Eversheds' Pensions White Paper
Rebuilding the consensus

MAY 2015

EVERSHEDS

Introduction

It is nearly 10 years since the Pension Commission led by Lord Turner and supported by Baroness Jeannie Drake and Professor Sir John Hills issued its second and final report *'A New Settlement for the Twenty-First Century'*. In that report, the Commission made a series of recommendations on the future of the UK pension system, which were designed to address the challenges posed by an ageing population and the fact that millions of people were not saving enough for their retirement. Central to the Commission's recommendations was the introduction of automatic enrolment, which began being rolled out in October 2012 and has already led to over 5 million more people saving for their retirement in a workplace pension scheme.

Automatic enrolment may be the Commission's greatest legacy, but its greatest achievement was the consensus that Lord Turner and his colleagues were able to build around the challenges facing the UK pension system and the steps that needed to be taken to address them. This 'buy-in' from politicians and stakeholders of all persuasions has resulted in most of the Commission's recommendations having now been implemented and it has guided pensions policymaking in the UK for much of the last decade.

Over the past year, however, the pensions consensus has begun to unravel. The Chancellor's surprise announcement of pensions freedom and choice in March 2014 – a policy introduced without consultation – has been followed by a series of policy announcements which seem to signal a shift back to short-term pensions policymaking based on political expediency in place of long-term, strategic policymaking based on clearly articulated aims and objectives.

On 9 March 2015, we hosted a Pension Reform roundtable, which was attended by a number of leading figures from within the pensions industry (see below). The overwhelming message from that event was the crucial importance of rebuilding a long-term consensus around UK pensions policy to ensure that the progress that has been made since the Pension Commission concluded its work is not in vain.

Ensuring that each generation has enough to live on in retirement, and does not place too great a burden on either the state or future generations, takes long-term, strategic planning. That is why we are calling on the new Government to establish a new independent pension commission to review the progress made in the past 10 years and to rearticulate the long-term, strategic goals for UK pensions policy in the future.

In our view, a new independent pensions commission is essential if we are to rebuild the pensions consensus. A great deal of work and dialogue with all stakeholders will also need to go on to secure this. Without it, UK pensions policy is in danger of being blown to and fro by the winds of political expediency and short term economic pressures, which risks leaving millions without the safe harbour of an adequate income in retirement.

This White Paper is explicitly not party political. Rather it seeks to encourage the new Government, of whatever flavour, to work to rebuild the consensus around the UK's long-term pensions policy and strategic aims.

Pension Reform roundtable

The recommendations set out in this White Paper are informed by the lively discussion and debate at our Pensions Reform roundtable, which we held in London on 9 March 2015. The participants represented a range of different stakeholders with different views and priorities. Not everyone at the event therefore agreed on every point – in fact some vigorously disagree on some points – so the recommendations in this paper will not be endorsed by every participant. In particular, some of the participants were not in favour of changes to automatic enrolment or a new Pensions Commission.

The roundtable was attended by:

- **Francois Barker** – Head of Pensions, Eversheds LLP (Chair)
- **Adrian Boulding** – Pensions Strategy Director, L&G and Chair, Pension Quality Mark
- **Yvonne Braun** – Director, Long Term Savings Policy, Association of British Insurers
- **Chris Curry** – Director of the Pensions Policy Institute
- **Katie Dash** – Pensions Policy Adviser, CBI
- **Jeannie Drake** – Member of the Pension Commission
- **John Hutton** – Former Secretary of State for Work and Pensions
- **Tim Jones** – Chief Executive, NEST
- **Darren Philp** – Head of Policy, The People's Pension
- **Joanne Segars** – Chief Executive, NAPF
- **Tim Smith** – Pensions Policy and Technical Specialist, Eversheds LLP
- **Nigel Stanley** – Head of Communications and Campaigns, TUC
- **Mark Wood** – Chief Executive, JLT
- **David Yeandle** – European Employers' Group

Civil servants from the relevant Government Departments were also in attendance to observe the discussion.

I would like to thank everybody who attended the roundtable for their valuable contribution to the debate, with particular thanks to David Yeandle for his help in making the event happen.

