Written evidence from Aegon UK (APS0009)

Aegon is one of the largest providers of life insurance, pensions and asset management in the UK and work closely with advisers, employers and individuals. We're proud to provide long-term savings, investments, pension solutions and protection products to over 3.9million customers in the UK, helping them create the tomorrow they want.

Aegon welcomes the opportunity to respond to the Work and Pensions Select Committee's inquiry into "Protecting pension savers: five years on from the Pension Freedoms: Accessing pension savings."

The pension freedoms give people a choice about when and how to take their pension savings from age 55 (57 for some benefits from 2028) with access to Pension Wise guidance from age 50, which may be too late for some. The pension freedoms policy is still in its relative infancy and is untested for when people's retirement needs change as they approach later life. This is an area the Government needs to focus on.

Another pension policy, auto enrolment, has meant more people are saving in a pension, but due to the reliance on inertia, pensions awareness and engagement are far too low and too many people aren't financially prepared for retirement or equipped with the knowledge and understanding to make well-informed retirement decisions. Although auto-enrolment has been successful, paying pension contributions at the minimum level is unlikely to generate an adequate and sustainable retirement income for most people, limiting their choices.

Arguably these two polices are conflicted. The aim of auto enrolment is to use the power of inertia to give people access to a workplace pension so they are saving for a retirement income 'by default'. At the point of retirement, people need to make decisions about how and when they want to take their pension savings, which may include cashing in their pension savings rather than having a retirement income. The consequences of people's actions, for some, could prove to be detrimental to their later life finances.

Both these policies are still in their infancy, and many people currently accessing their pensions are in the fortunate position of having both defined benefit and defined contributions pensions, combining a guaranteed income with flexibility. In future, fewer people working in the private sector will have defined benefit pensions, and if they do, it's likely to be much smaller than for those retiring today. Future retirees will be reliant on their defined contribution savings to provide a sustainable retirement income.

Ultimately people need more support in the workplace to help them prepare for retirement. Knowledge and understanding need to start early and gradually build up as part of auto-enrolment. Pension providers are well-placed to provide this with the support of employers. We believe pension providers should be allowed to provide more personalised and therefore more helpful guidance.

The constant erosion and complication of the pension tax rules, since pension tax simplification in 2006, including the recent five-year freeze of the standard Lifetime Allowance and the draconian Money Purchase Annual Allowance, cause uncertainty and distrust. Pensions are long-term investments, which people might use to save for 40 plus years, then use to provide an income for another 30 plus years. People need greater certainty to be able to plan for and in retirement.

Do people have access to a range of pension options to meet their needs for later life and how might these needs change in future?

There is already a wide range of pension options and products available at retirement in the decumulation market, including flexi-access income drawdown, cash (uncrystallised funds pension lump sum) and a variety of different annuities. These give individuals a choice between flexibility and a guaranteed income and can be combined for different tranches of pension savings, at different times, to provide a blended retirement income.

However, there is a lack of consumer awareness that it's not a binary choice between having a flexi-access income drawdown product or a guaranteed income via an annuity. People may be unaware that they could move their pension savings into a flexi-access drawdown account, and at a later date, use some of their unused funds to buy an annuity providing a guaranteed income. This results in many people, without advisers, using only one product to provide a retirement income.

Ideally everyone should have a retirement plan. Ultimately people need more support in the workplace to help them build their plan so they can prepare for retirement. Knowledge and understanding needs to start to be built up as part of auto-enrolment from an early age.

The more people are able to save, the more retirement income choices become available to them. The current pension tax allowances restrict the amount people can save annually and over their lifetime without facing a tax charge. The Money Purchase Annual Allowance, which limits pension contributions to £4,000 a year once pension income has been flexibly accessed, can be extremely detrimental to an individual's retirement savings plan. Modern working patterns mean that many people will access their pension to increase their earned income while phasing into retirement. The pandemic has meant that many have had to access their pensions earlier than anticipated to provide an income for their families, without realising the impact on their future pension savings. Many of those impacted will be people with mid to lower incomes. Once triggered the money purchase annual allowance applies to all future contributions, making it challenging for people to rebuild their pension savings. Unfortunately, too many people are accessing their pensions without taking guidance or advice which can lead to poor outcomes.

We believe the level of the money purchase annual allowance should be increased to £10,000 to give people increased savings flexibility and reflect modern day working patterns.

