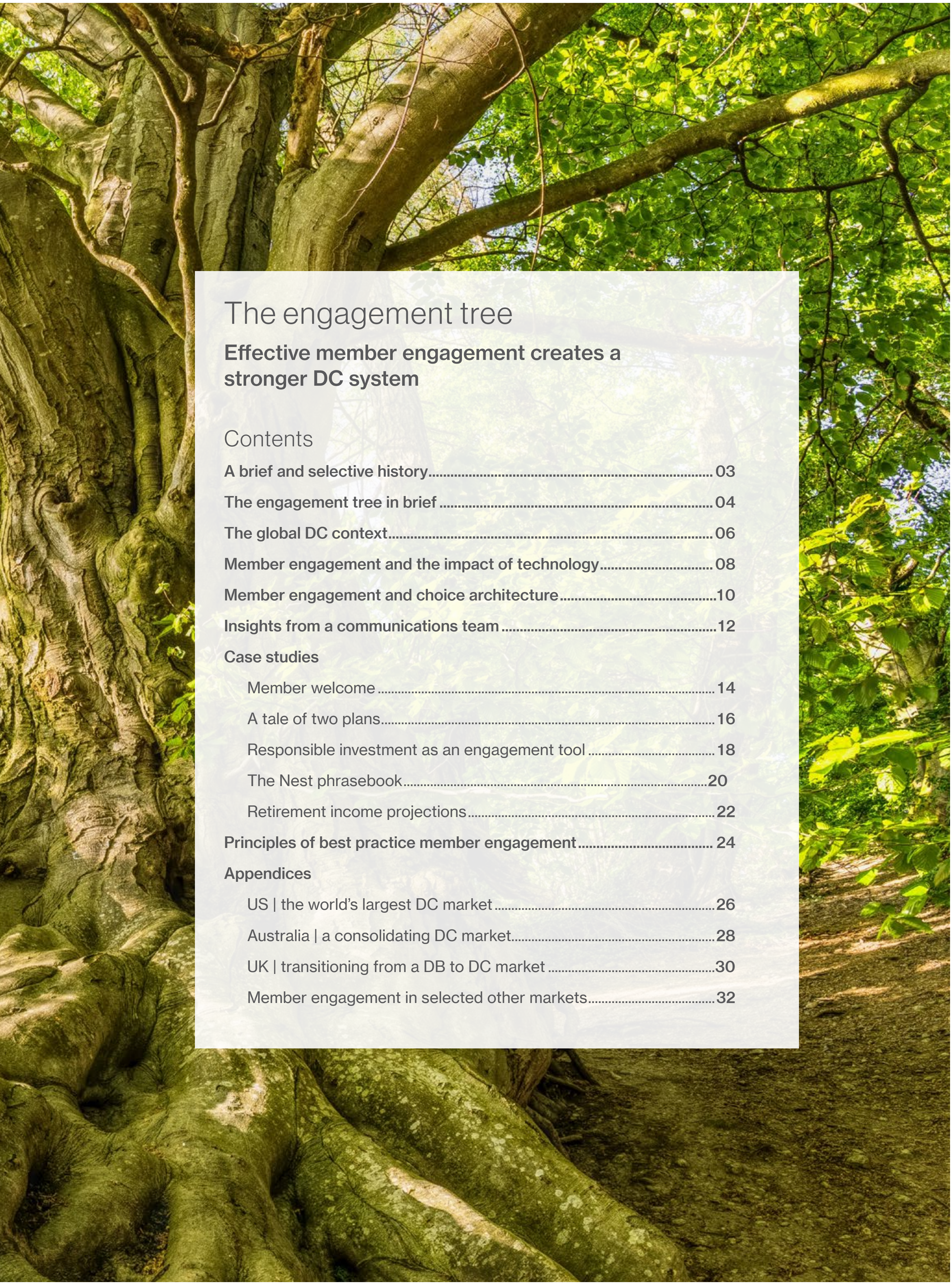
Thinking Ahead Institute

The engagement tree

Effective member engagement creates a stronger DC system



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Contents

Defined contribution working group

This document has been written by members of the Thinking Ahead Group following research and discussion conducted by the Thinking Ahead Institute's defined contribution working group. We are grateful to the members of the working group for their input and guidance, but stress that the authors alone are responsible for any errors or omissions in this paper.

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A brief and selective history

We start by noting that none of us on the working group are experts in engagement, or communications, or technology. We do, however, care passionately about the development and improvement of defined contribution (DC) arrangements for the benefit of the end saver. This paper can be seen as the culmination of our collective, holistic assessment of DC. It was originally planned to be the third paper in a series – it has turned out to be the fifth.

Proposing a stronger DC purpose argued strongly that the purpose of DC is to support post-work consumption. It called for plans to integrate the accumulation and drawdown phases of a DC member: instead of targeting CPI-relative time-weighted returns to the point of retirement, practice needs to evolve to focus on whole-of-life money-weighted returns for individual members.

DC: the movie – It's a wonderful life or Oliver Twist built on the stronger purpose paper, putting the end saver at the heart of the defined contribution pension story. It is about managing the whole of a member's journey.

Lifetime income – the DC system's missing design feature describes what we believe to be the required steps to resolve the absence of lifetime income solutions. In particular we call out the longevity tail – the possibility of living an unexpectedly long life – as the unsolved part of the retirement income puzzle.

Shifts for the DC organisation of tomorrow drew on the insights of ten leading organisations on four different continents that are defining the next generation of best practices.

Turning attention away from ourselves and to the wider context, we note that the evolution of member engagement has largely been about choice architecture, ie how decisions are presented to participants. A key element of this choice architecture has been nudging, whereby, for example, typical enrolment rates in US 401(k) plans have been found to increase sharply when members are auto-enrolled (and offered the choice of opting out) rather than requiring member action in order to enrol.

The use of choice architecture, including nudging, will continue to be a central consideration in member engagement in future, but it is not the whole story. So, in this paper, we set out our high level thoughts on member engagement and propose a set of best practice principles – driven by our belief that **effective member engagement creates a stronger DC system**.

The engagement tree in brief

Effective member engagement is rooted in understanding the audience (members, participants), and so we use a tree as an analogy. Good engagement is a two-way street, we both speak and listen. From here we branch into the what, how and when. Finally, we suggest that effective engagement is an evergreen activity – through the building of rapport and staying in touch we maintain a healthy leaf cover and don't have to regrow new leaves when we next wish to communicate. Besides, leaves send sugars back down to the roots.

Our thinking regarding member engagement is based on a number of beliefs. The relevant ones at this stage are that members generally recognise they are not financial experts; consequently they want help; and are not all the same. This leads to our first best practice principle:

1 Members are individuals and, where possible, should be treated as such

In truth it is usually very difficult to treat DC members as individuals. However, this paper looks forward to the point where technology does allow individual engagement. In the meantime it is possible to better *understand the audience* and below are case studies from Australia and the US to illustrate this. Further, as organisations spend more time and effort *listening* to members they will be able to supplement the data they already have (eg age, gender, account balance, contribution rate, employer etc) and deepen their understanding.

Arguably, *listen* is the area where historic approaches have failed to the greatest extent. Communications tended to focus on pushing out information, with very few channels for members to respond. Interestingly, there are non-verbal ways to listen as illustrated in the Nest case study on responsible investing, where they tested what resonates with members. This can be generalised to monitoring all management information to see how members respond to/act on engagements. Several large DC organisations now have data science teams conducting, among other things, A/B testing to see how different forms of communication resonate with members.

Listening also helps to *build rapport.* The member welcome case study is a great example here – identifying that we need to talk differently to new members, seeking to quickly establish a relationship which can be built on once a level of trust has been established.

"Arguably, *listen* is the area where historic approaches have failed to the greatest extent. Communications tended to focus on pushing out information, with very few channels for members to respond."

2 All communications should aim to help the individual

While this best practice principle can be considered a statement of the blindingly obvious, it stems from the belief that members are not financial experts and want help. It follows that even communications required by legislation or regulation can be more or less helpful, depending on the care and attention put into their crafting. As far as the engagement tree is concerned, this principle relates to *speak* and *what.*

Technology is important here too as it is (a) changing the way we generally *speak* to each other and (b) creating different channels for talking to people about their pension savings, allowing us to overcome barriers such as a widely scattered membership. But the human touch is equally important, as shown by the Nest case study which illustrates the importance of the language used whenwe speak.

As for the *what*, we refer the reader to the section on choice architecture. In short, we view engagement on savings rate, investment goals and retirement income as both important and helpful to the member (it's about managing the member journey[1]). We view engagement on investment choices as likely to be harmful to member outcomes. The First State Super case study on retirement income projections is a great example of *what* to engage on.

3 Respect the medium, as well as the message

As non-experts in communication we tread lightly when it comes to the *how.* However, as the phrase goes, a picture speaks a thousand words, and we are fully convinced that the medium matters. Consequently this paper discusses technology where there is enormous potential power in personalising engagements, and draws on the insights of a full-time DC communications team. The tale of two plans' case studies further illustrates how important the medium is.

The *how* can also refer to the framing used within the communication, and there is a strong choice architecture theme running through the paper. An example of framing is the contribution rate. While the default contribution rate is clearly significant, so is the matching range – this typically leads to members either contributing at the minimum (usually the default) or the top of the matching range, even when they were previously contributing at a higher rate.

4 Engagement bandwidth is limited – use it wisely

This principle relates to *when* and *staying in touch*. A mindset of managing the member journey suggests a natural tailoring of communications and engagement opportunities to different life stages. Respecting a limited bandwidth while seeking to stay in touch represents a more difficult balancing act. It is important to be in regular contact to maintain trust. Annual statements are generally mandatory (and should be made as useful as possible), but more regular, shorter messages can help with engagement.

