PENSIONS AND LIFETIME SAVINGS ASSOCIATION

DC DECUMULATION:

EVOLVING THE PENSION FREEDOMS

- FINAL RECOMMENDATIONS

PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

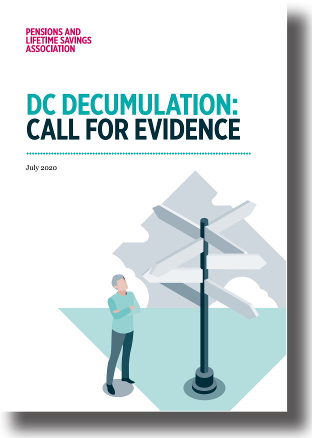
EXECUTIVE SUMMARY

1. The imperative to place savers needs at the heart of pensions policy and delivery is as strong as ever. In a world marked by fast paced change and uncertainties, this focus remains a constant.

2. The pension freedoms announcement in 2014 radically revised policy and practice in at-retirement options - bringing new opportunities, challenges and risks to savers and pension schemes. The market and regulators have responded – and new developments continue to emerge.

3. But we believe more needs to be done to support the evolution of the pensions freedoms. This document sets out PLSA's final recommendations for a new framework for DC Decumulation.

4. In July we published our *DC Decumulation Call for Evidence* setting out our proposals to support and enable schemes to better support savers with their at-retirement decisions. This sought to operationalise our widely supported vision for guided at retirement outcomes (*Hitting the Target 2018*). This work has been driven by PLSA's mission, to help everyone achieve a better income in retirement, and seeks to place savers at the heart of at-retirement policy and delivery.



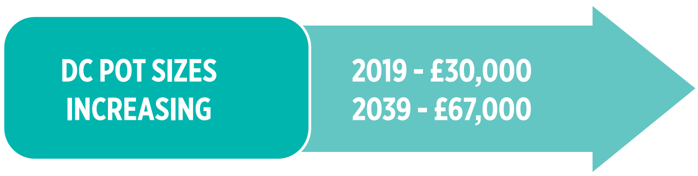
5. *The Call for Evidence* period has been marked by dynamic discussions and debate. We are extremely grateful for the quality of responses and engagement on the issues. We received 25 written responses, ran 7 roundtables including schemes, advisers, providers and consumer representatives. The input and views have reflected the breadth of our membership, wider industry and consumer representatives. And the clarity of focus on the saver has been prominent throughout.

6. The framework proposed in the *DC Decumulation Call for Evidence* received widespread support and therefore remains broadly unchanged. But some of the detail has been enhanced, refined, clarified and added to.

7. The **case for change** (Section 1) remains clear, and has been further informed by input from stakeholders. The landscape into which the pension freedoms have been introduced continues to evolve and provides key context, informing the risks to be managed and opportunities to be maximised.

8. There needs to be a bridge between the approach to using inertia to get people into pension saving, and the complex decisions they are required to make at retirement.

DC pots are growing, reliance on DC saving is increasing, and the market continues to move towards scale operations that could be beneficial for decumulation options for all savers.



9. It is clear that the economic risks and decision-making risks faced by savers need to be addressed more actively, and also that schemes are well placed to offer further assistance. But there are some significant barriers preventing schemes taking action, including litigation that can arise for schemes in providing additional support, including signposting. This can best be mitigated by radical change – namely regulatory requirements. There is an opportunity to act now to address these risks – and to act in a way that evolves the pension freedoms, shaping the landscape for a better future.

10. Key aspects of input and discussion during the call for evidence period (Section 2 and annexes) have included for example: additional risks to savers; more evidence and information; debate about defaults and statutory obligations; examples of products that address key risks; the place of advice, guidance and signposting; and the impact on small schemes. All these elements are catered for in our final recommendations.

11. Our **final recommendations for a new decumulation framework** (Section 3), incorporate what we have heard during the call for evidence and the conclusion we have drawn from those discussions.

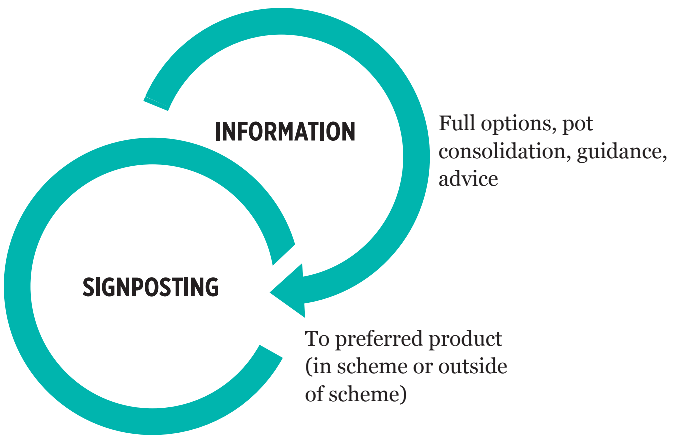
12. This new framework, and the details within it, work together in combination to meet the key **objectives** we set out:

- ✓ To provide more support to savers who do not engage with their options – using the lessons from Automatic Enrolment and Open Market Option – as well as supporting freedom and choice for those who do;
- ✓ To facilitate and influence future product development with a view to managing the risks for savers as Defined Contribution (DC) pots grow and dependency on DC derived incomes increases;
- ✓ To utilise the benefits of scale and mechanisms such as the trust-based fiduciary duty and Independent Governance Committees (IGCs) responsibilities;
- ✓ To support similar saver experiences across the market, whilst enabling innovation to flourish; and
- ✓ To mitigate or help manage some of the savers risks;
- ✓ To mitigate some of the key risks schemes are facing – including litigation, financial and operational risks.

13. In summary – the framework delivers:

14. A **saver communication and engagement journey via minimum standards** using nudge theory, deploying a 'path of least resistance' by signposting the saver to a preferred solution (in scheme or outside of scheme) – seeking to remove the risk of the poorest outcomes.

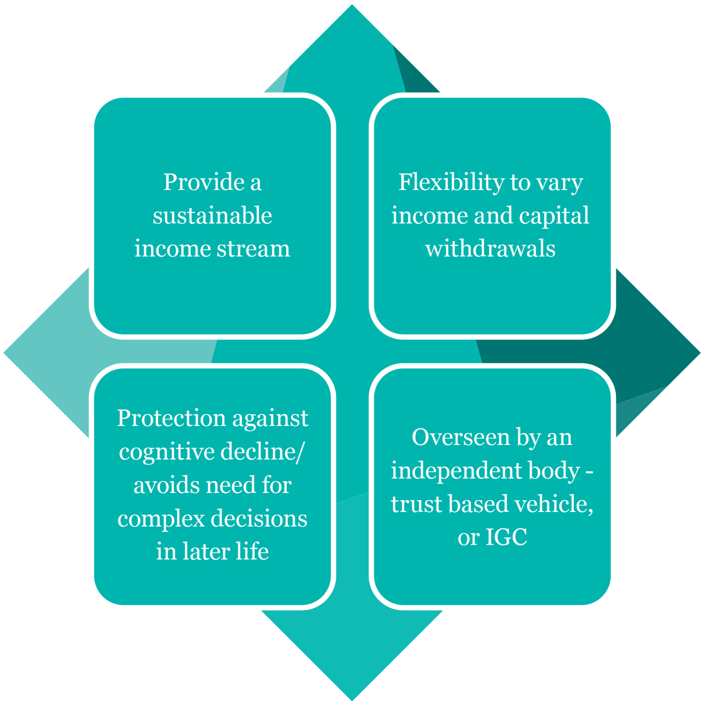
- The process is a 'consent/opt in' model, schemes will issue key messages and support regarding guidance and advice that is available.
- It incorporates a default into an investment strategy (an opt out model) for those who do not engage at all.
- The signposting also benefits the saver by utilising the knowledge, expertise and purchasing power of the industry – including schemes and trustees - on behalf of the saver.
- By enabling signposting to products outside of the scheme we can help ensure the new requirements don't exert unreasonable costs or regulatory burdens on schemes who may not wish to provide a product in-house



- Member can take wider advice/ guidance at any point
- Member has to 'opt in' to preferred option
- Member can choose to take other options
- If member doesn't engage - default investment

15. A set of **minimum product standards** – taken together with the saver communication and engagement the product minimum standards respond to what we have been able to assess of current saver behaviour, which suggests that people are not well equipped to trade off the numerous and complex risks they face. The product standards therefore seek to:

- help savers with these trade-offs by outlining the key considerations about product features for the scheme to use in establishing a preferred solution;
- reflect the phases of retirement and changing needs of the saver, helping to also manage the economic risks the saver faces – and seeking to secure a sustainable income in retirement;
- add weight to the demand side to influence supply side developments in a direction that addresses key economic and decision risks for savers.



16. Key **governance minimum standards** which along with the product and saver communications and engagement standards:
    - support schemes in putting this framework into delivery;
    - ensure transparency about the extent and scope of responsibility;
    - provide assurance to schemes and trustees who might be seeking to signpost their savers to another scheme or provider for their decumulation options – because where the framework applies, the product is subject to the same standards they must consider when signposting.

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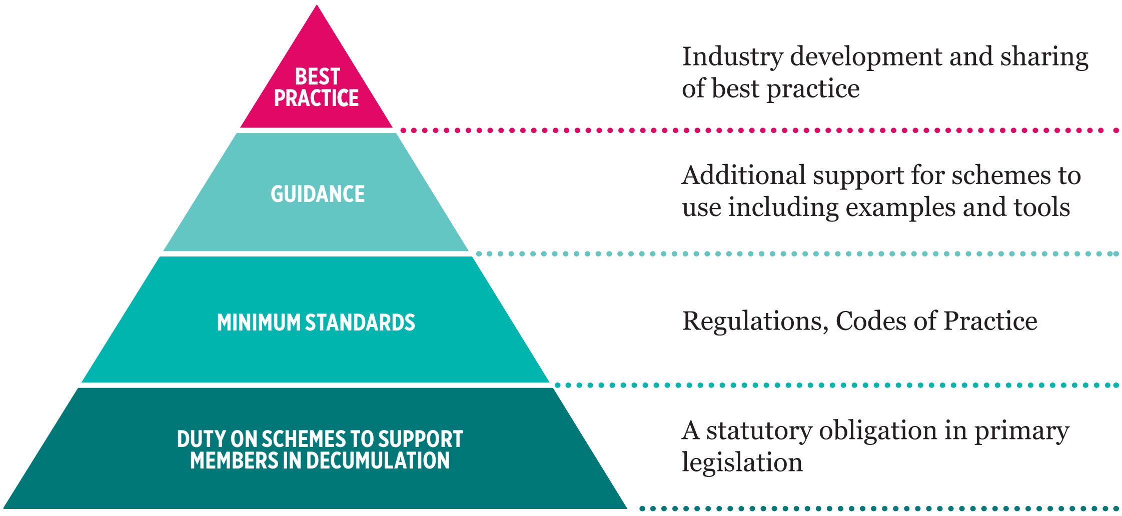
17. By creating a **statutory requirement on schemes**, we can generate a stronger demand side, grow and utilise the information and expertise within the industry for the good of the saver, and also help mitigate litigation risks and some costs for schemes. It will also support a more consistent saver experience across the numerous schemes they may be part of.