People are living longer and may not have the ability to manage income drawdown in later life, without the support of an adviser. This is a concern as many individuals have taken out an income drawdown account on a non-advised basis. People's needs and circumstances change as they grow older and due to cognitive decline, some may be unable to manage their income drawdown if they don't have an adviser. This risks leading to poorer outcomes in later life. As the pension freedoms are still in their infancy, the consequences of non-advised drawdown are unknown. This is an area that requires more focus.

Investment pathways have recently been introduced, but as it's early days they remain untested. Furthermore, they are designed to support individuals make a broadly appropriate choice of investment, but don't help them determine a sustainable income.

As people grow older, they will continue to need retirement support, either in the current form of guidance, regulated advice and ideally a new form of more personalised guidance. The first of these should be available from guidance bodies, pension providers and advisers. The latter two should be available only from regulated firms. Currently unless the individual has an adviser, there is little provision for this ongoing support in the market.

One specific example where individuals may need support is to ‘drip feed drawdown’. Here, an individual can crystallise parts of their accumulated pension in stages, going into flexible access drawdown. On each occasion they can use the tax-free cash as part of their required income and supplement this with income from that and previous tranches. This is a highly tax efficient means of taking income in retirement but is also highly complex to arrange and to carry our ongoing calculations. As a result, it may be difficult to access or use effectively for those who don’t seek advice both at the point of, and throughout, retirement.

One challenge that has still to be addressed is how later life social care is to be funded. Government policy has still to be developed in this area. Much greater certainty would allow people to adapt their retirement plans accordingly. Before products can be developed, the Government needs to set out a future deal which should be fair and sustainable. This should involve a sharing of costs between the state and what affected individuals can afford to pay, based on their wealth, We strongly believe an individual’s contribution should be subject to an overall cap. This will then allow individuals to plan ahead. One means of saving for this possible future need would be through flexi-access drawdown. The individual might notionally ringfence part of their pension pot at retirement, taking an income from the balance. This would mean sufficient funds were available should the individual need future care, but if not, the funds could be used for regular retirement income in later years or passed to a beneficiary on death.

It is possible that the current HM Treasury proposals to implement the increase in normal minimum pension age from 55 to 57 may create additional real or perceived barriers to individuals accessing the options that best meet their needs. Individuals who currently have the right to draw benefits from age 55 or earlier may lose that on transferring. Even if they might not in practice have accessed benefits below age 57, the loss of the option to do so may discourage transferring and in doing so limit access to the wider range of options available within more modern pensions.

1. ***Are there other pension options, not currently available in the UK, which would better meet people’s needs in later life?***

Research often shows that people want a guaranteed income for life along with flexibilities such as those provided by income drawdown. It’s possible to achieve this by having a blended retirement income strategy by combined the use of income drawdown and annuities, possibly with different providers at different times.

In the past some UK pension providers, including Aegon, offered so-called ‘third-way products’ which combined guarantees with the potential for investment growth. These products originated in the USA.

However, they were not particularly successful in the UK as they were complex and perceived to be expensive products, and as such could only be sold on an advised basis. Providers have withdrawn from this market and these ‘third-way‘ products are no longer sold in the UK. Due to the environment of low

interest rates and the cost of guarantees, complexity and lack of demand these products are unlikely to be relaunched in the foreseeable future.

Other third-way retirement income products such as variable annuities, do exist in the UK, but again they are complex and considered to be expensive.

In addition to pensions, people can use ISAs as part of their retirement income. These are useful in giving people more flexibility in how and when they start to take their retirement income, separately to taking a pension income, particularly to avoid triggering the money purchase annual allowance.

2. ***Are there barriers to providing other pension options which meet a need and are not currently available in the UK?***

Please refer to our responses to questions 1 and 2.

3. ***Are people receiving the guidance and advice they need to make informed decisions about how they access their pensions?***

There continues to be a low take-up of advice and guidance. Too many people access their pension without taking any advice or guidance. The Stronger Nudge to Pensions Guidance for occupational pension schemes and contract-based schemes should led to a higher take up of the Pensions Wise guidance service.

Only 8% of UK adults receive financial advice according to the FCA. Advice is often either in reality or perceived as too expensive by many people and, coupled with a lack of trust, this acts as a barrier to people using an adviser. This isn't helped by the shortage of supply of advisers.