5 The organisational design implications are within your control

Whether this is truly a best practice principle for engagement, or more generic, we will gloss over. We include it because our thinking represented in this paper made the organisational implications of good engagement inescapable. The importance, and rapid development, of technology suggest that DC organisations will need to be agile in their adaptation. Ditching expensive software before the end of its planned life seems a plausible scenario to consider. Similarly, defaults and nudges have been very useful but we hope this paper clearly makes the case that, when it comes to engagement, nudging is not enough. We think this carries implications for organisations. Finally we note that being helpful to members will take organisations very close to, and perhaps across, the line which delineates where advice starts. We suggest that governing boards should recognise and grapple with this issue before any problems start to manifest. Further, we would encourage fiduciaries to be appropriately brave in their serving members' best interests.

This paper now considers the impact of technology, choice architecture and perspectives from a communications team. There are five case studies, as referenced above, and an appendix providing overviews of the US, Australian and UK markets and introductions to Spain, Chile and Brazil.

[1] As described in DC: the movie - It's a wonderful life or Oliver Twist, Thinking Ahead Institute (2018)

The global DC context

In 2018, total defined contribution (DC) assets across the aggregate of the six largest pension markets in the world[2] exceeded defined benefit (DB) assets for the first time.

For participants, the way the two systems work is quite different. DB requires little involvement from the individual worker: the inner workings of the process are hidden from view. However, DC is personal, and to work effectively, the member must be engaged. By this we mean the member trusts their DC provider, and the communications they are sent, and that they respond appropriately when necessary. We are not advocating for active investment switching in response to large market movements.

This paper describes the nature of the member engagement challenge and sets out pointers for how it can be addressed. We include specific consideration of the three largest DC markets (US; Australia; UK) and propose some best practice principles. The role of choice architecture (colloquially: nudging) is central, and we consider both the theory behind it and its practical application.

Although the participant is the primary stakeholder in the DC plan, they may lack the expertise to make the best decisions. The choices they face can be difficult and confusing, and the issues are unfamiliar to most individuals. In later life, there is the additional complication of cognitive decline *(see blue box across)*.

When members are left to their own devices, certain patterns can emerge. Decisions may be put off or avoided altogether, or they may be too strongly influenced by recent investment performance. After retirement, it is particularly difficult to strike a balance between drawing down too much income (with the risk of running out of money as a result) and drawing down too little (leading to an unnecessarily low standard of living).

Aging and cognitive decline

In *Old Age and the Decline in Financial Literacy*, Prof. Michael Finke[3] and his co-authors find that knowledge of basic concepts essential to effective financial choice declines steadily after age 60. There is, however, no corresponding decline in the confidence that people have in their financial decision-making abilities.

Thus, even though the primary focus of choice architecture to date has been the pre-retirement period, it may be even more important *after* retirement.

Effective member engagement can play a valuable role in preventing poor long-term decision-making.

Nudging: a partial answer

Nudging is widely seen as one of the most effective means (short of compulsion) of increasing participation in a DC plan. Indeed, retirement plan enrolment is one of the central case studies of the book that gave nudging its name[4]. We can be confident that, for the great majority, joining a retirement plan is an appropriate decision. This allows us to be comfortable taking a paternalistic stance, auto-enrolling those who are eligible[5].

[2] US, Japan, UK, Australia, Canada, Netherlands. Source: Global Pension Assets Study 2019, Thinking Ahead Institute. DC and DB assets combined across those six markets totalled $36 trillion.

[3] Michael S. Finke, John S. Howe, Sandra J. Huston (2017) "Old Age and the Decline in Financial Literacy" Management Science 63(1).

[4] Richard H. Thaler, Cass R. Sunstein (2008) Nudge: Improving Decisions about Health, Wealth and Happiness Yale University Press.

[5] In most countries, auto-enrolment comes with the choice of opting out, hence the notion of libertarian paternalism, which is the founding principle of Nudge; the book was largely based on an earlier paper by the same authors with the title Libertarian paternalism is not an oxymoron.

What works for enrolment does not, however, necessarily work as well for other important DC planning decisions. These other decisions are generally less straightforward, and are more heavily dependent on the individual's circumstances and priorities. For example, it is less easy to be confident in a paternalistic approach to investment decisions or the level of drawdown after retirement. Those decisions are more nuanced than auto-enrolment. Choice architecture, or nudging, can still play a role, but is not an entirely satisfactory answer.

Even auto-enrolment can be a double-edged sword, if the contribution rate is static or set at a low level. Some participants may stick with the lower default rate, assuming this to the appropriate rate at which they should be saving. Exactly such an effect has been observed in the US, where a 3% default contribution is widespread[6].

A few of the questions for which some member engagement is particularly valuable are: the level of saving, the amount of investment risk to take, the rate of income drawdown after retirement, and longevity tail insurance. In each of these cases it can be difficult to generalise a typical participant's needs to the whole population. Simply put: one size may not fit all.

Gathering the data for targeted solutions

Better nudges and more customised defaults are possible if more data can be gathered. This does not necessarily require the direct involvement of the participant, as long as the provider is able to get the required data from a different source. For example, many DC plans around the world use a default investment strategy that is based on a participant's age. But some are basing their approaches on a broader suite of data, including: gender, account balance, salary, market conditions, estimated social security benefits, deferral rates and expected timing of withdrawal/ target retirement age. The value of such customisation is greater at older ages, as the account size increases and there is bigger variation in individual circumstances, needs and preferences.

As technology and data management advance, the possibilities for segmentation along these lines will grow.

Clearly, far more is possible if the participant is directly engaged. Member input allows outside assets to be taken into consideration, customisation of risk preferences, and a more precise specification of goals and priorities. Here, too, technology may help. For example, gamification may offer a more accessible (and, indeed, reliable) way to express risk preferences than traditional questionnaires. By lowering the barriers to direct member engagement, technology can offer the possibility of solutions that are more targeted to the individual's needs.

Member engagement

The DC system globally is a work in progress and will continue to be so for the foreseeable future. The general level of member engagement currently falls short of what it should be. This shortfall is being addressed by leading organisations around the world in various ways. In the appendix, we look more closely at the state of play across the three largest DC markets in the world.

[6] Brigitte C. Madrian and Dennis F. Shea (2001) The power of suggestion: inertia in 401(k) participation and savings behaviour The Quarterly Journal of Economics 66(4). Thaler traces the origin of the 3% level to a hypothetical plan description in a June 1998 Department of Labor ruling. The authors of that ruling chose a low contribution level because it was "less likely to arouse opposition and at the very least would establish the guiding principle." They did not anticipate the anchoring effect this would have. Richard H. Thaler (2015) Misbehaving: the making of behavioral economics W.W. Norton.

Member engagement and the impact of technology

Technological development is opening up new possibilities in the field of member engagement

Technology may prove especially valuable in supporting the definition of clear objectives and in improving interaction with the participant (for example, through gamification)

Technological advancement presents challenges as well as opportunities for DC member engagement

Throughout the development of defined contribution over the past fifteen years, it has been taken as given that member engagement is difficult. This has led to a move away from participant education towards choice architecture, as discussed above. This can be seen as a form of member engagement, albeit indirect.

Improvements in technology allow for a better understanding of an individual's circumstances even without their active input. This in turn permits more customised solutions and refinement of DC strategies. Technology also lowers the barriers to getting specific input from individuals through direct engagement. Hence, the aspiration of DC 3.0 to significantly greater customisation is closely tied to advances in technology. We know that machine learning has made massive strides in some areas; that artificial intelligence is developing, albeit with technical arguments over whether it is truly intelligent; and we hear that quantum computing is almost with us. What we do not know is how all of this will affect the delivery of DC. Since the future path of technological change is uncertain, this creates path dependency for the development of member engagement within DC plans[7]. Whatever the path, it seems likely that the norms of DC plan operation will be significantly reshaped by technology in the coming decade.

The advice model

The role of advice within a DC structure can be problematic. The possibility of conflicts of interest means that regulators take an interest in this area, and this in turn makes organisations wary. In the context of investment advice, the possibility of sound advice leading to losses is unavoidable. This can make fiduciaries risk averse. Yet, without guidance and advice, plan participants can be less likely to take appropriate actions.

Here, too, technology appears to offer the prospect of a way forward. Indeed, the hyper-customisation that we have argued is a defining feature of DC 3.0 is probably only achievable through better technology.

Technology could be especially valuable in supporting the definition of clear objectives for a particular individual.

Gamification

Future technology in the DC system is likely to leverage the principles of gamification. Gamification applies elements of game-playing to non-game contexts. For example, a DC plan may be able to improve its interaction with participants via game-like interfaces. Points and badges can be awarded, for example, for providing beneficiary nominations or other information, or for completing education modules.

Gamification potentially may prove particularly useful in establishing risk tolerance. This is notoriously difficult to estimate, partly because the concept itself is rather loose.

[7] Technology is not the only source of path dependency; regulation is another. Indeed, variation across markets is more likely to be driven by the regulatory context than by differences in technology.

Total wealth management

For most DC plan participants, the plan is only one part of their total balance sheet, which may also include other retirement arrangements (eg from previous employment), other savings and home ownership. For the employer, the plan is generally only one part of the benefit program, which may include broader financial wellness elements.

As technology moves towards greater integration of total wealth management, the question will arise of where the nexus for this should sit. If the DC plan aims to be the focal point of total wealth management, then considerable effort will be needed to draw in the broader elements. If, on the other hand, the focal point lies somewhere else, then the plan will need to integrate effectively into the appropriate program. At this stage, it seems likely that different patterns will emerge in different markets.