18. The **minimum standards** will provide transparency of legal obligation, and guidance will help support schemes to deliver. By keeping the standards at the appropriate level, the cost burden can also be managed, but innovation can also flourish. In response to what we have heard in the *DC Decumulation Call for Evidence* period we will, in addition, remove the requirements from the smallest schemes, add further guidance and templates, and explore potential best practice kite marking - to help schemes keep costs down.

19. Some schemes already have impressive offerings for their savers – and we want to keep that drive for continuous improvement. Sharing best practice will support momentum, and following calls for kite marking PLSA will also explore the potential for providing 'best practice standards'.

20. In these various ways the framework supports savers with the risks they face – and seeks to do this in a way that addresses key risks faced by schemes. It supports future developments, and seeks to frame those in a way that places the saver at the heart of pension policy and delivery.

21. Section 4 sets out the next steps and our call to action – in summary the PLSA:

- calls on Government and Regulators to deliver the new framework in consultation with industry to evolve the freedoms and meet the needs of savers;
- calls on industry to embrace and support the framework; and,
- commits to further work with the industry and government and regulators – to develop and support detailed guidance, mitigations for small schemes, and explore the potential for best in class standards.

CONTENTS

THE PLSA

Our mission is to help everyone achieve a better income in retirement. We work to get more people and money into retirement savings, to get more value out of those savings and to build the confidence and understanding of savers.

We represent the defined benefit, defined contribution, master trust and local authority pension schemes that together provide a retirement income to 20 million savers in the UK and invest £1 trillion in the UK and abroad. Our members also include asset managers, consultants, law firms, fintechs and others who play an influential role in the governance, investment, administration and management of people's financial futures.

THE CALL FOR EVIDENCE

The *Call for Evidence* opened on 28 July 2020 and closed on 4 September 2020. Over the *Call for Evidence* period, the PLSA engaged with 47 people from across the pensions sector via 7 roundtables and bilaterals on the proposals set out in the document.

We received 25 written responses, with 15 providing specific responses to all the questions posed in the *Call for Evidence* and 6 providing extensive sources of evidence that address many or all of the *Call for Evidence* questions.

THE PLSA TEAM

The PLSA team that worked on this report were: Nigel Peaple, (Director of Policy & Research); Lizzy Holliday (Head of DC, Master Trusts & Lifetime Savings); George Currie (Policy Lead: DC & Lifetime Savings); and Alyshia Harrington-Clark (Policy Lead: DC).

We have worked closely on the proposals contained in this document with the members of our Defined Contribution Committee, Master Trust Committee, and Policy Board, as well as with our member working groups.

SECTION 1 – THE CASE FOR CHANGE – RISKS & OPPORTUNITIES

SUMMARY

22. The Pension Freedoms revolutionised the way in which people could access their pension savings. There is great appeal in the idea of creating 'freedom and choice' for individuals. But the consequences are significant - including greater complexity of decision making and increased risks for the individual saver – and many could be losing out. We believe further change is needed to help evolve the pension freedoms – to enable freedom and choice but with more support to help savers manage these risks.

23. Where options are increased and new risks introduced for savers, the litigation risk for schemes in providing support and offering solutions rises commensurately. Our research[1] indicates that schemes responses to the pension freedoms have varied – with subsequent disparity of experience of savers – this generally reflects the perception of risk. There also appears to be a gap in product design as available products are not serving the various changing requirements for income in retirement, and mitigating some of the economic risks for savers.

24. Our solution seeks to reduce the risk to savers, and address the tension between support savers need and the risks in providing for it. It also seeks to provide a clear framework of expectations designed to deliver a more consistent experience for savers across the market, to support demand side pressures, and to help support emerging innovation and drive future change.

LANDSCAPE

25. The long-term savings environment has been transformed over the course of the last decade. The introduction of Automatic Enrolment (AE) has enabled more than 10 million people to start saving for retirement or to save more than they were previously. This has revolutionised the way people accumulate pension savings and given greater retirement security to many.

26. AE's success is largely due to the use of behavioural economics - specifically, harnessing the power of inertia. The pension freedoms pose a real contrast to the approach taken with AE, and also to the trends observed regarding engagement and decision making generally, as well as with the open market option. Something more is needed to bridge the gap - between reliance on inertia at the start of savings, and unsupported complex decision making for the individual when they start to access them.

27. The launch of Pension Wise to help people understand their options is welcome, and its interactions have increased by some 49% between 2017/18 and 2018/19. However,

[1] https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2020/The-Evolution-of-Drawdown-2020-Addendum.pdf?ver=2020-07-28-114627-370 and https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2020/The-Evolution-of-Drawdown-2020.pdf?ver=2020-08-10-120558-677

findings from the FCA review of the Financial Advice market[2] indicates that not all consumers have appropriate access to a wide range of services to help them with financial planning, particularly those with smaller amounts of money – and that this issue has worsened in recent years. The Money and Pensions Service estimate around half people accessing DC pots in 2018-2019 did not receive regulated advice or Pension Wise guidance[3]. More needs to be done to support the saver with decision making and navigating their options.

28. AE has contributed to the significant growth of the number of people saving in DC pensions, as has the changing nature of Defined Benefit (DB) funding regulation and closure of DB schemes. Over time these shifts will mean more people than ever will be reliant on DC only savings to provide their income in retirement[4].

29. The level of these DC savings is also forecast to rise – from a median of around £30,000 in 2019 to around £67,000 in 2039[5]. While we are seeing some developments in products, this growth is likely to make more sophisticated options for retirement incomes possible in the future. For example, products supporting additional options for securing an income stream from savings, as well as products which address the changing needs of retirees throughout their retirement or phased retirement journey. So while we need to act now to support current savers, those changes need to be made with eye to the growth of savers and their savings in this space – and in a way that helps to shape that future provision.

30. The success of AE has also led to growth of the Group Personal Pension (GPP) market and master trusts - and new regulations including the Master Trust Authorisation Regime. Employers are increasingly entering fully bundled arrangements with master trust or providers, or undertaking a bulk transfer. We might expect to see further consolidation over time – forecasts suggest that master trust and GPP assets under management (AUM) will continue to grow strongly over the course of this decade, with master trust AUM growing particularly strongly[6].

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[2] FCA, Evaluation of the Retail Distribution Review and the Financial Advice Market Review: Call For Input (2019).

[3] T. Shanmugarasa et al, Pension Wise Service Evaluation: Experiences and Outcomes of Customers Using Pension Wise in 2018/19) (2020).

[4] For example, PPI research found that people reaching State Pension age over the next five to ten years vary considerably in their pension and non-pension saving. Within this population there are segments who are more reliant on their DC savings to secure an adequate income. https://www.pensionspolicyinstitute.org.uk/research/research-reports/2014/27-11-2014-transitions-to-retirement-how-complex-are-the-decisions-that-pension-savers-need-to-make-at-retirement/

[6] Broadridge analysis

	2019	2039
Existing DC schemes	3.1m	1.7m
New DC schemes post AE	2.0m	2.5m
Master trusts	8.1m	10.0m
Total DC	13.3m	14.2m

31. This growth of large scale operations offers an opportunity for development of decumulation support and products which can also work alongside schemes which may not wish to deliver decumulation products options.

SAVERS AND THE RISKS THEY FACE

RISKS

32. The removal of the requirement to annuitize has introduced a plethora of new economic risks which are now borne by the individual. These include longevity risk; the risk of running out of money altogether, or not living as well as they might due to fear of running out of money. Also, ongoing exposure into retirement to investment risks – as well as the need for ongoing management of those investments. With an annuity, these risks are managed in retirement for the individual.

33. There are also a number of challenges and risks associated with the nature of the decision making process. For example, the complexity of economic risks to mitigate and trade off, the potential for diminished decision making capacity into later life, the need for planning varying income needs through the changing needs in retirement, and considerable information asymmetry and purchasing power imbalances.

SAVER BEHAVIOUR

34. The available evidence regarding saver behaviour suggests that people are not seeking to balance their short- and long-term needs in their decumulation decisions. Instead it appears savers are favouring immediate access to cash over long-term security. Research by The Peoples Pension (TPP) found that participants perceived drawdown simply as a by-product of accessing tax free cash and people had given little thought to their remaining pension savings[7]. The Defined Contributions Investment Forum report came to similar conclusions[8].

[7] TPP & SSGA, New Choices (2016).
[8] DCIF, Five Years of Freedom (2019).

35. Other findings include that savers postpone the decision until they feel able to dedicate the 'mental bandwidth' necessary to consider them properly[9] - and that they tend to take the path of least resistance, which can lead to poor retirement outcomes[10]. The FCA Retirement Outcome Review reported that few people were shopping around, and were entering drawdown products from their pension accumulation provider[11]. This repeats the pattern observed before the Freedoms in relation to the Open Market Option.

MARKET CONTEXT

RISKS FOR SCHEMES AND PROVIDERS

36. The key challenges and opportunities to schemes and providers are to support savers in engaging with their options, and to provide products that cater for the breadth of risks that they face. The key risks they face in doing this include:

- Litigation risk – that schemes endeavour to support members, but in stepping beyond what is required in legislation and regulatory requirements, they could be subject to legal action. For example where savers could in the future consider they have achieved a sub-optimal outcome, or in respect of what has or has not been communicated to them. This could have a knock on effect to the employer in single employer trust based schemes, who may be financially accountable and may also suffer reputational damage to their brand.

- Information risk is also seen as a barrier to understanding individual savers' needs – along with additional costs and complexity of delivering support and products.

- Regulatory, marketing and advice risks - these all relate to schemes potentially breaching various requirements if they provide more than the required minimum in decumulation activity and provision.

PRODUCT DEVELOPMENT

37. The number of ways of accessing pensions since the freedoms have grown – but there is room for further innovation and development – particularly in the evolution of composite models that balance short term and long term needs of retirees. For example, combining flexibility in earlier years of retirement with security in later years – and in securing longer term needs in advance.

38. Some of this might develop further as pot sizes grow, to address some of the economic feasibility challenges which arise from the various funding regimes across the pensions landscape. However, the pace and direction of travel might be impeded by a weak demand side, where this is dependent on individual savers – due to the information

[9] TPP & SSGA, New Choices (2016).
[10] FCA, Retirement Outcome Review: Final Report (2018).
[11] FCA, Retirement Outcome Review: Final Report (2018).

asymmetry, weak purchasing power and tendency to take the path of least resistance as highlighted earlier.

39. This is why our final recommendations include some steers and standards on products. We are seeking to exert additional demand side pressure through the use of required minimum standards, and the purchasing power of schemes.

MARKET PRACTICES

40. We know from our previous research[12] that member experience and scheme provision have varied in the trust based landscape – several master trusts are leading the way in the development of new income drawdown solutions including multi-pot options that seek to address risks posed to retirees financial wellbeing by later life issues, and there has been growth in the number of single employer schemes that are signposting to master trusts. But we consider more needs to be done to support and accelerate these developments, and to cover the whole of the market.

41. The FCA Investment Pathways, due to be fully implemented by February 2021, go some way to help address one of the key risks for savers and have shaped the market response. Where savers decide to access their pension through drawdown without taking advice, the pathways nudge savers to allocate their pension saving to one or more of four investment pathways[13], according to their objectives. FCA has also introduced a new duty on IGCs to oversee the value for money of investment pathways solutions for pension drawdown.

