# Written evidence from Scottish Widows (APS0037)

Thank you for the opportunity to contribute our views to this inquiry. What to do with a lifetime of savings is a hugely important question for individuals. It will become even more important in future, as we see the decline of defined benefit (DB) pensions followed by bigger defined contribution (DC) pots.

We believe that, in the broad sense, customers have the options they need to make the most of their retirement savings. The fundamental building blocks – annuities, encashment and drawdown – serve different purposes and can be used in conjunction with each other to address individual needs and provide for a tailored retirement journey.

The biggest problem we face is the advice gap. People need help in making these big decisions. Many people really want that help in the form of an expert telling them what to do but they can't or don't want to pay for this. One part of the solution could be more personalised guidance, which could mean shifting our view of where the boundary between advice and guidance sits. Another would be finding a way to supply more streamlined, focused advice at low cost.

At the same time – and perhaps slightly contradictory to the concept of streamlined advice – we also need a more holistic view of funding retirement. Pensions aren't the only source of retirement income, so we need to help people to consider their pensions, property and other assets in a more joined up way. This isn't currently as easy as a it should be and we expect there is a role for the Money and Pensions Service (MaPS) to play, both directly and through collaboration with industry.

At the time of writing, the FCA is considering new rules to nudge more customers to Pension Wise. We certainly see value in customers receiving additional help with major, irreversible decisions, but are mindful that this may not always be necessary for smaller pots, nor would it be necessary to try and make customers have separate appointments for each pot they have. We're particularly keen to explore what pension providers can do to complement Pension Wise and other work undertaken by MaPS.

While too early to assess in full, with think the FCA's Retirement Outcomes Review has improved the retirement journey, particularly for non-advised customers taking their benefits through drawdown. The FCA's remedies only apply to contract-based pensions though, so we need the Department for Work and Pensions (DWP) and the Pensions Regulator (TPR) to set up an identical framework for occupational pensions.

Finally, transfers out of DB schemes can make the flexibility of the pensions freedoms available to more people. But this comes at the loss of valuable certainty and introduces new risks. Too many DB savers are faced with a cliff edge decision of transferring everything or nothing; we'd like to see partial transfers more widely available.

We would be happy to provide further information and answer questions from the Committee.

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?**

Pensions are important for funding people's needs in later life but they are not the only source that can be called on. Some people will be able to draw on other forms of savings and investments or on property – including their own home. Helping people make the most of these different sources of income will require a more joined-up approach to retirement planning.

It should be easier for people to plan for retirement more holistically and to access support, guidance and education that has a wider scope than pensions. We have done a lot of work on the role of property in retirement. Not only is a home a potential asset that can be used to fund later life but home ownership itself, being free of rent and mortgage, has a major impact on retirement income needs.

With regard to pensions specifically and the different options for taking benefits, the pension freedoms have broadened savers' options. This has been largely welcomed because all our customers have their own retirement journeys with varying needs that can change over time and therefore different solutions are required.

The building blocks of pension freedoms – annuities, drawdown, partial and full encashment – address key customer needs in different ways. Annuities offer certainty and security. The others offer flexibility.

These are not binary choices and many customers will want and benefit from both certainty and flexibility. For example, some may want the flexibility earlier in retirement, when they have greater expenses and are more confident managing money and then the certainty becomes more important later on. Others may seek certainty and flexibility at the same time – taking a guaranteed income to cover their essential needs but enjoying flexibility with their remaining savings.

We believe the key building blocks are already there for customers but they're not coming together in the optimal way. Our priority should be to crack how we draw them together, along with non-pension assets, particularly in the context of low take-up of financial advice (see Q4).

Customers with defined benefit (DB) savings will also value both flexibility and certainty. But many are forced to take a binary choice because their schemes do not offer partial transfers. This may have contributed to a number of cases where customers have completely transferred out of a DB scheme when it was not in their interest. We would like to see the option of partial transfers made more widely available.

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

As outlined above, we believe the fundamental building blocks are largely in place, though we do not have a holistic approach to using pension and non-pension assets. In Q3 we address some ways in which these building blocks could be further developed.

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

There are a number of 'soft barriers' we should consider – they don't strictly prevent us making new options available, but they are difficult to take to a competitive market. This is particularly true for guarantees, which used to be a common way for insurers to take on retirement-related risks that would otherwise be borne by customers.

Solvency requirements

High capital requirements tend to make guarantees and other forms of risk-sharing commercially unattractive. A recent report from the Institute and Faculty of Actuaries, *The Great Risk Transfer*[1], recommends that "HM Treasury should use the Solvency II review to implement regulatory changes that will enable and encourage insurance companies to offer affordable guarantees."

Price as the basis for comparison

We have seen many consultations, reports and guidance from Government and regulators that all recognise price is not the only determinant of value, but they often lead to price being the key focus at the expense of other drivers of value.

Risk sharing is inherently more expensive than managing and investing a pot of money for a customer. A broader appreciation of value could see markets adapt with greater value-adding propositions.

Complexity

Similar to the point made above, there has been a general drive against complexity and towards simplicity. We have been largely supportive of this, particularly in regard to opaque charging structures used for what should be simple products.

But – again – insurance and risk-sharing is more complex than managing savings and investments.

We would welcome the regulators and Government exploring whether the pensions industry could reduce risks faced by customers by taking on risk themselves.

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

The need for pensions guidance and advice has greatly increased over recent years. Changes in legislation have led to millions more people saving into a pension and pension freedoms has given them more choices. Consumers face complex decisions with varying levels of financial capability. We welcome the publication of the Money and Pension Service's (MaPS) Financial Wellbeing Strategy, which aims to improve the lives of millions by setting goals across five key areas – financial education, saving, credit, debt advice and retirement.