Challenges

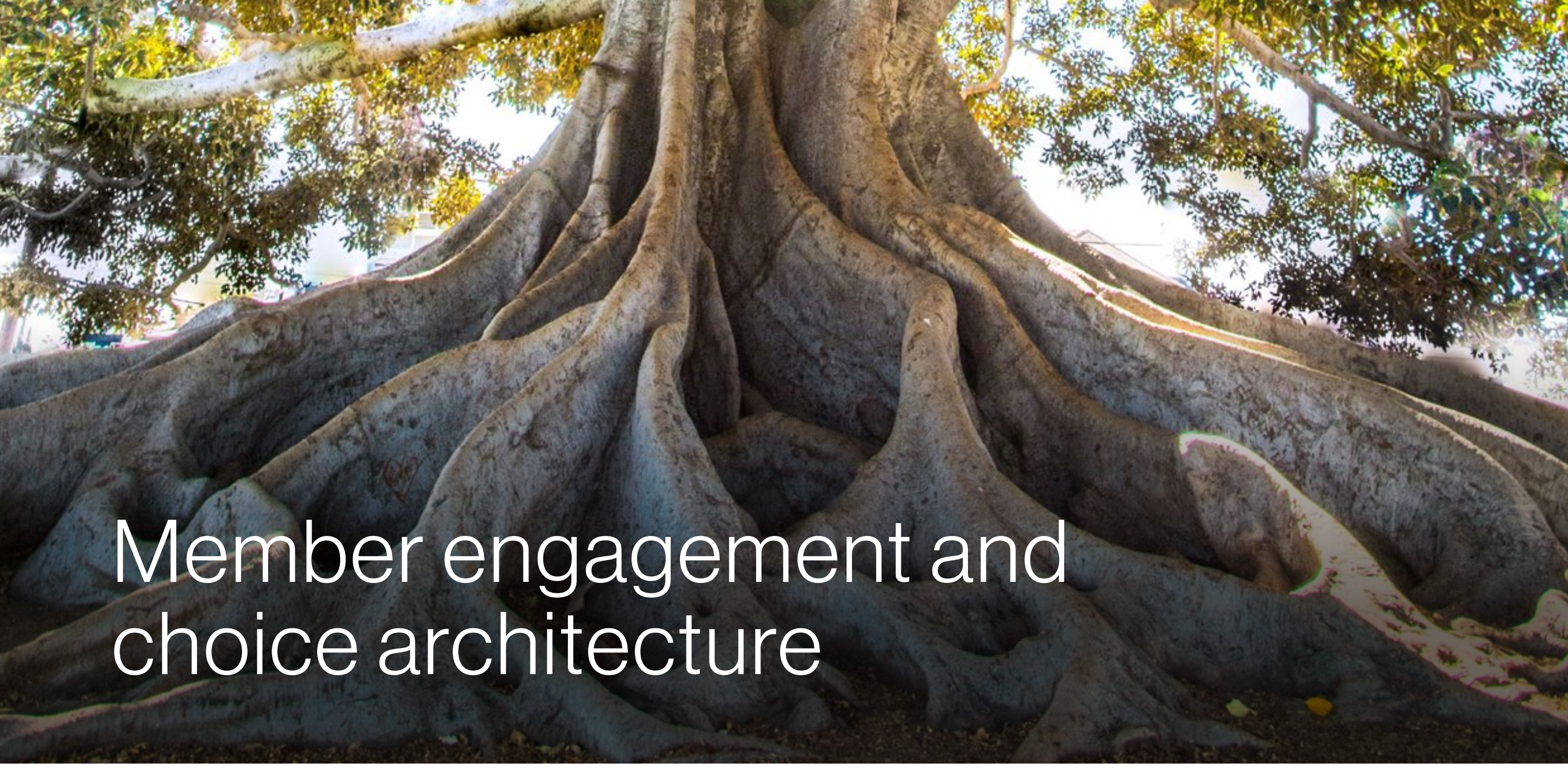
Technological advance presents challenges as well as opportunities for DC member engagement.

The increased potential for cybercrime is one notable risk. As noted in a recent TAI study[8], security has become a pressing issue for some large DC providers. In the past, retirement programs have typically had less cause for security concerns than other areas of financial services, partly due to low levels of transaction. Increased technological sophistication could bring increased risk of fraud.

Increasing the profile of, and ease of access to, a DC account also creates the possibility of an increase in undesirable activity: specifically, accessing balances for non-retirement purposes (leakage) and/or overtrading. On the latter, the weight of evidence has, for many years, shown that participants' tendency to chase returns means that higher levels of trading are strongly associated with reduced rates of return.

The final challenge we would highlight with regards to technology is the expense. As the pace of development continues to accelerate, the cost of remaining competitive may become an increasing burden for DC providers, and prohibitive for those that lack scale.

[8] Shifts for the DC organisation of tomorrow. Insights from a global best practices peer study, Thinking Ahead Institute (2019)



Member engagement and choice architecture

The concept of choice architecture has been embraced by the DC community, especially in regards to plan enrolment

For other elements of DC plan design – including contributions, investment, retirement drawdowns and insurance – effective choice architecture demands a greater degree of member engagement

The value and the limitations of choice architecture

As behavioural economics gained prominence in the early 2000s, the principle of nudging gave the UK and US DC systems a solution to a long-standing problem: how to get workers to join the plan. Defaulting workers into the plan meant that the only non-participants were those who had a clear preference to opt out; the many workers who previously would not have joined due to inertia, lack of information or unfamiliarity were now being enrolled in the plan rather than left out. The impact has been significant: typical participation rates at US plans with an auto-enrol feature are around 90%, compared with 68% at plans that do not[9]; in the UK, almost 10 million workers were enrolled into DC plans in the five years following automatic enrolment legislation in 2012[10].

Choice architecture is built around the recognition that member engagement can be indirect a well as direct and that those who do not select an option would not necessarily have selected its opposite. Hence, effective choice architecture design involves a judgment of where to seek direct member engagement (positive input) and how to manage indirect engagement (default pathways, usually with the ability to opt out).

The success of auto-enrolment resulted in a shift of philosophy at many plans. No longer did fiduciaries see their primary responsibility as being to ensure that members had sufficient options available for an appropriate choice to be made. Instead, better outcomes were in practice more likely to be achieved by focusing attention on the default options, ensuring the plan offered reasonable and prudent strategies for the broad participant base.

On the question of plan enrolment, effective choice architecture demanded very little direct member engagement – workers are allowed to opt out but otherwise provide no input. Once individuals are participating in the plan, however, it is helpful to have a somewhat higher level of engagement. Specifically, we will consider the key questions of contributions, investment and retirement drawdowns.

90%

typical participation rates at US plans with an auto-enrol feature, compared with...

68%

at plans that do not [9]

[9] Defined contribution retirement plans take center stage, 2017 Defined Contribution Plan Sponsor Survey, Willis Towers Watson.

[10] https://www.pionline.com/article/20181218/ONLINE/181219770/u-k-auto-enrollment-rules-boost-worker-participation-in-dc-plans

Savings rate

In most of the world, typical DC contributions fall well short of the levels seen in defined benefit arrangements[11]. As a result, pensions adequacy is a concern.

Setting a default contribution rate involves a trade-off between adequacy (retirement provision is an expensive undertaking) and acceptability (potential participants might be driven away if the cost is seen as too large because it reduces current consumption). In the absence of direct member engagement, this trade-off tends to result in a lower, rather than higher, contribution. Indirect engagement can provide a limited solution: for example, auto-escalation approaches such as Save More Tomorrow[12] can help to overcome behavioural impediments to saving.

Investment

One reason for fiduciaries looking to do more than simply ensuring sufficient options are available to participants is that results from that approach were poor. Defined contribution plans have tended to underperform defined benefit over long periods, with participant habits such as chasing returns one factor in that underperformance[13]. In addition, a number of recent Australian studies have shown that members who make a choice tend to underperform those in defaults.

So one area in which member input can justifiably be seen as (in most cases) undesirable is the question of market timing. Asset allocation and portfolio construction are specialist skills. As with the question of auto-enrolment, it makes sense to allow individuals to over-ride default strategies – but in the majority of cases, better outcomes can be achieved if members are not expected to become investment specialists.

However, appropriate investment strategy is not derived only from market opinions and analysis, it also requires a clear specification of circumstances and objectives. In this aspect, member engagement is valuable. Better decisions can be made if they are based on the total financial picture of an individual (including other savings) rather than in isolation. We have characterised DC version 3.0 as being hyper-customised; this represents an extension of choice architecture from a crude focus on default paths only, toward a richer structure drawing on a broader set of input data.

Retirement drawdowns

A correct understanding of objectives is even more important when we consider the retirement period. A DC plan may play a number of different roles. For some, it is a supplemental top-up to a defined benefit plan, intended to provide additional discretionary financing to support a desired lifestyle. For others, it is the primary source of capital to support retirement, and is being counted on to provide income throughout the remainder of life, however many years that might be. For yet others, it is simply part of a wider portfolio of investment assets, and is likely to remain primarily an investment vehicle even throughout retirement, and to be incorporated into estate planning strategy. Or it may be seen as a rainy day fund, a reserve against unexpected contingencies. Or it may be a combination of these.

Because these situations vary so widely, member engagement takes on particular significance in the lead up to retirement. Through direct engagement with the member at this stage, a more accurate understanding of the individual's financial context can be obtained, allowing better investment and drawdown strategy than would be possible using choice architecture that attempts to adequately cover all the possibilities at once.

In the TAI paper *Lifetime income – the DC system's missing design feature,* we call out the longevity tail as the unsolved part of the retirement income puzzle: "it's the longevity tail risk – the possibility of living an unexpectedly long life – that is the problem. This is why we argue that this is really a longevity tail insurance problem." For reasons relating to supply, to demand and to other contextual considerations, the longevity tail insurance problem is a difficult one to solve. The paper notes that choice architecture may be able to play a role in addressing the demand questions in particular.

"...member engagement takes on particular significance in the lead up to retirement. Through direct engagement with the member at this stage, a more accurate understanding of the individual's financial context can be obtained, allowing better investment and drawdown strategy..."

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[11] Australia comes closest to DB-like contributions. The Australian superannuation guarantee currently sets a 9.5% contribution rate and relatively few participants elect to contribute more than that. For comparison, it has been estimated that the contribution rate required to match a typical UK DB arrangement (fuly guaranteed, fully indexed etc) would be 40% or higher.

[12] Richard H.Thaler and Shlomo Benartzi (2004) Save More Tomorrow™: Using Behavioral Economics to Increase Employee Saving, Journal of Political Economy 112(S1)

[13] See for example, Boston College's work at https://crr.bc.edu/briefs/investment-returns-defined-benefit-vs-defined-contribution-plans/. Over shorter periods, relative returns are driven by asset allocation differences (DC has higher allocations to equity markets, so tends to do better in strong equity markets). Fees are the third significant source of difference.

