ILAG

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DWP: Helping savers understand their pension choices: supporting individuals at the point of access

The Investment & Life Assurance Group (ILAG) is a representative body, with membership from across the Life Assurance and Wealth Management Industries.

We openly share and develop practical experiences and expertise, applying this practitioner knowledge to the development of businesses, both individually and collectively, for the benefit of the membership and its customers.

ILAG is run by practitioners for practitioners, whether by engagement with industry associated bodies or through active consultation.

The ILAG membership list is at the end of this submission.

We welcome the opportunity to respond to this consultation and have provided responses to the consultation questions below.

Consultation questions

Question 1:Should it be up to trustees to determine the other suitable suites of products?

It wouldn't be appropriate for Trustees to advise members, but they should outline the options available and suggest members seek advice in addition to that offered by PensionWise.

On this basis it would be helpful for DWP to provide greater clarity on the proposals and the policy objectives.

We are uncertain if DWP intends to require trustees to provide a minimum level of decumulation offering through their scheme, or a partnering arrangement, without the need for a member to transfer. Where schemes do need a minimum level of decumulation offering, how this is determined is also not clear. For example, the minimum offering could be a lump sum and annuity, or it could be much more than that. To ensure the intended outcome is achieved, explicit guidance is essential.

The DWP's objective is to place a duty on trustees to offer decumulation services, which are suitable for their members and consistent with pension freedoms.

This seems in line with how trustee fiduciary duties work in other areas where trustees can bring their control or influence to bear on customer outcomes. Even without a prescribed set of requirements, trustees could be criticised for not helping members in a way which is proportionate.

Since *Freedom and Choice*, workplace DC occupational pension schemes have evolved from annuity savings vehicles. These are now the savings vehicle for a complicated range of retirement options, as well as, in some cases, being the post-retirement option.

We agree that there are four key areas where schemes can support their members to make the most of their pension pots:

- Directly offering a suite of products and services.
- Partnering with other organisations to offer a similar range of products and services.
- Organising advice sessions.
- Signposting to appropriate guidance services.

The options that are appropriate for a particular scheme will depend on things such as resource, budget, expertise, and scheme specific constraints, which may exist in scheme rules. It also allows schemes to consider whether, and to what extent, the demographic of members, or variances across the demographic, will engage with certain options or services.

Suitability obviously has a particular meaning in investment circles, but it seems that, in this context, 'suitability' has a different meaning, which is not necessarily aligned with the outcomes of a financial advice process.

It is extremely important that a definition of 'suitability' makes this clear, or ideally, that the term 'suitability' is avoided altogether. There are examples in legislation which cover the considerations trustees should account for when forming a view. The same structure could be used here. There are also similarities with the Investment Pathways which could be borrowed from.

Finally, we note that measures are also under consideration in relation to the role played by Investment Consultants, by way of another consultation.

Question 2 – What can government do to help a CDC-in-decumulation market emerge?

The government needs to reconcile the highly individualised sentiment behind *Freedom and Choice* with the collective experience of CDC. The two regimes do not sit well together.

DWP says (in paragraph 49) that '*The balance we are trying to achieve through this proposed approach is to continue to adhere to the ethos of freedom and choice, whilst enabling individuals to shop around for the products and services that best meet their needs*.'

This statement appears to contradict with a CDC scheme that will rely on members pooling risk and money over a long period to, as an aspiration, benefit the whole, rather than specific individuals.

The government might also consider how it can reassure employers that they will not be liable for an increasing CDC cost burden in future, as has historically been the case with DB schemes. Concerns about escalating costs imposed unilaterally by government or trustees under the terms of a trust may be a deterrent to participating in a CDC scheme. There have also been examples of supposed DC schemes amounting to DB schemes on technicalities, and again this will be of concern to employers who may otherwise be interested in embarking on a CDC journey.

Question 3 – We would welcome views to understand what are the minimum requirements that trustees should put in place for members facing decumulation?

Minimum offering could be a single lump sum and an annuity offering through the scheme or a partnering arrangement, along with signposting to additional supporting services.