FCA data also shows that people are on average taking 8% as regular withdrawals from flexi-access income drawdown. While this figure may be distorted by some taking very large amounts with the intention of using their DC pot to provide only a temporary income, anyone taking this level definitely risks them extinguishing their pension savings too quickly. For most people this isn't sustainable, unless they have other sources of wealth, including defined benefit pensions. A more sustainable income withdrawal rate is in the region of 4% or less depending on life expectancy and investment strategy. In future fewer people will have a defined benefit pension, so it becomes increasingly important that people are made aware of the risks of drawing down too much retirement income too early. Investment pathways do not help in this regard.

There's a 'support' gap between what can be offered under guidance (without charge) and what a customer receives under advice, which comes at a cost which many are not prepared to pay. We'd like to see firms (providers or advisers) being able to offer more personalised guidance, which would stop short of a specific product recommendation (advice) but go further than simply providing a list of non-personalised options. We also believe the Money and Pensions Service (MaPS) and Pensions Wise can currently offer some services under a guidance banner which would be considered advice if offered by a regulated firm and would like to see alignment here too. Use of online modeling tools, currently used by advisers, could help customers to become more aware of the impact of withdrawals on their future retirement income.

We strongly believe that people need personalised guidance to increases awareness of complex tax rules such as the money purchase annual allowance.

4. ***What role should the Money and Pensions Service have in supporting people accessing their pensions for the first time, including through pension dashboards?***

   MaPS via Pension Wise already offers a guidance service for people accessing their pensions for the first time. This is available to those aged 50 and over.

   People will not be able to access their pensions through pension dashboards, including the MaPS dashboard. Pension dashboards will allow people to reconnect with their pension savings and view these online in one place. It's expected there will be commercial dashboards in addition to one provided by MaPS, and that these will be embedded in each provider's 'customer journey'. People should be encouraged to access a pension dashboard so they have a full picture of their pension savings before they get guidance or advice.

   As mentioned in our response to question 4, we believe regulated firms, including pension dashboard providers should be able to offer the same level of guidance as MaPS and Pensions Wise.

   As customers will have built up a relationship with their existing pension provider, we believe that it's more likely that an individual will seek guidance from the entity providing the dashboard, rather than from MaPS.

5. ***Should the Money and Pensions Service offer enhanced guidance or limited advice for people making decisions about their pensions?***

   We are keen that all regulated firms who wish to should be allowed to offer more personalised guidance. We support encouraging more people to seek guidance from MaPS, but as MaPS is not a regulated entity, we do not believe it should offer more personalised guidance or advice.

6. ***Can the success of auto-enrolment in helping people save into pensions be replicated for people in retirement through investment pathways?***

   Auto-enrolment has been successful in getting more people saving through inertia. However, the 'savings' part of someone's pension lifecycle is very different from how they access those savings. Accessing retirement income is much more personalised part of the customer journey. How and when people access their pension savings will depend on an individual's financial circumstances and mindset and will be unique to each individual.

   Investment pathways are designed to help those who don't seek advice select a broadly suitable investment option in drawdown. As they were only launched in February, it's far too early to assess effectiveness. Investment pathways do not help with longevity risk or in arriving at a sustainable level of income.

The investment pathways rules only apply to contract-based schemes; they don't apply to trust-based schemes. However, some trust-based schemes may have voluntarily implemented investment pathways and some members may take their proceeds and transfer to access flexi-access drawdown and if non-advised, will then be presented with investment pathways.

Rather than try to replicate auto-enrolment we need to help people move from inertia to engagement with the help of either advice or personalised guidance. We believe this will improve member outcomes.

7. ***Including costs, what information do consumers need about different retirement products to make an informed choice?***

Costs are an important factor in helping members compare retirement income products, but they are only one factor. Consumers need to consider the various elements that make up the value for money criteria. This includes investment choice, ongoing support through tools and personalised guidance and communication.

8. ***Are pension schemes communicating options effectively to members and are there material differences between trust-based and contract-based pension schemes?***

We use a consistent way of communicating to members across our trust-based and contract-based pension schemes.

Employers have an important role to play. Our experience shows that member engagement is higher when employers support Aegon's member communications. We would like to see employers being able to do more in the workplace to promote the value of saving in a pension.

Simpler annual benefit statements, when implemented, will bring more consistency across the pension industry. Hopefully these will go some way to improving member engagement and understanding.

9. ***Can the issues around small pension pots be solved through behavioural changes by savers?***

We believe that the only realistic way to solve the small frozen pension pot issue is by implementing an automated or automatic solution. The DWP small pots working group is progressing their work, and we suggest that the Committee asks for regular updates from this group.

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