Insights from a communications team

In this section, we look at the question of member engagement from the perspective of communications. The section consists of an analysis of current communication trends provided by Willis Towers Watson's DC communications team, with a focus on how these trends can be applied to improving member engagement.

1

Using behavioural insights

Communications can be considerably improved by recognising that member behaviours will persist and taking the responsibility for adapting our communications to accommodate them.

- If members think pensions are difficult to understand … we should ensure our messages are simple, targeted and relevant. We can also support members by providing them with financial education
- If members think pensions are a long way off … we can use projections to show members the long term impact of their decisions
- If members think pensions are just a small part of their future planning … we can position pensions as part of broader financial wellbeing
- If members only think about their pension at key financial moments … we can target members at the right time. For example, starting to deliver pre-retirement content from age 50
- If members think having debt means they cannot save into a pension … we can educate them about debt management.

2

Using insights drawn from data

We return to our belief that members want help changing their pension behaviour for the better. In this light, using data insights in communication design can increase engagement and influence behaviour because:

- Consumer channel communication is increasingly data-led, targeted and personalised. Members will come to expect this for their pension communications as well
- E-marketing journeys can respond to member behaviour. Using artificial intelligence we can build individual experience profiles, eg "you looked at this page so we think you may also be interested in this page too"
- Dynamic portals can aggregate relevant content all in one place – and the more mobile-friendly, the better
- We now have more data to help us understand members' behaviours. This informs who to target this quarter, what changes to make, and what to measure so that we can learn for the next quarter.

3

Applying content and design insights

We can also learn from external marketing techniques:

- Information is retained better when it is paired with a relevant image
- Infographics, numbers, illustrations and layering content are easier to read and follow than written-only directions. This is true both online and offline
- Less is more. Attention spans are short and drip-feeding content helps to avoid overload
- One message at a time
- People love video. Short, bite-sized chunks of animated content makes the complex simple and connects emotionally with members.

4

Using multiple communication channels

In a multi-device world, different employees have different preferences. Technology plays a big role in multi-channel development. Pension management on the go from our phones is being normalised, just as for banking, payment systems, insurance policies and credit card statements. Social media has saturated peoples' lives, even older generations. Facebook can be more effective at driving action than a letter sent in the post.

Social media platforms used by UK internet users, by age, September 2107

% of respondents in each group

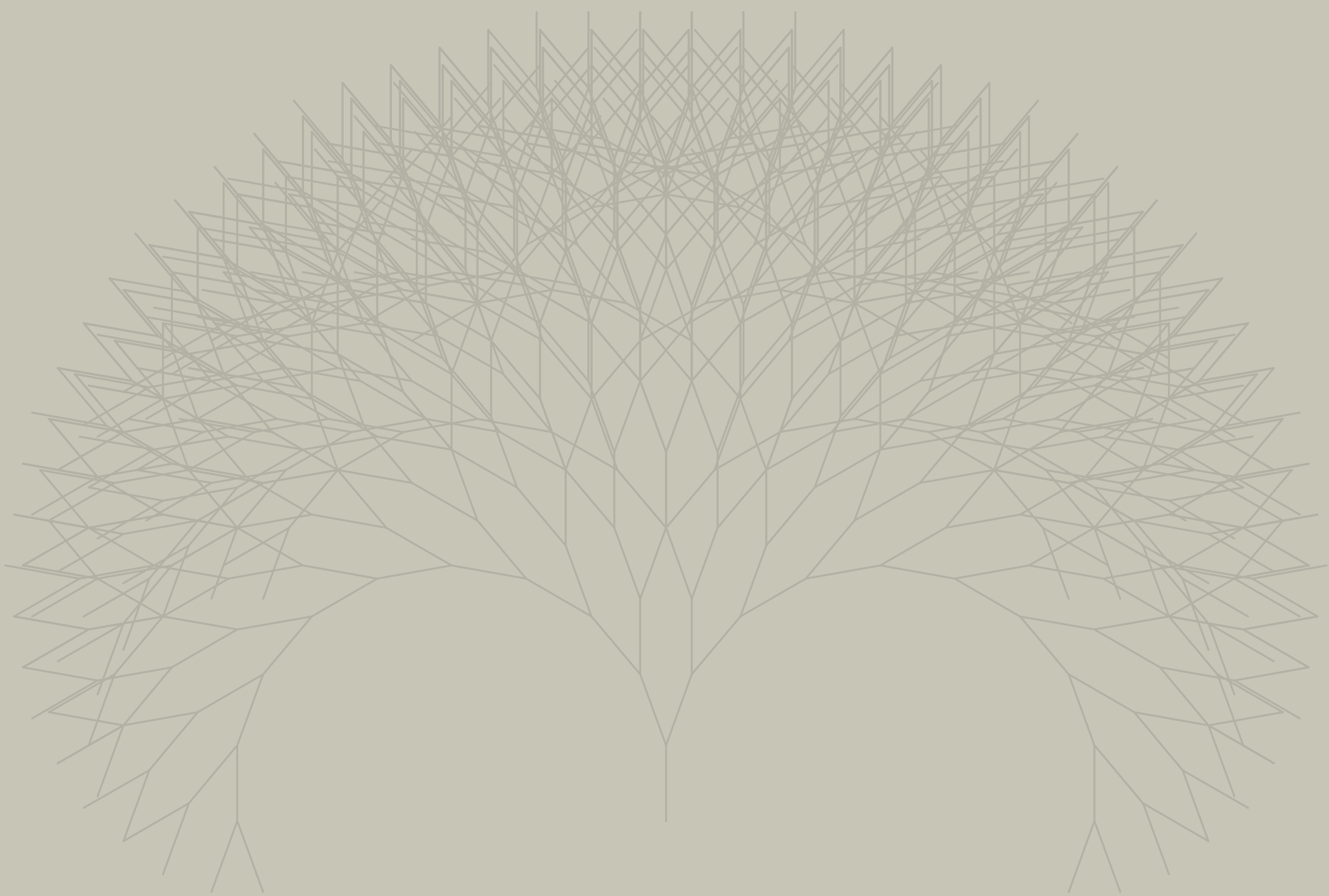
	16-22	23-34	35-49	50-65	Total
Facebook	75%	80%	69%	58%	71%
YouTube	72%	55%	39%	32%	52%
Twitter	44%	37%	31%	17%	33%
Instagram	59%	38%	16%	9%	33%
Snapchat	56%	20%	6%	3%	25%
Pinterest	16%	20%	13%	12%	16%
Linkedin	8%	20%	17%	12%	13%
Tumblr	17%	6%	2%	1%	8%
Twitch	13%	4%	1%	-	6%
Other	2%	1%	1%	1%	1%
None of the above	3%	5%	15%	26%	11%

Note: n=3,007

Source: BBC Newsbeat conducted by Ipsos MORI, Sept 25, 2017

Case study:
member welcome

Market: Australia
Focus: ***understands*** that new members (***when***) have different needs; a series of communications (***stay in touch***) to ***build rapport***



The first contact with a new plan member sets the tone for the future relationship. First State Super, an industry fund based in Australia with around 800,000 members, created a member welcome program in order to provide a positive initial experience and to make use of this critical window of opportunity for positive engagement.

New joiners are excluded from main fund communications in order to be given a tailored experience. Within ten days of joining the fund, a welcome pack is provided to encourage key actions that will help protect and grow their super: (a) registration for online access (b) consolidation of super accounts (c) nomination of a beneficiary, and (d) consideration of increased contributions. As part of the welcome experience, members are sent campaign communications at 10 days, 30 days, 2 months, 3 months, 6 months, and 12 months after joining the fund. A sample of new members also receive welcome calls within the first fifteen days of joining.

The list of key actions is dynamic and updated as members take (or do not take) each step. As a member progresses through their 'to do list', actions taken are ticked off the list and their progress is noted. Members can choose to take all their actions up front or at their own pace. Throughout the welcome experience members will receive additional nudges designed to reengage them with the task list. Follow-up contact is made (if necessary) after six months as a prompt for any outstanding actions to be taken. A summary of activity is provided at twelve months (or earlier, if all of the initial engagement steps have been taken).

The majority of new members join the fund through their employer, so the welcome program can serve to counteract passivity and the sense that superannuation is not "real money". It is important to provide easy points of contact so that the initial window of opportunity to engage is not missed (the most common enquiries from new members are "am I a member?" and "what is my member number?"). For the same reason, testing of different designs implied that drip feeding of information made the program less effective.

The program incorporates segmentation of plan membership, allowing customisation of communications. This includes identifying those members who may require financial planning (such as those approaching retirement, or with large account balances and/or high contributions). The campaigns are also segmented by age so that the benefits are expressed in terms relevant and attractive to the target audience.

