PENSIONS AND LIFETIME SAVINGS ASSOCIATION

HITTING THE TARGET

DELIVERING BETTER RETIREMENT OUTCOMES

CONSULTATION RESPONSES

CONTENTS

INTRODUCTION

IN OCTOBER 2017, THE PLSA PUBLISHED A CONSULTATION: *HITTING THE TARGET: DELIVERING BETTER RETIREMENT OUTCOMES*. THIS CONSULTATION PRESENTED OUR ASSESSMENT OF PUBLIC POLICY ON RETIREMENT INCOME PROVISION AND A SERIES OF PROPOSALS AIMED AT REFORMING PUBLIC POLICY AND INDUSTRY PRACTICES TO FACILITATE BETTER RETIREMENT OUTCOMES.

More than 100 stakeholders from over 50 different organisations took part in our consultation. We received 16 written consultation responses from organisations operating across the retirement savings industry. In addition to the written responses, the PLSA also sought feedback from relevant stakeholders through a series (eight) of expert roundtable events. The roundtable events covered (in chronological order) the following subjects: retirement income targets; equity release; working longer; pension tax relief; governance and value for money; engagement; and automatic enrolment.

This document outlines the principal findings from the written responses and the stakeholder events. It is structured in the following order:

1. **Thematic Overview:** The first section of this document sets out a summary of the overall findings of both the written responses and the roundtable events. This information is divided by theme and covers all of the areas addressed in the *Hitting The Target* consultation.
2. **Expert Roundtable Summaries:** The second section of this document contains detailed summaries of each of the expert roundtable events held by the PLSA. These are also divided by theme.

The PLSA would like to thank all of the organisations and individuals that contributed to the consultation process, through either a written response or attendance at one of the roundtable events. The feedback that we received during the consultation process shaped the changes to public policy and industry practice that we recommend in *Hitting The Target: A Vision For Retirement Income Adequacy*, which was published on the 5th July 2018.

SECTION 1
THEMATIC OVERVIEW

RETIREMENT INCOME TARGETS

THE IDEA OF DEVELOPING A SET OF NEW RETIREMENT INCOME TARGETS RECEIVED WIDESPREAD SUPPORT FROM STAKEHOLDERS WHO TOOK PART IN THE CONSULTATION PROCESS. GOAL SETTING HAS BEEN SHOWN TO INCREASE CONTRIBUTION RATES AMONGST SAVERS AND A SERIES OF SIMPLE TARGETS, ROLLED OUT AT THE NATIONAL LEVEL HAVE THE POTENTIAL TO TRANSFORM THE RETIREMENT SAVINGS LANDSCAPE.

The vast majority of respondents supported a tiered approach to the definition of retirement income targets. However, the number of targets was a subject of debate. One stakeholder felt that no more than one high level target should be developed, which savers could tailor using tools (fintech) and guidance/advice, whilst another expressed concern that three targets would not be enough, given the degree of variation in the population.

Some stakeholders felt that the inclusion of a ‘minimum’ target might lead to a levelling process that would result in relatively poor retirement outcomes. There was widespread concern that the branding and communication of targets might lead to negative inferences, particularly for the ‘minimum’ and ‘modest’ levels. As a result, care needs to be taken when choosing the target titles.

The development of baskets of goods was widely accepted as an appropriate means of determining the different targets. However, some alternative approaches were suggested for arriving at the various levels. In particular, although most respondents accepted the Joseph Rowntree Foundation Minimum Income Standard as a good basis for the ‘minimum’ standard, two proposed the use of the State Pension plus a top up.[1] There was no clear consensus as to whether the baskets of goods should be developed for singles/couples, include property costs, or vary by UK region.

A variety of organisations were suggested as potential owners of the targets, including the Government (specifically the Department for Work and Pensions), industry bodies (such as the PLSA and ABI), independent national bodies (like the ONS), and independent charities. Many respondents expressed concerns that if this proposal was undertaken by the Government or an industry-related body, there would be a very real possibility of conflicts of interest arising.

1 Based on either the savings accrued from automatic enrolment contributions at the level of the National Living Wage or an increment of 10-15% on the JRF MIS.

AUTOMATIC ENROLMENT

ALL CONSULTATION RESPONDENTS AND ROUNDTABLE PARTICIPANTS AGREED THAT AUTOMATIC ENROLMENT CONTRIBUTIONS, EVEN AT THE FULL RATE POST-PHASING, ARE UNLIKELY TO BE SUFFICIENT TO PROVIDE SAVERS WITH AN ADEQUATE INCOME IN RETIREMENT.

An increase in minimum contributions from 8% to 12% was universally supported in principle, though most respondents noted that a full analysis of the consequences of the current phasing period would be required before any final decisions are taken. However, a number of consultation respondents stated that contributions at the rate of 12% are unlikely to be sufficient to enable savers to achieve an adequate retirement income. A savings rate of 15% was widely considered to be more likely to achieve that end.

A rebalancing of employer/employee contributions was widely supported by both those who responded to the consultation and those who attended the roundtable on this issue. The UK is an outlier in the context of the international community; in other countries employers tend to pay a much higher proportion into employees' pensions than is the case in Britain.

Moreover, higher employer contributions will become increasingly important as phasing progresses, especially if the Government decides to increase minimum contributions beyond 8%. Evidence suggests that matching or higher employer contributions will minimise opt-out rates and encourage positive saving behaviour. In order to help employers adjust to a higher rate of contributions, a clear and long-term timetable should be set out by the Government.

Other means to help people save a sufficient amount for long-term needs should be explored. For example, evidence suggests that 'save more tomorrow' strategies can be effective in encouraging people to contribute more to their pension savings. Mechanisms to help savers balance short- and long-term needs, such as the NEST 'sidecar',[2] were treated with caution; though some respondents believed that this could be a helpful mechanism to reduce the risk of over-saving.

Although a number of respondents thought that initiatives such as this should be examined further, many concerns were raised about using pension savings in this way. First among these was the impact that early access arrangements could have on the sufficiency of retirement savings through increased administration costs and lower overall savings levels. The increased complexity that would be introduced into retirement savings, particularly automatic enrolment, was a secondary concern; this could confuse savers and lead to lower savings levels. There was also a sense that pensions were not the right vehicle to use in order to solve savers' short-term financial difficulties.

There was universal support for including 18-21 year olds and multiple job holders within the scope of automatic enrolment. However, no clear consensus appeared regarding the inclusion of the self-employed within the scope of this policy. Some respondents did not believe that the inertia principle would work effectively amongst self-employed groups, who tend to be more aware of their finances. Amongst those who supported using automatic enrolment to bring the self-employed into regular pension saving, various approaches were suggested to achieve this objective, including:

- Increasing National Insurance Contributions and allocating the additional sums to a scheme of the saver's choice via a carousel of options;
- Using the tax system to collect contributions, which would be allocated by default to a fund provided by NEST;
- Encouraging self-employed people to save via an alternative incentive, such as a higher rate of tax relief; and
- Making contributions more default-like once saving has begun. This could be done through common digital transactions, such as invoices, from which deductions could be taken.

2 In a sidecar, some of the funds saved through automatic enrolment would be allocated to a liquid account that could be used to meet short-term costs.

PENSION TAX RELIEF

ROUNDTABLE PARTICIPANTS STATED THAT NO CHANGES SHOULD BE MADE TO PENSION TAX RELIEF UNLESS THEY ARE LIKELY TO HAVE A BENEFICIAL EFFECT. ANY FUTURE MODIFICATION SHOULD BE FUNDAMENTAL, AS OPPOSED TO TECHNICAL, IN ORDER TO ENSURE THAT IT ENDURES FOR THE LONG-TERM.

At present, the vast majority of tax relief is dedicated to Defined Benefit (DB) saving (deficit recovery contributions in particular) and only a small amount is expended on Defined Contribution (DC) saving. Tax relief dedicated to DC saving is expected to double by 2030. However, official figures on the cost of tax relief are very misleading and should be reviewed to ensure their reliability.

The difficulties (political and technical) involved in altering the existing regime for DB suggests that it could be appropriate to adopt different tax relief solutions for DB and DC savers. The existing tax regime could be maintained for the former and the latter could be subject to Taxed, Exempt, Exempt (TEE) treatment. However, tax relief should not be considered in isolation to other aspects of the problem, such as the value of the State Pension or the existence of the Net Pay and Relief at Source regimes.

Some consultation respondents rejected the idea of modifying current tax relief arrangements on the basis that the adoption of new retirement income targets should not be hindered by a debate over tax relief and changing the tax system would introduce more complexity into the pension system. The Exempt, Exempt, Taxed (EET) system received support from a number of respondents. However, many believed that more should be done to inform people about the benefits of the existing tax relief regime. A number suggested that the Lifetime Allowance should be abolished and the Annual Allowance reduced in order to encourage people to work longer.

Reform of the tax system was supported by other stakeholders who responded to the consultation, one of whom proposed a 'root and branch' review of the over-complex regime (including the inconsistencies between DB and DC). Other supporters of reform were more specific in their recommendations. Moving to a flat rate Income Tax relief regime was proposed by one respondent on the basis that it would redistribute Income Tax relief from higher earners to low and middle earners. According to another supporter, any consideration of tax reform should include a review of:

- The benefits of flat rating or even 'bottom loading' tax relief, to the benefit of lower earning savers;
- The potential for linking tax relief to level of savings rather than income – for instance, introducing a generous (say 50 per cent) tax relief payment against the first £20,000 of savings;
- How tax relief can be better framed as an incentive to save in member communications; and
- The framing of the 25% tax free lump sum and ways of counteracting the social norm of withdrawing the full amount early in retirement.