42. We believe our solution works in conjunction with the pathways, but provides a broader response to a number of additional risks that need to be addressed.

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[12] https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2020/The-Evolution-of-Drawdown-2020-Addendum.pdf?ver=2020-07-28-114627-370 and https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2020/The-Evolution-of-Drawdown-2020.pdf?ver=2020-08-10-120558-677

[13] The FCA has mandated the working and numbering of the objectives and has introduced a timeframe for each to improve clarity for savers. Larger pension providers must deliver pathway solutions for at least two of the four objectives and refer consumers to another provider's pathway solutions for any objectives for which they do not themselves provide a pathway solution.

SECTION 2: CALL FOR EVIDENCE – AN OVERVIEW

SUMMARY

43. The call for evidence period has been marked by dynamic discussions and debate. Three broad themes of agreement emerged:

- The principle of providing support for savers and the need to go beyond current regulatory requirements to do so;
- The need to find an appropriate way to bridge the gap between AE's successful use of inertia, defaults and opt-outs and the extensive complexity of decisions that the freedoms have left savers to grapple with; and
- The risks and cost inherent in navigating the current regulatory frameworks, in order to deliver what all can see is needed and that all desire to deliver.

44. Consensus to drive change was clear, with the most challenging debate on the question of how to deliver a framework to achieve the best outcome for savers – including themes such as:

- risks to savers
- harnessing inertia, use of signposting and the place of advice and guidance
- product availability and potential future innovation

Our final recommendations have incorporated the key themes raised. The annex provides further detailed commentary.

RESPONSES: CASE FOR CHANGE – RISKS AND OPPORTUNITIES

45. In our call for evidence paper we asked a number of questions about risks savers and schemes face, drivers and behaviours relating specifically to trust based savers, and implementation of the FCA pathways. We wanted to check our assessment of the context and landscape as set out in our *DC Decumulation Call for Evidence* (Sections 1 -3) and summarised in Section 1 above

    - Risks for savers: The majority of stakeholders agreed with our analysis of the risks faced by savers, and some suggested additional risks, which we believe our solution can help mitigate. These included scams and fraud, taking no or limited advice, and principal agent risks.
    - Trust based savers: Generally, stakeholders shared our view that savers in contract-based arrangements, where much of the current evidence is on saver behaviour, exhibited similar preferences to those in trust based arrangements.
    - Scheme & employer risk: Responses also agreed with the risks to employers and schemes identified by the PLSA. In particular the risks of signposting to products without a regulatory framework to support that.

- FCA Pathways: Respondents to the consultation identified a mixture of practices regarding the implementation of the FCA's 'Investment Pathways'. The majority of trust-based respondents did not think pathways were suitable for their members, and felt that they could deliver more appropriate solutions that would not be pathways equivalent and that would not have been possible in contract environments. Some contract-based schemes also expressed the view that some of the best quality and high value options did not sit comfortably within the pathways framework. We believe our solution works in conjunction with the pathways, but provides a broader response to a number of additional risks that need to be addressed.

46. Our Final Recommendations incorporate these comments.

RESPONSES: PROPOSED DC FRAMEWORK

47. In our *DC Decumulation Call for Evidence* we set out our proposed new framework – a statutory obligation for schemes to support their savers with their decumulation. This support should consist of three elements – member engagement and communication; decumulation products (provision of or signposting to) and scheme governance processes in relation to design or selection and delivery of member engagement and products. Also that a set of standards should apply to each of those three elements, and finally, that guidance should support schemes to deliver the three elements and work within the standards.

STATUTORY OBLIGATION

48. Several stakeholders indicated the proposed statutory obligation would be a step forward. Others felt without the changes that we proposed the constraints or barriers to delivering good retirement outcomes for their members would remain significant.

    "Our priority is that law and regulation allow streamlined decumulation pathways, along the lines of the bulk of the call for evidence paper. We feel that these should be appropriately regulated."

49. Many stakeholders were reassured that the statutory obligation and minimum standards within our proposals provide protection regarding litigation risk they currently face – especially regarding signposting decumulation solutions outside of the scheme. A few felt strongly that the PLSA should be calling for a full safe harbour, potentially linked to Master Trust authorisation status.

50. A minority of stakeholders questioned whether it is proportionate to introduce a new statutory obligation on trustees, particularly for small schemes. Others felt it was proportionate.

    "We believe the solution set out by the PLSA is proportionate."

51. Taking into account the balance of views, the value and consistency of support for savers, and additional protection for schemes, we have retained the statutory obligation in the final recommendations. But we have added some mitigations to complement

those already embedded in our proposals, to go further to support small schemes and mitigate costs (See section 3).

MEMBER ENGAGEMENT AND COMMUNICATIONS

52. Generally, stakeholders were enthused by our proposals to improve member engagement and communication, and emphasised the importance of doing this starting early, building over time and continuing after retirement. Many respondents felt this is one of the key aspects of the framework.

53. The guided pathway approach, using a path of least resistance, was welcomed by most stakeholders - as it was in the Hitting the Target proposals.

"The mechanism should be to nudge savers into choosing the suggested product, at the appropriate stage of their journey."

54. Some respondents were concerned that the signposting or offering a product in-house would constitute advice or financial promotion. We consider that our proposals for a regulatory framework is key to mitigation of this risk. We believe that carefully designed signposting to a third party or in-house products should not constitute advice or financial promotion. But further clarification is required to enable trustees, schemes and providers to act – our recommendations seek to create a step change on this issue.

55. Guidance and advice was also a common theme – including the default guidance measures in the Financial Guidance & Claims Act 2018, the importance of taking advice where appropriate, along with recognition that savers may not sufficiently value advice and the challenges in sourcing it. Discussions included the need to keep up efforts to engage alongside signposting – and the potential for fintech, robo-advice and guidance to support the customer journey overall. Our framework is consistent with and complementary to these sources and types of guidance and advice.

PRODUCTS

56. The vast majority of stakeholders were supportive of the overall approach we proposed as a way of mitigating risk for members, supporting trustees in identifying preferred solutions, and in helping shape the future market.

57. Some asked specifically for more to be done to help savers develop an appropriate withdrawal strategy. A small minority of respondents were concerned that the current proposed minimum standard could not be met as appropriate products do not exist.

58. Others outlined potential products that might facilitate better or more sustainable outcomes for savers as they enter and progress through retirement. For example, Collective Defined Contribution schemes, deferred annuities, guaranteed drawdown, and individual mortality underwriting (see Annex for further information).

59. Our recommendations support innovative solutions coming to market, and we will explore the potential for additional guidance on specific elements. We expect the potential for products that tackle savers needs throughout retirement to grow over time,

as the size of DC pots grow and the demand side, supported by this framework, helps to shape the innovation.

GOVERNANCE

60. Respondents generally agreed with the governance requirements set out in our proposal. Stakeholders emphasised the importance that governance procedures assess that products are fit for purpose and, where applicable, offer good performance and value for money. Also, that the processes should focus on the review of products and solutions that fulfil the generality of members, and should acknowledge the limitations of the ability of trustees when overseeing the products of a third party.

    "The quality and effectiveness of the associated governance processes should be key. If trustees demonstrate that they undertook this to the best of their abilities, they should not be at risk of recourse or compensation that only the benefit of hindsight would present."

61. Some respondents proposed additional governance requirements around management information, minimum consent timeframes and disclosure.

GUIDANCE AND BEST IN CLASS

62. Stakeholders also raised the importance of improving the resources for and knowledge of trustees to help deliver the new minimum standards and supported our intent that guidance also be provided alongside any statutory objective and/or regulation. Some respondents called specifically for PLSA guidance.

63. Some stakeholders urged the PLSA to find a way to ensure the minimum standards are a true baseline and not targeting best in class, and to encourage providers and schemes that already deliver best in class solutions. Our proposals are, indeed, designed in that way

    "*The policy as developed should seek to avoid 'hard wiring' the framework to the extent the future developments in the market that are beneficial to members and provide good solutions for schemes may fall outside of the recognised 'good practice' and not be appropriately recognised"*

    "The PLSA has rightly referred to providers that already provide higher levels of support, and this should be encouraged"

64. Furthermore, an industry accreditation scheme was noted to have the potential to reduce the burden on smaller schemes when selecting a solution to signpost to. We have therefore added to the proposal, so that our final recommendations incorporate a commitment for the PLSA to explore the potential for providing 'best practice standards'.

WHOLE OF MARKET SOLUTION

65. Stakeholders agreed that the principle aims we had to improve member outcomes in the trust-based environment were also appropriate for the contract-based environment. Concerns were raised about whether placing additional responsibilities on IGCs was the appropriate way to achieve this - reasons including scope and reach of IGCs.

66. We agree that responsibilities for the minimum standards need to be appropriately delineated between the employer, provider and IGC to deliver a similar outcome as a requirement on trustees. This would include an oversight but not executive role for IGCs and, where IGCs do not provide this oversight function, other appropriate governance structures may be more appropriate.

SECTION 3: FINAL RECOMMENDATIONS - A NEW DECUMULATION FRAMEWORK

SUMMARY

67. The Pension Freedoms created opportunities and risks for savers, schemes and providers. Following the *Call for Evidence* we believe our final recommendations mitigate the main risks, provide key support for savers and schemes, while also allowing freedom and choice and future innovation to flourish.

68. The key elements of the framework are as follows, and they work in combination to meet the above objectives listed below.

a. To provide more support to savers who do not engage with their options - utilising the lesson from AE and OMO – as well as supporting freedom and choice for those who do;
b. To facilitate and influence future product development with a view to managing the risks for savers as DC pots grow and dependency on DC derived incomes increases;
c. To utilise the benefits of scale and mechanisms such as the trust-based fiduciary duty and IGCs responsibilities;
d. To support similar saver experiences across the market, while enabling innovation to flourish; and
e. To mitigate or help manage some of the savers risks
f. To mitigate some of the key risks schemes are facing – including litigation, financial and operational risks

69. This framework, and the details which sit within it, deliver a process to support the saver, which recognises that many do not currently arrive at decumulation as informed decision makers.

