Written evidence from the Royal London (PSL0031)

ABOUT ROYAL LONDON

Royal London is the largest mutual life insurance, pensions and investment company in the UK, with assets under management of £153 billion, 8.8 million policies in force and 4,075 employees. Figures quoted are as at 30 June 2021.

KEY POINTS ON OUR CONSULTATION RESPONSE

1. Automatic enrolment has been a very successful policy, significantly increasing the number of people saving for later life. There are still many however who are at risk of not having sufficient savings for retirement. While increases in the statutory minimum levels of workplace pension contributions should be considered in future, the immediate priority is to ensure the implementation of the 2017 Automatic Enrolment recommendations as soon as possible and phased in where appropriate.
2. There are recognised challenges around encouraging those in self-employment to save appropriately for retirement. We recommend harnessing the nudge principles which have been successful in automatic enrolment to encourage greater pensions savings in this group. We set out our proposal for this in our response.
3. Collaboration between the Government and the pensions industry is essential to ensure we focus resources clearly on the initiatives that are most likely to drive the best outcomes for savers. There is a finite amount of resource and limited consumer attention span meaning clear messaging is needed to drive the most appropriate engagement. This work needs to be joined up with the relevant stakeholders and a clear way forward agreed. To help facilitate this, it would be useful, as far as possible, to have cross party consensus on the key longer term pension policy priorities.
4. Responsible investment and climate change are very important when considering the subject of saving for later life. Government and the pensions industry need to work together to harness the power of the money invested for the long term in later life savings. Responsible investment has another very important role to play – engaging customers to think about their pension as an ongoing force for good, not just something that should help them later in life. We have found that educating customers on their pension investment, in terms of the positive impact it can have on climate and social factors, can really connect, and this is something positive that we can work together to harness.

ANSWERING THE QUESTIONS YOU RAISED

Q1. Do households in the UK have adequate pension savings for retirement?

5. The answer to the question of adequacy of household pension saving has a number of constituent parts. Some households are very well served in terms of pensions saving, while others have little or no savings.
6. Automatic enrolment has been a significant policy success in increasing both the number, and broadening the range, of people now regularly saving for their retirement. Prior to automatic enrolment, while there were significantly fewer people saving for (or building up benefits towards) their retirement, those that were doing so are more likely to have adequate pensions and more certainty about the likely amount of their pension. Those with longer periods of Defined Benefit (DB) pension accrual in particular are likely to have adequate pension saving in retirement. DB pensions however are now almost exclusively the preserve of employees in the public sector. This means there is a divide in UK pensions saving adequacy between those in the public sector and those in the private sector, with the costs of these public sector pensions continuing to rise and funded by future tax payers.
7. In the private sector, the majority of employed workers now have a pension, but many of those will not achieve an "adequate" level of pension saving. While defining adequacy is in itself not straightforward (as is well explained in the PPIs recent report - "what is an adequate retirement income", published June 2021), it is clear that a significant number of people who have been automatically enrolled will not achieve an appropriate level of savings for retirement. The research notes that where the Pension Commission's proportional targets are used, only around a half of people can expect to maintain a personally acceptable level of income in retirement. Using fixed income targets, around 3 million people are at risk of not reaching the Joseph Roundtree Foundation's Minimum Income Standard.
8. There are certain groups who are particularly at risk of not achieving adequate pensions income. These include part time workers (the majority of whom are women) certain ethnic minorities and disabled people. Those who are self-employed are also at a higher risk of not having adequate pensions savings.
9. We explore what can be done to help influence better outcomes for people in retirement in response to the Committee's following questions.

Q2. Are changes needed to auto-enrolment to provide an adequate level of pension savings for retirement?

10. Although automatic enrolment has been successful in starting to address the problem of adequacy, we now need to take further steps to build on this success.
11. It is important to acknowledge that many employers are enrolling their workers at the 8% qualifying earnings minimum and that this will not deliver adequate pensions savings for a significant proportion of employees (particularly those with higher working earnings). We do however appreciate

the difficulty in the current economic climate in asking much more of employers and members at this time.