Francois Barker
Chair of the Eversheds Pension Reform Roundtable
Partner and Head of Pensions, Eversheds LLP

Commentary by Lord Hutton of Furness, Secretary of State for Work and Pensions at the time of the publication of the Pension Commission's final report in November 2005

Today our pension system stands at a crossroads.

The Turner Report in 2005 helped lay the foundations for a new consensus designed to encourage a significant increase in workplace pension saving. The Report was based on a clear analysis of the problem we faced and had a compelling and simple argument underpinning its central recommendations – that we all needed to save more for our retirement. As a consequence of this new and welcome consensus, auto-enrolment has resulted in over 5 million new pension saving accounts being opened. People now recognise not just the need to start saving but also that they will almost certainly need to work longer too if they are to enjoy the lifestyle they aspire to when they retire. Reforms to the state pension have also been designed to encourage and reward retirement saving. As a result, there are now good reasons to be optimistic that we will be able to prepare ourselves financially for the accelerating pace of societal ageing.

More recent changes to the rules on annuities have, however, opened up a new debate and so far there appears to be little evidence of a consensus on the right way forward. Giving savers more freedoms and choices about what to do with their money when they retire seems like the right thing to do. Who can be opposed to freedom after all? But what about the risk that savings will be depleted? What if the money runs out sooner than we thought? What therefore is the right balance between financial freedom and financial security and what should the principal drivers of public policy be in this area? These are questions of first order importance.

The good news is that policy makers are at least continuing to focus their efforts on creating the right policy framework. Pension policy remains high on the list of political priorities for all of the main Parties. But getting things right here is so vital to the long term wellbeing of our society and our economy. How can we ensure we take the right path going forward? How do we build for the long term?

This excellent document addresses all of these main questions and sets out the real pensions policy challenges facing this Parliament and the new Government of our country. It identifies a number of priorities and suggests some of the next steps we should take as we try and establish an enduring consensus about the best way to encourage people to take responsibility for their financial needs in retirement. Consensus is a necessary pre-condition for establishing a sustainable system of workplace saving because policy in this area needs to be stable over the long term. In this document are set out some of the measures that might set us on the right course.

Recommendations

In order to build on the progress that has been made in the past decade and address the challenges posed by widespread under saving for retirement and an ageing population, our 10 recommendations for the new Government in relation to UK pensions policy are:

1. Work to rebuild and maintain the consensus around the UK's long-term pensions strategy
2. Establish a new independent pensions commission to clarify the long-term strategic aims for UK pensions policy and to help rebuild the consensus
3. Consider the case for increasing the age at which individuals can access their pension savings flexibly
4. Ensure the successful roll out of automatic enrolment to workers of small and medium sized employers
5. Assess the case for raising the minimum automatic enrolment contribution rate by the end of this Parliament
6. Ensure that savers get value for money during decumulation
7. Facilitate the establishment of an online pensions 'dashboard' to help people manage their pension savings
8. Build alliances within Europe to oppose the introduction of the holistic balance sheet and to ensure any new EU pensions regulation works for the UK and respects the diversity of pension systems within the EU
9. Help people understand how much they need to save for their retirement, and
10. Move away from micro-managing the governance of workplace pension schemes.

1. Work to rebuild and retain the consensus around the UK's long-term pensions strategy

The Pension Commission, led by Lord Turner, worked extremely hard to build a consensus among politicians from all parties and other stakeholders around the future direction of UK pensions policy. This consensus lasted for nearly a decade, but it is now starting to unravel.

Given the long-term nature of retirement savings and the challenges posed to society by under saving and an ageing population, it is essential that the new Government:

(i) identifies the long-term strategic aims for UK pensions policy

(ii) develops a clear narrative around pensions policy making, and

(iii) works hard to rebuild and maintain a consensus (across all political parties and key industry stakeholders) around these strategic aims.

2. Establish a new independent pensions commission to clarify the long-term strategic aims for UK pensions policy and to help rebuild the consensus

We believe that a new independent pension commission is essential if the incoming Government is to rebuild the consensus around long-term pensions policy. The commission should be established early in this Parliament, so that the new Government has time to implement its recommendations.