PROPERTY

CONSULTATION RESPONDENTS STATED THAT EQUITY RELEASE OFFERS A USEFUL ADDITIONAL SOURCE OF RETIREMENT INCOME FOR THOSE WHO DO NOT HAVE SUFFICIENT PENSION SAVINGS OR SUFFER FROM EXTRAORDINARY COSTS, PARTICULARLY THOSE ASSOCIATED WITH LONG-TERM CARE. STAKEHOLDERS IDENTIFIED A NUMBER OF WAYS IN WHICH EQUITY RELEASE PRODUCTS COULD BE MADE MORE APPEALING TO POTENTIAL CUSTOMERS AND EASIER TO USE AS PART OF AN INCOME STREAM.

Products could become more appealing to retirees if minimum loan amount requirements and processing costs were to be reduced, so that the products can be used more like bank accounts. Mechanisms like this already exist in the mortgage market. This would make lump sums drawn from lifetime mortgages less 'lumpy' and easier to use as part of a retirement income. There are also specific regulatory challenges that could prevent equity release from reaching its full potential. In particular, the EU's Solvency II regulations were deemed to be "excessively strict" and may limit the UK insurance sector's ability to offer equity release products.

Roundtable participants stated that the equity release market is growing by 25% a year. The typical customer is 79 years old, has a house worth £200,000 and borrows around £30,000 against it. There was a total of £2 billion in lending in 2016, which represented a new market high. Despite this degree of growth, there are specific cultural, political, product and advice barriers that hinder wider use of equity release mortgage products.

The PLSA's proposals for more flexible products would address many of the reasons that consumers cite for not using equity release mortgages to support their retirement income. Employers could usefully 'auto-enrol' employees into guidance and advice, such as a Mid-Life Financial Health Check. This would help more people to consider their retirement options as a whole. However, there is a capacity challenge in the equity release market. More advisers are needed and better links between advisers would improve the customer journey.

Stakeholders stated that the likelihood of pension funds investing in property assets will increase as assets under management grow over time. Attractive income returns can be generated through 'Build to Rent' investments. The challenge in this sector is that there is very little stock to acquire, which means if schemes wish to access a stable cash flow over the long-term they need to take short-term development risk to create the stock.

Stakeholders argued that the Government should focus on making the regulatory environment more conducive to investment from institutional investors, such as pension funds. Pension schemes would also welcome a more consistent approach to housing policy from the Government, which could improve their willingness to invest in such assets.

Stakeholders also stated that pension schemes find it hard to invest in housing association debt, because there is very little available in the market. Investment in social housing has been a typical strategy amongst pension schemes that have wanted to invest in housing assets. However, there are some real challenges that constrain the ability of schemes to invest further, including:

1. **Rent-Setting Formula:** To achieve savings and bring rents down within the social housing sector, the Government has committed to reducing rents in social housing in England by 1% a year for four years from 2016. This has made investment in social housing more difficult for institutional investors. Stakeholders stated that if the Government maintains this policy over the course of the next rent-setting period, social housing investment will remain difficult for pension schemes.

2. **Benefits System:** Changes made to Universal Credit mean that all payments, including money for rental costs, go directly to claimants themselves. This is a change from the former system, where money for rental costs was paid directly to the social housing provider. This introduces two risks: default risk (in which claimants may choose not to pay rent and spend Universal Credit payments on other goods/services) and reputational risk (in which institutional investors could be criticised if they were to evict social tenants from properties that they own).

3. **Planning Issues:** The convoluted planning system constrains the amount of property that institutional investors are able to invest in, because it prevents the development of viable sites.

WORKING LONGER

ROUNDTABLE PARTICIPANTS ARGUED THAT RETIREMENT SHOULD BE A POINT AT WHICH PEOPLE HAVE ACHIEVED THEIR FINANCIAL OBJECTIVES, RATHER THAN THE POINT AT WHICH THEY ARE FORCED OUT OF THE WORKFORCE. THEY STATED THAT IT IS NECESSARY TO DEVELOP A BETTER UNDERSTANDING OF THE DIFFERENT FACTORS THAT LEAD PEOPLE TO STOP WORKING AND THAT THE COMBINATION OF DEFERRING THE STATE PENSION AND PENSION FREEDOMS COULD CREATE INCENTIVES TO CONTINUE WORKING.

The roundtable identified the need for better co-ordination across government to help people to continue working. This could include a stronger skills agenda and a drive to ensure that local authorities do not push people towards swapping work for caring responsibilities in order to protect town hall social care budgets. The relationship with the employer, particularly the line manager, is crucial to helping people to stay in the workforce. A line manager who takes a flexible approach (e.g. time off for caring responsibilities) can make a big difference. Employers also have some responsibility for ensuring people have a grasp of the potential long-term consequences of their decisions on retirement income.

Consultation respondents noted that public policy needs to address two challenges: firstly, it needs to enable those older workers who want to work to do so, and, secondly, it should ensure that those who cannot work are provided for. Longer working lives should not be seen as an easy remedy to the problem of poor pension provision. The answer to this is better pension provision. Relevant management training should be offered by employers. This should cover issues such as general health, stress and mental health. Additional training may also be required on how to have confidential sensitive conversations with employees.

A number of practical suggestions were made that could help older workers to remain in the workforce. The most common proposal was the introduction of a mid-life 'MOT' that would enable savers to understand where they are on the retirement savings journey and what they need to do in order to remain employable should they need or want to continue working in later life. Similarly, retirement seminars for the over-50s in the workplace could help savers to understand their options.

GOVERNANCE AND VALUE FOR MONEY

ROUNDTABLE PARTICIPANTS STATED THAT A ONE-SIZE FITS ALL APPROACH TO THE REGULATION OF SCHEME GOVERNANCE DOES NOT EXIST AND SHOULD NOT BE ATTEMPTED. GIVEN THE VARYING QUALITY OF GOVERNANCE ACROSS THE SECTOR, THE PENSIONS REGULATOR (TPR) WAS RIGHT TO ADOPT ITS CURRENT MODEL. NEVERTHELESS, SCHEMES HAVE DIFFERENT NEEDS, DEPENDING ON THE QUALITY OF TRUSTEES THEY POSSESS, AND TPR'S APPROACH NEEDS TO BE FLEXIBLE ENOUGH TO ACCOUNT FOR THESE DIFFERENCES.

There was widespread agreement amongst stakeholders who took part in the roundtables on the need to improve the overall quality of trustees. There is scope for some regulatory convergence, particularly in relation to fit-and-proper tests for trustees with control positions. However, respondents cited a number of reasons why any move towards professionalisation should be treated with caution. Firstly, there is unlikely to be the talent pool sufficient to satisfy the number of schemes operating in today's market; secondly, it would risk reducing diversity of thought amongst trustees; and, finally, professionalisation could reduce the number and/or impact of Member-Nominated Trustees.

Consultation respondents stated that Independent Governance Committees (IGCs) chairs believe that supervisory continuity across the retirement journey is desirable. Providers are concerned that extending their remit will dilute IGCs' focus on the accumulation phase, with negative outcomes for savers. Regardless of whether IGCs are given additional responsibilities, it is clear that convergence in the realm of governance between different types of scheme and product is desirable.

Consultation respondents suggested that ICGs could be given similar legal obligations to trustees in safeguarding the best interests of their members. Many respondents stated that IGC powers should be enhanced; a particular area where additional powers could be granted is the ability to make transfers of savers' funds from low quality defaults to better equivalents without members' consent.

The idea of developing new metrics was welcomed by stakeholders, who are frustrated with the equation of low cost with value for money. New metrics could be particularly helpful to trustees, but they should not be developed for their own sake, nor should they be used as a proxy for expert judgment or to replace it. Several proposals have already been made in this field that could be adopted and developed by the PLSA. Any effort to bring forward new metrics must be industry-wide if it is to have any impact.

DECUMULATION

THERE WAS WIDESPREAD, THOUGH NOT UNIVERSAL, SUPPORT AMONGST CONSULTATION RESPONDENTS FOR THE IDEA OF TRUSTEES PROVIDING STRONG SIGNPOSTING FOR SAVERS AT THE POINT OF RETIREMENT. IT WAS SUGGESTED THAT THE PROCESS PROPOSED IN THE CONSULTATION ASSUMED THAT SAVERS WOULD ENTER A DRAWDOWN PRODUCT BY DEFAULT AND THAT THIS PATHWAY WOULD NOT NECESSARILY BE THE BEST OR THE SAFEST CHOICE FOR SCHEME MEMBERS.

Safe harbour provision for trustee boards that provide signposting services for scheme members received a mixed reception. Some respondents stated that it is essential if the decumulation pathway proposed by the PLSA is to work. Others felt that safe harbour would be unnecessary, so long as signposting were to be provided as part of a broad mixture of guidance (including mid-life MOTs, wake-up packs, etc.). One respondent considered that the provision of safe harbour would reinforce drawdown as the default retirement product.

