

## Danish pensions are top of the class in transparency

*An external evaluation of openness and transparency initiatives in the Danish pension industry documents that the level of openness and transparency for the Danish consumers on the pension market is high.*

As a part of a political agreement the Danish Insurance Association (DIA) and the Danish Ministry of Business and Growth agreed to have an evaluation of the DIA openness and transparency initiatives on pensions carried out.

The purpose of the evaluation was to assess whether the DIA transparency initiatives satisfy the consumers' need for information. In particular, to assess if the information and transparency resulting from the initiatives do in fact ensure Danish consumers both openness, overview and comparability on pensions across the market.

Besides the transparency initiatives it was also agreed to review the DIA Cost Recommendation and the underlying methodology. In particular, the aim was to evaluate the extent to which the Recommendation ensures full transparency on all costs paid by the consumers in relation to their pensions.

To perform the evaluation the DIA and the Ministry agreed to commission Towers Watson. The full version of the evaluation can be found on the DIA website, [www.forsikringogpension.dk/temaer/evaluation-of-the-DIA-transparency-initiatives/Sider/forside.aspx](http://www.forsikringogpension.dk/temaer/evaluation-of-the-DIA-transparency-initiatives/Sider/forside.aspx).

More information about the DIA initiatives evaluated can also be found in the evaluation report.

As a part of the evaluation Towers Watson developed a theoretical framework over the consumers' needs for information based on expert literature and behavioural economics theory. The framework considers the information required to enable consumers to make informed decisions in relation to their pensions. The framework was used to assess whether the DIA initiatives meet the needs of the consumer. Towers Watson's Consumer Needs Framework comprises insights and knowledge about consumer needs, design of information and of information requirements. It is our learning and experiences from this work that we aim to share with this article.

However, to start off we will briefly sum-up the evaluation and the key findings of Towers Watson.

### **The approach of Towers Watson**

The DIA presented and described its key transparency initiatives to Towers Watson. On this basis, Towers Watson evaluated the DIA initiatives by doing the following:

- Evaluating the DIA initiatives against a theoretical framework on the consumers' need for information.
- Evaluating the knowledge of the Danish consumers about their pensions
- Evaluating how the consumers assess the information they receive about pension

Towers Watson also compared the range of DIA initiatives on transparency with the range of similar initiatives from industry associations in Germany, Netherlands, Sweden and UK. Here the different nature of each country and its pension system should be kept in mind. This comparison was made with the primary aim to investigate the role of the DIA as an industry association in promoting transparency on the Danish market. The comparison did not compare nor evaluate the quality or coverage of the initiatives in the different markets.

To be able to evaluate the initiatives effectiveness and use to the consumers Towers Watson developed a theoretical framework of the consumers' needs for information in order for consumers to be able to make well-informed decisions about pensions.

### **Towers Watson's key conclusions**

Towers Watson concluded that the DIA has been very active in the field of openness and transparency with a comprehensive set of initiatives. The evaluation showed that the overall coverage of the DIA initiatives is comprehensive and meets the consumers' needs. Towers Watson was able to map all of the existing initiatives to steps in the Consumer Needs Framework. This indicates that all the initiatives are playing a positive supporting role in addressing consumer needs.

### **Cost Recommendation**

Following years of challenging work and technical discussions the DIA published a recommendation on costs, including Annual Cost in Krone (ACK) and Annual Cost in Percentage (ACP), in 2010. The aim was to inform consumers about all costs of a pension scheme in one single figure. The DIA has published a recommendation on the reporting and auditing of pension scheme-related costs. The Cost Recommendation sets out the methodology for the calculation of all costs' related to a pension-scheme. It also sets out the standards for the information the companies must provide. The Cost Recommendation covers calculation approaches for both customer-specific cost and cost calculators for all pension schemes provided by DIA members. Finally the Cost Recommendation has specific requirements for auditing and reporting.

Towers Watson's concluded that the approach underlying the DIA Cost Recommendation was comprehensive and addresses the significant cost elements that they would expect given the available data on the financial markets.

### **Recommendations**

Towers Watson also recommends ways in which the transparency initiatives of the Danish pension industry can be improved. The three main recommendations are:

- Improve usability of the initiatives
- Increase the use of prompting
- Increase the general level of financial literacy of consumers

Naturally the DIA is happy to note the positive evaluation on the DIA transparency work and the initiatives. However, even more important the evaluation has provided the DIA with valuable knowledge and insights into consumers' needs and how consumer information and the tools can be designed and presented to optimise the effects and benefits to the consumers.

Going forward DIA will use this knowledge to improve our initiatives and generally in our continued work to ensure consumer transparency and the required information.