This pensions commission should be given a wide remit to review the UK pension system and make recommendations for the future direction of UK pensions policy. As part of this, it should be asked, in particular, to:

(i) review the impact of automatic enrolment on the UK pensions landscape and identify any changes that need to be made to the current approach

(ii) identify what needs to be done to encourage people to save enough for their retirement

(iii) assess the impact of the introduction of "*freedom and choice*" on the UK pensions system

(iv) examine the decumulation phase and identify what needs to be done to ensure that individuals can use their pension savings effectively and efficiently to provide themselves with an income in retirement

(v) consider the suitability of the current pensions system for the low paid, those with multiple jobs, those with variable working patterns, women and the self-employed.

3. Consider the case for increasing the age at which individuals can access their pension savings

At a time when the state pension age is gradually rising and the Government is encouraging people to work for longer, allowing people to access all of their retirement savings flexibly from age 55 risks sending a contradictory message. It suggests that 55 is old enough to retire, when for most people they will not be able to afford to retire until much later than this. There is also widespread concern that many people will spend their *retirement* savings before they even retire.

Increasing the age at which people can access their *retirement* savings could help to address these concerns by ensuring that people have retirement more in their sights when they do so.

One of the consequences of the introduction of freedom and choice is that pension schemes could simply become long-term savings vehicles. This is likely to impact the attitudes of policymakers, as well as some employers and individuals, towards them. We believe that moving the age of access closer to retirement might help to ensure that pension schemes continue to be effective *retirement* savings vehicles.

4. Ensure the successful roll-out of automatic enrolment to SMEs

The job of introducing automatic enrolment is only half complete, with over one million small and medium sized employers (SMEs) yet to reach their staging date. So far, the introduction of automatic enrolment has been an overwhelming success. However, extending this to SMEs, and especially micro-employers, is a challenge on a very different scale and the successful implementation of auto-enrolment could be undermined if there is large scale non-compliance among SMEs.

Therefore, the incoming Government should:

- ensure that everything is being done to ensure the successful roll-out of automatic enrolment to workers in SMEs, including ensuring that automatic enrolment communications to SMEs from the Pensions Regulator and the DWP are appropriate for that community, and
- not make any further changes to the automatic enrolment legislation until the end of the implementation period to enable pension providers, payroll providers, advisers and other stakeholders to focus on the task of ensuring the successful roll-out of automatic enrolment among SMEs.

That said, the independent pension commission that we are recommending should be set up by the new Government ought to:

- review the impact of automatic enrolment on the UK pensions landscape and identify any legislative changes that may need to be made to the current approach at the end of the implementation period, and
- examine the case for increasing the minimum automatic enrolment contribution rate towards the end of this Parliament to help address the issue of widespread under saving for retirement and consider how this can best be achieved.

5. Assess the case for raising the minimum automatic enrolment contribution rate

Although as a result of automatic enrolment more people are now saving for their retirement, most people are still not saving enough. In addition, a significant risk with automatic enrolment is that some people will think that their financial security in retirement is now taken care of and that they don't need to do anything else. Many people under this misapprehension will get a nasty shock when they come to retire.

To help address this, the new Government ought to consider the case for increasing the minimum automatic enrolment contribution rate and how this can best be achieved.

The new Government should also consider what steps it can take to promote other means of increasing employer and member contribution rates on a voluntary basis, such as:

(i) rewarding employers and members who pay in more than the minimum level of contributions

(ii) facilitating the widespread use of auto-escalation as a default (perhaps even as part of the automatic enrolment requirements), and

(iii) raising public awareness of how much people need to save for their retirement.

6. Ensure that individuals get value for money during decumulation

Trustees and Independent Governance Committees (IGCs) have been tasked by the Government with ensuring that workplace defined contribution (DC) pension schemes are delivering good value/value for money during the accumulation phase. However, this fiduciary oversight does not extend to the decumulation phase, which is arguably even more critical in determining member outcomes and even more difficult for individuals to navigate.

Therefore, we believe that the remit of trustees of DC schemes and IGCs should be extended to include assessing good value/value for money during the decumulation phase as well as during accumulation.