12. The appropriate next step is therefore to implement the outstanding recommendations from the 2017 Automatic Enrolment review conducted by the Department of Work and Pensions (DWP). Reducing the age at which people are automatically enrolled from 22 to 18 will bring more people into pensions savings and help them to form a saving habit earlier in their working lives. Removing the lower earnings limit - meaning contributions are calculated from the first pound earned - will increase contributions for the significant number of people whose scheme uses qualifying earnings. This will also help those on low earnings and those with multiple jobs, as they will get an employer contribution (if they don't opt out).
13. Implementing these reforms will help some of the at-risk groups noted in response to the first question. It would therefore make sense to implement these as quickly as is practical, and to phase in the changes where prudent. In particular, we would recommend that the lower earnings limit is not removed in one go in the mid-2020s. It would be better to phase the reduction in over 2-3 years, starting as soon as proper communication to employers and customers could be achieved. This would mean that lower paid workers would not see such a sharp reduction in take home pay as a result of the increased contributions.
14. The Government should also consider maintaining the automatic enrolment earnings trigger at £10,000, as it has done in the past qualifying criteria reviews. This will help more part time and lower paid workers to start their pensions saving journey. This starting of the saving journey is important, even if there are relatively modest contributions in the early years. Once people begin saving in a pension, pension schemes and providers can, through good engagement, provide relevant information and encourage additional saving if appropriate.
15. It is clear from analysis carried out that average employer contributions to DC scheme members falls significantly short of those that were being paid to DB schemes. It is also true that the average level of contributions being paid to schemes prior to the introduction of automatic enrolment was greater than it is now. Data on the level of reduction in contributions has been provided by ONS in their workplace pension participation and savings trends 2009-to-2020 analysis, published in September 2021.
16. We therefore suggest that while we are implementing the recommendations of the Automatic Enrolment review 2017, discussions should start with relevant stakeholders (e.g. employer representative bodies, trade unions, pension schemes and providers) to build a consensus on the appropriate longer term level of contributions required to achieve adequate retirement savings. As significant increases are likely to be necessary from the current minimum, we should again seek to phase in the introduction of any increases and also aim to reach parity of contributions between the level of employer and member contributions.
17. This will require a long-term approach and cross-party consensus – factors which have been imperative to the success of automatic enrolment to date and which the Pensions Commission, as a well-respected, independent body, was instrumental in delivering.
18. We suggest that re-establishing a Pensions Commission to examine the specific issue of future contribution increases is one that merits serious

consideration and could play a pivotal role in improving the adequacy of retirement savings.

Q3. What advice and guidance do people need when saving for retirement?

19. Many employees are being automatically enrolled into their employer's workplace pension scheme on the minimum contribution basis or the level set by their employer. It is difficult for most employees to know whether this is going to provide an adequate level of income in retirement or if they should be saving more. Self-employed people don't benefit from automatic enrolment and therefore need to be encouraged to start saving in a pension. Likewise, they often don't know how much they need to save for an adequate income in retirement or the best way to go about doing this.
20. Money Helper can educate individuals on the need for saving for retirement and the trade-offs between paying more, retiring later or retiring with a lower income. They can also provide context on wider financial issues which should be taken into account - e.g. prioritising and paying down debt. However, providers also have an important role to play in helping customers to reach better retirement outcomes by building on the existing relationship. This is strongly aligned to the aims of the FCA's proposed new Consumer Duty.
21. The Pension Dashboard will enable individuals to see all their pension savings in one place and it would be valuable for it to show their projected income at retirement in today's terms and compare this against their current salary or income. The PLSA Retirement Living Standards can help individuals to see where they sit against minimum, moderate and comfortable incomes in retirement. We discuss this further in our answer to Q4.
22. It is useful for rules of thumb and illustrative figures to be produced (again explored further in Q4), but the approaches that are likely to have the best success for many mass market savers are personalised guidance and simplified advice. At present providers have regulatory concerns which hamper the provision of the type of guidance that customers are seeking. Industry and regulators need to work closely together to ensure customers can get the best possible service and support from their providers.
23. By personalising the guidance, it can be tailored to the individual's personal circumstances. There is a lot more pension providers and others can do to help individuals, but they are afraid to do so for fear of stepping over the advice/guidance boundary. For example, it could be genuinely helpful if customers are able to find out how much a good standard of living in retirement might cost and if they can see the effect of, for example, delaying retirement, paying more into their pension and/or making cutbacks to their retirement expectations. However, if customers are also able to pay extra into their pension easily, because the guidance is delivered via a pension provider's app or website, does that guidance stray into the territory of funnelling or advice? Would it be a better consumer outcome for someone who has identified that they are not saving enough, if they are not given the option of paying more into their pension? As many individuals are unwilling to pay for full advice on cost grounds, a simplified advice offering at a cheaper cost would allow more individuals to be able to access affordable advice on saving for retirement, or using their pension savings in the most appropriate way.