### **The consumers' needs**

*What is required to ensure that consumers' can make informed decisions?*

The Consumer Needs Framework is one of the main outputs of the evaluation. Towers Watson has developed a theoretical model by considering a wide range of relevant academic literature regarding consumer decision-making and behavioural economics theories. In the course of this work Towers Watson also met with leading experts within these fields to ensure the validity and soundness of the framework. The framework gives a comprehensive understanding of the consumers' different needs for information through their decision making processes regarding financial decisions.

The framework looks both at the situation where the consumer is making an actual purchase and at the situations where the consumer is in the process of evaluating and optimising existing products and/or solutions.

The Consumer Needs Framework demonstrates the ideal behaviour which we know is at best rare if not unlikely in "the real world". Nonetheless it can provide useful inspiration to both industry and legislators when designing consumer information and rules on information requirements.

### **An overview of The Consumer Needs Framework**

There are some fundamental requirements that need to be in place in order for a framework like this to work optimally. The consumers must have trust and confidence in the pension system, they need to be motivated and they must have a basic level of numeracy and financial literacy.

The Towers Watson Consumer Needs Framework is composed of five steps and four dimensions which are combined in an iterative process.

The five steps are:

1. Awareness of need
  - The consumer must be brought to a point where they recognises that there is a need of some sort. For example to reconsider the level of insurances after giving birth
2. Identify functional requirements
  - This would for example be that the consumer recognises that they need additional income in retirement.
3. Chose an appropriate type of product/solution
  - The consumer must decide what available products are suitable to meet the needs and functional requirements. For example is a pension scheme or private savings the appropriate choice?
4. Evaluate the specific product/solution
  - The consumers must decide the characteristics of the desired product. For example should it be a unit link product or a traditional with-profit product?
5. Post-commitment process/evaluation
  - The consumer should asses on an on-going basis the given product/solution to ensure the product/solution still meets their needs. If they do not fulfil the expectation or if the needs change the consumer will start the process in step 1 once again

The four dimensions of the consumer journey are:

1. The decision making process
  - This dimension maps out the five steps that the consumer will have to go through in the decision making process ad described above
2. Desired consumer behaviour
  - This dimension describes the desired consumer behaviour from an objective point of view in an ideal world
3. Information to enable the desired consumer behaviour
  - Hands on recommendations to the type of information that is relevant through the steps and to the content of the information
4. Requirements presenting information

- This dimension considers how information must be framed and presented to enable the consumer to make informed decisions

When all this is combined you get an overview of what kind of information the consumer needs and when the consumer needs the information and how the information should be framed in order for the information to have the desired effect. It is important to note that this is a theoretical approach to the consumers' behaviour. The model must be seen as a mapping of the consumers' needs and to what extent the needs are covered given the information available.

Behavioural economics specifically recognises that individuals do not always make decisions on the basis of rational logic and a structured process. According to the framework however, where consumers are given the right information that is presented and framed in the right manner, the consumers can potentially be encouraged to make a decision and/or take actions that are more likely to be aligned with their best interests. On this basis, the framework attempts to show what the "optimal consumer journey" should look like as the basis for structuring and appraising what information the consumer need – and how that information should be presented - in order to optimise the likely effect and usefulness of the information to the consumer.

A thorough explanation of the framework is presented in the evaluation report.

### **Towers Watsons' checklist for design of information requirements**

Based on the Consumer Needs Framework Towers Watson extracts a checklist that highlights the critical topics that must be considered when designing consumer information and regulating information requirements.

According to this checklist it is key to consider if and how the information encourage the consumers' to take appropriate action.

The checklist provides a line of questions that should be considered when designing information to ensure that the needs of the consumers' are met and to ensure the information is effective. These questions are listed below:

#### **Purpose**

- Does the information have behavioural purpose?
- Does the information have personal relevance?
- Does the information have context?

#### **Content**

- Is the information up to date, factually accurate, and sufficiently complete to enable the consumer to complete the decision step?
- Is the message of the information clear to the user?

## Presentation

- Is the information presented in an aesthetically pleasing manner?
- Is the information structured - both in terms of complexity but also importance?
- Is the information correctly framed to engender action?

The points above should be taken into account in the design or enhancement of initiatives and in design of legislation on consumers' information.

## Contact

If you should have any questions concerning the evaluation, the Consumer Needs Framework or the DIA's transparency work in general please contact Senior Consultant Dianne Louise Schow [dls@forsikringogpension.dk](mailto:dls@forsikringogpension.dk) or Consultant Rasmus Højland [reh@forsikringogpension.dk](mailto:reh@forsikringogpension.dk).

*Rasmus Højland*