	Objectives	Framework ingredients
a	Provide more support to savers who do not engage with their options – utilising the lesson from Automatic Enrolment and the Open Market Option – as well as supporting freedom and choice for those who do	**Utilising a 'path of least resistance'** approach to guide savers to products which meet minimum standards which seek to mitigate key economic, decision and information asymmetry risks savers face by introducing a: • **Statutory obligation** for schemes and providers to support savers in their at retirement decisions – including • **Saver communications and engagement journey** – and specific minimum standards in regulations, along with guidance for schemes • **Signposting to a 'preferred' decumulation option** identified by trustee/provider either in scheme or elsewhere - and specific minimum product standards Savers are required to opt in to this preferred option • **Backstop of default investment strategy** for those who do not engage/respond to the preferred solution **Messaging in communications to include flagging additional options**, other guidance, and advice options at appropriate points in the customer journey
b	To facilitate and influence future product development with a view to managing the risks for savers as DC pots grow and dependency on DC derived incomes increases;	**Statutory obligation** to include signposting to build momentum on the demand side **Minimum standards for products** - to help shape product development which: • reflect key elements of saver risk - access to cash/flexibility, sustainable income, secure income in later life • are principles based - to enable and encourage innovation • can evolve over time as pot sizes grow and dependency on DC incomes increases **Guidance** could cover more detailed product design elements or options for trustees to consider **Best practice product standards** – potential kite-marking
c	To utilise the benefits of scale and mechanisms such as the trust-based fiduciary duty and IGCs responsibilities;	**Statutory obligations and requirements** – to enable and require trust based schemes to provide support, unlocking fiduciary duties and, where appropriate seeking to replicate this across the market via IGCs and providers **Signposting** to a preferred solution outside of the schemes - enabling smaller schemes to utilise relatively new developments such as Master Trusts as well as providers **Product minimum standards**
d	To support similar saver experiences across the market, while enabling innovation to flourish	**Statutory obligations and minimum standards** seek to create similar experiences for savers irrespective of their scheme or provider **Seeking to apply in both trust based and contract based regimes** – starting with trust-based where regulatory requirements are less developed **Saver communications and engagement journey** – reflecting key elements, where appropriate, of the FCA pathways **Saver communications and engagement journey -** can include and deploy various technologies and support emerging innovations
e	To mitigate or help manage some of the savers risks	**Utilising path of least resistance approach** **Signposting or provision of decumulation preferred solution & product minimum standards** which reflect key elements of saver risk - access to cash/flexibilities and sustainable income, secure income in later life **Default investment strategy** for those who do not engage **Saver communications and engagement journey** to include prompts to seek guidance and advice

f	To mitigate some of the key risks schemes are facing – including litigation, financial and operational risks	**Statutory obligation & minimum standards** – together help mitigate litigation risk **Signposting to product outside of the scheme** to alleviate cost and other risks associated with providing the product from within the scheme **Minimum standards** on product, governance and saver communication and engagement journey help support /ensure some elements of the due diligence & governance processes in providing or signposting to other providers To help mitigate risk of costs/regulatory burdens of these recommendations for small schemes • Not applying requirements to the smallest schemes • **Guidance** to ensure that templates and check lists are available to reduce costs for smaller schemes

SAVER COMMUNICATION AND ENGAGEMENT JOURNEY

Summary: Saver communication and engagement journey

Our new framework delivers a ***saver communication and engagement journey via minimum standards*** *using nudge theory.*

It deploys a 'path of least resistance' by signposting the saver to a preferred solution, in the scheme or outside of it – seeking to remove the risk of the poorest outcomes. The process is a 'consent/opt in' model. Schemes will also issue key messages and support regarding guidance and advice that is available from other sources. The process incorporates a default into an investment strategy (an opt out model) for those who do not engage at all.

The 'signposting' also benefits the saver by utilising the knowledge, expertise and purchasing power of the industry – including schemes and trustees - on behalf of the saver. By enabling signposting to products outside of the scheme we can help ensure the new requirements don't exert unreasonable costs or regulatory burdens on schemes who may not wish to provide a product in-house.

70. The evidence and wider research that we have explored, as set out in the call for evidence and summarised in Section 1, demonstrates to us that savers need more support with the complex decisions that they are faced with at decumulation.

71. By providing a path of least resistance our final recommendations for a new framewok seek to ensure that those who do not undertake extensive research or take regulated advice are protected from worst outcomes.

72. We consider that our framework is key to mitigating the risk of litigation that schemes feel they face in navigating how to support their members. It is also key in managing the risk that signposting could result in schemes falling into advice or financial promotion activities. We believe carefully designed signposting to a third party or in-house product/solution should not constitute advice or financial promotion. The framework will make clear what is permissible - including key messages that are important and that scheme members understand throughout their consumer journey.

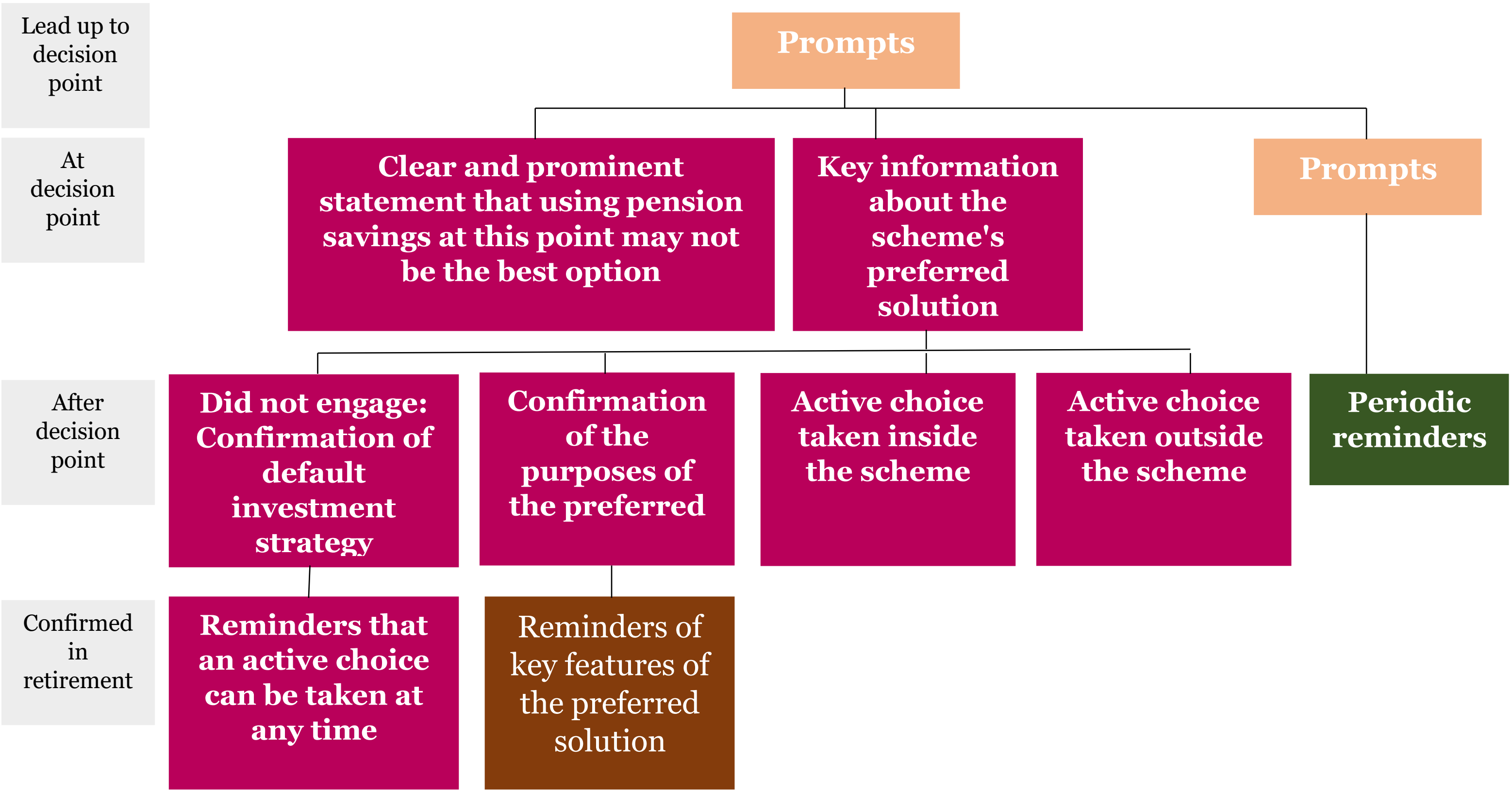
73. The communications under this framework include flagging sources of guidance and advice which savers can take – the support from schemes is not intended to replace those avenues nor is it requiring schemes to step into an advice function. The approach

is one which is consistent with and complementary to guidance and advice from other sources.

74. Key elements of the communications will also include information and prompts not only to consider guidance and advice, to think about wider financial circumstances, but also about consolidation of small pots. In time the pensions Dashboard will be key to helping savers make better sense of their options too.

75. The development of robo-advice and guidance is likely to help support this framework, and we welcome these developments along with wider fintech solutions which can assist schemes and trustees in engaging their members on decumulation matters, as well as with wider engagement.

76. Providing a framework around decumulation engagement and communications also achieves greater consistency for savers' experience – many savers may be saving across a number of pension schemes in different parts of the market.



PRODUCTS

Summary: product minimum standards

*The saver communication and engagement journey taken together with the **product minimum standards** respond to what we have been able to assess of current saver behaviour.*

The evidence suggests that people are not well equipped or effectively trading off the numerous and complex risks they face. The product standards therefore seek to help with these trade-offs by outlining the key considerations about product features for the scheme to use in establishing a preferred solution.

These pointers to consider reflect the phases of retirement and changing needs of the saver, helping to also manage the economic risks the saver faces – and seeking to secure a sustainable income in retirement.

The provision of product standards will also help guide innovation in a direction that addresses key economic and decision risks for savers.

77. The product standards elements of our final recommendation for a new DC Decumulation framework seek to steer schemes and savers in a direction that addresses some of the risks that savers face, and deal with the changing needs over the phases of retirement.

78. The standards focus on key aspects of financial risk for the saver, and seek that the trustees consider these when selecting a preferred product – either to provide in-house or to signpost to in another scheme. For example, a relatively constant income during retirement, managing longevity risk and market risks; some flexibility for capital withdrawals for a defined period in retirement; and some protection against dementia risk. This reflects the changing phases during retirement. We will also explore additional guidance to support the standards, including in respect of withdrawal rates.

79. We do not set out specific named products in the standards, as we expect these to grow and evolve over time. The forecast growth in the size of DC pots and numbers of DC savers coming to retirement with only DC savings indicates there is potential for these products to develop over time.

80. But more is needed to influence the shape of those products. Our framework is intended to support innovative solutions coming to market, and also to help shape them - to encourage products that tackle these risks for savers. It will also help support the demand side pressure - schemes seeking these types of solutions will exert more pressure than a mass market of individuals - especially given the information asymmetry and complexity for the consumer in articulating the demand. A regulatory structure will give some support to the supply side too – in terms of consistency of demand to respond to.

81. The product standards will also support trustees seeking to signpost to other schemes – they will know those schemes are also working to these regulatory standards.

82. In summary - we think this new framework and the product standards have a key part to play in mitigating risks for savers, supporting that demand side and in shaping ongoing innovation.