The minimum would logically be a signpost to a specified master trust or workplace personal pension scheme, which offers the full range of retirement options, subject to the Charges and Governance regime, or similar. This would, at least, mean the retirement partner scheme is low cost and independently assessed as 'good value'.

We assume that the partnering arrangement would involve the existing workplace pension scheme having a documented arrangement with a preferred receiving scheme for transfers, with negotiated terms, processes and possibly volume discounting on pricing. This would need to be subject to governance oversight. It would be helpful to see some clarity on what partnering should entail.

Nonetheless, if the policy objective is to avoid transfer-out to access all decumulation options, we don't object to transfers providing a good solution for members.

A minimum offering will be a challenge because small schemes will struggle to operate a partnering arrangement that they have effective oversight of and will also have trouble delivering retirement options in-scheme. However, over the medium term, these smaller schemes will consolidate anyway.

Small occupational pensions, which are insured, will often assign the policy into the member at maturity. This is likely to continue.

Question 4 – What factors should a trustee / scheme take into account when developing their decumulation offer?

Factors should include:

- budgetary constraints: cost and resource,
- available administration, systems, and investment capability and expertise,
- the demographics of the membership, and numbers of membership, and,
- size of member pots.

Some occupational pension schemes are very small and will have limited ability to complete this sort of assessment.

Question 5 – We would welcome views to understand if these are the right questions to capture the majority of ways an individual will want to use their pension wealth?

Investment pathways help to ensure members aren't investing indefinitely in cash after taking drawdown. These pathways are targeted at the short-term and the start of a retirement journey. The four questions adopt the same approach:

- do you only want a regular income?
- do you only want flexible access to your pension benefits?
- do you want a combination of both?
- do you want to do something else?

We expect that the right questions to ask should also take account of longer-term needs including, importantly, those of individuals and their survivors. In this context, the proposed questions seem quite limited. DWP should make it clear if it is expecting a full assessment of customer needs.

We acknowledge that few members will truly understand these questions, and that adding any more searching questions may stray into suitability reports and advice. More explanation is required, as these questions represent a blunt instrument and do not mention risk or talk of regular income requirements.

MoneyHelper may help to demystify this, but we consider that it would be useful to share where in the retirement journey these questions are expected to feature, for example, as part of the mid-life MOT. If the intention is that the journey should mirror that of personal pension schemes, then this may make sense for small schemes where, in practice, the insurer might be asking these questions rather than a trustee board.

Ultimately, the questions should be sensibly calibrated to the size of the pot, with small pots and low earners having far fewer options, and less need for signposting to options that may not apply.

It may be that there are lessons from 'Improving Outcomes in Non-Workplace Pensions' that could influence this initiative as well.

Question 6 – Are there any other questions we should include in the framework?

There should not be too many questions, but it is prudent to consider both health and dependants in addition to the questions proposed. Asking questions about other available income creates unease, as this could easily stray into crossing the boundary into suitability and advice. Other questions could include:

- do you want to take all your retirement funds at once?
- do you want to take tax-free cash and leave the rest of the fund invested?
- do you have dependants that you also need to provide for?
- do you have health issues that may mean you could be entitled to an enhanced annuity?

In addition, although not a question, the framework could also be used to refer to State Benefits and other forms of help and support.

Question 7 – We welcome views on whether you see any issues with this approach and whether there are potentially any implications due to the advice/guidance boundary.

Asking the members to answer questions is only one part of the solution, the resulting trustee action is equally important. DWP should be explicit about the response it wants from trustees. From a member perspective, the more questions asked; the greater the individual's expectations will be that the solution is tailored to their needs and wants. In practice, this is likely to create a mismatch of expectations.

In many respects, trustees would want to know the answers to the sorts of questions that might arise in a financial advice fact find around other sources of income, wealth, and savings, as well as longer-term goals, objectives, family circumstances, and (potentially) health.

This is straying dangerously close to crossing the advice / guidance boundary and causes concern about the trustee resource required to support it. We believe an alternative could be for the questions to be asked by a partnering organisation, for example, third-party advice or guidance solution, rather than the trustees.

