Written evidence from LEBC Group Limited (APS0028)

Protecting Pension Savers - Five Years on From Pension Freedoms

LEBC Group is a national employee benefits and financial planning firm, regulated by the FCA. Established in 2000 we have offices throughout the UK. We provide retirement advice via the workplace and to individuals.

1. **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?**

   Since 2011 the choices permitted by legislation to pension savers, who start drawing on their savings, have been expanded both in terms of the timing of those withdrawals and the ways in which their retirement income can be structured, with and without guarantees.

   The removal of the legislative requirement to cash in all pension plans by age 75 and near compulsion to buy an annuity with any remaining savings, has had a positive impact on the willingness of individuals to save for retirement.

   The retirement income options available range from those offering a fully guaranteed and fixed income for life, through to no guaranteed returns and total flexibility on withdrawals, wholly dependent on investment returns. There are also many options which offer a combination of guarantees and flexibility.

   There is no obvious need for more product choice or design but rather a need for consumers to be better equipped to plan for retirement and understand and manage those choices.

   Not all pension schemes offer their members flexible retirement options. Some older legacy contracts still require total annuitisation at age 75, often restricted to the provider's terms. Many trust-based schemes do not offer flexibility, nor offer the member access to advice, nor guidance, nor online tools to drive member engagement.

   Measures taken so far to assist those accessing their pensions focus too much on last minute decision making and their short- term needs. For example, those accessing their pensions without advice, are offered default investment options which consider their likely needs over a 5-year period. While 5 years may be an easier time frame for consumers to consider their immediate needs, it risks ignoring the need to ensure that income remains sustainable over the long term which could be 30 -40 years.

   To successfully manage retirement income needs, without the benefit of defined benefit pension underpin, consumers need to consider all of the options available, to include other savings, not just pensions, to include options not offered by the pension provider, taking account of taxation, personal family circumstances and needs of dependants and expected longevity.

   Default investment pathways make it too easy for the consumer to access their pensions without consideration of these matters. It leaves them too reliant on guidance from the provider with which the pension fund was built up, so that other options may not be fully considered.

   Those who access their pension flexibly to provide essential income need ongoing support. Including managing their investment risk and adjusting the income as circumstances and needs change. Without this support sustainability of income for their lifetime may not be achieved.

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

No comment

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

No comment

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

Access to guidance and advice to help individuals navigate the choices on offer and to drive engagement in their retirement planning, from the start of their working life, needs to be expanded. This is the route to helping them be better equipped to manage their short-term finances, to facilitate greater saving for their retirement and then navigate the choices they have in retirement. Without this additional impetus to workplace education and saving, pension freedoms are unlikely to be relevant to future generations, as they will have too little saved to take advantage of them. [1]

Government initiatives to offer guidance (Pension Wise/ "wake up packs ") currently only start from age 50, or once an individual is ready to access their fund after 55. Evidence given to the FCA's Retirement Outcomes Review shows that this is often too late, with many individuals who deal with a product provider simply focussing on the mechanics of accessing the funds, dealing with pension pots piecemeal and not considering other options, or the wider implications of their actions.

Long term needs are harder for consumers to envisage. Regulated advisers who specialise in retirement planning use cash flow modelling to help consumers understand the risks of an inappropriate withdrawal strategy. Advice and guidance delivered on a regular basis can help coach them to arrive at solutions more likely to provide sustainable income. This is also framed within a holistic review of their overall wealth and income from all sources, rather than the piecemeal approach of considering only pensions or one product at a time. Other investments and housing wealth play an important part in retirement income planning so guidance and advice needs to encompass all assets and income to be effective.

Bridging the information and skills gap will become increasingly important as a determinant of consumer outcomes when fewer have a defined benefit pension underpinning their retirement income needs. Those reaching age 57, from the 2030s onwards, are expected to have much less saved than earlier or later generations.[1] Many "Generation X "workers were not offered defined benefits schemes, nor the benefit of auto enrolment from age 22, as is now the case. Future retirees, with fewer guaranteed sources of income, and lower levels of defined contribution savings, risk running out of retirement income sooner than the cohort currently enjoying pension freedoms.