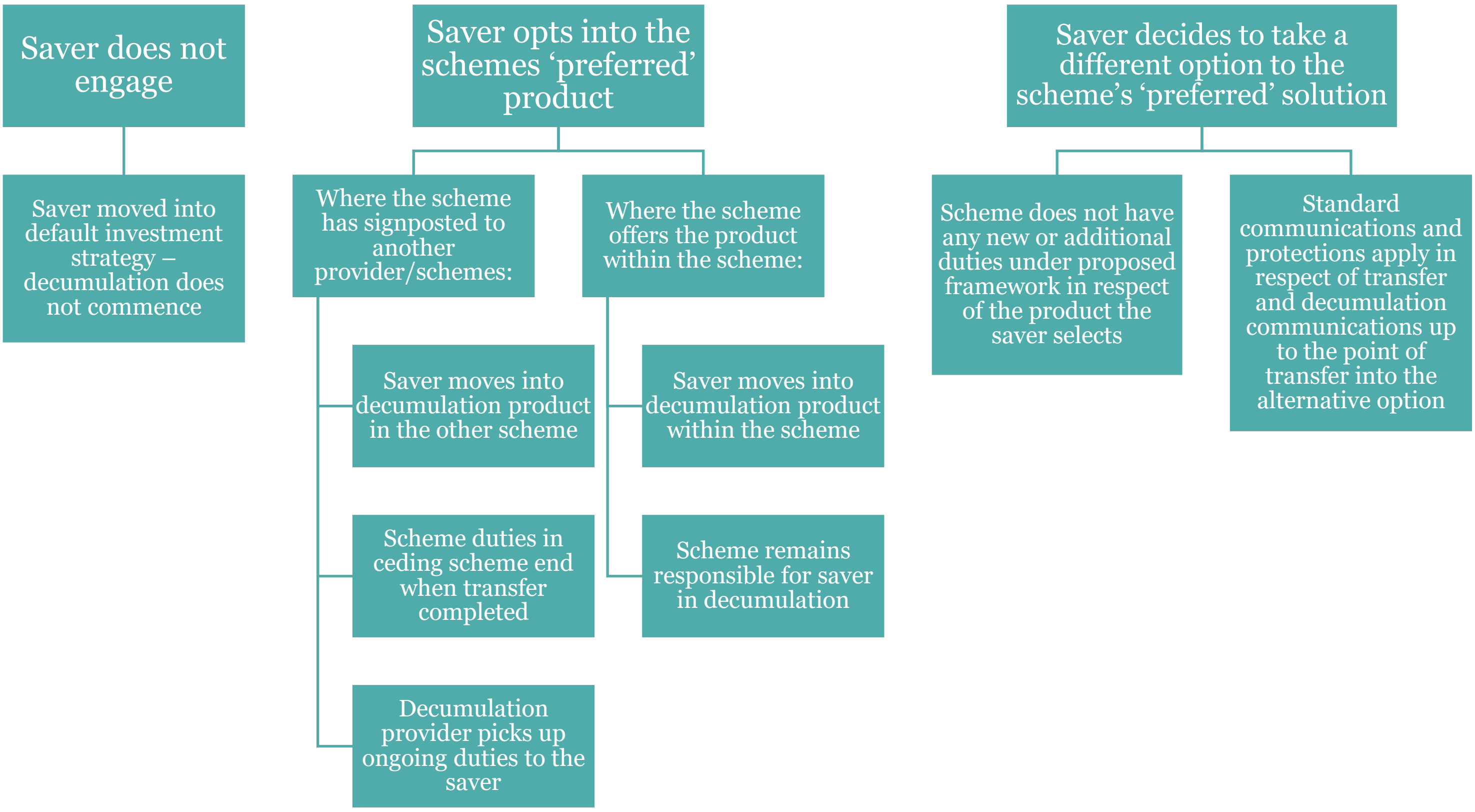
GOVERNANCE

Summary: governance minimum standards

*The **governance minimum standards** support schemes in putting this framework into delivery. Along with the product and saver commnications and engagement standards, they also provide assurance to schemes and trustees who might be seeking to signpost their savers to another scheme or provide for their decumulation options rather than provide a decumulation product in-house. This is because where the framework appplies, the product is subject to these standards they are being asked to consider when signposting.*

83. The governance standards cover processes schemes use to make decisions about the preferred product, signposting, and communicating with savers.

84. They are intended to assist trustees and schemes in providing clarity about requirements in relation to selecting products. The governance standards also provide assurance that where a scheme signposts to other products subject to this framework that the standards will continue to be met, once the saver has left their scheme to join another product.


Saver does not engage
Saver moved into default investment strategy – decumulation does not commence
Saver opts into the schemes ‘preferred’ product
Where the scheme has signposted to another provider/schemes:
Saver moves into decumulation product in the other scheme
Scheme duties in ceding scheme end when transfer completed
Decumulation provider picks up ongoing duties to the saver
Where the scheme offers the product within the scheme:
Saver moves into decumulation product within the scheme
Scheme remains responsible for saver in decumulation
Saver decides to take a different option to the scheme’s ‘preferred’ solution
Scheme does not have any new or additional duties under proposed framework in respect of the product the saver selects
Standard communications and protections apply in respect of transfer and decumulation communications up to the point of transfer into the alternative option

	MEMBER ENGAGEMENT	PRODUCTS/SOLUTIONS	GOVERNANCE
PURPOSE	▸ Minimum requirements in this area would cover the information schemes should provide savers with and seek to receive from them.	▸ Minimum requirements in this area would cover the construction of the default solution and the features of the products selected to fulfil it.	▸ Minimum requirements in this area would cover the processes schemes use to make decisions about their default decumulation proposition and approach to communicating with savers.
REQUIREMENTS	i. Trustees would seek to obtain and check information on the generality of members that would inform the development and ongoing maintenance of a relevant decumulation strategy for the generality of members. This should be with specific intent to identify those who might benefit from the default retirement investment strategy. ii. Trustees would provide savers key items of information starting early in and continuously throughout the appropriate stages of the consumer journey – including the run up to the wake up pack and beyond – using industry standard accessible language covering matters such as key options' savers should consider, key information about what the scheme is offering, and examples of how to prepare for decumulation (e.g. setting a target retirement date, consolidating pots, appreciating the implications of any lump sum or drawdown components of the default, if applicable, etc.). iii. At appropriate stages in the consumer journey, trustees should continue to signpost to and/or encourage savers to seek guidance and advice services and remind savers that open market alternative options may be available. iv. Trustees must design a mechanism that enables savers to elect to take an active choice outside of the path of least resistance. Trustees should provide information and options to savers carefully and clearly, with the objective that they understand the implications of not taking an active choice.	i. Trustees would provide a default investment strategy that operates in the interest of members. ii. Trustees would offer or signpost to a preferred suite of products or solutions that can that can provide, fulfilling the retirement needs of the scheme's membership, the opportunity to achieve: ▸ A relatively constant income in retirement, which can be achieved via means the scheme feels most appropriate to the membership (e.g. drawdown, UFPLS, etc.). ▸ Protection against longevity and decision-risk (including the risks inherent in cognitive decline). ▸ Some flexibility for capital withdrawals for a defined period in retirement. iii. Trustees would carefully consider the investment mix of the preferred product suite so that: ▸ Members are not unduly exposed to market risks (in normal market conditions) that are likely to have a material impact on their retirement income (i.e. expose them to significant market volatility). ▸ Members can remain appropriately invested over a long time horizon (i.e. 20 to 30 years). ▸ Members are not unduly exposed to inflation risk (e.g. this will likely entail some limit on the cash or cash equivalent allocation). ▸ Members' accumulated savings are not being eroded by disproportionate investment costs and charges. iv. Trustees would, in their product/solution selection, limit the need for people to take complex unadvised decisions in later life.	i. Trustees must follow appropriate processes for initial design of the decumulation proposition, as well as those related to ongoing review of the proposition such as by designing regular (at minimum annual) reporting on the decumulation solution and the decisions members are making. A specific, wider review of the overall solution should be undertaken at least once every three years.Trustees should consider the governance and administration implications of choices to provide adequate saver protection. ii. Trustees must implement processes concerning the investment approach adopted. These would include assessment of the appropriateness of any component products and the overall solution, against the objective of the strategy, and the suitability of this strategy for target members over time. iii. Trustees would implement processes for reviewing costs and charges, in relation to the risk and performance of the investment strategy, to assure themselves that the designated approach continues to operate in the best interest of members. iv. Trustees must undertake adequate review of third parties on which their solution is dependent, where applicable, and achieve comfort that any providers engaging with their membership are sufficiently expert, resilient, compliant, and that their charges are proportionate to the value they offer. v. Trustees must be satisfied that members' assets will remain secure with any third party to which they are signposted.

STATUTORY OBLIGATION

Summary: Statutory obligation

*By creating a statutory **requirement on schemes**, we can generate a stronger demand side, grow and utilise the information and expertise within the industry to the good of the saver, and also help mitigate litigation risks and some costs for schemes. It will also support a more consistent saver experience across the numerous schemes they may be part of.*

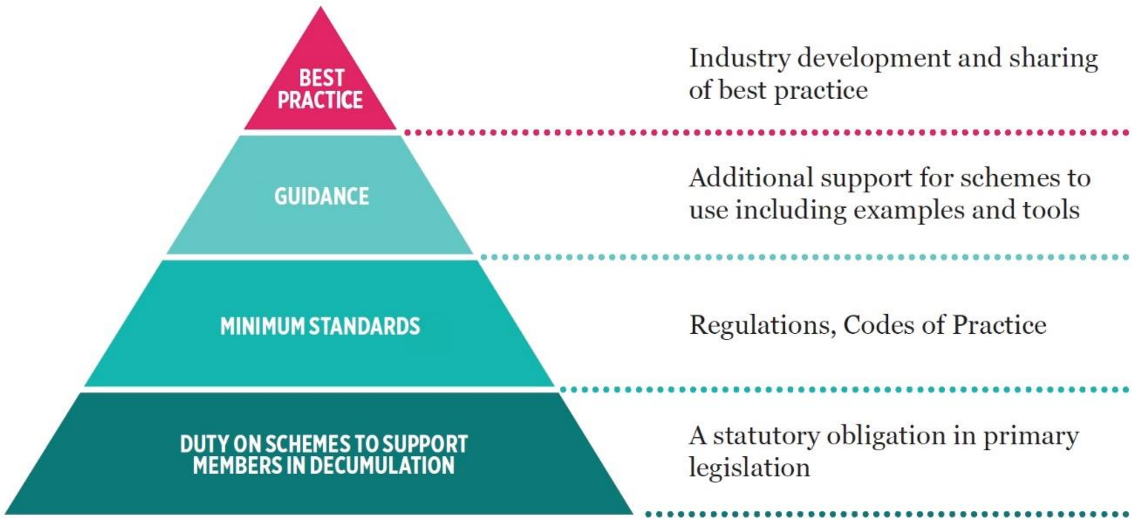
The minimum standards will provide transparency of legal obligation, and guidance will help support schemes to deliver. By keeping the standards at the appropriate level, the cost burden can also be managed, but innovaton can also flourish. In response to what we have heard in the Call for Evidence period we will, in addition, remove the requirements from the smallest schemes, and add additional guidance and templates to help help schemes keep costs down.

85. The statutory obligation along with the minimum standards within our proposals provide protection regarding litigation risk above that which is currently afforded to trustees signposting decumulation solutions outside of the scheme.

86. We have added some mitigations to complement those already embedded in our proposals, to go further to support small schemes manage these costs further.

MITIGATIONS FOR SMALL SCHEMES

- The provision to signpost to products outside of the scheme means no-one is being asked to develop and directly provide a decumulation product for their savers if they do not wish to do so.
- The minimum product standards will provide an element of assurance to trustees seeking to identify products to signpost to – anyone working under this framework will need to meet the minimum standards. So trustees in scheme A looking to signpost to a scheme B, can be reassured that any scheme or provider who works under the same requirements and offers a decumulation product, will be meeting the same obligations.
- The framework also provides for clear guidance for trustees on all three elements of the solution to support their delivery of the regulatory requirements.
- We have also added a Kitemarking proposal - for the best in class schemes in relation to their decumulation offerings – the PLSA will explore the potential for providing "best practice standards' – providing a further assurance to those seeking to sign post.
- We anticipate the clarity the framework provides, and the effect of a statutory obligation, will mean that services used by schemes will start to incorporate the solution.
- We also have also incorporated a limited carve out for small schemes from the obligation- details of this will be developed in the coming weeks.