However, it may be possible to use this information to create a generic tool that works for the majority without being specifically designed with any individual in mind. This is not unlike how default investment is designed or lifestyling glidepaths that target a default retirement option. In these instances, the communications make the nature of the default and or lifestyle clear and include reference to any limitations. By adopting a similar approach here it may be possible to obtain the information and remain outside the advice / guidance boundary.

Question 8 – Do you have any suggestions for key metrics or areas that would need to be included if the proposed value for money framework was extended to decumulation or suggestions for where proposed metrics may no longer be required?

Value for Money is a ‘what you pay for what you get’ test. It largely revolves around the relationship between cost and investment performance relative to objective and net of fees. Other non-investment related aspects also feature, for example, communications and administration.

For decumulation, the existing framework will generally apply.

For schemes delivering in-scheme drawdown, the additional aspect will be whether the investment solution is delivering the intended withdrawal rate on a consistent basis. It may also be sensible to compare the withdrawal rates against the annuity market from time-to-time, where members could achieve a similar pension income but without the investment risk (taking into account the cost of setting up the annuity).

Some of these metrics are very difficult to apply to small schemes, as there are too few members to draw conclusions.

The key focus should be on establishing what the metrics are for and whether the comparison of similar products within a market or comparison of all retirement products is outcome focused or backward looking.

Question 9 – Do you have safeguards in place for members in the decumulation stage? If so, what are these safeguards and what information do you provide to members?

We suggest that DWP refers to the conclusions of the ‘Improving Outcomes in Non-Workplace Pensions’ to establish if it resulted in insights that could be applied to this initiative.

Question 10 – Do you use the same charge structure as you do in the accumulation stage?

This will depend on individual organisations.

Question 11 – We would welcome views to understand what are the practical considerations of partnering arrangements?

It would be helpful to have an explanation for partnering and what it entails, as well as greater detail about how DWP envisages it will work.

Practical considerations include:

- how this will work for small occupational pension schemes
- the practicality of multiple partners
- finding partners with track record, and expertise (this is a due diligence and scheme supplier management exercise)
- data protection and cyber security
- responsibility and liability allocation between parties (this is a contractual matter for the parties)
- concerns about straying into advice territory when signposting a particular partner (which may be regulated).

There are ways to manage these considerations, but it seems appropriate to have certain easements or discharges in relation to advice, for example, signposting should be in accordance with the prescribed requirements to signpost.

There may be some small schemes that face challenges in finding a partner willing to work with small, fragmented business. In which case DWP should explain whether it envisages a default partner to operate in areas where the market cannot provide a solution.

Partnering, and associated measures may be a way to resolve ongoing issues with orphaned schemes. This would help further the various policy objectives and support good outcomes for the members of those schemes.

Question 12 – Should government set out a minimum standard partnering arrangement?

We appreciate that, generally, schemes should partner in accordance with effective system of governance requirements and scheme management of suppliers, however, small schemes will find this difficult.

Other than certain easements or discharges, in relation to advice, it seems wise to retain this sort of content in statutory guidance or other regulatory material, such as General Code.

Question 13 – a) Should all schemes be allowed to establish partnership arrangements or only schemes of a certain size?
b) If only a certain size what should that be?

All schemes should be allowed to establish partnership arrangements. It is unreasonable to force savings arrangements to become retirement product providers. This may even mean that certain, large, and well-managed employer-run trusts exit the market, because such an approach would overstretch resource and capability.

We also expect that some scheme rules will not allow for the transformation of a savings arrangement into a decumulation arrangement, although a statutory override could enable this.

Question 14 – Is there a role for a centralised scheme to deliver decumulation options, where trustees are unwilling or unable to offer these directly?

It depends on the minimum decumulation offer level. Small occupational pension schemes will need an easy way of meeting requirements, and perhaps the solution is that a centralised scheme is only an option for occupational pension schemes that are below a certain number of members or fund value.

DWP should consider whether a tender process for centralised schemes is required and if there will be sufficient competition to produce a good, centralised scheme.