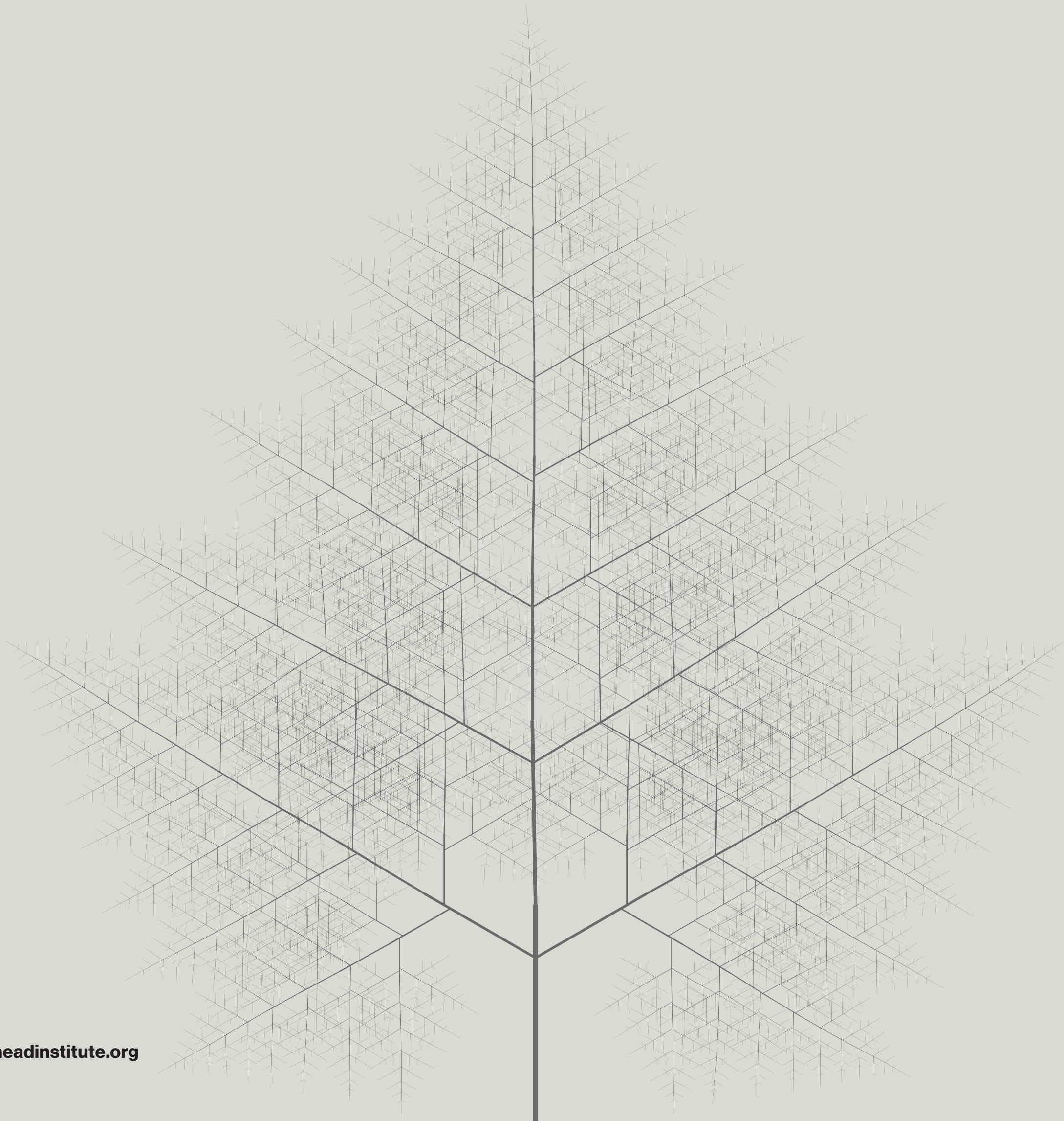
Although relatively new, early signs are that the program has been effective. For members with online access, response rates have been strong, with email open rates around 60%. Nineteen percent of members on this program have rolled-in (transferred in other super balances). This is an 18.5% increase in members taking action based on the business-as-usual campaign program (ie members with a tenure of 12 months plus). Consolidation is especially important in the Australian market for cost management, due to dollar-based fund charges and the presence of insurance premiums.

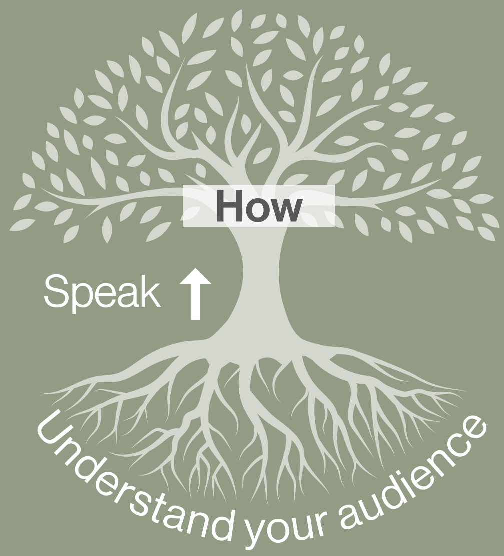
Beneficiary nominations and the number of members electing to make additional contributions are also higher.

The long term objectives of the project are to encourage actions that improve member outcomes (building wealth, managing costs, and ensuring access to advice where appropriate) and to support member retention for the fund. To that end, it is never too soon to engage with members and this program has identified and successfully made use of an important window of heightened awareness, interest and engagement.

Case study:
a tale of two plans

Market: US
Focus: ***understanding*** the respective target workforces, and choosing appropriate communication channels (***how***) to ***speak***





Collectively, American plan sponsors spend millions of dollars each year to increase participant (member) engagement and education on retirement savings. Much of the money spent is focused on technological enhancements to reach participants in new and exciting ways. But different situations call for different tactics. Below is a tale of two US plans and their different ways of successfully engaging with their employee base.

The workforce of Company A, a construction company, was rarely in contact with technology, so would creating a new app or online portal connect with them? Since technological solutions only solve problems if employees use the technology, the company decided to focus on human interaction and conversation to drive engagement. The benefits team travelled to job sites and had conversations with employees about the importance of retirement saving. They found that employees responded positively when they saw that their corporate office cared about their individual well-being. This solved the problem of employer trust, but the company didn't stop there.

The strict work schedules maintained by construction managers left little time for conversations on retirement saving. Often, without a foreman's support, face-to-face interactions would never take place. In response, the company created a new position, the "communication expert". This individual was experienced with retirement benefits, was known to the workforce and enjoyed strong connections with the project foremen. The benefits team would go to each site, engage and educate the foreman, and encourage workers to sign up for the plan. With the foreman's support, employees were much more likely to sign up for the plan.

The company decided not to follow the latest trends in participant engagement technology; instead, they found their own solution, one that was more sensible and effective given their employee demographic. They didn't care if it was considered old-fashioned, they cared that it worked.

Company B chose a different route. It is a technology company, with a younger, more-tech-savvy plan participant base that did not engage well with traditional methods such as reading brochures or attending meetings. An online approach was needed, and the benefits team decided to split their approach into two distinct parts – the *medium* and the *message*. The online benefits portal (*medium*) is comprehensive, easy to navigate and technologically advanced, but the *message* is where Company B really went on their own path.

Although auto-enrolment was an important first step, increasing participation from below 25% to over 75% over 5 years, Company B knew they needed to do more. Realizing that their youthful participants would respond well to entertainment, the benefits team incorporated a range of fun sessions to pass along information. These included game-show sessions, where participants had an entertaining way to learn about maximum company contributions, and an explanation of how a 401(k) match works based on a dating site analogy. Company B continued to evolve their approach, in response to changes in the technological landscape and to the lessons learned from how their participants reacted to the messaging. The benefits team has since added several online videos, with topics ranging from the most basic to complex, and performed benchmark studies to determine how effective their messaging was. Communication is moving away from simply describing plan mechanics and investment basics to a more comprehensive discussion around retirement readiness.

So while Company A's approach was built around traditional forms of communication and building employee trust, Company B's was online and designed to be informative yet fun.

Company A and Company B's retirement plans look very different on the surface, but at their core they align on one simple principle: **know your employees**. These two plans found success while using significantly different approaches because each asked the right questions: 1) will this provide the easiest and most effective way to contact employees? and 2) will participants respond positively to these attempts?

Once a plan has a better understanding of how its participants absorb information, the job of driving engagement becomes much easier.

Case study: responsible investment as an engagement tool

Market: UK
Focus: there are non-verbal ways to ***listen***

Nest (the National Employment Savings Trust) was set up in 2010 by the UK government as part of the introduction of a national auto-enrolment programme, to ensure that every employer has access to a workplace pension plan. This origin leads to particular challenges around member engagement. As CIO Mark Fawcett notes in the introduction to the 2018 Responsible Investment Report, “Generating interest in pensions is hard at any time, engaging savers who haven’t made an active choice to join a pensions scheme is even harder”.

Although a relatively young organisation, Nest has grown quickly. From a standing start, by 2018, it served over 6 million members. As the initial set-up phase passed, and as account sizes have grown, questions of member engagement have moved up the agenda. Hence the organisation’s conclusion that “now is the right time to start thinking about how we can talk to our membership about their investments in a more meaningful way”.

Responsible investing is one of the first channels chosen for doing this. This choice aims to “help engender trust in pensions, improve engagement and provide members with a greater sense of ownership and appreciation of their pension”.

Members surveys supported this approach. When asked, for example, how important it was to them that Nest considers how the companies and markets they invest in are run, and how they treat people and the planet, 47% replied it matters a lot; 26% agreed with this if it produced better returns; and only 12% said it doesn’t matter at all. Similarly, 38% of members said that knowing Nest holds investee companies to account on things like executive pay, environmental damage and human rights would give them a greater sense of trust (compared to just 16% who said that seeing Nest rated highly by the media and organisations they trusted would do so).

As a result, responsible investing is being treated as a key component of efforts to increase member engagement. More information is now being provided to members regarding responsible investing, including stewardship activities as well as the exercise of voting rights. Different forms of communication are now being tested to see what resonates with members.

> “...38% of members said that knowing Nest holds investee companies to account on things like executive pay, environmental damage and human rights would give them a greater sense of trust...”

Source: Building new norms. Nest responsible investment report 2018. https://www.nestpensions.org.uk/schemeweb/nest/aboutnest/investment-approach/responsible-investment/responsible-investment-reports.html

Case study: the Nest phrasebook

Market: UK
Focus: the importance of the language used when we ***speak***

Communicating about pensions with end savers is notoriously difficult. This challenge was especially stark for Nest (the National Employment Savings Trust). Nest was set up in 2010 by the UK government as part of the introduction of a national auto-enrolmentprogramme, to ensure that every employer has access to a workplace pension plan. Since the great majority of its members join through auto-enrolment, the typical Nest saver has no previous experience of pensionsaving. So, even compared to the limited familiarity with pensions of the typical plan member, Nest's savers are at a disadvantage.