24. Key to making all this a success is greater engagement and encouraging individuals to save through pensions, delivered through effective communications and tools. This requires the appropriate resources being targeted at the right time in the customer's savings journey and in line with their preferences. Many individuals review their financial position around their birthday or at the start of the year, so communications encouraging individuals to review pension savings should be targeted at such times to have the greatest impact.
25. We need to be mindful, however, that many employers have adopted their own specific approach to communicating with members of their company pension scheme, which is aligned to their wider business operations. For example, the timing of salary reviews, flexible benefit windows and accounting periods can influence when employers issue pension statements to scheme members, and it is important that this flexibility is maintained.

Q4. Could retirement income targets help savers plan for retirement?

26. Retirement income targets can be useful if presented to, and used by, customers in the right way. There are a number of ways such targets can be developed and useful work has been done on this subject. For example the Joseph Rowntree Foundation (Minimum Income Standards) and PLSA (Retirement Living Standards) have produced work aiming to show how much annual retirement income may be needed to provide a particular living standard against a defined basket of goods. While retirement income targets are good in concept, everyone is different and has different views on what is an appropriate level. Nevertheless, it is a helpful starting point.
27. As well as engendering thought about a target income, it is also important for retirement planning to help customers understand how much they may need to save and how much they should be aiming for at particular points in time. On the latter point, Fidelity Brokerage Services produced rules of thumb to help their customers in the US market understand how much they should aim to save by a particular age. They cite a target to have saved at least 1x your income by age 30, 3x by 40, 6x by 50, and 8x by 60. While the pension system and level of Government support is different in the UK, similar rules of thumb can be used to help customers get a sense of interim targets. In relation to how much customers need to save, the Institute and Faculty of Actuaries has produced two papers providing useful analysis on this topic. In its latest paper, Savings Goals for Retirement paper 2, it notes the importance of adopting savings goals that are affordable, and for many people this is likely to mean targeting a pension that sits somewhere between the 'Minimum' and 'Moderate' retirement living standards set out by the PLSA. The paper helpfully sets out savings goals for a range of target living standards and salary ranges which can be used to give customers a sense of what the appropriate contribution input could be.
28. The difficulty with retirement income targets and providing more clarity on the levels of contributions needed to achieve them is that for many the saving levels are simply not attainable for a number of reasons:
    a. The level of employer contribution is too low to support the worker to reach the required input level.
    b. The worker started contributing to a pension late or did not make sufficient contributions in the early years, leaving too much of a gap to make up.

c. The retirement age is not attainable. For certain occupations a retirement age of 68 would not be possible. We should also recognise that many cannot retire at the same time as their state pension age for reasons of ill-health. A report by TUC in March 2021 found that 1 in 8 people are forced to stop working before state pension age due to ill-health or disability.
d. Other calls on money. Milliman's "Decision Citizens" white paper in 2017 highlighted that many cannot afford to save at appropriate levels for reasons such as housing costs, student debt and other essential spending.
e. Results from a PLSA survey issued on 24th January 2022 found that almost half (47%) of those not retired say that they cannot afford to save right now due to the rising costs of everyday living.

29. This highlights the importance of taking into account individual circumstances where possible and providing appropriate guidance or advice. There is a danger in providing information about required levels of saving which for many are unrealistic and may have an adverse effect on workers, making saving for retirement seem pointless. Care is therefore needed in using retirement income targets and 'required' contribution levels.
30. The level of pension contribution needed for even a modest retirement reaffirms the importance of ensuring appropriate levels of minimum contribution rates and ensuring workers start saving at an early age.

Q5. Apart from increasing contributions, how can the Government improve outcomes for savers?

31. Collaboration between Government and the pensions industry is essential to ensure we focus time and money clearly on the initiatives that are most likely to drive the best outcomes for savers. There is a finite amount of resource and limited consumer attention span, meaning clear messaging is needed to drive the most appropriate engagement. As far as possible, it would be helpful to have cross-party agreement on the key longer term pension policy priorities.
32. There is a strong consensus that engaging the public on pensions savings is vital and the launch of Pensions Dashboards represents an opportunity to invigorate interest in pensions.
33. It is important that government, industry, employer and member representatives work together to ensure the public embraces dashboards and uses them as part of their planning for later life. Enabling dashboard providers to use the data to engage customers and inform them about their existing pension arrangements – both State and private - will lead to better outcomes.
34. It would be prudent for the Government, industry and employer and member representatives to work together to ensure the public embraces dashboards and uses them as part of their planning for later life.
35. Responsible investment is a very important issue for the Government, industry and customers and is the subject of considerable work from policymakers and regulators. Removing barriers for investment in broader options, such as new asset classes, will help savers contribute to meeting the UK's global climate goals, whilst also allowing for greater diversification in their savings. This will require collaboration between industry, Government and members, to ensure focus is directed at the most appropriate and relevant areas.