Roundtable participants believed that the adoption of a series of common principles underpinning the new decumulation process could be hard to achieve, given the Government's reluctance to legislate in this area. However, this could be achieved through changes to FCA regulations. International examples of where this approach has been pursued could help to generate a consensus amongst policy makers.

All roundtable participants agreed on the need for better guidance and advice procedures to support decumulation choices. Guidance in particular can play a fuller role in helping savers to make the right choices prior to and throughout retirement. The Single Financial Guidance Body (SFGB) will have an important role to play in ensuring that appropriate guidance is available to savers.

This could be achieved by automatically enrolling savers into free guidance sessions prior to accessing funds, which could improve understanding of financial issues and pension products, and reduce losses to pension scams. One respondent suggested that a standardised 'decision tree' could be used. The 'decision tree' would help savers to assess their preferences in regard to drawdown, annuitisation and the other options available to them.

Other means of improving decumulation outcomes for savers, such as the creation of a deferred annuity market or Collective Defined Contribution (CDC) schemes, face serious barriers. In the case of the former, stakeholders stated that the capital holding provisions of the EU's Solvency II Directive make it difficult to create such a market; in the latter case, participants argued that many different forms of CDC exist and the benefits of pooling can be achieved in conventional DC schemes.

ENGAGEMENT

ROUNDTABLE PARTICIPANTS STATED THAT THE PENSION INDUSTRY'S ENGAGEMENT WITH SAVERS IS HAMPERED BY THE PERSISTENCE OF LEGACY COMMUNICATION SYSTEMS, WHICH ARE DIFFICULT AND COSTLY TO CHANGE. HOWEVER, THE INDUSTRY IS CHANGING AS A RESULT OF COMMERCIAL PRESSURE AND SOME BEST PRACTICE HAS EMERGED WITH REGARD TO ENGAGEMENT. FOR SAVER INTERACTION TO IMPROVE FURTHER, THE INDUSTRY NEEDS TO DEFINE THE GOALS OF ENGAGEMENT, AS WELL AS IMPROVE THE PROCESSES AND PRODUCTS IT EMPLOYS.

No single action will improve saver engagement with pensions. A fundamental culture change amongst savers, providers and regulators is required to increase appropriate engagement. The value of saving and investment needs to be inculcated in savers, and the risk culture amongst providers and regulators needs to change in order to facilitate innovation in engagement tools and techniques.

Fintech is likely to drive reform of the pension industry. The continuing evolution of fintech, particularly the Pensions Dashboard, is crucial to improving engagement with pension savings. Used effectively, fintech could drive better engagement by making personalised communications possible en masse and enabling savers to tailor their savings targets to suit their needs. Regulators can encourage innovation in this area by embracing the FCA's 'regulatory sandbox' approach, which encourages providers to experiment with new tools and techniques. Providers themselves need to embrace the spirit of fintech and understand how it could encourage better pension engagement.

Consultation respondents identified a number of operational barriers that could limit the use of new tools. In particular, the pension industry may lack the necessary capacity to transfer member data seamlessly between platforms. Poor internet connections in secure locations might also reduce the degree to which savers are willing to use fintech tools. Regulatory risks were also identified as a potential barrier to the development of innovative fintech tools. Commercial interests might also limit the use of fintech, as providers/asset managers might not be willing to implement non-proprietary solutions.

Respondents argued that the pension industry has not used 'teachable moments' and heuristics effectively in the past. Support for the use of teachable moments to reinforce positive saving behaviour was clear, though stakeholders noted that existing evidence does not demonstrate that strategies that use 'teachable moments' are effective. More work is needed to identify 'teachable moments' and assess their effectiveness. This applies to the proposed mid-life MOT.

There was widespread support for a broad standardisation of communications. However, there was no consensus regarding the degree to which particular documents should be standardised. Suggestions included the inclusion of a minimum level of data in all industry communications, the development of a standard glossary of terms by the Single Financial Guidance Body, the use of common terminology across the pension industry, and the full standardisation of annual statements and other documents (e.g. pre- and post-sales materials).

SECTION 2
EXPERT ROUNDTABLE SUMMARIES

RETIREMENT INCOME TARGETS

20TH NOV 2017

EXECUTIVE SUMMARY

- **Support:** There was universal support for the creation of Retirement Income Targets. Participants felt that the 'baskets of goods' approach that the PLSA proposed was appropriate. However, they felt that it would be crucial to get the labels of each target level right in order to ensure that they promote aspirational saving behaviour. Stakeholders concluded that income-based targets are preferable to pot-based targets, due to the possibility of large pot-sized targets discouraging people from saving for retirement.
- **Simplicity:** There is a tension between tailoring the targets to reflect individual circumstances and keeping them simple. The general consensus favoured simplicity. This means individual, as opposed to dual occupancy, household targets and no regional variations. There was a range of views on whether to produce separate versions of the targets to reflect renting and home ownership.
- **Use:** For targets to be successful, employers, industry, the Government and the Single Financial Guidance Body will need to give them strong support. It will also need to be clear what people should do with the targets information.

DISCUSSION OF PROPOSALS

OVERALL VIEW OF RETIREMENT INCOME TARGETS (RITS)

Stakeholders supported the RITs concept and there was strong support for the 'basket of goods' approach proposed by the PSLA. A minority of participants suggested that a three-level system might lead to people aiming for the middle level by default and argued that two or four levels might be better. The proposed 'comfortable', 'modest' and 'basic' labels for the targets were felt to lack 'snappiness'. An alternative that might resonate more with savers could be 'gold', 'silver' and bronze', as these titles might create a greater sense of 'aspiration'.

Participants stated that the development of RITs created a small number of manageable risks. For example, the PLSA needs to be careful that it does not set a 'social norm' that seems unattainable. The PLSA should also beware of inadvertently prompting opt-outs, due to increased engagement resulting from the RITs.

DEVELOPING THE TARGETS

Stakeholders stated that savers would require clear guidance on how to use the suggested RITs. There will be a need for heuristics and supporting tools (e.g. to check progress at 40/50/60 years of age). The targets will also need to be indexed to prices.

Participants discussed whether the targets should be based on pot size, rather than income level. All favoured income level targets, because pot size-based targets risk appearing completely unattainable. However, the PLSA needs to bear in mind that the Dashboard will cover pot size and it will need to link seamlessly to income-based targets.

Stakeholders considered whether the targets should be personalised. Some assumed that they would be and stated that some providers (notably Aviva and Zurich) have systems that work along these lines. One option would be to get people to the 'minimum' level that is appropriate for them and then look at how they could get to the next level. The PLSA will need to consider the potential impact of 'shocking' people into knowing how much they need to save. There might be a case for 'interim'/5-year landmarks or milestones that can give savers targets that appear achievable.

A further consideration participants discussed concerned the single/dual household targets. There was a consensus that the targets should be as simple as possible and should, therefore, only be based on single households. This could be accompanied by a clear message that both partners in a couple should be using the targets.

Some participants felt there was a need to produce separate versions of the targets to reflect renting and ownership. The retirement targets used in Australia assume home ownership. Others felt that Millennials or lower earners might disengage if they realise that the targets assume home ownership. Stakeholders did not reach a consensus on this issue.

DEVELOPING THE BASKETS OF GOODS

Stakeholders supported the PLSA's proposed 'basket of goods' approach to target development, but felt that a highly complex basket (e.g. including care costs) would not necessarily deliver any extra engagement. They favoured the use of specific numbers (rather than ranges) for the targets, but suggested they be seen as a guideline with some tolerance around them.

One participant suggested using a 'my gold', 'my silver', 'my bronze' system with average and double average earnings. There is a risk that having only the three levels will make the whole system irrelevant to, perhaps, the upper third of earners, who have the most discretionary decisions to make.

There was a general view that the targets should be as simple as possible. People know that costs vary for regions to region and will take account of that. The PLSA team undertook to check whether other regions are much more expensive and deal with that point if necessary – but otherwise try to keep the system simple.

ACHIEVING HIGH TAKE-UP

Stakeholders felt that employers and pension schemes would have a major role to play in achieving high uptake of the targets amongst savers. The industry and the Government particularly the Single Financial Guidance Body would also have to play a significant role. Key to making RITs genuinely useful will be to incorporate a 'so what?' into the design of the targets, so that savers are clear what they should do with the information.

EQUITY RELEASE

24TH NOV 2017

EXECUTIVE SUMMARY

- **Use:** The equity release market is growing by 25% a year. The typical customer is 79 years old, has a house worth £200,000 and borrows around £30,000 against it. There was a total of £2 billion in lending in 2016, which represented a new market high.
- **Barriers:** There are specific cultural, political, product and advice barriers that hinder wider use of equity release mortgage products. The PLSA's proposals for more flexible products would address many of the reasons that consumers cite for not using equity release mortgages to support their retirement income.
- **Guidance and advice:** Employers could usefully 'auto-enrol' employees into guidance and advice, such as a Mid-Life Financial Health Check. This would help more people to consider their retirement options as a whole. However, there is a capacity challenge in the equity release market. More advisers are needed and better links between advisers would improve the customer journey.

DISCUSSION OF PROPOSALS

EQUITY RELEASE – STATE OF PLAY

Stakeholders stated that the equity release market has changed significantly over the course of the past two decades. Twenty years of robust regulation has gone a long way towards addressing many of the negative perceptions of the equity release industry.