Rather than simply trying harder, Nest approached the communication challenge methodically. Their research started with a literature review, workshops and broad consultation. An external research agency was used to lead these efforts. Specific terms and concepts were tested through focus groups and surveys. This externally-focused approach was taken because, as one employer put it, "communicating with the public should not be with jargon, not written by those who have a lifetime working inthe industry". Certain concepts – asset classes or diversification, for example – were felt to be so familiar to investment professionals that they are not even perceived as jargon.

The results of this work are captured in eight principles that Nest term their **"golden rules of communication"**.

These principles are:

1. Keep it real
2. Rights not responsibility
3. Out with the old *(ie talk in terms of peoples' lives today, not the distant future)*
4. One for all
5. Tell it like it is
6. Take people as you find them
7. Give people control *(even if they don't use it)*
8. Be constructive.

These rules are designed to make it easy for savers not only to understand, but also to engage with, their pensions.

To ensure that the rules are applied in practice, Nest maintains a phrasebook. This lists specific alternatives to the most common examples of industry jargon. Instead of saying “fiduciary duty” for example, Nest communications use the term “legal duty to act in member’s interests”; “asset classes” and “diversification” become “different types of investment” and “the spread of your money acrossa range of different investments” respectively. In other cases, the phrasebook requires that certain terms be defined the first time they are used. Rather than always avoiding the term “annuity”, for example, communications will include a definition: a guaranteed income for the rest of your life, that you can choose to purchase with your pension pot.

Although unique in some regards, the core of the challenge faced by Nest is shared by every organisation that must communicate directly with end savers. Nest have been exceptionally thorough in tackling the challenge,and the lessons in their work are widely applicable. The communication principles and phrasebook are publicly available; as they note “they’re not just for us. They’re relevant to anyone communicating with the new generation of savers who’ll join a workplace pension scheme through auto enrolment.”

Sources: The Nest phrasebook. https://www.nestpensions.org.uk/schemeweb/NestWeb/includes/public/guides/NEST-phrasebook,PDF.pdf
Nest’s golden rules of communication. https://www.nestpensions.org.uk/schemeweb/dam/nestlibrary/golden-rules-of-communication.pdf

Case study: retirement income projections

Market: Australia
Focus: a great example of ***what*** to communicate

In a defined contribution arrangement, an account balance is converted into income only after retirement. Hence it can be more difficult in DC to measure progress against a retirement income goal than it is in a defined benefit arrangement.

The initial focus of DC schemes and members on accumulating wealth typically leads to a focus on balances. This makes it difficult to reframe the discussion in terms of retirement income and may lead to a false sense of security, increasing the danger of inadequate income. Because lifetime income provision is expensive, an apparently healthy account balance may in reality support a disappointingly small retirement income.

For this reason, lifetime income reporting is the subject of interest in a number of markets, including Australia. A number of organisations have developed retirement income calculators to allow members to measure their progress in retirement income terms. However, these calculators can be complex to follow, are typically not well customised to individual circumstance and/or don't guide the user to take the necessary steps to address any income gaps.

First State Super, an industry fund based in Australia with around 800,000 members, has attempted to address this gap with their *explorer* tool. The calculator personalises projected incomes against user-defined retirement goals, as well as the ASFA retirement standard (which establishes benchmark annual income levels for modest and comfortable lifestyles[14]). The use of descriptive benchmarks such as a comfortable lifestyle reflects the way members tend to think of their retirement and was found to result in stronger engagement than a simple dollar amount.

The tool uses information already held by First State Super including current account balance, investment profile and savings level combined with user-input data of their broader wealth. An internal algorithm provides a customised retirement income projection and measures whether members are on track to achieve their desired retirement lifestyle. As they navigate through the tool the individual can see how different actions, like saving more or retiring later, can address any income gap they may be expected to face.

Because the projections are based on personalised data, the tool generates (as required by Australian law) a formal statement of advice. This statement will include recommendations based on user-nominated actions. In this way *explorer* aims to reduce what can be a daunting exercise into simple actionable steps, which are stored so the user can be prompted to take these actions at a future date.

The tool is too new for its effectiveness to be measured yet, but a pre-launch pilot test produced significantly improved engagement. This 2,000-member pilot program used a simplified approach based on the regulatory projection basis[15]. 60% opened the emails, and 86% of those clicked through to the results; there was an increase in the number of members making additional contributions, both in terms of in roll-ins to the fund and in the number of members seeking personal advice. The success of the live program will be judged by usage and by changes in behaviour associated with use of the tool.

The sophistication of tools such as this will almost certainly increase over time. Ease-of-use will continue to be critical, however, and many members will continue to need access to personalised support in order to act upon the advice generated.

See: https://firststatesuper.com.au/member/super/how-much/super-projection

[14] As of June, 2019, these were A$40,054 and A$61,522 for a couple both aged 65.

[15] This is a very simple projection basis, with standard return assumptions that do not vary by asset class.

Principles of best practice member engagement

This paper has explored defined contribution member engagement from several angles. We have provided case studies of some leading-edge developments, and touched on the implications for member engagement of technology and of the emergence of choice architecture as a key DC design consideration. In the appendix we also consider the state of play in key markets.

From these elements, certain best practice principles emerge.

1 members are individuals and, where possible, should be treated as such

Different workforces have different characteristics; what works effectively for one plan may not work for another. Similarly, within a plan, not all individuals the same. The next few years may see significantly increased scope for customisation. Multi-channel engagement is likely to increase. The future of DC is likely to be hyper-customised.

2 all communications should aim to help the individual

Even communications required by legislation or regulation should be made as helpful as possible. Technology is important here too as it is (a) changing the way we generally speak to each other and (b) creating different channels for talking to people about their pension savings, allowing us to overcome barriers such as a widely scattered membership. We also touched on the importance of the language we use when we speak.

3 respect the medium, as well as the message

The effectiveness of member interaction depends on language and design elements as well as on the subject matter. The financial services industry is especially prone to jargon. Technology offers enormous potential power to personalise engagements.

4 engagement bandwidth is limited – use it wisely

A mindset of managing the member journey suggests a natural tailoring of communications and engagement opportunities to different life stages. Respecting a limited bandwidth while seeking to stay in touch represents a more difficult balancing act. It is important to be in regular contact to maintain trust. Targeted engagement provides better insight. Not all communication needs to seek direct engagement. A great deal of member communication is required for statutory reasons, or because it may be helpful to a small number of participants. Cognitive decline at advanced ages means that late-life strategies need to require less direct participant input at older ages.

5 the organisational design implications are within your control

The rapid development of technology suggests that DC organisations will need to be agile in their adaptation. Technology brings challenges – such as overtrading and the potential for cybercrime. Remaining at the leading technological edge is expensive.

Defaults and nudges, while very useful, are not enough to ensure effective engagement. They are less effective in areas such as determining retirement strategy. Being helpful to members will take organisations very close to the line which delineates where advice starts. We suggest that governing boards should recognise and grapple with this issue before any problems start to manifest. Further, we would encourage fiduciaries to be appropriately brave in their serving members' best interests.

Appendices

US | the world's largest DC market

The US has more DC assets than any other nation on earth – approximately US$15 trillion in total.[16]

The Thrift Savings Plan (a supplemental DC plan open to federal government employees) is the world's largest DC plan, totalling over US$500 billion. A further US$7 trillion lies in 401(k) or other employment-related DC plans sponsored mainly by single private-sector employers, and around US$9 trillion is in Individual Retirement Accounts[17] (IRAs), the great majority of which was rolled over from employment-based DC plans (and which is hence counted here as DC assets).

Despite the size of the system, coverage and adequacy are significant concerns: between one-third and one-half of the private-sector workforce does not have access to a workplace-based retirement savings program. The DC system has transitioned from being largely a supplement to DB to becoming the primary retirement savings vehicle for most private sector workers. Levels of saving for many years did not reflect this role: in 2008 more than 70% of plans used a default savings rate of 3% or less – positively, by 2018 that figure had fallen to 40%. Recent years have seen steady increases in plan contributions, which now average around 12% of salary (7% from employees and 5% from employers).[18]

Selective comments on regulatory background

The primary form of DC plan in the US is the corporate 401(k) plan, whose name is a reference to the section of the Internal Revenue Code which confers tax benefits on them, and which first appeared in the early 1980s.[19] By 1990, more private sector workers had access to DC plans than DB, and DC assets had surpassed DB by the turn of the millennium.

In recent years, DC fiduciaries have been the targets of numerous class action participant lawsuits. The primary areas for litigation to date have been alleged excessive fees, inappropriate investment options (including company stock) and self-dealing. The selection of investment options, in particular, is prone to litigatory cherry-picking driven by the benefits of hindsight: underperforming strategies are easy to identify after the fact.

This litigious environment has left fiduciaries loathe to take any action that they perceive as potentially leaving them open to lawsuits, even if the action – on the balance of probabilities – is believed to be in participants' best interests. Such concerns led, for example, to the widespread use of low-risk-low-return capital-guaranteed products as default investment options prior to the creation of a safe harbour by the Pension Protection Act of 2006 (PPA). These concerns are a significant explanatory factor in the use of passive investment being more widespread among DC plans than DB.

Fiduciary concerns have created a strong disincentive to innovation in member engagement; the potential downside for fiduciaries from taking steps that are not established practice, providing value but at a higher fee point and/or not supported by a regulatory safe harbour, is often seen as outweighing any potential benefits.

Fiduciary concerns, allied with regulation, make the provision of advice a difficult area. Fewer than 40% of plans offer investment advice to participants.

A significant potential future development in the US market is the open multiple employer plan (open MEP), an idea whose support has been building in recent years. Open MEPs would reduce the barrier to offering a DC plan, expanding coverage. The platform-like nature of these plans (and the competitive dynamic) would mean a different model of member engagement than has been the norm in single-employer plans.

[16] See Global Pension Assets Study 2019. Thinking Ahead Institute.

[17] Source: Pensions&Investments, "U.S. retirement assets at $28 trillion in Q1, little changed from end of 2017", June 21, 2018.

[18] Source: Plan Sponsor Council of America.

[19] A clear and concise history of the regulatory and other developments can be found in "In 401(k) We Trust" by Jim Miller of Dimensional Fund Advisors.