There is an established market for decumulation options which continues to develop. This market covers the full range of savers, and those with small savings may not need a decumulation option that extends beyond cash. Those with substantial savings have a mature SIPP market to make use of. In the middle of this spectrum there is a mass market that, we expect, comprises the likely users of the retirement options and services this consultation sets out to deliver.

The possible gap in the market for a centralised scheme (or schemes) to fill would be a solution for small schemes. This may become a default because it is low cost and straightforward rather than an optimal solution. We expect the centralised schemes to be accessed by transfer and would value DWP confirming this is also its intention.

Question 15 – We would welcome views on if there is an alternative to our approach for legislation that would achieve the same results?

It is unlikely that major change will arise without a legislative framework.

Market forces could produce a similar outcome over the medium term. Consolidation into fewer, larger schemes is already happening at pace. To win consolidation business, consolidators are having to develop retirement propositions. Once consolidation is complete, consolidators will compete among themselves on, among other things, the quality of the retirement proposition.

An alternative might be greater support for advice and guidance solutions, as well as revisiting the boundary between them.

Question 16 – We want to work with industry during the implementation of these proposals; what timeline should we work to implement these changes?

The timeframe to implement should be at least 18 months after the final legislation and regulations are in place and this should be in addition to related communications requirements. When combined, this timescale should give trustees sufficient time to acquire a partner and change the supporting communications, such as wake-up and claims letters, which explain their decumulation offering.

Depending on what is meant by partnering, especially if this is other than by way of transfer, the market will need time to develop. This may take longer than 18 months unless the changes are phased in gradually.

Question 17 – When we introduce legislation should this only apply to Master Trusts in the first instance?

It will be easiest to embed the legislation if the measures are phased in and begin with master trusts, and master trust-sized employer-run schemes, with schemes of less than £100 million in assets part of a later roll-out stage.

Having said that, it also makes sense to consider market dynamics before rolling out these measures across the market, whether in whole or in part.

As it happens, competition is already driving the master trust market to enhance its retirement proposition. Indeed, this market has a degree of self-interest since retirement proposition is often one of the questions on RFPs for master trusts and is also a way to retain valuable AUM over a long period.

DC sections of employer-run hybrid schemes are often used by members to fund the PCLS and avoid eroding the value of the connected DB pension. Consequently, members in such circumstances may not, need the kind of retirement services and options envisaged by the consultation.

This means that a prescribed set of options may serve members better if they are targeted at DC-only trusts run by employers. Currently, this market is, undergoing a fast-paced transition and many such schemes are in the process of transferring their assets, and members to master trusts or will do so in the relative short term. Forcing such schemes to partner, or select other options, will be an unnecessary distraction to consolidation, since the relevant members are likely to decumulate in another scheme in any case.

If a partnership approach is taken, each partner could then be included in the scheme return.

Question 18 – Do you have views and evidence on how this can be delivered in ways that achieve our policy aims of stimulating CDC in decumulation, enabling Nest to provide the services outlined in this consultation, while ensuring a healthy competitive marketplace?

No comments.

Question 19 – Are you able to quantify any of the one-off or on-going costs at this stage?

No comments.

Question 20 – Are you able to provide a breakeven point in pot size for providing certain decumulation products or services? Would this be different for decumulation only CDCs?

This will depend on individual organisations.

Question 21 – What benefits do you expect there to be from the proposals members/schemes/wider)? Do you think they are quantifiable?

The key benefit is that these proposals should help members avoid taking the ‘wrong’ option because of the cost of advice, which might leave retirement savings invested in cash over an extended period.

Members should also become more engaged with choices and be increasingly capable of making better decisions.

Question 22 – Do you think the benefits from the proposed changes outweigh the costs?

Generally, this may be the case for reasons set out in Question 21.

For small pots, the benefit may not outweigh the costs because the options are so limited. Nevertheless, this may tie in with consolidation of small pots which falls outside the scope of this consultation. To help manage this, small pots could be excluded from the measures while the small pot consolidation drive is underway, as this may resolve the issue for many members.

Yours faithfully

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Investment & Life Assurance Group

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