The equity release market is growing by 25% a year. The typical customer is 79 years old, has a house worth £200,000 and borrows around £30,000 against it. There was a total of £2 billion in lending in 2016, which represented a new market high. The industry loan book stands at around £20 billion. The theoretical limit is circa £180 billion, so there is huge potential for growth. Nationwide's recent entry into the market will help equity release be seen as a mainstream product.

The maturation of large numbers of interest-only mortgages, (approximately £24 billion over the next 5 years for over-65s), pension freedoms and increasing care costs will all help to generate increasing demand for equity release products. The principal uses of equity release funds at present are: mortgage repayment (1 in 3), debt clearing (1 in 4), home improvement, and other uses including supplementing income and gifts to family members. Housing equity is also already being used to fund care costs.

KEY CHALLENGES FOR THE EQUITY RELEASE INDUSTRY

Despite the growing use of equity release mortgages as a means of funding later life needs, a number of barriers remain that prevent more people from accessing their property wealth. These barriers include:

a. **Culture:** People are generally pro-home ownership and most, especially older generations, are debt-averse. The industry is still held back by negative perceptions (including some journalists' views). People are often pleasantly surprised when they have full information about equity release. The total compensation paid by the industry due to Financial Ombudsman rulings over the past 12 years is just £6,500. This shows that bad practice is no longer an issue.

b. **Political:** Politicians' awareness and understanding of equity release is poor and there are regulatory challenges, such as the Solvency II Directive, that constrain the equity release market.

c. **Products:** Products have become more innovative, but more consumer research is needed to ensure that they meet customers' needs. In particular, providers need to do more to take account of changing circumstances over the course of retirement.

d. **Advice:** People say they don't want to go from pillar to post; they want a single adviser to help them make the right decision. The industry needs to improve the links between, as well as the supply of, advisers. The relative lack of advice providers has tended to drive up the cost of advice.

HOW EMPLOYERS COULD IMPROVE EMPLOYEES' AWARENESS AND UNDERSTANDING OF EQUITY RELEASE PRODUCTS

There was a discussion about why employers would get involved in this area. The motivation would be similar to that for providing good workplace pensions – to help manage the workforce. Larger employers with trust-based schemes are the most likely to explore how they can better help their employees manage their finances. Siemens is a good example of this sort of attitude from an employer.

Stakeholders stated that employers could usefully 'auto-enrol' employees into guidance and advice, such as a Mid-Life Financial Health Check. This would help more people to access PensionWise and consider their retirement options as a whole. Pension providers could also do this.

WORKING LONGER

28TH NOV 2017

EXECUTIVE SUMMARY

- **Evidence Base:** A better understanding of the different factors that can lead people to stop working prematurely is required in order to tackle this issue effectively. Retirement should be a point at which people have achieved their financial objectives, not the point at which they are forced out of the workforce.
- **Better Government Co-ordination:** There is scope for better co-ordination across government, as well as between government and the private sector, to help people to continue working. This could include a stronger skills agenda for people over the age of 24, as well as the collection and dissemination of best practice on longer working lives to employers.
- **Decision Support:** Employers have some responsibility for ensuring people have a grasp of the potential long-term consequences of their decisions, such as scheme members being rendered ineligible for welfare benefits some years after 'depriving themselves of capital' by taking cash from a pension pot.
- **Best Practice Principles:** The meeting identified a number of principles to help people work longer. These covered the role of the employer, enabling people to make informed decisions that suit their circumstances, and helping people to feel secure when they can no longer work.

DISCUSSION OF PROPOSALS

HOW WORKING LONGER CAN HELP TO ENSURE PEOPLE HAVE ADEQUATE SAVINGS IN THEIR 50S, 60S AND 70S

Stakeholders agreed that retirement should be the point at which people achieve their financial objectives and are able to retire if that is what they desire. Where people have to use their pension savings to 'bridge' the period to State Pension entitlement (because they are not working), this undermines the whole point of pension saving.

In order to help people work for longer, where they need or want to, we need to develop a comprehensive understanding of the factors that stop them from working. Participants stated that different solutions are required for different groups (e.g. manual workers with ill health).

Incentives and planning tools can play a role in helping people to remain in the workforce, though it is not clear that these mechanisms work for all. For example, the option to defer taking the State Pension (on the basis that a saver will receive a higher sum when retirement occurs) is not widely understood.

POTENTIAL GOVERNMENT ACTIONS TO HELP PEOPLE WORK FOR LONGER

Stakeholders identified a number of areas in which the Government can take the lead in helping people to work for longer. Its role includes setting the legislative framework (e.g. on default retirement age) and sharing evidence on best practice, working with employers and supporting Local Enterprise Partnerships (LEPs). There is also scope for better co-ordination across government. For example, the Department for Education could give a higher priority to particular issues, such as a skills agenda for people aged over 24.

Some existing initiatives to help people work longer would benefit from a higher profile. For example, there is little awareness that people can claim for 'reasonable adjustments' to help them to continue working. A recent proposal suggested that this funding should follow people from job to job. There is also a mental health support scheme to help people keep working.

Participants stated that employees' relationship with their employer – particularly their line manager – is crucial to retaining people in the workforce. A line manager who takes a flexible approach (e.g. time off for caring responsibilities) makes a big difference. Many small businesses try to 'do the right thing' in helping people to remain employed for longer and would be receptive to a public information campaign on these issues, as well as information on the support available.

Stakeholders argued that the UK's changing demographic profile will, in itself, promote the interests of older workers in the labour market. Most businesses have not looked at the age profile of their workforce and considered how it will evolve over the course of the next decade. Participates stated that there might be scope for the Government to encourage employers to do this.

PRINCIPLES FOR WORKING LONGER

Stakeholders were enthusiastic about the idea of developing a set of best practice principles for employers that could help them to attract and retain older workers. A number of principles were suggested, including:

a. **Informed Decision-Making:** A key principle is that people should be able to take informed decisions that suit their personal circumstances. They should avoid hasty decisions.

b. **Employer Support:** A good employer would inform people of the risks of taking particular actions. For example, an employer might tell staff that taking cash from their pension pot could render them ineligible for welfare benefits some years later, because they had deprived themselves of capital. It is important that people have a grasp of the potential long-term consequences.

c. **Security:** We should aim to make people feel secure when they can no longer work. Security and the removal of uncertainty should be key considerations.

d. **Personal Development:** From the employer's perspective, helping people to work for longer is partly about ensuring they have access to the skills they need.

FURTHER STEPS THAT PENSION PROVIDERS CAN TAKE TO HELP PEOPLE WORK FOR LONGER

Stakeholders stated that schemes could ensure members are aware of the full range of options, including, for example, working fewer hours, 'job-chunking' and upskilling. Members should not feel they only have a 'black and white' choice between continuing full-time work and full retirement.

Auto-enrolment provides a new opportunity to talk to a generation of savers in a new way. For example, one scheme has had good results from combining auto-escalation with communications that do not mention pensions but simply tell people how much they are now worth. This positively reinforces saving behaviour. This approach is underpinned by comprehensive research and segmentation.

PENSION TAX RELIEF

4TH DEC 2017

EXECUTIVE SUMMARY

- **National Retirement Income Targets:** These might improve savings levels on their own. Changes to tax relief might not be required in order to achieve this end. No changes should be made to pension tax relief unless they are likely to have a beneficial effect. Any future modification should be fundamental, as opposed to technical, in order to ensure that it endures for the long-term.
- **Data Quality:** At present, the vast majority of tax relief is dedicated to DB saving (deficit recovery contributions in particular) and only a small amount is expended on DC saving. Tax relief dedicated to DC saving is expected to double by 2030. However, official figures on the cost of tax relief are very misleading and should be reviewed to ensure their reliability.
- **DB vs. DC Solutions:** The difficulties (political and technical) involved in altering the existing regime for DB suggests that it could be appropriate to adopt different tax relief solutions for DB and DC savers. The existing tax regime could be maintained for the former and the latter could be subject to TEE treatment.
- **Alternative Approaches**: It is unwise to consider tax relief in isolation to other aspects of the problem, such as the value of the State Pension or the existence of the Net Pay and Relief at Source regimes. The system level objectives should be set out by the Government and the most appropriate tools used to achieve them. The fiscal system might not be the best lever to pull in this context and alternative solutions should be considered.

DISCUSSION OF PROPOSALS

Participants stated that changing the way in which people engage with their retirement savings through the introduction of a series of National Retirement Income Targets might be enough to encourage more saving. As a result, these need to be fully implemented and evaluated prior to any modification of existing tax relief arrangements.

Participants felt that the PLSA's proposals are unlikely to work if the existing system of marginal rate relief is maintained, particularly as one of the PLSA's principal arguments is that current arrangements are poorly understood. A system of 'bonus' payments in the context of the current system would likely result in further complexity. This would do little to aid saver comprehension.

Moreover, the suggested mechanism by which 'bonus' payments would be financed – a reduction in either the Annual Allowance or the Lifetime Allowance (or both) – would also increase complexity. By reducing one or both of these allowances further, an increasing number of people would find themselves constrained in their ability to save. This would further complicate the already complex system. Equally, any modification of the DB conversion factor in order to increase equity between savers in different schemes would also increase complexity and could increase the likelihood of future 'tinkering' (e.g. if annuity rates improve).