Government initiatives so far have focussed on "at retirement" guidance offerings and increasing workplace savings through the inertia of auto enrolment. These solutions are welcome steps but are limited in their capacity to resolve the problem of the decline of defined benefit pensions (only 1 million private sector workers are accruing defined benefits pensions) [1]. Increasing reliance on investment returns coupled with increasing longevity requires greater education and ongoing support for retirement savers.

Guidance and advice to be effective must be delivered over a long timeframe. Starting from the first day at work to embed the need to only spend what they can afford, to set aside savings for short term emergencies and invest for longer term goals. This can be assisted by technology using open banking, apps and nudges but also requires coaching. It can best be provided through active member engagement in workplace pensions extending to personalised advice through retirement.

Delivering guidance and advice well ahead of any immediate income need is more likely to enable individuals to be equipped to manage the risks of relying on investment returns for some of their income.[3]

Government has already enabled employers to pay for access to guidance and advice for their employees with up to £500 per employee, per year, as a non -taxable benefit. The availability of this tax-free benefit should be better publicised to consumers, employers and trade unions and encouraged as employer best practice.

Workplace based guidance can be delivered at scale, repeated over a longer timeframe, and can be supplemented by regulated advice at key decision points. Delivery by regulated advisers makes this a smooth transition process and provides the consumer with the safeguards of regulated advice which extend well beyond the help of a guidance only service.

A strategy to expand workplace-based advice and guidance throughout the working life is likely to have a far greater impact on long term outcomes. 2,3.

1. The Ski slope of doom – Lane Clarke and Peacock April 2021
2. International Longevity Centre "The Value of Advice "showed that those who took advice were on average £47,706 better off at age 65 compared to those who did not.
3. International Longevity Centre study showed that those who took advice regularly were 90% confident about their retirement plans.

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

The Money and Pensions Service has a role in providing information and education. Better informed consumers are likely to make better decisions which in turn improve their retirement outcomes. However, it is important to recognise the limitations of the service, which has insufficient resources to provide more than generic guidance, and that consumers expectations of the service are aligned with what it can be reasonably expected to deliver.

The Pensions Dashboard will be unique in mandating all providers to supply accessible information about pensions and so will be helpful. It may reduce the cost of advice delivery.

There are already many commercial applications providing a dashboard for savers using open banking technology. The best of these provide a fuller picture than pensions alone, including credit cards, loans, and mortgages, as well as other types of savings and investments from a wide range of providers.

Pensions are only one source of retirement income, with other savings and property wealth also playing a significant part in retirement planning. Commercial dashboards and models used by regulated advisers can capture data on all of these sources of wealth, so while the Dashboard is a welcome innovation it's practical use may be limited.

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

The regulatory boundary between advice and guidance must be maintained in the interest of consumer protection. Providing a halfway service would in practice be difficult to navigate and would confuse consumers who may be disadvantaged as a result.

It is vital that consumers understand whether they are being offered guidance or advice. Guidance is generic information, not taking account of their needs and circumstances, they must make their own minds up and have no consumer protection if they misinterpret the guidance. .

Regulated advice requires firms to make recommendation, having taken personal circumstances and needs into consideration. Advisers bear full responsibility for the advice, which places the consumer interest at its heart, takes account of all their circumstances and is backed up by qualifications and training, professional indemnity, regulatory oversight, and access to an Ombudsman service.

The Principles underlying regulation cannot be watered down without the risk of significant consumer harm. Would limited advice require full knowledge of the consumer, what would the training and qualification standards be of those delivering it, who would compensate the consumer if the limited advice led to consumer detriment?

For those who do not have the benefit of all their income needs being met from guaranteed income, the availability of advice and guidance needs to be an ongoing feature of managing their money in retirement and adapting plans to changing family circumstances. Regulated firms can provide both guidance and advice on an ongoing basis, to keep retirement plans up to date with changing needs and to consider all options available to the consumer.

It is hard to envisage how a free service could sustain the need for ongoing guidance and advice to the standards required of regulated advice or how it would be funded sufficiently to do so.

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

While auto enrolment has been a success in bringing 10 million more workers into retirement saving, it is not an unqualified success. Low paid workers and the self employed are excluded and the 8% contribution is insufficient to provide more than a minimal standard of living.