36. Responsible investment has also proved to be an effective way of encouraging customers to take an interest in their pension, for example by highlighting that investment is not just about returns but can be a force for good too.
37. Last year we made enhancements to our default investment proposition. As part of this work we invested in educating customers about how their pensions are helping to fight climate change. We ensured that this information was offered in an accessible way using animations, talking head video, mobile app notifications and social media to facilitate good engagement. We followed up this activity with our 'Invested Generation' campaign that included TV and billboard advertising and we launched a Facebook community.
38. This campaign sought to promote our position as a responsible investor and how we are acting on behalf of our customers to influence positive change in large companies they are invested in on environmental, social and governance issues. We have been very encouraged by the engagement of our customers across our various activities, in response to this work.
39. Education around this issue is key; we cannot assume our customers understand that having a pension makes them an investor. In fact, our research shows that many of our customers do not make this connection. A PLSA survey published on 24 January 2022 found that 31% of respondents were unsure if their pension savings were invested in stocks, bonds, or other investments. Government could help play a role in educating consumers from a much younger age about the power of pensions and the positive impact that responsible investment can have on our quality of living. This, in conjunction with providers investing responsibly, could help make consumers more engaged with their pensions and help create a better standard of living in retirement for people.
40. More can be done to help customers who have been supported, or sufficiently engaged, to pay above the minimum level of contribution to remain on this positive path when they change job and pension scheme. See point 49 for the what the Government can do to help here.
41. We welcome the Committee's call for regulators to conduct further research into the merits of decoupling tax free cash from the rest of the pension. While it is true that over focusing on accessing tax free cash can cause customers to make poor decisions, it is important to be sure that the cost of implementing the change would bring about a positive shift in consumer behaviour.
42. We also support the abolition of the Lifetime Allowance (LTA), as it essentially imposes a penalty on those who have achieved good investment performance. The amount of tax relief available to individuals should instead be controlled through appropriate use of the Annual Allowance (AA). We believe that it is preferable to manage the input, as opposed to penalising good product performance. This is a salient issue in certain sectors, for example in the NHS, where it is important not to create a disincentive for individuals to remain in their jobs.
43. In addition, we are in favour of increasing the Money Purchase Annual Allowance from £4k to £10k (as it was previously), which would enable consumers who have had to access their pension savings (e.g. due to Covid) to replenish them. This would improve outcomes for these customers and allow full advantage to be taken of employer contributions.

Q6. Can pension providers change the design of pension products to improve outcomes for savers?

44. Pension providers will continue to innovate, as far as possible, to provide the best possible products for customers. There is, however, a significant amount of regulatory change which will continue to take up a large proportion of the industry's available resources over the coming period. This is why the point about clarity of focus and direction of travel highlighted in 3 is so important.
45. It would be useful for providers to focus on the benefits of phased drawdown, encouraging customers to take payments (Pension Commencement Lump Sum (PCLS) and taxed income) from their fund when it is needed, instead of consumers taking their PCLS upfront. Taking PCLS as part of their regular income stream can help individuals to reduce future tax bills and avoid inheritance issues.
46. We are also likely to see greater efforts by providers to encourage customers to pay more (where it is prudent to do so) through enhanced engagement methods. Mechanisms such as Save More Tomorrow (using Behavioural Economics to Increase Employee Saving by Richard H. Thaler and Shlomo Benartzi) have the potential to deliver strong improvements in retirement outcomes, but very few firms have adopted this at the present time.
47. Some employers also pay in excess of the required minimum contribution, often where the employee does so too. But when a member changes employer, the pension entitlement rules change with that of their new employer's scheme. For example:
    a. An employee is in a pension scheme which requires member contributions of 6% of salary, or where the pension provider has encouraged the member to increase pension contributions to 6% of salary to improve their retirement outcome.
    b. The employee changes job and the new employer scheme only requires the member to pay 4% of salary, and is automatically enrolled into the new employer scheme at the lower rate.
    c. The employee had been used to paying 6% and could afford to do so, but it is likely they will continue to pay 4% into the new scheme through inertia.
48. It is important, where customers have been engaged to contribute more to their pension savings (or were required to pay at a higher rate in the previous scheme), to avoid reverting to lower levels of saving where possible.
49. One solution would be for all employees to be enrolled in their new employer's scheme at the same level of member contribution as their previous scheme, where this was higher. An addition to the P45 could be used to record the level of the member contribution paid in the last employer's scheme. The new employer could then compare this to their member contribution requirement and enrol them at the higher figure.
50. This would ensure that the member continues to save automatically at the higher level. They can of course ask the employer to reduce their contributions to the lower level required in the new scheme if they wish, but many, having been used to paying the higher level, are unlikely to do so.