Trends in member engagement

The use of auto-enrolment increased sharply following passage of the PPA, and over half of DC plans now auto enrol new hires. Target date funds have been the most popular default investment option, although managed accounts are slowly increasing in popularity, especially at older ages.

One downside of reliance on default pathways has been an anchoring to relatively low contribution rates. Choice architecture alone can only go so far in determining an appropriate savings level, level of risk tolerance for a given individual, or in setting an appropriate strategy for the retirement period; variations in objectives and circumstances make it much more difficult to establish a one-size-fits-all design in retirement.

There is increased use of electronic means to interact with participants, although this is not yet universal. Around 75% of plans handle balance inquiries and investment changes, for example, through the internet and 30% via mobile technology (as compared to around 40% via vendor benefit centres and 20% via sponsor staff)[20]. Electronic interaction creates the potential to enhance and customise member engagement by using the data gathered.

Education and information efforts are mainly focused on encouraging participation in and appreciation of the plan. Most sponsors prioritise plan design and building strong default options over educating participants to make better decisions (an approach that is seen as having failed). The use of nudges has become focused on the aim of motivating positive action in support of financial wellness, in recognition that past education has not tended to elicit more informed decision making.

With regard to sustainability, what little member engagement there has been to date has been member-driven and reactive (eg offering ESG options in a fund menu) rather than proactively being integrated into the default options. This seems unlikely to change as long as the Department of Labor (DOL) maintains that "Fiduciaries must not too readily treat ESG factors as economically relevant", effectively signalling a presumption that sustainability considerations are primarily driven by values rather than financial considerations.

Participant engagement around the point of retirement is especially significant, since a large majority of participants have historically rolled over assets into IRAs at retirement. Concerns about predatory practices have been a major factor in the DOL's efforts to widen the applicability of the fiduciary standard. Preferences differ among employers regarding the retention of assets in the plan (bringing economies of scale) or transferring assets out (reducing the administrative burden), however, increasingly the trend is towards the desire to retain participants and scale. As a result, greater attention to retirement income is leading to efforts to change the focus of reporting away from account balances and towards income reporting.

The member engagement emphasis in the US appears to have broadened from purely a pension focus to a desire to motivate action to improve financial wellness.

[20] Source: Plan Sponsor Council of America.

Australia | a consolidating DC market

Measured as a proportion of GDP, Australia has the largest DC market in the world (over 130%)[21]. As of 2018, assets averaged roughly A$100,000 (US$76,000) for each member of the population.

Very few plans in Australia are sponsored by a single corporate employer. Instead, the market is dominated by three groups: retail funds, industry funds, and self-managed superannuation funds. Retail funds are profit-for-owner, operated by banks or insurance companies. Industry funds are profit-for-member with participation, in some cases, open to those employed within a certain industry or geography, or, in other cases, open to all Australians. Self-managed superannuation funds typically serve one or two high-net-worth individuals (four members being the maximum).

Recent Royal and Productivity commissions into the wider financial services industry also impacted superannuation. One likely consequence is further consolidation within the industry, with many commentators projecting that the number of large funds will fall by half in the next 5-10 years. As the system has matured, retirement arrangements have emerged as a visible area of weakness within the system, receiving increasing attention from regulators.

Selective comments on regulatory background

Australia's position as a global DC leader can be traced back to the introduction, in 1992, of a "Superannuation Guarantee". Subsequent legislation has increased the required contribution to 9.5% with further increases planned. One effect of setting a minimum contribution (rather than a minimum benefit) was to trigger a rapid transformation from defined benefit to defined contribution, rather than the slow-but-steady shift that has been seen in a number of other countries. Another observable effect is that the minimum contribution level has become the *de facto* standard, with few employers offering contributions in excess of the minimum.

Australia has stringent privacy laws, protecting individuals from unsolicited email for example. This has slowed down, although not stopped, the trend toward electronic communication. It has also made it more difficult to address the question of orphan accounts: the onus is on the individual to take steps to consolidate. However, recent regulatory initiatives aimed to protect and consolidate low balances have significantly improved the number of duplicate accounts.

Since contributions are material, as the system matures, retirement arrangements have begun to receive more attention in Australia than elsewhere, with a knock-on effect on member engagement. Retirement income projections may be included in member statements, although the calculation of these projections is currently very basic and fund take up has been slow. There has also been a proposal to create *comprehensive income products for retirement* (CIPRs) – a retirement product which, unlike the widely used account-based pensions, would be required to incorporate longevity protection. A sticking point in this process is finding a balance between customisation (fitting the retirement income solution to the individual circumstances) and standardisation. This challenge is closely related to the question of member engagement.

Rules concerning the provision of advice also affect how organisations approach member engagement. Only licensed advisors are permitted to provide financial advice. This shapes how organisations view customisation; while many funds have ambitions to provide a comprehensive advice service for members, particularly those approaching retirement, there is also interest in ideas relating to 'mass customisation' and building advice and guidance into products in recognition of the difficulty in engaging with large numbers of their members.

[21] See *Global Pension Assets Study 2019*, Thinking Ahead Institute.

The fiduciary role in Australia, as elsewhere, requires fiduciaries to act in the best interests of plan participants. Unfortunately, an elevated focus on peer group comparisons has served to discourage innovation and the exploration of new ideas. It has also led to a significant focus on fees over and above value to members, and can distort reporting – creating an incentive to game the way in which products are categorised for risk purposes, for example.

Trends in member engagement

The use of electronic delivery and online member engagement is increasing (despite strict privacy laws), making information more accessible to members. For example, a 2013 Willis Towers Watson survey found a 45% average overall take-up rate of digital technology across eight categories (including websites, email, apps, and so on). The focus was only just beginning to broaden away from the website at that point. By 2017, that take-up rate had risen to 79%. The increase in the use of social media has been especially notable. This has required considerable investment: a significant number of organisations reported annual digital technology spends of greater than AUS$1.5 million.

There is greater competition for members in Australia than in markets where corporate-sponsored plans are more common. The attraction and retention of members is a driving force behind much of the innovation in member engagement, especially online engagement. Other motivations include supporting members to save for an adequate retirement, improving efficiency and timeliness and supporting consolidation of multiple accounts.

Another current area of focus is segmentation, which enables communications and investment decisions to be more targeted to an individual's circumstances. As organisations become more adept in handling the data that is increasingly available to them, the scope to tailor communication to reflect member preferences, improve member engagement and customise solutions to suit personal circumstances seems considerable.

Public interest in sustainability issues, especially climate change, is high and drives considerable member engagement. This interest has had a growing impact on investment decisions and product structures. Increasingly, funds are leveraging these efforts to help engender trust and improve engagement.

Finally, as evidenced by the Royal Commission, public trust in financial institutions has been weakened. Organisations that are able to strengthen relationships through enhanced member engagement will be well-placed to grow. Reputation is at a premium.

"...a 2013 Willis Towers Watson survey found a 45% average overall take-up rate of digital technology across eight categories..."

"By 2017, that take-up rate had risen to 79%. The increase in the use of social media has been especially notable."

UK | transitioning from a DB to DC market

The UK has a long history of pension provision, and today represents about 7% of global pension assets, making it the 3rd largest pension market in the world. Although defined benefit historically dominated, and over 80% of pension assets are still DB assets, new hires to 99% of FTSE 350 companies today are offered only a DC plan. So the UK is on the same path already taken by Australia and the US to becoming a DC market.

DC provision comes in two forms: trust-based occupational plans (or “schemes”) and contract-based personal pensions.

Traditionally, UK pensions were delivered in the form of an annuity, with a maximum of 25% of the value being taken as a lump sum at retirement. Tax rule changes in 2015 – generally referred to as pension freedoms – introduced greater flexibility in the way benefits can be taken. This increased the level of engagement in pensions, but also led to a significant increase in members taking their benefit as a lump sum rather than as retirement income.

Selective comments on regulatory background:

Oversight of pension provision is split between the Pensions Regulator (tPR), responsible for trust-based arrangements, and the Financial Conduct Authority (FCA), responsible for personal pensions. While the rules are similar for the two types of arrangement, they are not the same.

The most significant regulatory development of recent years was the broad automatic enrolment initiative that was phased in between 2012 and 2017. This brought some 10m new members into workplace-based pensions arrangements. Minimum contributions were low initially but increased to 8% of qualifying earnings in 2019.

This brought a stronger regulatory spotlight onto workplace DC schemes and served as a catalyst for a substantial increase in regulatory activity.

Auto-enrolled employees receive basic information such as their right to opt out (although employers cannot encourage them to do so), contribution rates (and how to vary these), investment options and charges. Those who do not qualify for auto-enrolment must be told about the workplace pension and their right to join it.

More information is included in a Chair Statement, which must be prepared annually and (from 2019) is available on a public website. This outlines the governance of the scheme strategy, findings of the value for member assessment, charges (including transaction costs) and default arrangement Statement of Investment Principles. The scope was widened in 2019, to include further information such as an illustration of the impact of costs on pension outcomes. An additional Implementation Statement will be required from October 2020, outlining how the stated investment policy has been followed and acted upon. One effect of this expansion of scope has been to leave many fiduciaries viewing the statement as a purely legal requirement, rather than as an effective way to communicate with members.

Annual member statements provided by trust-based schemes include a projection of benefits expressed in today's money (ie net of inflation) and information on how to access further information, including the Chair Statement.

While tPR guidance encourages trustees to seek member views, there is no legal requirement to do so. They suggest a wide range of approaches, including engagement via member-nominated trustees or union representatives, the use of staff forums, monitoring social media or web forums, tracking the use of digital services, conducting online member surveys and listening to member helpline calls.

Helping members to prepare for the choices they will have to make, especially at retirement, is an area of emphasis for regulators. Providing information at the right time in the right format is seen as a key element of good member engagement. Tailoring of communication to reflect member preferences format is encouraged, as is the use of tone and language that reflects the membership demographic. The changing and expanding role that technology can play in supporting good decision-making is also recognised.