Participants highlighted the possibility that the proposed approach could introduce perverse incentives into the retirement saving system. Firstly, they were concerned that if savers with smaller pots get a higher bonus, the unintended consequence would be to encourage people to save less. Secondly, it was noted that the 'bonus' system could be used by savers to underwrite riskier investment strategies in the knowledge that shortfalls would, in effect, be subsidised by the taxpayer. Aside from the technical issues identified above, further concern related to the affordability of the proposal. Participants did not believe the 'bonus' system to be financially sustainable, unless bonuses were set at a very low level.

There was also widespread suspicion regarding the quality of the numbers present in HMRC's PEN 1-6 tables,[1] which show little change in the overall level of tax relief over the last 5 years. Given the changes to the Annual Allowance and Lifetime Allowance, participants did not think this was plausible. Participants stated that data of a higher quality is urgently required if the true impact of tax relief on the Exchequer is to be understood.

ALTERNATIVE APPROACHES

Participants believed that the only way of achieving the bonus system via the tax system would be to move away from the underlying commitment to marginal rate relief. In the absence of such a change, there is little that can be achieved through minor modifications that would result in the desired outcome.

A more radical solution would be to separate the tax treatment of DB pensions from DC pensions. The existing tax regime could be maintained for the former and the latter could be subject to TEE treatment, which some participants thought might be the most effective solution over the long-term. Given the current situation, there is no 'one size fits all' solution and this approach could offer a viable way forward that respects this reality whilst enabling change.

Some participants stated that the desired objective sitting behind the pension tax relief proposal in the consultation – to help people achieve a better retirement income – is a social, rather than a fiscal, policy issue. They agreed that it is desirable that those least able to save should receive the most help from the Government. However, the PLSA should consider if there is a more appropriate means of achieving the social objective desired than attempting to do so via the tax system.

One possible means of improving outcomes, it was suggested, would be to adopt proposals for a pre-annuitisation reward or 'top up'. This could spread the Treasury-funded incentive over the period of retirement more effectively than the current tax relief regime. However, the obvious barrier to this being a viable solution is that annuities are unpopular and, increasingly, used less than in the pre-2015 pension market.

A further alternative that would achieve the social objective (i.e. to deliver a better retirement incomes for all) set out in the PLSA's consultation would be to have a higher State Pension. Although this would apply to all, it would make the system easier to understand and, crucially, enable those with the lowest level of savings to achieve a better income in retirement.

The group suggested a number of other reforms, including:

- Finding a solution to the net pay/relief at source issue, which means that some savers earning between the trigger (£10,000) and the income tax threshold (£11,500) are unable to receive tax relief.
- The abolition of the Lifetime Allowance. Initially, it was introduced as a temporary measure, but has become a permanent feature of the pension landscape.
- The reduction or removal of the tax free lump sum. If the objective is to improve income in retirement, reducing or removing the tax free lump sum would nudge people into accessing their savings in the form of an income. However, this would be politically difficult due to the popularity of the lump sum.
- Finding a means of moderating deficit recovery contributions (DRCs) in DB schemes (e.g. spreading deficit repair over a longer time period). Most tax relief is spent on DB saving, in particular DRCs. Ameliorating the impact of DRCs would free up tax relief that could be used to improve outcomes for those at the lower end of the savings' spectrum.

1 The PEN 1-6 tables set out HM Revenue & Customs' *Personal Pensions Statistics*.

GOVERNANCE AND VALUE FOR MONEY

12TH DEC 2017

EXECUTIVE SUMMARY

- **Regulatory Approach:** A one-size fits all approach to the regulation of scheme governance does not exist and should not be attempted. Given the varying quality of governance across the sector, TPR was right to adopt its current model. However, schemes have different needs, depending on the quality of trustees they possess, and TPR's approach needs to be flexible enough to account for these differences. There is scope for some regulatory convergence, particularly in relation to fit-and-proper tests for trustees with control positions.
- **Trustee Quality:** Trustees should, of course, always endeavour to provide a high quality of service to scheme members. However, the drive to professionalise trustees is problematic for a number of reasons. Firstly, there is unlikely to be the talent pool sufficient to satisfy the number of schemes operating in today's market. Secondly, it risks reducing diversity of thought amongst trustees. Finally, professionalisation could reduce the number and/or impact of member trustees.
- **IGC Purview:** Although many IGC chairs believe that supervisory continuity across the retirement journey is desirable, providers are concerned that extending their remit could dilute their focus on the accumulation phase, with negative outcomes for savers. Regardless of whether IGCs are given additional responsibilities, it is clear that convergence in the realm of governance between different types of scheme and product is necessary.
- **New Metrics:** New metrics should not be developed for their own sake, nor should they be used as a proxy for expert judgment or to replace it. We need to have a defined outcome in mind if metrics are to be effective tools for trustees. Several proposals have already been made in this field that could be adopted and developed by the PLSA.

DISCUSSION OF PROPOSALS

DO YOU AGREE TPR SHOULD REBALANCE ITS PRIORITIES TO FOCUS MORE ON TRUSTEE EFFECTIVENESS? HOW DO YOU THINK THAT TPR CAN BE MORE EFFECTIVE IN PROMOTING THE APPOINTMENT OF HIGH-QUALITY TRUSTEES?

The DC scheme landscape is extremely complicated and all types of scheme have positive and negative features. It is important that trustee boards consider things from a member perspective. Members have little or no knowledge of the type of scheme that they are part of and would be shocked if they knew that there were different governance arrangements for different types of scheme.

The danger in moving away from the approach that has been adopted by TPR is that a number of trust-based schemes do not carry out the most basic functions of governance properly. For schemes of this sort, the regulator has done the right thing in intervening at the basic level. There is no one-size fits all solution. Focusing on the inputs, as opposed to the outputs, works really well for those schemes that are getting the basics right already, not necessarily for those who are not.

It is also clear that the trustee talent pool is not sufficient to provide high quality trustees to the more than 35,000 schemes operating in the market at present. As a result of the above, a much more segmented approach to regulation and supervision is required in order to ensure that all types of scheme are appropriately overseen by the Government. TPR and the Financial Conduct Authority (FCA) are in the process of drafting a joint report, which will set out how they intend to work together in the future.

Given the amount of money involved and the responsibility placed on trustees, it is almost unbelievable that no official approval process exists for the appointment of trustees. Trustees need to have right balance of knowledge and skills, and should conform to appropriate standards. Control positions in FCA regulated firms require approval from the regulator. Master trusts will soon have to abide by a similar approval process in order to appoint trustees. A similar regime should be rolled out for other types of scheme.

At the level of the scheme itself, soft skills on the trustee board are as essential as professional competences in essential areas. For example, in order to ensure proper time management, which will affect the scheme's ability to deliver good outcomes for members, an effective chair is required. Moreover, evidence also suggests that diversity of thought is crucial to good scheme management. This is most easily achieved by appointing trustees from different backgrounds, genders and races.

A real danger inherent in the PLSA's proposal to improve the quality of trustees is that this could unintentionally reduce diversity of thought. Given the constitution of the existing talent pool, any drive to professionalise trustees could result in fewer people being appointed from diverse backgrounds. It could also reduce the member trustee voice, which is essential to ensuring that trustees' decisions are aligned with the desires of scheme members.

One way of improving trustee performance would be to implement annual appraisals for trustees. An assessment of this sort would, as with any other employee, help trustees to understand their strengths and weaknesses, and, where necessary, any training requirements. Another means of improving trustee performance would be for the regulator or a third-party organisation (like the PLSA) to carry out OFSTED-style inspections of trustee boards on an annual basis and provide detailed feedback.

DO YOU BELIEVE THAT THE POWERS OF IGCS SHOULD BE ENHANCED IN ORDER TO DELIVER BETTER OUTCOMES FOR SAVERS?

There have been a number of providers looking to perform bulk transfers of members into different funds without their consent. The FCA is becoming more flexible in regard to these issues. Changing investment is the one power that IGCs should definitely have. Members probably expect them to have this power already. Pension providers like the idea that IGCs could select the default fund to an extent. IGCs are there to address a weakness in the buy-side and, as a result, modifying the default for members who are not in a suitable one would most likely be welcome.

However, extending IGC powers into the realm of decumulation might not be so welcome, because it could lead to them losing focus on their principal area of responsibility. The provider perspective is that IGCs are there to do a particular role and that they need to be supported to do it well. Nevertheless, many IGC chairs believe that continuity across the retirement journey could help to improve outcomes and, as a consequence, they favour an extension of powers into the area of decumulation. This is particularly pointed given that there is now, post-pension freedoms, no clear point at which retirement starts.

Regardless of whether IGCs are given new responsibilities in regard to the decumulation process, it is clear that convergence in the realm of governance between different types of scheme and product is necessary. This is already taking place to a certain extent (e.g. master trusts and Group Personal Pensions). From the perspective of scheme members, who value simplicity, complete convergence is preferable, as it would remove some of the confusion people feel around pensions. Moreover, evidence suggests that security is the most important concern for savers. Currently, it does not form part of TPR's code. If we are to bring the regulation together, this needs to be front and centre.