Q7. What should the Government be doing to support self-employed people to save for retirement?

51. It is important for self-employed people to become more aware of the risks and consequences of not saving more for retirement. A survey by NowPensions in 2021 revealed that 64% of those self-employed people do not have a pension. However a report by Nest Pensions in December 2020 on the saving outlook of the self-employed revealed that 3 in 5 of those who are self-employed like the idea of automatically diverting a proportion of their income into retirement saving. Government and the industry can work together to develop plans to address this under saving, but this needs to go beyond messages and guidance provision to have any real impact. In particular, we should look to what has made automatic enrolment so successful in increasing savings for employed workers i.e. a nudge and incentive to save.
52. In 2016 Royal London published a policy paper (entitled Britain's Forgotten Army) which sought to harness these elements and proposed the following recommendations:
    a. The main rate of National Insurance paid by the self-employed (Class 4) would be increased from its current level of 9%; given that the employer contribution under automatic enrolment will be 3%, we suggested that the rate of Class 4 NICs would be increased by 3% to 12%;
    b. Self-employed people would be able to elect to have those additional contributions diverted into a pension, provided that they also contributed at a specified level; again, based on automatic enrolment legislation, a minimum gross contribution of 5% (including tax relief) might be required;
    c. We would welcome further work to look at a more strategic solution for the self-employed, such as that mentioned above, in addition to the good work already underway to trial different ways to improve pension saving in the short term.

Q8. Are different or additional measures required to help gig economy workers save for retirement.

53. A key factor for gig economy workers and those that contract with them, is to have clarity about their employment status. In the most high-profile example, the Supreme Court's judgement in Uber v Aslam in February last year upheld that, when drivers had the Uber app switched on and were ready and willing to accept passengers, they were classed as 'workers'.
54. When worker status is conferred, this has important implications, not just for minimum wage and holiday pay entitlement, but for pension outcomes too. Workers should have the right to be automatically enrolled into a workplace pension, subject to meeting minimum age and earnings thresholds. It is therefore important for rules on worker status to be as clear as possible.
55. It is also important that workers in the gig economy recognise the value of setting aside part of their earnings for later life. It can, however, be difficult and costly in terms of communication and campaigns to get this message across. It may be prudent to tie in any expenditure on this with the proposal for nudging self employed workers, noted in point 56 in our response to Q7.

Q9. Are there measures which the Government should consider to close the gender pension gap?

56. As referenced in our answer to Q2, implementation of the 2017 Automatic Enrolment Review recommendations will help bring more women into pensions savings and therefore to some extent will help address the gender pension gap.
57. It is also important to ensure the proper and swift implementation of the Net Pay tax anomaly solution by HMRC. The proposed solution, whilst welcome in principle, means that in practice impacted customers will not be able to claim top ups until the 2025/26 tax year. This protracted implementation timetable seems suboptimal and will disproportionately impact women.
58. Although implementing the above changes will help, the root of the issue remains that a higher proportion of women tend to be in lower paid occupations. Tackling the underlying reasons behind this disparity will feed through to reducing the gender pensions gap.
59. Both women and men can miss out on National Insurance credits towards their State Pension if they do not register for Child Benefit or Carer's Credits. However, women are far more likely to lose out. Our most recent FOI request into uptake of Carer's Credits, in 2018, showed that 97% of eligible carers were not claiming the credit in 2016/17. Although progress has been made to improve this, there remains room for improvement.
60. More should be done to highlight the use of pension sharing orders on divorce. The issue of legal rights to pensions sharing orders for cohabiting couples should also be considered. The Chartered Insurance Institute's Insuring Women's Futures Solving Women's Pension Deficit report in 2019 found that 35% of people do not realise cohabitates have no legal rights to pension sharing.

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