Our research tells us that 76% of consumers cannot afford or don't want to pay for advice but, as financial decisions can be complex, they still want an expert to be able to tell them what to do. Many are willing to spend around £50 - £100 but whole of life advice currently costs consumers approximately £2000.

[1] [The Great Risk Transfer | Institute and Faculty of Actuaries]

For the 76% of the population who are unwilling or unable to pay for advice, guidance, in its current form, is not always the solution – people want experts to help them reach an answer. Many speak to friends, family and often use Google while experts, who may be able to support, are prevented from doing so without straying into giving advice.

We value the work the FCA is are doing through the Consumer Investment Market Review to close the advice and guidance gap. Early conversations with industry are considering an enhanced guidance approach or a model of restricted advice:

- Enhanced guidance – this would allow more personalisation but would stop short of recommending a single course of action
- Restricted advice – this would allow advice on a direct course of action based on some focused customer inputs, but not require a wide ranging investigation into and consideration of the customer's broader circumstances

More broadly – it should be easier to access more holistic guidance and advice to take into account the role non-pension assets can play. It's not currently easy to get advice or guidance that considers your pensions, other savings, equity in your property etc.

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

MaPS has a key role in supporting people accessing their pensions for the first time but also before this point. As the initial provider of pension dashboards, MaPS has an opportunity to provide appropriate guidance journeys for customers as they engage with the dashboard.

As well as directly helping people through its own services, MAPS should work with industry and other stakeholders who can lend further capacity to better help customers. We would be interested to explore whether MaPS could franchise elements of its support to industry. It may be possible that we can connect customers to MaPS' impartial support, without having to hand customers off to them – addressing the risk that customers don't follow up with MaPS to get the help they need.

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A key area MaPS should look at for customers accessing pensions for the first time is drawdown withdrawal rates. Currently, withdrawal rates in drawdown are often at levels too high to be sustainable through retirement. Notwithstanding the role advice or guidance could play here, MaPS could help with generic rules of thumb on sustainable withdrawal rates, which the industry can then present to customers, without straying into realm of giving investment advice.

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

We are very supportive of the work on enhanced guidance and limited advice in light of the FCA's Consumer Investments Market Review and hope that as a result, more personalised guidance and cheaper advice options may become available, which will open up more support for consumers.

MaPS should certainly be able to offer enhanced guidance, though with limited capacity it should consider how it makes best use of its resources and how the industry could complement it.

A personal recommendation – advice – may be a step too far. Should MaPS go down this route, providing advice, they would take on certain liabilities and may be open to compensation claims if customers experience detriment. However, recent qualitative research we have done with advisers suggests that while they see a place for limited advice they don't necessarily all see themselves fulfilling that need. It's certainly worth further exploring whether MaPS or other organisations could play a role here.

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

The decisions about what to do with your savings at and approaching retirement are completely different to the decisions made in regard to accumulating savings for retirement.

It is much easier to have a one-size approach for accumulating savings; the vast majority of people are better off being automatically enrolled than not, and are well served by governed default investments.

With so much more variety in individuals' retirement journeys, we don't think the same principle can apply to investment pathways. What the pathways should do well, is help make investment decisions simpler and steer customers away from major pitfalls (such as leaving all their money in cash to be eroded by inflation).

Perhaps the next step from pathways is to help more drawdown customers manage longevity risk. The pathways should get them into appropriate investments but this will not lead to good outcomes if customers make withdrawals at unsustainable rates. This is going to be increasingly important as customers approaching retirement will be less reliant on DB and will increasingly have large DC pots for drawdown.

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

Customers need to understand the key building blocks and the purpose(s) each one can serve. Broadly speaking, that's annuities for a guaranteed income for life and drawdown for flexibility and investment exposure etc.

Then there's another layer they should understand e.g. different types of annuity – single or joint life, standard or enhanced. There should be as much focus on this as on the first point. We see cases where people who had relied on their partner's pension income are greatly surprised and distressed to learn a single life annuity stops paying out after their partner's death.

Finally, once they know what type of product(s) they want, they can consider different providers. Advised customers are well served in this regard but it is more difficult for non-advised customers, particularly when selecting a drawdown provider.

They need to know the cost and this can be complex due to different charging models – charges for the product/platform and further charges for funds (sometimes the two bundled together, sometimes not), further fees for certain activities, changes in charge when your funds go under a certain value etc.

Then they also need to know what they're getting for the price: the investments, the online functionality, customer service support, education etc. The MAPS drawdown comparator tool has potential to help here, although it may still focus heavily on price.

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

The key difference between trust- and contract-based schemes is that the remedies arising from the FCA's Retirement Outcomes Review, including drawdown investment pathways, do not apply to trust based schemes.

It is less common for trust-based schemes to offer in-scheme drawdown but when they do, it is clear that customers should get the same support and protection regardless of the type of workplace arrange they save into. The DWP and the Pensions Regulator should introduce new rules that mirror the FCA's.

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

We are contributing to the industry initiatives on small pots. While we will continue to invest and innovate to get people more engaged with saving for retirement and to highlight the options for customer-initiated consolidation, we have no confidence that this alone will make significant inroads on small pot proliferation.

The small pot problem is an inevitable consequence of automatic enrolment (AE). AE itself is founded on the idea that savers don't actually have to do anything.

We think some form of automatic consolidation would be required to reduce the number of small pots and this will require Government intervention. To the extent small pots is an efficiency problem as well as an engagement problem – duplicating costs unnecessarily – we will need to be careful that any intervention isn't more costly than the original problem, and that auto consolidation can be done at low cost.

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