DO YOU AGREE THAT THE PENSIONS INDUSTRY SHOULD DEVELOP METRICS TO MEASURE VALUE FOR MONEY? IF SO, WHICH METRICS WOULD BE MOST USEFUL TO AID COMPARISON OF THE VALUE FOR MONEY OFFERED BY PENSION SCHEMES OR PROVIDERS?

New metrics should not be developed for their own sake. We need to have a defined outcome in mind if metrics are to be effective tools for trustees. For example, the Australian approach to transfer or wind up is a useful example of how metrics could be used in order to effect a change in scheme behaviour. Moreover, if new metrics are designed, they should not focus exclusively on charges, because this could have serious unintended consequences. For example, if every scheme is invested in passive equities at the lowest possible cost, then there is a systemic risk to the whole pension system if these stocks crash.

Metrics should not be used as a proxy for expert judgment or to replace it. Expert judgment is required to enable the findings of the metrics to be placed in their proper context. Sackers and Standard Life have been working together on a benchmarking project to help IGCs to compare what their scheme provides versus others in the market. This is a helpful example of how metrics and expert judgment can be combined to the benefit of savers.

DECUMULATION

14TH DEC 2017

EXECUTIVE SUMMARY

- **Soft Defaults:** A new decumulation process, relying on a 'soft' default, is desirable. However, stronger consideration needs to be given to how the signposting process will be structured – particularly how 'hard' it will be. Participants also agreed that a range of default options could be designed, depending on the characteristics of individual schemes. Trustees' and employers' nervousness about providing a 'soft' default pathway can be alleviated through the introduction of new protections, such as a safe harbour for trustees.
- **Guidance:** Alongside a new approach to decumulation, guidance can play a fuller role in helping savers to make the right choices prior to and throughout retirement. The Single Financial Guidance Body (SFGB) will have an important role to play in ensuring that appropriate guidance is available to savers.
- **Decumulation Principles:** The adoption of a series of common principles underpinning the new decumulation process could be hard to achieve, given the Government's reluctance to legislate in this area. However, this could be achieved through changes to FCA regulations. International examples of where this approach has been pursued could help to generate a consensus amongst policy makers.
- **Alternative Ideas:** Other options for improving decumulation outcomes for savers, such as the creation of a deferred annuity market or Collective Defined Contribution (CDC) schemes, face serious barriers. In the case of the former, the capital holding provisions of the EU's Solvency II Directive make it difficult to create such a market; in the latter case, many different forms of CDC exist and the benefits of pooling can be achieved in conventional DC schemes.

DISCUSSION OF PROPOSALS

DO YOU BELIEVE THAT THE PROPOSED DECUMULATION PROCESS PROVIDES AN EFFECTIVE MEANS OF GUIDING SAVERS TO DECUMULATION PRODUCTS OR SOLUTIONS THAT ARE APPROPRIATE TO THEIR NEEDS? IF NOT, WHAT ALTERNATIVE APPROACH DO YOU SUGGEST?

Participants indicated their support for the decumulation proposals set out in the consultation document, though they indicated that a number of nuances should be considered. In particular, participants were keen to explore whether the proposal would be, in effect, a default pathway or a preferred pathway with other options given equal prominence. In other words, participants wanted to see a stronger consideration of how signposting would be structured, how 'hard' it will be and, where appropriate, how members will be encouraged to make active choices. The proposal does not envisage how this will work at present. It leans towards a single free choice rather than a hard default.

One participant favoured a joining mechanism that pushes people more strongly towards an income stream than the PLSA proposal envisages. This was partly a result of the specific characteristics of the scheme represented by this individual. However, it was also a result of the available evidence, which shows that most savers want someone else to choose a product solution for them. All agreed that a range of default options could be designed, depending on the characteristics of individual schemes.

Participants stressed the role that guidance can play in helping savers to make active decumulation choices that are in their best interest. Regulated advice, like that offered by LV=, is unique in the market and is likely to remain rare, even as robo-advice develops. This places greater pressure on the guidance market. As a result, the industry needs to be much smarter in how it delivers guidance. Guidance can lead people towards a solution without regulated advice ever being given. For example, this can be done by showing individuals cohort choices and encouraging them to consider their decisions in light of this information. This approach also negates the fear of provider liability for poor outcomes.

Trustees would appreciate having a place to send members for guidance as part of the suggested process. This should be the Single Financial Guidance Body (SFGB). However, the way in which savers interact with this body needs to differ from how they have engaged with its predecessors. The SFGB body should become a regular point of contact that trustees and employers can direct scheme members to whenever a pension (or wider lifetime savings) question arises.

Moreover, in order to ensure that members are continuing along the most appropriate pathway throughout the course of later life, age triggers could be employed to remind them of their default pathway and any upcoming changes within it. This should act as a trigger for them to seek guidance. This idea of continuous review is essential and should be built into the next iteration of this proposal.

Participants were vocal on the need to guard against providers choosing the best pathway for them, as opposed to the member. NEST, being a not-for-profit organisation, is well-placed to lead the market in this sense. However, for the market as a whole, strong and independent governance is required in order to ensure the best outcomes in the interest of members.

ARE THERE ANY LEGAL OR OPERATIONAL IMPEDIMENTS TO THE PROPOSED METHOD OF ACHIEVING GOOD OUTCOMES FOR SAVERS AT THE POINT OF DECUMULATION?

Trustees' and employers' nervousness about providing a soft default pathway is an impediment at the moment and this can only be solved with regulation. Safe harbour for trustees is absolutely essential if they are to have the confidence to implement the PLSA's decumulation proposals. A series of case studies on how guidance has worked in leading people to outcomes similar to those that the PLSA wants to achieve could help trustees and employers to overcome their reticence in the absence of/prior to legislation to provide them with safe harbour. TPAS should hold this information.

The absence of a deferred annuity market limits secure income provision for savers in later life, particularly those who will have serious care needs. It is harder than ever to develop a market of this sort, as a result of the capital holding provisions of the EU's Solvency II Directive. Legislation would need to change in order to enable this market to develop.

The proponents of Collective Defined Contribution (CDC) arrangements suggest that pooling of this sort can offer protection against longevity risk for savers. The protection that these scheme types provide differs from an annuity as a consequence of the fact that they are not constrained by the same capital requirement as insurance products, given that Solvency II does not apply to them. However, participants noted that the current debate regarding CDC is disingenuous. Though the benefits of pooling are clear, CDC is being presented as a uniform entity. In reality, there are many different forms of CDC. Moreover, there are easier ways of achieving the benefits of pooling in conventional DC schemes, such as the creation of collective mortality pools.

TPR is likely to be nervous about the prospect of regulating drawdown, as a result of the lower level of resource that it possesses compared to the FCA. This could present a regulatory barrier. A sharper consideration of how the suggested process would be regulated and by which body is required in the second version of this report. In operational terms, it is clear that this model works at a large scale. The examples of JP Morgan and Thomson Reuters demonstrate this. However, the real challenge is whether this model can work at a small scale. Participants were unsure whether it would.

DO YOU AGREE THAT THE PRODUCT/SOLUTION PRINCIPLES WE PROPOSE SHOULD BE MANDATED BY GOVERNMENT? ARE THERE ANY OTHER PRINCIPLES YOU CONSIDER TO BE APPROPRIATE?

Principles of the sort proposed could form part of FCA regulations. In order for this to be effective, FCA regulations would have to apply to both trust-based and contract-based products. In short, they would need to be written into the Conduct of Business Sourcebook.

The major challenge to achieving this end is that the Government does not like to legislate in this area. In order to persuade stakeholders of the need for legislation, the case would need to be cast iron. International examples about how this could be done easily and effectively might be a useful means of illustrating the benefits of the approach to officials. It is essential to ensure that both regulators support this proposal before proposing it to the Government.

The PLSA's ability to build a rigorous case study example depends, to a large extent, on the success of the Australian model, which is practically identical to the PLSA proposal. However, there are some similarities between the PLSA proposal and the Swiss model for decumulation. The Swiss approach, though, places restrictions on the level of flexibility that savers have, depending on their ability to maintain a sustainable income. That is to say, flexibility for capital withdrawals is not permitted unless a sustainable income is practically guaranteed. This is to prevent people falling back onto the state.

ENGAGEMENT

8TH JAN 2018

EXECUTIVE SUMMARY

- **Industry Readiness:** The pension industry's engagement with savers is hampered by the persistence of legacy communication systems, which are difficult and costly to change. However, the industry is changing as a result of commercial pressure and some best practice has emerged. For saver interaction to improve further, the industry needs to define the goals of engagement, as well as improve the processes and products it employs.
- **Required Reforms:** No single action will improve saver engagement with pensions. A fundamental culture change amongst savers, providers and regulators is required. The value of saving and investment needs to be inculcated in savers, and the risk cultures amongst providers and regulators needs to change in order to facilitate innovation in engagement tools and techniques.
- **Fintech:** Fintech is likely to drive reform of the pension industry as it develops. Regulators can encourage innovation in this area by embracing the FCA's 'regulatory sandbox' approach, which encourages providers to experiment with new tools and techniques. Providers themselves need to embrace the spirit of fintech within their organisations and explore how it can encourage better pension engagement.
- **Teachable Moments:** The pension industry has not used 'teachable moments' and heuristics effectively in the past. More work needs to be done to identify them and assess their effectiveness. This applies to the proposed mid-life MOT. On a wider note, schemes, employers and the Government need to find opportunities to promote a 'herd' mentality amongst savers that favours appropriate engagement.
- **Standardisation:** There are potential benefits and drawbacks to the standardisation of communications across the industry. Consistency of information is crucial in order to make statements and other forms of communication comparable. However, a dirigiste approach to presentation will remove important opportunities for innovation and improvement.