Trends in member engagement

The full effects resulting from wider auto-enrolment have not yet fully played out. One development that is likelyto prove particularly significant in time is the emergenceof master trusts (ie multi-employer trusts). Master trusts pre-date auto-enrolment, but are closely associated with it, thanks to the shake-up of the market that resulted, and the creation of the National Employment Savings Trust (Nest) to act as a scheme that would guarantee to be available to all employers, regardless of size or commercial value. Over half of those auto-enrolled as a result of the new legislation have joined master trust arrangements. An authorisation process for master trusts was initiated in 2018 and, at the time of writing, 35 master trusts have been authorised under this process[22].

Engagement around investment choices is limited, with an emphasis on default glide paths (or "lifestyles"), which generally adjust risk as members approach retirement. There is some variation, however, in the assumptions regarding how members will take their benefits in retirement. Partly as a result of this, it has become common to offer members a choice with 9 out 10 trust-based and 8 out 10 contract-based arrangements offering more than one lifestyle choice[23].

When legislation was recently introduced requiring ESG factors to be considered in the design of investment strategy, initial proposals called for member views to be taken into account. This was contested as impractical,and was not included in the final rule. Nevertheless, some schemes have sought to engage members on this topic (see, for example, the Nest responsible investmentcase study).

The FCA has raised concerns about members following a path of least resistance. For example, 94% of members who do not take advice accept the default drawdown solution offered by their provider while only 35% who received advice do so. Proposed remedies include the sign-posting of guidance services and provision of wake-up packs to members on turning 50 and then every 5 years until they take their benefits.

"Helping members to prepare for the choices they will have to make, especially at retirement, is an area of emphasis for regulators. Providing information at the right time in the right format is seen as a key element of good member engagement. "

[22] See https://www.thepensionsregulator.gov.uk/en/master-trust-pension-schemes/list-of-authorised-master-trusts

[23] Source: Willis Towers Watson FTSE 350 DC Pension Scheme Survey 2018.

Member engagement in selected other markets

Spain

Spain has a relatively new private pension system (1987). Occupational pensions are voluntary, and mainly DC (90%). Assets in 2018 were €107bn, across 2,523 private pension plans of which 1,293 were occupational. There is a maximum permissible contribution to an individual's pension plans of €8,000 per year. Enrolment is voluntary.

In relation to member engagement, the fiduciary manager of the pension plan reports the current balance. Lifetime income is not reported, although some of the pension management firms have calculators on their websites. Information must be made available to members at least quarterly, and sent semi-annually.

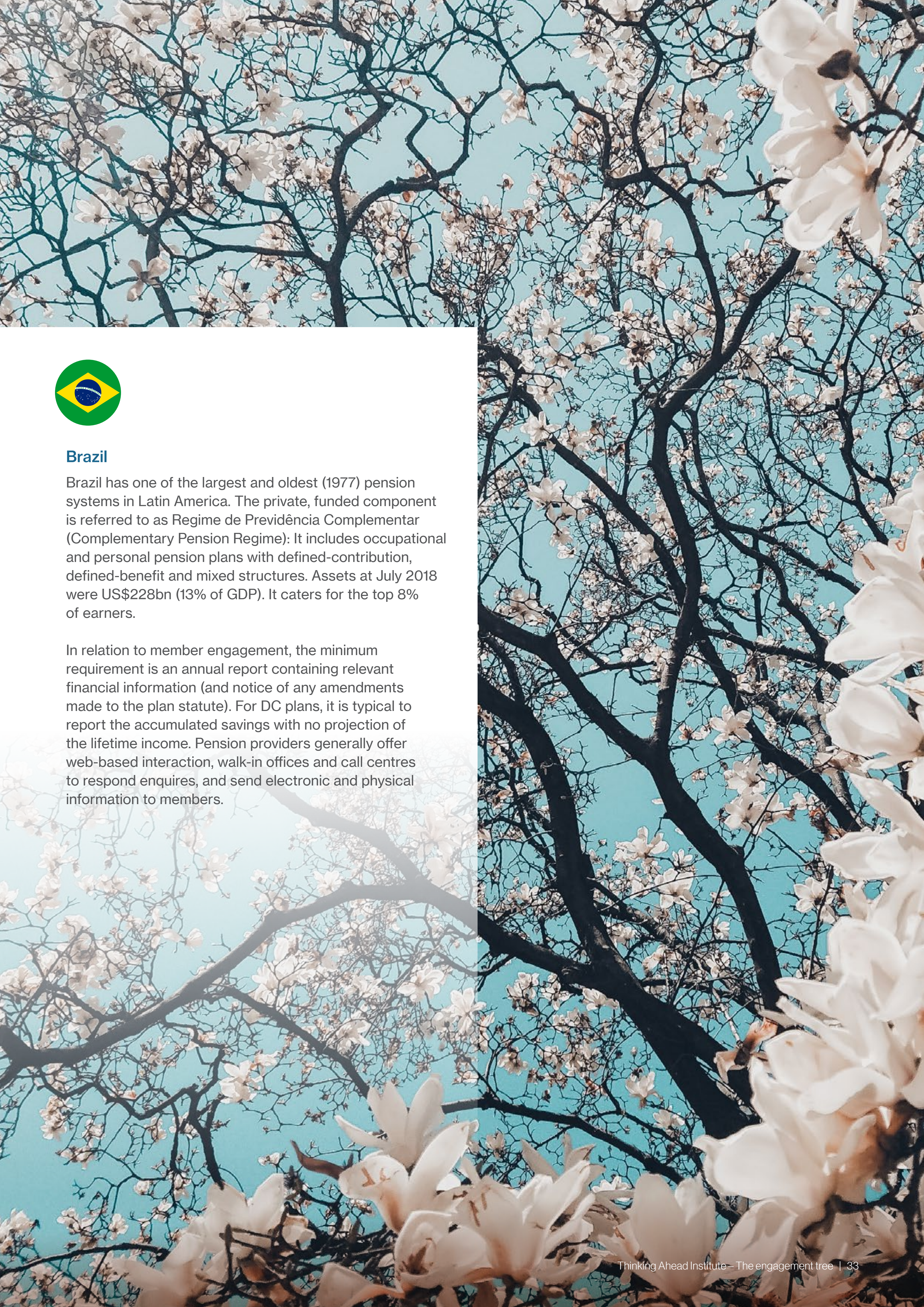
Spain has a generous pillar 1 pension system, and so the demand for private longevity hedging is not high. Nevertheless, on retirement, annuities are one of the options available to members. They can also opt for a non-guaranteed stream of payments which depend on the ongoing performance of the assets, or they can specify their own ad hoc payment schedule.

Chile

Chile has one of the biggest DC markets in Latin America (US$190bn, 65% of GDP). The DC pension system was created in 1980 and is compulsory for employees (10% contribution rate); voluntary for the self-employed. There are 6 pension fund administrators (AFP), each offering 5 risk-graded funds

In relation to member engagement, the law created the role of pension advisor. The advisors are paid by the AFP and licensed by the regulator of the system. As such they appear to advise only on the choice of 5 risk levels, with the member having the right to choose the AFP. The required content of regular statements is dictated by the regulator. These account balance statements ("Cartola") are sent electronically or by mail at least once every four months, and are also available on the internet or at the AFP's physical offices.

At retirement, members choose between a lifetime annuity (account balance transferred to insurance company) or drawdown (account remains with AFP). The member must use the SCOMP system (Sistema de Consultas de Montos de Pensión), developed by the AFPs and insurance companies to offer a clear and transparent way to compare pension options. Under SCOMP, the AFPs and the insurance companies enter into a bidding process to offer different pension options to the member. The member can hire an independent (and licensed) pension counsellor to help, or can use the service of a sales agent from an AFP or an insurance company. From inception to 2016 490,000 individuals used SCOMP with 65% opting for an annuity and 35% for drawdown.



Brazil

Brazil has one of the largest and oldest (1977) pension systems in Latin America. The private, funded component is referred to as Regime de Previdência Complementar (Complementary Pension Regime): It includes occupational and personal pension plans with defined-contribution, defined-benefit and mixed structures. Assets at July 2018 were US$228bn (13% of GDP). It caters for the top 8% of earners.

In relation to member engagement, the minimum requirement is an annual report containing relevant financial information (and notice of any amendments made to the plan statute). For DC plans, it is typical to report the accumulated savings with no projection of the lifetime income. Pension providers generally offer web-based interaction, walk-in offices and call centres to respond enquires, and send electronic and physical information to members.

Limitations of reliance

Limitations of reliance – Thinking Ahead Group 2.0

This document has been written by members of the Thinking Ahead Group 2.0. Their role is to identify and develop new investment thinking and opportunities not naturally covered under mainstream research. They seek to encourage new ways of seeing the investment environment in ways that add value to our clients.

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The Thinking Ahead Institute

About the Thinking Ahead Institute

The Thinking Ahead Institute seeks collaboration and change in the investment industry for the benefit of savers. It was established in January 2015 by Tim Hodgson and Roger Urwin, who have dedicated large parts of their careers to advocating and implementing positive investment industry change. It is a global not-for-profit research and innovation group made up of engaged institutional asset owners, asset managers and service providers committed to changing and improving the investment industry. Currently it has over 40 members around the world and is an outgrowth of Willis Towers Watson Investments' Thinking Ahead Group, which was established in 2002.

The Institute aims to:

- Build on the value and power of thought leadership to create positive change in the investment industry
- Find and connect people from all corners of the investment world and harnesses their ideas
- Work to bring those ideas to life for the benefit of the end saver.

It does this by identifying tomorrow's problems and investment solutions through:

- A dynamic and collaborative research agenda that encourages strong member participation through dedicated working groups
- A global programme of events including seminars and key topic meetings, webinars and social events
- One-to-one meetings between Institute member organisations and senior representatives of the Thinking Ahead Group.

These solutions fall into three overlapping areas:

- Better investment strategies
- Better organisational effectiveness
- Enhanced societal legitimacy.

The Institute has a governance board comprising both Institute members and Thinking Ahead Group representatives. For all membership enquiries please contact:

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