GUIDANCE AND BEST PRACTICE

Summary: guidance and best practice

Some schemes already have impressive offerings for their savers – and we want to keep that drive for continuous improvement. Sharing this via best practice will help keep momentum on continuous improvement, and following calls for kite marking PLSA will explore the potential for providing "best practice standards".

87. The guidance will be provided alongside any statutory objective and/or regulation – and will help support schemes and trustees by providing resources to help schemes deliver the new minimum standards. We would expect Government and regulators to play a key part in providing guidance. The PLSA will continue to explore with stakeholders what type of support the PLSA could helpfully provide – taking into account the Government response to the final recommendations.

88. The minimum standards are designed as a baseline and not as a target of best of in class. To recognise providers and schemes that already deliver best in class solutions, encourage others to do so, and to help support schemes in signposting to outside of their scheme, PLSA will explore the potential for providing "best practice standards'.

WHOLE OF MARKET SOLUTION

Summary: whole of market solution

We believe that to drive consistent experience across the landscape the requirements should apply across the market – utilising providers as well as IGCs where appropriate.

89. We believe the framework should apply across the market – because the principle aims to improve member outcomes are appropriate for the contract-based environment as well as for trust based schemes. This is also key to ensuring consistent experience for the saver who may have savings invested in different parts of the market.

90. To achieve this, the responsibilities for the statutory obligation and minimum standards need to be appropriately delineated between the employer, provider and IGCs to deliver a similar outcome as a requirement on trustees and trust-based schemes. This would include an oversight but not executive role for IGCs and, where IGCs do not provide this oversight function, other governance structures may be more appropriate.

CONCLUSION

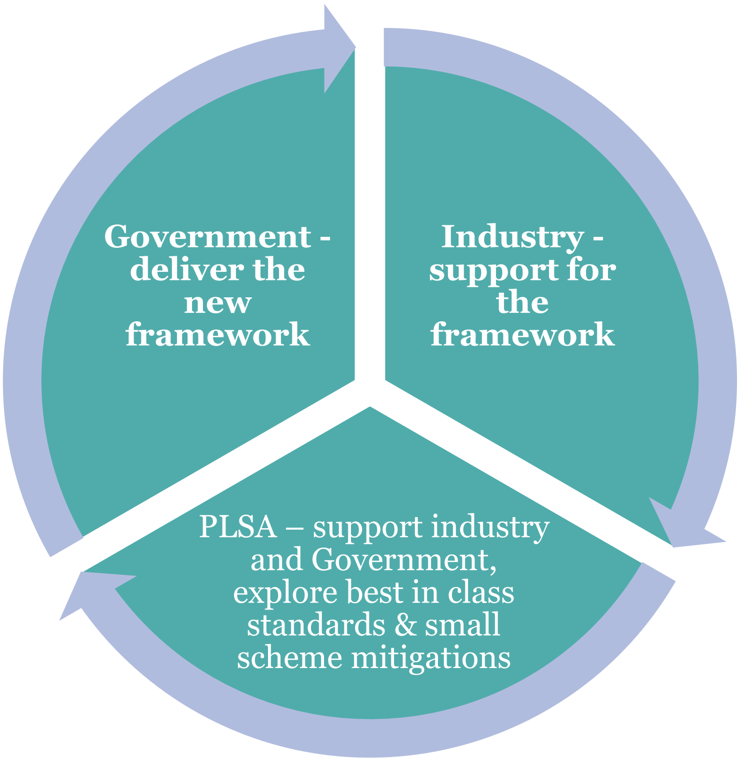
91. As described above, including refinements following our call for evidence period, our final recommendations for a new DC Decumulation framework supports savers with the risks they face – and seeks to do this in a way that addresses key risks faced by schemes. It enables future developments, and seeks to frame that in a way that places the saver at the heart of pension policy and delivery.

92. In conclusion – the PLSA:

- calls on the Government and Regulators to deliver the new framework in consultation with industry to enable them to ensure the freedoms meet the needs of savers;
- calls on the industry to embrace and support the framework; and,
- commits to further work with the industry and government and regulators – to develop and support detailed guidance, mitigations for small schemes, and explore the potential for best in class standards.

SECTION 4 - SUMMARY OF OUR NEXT STEPS

The Government and the pensions industry should adopt this new regulatory framework for decumulation.



93. In conclusion – the PLSA

- calls on the Government and Regulators to deliver the new framework in consultation with industry to enable them to ensure the freedoms meet the needs of savers;
- calls on the industry to embrace and support the framework; and
- commits to further work with the industry and government and regulators.

94. To reinforce the pension industry's efforts to support savers we also further commit to the following specific actions:
    - explore the potential for best in class standards;
    - work with industry to consider detailed guidance on some elements of communication such as withdrawal rates and pot consolidation prompts;
    - call on government to consider the role of CDC in decumulation and, particularly, should not limit the potential of CDC through the Pensions Bill;
    - call on TPR/FCA to deliver further guidance to clarify the scope of regulated activities insofar as they might capture schemes' decumulation approaches;

- call on government to consider decumulation in the round, and ensure any conversations about decumulation charge caps take into account the breadth of the challenge schemes face;
- seek to hold a roundtable discussion with industry, government and regulators to set out the framework and discuss next steps.

ANNEX – CALL FOR EVIDENCE FINDINGS - FURTHER DETAIL

In addition to our working groups (see introduction pages) we

- received **25** written responses from different organisations or bodies
- ran **7** roundtables including approaching 50 individuals
- held related bilaterals with further stakeholders across the industry

on the proposals set out in the *Call for Evidence* document.

Written responses: Of the 25 written responses 15 provided specific responses to all the questions posed in the Call for Evidence and 6 providing extensive sources of evidence which provide coverage of many or all of the *Call for Evidence* questions.

Roundtables: The PLSA engaged with more than 47 individuals from across the pensions sector via 7 roundtables on the proposals set out in the document. Roundtable discussions have been wide ranging, with predominant focus on our proposals.

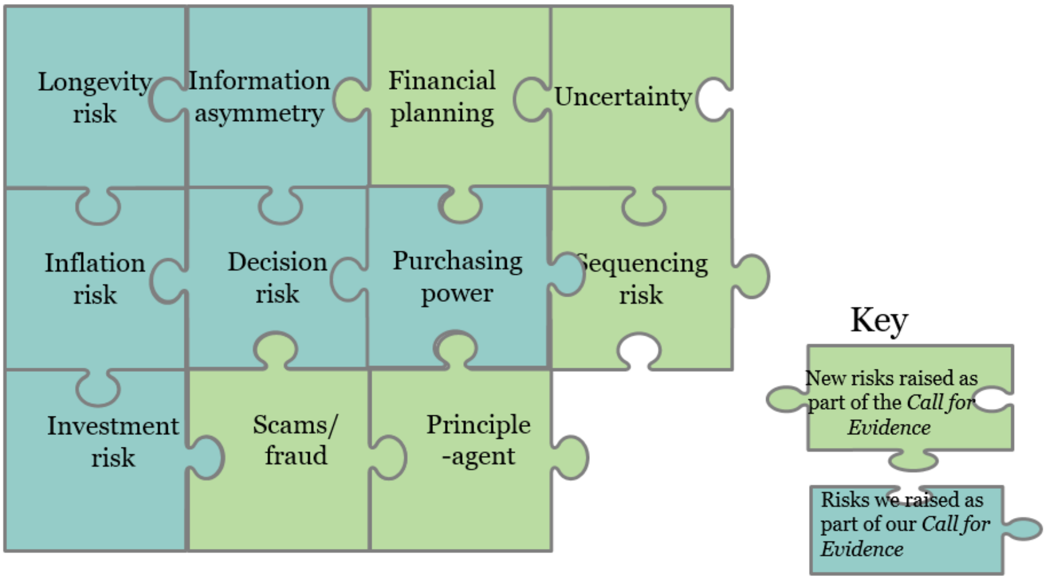
Headline stats

- More than 20% of roundtable attendees represented single employer trusts, not including those from professional trustee organisations
- Master trusts and multi-employer trusts were represented in a further 20% of roundtable attendees
- 60% of written responses covered all of the questions posed in the *Call for Evidence* and a further 25% provided extensive sources of evidence which provided coverage of many or all of the questions we posed
- Approaching 40% of written responses were from pension schemes
- A small number of academics and independent researchers engaged with us during the *Call for Evidence* period

CASE FOR CHANGE

RISKS TO SAVERS

95. The majority of roundtable and written responses to our call for evidence agreed with our analysis of the risks faced by savers, and some suggested additional risks, which we believe our solution can help mitigate. These included scams and fraud, taking limited advice, and principal agent risks.



- **Scams/Fraud:** Where savers are taking decisions about how to use their accumulated pension savings, there is clearly potential for scammers to exploit this decision point for their own gain. One respondent noted that

  > *"The risk of scams in this complex area of financial planning is very high. We have seen time and again with any area of financial decision-making that requires a significant stretch of individuals' level of knowledge and understanding that scammers will step in, spotting an opportunity."*

- **Financial Planning:** We had highlighted this risk as relating to the need for planning to take account of varying income needs over retirement – stakeholders commented that there are clear risks associated with limited or poor financial planning, particularly where savers do not see the value in taking financial advice, or only access retirement advice and don't consider other assets which could lead to poorer outcomes. Research also finds that the need for advice and guidance changes throughout the course of retirement - as people's cognitive abilities are impaired people often increasingly struggle to understand financial concepts (such as inflation or charges)[14].

- **Principal-Agent:** Where the interests of product providers/advisers and savers are not aligned, there is a risk that the conflicting priorities this engenders could result in product providers/advisers acting in ways that are contrary to the best interests of savers. The principal-agent problem has been a recurring source of concern in financial services more broadly, including in the pensions sector.

- **Sequencing:** Sequencing risk is a subset of investment risk. It is the risk that the timing of withdrawals from a pension will damage a saver's outcome. This is dependent on market circumstances and is clearly increasingly relevant, given that

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[14] https://www.pensionspolicyinstitute.org.uk/research/research-reports/2019/2019-10-22-supporting-later-life/ and see also, for example, Agarwal, Sumit and Driscoll, John C. and Gabaix, Xavier and Laibson, David I., The Age of Reason: Financial Decisions over the Life-Cycle with Implications for Regulation (October 19, 2009).

savers are now more likely than ever to remain invested during retirement (in a drawdown product). For example, withdrawals during a bear market are more costly than the same withdrawals in a bull market, given they crystallise investment losses rather than maximise investment gains.

SAVER BEHAVIOUR

96. In our call for evidence we asked for data regarding how savers in trust-based pensions are using the Pension Freedoms and what is driving their behaviour, particularly where this was materially different to how savers in other arrangements are accessing their pension savings.

97. Generally, stakeholders shared our view that savers in contract-based arrangements, where much of the current evidence is on saver behaviour, exhibited similar preferences to those in trust-based arrangements. This was despite many stakeholders pointing out that the characteristics of the average trust-based saver is likely to be quite different from the average contract-based saver; as trust-based savers are more likely to have been automatically enrolled.

98. Respondents also pointed to sources of research about multi-stage lives and the implications which include the need for more flexible financial planning[15]. For example, double the amount of 70-74 year olds are still in employment compared with 30 years ago[16]. Respondents noted that there is a danger that, without education, members take their benefits to boost their income too early even when they continue to work and that in later life retirees struggle to understand and adjust to more modest retirement incomes. Research[17] also found that variations in healthy life expectancy mean that some individuals are less likely to experience the benefits of the Independent Phase of retirement than others.

