administration platform which has been successfully implemented within timescale and budget constraints for a large number of diverse clients over a number years.

Future Industry Developments

What significant developments do you envisage may affect the way in which the personal accounts scheme should be designed, implemented and operated within the pensions provision, fund management and pensions administration markets between now and 2012?

aquila Response

Increasing use of the web by employers and individuals to transact business, carry out enquiries and communicate is clearly a major trend that will undoubtedly have a big impact on the design and delivery of personal accounts.

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As we mentioned earlier, we also believe that the use of standard XML messaging between administrators and Fund Managers and between administrators and Payroll Systems will impact on the design and delivery of personal accounts.

The ISO 20022 message set for dealing with Fund Managers is becoming established and should form part of the personal accounts delivery solution to ensure an efficient, robust and scalable solution.

One can envisage a possible scenario where employers have to remit personal account contributions (employer/employee) through an approved payroll system that supports a standard message format or they have to remit contributions over the web. One of our existing clients uses the latter functionality to collect contribution from small employers using a web application built by us using our web enablement tools. We understand that some PADA representatives have already seen this.

As the leading provider of software solutions for the administration of pensions through occupational pension schemes in the private and public sector and through financial services companies, *aquilaheywood* are pleased to be able to contribute to the debate about the development of personal accounts.

We hope you have found this response informative and interesting and would value any feedback on our response.

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July 2008