In addition, trustees of most occupational DC schemes do not currently want to retain members’ funds within their scheme post retirement and allow members to drawdown an income over time from the scheme due to the cost and complexity of doing so. However, this means that if members of such schemes want to enter drawdown they will be required to choose their own drawdown vehicle in the retail market, which is likely to be subject to higher charges and not benefit from fiduciary oversight. This does not seem satisfactory. To address this:

(i) steps should be taken to ensure that members who transfer their retirement savings from trust-based occupational pension schemes into a retirement income product through the retail market get value for money,

(ii) trustees that do not want to offer a drawdown facility within their scheme should be encouraged to select a preferred decumulation provider for their members which offers good investment options and good value, and

(iii) the Government should consider giving trustees a statutory discharge where they transfer members automatically to a suitable decumulation provider at retirement.

7. Facilitate the establishment of an online pensions 'dashboard' to help people manage their retirement savings

Most individuals do not engage with their retirement savings until they want to access them and many lose track of their pension savings when they change jobs. We believe that the creation of an online pensions 'dashboard', which enables individuals to view and manage all of their retirement savings (including their state pension entitlement) in one place would help to address these issues. It would also help people to plan for their retirement.

Tools like this have been successfully developed in other countries. For example, in the Netherlands, the pension federation, together with Dutch pension funds and the social security bank (SVB), have developed an online pensions dashboard. This informs every individual about all of the pension entitlements they have built up with different pension funds over their lifetime (including their state pension entitlement). According to the FCA's interim report on its retirement income market study, the Dutch pensions dashboard has "encouraged consumer engagement with pensions by making them more tangible and visible" and played a part in improving "self-reported measures of financial awareness" .

8. Build alliances within Europe to oppose the introduction of the holistic balance sheet and to ensure any new EU pensions regulation works for the UK and respects the diversity of pension systems within the EU

It is essential that the incoming Government builds alliances within Europe and works to ensure that any new EU pensions legislation and/or regulation is necessary, proportionate and respects the principle of subsidiarity (with matters only being dealt with at a European level where this is absolutely necessary). It is also essential that any new legislation works for UK pension schemes and recognises the diversity of the different pension systems within the EU.

More specifically, the new Government should:

- secure changes to the proposed draft IORP Directive to reduce the level of prescription in it, and ensure that any new requirements are necessary, proportionate and deliver value for money for pension scheme members, and
- oppose the introduction of the proposed "holistic balance sheet" that is being developed by the European Insurance and Occupational Pensions Authority (EIOPA), which based on EIOPA's own estimates could add at least £150bn to the deficits of defined benefit pension schemes in the UK.

The incoming Government should also ensure that any new EU pensions legislation complies fully with the EU's own principles on "better regulation".

9. Help people understand how much they need to save for their retirement

If you aim for nothing you will hit it! This makes it particularly concerning that most people in the UK do not know how much they need to save for their retirement. We believe that the Government could and should do more to help people understand how much income they will need in retirement and how much they need to save to secure this.

In this regard, the new Government could follow the lead of Australia, where the Association of Superannuation Funds of Australia publishes the *ASFA Retirement Standard* which indicates the annual budget needed by Australians to fund either a "*comfortable*" or a "*modest*" standard of living in their post-work years. It is updated quarterly to reflect inflation, and provides detailed budgets of what single people and couples would need to spend to support their chosen lifestyle.

If the new Government published indicative figures such as this, it should help to stimulate public awareness of how much people may need in retirement. It would also help employers, pension providers and trustees give their employees and members a steer about how much they need to save for their retirement.

10. Move away from micro-managing the governance of workplace pension schemes

Instead of micro-managing the governance of workplace pension schemes, the focus of future Governments and regulators should instead be on ensuring that the people running such schemes (when looked at as a whole) have sufficient experience and expertise to run the relevant scheme(s) effectively.

Amongst other things, these requirements could include the introduction of a formal CPD requirement for all pension scheme trustees and members of Independent Governance Committees.

About Eversheds LLP

Eversheds LLP and its worldwide offices have over 4,000 people who provide services to the private and public sector business and finance community. Access to all these services is provided through 55 international offices in 29 countries. Eversheds combines local market knowledge and access with the specialisms, resources and international capability of one of the world's largest law firms.

Eversheds has the largest pensions team in the UK with around 70 specialist pensions advisors. Its market-leading team advises trustees and sponsors of occupational pension schemes as well as pension providers, investment managers and Government departments. The team also contributes to several industry bodies and pensions policy forums.

Eversheds also advises on global pensions matters and the pensions aspects of multi-jurisdictional transactions through its international pensions practice.

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Notes

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