To ensure that future generations can afford to retire and be financially independent, active engagement in saving needs to be the norm and the ideal balance between spending and saving better understood. This can be achieved through workplace education and guidance with workers coached to defer consumption to provide for their future. The level of funding needed to achieve a reasonable living standard in retirement cannot be achieved through inertia or coercion without becoming another form of taxation.

Decumulation of funds over a lifetime requires careful planning. Plans need to factor in and adapt to complex family circumstances, likely to change over time.

With other savings also playing a part in providing retirement income, a successful retirement income strategy needs to take account of all assets and sources of income to include consideration of investment risk and taxation. An automated default strategy which disregards all sources of income and assets and taxation thereof would not work.

An auto enrolment approach would likely leave consumers disengaged from the need to spend prudently and choose an appropriate investment risk. The consequences in decumulation could be disastrous for them. A better solution is to provide them with the skills needed to achieve financial capability in the accumulation phase, in readiness for managing income in retirement.

Patterns of retirement and the transition into retirement are nuanced since the Discrimination Act has abolished default retirement age. Pension freedoms serves this well, enabling individuals to transition to full retirement over time, taking account of their needs and other resources. Default strategies would be difficult to manage in this context and undermine the benefit of pension freedoms.

Consumers need to be helped to make active choices, from an informed position. Workplace advice and guidance, supported by employers, trade unions and a tax subsidy can create better financial capability amongst the working age population leading to financial capability in retirement.

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

Consumers need to know the costs of the product, platform and fund manager, cost of advice, the investment options available, the investment risk these entail, projected returns from the underlying investment and probability of these being met, likely sustainable income level, whether there are any underlying guarantees offered with the product and how these work, penalties or charges for encashing the product, tax treatment on income and the fund on death.

They also need to understand the role which the product plays in their overall retirement income strategy, whether it is essential to their standard of living, whether it offers the potential or guarantee of inflation protection, the extent to which the income can be increased or decreased and its tax treatment, its purpose alongside other investments and sources of income.

Taxation of the product and impact of withdrawals on future pension savings, such as the imposition of the money purchase annual allowance, which restricts future pension savings to no more than £4,000 per year, once any income in excess of the tax free cash has been withdrawn. A rule little known by consumers until it is too late.

Similarly, the impact of lifetime allowance charges, depending on the order in which pensions are encashed, can be a key consideration for pension savers who find this tax hard to understand.

Impact on benefit eligibility if pensions are accessed before State retirement age.

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

There is considerable variation in the quality of information provided and the ease of access which consumers have to that information. Some trust-based schemes provide access to information more efficiently than others.

Some trust-based schemes do not offer access to flexible retirement options. The extent to which members receive information on investment choices, valuations and projected income also varies as does access to advice and guidance. Once a member leaves service it is not usually possible to continue funding a trust-based pension pot without transferring it to an individual arrangement, a process which can be difficult for the member to negotiate.

Contract based providers who remain active in the pension market tend to supply information and guidance more readily than those who are administering legacy contracts, for providers no longer active in the accumulation market. This latter group and the less well-resourced trust-based schemes can add considerably to the cost of delivering advice.

Not all contract based schemes established before 2015 offer flexible retirement options, contractual terms may offer limited choice, creating pension prisoners from age 75.

Technology can greatly assist the provision of accurate and up to date information. Companies active in the market are embracing the use of open banking technology to make information more readily available to pension savers.

Investment in secure technology is one of the ways that the cost of advice can be reduced to create wider access to advice and to help consumers be better informed. When ongoing advice and guidance is also offered members become more engaged and can plan for retirement with greater confidence.

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

Education of savers, assisted by open banking technology, which enables savers to retain access to valuations of their plans digitally, can greatly assist the issue of lost pensions currently worth £19.4 billion according to industry estimates.[1] This in turn can assist with consolidation of pension pots if appropriate.

Given that other savings pay an increasing role in retirement income provision, the use of open banking technology to capture other savings can also help to reduce orphaned accounts which make up £14.35 billions of savings to be invested or spent in the economy [2].

1. Estimate made by the Association of British Insurers May 2020
2. Unclaimed Assets UK June 2020

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