99. Respondents pointed to research that provide additional explanations about why savers often find both fully withdrawing and holding money in cash appealing. This is often, at least in part, because they believe they cannot have control over their pension money or that it is not safe. People often state they want to have 'control' of their money even where they have not made decisions relating to investments in accumulation which suggests that this is a 'general feeling about the loss of control than a real desire to manage it themselves'[18].

100. We also asked for evidence on the impact of COVID-19. Evidence provided by respondents suggest that a small proportion of people considered reducing their

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[15] https://www.pensionspolicyinstitute.org.uk/research/research-reports/2018/2018-11-20-funding-the-future-life-the-implications-of-a-longer-life/
[16] https://www.lgim.com/landg-assets/lgim/_old-document-library/solutions/four-pots-for-your-retirement.pdf
[17] https://www.pensionspolicyinstitute.org.uk/research/research-reports/2019/2019-07-17-living-through-later-life/
[18] https://www.lgim.com/landg-assets/lgim/_old-document-library/solutions/four-pots-for-your-retirement.pdf

withdrawal amounts on account of coronavirus-induced decreases in pension values, suggesting many could be at risk of running out of money early in their retirement. A number of respondents have seen little or no impact and several noted a decline in activity. Several respondents were cautious about current data on the impact of Covid-19 on pension access decisions, as they do not believe the full impact of the pandemic has been felt. This is largely because of the Government's initiatives to support employers and employees, such as the Coronavirus Job Retention Scheme. Research over the longer term suggests that negative macroeconomic events can have a long-term effect on individuals' attitude to risk[19].

101. HMRC data[20] for scheme withdrawals show that, by value, £2.3 billion was withdrawn flexibly from DC pensions in Q2 2020, which is a 17% decline on the same quarter last year. There is, typically, a rise in the second quarter any year relative to the first quarter, however in 2020 the number of individuals making withdrawals was lower in the second quarter than the first. HMRC commented that 'this change in behaviour may be attributable to the impact of the COVID-19 pandemic'. This does not, therefore, support the speculation that individuals would dip into their retirement pots either to replace their own income or to help family members out as a result of loss of earnings during the pandemic.

102. The ABI has reported[21] an even more dramatic fall in withdrawals from its members' DC schemes: as of April 2020 individuals:

- accessing flexible drawdown fell 42%,
- taking a tax-free lump sum fell 53%,
- withdrawing their whole pot was down 30.2%; and,
- purchasing an annuity was down 56.3%.

STATUTORY OBLIGATION

103. We asked respondents whether the key elements we proposed were the only areas a statutory obligation should refer to and whether other areas should be covered. Several stakeholders indicated the proposed statutory obligation would be a step forward. Others felt without a change in requirements the constraints or barriers to delivering good retirement outcomes for their members would remain significant.

> *"Our priority is that law and regulation allow streamlined decumulation pathways, along the lines of the bulk of the call for evidence paper. We feel that these should be appropriately regulated."*

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[19] See, for example: Malmendier, U. and Nagel, S. (2009) *Depression babies: do macroeconomic experiences affect risk-taking* https://www.nber.org/papers/w14813 and PR Newswire (2000) *Kemper Funds Client Life Stage Solutions Holds That The Most Effective Investing Strategies Reflect Investor Attitudes and Past Life Experience* http://libezproxy.open.ac.uk/login?url=https://search.proquest.com/docview/453466831?accountid=14697

[20] HM Revenue & Customs (2020) *Flexible payments from pensions. July 2020 official statistics* https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/904548/Pension_Flexibility_Statistics_July_2020.pdf.

[21] Association of British Insurers (2020) *Pension savers press pause in lockdown*, News release https://www.abi.org.uk/news/news-articles/2020/07/pensions-savers-press-pause-in-lockdown.

"Make it clear to pension firms that they could not just sit back and do nothing for and say nothing to their non-advised drawdown customers. The FCA had to make the risks of inaction greater than the risks of action. Pension providers must be required to provide some help and support to these customers."

104. Many stakeholders were reassured that the statutory obligation and minimum standards within our proposals provide protection regarding litigation risk above that which is currently afforded to trustees signposting decumulation solutions outside of the scheme. Although a few felt strongly that the PLSA should be calling for a full safe harbour, potentially linked to Master Trust authorisation status.

105. A minority of stakeholders questioned whether it is proportionate to introduce a new statutory obligation on trustees, particularly for small schemes. Others felt it was proportionate.

"We believe the solution set out by the PLSA is proportionate."

106. Taking into account the balance of views, and the value and consistency of support for savers, and additional protection for schemes, we have retained the statutory obligation in the final recommendations – but added some mitigations to complement those already embedded in our proposals, to go further to support small schemes mitigate these costs further.

SAVER ENGAGEMENT AND COMMUNICATIONS

107. Generally, stakeholders were enthused by our proposals to improve member engagement and communication, and emphasised the importance of doing this starting early, building over time and continuing after retirement. Many respondents felt this is one of the key aspects of the framework.

NUDGE

108. The guided pathway approach, using a path of least resistance was welcomed by most stakeholders - as it was in the Hitting the Target proposals.

"The mechanism should be to nudge savers into choosing the suggested product, at the appropriate stage of their journey."

109. Several stakeholders agreed that our proposals included additional and helpful guidance to the saver to help them make better decisions. Specific prompts to consider pot consolidation were supported by stakeholders. A very small number of stakeholders felt we could go further with our proposals, particularly calling for mandatory advice, specific engagement tools or information to be provided on, for example, the tax implications of choices, longevity risk and withdrawal rates.

SIGNPOSTING – ADVICE AND MARKETING RISK

110. Some respondents were concerned that the signposting or offering a product in-house would constitute advice or financial promotion – but others were not at all concerned that signposting represents a risk to schemes. Some suggested clear guidance for schemes would help them deliver our proposed framework with confidence.

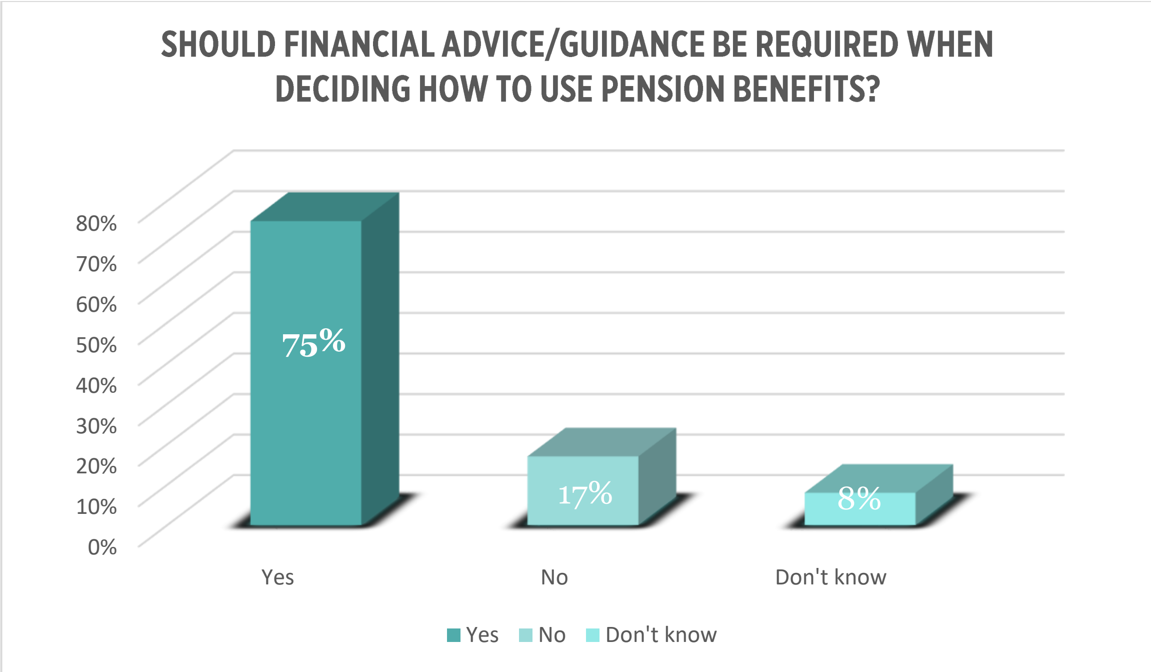
111. We consider that our proposals for a regulatory framework is key to mitigation of this risk. We believe that carefully designed signposting to a third party or in-house products should not constitute advice or financial promotion. But further clarification is required to enable trustees and schemes and providers to act – our recommendations seek to create a step change on this issue.

112. We will continue to press for additional clarification from FCA, as part of this project and also our wider Financial Wellbeing work that includes exploring provision of guidance by schemes at key points in the savings life cycle.

WIDER GUIDANCE AND ADVICE

113. Some respondents raised the Financial Guidance & Claims Act 2018 provisions to require DC schemes and providers to ensure savers have first used a regulated adviser or impartial pensions guidance (or opted out of impartial guidance) prior to accessing their pension benefits. Although these provisions have yet to be implemented, the FCA is currently considering how to apply this new legislative requirement in practice.

114. Research by Just Group has found that the implementation of 'default guidance' processes have widespread support amongst savers (see chart below).



115. Stakeholders also see default guidance proposals as a means of raising stubbornly low engagement with Pension Wise services, helping a higher volume of people to understand their options under the Pension Freedoms, and protecting savers from scams related to retirement decisions.

116. Stakeholders also drew attention to the importance of other ongoing initiatives that could facilitate the development of a more inclusive and widely used advice market. This included the emergence of robo-advice and other online retirement planning tools[22], which may reduce the cost and increase the ease with which savers can take advice. However, different initiatives were noted to be likely to be impactful for different groups of savers. For example, younger people are more likely to engage with digital solutions, defaults work well for the non-engaged and regulation and consumer protection efforts are likely to benefit those that 'consume' financial services and, so, the more engaged[23].

117. Stakeholders also flagged innovative retirement advice and guidance tools; these include online and app-based solutions that guide and advise savers through retirement decisions. Examples of these were provided by respondents, some hybrid-robo solutions which offer the opportunity to receive full advice, others interactive guidance and some deliver specific tools on aspects of the risks savers face in retirement such as budgeting or withdrawal rates.

118. The development of pensions Dashboards also has much to offer - stakeholders indicated that it could reduce the cost of financial advice by reducing the length and difficulty of the 'discovery phase' (in which advisers attempt to find all information relevant to an individual's financial position).

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[22] For example, see Age UK (2019) discussion paper *Fixing the Freedoms: Helping smaller savers get the most out of the pension reforms*

[23] https://www.pensionspolicyinstitute.org.uk/research/research-reports/2017/2017-07-19-consumer-engagement-the-role-of-policy-through-the-lifecourse/

119. We view guidance and advice as a key part of the journey – our framework includes the provision of clear communication about advice and guidance that is available – and it also has the flexibility to incorporate further developments in this space.

STRUCTURE AND CONTENT

120. Stakeholders also raised some general points about the proposals on saver engagement and communications. They agreed with the potential issues with providing guidance to members that we had noted - in particular where this communication and guidance could risk being construed as personal recommendations, and felt our proposals were appropriate to minimise this risk.