GENERAL DISCUSSION

Retirement Income Targets, of the sort proposed for the UK, have not been fully assessed in Australia – the only country in which they have been in operation for any significant period of time. Nevertheless, there are clearly areas in which such targets can be useful. The first is at the level of policy development, where targets can act as goals around which the mix of policy levers (State Pension, automatic enrolment, tax relief, etc.) can be organised.

The second is at the level of consumer behaviour, where the targets could potentially motivate a positive change in attitudes to long-term saving and, consequently, the degree of saving taking place. They could also promote better understanding amongst savers, as clear targets – expressed in pounds and pence – are more user friendly than target replacement rates and other existing tools.

A significant opportunity exists for better engagement where it is well-targeted. Where it is not well-targeted, engagement can be counter-productive. However, effective engagement, which is targeted and well-timed, is hard to scale to the level required to service the number of people who have now been auto-enrolled. As a result, it needs to be targeted at the groups that need it or will benefit the most from it.

There is a lot of diversity in the pension sector, particularly amongst employers. There are some beacons of best practice, such as the guidance and advice solutions offered by The People's Pension/LV=. However, most auto-enrolment employers view pensions as a compliance exercise, which does not lead to good engagement. Moreover, employers have different degrees of appetite, resource, etc. to deliver good engagement.

The pensions sector has not necessarily made the case for saving to the appropriate degree. Improving this case is crucial to delivering better engagement. Pensions should not be considered in isolation; they should be considered in the context of relevant cost pressures and other sources of retirement finance. For example, there is a guaranteed State Pension in the UK, which is different to the Australian system, and, as a result, modifies the sort of savings messages that need to be communicated to people.

Established providers do not have a sophisticated understanding of their existing customer base at present. However, commercial motivations are driving a clearer focus amongst some providers on customer segmentation and appropriate engagement. These include the impact of disruption (i.e. losing new business to start-ups in the savings market); retention (i.e. losing existing customers to competitors); and fear of intervention by the Government if standards do not improve.

It is important to define the desired end goal of engagement. It is about more than giving people a better retirement income, because there are easier tools available to achieve this. Is engagement about getting people up to a 'half decent' level or about optimising decisions once that level has been achieved? It is important to create aspiration for a good (i.e. better than basic) retirement income, even amongst those who are on modest incomes in all or part of working life.

DISCUSSION OF PROPOSALS

WHAT REFORMS OR ACTIONS WOULD BE MOST EFFECTIVE IN GETTING PEOPLE MORE ENGAGED WITH THEIR RETIREMENT SAVING? DO RETIREMENT INCOME TARGETS HAVE A PART TO PLAY?

No single action can be taken in order to improve saver engagement; a multitude of steps are required. Fundamentally, a change in culture is necessary in order to promote saving and investment. To achieve the required culture change, the appropriate channels need to be utilised to deliver messages. For example, for the most part of the automatic enrolment population, employers cannot be relied upon to engage effectively with employees. Consequently, the Single Financial Guidance Body (SFGB) will need to be at the heart of engagement with these savers.

Reforms to regulations and organisational risk cultures are essential to enable providers to innovate. Some providers have already started to introduce innovative engagement approaches. For example, TPP supplies electronic-only statements and Legal & General has introduced video statements. Both of these approaches are intended to make pension information more easily accessible for savers.

Although it is unclear where existing regulations can be modified in order to improve engagement, it is clear that regulators and the Government can facilitate improvements by encouraging innovation amongst providers. The principal barrier to designing and delivering an omni-channel engagement strategy is often the presence of legacy systems that remain in place amongst providers. Changes to these systems are costly. For example, it cost one major insurance provider approximately £1 million to change the presentation of pension information from percentages to pounds and pence.

Where the profit motive is involved, there is a clear and present incentive to innovate to retain or win business. However, not all schemes are profit-oriented and, as a result, may not view savers as customers. It is more difficult to encourage change amongst schemes of this sort. Alternative means need to be considered to improve engagement in the different types of scheme.

IF ADOPTED, THE PENSIONS DASHBOARD SHOULD LEAD TO GREATER USE OF FIN-TECH SOLUTIONS ACROSS THE PENSIONS SECTOR. WHAT ELSE COULD FACILITATE FIN-TECH IN PENSION SAVING?

Fintech is likely to drive reform of the pension industry, not the other way around. The dashboard will provide the infrastructure around which innovation can occur. It removes a key barrier to better engagement, which will facilitate innovation. It will also enable other changes, such as the consolidation of small pots, which might make engagement with pension savings more attractive.

Providers need to bring fintech in-house (or, at least, the spirit of fintech). It should not be perceived as something foreign to the industry, but as a core part of ongoing business now and in the future. It remains the case that a more flexible regulatory culture is required to promote innovation. The FCA's 'regulatory sandbox' work is a good example of how the regulator can support the development and usage of innovative engagement tools and techniques.

IN THE CONTEXT OF WORKPLACE PENSIONS SPECIFICALLY, WHICH HEURISTICS AND 'TEACHABLE MOMENTS' HAVE PROVED MOST EFFECTIVE? HOW COULD WE DESIGN THE 'MID-LIFE' MOT SO IT HAS MAXIMUM IMPACT?

The pension industry has not used 'teachable moments' and heuristics effectively in the past. Particular life events provide a potentially powerful hook on which to hang engagement. NEST has carried out research into the sorts of life events that could offer providers the best opportunities to engage with savers. However, more work is needed in order to prove that engagement at these moments is effective; the case has yet to be proven definitively.

People are more likely to be influenced by colleagues than by information that comes from 'on high' (e.g. H.R. departments, the Government, etc.). To improve engagement across the board, it is important to create a 'herd' mentality that is favourable to it. This is much easier to do in an employer scheme than in other types of scheme.

In regard to developing and rolling out a mid-life MOT, it is important to find out what people want and what will be useful to them. Testing these solutions is crucial. An assumption has been made that mid-life is the right time. This may not be correct. Decennial MOTs might be more appropriate than a single 'check-up' at 50. Even if it is correct, mid-life means different things to different people. It is also important to be practical when considering a measure as substantial as a mid-life MOT. The cost, format and mode of delivery all need to be given careful consideration.

One insurer is in the process of piloting a mid-life MOT. Educating management about the expectations of employees at the age of 50 has formed as much a part of this process as informing employees about their options. For example, many members of Aviva's management structure were not aware that mid-life employees were not winding down to retirement and were still interested in career development.

On a broader note, the interaction between the launch of the proposed retirement income targets and the automatic enrolment phasing process needs to be considered. According to the current timetable, the targets are likely to be launched in the middle of the forthcoming phasing process. The targets could offer a useful means of reinforcing the need to save throughout this period, which could help to minimise opt-out rates. The industry should co-ordinate its response to the phasing of contributions.

DO YOU AGREE THAT THE LANGUAGE AND LAYOUT OF KEY CUSTOMER COMMUNICATIONS AND ASSUMPTIONS SHOULD BE STANDARDISED? IF SO, WHICH ELEMENTS SHOULD BE STANDARDISED?

It is important to establish what is meant by standardisation. Consistency of information is crucial in order to make statements and other forms of communication comparable. However, a dirigiste approach to presentation will remove important opportunities for innovation and improvement.

Standardised benefits statements will help with comprehensibility for savers. The style can be different, but the information should be consistent and, perhaps, in approximately the same place on every statement. However, once the dashboard is in place, strong consideration needs to be given to whether the annual benefit statement is required any longer.

AUTOMATIC ENROLMENT

9TH JAN 2018

EXECUTIVE SUMMARY

- **Contribution Rate:** An increase in the rate of minimum pension contributions to 12% of salary is considered to be ambitious. In effect, it represents a doubling of total contributions. Employers and employees need to be incentivised to save more. Changes to tax relief represent one way of achieving this end, though other options are available.
- **Employer vs. Employee Contributions:** Employer contributions are very important to achieving good saving behaviour, especially in the context of low wage growth and increasing minimum contributions. A matching contribution should be the minimum we expect from employers. However, it will be very difficult to get business groups to sign up to increases in employer contributions and cross-party alignment will be required for this to happen.
- **Phasing Increased Contributions:** Only in 2020 will the impact of phasing on people's decision to continue saving be known. As a result, it is unlikely that minimum contributions could be increased before then. However, there is nothing to stop employers moving to a non-LEL system and some already have done so. This depends on where and when the employer scheme originated.
- **Early Access Options:** There is a risk with the automatic enrolment system that some savers will have a higher income in retirement than they had in working life. Some pre-55 flexibility in regard to access should be considered to smooth low earners' income over the course of their lifetimes. However, designing a mechanism that would allow this whilst avoiding the potential for scams is difficult. The NEST 'sidecar' approach is regarded as the best model that has been proposed to date.
- **Excluded Groups:** None of the proposals submitted to the Automatic Enrolment Review 2017 for incorporating the self-employed within the existing regime were considered to be practicable. The Government's response to the Taylor Review might solve the 'gig' economy issue, though better data regarding the period of time people spend in this sector is required to design an appropriate solution. Requiring contributions from the first pound earned will, when introduced, make it easier for multiple job-holders to save for the long-term, though this is not a perfect solution.

