Written evidence from Centre on Household Assets and Savings Management (CHASM), University of Birmingham (APS0052)

Background

This submission provides an overview of the core issues identified by stakeholders of the research project *Pension Decision-Making in the New Retirement Landscape: Understanding and improving outcomes for consumers*. This project is being carried out by the Centre on Household Assets and Savings Management (CHASM) at the University of Birmingham. CHASM is an interdisciplinary research centre based at the University of Birmingham within the College of Social Sciences. The Centre's areas of expertise include financial inclusion, financial capability, financial assets, and financial transfers and tax. The project is being funded by the Standard Life Foundation and led by Dr Louise Overton, Director of CHASM.

Pension Decision-Making in the New Retirement Landscape is a qualitative research project designed to understand the decisions people make regarding the decumulation of their defined contribution (DC) pension savings, and the effectiveness of existing consumer protection strategies. The project is currently in the pre-fieldwork phase and, as part of this, a workshop was held with stakeholders from across the pensions industry, third sector, and academia.[1] Participants were asked to identify the key risks and challenges for defined contribution consumers in the current pensions landscape.

This submission is not intended to provide a comprehensive overview of all the issues being faced by DC consumers, nor does each point necessarily represent the views of all participants or their organisations. However, it does provide a snapshot of some of the key challenges relating to pension freedoms which may be useful to the Committee. The project is due to release its full findings in December 2021, and the research team will gladly send a copy to the Committee when it is completed.

Risks and Challenges for Defined Contribution (DC) Pension Consumers

- **DC pensions are being used for several things aside from income, including as a form of emergency savings** – Following the introduction of pension freedoms, consumers have increasingly come to see DC pension pots as a form of *savings* rather than income. This means that many consumers are turning to their DC pension pots to get out of immediate financial trouble. This is usually a suboptimal solution when compared to other remedies available, such as debt advice or managing with creditors. Consumers could be steered away from this if they were accessing appropriate advice or guidance, but unfortunately in most cases this is not happening. Individuals accessing DC pension pots to meet short term needs could also create issues down the line when these consumers are unable to use their pots as a form of retirement income because

[1] This included individuals from: The Money and Pensions Service (MaPS), Just Group PLC, Ignition House, the Pensions Policy Institute, the University of Leeds, and a range of independent professionals, including an influential financial services consultant, and a consumer advocate and policy expert.

they have already spent it elsewhere. A reframing may therefore be required to re-establish the mental link between DC pensions and income. The perception of DC pension pots as savings is also often reinforced by DC pensions existing as several small pots rather than one big pot.

Related to the above, there are some early indications that Covid may have increased the extent to which DC pension pots are being used to meet urgent family needs, such as intergenerational transfers. More research is needed as to whether this is the case.

- **Changes in how people think about retirement** – There are several labour market effects associated with Covid that may start to impact how people access their DC pension savings. For instance, people in their 50s may be experiencing job loss or a reduction in working hours, and it can be very difficult to re-enter the labour market at this age. Indeed, ONS labour market data show that, after 18-24-year-olds, workers aged 50+ experienced the greatest falls in employment in 2020. The same survey data also suggest employment among people aged 50+ will fall further when furlough ends. At the same time, the increasing prevalence of working from home may have persuaded others to delay retirement, and access to pension savings (i.e., because they no longer must commute).

- **Policy makers acting on incomplete data** – The FCA still primarily tracks outcomes for DC savings at pot level, rather than person level. This is better than nothing, but it would be more useful to track outcomes based on other consumer characteristics, such as whether they have accessed Pension Wise guidance or the type of DC scheme they are enrolled in (i.e., trustee based or non-occupational).

- **Existing 'signposting regime' does not provide consumers with enough support** – A huge amount of regulatory focus has gone on measures such as 'Wake-Up Packs' or 'stronger nudges' which encourage consumers to seek further guidance or support from a range of sources. However, the impact of these interventions is small or non-existent. For instance, 'stronger nudge' trials carried out by MaPS and The Behavioural Insights Team delivered an 8 percent increase in attendance of Pension Wise appointments (Farghly et al 2020). This is nowhere near the Government's stated goal of making Pension Wise appointments a 'natural part of the journey individuals embark on when making decisions about their pension savings' (DWP 2020).

- **There is a general disparity between the worldview of policy makers/ insiders and everyone else** – Most people have little understanding of pensions and therefore, understandably, leave their decumulation decision until very late and/ or delay this where possible. This is particularly because of the importance of the choice, and also a range of behavioural barriers. There is an underlying assumption among policy makers that increased engagement will solve this. However, it will be extremely difficult to get some individuals to engage and there are deep seated reasons (such as behavioural factors) which prevent this.

Different types of government/ regulatory interventions may therefore be required to address this issue.

- **The 'path dependency' of existing choices** – The current system creates a 'path dependency' wherein an initial choice has large 'knock-on effects' which impact on consumers for the rest of their lives. This acts as a further reason for why people may not want to engage with decision making and may also direct some individuals down unsuitable pathways.

- **Lack of innovation and the flawed 'choice paradigm'** – The original assumption among policy makers was that improved choice for consumers would lead to increased market innovation, better products, and therefore better outcomes. However, this does not seem to be happening.

- **People getting 'stuck' in poor value products** – Many consumers, particularly those who are on a non-advised drawdown pathway, are choosing the 'path of least resistance' with their current provider and are ending up in poor value products. There is currently no incentive for providers to act to improve outcomes for these captive and/ or inert consumers, meaning more robust regulatory action may be required.

- **There is currently too much onus on consumers to make the 'right choices', rather than on providers to protect consumers** – Given we know there are large numbers of captive and/ or inert consumers, more duties may need to be placed on providers to ensure consumers come up with optimal withdrawal strategies. This could include interventions such as duties of product design, price caps, and 'guard rails.'

- **Lack of consideration in existing policy of *household effects*, particularly on a surviving, lower earning, partner (usually women)** – There is currently no way of safeguarding the interests of a lower earning second partner when it comes to DC pension decision making. This is likely to lead to lots of older women down the line who are struggling financially. A more interventionist regulatory approach would probably be required to address this issue.

- **People need more support to steer them away from bad outcomes so they can benefit from pension freedoms** – More critical engagement is required to explore whether the guidance guarantee is enough to prevent poor outcomes and, if so, how the take-up of impartial pensions guidance can be increased.

- **Suboptimal long-term choices from individuals *now* creating issues for the state further down the line** – The current ways people are using their DC pension pots could create issues for the state down the line in terms of the numbers of people who will need support from the care system, benefits etc.

- **Supply side interventions, such as investment pathways, currently only apply to new drawdowns** – The idea of default pathways could be expanded to other types of withdrawal, not just new drawdowns. This could help to give consumers a more manageable number of options. For example, there could be a more general default decision making pathway/ withdrawal pathway. Regulators could also take a more interventionist approach regarding a charge cap for drawdown/ decumulation in general (currently the charge cap only applies in accumulation), or NEST could be allowed to come into the market.

- **Risk of a pension freedoms scandal (including around charges) –** Existing research suggests that several firms and providers are concerned that some form of scandal around pension freedoms will emerge in the coming years (Lindley 2019: 4). However, there is a lack of proactive action regarding this as everyone within the industry assumes that they will not be directly implicated or affected by it. Rather than waiting for things to go wrong, and then having to manage the fallout, there should be a more proactive use of powers now to prevent this from happening in the first place.

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Reference List

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