

Written evidence from The Institute and Faculty of Actuaries (IFoA) CDC Working Group (APS0054)

The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the UK Work and Pension Committee's call for evidence on 'Protecting pension savers – five years on from the Pension Freedoms: Accessing pension savings'. Below are the key points we wish to make.

Please note that the IFoA is submitting this response based on our recent work for our 'Great Risk Transfer' report and the work emanating from our Pensions CDC and Collective Benefits Working Party chaired by Simon Eagle. As such, we have responded below to only those questions that are most relevant to our activities in these areas.

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?

Although in law there are currently numerous pension options available for individuals in the UK, many individuals' employers no longer provide access to defined benefit pensions. This leaves just one option, Defined Contribution (DC) pensions. Although DC might be well suited to many individuals, in its current form it would not meet well the needs of others, especially those who want a regular retirement income for whole of life, no matter how long they live, but do not want to meet the expense of an insured annuity. Therefore we are of the view that there is not currently a sufficient range of pension options in the UK. And so we are encouraged by the Government's recent activities in this area and the W&PC's inquiry.

Connected with this, IFoA has identified that over recent decades there has been a trend of the transfer of risks from institutions – such as employers, the state and financial services providers – to individuals. Since the start of 2020 the IFoA has been campaigning on what we have termed 'the Great Risk Transfer' (GRT), and the consequences it may have for pension savers. Please see the box at the end of this response for more information on this.

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

Good pension provision represents a puzzle about how to provide an income which cost-effectively meets an individual's needs in retirement, when those needs and the individual's lifespan are unknown in advance. There is no perfect way to solve this puzzle, and so the task is to identify the least imperfect approach. Further, the answer to this is different for different groups of individuals in the UK, depending on matters such as their other sources of income, the type of expenditures that will make up their income needs, and their appetite for managing their own retirement savings. While some groups' needs might be well met by existing pension provision options, we are of the view that better options could be made available for some groups. We are open minded about the possibilities, and have recently been investigating two options in particular: Collective Defined Contribution (CDC), and modern tontines.

One of the options that we support is the provision of pensions through Collective Defined Contribution (CDC) pension schemes. These give individuals an income for life in retirement, at fixed cost for employers – these come with no guarantee of benefit levels but are invested to give an expectation of cost effective pensions. Based on the CDC design developed by Royal Mail with the Communication Workers Union, working with some of our members, the Government has made good progress in this area through the Pension Schemes Act 2021, and is committed to introduce regulations shortly to facilitate these. But we see this as only

the beginning - the IFoA, is seeking further Government action to show employers that CDC is an attractive alternative to DC schemes, address concerns employers may have, such as regulatory burdens and costs, and to support the introduction of multi-employer and master trust CDC schemes in order to provide employees of smaller organisations with access to CDC.

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The IFoA is carrying out further work on CDC, including conducting a survey (jointly with the Royal Society for Arts) of the pensions industry on preferred forms of CDC, and commissioning academic research into the benefits of the most favoured form of CDC.

Further, the IFoA is investigating the advantages of modern tontines. These would build on individuals' current option to drawdown from a DC pot in retirement, by introducing an additional 'product' through which longer-lived members, who therefore have need for additional funds, would receive top ups to their pots from those members who die relatively younger. Funds can still be retained for dependants. Tontines are another way of providing a more regular 'income for life'. Our initial academic research on this has been completed, and concluded that modern tontines are expected to generate much higher retirement income than a standard DC drawdown pot which is drawdown prudently to mitigate the risk of a long lifespan. We have commissioned further research into the feasibility of modern tontines and to compare outcomes with other pension vehicles. If this research indicates that modern tontines could be a superior way to provide benefits for certain groups of UK individuals, we would be keen to engage with industry over appetite and with Government over the feasibility of allowing DC pension trusts to provide tontines.

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

The main barrier relates to the law; employers must auto-enrol employees in pensions, and will consider only those pension designs which meet this legal requirement and receive the associated tax treatment that incentivises retirement savings.

The Government has made significant progress on the removal of this barrier, through the enablement of CDC through the Pensions Schemes Act 2021. We are encouraged that this will lead the pensions industry and employers to consider CDC and other new forms of pension provision, leading to further innovation to improve pension provision for the UK. We are seeking to help facilitate this through our campaigns and research. However as noted in 2 above, the Government and DWP will have a big part to play through the enablement of any further designs which can be shown to have merit and be sound.

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

Evidence suggests that people who take Pension Wise guidance feel more confident and have better outcomes than those who do not. However, there is concern about the low take-up of Pension Wise. In a recent Parliamentary debate the Shadow Pensions Minister, Seema Malhotra, stated that only 1 in every 33 people eligible to use Pension Wise do so. Less engaged consumers who opt for income drawdown often accept their own pension provider's default drawdown product, rather than shopping around. Providing automatic Pension Wise advice sessions before retirement would help consumers to consider the pros and cons of drawdown at that stage, so that they could later look separately at the choice of which product

would best meet their needs. In our GRT report, the IFoA recommend that the Financial Conduct Authority (FCA) should set a specific and ambitious target to achieve a significant increase in take-up by individuals of Pension Wise appointments before accessing their pension.

The IFoA's Great Risk Transfer Campaign

The IFoA has identified that over recent decades there has been a trend of the transfer of risks from institutions – such as employers, the state and financial services providers – to individuals. Since the start of 2020 the IFoA has been campaigning on what we have termed 'the Great Risk Transfer' (GRT), and the consequences it may have for pension savers

Our work suggests that the causes of this trend are complex, covering a variety of factors from increasing longevity to technological advances, the low interest-rate environment and changes in financial regulation. The GRT report has unearthed a number of considerations/recommendations relevant to the Work and Pensions Committee and the current call for evidence on accessing pension savings. Prominent examples of the GRT trend include the steady shift from defined benefit (DB) to defined contribution (DC) pensions and from annuities to drawdown.

For more information on the GRT campaign and recommendations see [here](#).

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