121. Several discussions and responses raised potential for perverse outcomes from increased communications.

> *"Any recommended changes to existing member communications (or their frequency) should be given serious consideration as the feedback that is regularly received from members is that retirement information/packs are too long. Simply adding more into these packs is unlikely to have the desired outcome in isolation."*

Research also suggests that timing of engagement is important; engagement is likely to peak when work has just stopped and when earning stops[24], though this peak of interest may not be well timed for savers to take the best decisions.

122. These views were particularly centred on what the regulatory minimum standard would equate to, and called for the recommendations to represent a true minimum. Stakeholders encouraged us to recognise the full spectrum of options or the best in class approaches to communication through other means (such as Quality Marks). We believe our framework achieves this - through the layering of the minimum standards, and guidance and we have now also added to the final recommendation that PLSA will explore the potential for providing "best practice standards'.

123. One stakeholder suggested savers would be confused by communications from multiple schemes, and so proposed that the requirements should apply only in respect of active members in a scheme. We think only communicating to active members would risk leaving too many members without this key support. We think by having a framework for those communications it will be possible to reduce potential confusion and overload – the framework itself could also be communicated more generally to the saver population including such as via more general websites and public communication exercises.

124. Stakeholders also called for consistency across different regulatory regimes to avoid savers becoming confused. For example, one stakeholder urged us to explain how the risks for consumers with multiple pension pots across different regimes and different schemes, particularly where the facility to compare products from different providers may differ. Our framework and the detailed minimum standards seeks to ensure that there is consistency in the journey across the regimes where this is helpful for members.

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[24] https://www.lgim.com/landg-assets/lgim/_old-document-library/solutions/four-pots-for-your-retirement.pdf

125. We also agree with stakeholders that previous and future industry standards on language, terminology and accessible communication style should be expressly incorporated into our proposals, and coordinated across providers of impartial guidance alongside that delivered by schemes[25].

PRODUCTS

126. The vast majority of stakeholders were supportive of the overall approach we proposed – as a way of mitigating risk for members, supporting trustees in identifying preferred solutions, and in helping shape the future market.

127. Some respondents therefore expressed the view that desirable innovation would be about delivering ways for savers to more easily blend and hybridise products to suit their needs. Stakeholders noted that, without support from their scheme and Pension Wise guidance, savers would be faced with complex decisions regarding which decumulation option (or options) is right for them. For example, survey data provided to us shows that of those who tried to access their pension, more than a quarter didn't go through with it because they were confused about the options, but also that where people had been provided with clear information from their provider they were more likely to state they had a plan about how to make a choice in the future[26].

128. Some respondents outlined potential products that might facilitate better or more sustainable outcomes for savers as they enter and progress through retirement[27]. For example, Collective Defined Contribution schemes, deferred annuities, guaranteed drawdown, and individual mortality underwriting. Some of these product options are currently available in the UK market, others are either conceptual or not yet available in the UK.

  a. **Collective Defined Contribution:** Collective defined contribution (CDC) pension schemes allow savers to pool their money into a single fund which pays annual pension income. Pension increases vary depending on the funding level and modelling suggests higher member pensions are expected than under traditional DC annuities. The Government is legislating to facilitate the operation of end-to-end (i.e. accumulation and decumulation) CDC schemes. Stakeholders saw potential value in decumulation-only CDC arrangements, which will not, initially, be permitted under the Government's legislative regime.
  b. **Deferred Annuities:** A deferred annuity is an insurance contract designed for long-term savings. Unlike an immediate annuity, which starts annual or monthly payments almost immediately, beneficiaries can delay payments from a deferred annuity indefinitely. These have been slow to appear in the UK market.
  c. **Guaranteed Drawdown:** Guaranteed drawdown products offer a middle ground between annuities and traditional drawdown. They provide the benefits of pension drawdown, leaving a client invested in the market, and an annuity, which provides a

[25] For example, when savers do engage they are likely to have varying numeracy levels and therefore potentially varied abilities to understand and engage with decision-making or to understand the implications of different options. Evidence suggests that clear and concise communication is vital if engagement is to be prompted and then sustained. https://www.pensionspolicyinstitute.org.uk/research/research-reports/2014/27-11-2014-transitions-to-retirement-how-complex-are-the-decisions-that-pension-savers-need-to-make-at-retirement/
[26] https://www.pensionbee.com/resources/drawdown-doldrums-report-2020.pdf
[27] For example, see David Blake (2016) *Independent Review of Retirement Income: Report*

guaranteed level of income until death. Depending on their structure, these products can offer inflation protection and some access to capital withdrawals. Several providers entered this market, but recently exited due to a lack of demand.

d. **Individual mortality underwriting**: Products created using lifestyle and health data combined with investment solutions to create bespoke drawdown solutions. Enhanced annuity providers have this expertise and are starting to sell these to the retail market. With investments chosen to match the expected shape of retirement with a more accurate assessment of the length of time over which that income would be needed there might be scope for the solution to be offered into the Master Trust market.

129. Innovative decumulation solutions could involve multiple products and, indeed, there have been some efforts to develop hybrid products. These are products containing multiple features that help savers to balance different needs. For example:

    e. One provider has developed, but not launched, a deferred annuity drawdown product that combines access to drawdown with a deferred annuity.
    f. Nest Guided Retirement Fund was designed to support members wanting stable and sustainable withdrawals throughout retirement while keeping pots invested via a diversified portfolio. This is currently only available through a regular UFPLS solution. The solution also offers support in providing for later life income via an annuity should members prefer a full guarantee then.

130. To clarify – our framework asks Trustees to consider various aspects of the product when they make their decisions about a preferred solution (in scheme or in another scheme). These aspects of the product could be met in a number of ways – and we don't prescribe specific products.

131. Our recommendations support innovative solutions coming to market. We expect the potential for products that tackle these needs to grow over time, as the size of DC pots grow and the demand side, supported by this framework, helps to shape the innovation.

DRAW DOWN RATES

132. Many stakeholders felt that more should be done to help savers develop an appropriate withdrawal strategy that mitigates the risks they face throughout their lives. It appears that, currently, schemes and providers feel that there are more risks associated with communicating to their members about this than not doing so; the regulatory risk, particularly the risk of being perceived as providing advice, was considered a significant deterrent by some. Stakeholders agreed that this can result in the risk of both exhausting their savings as well as underspending and suffering a poorer standard of living.

133. The latest data from contract-based plans shows that 42% of regular withdrawals were withdrawn at an annual rate of 8% or more of the pot value[28]. Respondents provided evidence that sustainable withdrawal rates are often widely misunderstood by savers.

134. Suggestions were made to improve the situation, including:

[28] https://www.fca.org.uk/data/retirement-income-market-data

- Offering sophisticated modelling tools that are emerging to help manage drawdown and would take account of investment performance, but some of these currently appear available only to advisers rather than directly to scheme members.
- Government Actuary's Department (GAD) rates – with an average and overall cap on how much money can be withdrawn each year.
- Better guidance and prompts delivered by schemes throughout the communications journey that is specifically exempted from being considered as regulated advice.

"…but there is no requirement to inform the member about what might be an appropriate sustainable level of income each month, or how long their pension fund may need to sustain that level of income. Members tend to underestimate their longevity based on rules of thumb or personal experiences of family members one or two generations older than themselves. At the same time, they may overestimate the sustainable level of investment growth and pay no attention to the impact of inflation on their income needs."

135. We believe trustees should provide members with indicative drawdown rates which communicate when they would anticipate a fund being extinguished. The PLSA will explore the potential for guidance and best practice on this matter.

INVESTMENT DEFAULTS

136. A small number of stakeholders expressed the view that existing requirements around investment defaults were, in effect, an existing duty on trustees to ensure that the design of any default in decumulation (whether the same or different to that offered in accumulation) is appropriate. They noted that because there is no forced retirement age, trustees are already required to provide defaults, take into account the full range of different retirement ages, perceived needs and expected behaviours, as well as ensuring an appropriate strategy for uncrystallised money for the majority of members.

137. Many stakeholders emphasised the importance of decumulation investment strategies' alignment with and consideration of accumulation investment strategies. Particularly, default accumulation and default decumulation strategies should be unified and interconnected where possible. The investment considerations, including the costs (realised and opportunity costs) of transitioning between accumulation and decumulation can be complex. Trustees should take account of the full saver journey and their default and preferred solution investment throughout all phases of saving and retirement, as well as for those that have taken an active choice where other options are available.

GOVERNANCE

138. Respondents generally agreed with the governance requirements set out in our proposal. Stakeholders emphasised the importance that governance procedures assess that products are fit for purpose and, where applicable, offer good performance and value for money. Also, that the processes should focus on the review of products and solutions that fulfil the generality of members, and should acknowledge the limitations of the ability of trustees when overseeing the products of a third party.

"The quality and effectiveness of the associated governance processes should be key. If trustees demonstrate that they undertook this to the best of their abilities, they should not be at risk of recourse or compensation that only the benefit of hindsight would present."

139. Respondents proposed additional governance requirements:

- **Management information:** This should be in advance and on an ongoing basis to help form part of the wider review of the ongoing effectiveness of the complete retirement support framework they offer
- **Minimum consistent timeframes:** Review timeframes over which default solutions should be standardised and aligned with accumulation default strategies (i.e. performance and value for money every year, and a wider review of appropriateness at least once every three years)
- **Disclosure:** Governance surrounding decumulation products should be declared in, for example, the Chair's Statement and external audited reports.

140. Respondents agreed that trustees responsibility for minimising the need for savers to make complex decisions later in life should be implemented with care; particularly where a preferred solution has been signposted the original scheme trustees will have no contact with savers after any transfer out. The responsibility is tightly limited to offering a preferred solution based on the generality of membership, and attention should be given to make sure members understand who the responsible scheme/provider is.

GUIDANCE AND BEST IN CLASS

141. Stakeholders also raised the importance of improving the resources for and knowledge of trustees to help deliver the new minimum standards, and supported our intent that guidance also be provided alongside any statutory objective and/or regulation. Some respondents called specifically for PLSA guidance.

142. Some stakeholders urged the PLSA to find a way to view the standards as a baseline and not as a target of best of in class, and to encourage providers and schemes that already deliver best in class solutions. Our proposals are, indeed, designed in that way.

"The policy as developed should seek to avoid 'hard wiring' the framework to the extent the future developments in the market that are beneficial to members and provide good solutions for schemes may fall outside of the recognised 'good practice' and not be appropriately recognised"

"The PLSA has rightly referred to providers that already provide higher levels of support, and this should be encouraged"

143. Furthermore, an accreditation scheme was noted to have the potential to reduce the burden on smaller schemes when selecting a solution to signpost to.

144. PLSA will explore the potential for providing "best practice standards'.

WHOLE OF MARKET SOLUTION

145. Stakeholders agreed that the principle aims we had to improve member outcomes in the trust-based environment were also appropriate for the contract-based environment. Concerns were raised about whether placing additional responsibilities on IGCs was the appropriate way to achieve this, - reasons including scope function and reach of IGCs.

146. We agree that responsibilities for the minimum standards need to be appropriately delineated between the employer, provider and IGC to deliver a similar outcome as a requirement on trustees. This would include an oversight but not executive role for IGCs and, where IGCs do not provide this oversight function, other governance structures may be more appropriate.

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