DISCUSSION OF PROPOSALS

DO YOU BELIEVE THAT THE LEVEL OF PENSION SAVING THAT WE HAVE IDENTIFIED (12%) IS SUFFICIENT TO PROVIDE PEOPLE WITH AN ADEQUATE INCOME IN RETIREMENT?

It is difficult to say whether 12% is the right contribution level. The main challenge is to determine what represents an adequate amount of income in retirement and what level of contributions is required to achieve it. It is also important to consider what the right balance between private pension provision and other sources of income is, and to consider pension contributions in this context.

An increase in contributions to 12% of salary represents, in essence, a doubling of the rate of contributions that will be required at the conclusion of the phasing process (8% of qualifying earnings). This is ambitious. In the context of the overall policy agenda, the PLSA needs to articulate how the 12% proposal links to the suggested National Retirement Income Targets.

Employers and employees need to be incentivised to save more. Tax relief is the obvious incentive, but there are others that could be explored in greater depth. The PLSA explored tax relief as part of its consultation. The main conclusion was that this issue needs careful consideration and a more comprehensive solution before any change is suggested. Inheritance might be an alternative source of income that could top up pension schemes. Lump sum payments might be invested in a scheme, which could improve outcomes.

The lowest level of the proposed targets could be highlighted as being the income that people are likely to receive if they do not save at an appropriate level. This could help to reduce opt-outs. It is important to give people some clear indication of what their outcomes might be.

IN THE EVENT THAT AUTOMATIC ENROLMENT DEFAULT CONTRIBUTIONS INCREASE FROM 8% TO 12%, HOW SHOULD THEY BE DIVIDED BETWEEN THE EMPLOYER AND EMPLOYEE?

The employer contribution is very important to achieving good saving behaviour. The higher the proportion contributed by the employer, the more likely an employee is to remain within the scheme. Evidence suggests that people tend to contribute up to an employer match and then stop. It is an extremely powerful behavioural signal. An employer match should be the minimum that is expected and is common when we look at international examples.

In the context of low wage growth, if minimum contributions increase without a rebalancing of the employer/employee split, then the behavioural signal for savers will be to opt-out. However, if employers are expected to contribute more to pensions, there is likely to be less money available to increase pay. This will not be attractive to the Government or employees and might mean that a longer phasing period will be required to increase employer contributions.

It will be very difficult to get business groups to sign up to increases in employer contributions. Cross-party support will be required in order to overcome this major obstacle. Nevertheless, there is a belief that business groups are not focused on DC pensions at present; they are concentrating on other issues, such as the problems facing DB pensions and the cost of the apprenticeship levy. The employer might not need to contribute a full 50%, so long as it was putting in the same amount as the employee. The Government's contribution through tax relief could increase, though this would require the assent of HM Treasury.

It is clear that there will be a low level of tolerance for an opt-out rate much above the current level, because expectations have changed as a result of what we have seen of automatic enrolment thus far. Moreover, it is important to ensure that we have accurate data about the behaviour of automatic enrolment savers on which to base judgments in future. For example, in the context of increasing contributions, the focus will no longer be on opt-outs, but on cessations.

There is very little evidence that low earners take up the opportunity to make lower levels of contributions in order to balance their short- and long-term saving needs. The Local Government Pension Scheme (LGPS) demonstrates that where there is the option to contribute at half the standard rate only those people who are in danger of breaching the Lifetime Allowance (LTA) tend to do so.

OVER WHAT PERIOD DO YOU BELIEVE AN INCREASE IN CONTRIBUTIONS TO 12% SHOULD BE PHASED? THE PLSA BELIEVES THAT THE DECISION TO REMOVE THE LEL IN THE AUTOMATIC ENROLMENT 2017 REVIEW IS WELCOME. BUT, SHOULD IT BE REMOVED EARLIER THAN THE MID-2020S?

Only in 2020 will the impact of phasing on people's decision to continue saving be known. As a result, it is unlikely that minimum contributions could be increased before the mid-2020s. If they were to be increased according to a shorter timeline, there is a risk that the evidence required to justify this measure would not be complete and/or employers and employees will have only a short period of time to adjust to the new contribution rate.

There is nothing to stop employers moving to a non-Lower Earnings Limit (LEL) system at present and some already have done so. This depends on where and when the employer scheme originated. Almost exclusively, employers running pre-automatic enrolment schemes make contributions as a percentage of total earnings.

But, if they entered the market post-automatic enrolment, they are, for the most part, making contributions at the statutory minimum rate. Moreover, the pension freedoms erode the workforce management potential of pensions, because they reduce the likelihood that accumulated resources will be used to provide a retirement income.

DO YOU BELIEVE THERE IS A RISK OF OVER-SAVING FOR THOSE ON LOW INCOMES AND, IF SO, WHAT SOLUTIONS MIGHT BE WORTH CONSIDERING? SHOULD EARLY ACCESS IN THE CASE OF 'FINANCIAL HARDSHIP' BE ONE OF THEM?

There is a risk with the automatic enrolment system that some savers will have a higher income in retirement than they had in working life. As a result, there could and perhaps should be some pre-55 flexibility in regard to access. The Pensions Policy Institute, in co-ordination with the debt charity Step Change, proposed a mechanism for early access that could be used for the alleviation of debt, which could have a significant impact on long-term income (due to the fact that servicing debt is costly and the cycle of debt repayment is hard to escape).

An alternative model that would enable some variety of early access is NEST's 'sidecar' approach. Evidence suggests that people are willing to contribute more to a pension if they are of the view that they could access a portion of it if necessary. However, for a product of this sort to be a viable early access solution, significant changes to Universal Credit are required to ensure that low income savers do not lose benefits as a result of having accumulated funds in the 'sidecar'.

One of the strengths of the automatic enrolment regime has been its relative simplicity. If additional features are incorporated into the existing system, this will undoubtedly increase complexity, which could be detrimental to the model as a whole. Early access also introduces moral hazard. There could be any number of scams associated with it. However, the 'sidecar' approach sidesteps the scam potential to a large degree.

It is very difficult to model the likely impact of early access arrangements on savers' overall financial resilience. They need to be introduced in order to be measured properly. NEST is in the process of attempting to set up a pilot study. Fundamentally, the industry needs to determine if automatic enrolment is the correct medium through which to achieve the end of in-work financial resilience.

CAN YOU SEE ANY IMPEDIMENTS TO OUR PROPOSED APPROACH TO THE INCLUSION OF THE SELF-EMPLOYED, MULTIPLE JOB HOLDERS AND YOUNGER WORKERS WITHIN THE AUTOMATIC ENROLMENT REGIME? IF SO, CAN YOU SUGGEST ANY SOLUTIONS TO THESE PROBLEMS?

None of the proposals submitted to the Automatic Enrolment Review 2017 for incorporating the self-employed within the existing regime were considered to be practicable.

The period of time that people spend in the 'gig' economy is unclear. There is a significant degree of churn. The people who spend a substantial period of time in the 'gig' economy are those that we need to be concerned about. The Government's response to the Taylor Review might solve the 'gig' economy issue. However, this will not solve the issue in regard to the traditional self-employed. HMRC will likely be involved in the trials on this issue moving forward.

One of the principal barriers to the inclusion of multiple job holders within the scope of automatic enrolment is that many of these people do not want all of their employers to know how much they are earning in other jobs. The obvious way to incorporate multiple job holders into the automatic enrolment system is to remove the earnings trigger, though this might capture many people who would be better off not being included (e.g. those earning below £10,000). Requiring contributions from the first pound earned will, when introduced, make it easier for multiple job holders to save for the long-term.

APPENDIX – LIST OF CONSULTATION RESPONDENTS AND WORKSHOP PARTICIPANTS

Aberdeen Standard Investments
Age Partnership
Age UK
AHC
Akzo Nobel UK Limited
Association of British Insurers
Association of Consulting Actuaries
Augentius UK Ltd
Aviva
The People's Pension
British Medical Association
Bruce Sayers Associates Ltd
Burness Paull LLP
Capital Cranfield
Capital Cranfield Trustees Pension Scheme
Cardano
Carillion Construction Ltd
Centre for Policy Studies
Citi
Dean Wetton Advisory Ltd
Department for Work and Pensions
Dimensional Fund Advisors Ltd
Equity Release Council
Ferrier Pearce
FirstGroup PLC
Federation of Small Businesses
Hargreaves Lansdown
HM Treasury
Hymans Robertson
Institute of Chartered Accountants of Scotland
Institute and Faculty of Actuaries
Irrational Insights Ltd
JLT Benefit Solutions Ltd
Johnston Press PLC
Just
KPMG
LGIM
LV=
Mercer
Money Advice Service
National Employment Savings Trust
NOW: Pensions
Pensions Policy Institute
PIMFA
Prudential Corporation
Resolution Foundation
River and Mercantile Group
Royal London
Sackers
Smart Pension Ltd
Spence & Partners Pension Scheme
Standard Life
Standard Life Pension Fund
T. Rowe Price
The Pensions Advisory Service
TPT Retirement Solutions
Trades Union Congress
Which?
Willis Towers Watson
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